



A Primer on the 1998 Tobacco Settlement

Emergency room care for a stroke patient; a nursing home stay for an emphysema sufferer; chemotherapy for a victim of lung cancer. All of these health care needs are very high cost, and all are often the result of tobacco usage.

Such costs as these, which have hit Medicaid budgets and state employee health insurance plans hard, eventually spurred an unprecedented piece of litigation referred to somewhat technically as the Master Settlement Agreement, and more commonly as the Tobacco Settlement of 1998.

Steam began to build towards instituting such a settlement early in 1997, when Florida, Minnesota, Mississippi, and Texas reached out-of-court settlements worth billions of dollars with tobacco companies. By mid-1997 41 states had reached a settlement with tobacco companies so far-reaching that it would require congressional approval. That approval never came, forcing the states to seek a new, modified agreement. This was finally reached in November 1998 in the form of the Master Settlement Agreement.¹

The agreement was signed by the six largest tobacco product manufacturers and by the attorneys general of the 46 states which had not already reached settlements, as well as the District of Columbia, Puerto Rico, the U.S. Virgin Islands, the Northern Mariana Islands, and Guam.

What the Settlement Does

Though less expansive than the settlement brought to Congress two years ago, the Master Settlement Agreement is still a far-reaching document, having profound effects on how tobacco products are sold and upon the states themselves. Here are some of its components²:

- ◆ A foundation, funded by the industry to the tune of \$25 million per year, must be established to advertise and educate the benefits of not smoking, and to track youth smoking.
- ◆ The use of cartoon characters in tobacco advertising and packaging is banned.
- ◆ Any industry attempts to garner a market among youth are prohibited.
- ◆ Companies involved must open and maintain, at their expense, web sites designed to provide easy public access to all documents and court files related to tobacco lawsuits.
- ◆ All outdoor advertising, such as billboards and signs in stadiums, is banned.
- ◆ The distribution and sale of merchandise and apparel featuring brand name logos is prohibited.

- ☉ Tobacco product manufacturers may not pay for product placements in movies, television shows, or elsewhere.
- ☉ Name brands may not sponsor events with a significant youth audience, such as team sports.
- ☉ Tobacco sponsored organizations, such as the Council for Tobacco Research and the Tobacco Institute, must be disbanded.
- ☉ Gifts based on purchases (such as through the collection of proofs of purchase) may be distributed only with proof of age.
- ☉ Tobacco companies may not lobby against laws meant to limit youth access to tobacco.

☉ Manufacturers may not suppress research data on tobacco in any way.

☉ A minimum pack size of 20 cigarettes is established, pending state legislative action.

☉ The industry is required to cover all legal fees incurred by the states regarding the agreement.

And last but not least, the industry must make payments to the states in perpetuity, with payments totaling \$206 billion through 2025.

Payments

Payments were designed to reimburse the states for funds spent over the years on health care costs related to tobacco use. Medicaid, state employee insurance plans, etc., have all paid out billions of dollars on care for tobacco-related illnesses.

Payments may begin only after the “state specific finality date,” which is the earlier of June 30, 2000, or the date when 80% of the states have had the agreement officially approved by a state court. Payments have already started despite this, but money is currently being held in an escrow account where it may earn interest in each state’s name until the finality date occurs, at which time the funds will be handed over to the states.

There has been a consistent threat that the federal government might attempt to claim some of the settlement money as its own, since under normal circumstances funds used to reimburse Medicaid are shared with Washington, which shares the burden of Medicaid costs. However, it seems increasingly unlikely that Congress will be willing to incur the political disfavor

inherent in stripping large portions of the settlement payments from the states. In fact, Congress added language within the FFY99 Emergency Supplemental Appropriations Bill to protect these funds from federal seizure.

South Dakota’s Share

The Big Six as We Know Them	
<p>Brown and Williamson Barclay Capri Carlton GPC Kool Lucky Strike Pall Mall Raleigh Tareyton Viceroy</p> <p>Commonwealth Tobacco Malibu Montclair Riviera</p> <p>Liggett and Myers Chesterfield Eve L&M Lark Pyramid</p>	<p>Lorillard Kent Newport Old Gold</p> <p>Phillip Morris Bond Marlboro Merit Virginia Slims</p> <p>R.J. Reynolds Camel Doral Salem Winston</p> <p style="text-align: center;"><i>N.B., Not an exhaustive list</i></p>

Each state was slated to receive an “up-front” payment (now in escrow) from the tobacco companies in 1998. No payment is scheduled for 1999, and then annual payments must begin by April 15, 2000. South Dakota’s first payment was scheduled to be \$8,374,699.41. To put that into perspective, that figure would have been enough to cover the FY00 general fund budget of the Department of Military and Veterans’ Affairs, the Department of Health, the Department of Game, Fish and Parks, the Department of Environment and Natural Resources, the Legislature, or the Attorney General. And this is the smallest payment the state will receive.

After that first payment, the schedule for South Dakota is as follows:

2000 = \$22,373,532.90
2001 = \$24,159,821.39
2002 = \$29,008,893.79
2003 = \$29,283,431.59
2004-2007 = \$24,440,164.46
2008-2017 = \$24,925,199.13
2018-2025 = \$27,929,622.54

Thus, total payments to South Dakota through 2025 will equal \$683,650,008.54. Adjustments are written into the proposal to take effect upon increases in the inflation rate. Also, annual payments may be reduced or increased if substantial changes in the volume of domestic tobacco sales so warrant over time. Broadly speaking, South Dakota, and every other state, has complete autonomy over how to spend this settlement money.

South Dakota Legislative Action

During the 74th Session of the South Dakota Legislature, five pieces of legislation were introduced connected to the Master Settlement Agreement. Three passed. Following is a short summary of each bill:

➤ **Senate Bill 28 (passed):** This bill was requested by the Attorney General’s office, and is meant to protect the state against tobacco companies not included in the Master Settlement Agreement from profiting in South Dakota without liability. The act establishes an escrow account into which such companies must deposit a fraction of each sale within the state. Should action be taken against such companies in the future, these funds will be used to pay their past liabilities. The act is also meant to encourage other companies to join the agreement, and prevent those which do not join from unfairly reaping profits through that competitive advantage.

➤ **Senate Concurrent Resolution 3 (passed):** This resolution requested that the President and Congress “allow the State of South Dakota complete discretion over all funds received” through the settlement, and “not to entertain any claims by the federal government on these funds.”

➤ **House Bill 1154:** This bill would have established a trust fund for settlement money received by the state. The principal would have remained untouched and the expenditure of the interest received would have been at the discretion of the Legislature. House State Affairs deferred this bill to the 41st day.

➤ **House Bill 1191:** This bill would have also created a trust fund for settlement money, but in this scenario interest would have been placed in a “South Dakota partnership fund,” to be used for “grants that encourage partnerships between government agencies and the private sector for grants related to educational and health programs.” This bill was also deferred to the 41st day by House State Affairs.

➤ **House Concurrent Resolution 1007 (passed):** This resolution encouraged Congress to pass a bill prohibiting the federal

government from recouping tobacco settlement money.

Action in Other States

State legislatures nationwide have been grappling with the question of what to do with their share of the tobacco settlement money. According to the National Conference of State Legislatures, “As of Thursday, May 20, 1999, there have been more than 465 bills introduced in 1999 that deal with the tobacco settlement. Approximately 145 of these bills have been acted on (passed one house of the legislature). Among the bills that have been acted upon, 46 have been signed and enacted into law, 1 has been vetoed, and 15 have been sent to the governor and are waiting to be signed or vetoed.” Among those concepts which have already been enacted³:

∞ *Nebraska* – Legislation has been passed creating the Nebraska Health Care Trust Fund, which will include money received from the Master Settlement Agreement. Interest will be transferred to a separate fund and used for grants and loans regarding health care. Settlement money will also be used to augment nursing facilities and the CHIP program.

∞ *Colorado* – A Tobacco Litigation Settlement Fund has been created by statute for all money and interest derived from the tobacco settlement. The General Assembly is given the power to expend money from this fund as it sees fit.

∞ *Arkansas* – Action was taken to appropriate \$2 million to the University of Arkansas for Medical Sciences (UAMS) for indigent health care costs.

∞ *Montana* – One million dollars of tobacco settlement revenue has been appropriated for FY00 and FY01 to the Montana Comprehensive Health Association, which is comprised of all insurers, HMOs, etc., in Montana.

∞ *West Virginia* – Two funds have been established to handle tobacco settlement funds. Each will comprise 50% of the settlement payments. The West Virginia Tobacco Settlement Medical Trust Fund will be used to stabilize the state’s health-related programs and delivery systems. The Tobacco Settlement Fund will be limited to expenditures for the public employees insurance agency, expansion of the Medicaid program in West Virginia, public health funding, and funding for any state-owned or operated health facilities.

∞ *North Dakota* – North Dakota has created a Tobacco Settlement Trust Fund. Money in the fund may be appropriated by the state legislature for the following purposes only: transfers to a Health Education Trust Fund to be administered by the Department of Health, transfers to the Common Schools Trust Fund, and transfers to the Resources Trust Fund to address long-term water development needs.

Next Steps

There is no clear answer to the question, “What’s next?” Within a year South Dakota will have to face an enviable task — handling the infusion of millions of dollars into the general fund, with no strings attached. It will be the Legislature’s duty and right to appropriate this money as it sees fit, but at the same time only the Legislature can decide how proactive of a role it wishes to take in spending or saving these funds. The possibilities are wide open.

This issue memorandum was written by William E. Pike, Fiscal Analyst for the Legislative Research Council. It is designed to supply background information on the subject and is not a policy statement made by the Legislative Research Council.

¹ Tubbesing, Carl and Joy Johnson Wilson, "States Settle Tobacco Suits: So Who Won?" *State Legislatures*. February 1999, pp. 14-19.

² www.naag.org/glance.htm

³ www.hpts.org