

HJR

12

FISCAL NOTE

No: 1

STATE OF ALASKA
1999 LEGISLATIVE SESSION

Bill Version: CSHJR 12 (FIN)
BILL NO. (H) Publish Date: 2/17/99

Title: NO FED. CLAIM ON STATE TOBACCO
SETTLEMENT
Sponsor: Rep. Harris
Requestor: H FIN

Dept. Affected: Law
BRU: Civil Division
Components: Fair Business Practices
Serial # 2206

EXPENDITURES/REVENUES: (THOUSANDS OF DOLLARS)

OPERATING	FY 00	FY 01	FY 02	FY 03	FY 04	FY 05
Personal Services						
Travel						
Contractual						
Supplies						
Equipment						
Land & Structures						
Grants, Claims						
Miscellaneous						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0
CAPITAL	0.0	0.0	0.0	0.0	0.0	0.0
REVENUE	0.0	0.0	0.0	0.0	0.0	0.0

FUNDING: (THOUSANDS OF DOLLARS)

General Fund						
Federal Fund						
Other						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

POSITIONS:

Full-Time	0	0	0	0	0	0
Part-Time	0	0	0	0	0	0
Temporary	0	0	0	0	0	0

ANALYSIS: (ATTACH A SEPARATE PAGE IF NECESSARY)

This resolution has a zero fiscal impact. However, if federal law is not enacted to prevent HCFA from asserting its claim against the settlement money, the result could be a loss to the State of Alaska of \$400 million over 25 years.

Prepared by: House Finance Committee *[Signature]* Date: 2/16/99
Representative Eldon Mulder *[Signature]* Phone: 465-2647
Representative Gene Therriault *[Signature]* Phone: 465-4797



Alaska State Legislature

REPRESENTATIVE JOHN HARRIS

District 35 - Valdez, Cordova, Whittier, Glennallen, Delta Junction, Tatitlek, Kenny Lake, Paxson, Gakona, Cherega Bay

Sponsor Statement

HJR 12 – Relating to federal claims against funds obtained by settlement of state tobacco litigation.

Last November, Alaska and 45 other states settled a comprehensive lawsuit against the nation's major tobacco producers for a total sum of \$246 billion, to be paid out over a period of about 25 years. The federal government, which was not a party to the litigation, asserts that it is entitled to recoup a significant portion of the settlement monies to reimburse it for Medicaid funds given to the states over the years.

We do not believe the federal government should be asserting a claim to any of the settlement monies. The lawsuit brought by the various states against the tobacco companies was based on violations of state laws. The federal government did not join the suit or assert any federal claims of its own.

For its part of the settlement, the State of Alaska is scheduled to receive a total of \$668,903,056.53 over the next 25 years, in annual payments of between \$21 million and \$28 million. The federal government, if successful in asserting any right to recoupment of the settlement funds, could take as much as \$400 million of Alaska's share.

The Clinton administration is evidently so determined to take the lion's share of the settlement funds that it has included them as a funding source in the FY 2000 budget introduced by the President on February 1.

Legislation has been introduced in the Congress to prohibit federal recoupment of settlement monies. HJR 12, directed at the President and our Congressional delegation, asks the Congress to enact such legislation and the President to sign it.

FREQUENTLY ASKED QUESTIONS

1. **Who are the parties to the Tobacco Settlement?** The parties to the settlement include 46 states (Florida, Minnesota, Mississippi, and Texas had previously settled with the tobacco manufacturers), Puerto Rico, the U.S. Virgin Islands, Guam, American Samoa, the Northern Mariana Islands and the District of Columbia, Brown & Williamson Tobacco corporation, Lorillard Tobacco Company, Philip Morris Incorporated, R.J. Reynolds Tobacco Company, Commonwealth Tobacco, and Liggett & Myers.
2. **What is the effective date of the tobacco settlement?** The parties signed the Master Settlement Agreement (MSA) on Monday, November 23, 1998, the Master Settlement Agreement Execution Date. States that sued the tobacco manufacturers must go to state court and file a motion for the approval of the settlement agreement by December 11, 1998. States that had not filed a suit, must go to state court to file suit and to make a motion to approve the settlement agreement by December 23, 1998. The effective dates for the non-economic provisions of the MSA vary, but many are related to the MSA Execution date (e.g. 60 days after the MSA Execution date). There are two important effective dates related to the economic provisions of the MSA: the **State Specific Finality Date** and the **Final Approval Date**. The State Specific Finality Date is the date when a state court gives final approval to the settlement and the consent decree. The Final Approval Date is the earlier of June 30, 2000 or the date when 80 percent of the states have obtained State Specific Finality and those states represent 80% of the payments.
3. **When do the settlement funds become available to the states?** No funds can be dispersed to the states until Final Approval is attained. If the requisite number of states have not reached State Specific Finality before June 30, 2000, the funds will become available to all states that have reached State Specific Finality on June 30, 2000. If a state fails to obtain State Specific Finality by December 31, 2001, its participation in the settlement is terminated.
4. **I understand that tobacco manufacturers will begin making payments in December 1998. Where will these funds go if they are not available to states until June 30, 2000?** The payments made by the tobacco manufacturers will be deposited into an escrow account. When a state obtains State Specific Finality, the funds that are to be allotted to that state will be moved from the general escrow account into a state specific escrow account, where the funds will accrue interest and will become available to the state on the Final Approval date.
5. **What must states do to attain State Specific Finality?** States must get the settlement approved by a state court. This includes approval of the consent decree. In addition, all opportunities for appeal of the approval must have expired, so that the court's approval is final.
6. **What will state legislatures need to do to implement the tobacco settlement agreement?** State legislatures will need to enact the model statute included in the Master Settlement Agreement (See question #12), regarding the treatment of non-participating manufacturers, before the state begins receiving its allotment from the settlement. In addition, if there is any question about the legislative appropriation of the settlement funds, legislatures may want to enact laws to clarify the treatment of the funds under state law. The settlement agreement is silent on that issue. Finally, the legislature should probably review the state's consent decree, the document that implements the settlement agreement in the state.
7. **What is the purpose of the model statute included in the Master Settlement Agreement? What happens if my state fails to enact the statute?** The model statute creates a reserve fund for non-participating manufacturers to pay future claims, establishing a level playing field between participating and non-participating manufacturers. The model act must be enacted by states exactly as it is drafted in the MSA (Exhibit T) and as a stand-alone piece of legislation or the state must enact a "qualifying statute," as determined by a firm jointly retained by the settling states and the original participating manufacturers. The ruling of the

firm is final. A "qualifying statute" is defined in the MSA as a settling state's statute, regulation, law and/or rule (applicable everywhere the state has authority to legislate) that effectively and fully neutralizes the cost disadvantages that the participating manufacturers experience (as opposed to the non-participating manufacturers) experience as a result of the MSA. If a state fails to enact the model statute or if a state enacts the model and a court subsequently overturns it, the state allotment will be reduced by no more than 65 percent.

8. **When the Final Approval Date arrives and the funds become available to the states, who controls the funds?** The Master Settlement Agreement is silent on the matter; therefore the general belief is that the funds will be appropriated according to state law.
9. **How are the amounts each state will receive determined? Are the state allotments listed in the Master Settlement Agreement the actual amounts each state will receive?** The state allotments were established by a formula developed by the Attorneys General. These allotments are subject to a number of adjustments, reductions and offsets. In addition, the federal government is laying claim to more than half the settlement dollars. The exact amount a state will receive is the net of the listed allocation minus any adjustments, reductions and offsets and may also be subject to recoupment of any settlement funds attributable to Medicaid.
10. **What is the basis of the federal claim on state tobacco settlement funds?** The U.S. Department of Health and Human Services (DHHS) contends that existing Medicaid law (Section 1903(d) of the Social Security Act) compels it to recover its share (federal Medicaid matching percentage) of third party payments, collected by states on behalf of Medicaid clients, and argues further that state tobacco settlement funds are third-party recoveries under the provisions of the Medicaid statute. DHHS has "recouped" some funds from states that reached an earlier settlement agreement with the Liggett Group, but temporarily suspended the collection of state tobacco settlement funds pending comprehensive federal tobacco legislation. An amendment to the Medicaid statute that would exempt tobacco settlement funds from recoupment must be enacted to prevent the seizure of state tobacco settlement funds when they become available to states in 2000.
11. **Does the Master Settlement Agreement restrict or earmark the settlement funds?** No. States will determine how the funds will be spent.
12. **If the federal government adopts an excise tax on tobacco products, will my state receive less money from the tobacco settlement?** Maybe. Under the provisions of the settlement, if the federal government enacts a tax or fee on tobacco products, and uses the proceeds to provide either unrestricted funds to states or funds earmarked for health care or tobacco-related health care, these funds would be subtracted from the state allotment on a dollar-for-dollar basis. The federal legislation offset would not apply if the funds were earmarked for assistance to tobacco growers or impacted communities.
13. **Aside from determining funding priorities and enactment of the model statute, are there other legislative actions related to the tobacco settlement state legislators might consider?** Yes. The settlement agreement prohibits the sale and manufacture of cigarettes in packages of less than 20 cigarettes. This prohibition sunsets December 31, 2001. The settlement agreement also prohibits tobacco manufacturers from opposing state legislation prohibiting the sale and manufacture of these small cigarette packages. If a state wants to continue the ban, considered a key provision to discourage youth access to cigarettes, state legislation would be required. In addition, the settlement agreement identifies areas of state legislation, law and administrative rule related to youth access to tobacco products, that the tobacco industry is prohibited from opposing. That list provides a starting point for considering future legislation. Finally, there is a wide range of youth access issues that are not addressed in the settlement agreement that could be the subject of state legislative initiatives.



CAPITOL to CAPITOL

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STATES PREVAIL ON FIRST TOBACCO RECOUPMENT SHOWDOWN. On March 4, Senator Kay Bailey Hutchison (R-Texas) successfully added language forbidding the federal government from seizing state tobacco settlement funds to S. 544, a FY 1999 supplemental appropriations bill (see related story below). The amendment was added by voice vote in the Senate Appropriations Committee. The committee also rejected an amendment from Senator Tom Harkin (D-Iowa) that would have compelled states to spend 25 percent of their settlement funds for federally designated purposes. full-court press by state legislators, including critical communications to Appropriations Committee chair Ted Stevens (R-Alaska) from his home state, and governors led to these opening "victories" on tobacco recoupment. When the supplemental hits the Senate floor, states will again be tested. Senator Orrin Hatch (R-Utah) is working on recoupment legislation that may earmark as much as 25 percent of state settlement funds. On the other side of the aisle, Senator Kent Conrad (D-North Dakota) is drafting a similar proposal that would designate that 10 percent to 20 percent of settlement funds be spent for smoking cessation, smoking abatement and related health programs. Senate floor action is scheduled for next week. State legislators should urge their U.S. senators to support the recoupment prohibition provision, as is, in the FY 1999 supplemental appropriations bill.

On the cosponsorship front, communications from state legislators and NCSL advocacy efforts continue to produce outstanding bipartisan results. S.346 now has 41 cosponsors with this week's addition of Senators Mike Crapo (R-Idaho), Carl Levin (D-Michigan), John Edwards (D-North Carolina), Chuck Robb (D-Virginia) and John Warner (R-Virginia). H.R. 351's cosponsorship count has soared to 90. Signing up this week were Representatives Adairholt (Alabama), Campbell (California), Tancredo (Colorado), Goss (Florida), Lucas, Northup, Rogers and Whitfield (Kentucky), Upton (Michigan), Sununu (New Hampshire), Roukema, Saxton and Smith (New Jersey), Gilman, Kelly and King (New York), Hayes (North Carolina), Noy (Ohio), Wamp (Tennessee), Barton, Combest and Lampson (Texas), Pickett (Virginia) and Sensenbrenner (Wisconsin). State legislators should continue to press their congressional delegations to cosponsor S. 346 and H.R. 351. (NCSL staff contacts: Michael Bird, Joy Johnson Wilson, Steve Lewis)

WELFARE BLOCK GRANT FUNDS "SEIZED." During further debate on S. 544, the committee that produced the recoupment victory also fired the first shot of what will likely be many attempts to reduce current year and future Temporary Assistance for Needy Families (TANF) funding. The Senate Appropriations Committee, without objection, took \$350 million of FY 1999 TANF funds as an offset for its \$1.8 billion "emergency" supplemental appropriations bill. The supplemental primarily provides disaster and foreign aid assistance. NCSL and governors objected strenuously. NCSL Health and Human Services chair, Representative Bill Martin (North Carolina), wrote on March 8 that this action "abrogates a fundamental agreement reached among state legislators, governors and Congress in 1996 regarding welfare reform." The White House opposed this offset. Many members of Congress believe that states are sitting on mountains of unused TANF funds, and therefore there is no need to stick to the agreement reached over two years ago, even though it was a five-year agreement. To stop these attempts in their tracks, state legislators should contact their U.S. senators and urge them to drop this \$350 million offset, preserve the 1996 welfare reform accord and protect the block grant commitment. (NCSL staff contact: Sheri Stelsel)

SENATE FIRST TO ACT ON Y2K LIABILITY PROTECTION. On a straight party-line vote (11-9), the Senate Commerce Committee voted to limit liability for Y2K failures. S. 98, introduced by Senator John McCain (R-Arizona), would preempt state tort law by setting federal caps on non-economic damages and liability of corporate officers and directors, and creating federally determined time periods for remediation before plaintiffs can proceed with lawsuits. McCain's bill also would create immunity from punitive damages for state and local governments. Awaiting action in the Senate Judiciary Committee is legislation, S. 481, introduced by Senator Orrin Hatch (R-Utah) which is similar to the McCain approach in capping damages. However, S. 481 would establish a program to provide financial assistance grants to state and local governments and small businesses to fix their Y2K problems. The Hatch bill has the support of the Chamber of Commerce and many other business associations. In the House, Representative Tom Davis (R-Virginia) has introduced legislation which is similar to the Hatch version, except that the Davis bill, H.R. 775, also would cap attorney's fees. While further Committee action is expected in the Senate, the Davis bill is on hold in the House Judiciary Committee. (NCSL staff contact: Neal Osten)



William T. Pound
Executive Director

Carl Tubbsing
Deputy Executive Director

Federal Affairs Staff

Michael Bird: (202) 624-8688
Joy Johnson Wilson: (202) 624-8688
Alyson McLoughlin: (202) 624-8691

Washington Office:
444 M. Capitol St., N.W., Suite 515
Washington, DC 20001
Ph: (202) 624-5400
Fax: (202) 757-1069

Denver Office:
1560 Broadway, Suite 700
Denver, CO 80202
Ph: (303) 836-2200
Fax: (303) 863-8023



NCSL

Federal Budget & Tax Update

An Information Service of the AFI Federal Budget and Taxation Committee
February 2, 1999, Vol. 5, No. 1

President's Budget for FY 2000 Released State Tobacco Funds Targeted

The President's **Fiscal Year 2000 Budget** released on February 1, 1999 calls for \$1.765 trillion in funding for the president's fiscal priorities. The budget reserves 62% of the expected budget surplus (over the next 15 years) for Social Security Reform. The president intends to reserve the entire projected FY 2000 surplus, or 117.3 billion for Social Security reform (see chart below). The president's five-year proposal raises spending by \$30 billion.

The Projected Budget Surplus. The president's broad plan for the surplus includes the following;

- reserve 62% of the surplus for Social Security, setting aside roughly one-fifth of that portion for investment in private securities;
- reserve 15% of the surplus for Medicare;
- dedicate 12% to fund a new presidential initiative for Universal Savings Accounts; and
- reserve 11 percent of the projected surplus for military readiness and domestic priorities.

Presidential Priorities. The FY 2000 Budget includes many of the proposals previously announced by the White

House, including a \$1,000 tax credit for long term care costs (\$5 billion over five years) and for a variety of health care, education, environment, international affairs and defense proposals. In education, the president proposes to spend \$200 million for performance accountability, \$600 million for after-school services, \$450 million for technology, \$22 billion for school construction and \$1.4 billion to continue the administration's 100,000 new teachers initiative.

The budget increases funding for child care, including \$6.3 billion over five years to expand the child and dependent care tax credit, \$1.2 billion to increase the child care and development fund in 2000, \$3 billion over five years for a new Early Learning Fund and \$173 million in 2000 for quality improvements.

Labor spending includes \$965 million for job training, \$144 million in additional spending in Welfare-to-Work to support housing and transportation and \$150 million to states to support fathers' efforts to pay child support.

The budget increases the low-income housing tax credit from \$1.25 to \$1.75 per capita (\$1.7 billion in cost over five years).

President's FY 2000 Budget Proposal

Budget Summary (Dollar amounts in billions)

	1998	Estimates					
	Actual	1999	2000	2001	2002	2003	2004
Receipts	1721.8	1806.3	1883.0	1933.3	2007.1	2075.0	2165.5
Outlays	1652.6	1727.1	1765.7	1799.2	1820.3	1893.0	1957.9
Reserve Pending Social Security Reform	69.2	79.3	117.3	134.1	186.7	182.0	207.6
Surplus	0.0	0.0	0.0	0.0	0.0	0.0	0.0
On-budget Deficit (-)	-29.9	-41.7	-12.2	0.2	44.4	31.4	49.8
Off-Budget Surplus	99.2	121.0	129.5	133.9	142.3	150.7	157.8
Resources contingent upon Social Security Reform							
Defense	....	....	....	9.6	17.1	13.0	15.0
Non-Defense	....	....	....	15.1	19.7	16.5	9.2
Priority initiatives	1.6	4.1	7.0	9.9
Debt Service	0.7	2.3	4.3	6.3
Remaining Reserve	107.2	143.6	141.3	167.3

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Committee Staff

- Gem Madrid, Senior Policy Specialist, 202-624-8670
gemmadrid@ncsl.org
- Jennifer Grant, Staff Assistant, 202-624-8188
jennifergrant@ncsl.org

Washington Office

444 North Capitol Street, N.W.
Suite 515
Washington, DC 20001
Phone: 202/624-5400
Fax: 202/737-1069

Health care spending includes \$930 million over five years to extend Medicaid benefits to legal immigrants, \$1.2 billion to help disabled workers buy into Medicaid and Medicare, and \$358 million for mental health grants. States would have the option to provide health care to legal immigrant children, to restore SSI eligibility to legal immigrants with disabilities, and to restore Food Stamp eligibility to certain aged immigrants (\$1.1 billion over five years). The proposal would allow states to provide health coverage to legal immigrant children and pregnant women under Medicaid or CHIP.

\$200 million supports state and local efforts to reduce emissions, \$800 million for the Clean Water State Revolving Fund, a reduction of \$55 million from 1999 levels, and \$825 million for the Drinking Water SRF, and increase of \$50 million over 1999.

Discretionary and Mandatory Offsets. Tobacco revenues, FAA user fees, health care savings, superfund revenues and other fees offset the \$17.1 billion in increased discretionary spending above the caps that the president recommends for 2000. Health care, student loan, revenue and other offsets totaling \$6.5 billion offset the class size, child care, health care, revenue initiatives and other mandatory program increases the president has proposed. Annual examination fees of state-chartered member banks of the Federal Reserve (\$450 million over five years) and state-chartered FDIC insured banks (\$458 million over five years) are included in the offset package.

Tax Plans. The president's budget includes an increase in the federal cigarette tax of 55 cents-per-pack and speeds up the timetable for the 15 cents-per-pack increase included in the 1997 BBA. These increases combined raise \$34.5 billion over five years. The budget offsets \$32 billion in spending by closing "tax loopholes and eliminating unwarranted benefits," the majority of these proposals are aimed at corporate taxes. Proposals that affect individuals include taxation of signing bonuses and income from residence rental, disallowance of interest on debt allocable to tax-exempt obligations, increased penalties for failure to file correct information on returns, withholding of gambling winnings, and a change to the foster child definition under EITC.

Human Services. The president's proposal restores Social Services Block Grant (Title XX) funding to its authorized level of \$2.38 billion, an increase of \$471 million over 1999. The president decreases the amount of TANF that may be transferred to SSBG from 10% to 4.25%, providing federal savings of \$600 million in 2000. The budget reduces the TANF Contingency Fund by \$360 million along with a legislative proposal making it easier for states to access the money. The proposal freezes Supplemental TANF Grants for population increases at FY 1999 levels, for federal savings of \$241 million over five years.

The proposal also eliminates the child support hold harmless payment and reduces the match for establishing paternity from 90% to 66%, providing federal savings of \$324 million over five years and adjusts child support orders, saving the feds \$85 million over five years.

Recoupment of State Tobacco Funds. As suspected, the 2000 Budget includes the president's plan to recoup \$15.98 billion of the \$246 billion settlement reached between the tobacco industry and states during the five-year budget period. Recoupment would not begin until 2001 to allow time for a resolution of the expected federal-state dispute. NCSL opposes efforts by the federal government to recoup state tobacco funds. The administration states (we) will work with the States and the Congress to enact tobacco legislation that, among other things, resolves these Federal claims in exchange for a commitment by the states to use tobacco money to address shared national and State priorities which reduce youth smoking, promote public health and children's programs, and assist affected rural communities.

Medicaid Cost Allocation. As was done with Food Stamps in the Agricultural Research bill, the president's budget reduces state administrative funds by \$300 million annually. For the impact on individual states of this reduction see: <http://www.ffis.org/misc/cost.htm>.

Transportation. Transportation spending includes \$6.1 billion for public transit and \$2.4 billion for planning and congestion. Highway obligation is \$28.3 billion in 2000, an increase of \$1.8 billion above 1999 funding. While providing an increase, the levels set in the president's proposal violate TEA21 because rather than distributing the revenue aligned budget authority (RAB-A) proportionately to the five core highway programs, the administration prioritizes the increase of highway trust fund revenues to other specific categories within transportation. FAA budget authority is set at \$10.1 billion for 2000. The president proposes to eliminate general fund contributions to aviation, reducing funding for the Airport Improvement Program.

Pension Portability. The president's budget allows the use of 403(b) and Section 457 plan funds to purchase service credit through a direct transfer to state and local plans without having to take a taxable distribution of these amounts.

Support for Selected State Programs. A summary of Major discretionary and Mandatory Program funding prepared by Federal Funds Information for States follows this update. The information is available online in PDF format at <http://www.ffis.org/misc/99jmpb.pdf>

President Budget Available On-Line. Access the president's budget at <http://www.gpo.gov/usbudget>

PRESENTATION ON TOBACCO ISSUES and HJR 12

Alaska Department of Law
to
House Finance Committee
February 16, 1999

INTRODUCTION

During the past two years, the Knowles administration, with the help of the Alaska Legislature, has addressed the problems caused by tobacco and the challenge of limiting access on a number of fronts. Our joint efforts have included legislation to increase taxes on tobacco products, measures to limit youth access to tobacco, and stepped-up enforcement activities, and, of course litigation and participation in the national settlement with the industry. The Department of Law's efforts have been closely coordinated with the Alaska Departments of Health and Social Services and Revenue, local tobacco control groups, and other state attorneys general.

ENFORCEMENT OF TOBACCO VENDOR AND TAX LAWS

- **TOBACCO VENDOR ENFORCMENT (STING OPERATIONS):** During 1997 and 1998, the Department of Law ("Law") worked closely with the Anchorage and Juneau Police Departments to coordinate enforcement and prosecution of tobacco vendors that sold tobacco products to persons under 19. Law plans to work with the Fairbanks Department of Public Safety and Fairbanks City Attorney's Office to enforce state tobacco laws during the early spring.
- Today, Law will announce a settlement related to tobacco business licensing litigation with 9 vendors operating a total of 11 stores (5 in Anchorage and 6 in Juneau). The vendors agreed to a settlement that requires. (1) a three-day suspension of their tobacco licenses, (2) that they re-train all of their tobacco sales clerks in stores where violations occurred, and (3) that vendors make contributions totaling more than \$50,000 to a statewide youth tobacco prevention television campaign. This television campaign will air statewide for a month this spring.

- **STATE SALES TAX ENFORCEMENT:** State law requires any person who causes cigarettes to be brought into the state for personal consumption or resale to obtain a license from the Alaska Department of Revenue and pay the appropriate taxes. A federal law known as the "Jenkins Act" requires persons shipping cigarettes into Alaska to provide the state with a list identifying the recipients. With the growth of Internet sales, the Alaska Departments of Law and Revenue have worked closely with the federal Alcohol, Tobacco and Firearms investigators and U.S. Attorney's Office to vigorously pursue illegal cigarette shipments. Investigations are currently underway, and additional investigations are likely.

LITIGATION AND THE NATIONAL SETTLEMENT

- **ALASKA'S LITIGATION:** In April, 1997, Alaska filed suit against the major tobacco manufacturers based on state consumer protection and antitrust laws. The suit was scheduled to go to trial in February, 2000.
- **NATIONAL SETTLEMENT:** On November 25, 1998, after extended negotiations the State of Alaska and 45 other states reached a final settlement of litigation with the tobacco industry – Mississippi, Texas, Florida, and Minnesota had already settled their lawsuits. The settlement, which was approved by the Juneau Superior Court on , ends the State's litigation with the industry. The settlement will mean payments of nearly \$670 million to Alaska over the next 25 years, starting in FY 2000.
- **PUBLIC HEALTH TERMS:** The significant public health terms of the settlement require: bans on marketing to youth; changes in corporate culture; disbanding trade associations; lobbying restrictions; opening industry research; and creation of a national teen smoking foundation and public education fund. The full settlement agreement is available at www.naag.org on the Internet.
- **THE PAYMENT STREAM:** The State of Alaska does not need to pass any legislation to receive payments under the settlement. However, legislation is required to protect Alaska's payments from the rather remote possibility of a nonparticipating manufacturer reduction, which is discussed in more detail below. The State also needs protection against attempts by HCFA (the federal Health Care Finance Administration) to recoup a portion of the state's funds, as will also be discussed below.

Under terms of the settlement agreement, Alaska will receive the following payments:

**PAYMENTS TO ALASKA
under
SETTLEMENT OF TOBACCO LITIGATION**

	Date of Payment	Amount of Payment
Up-front Payment	between April 1999 and June 2000 (depending on actions of other states)	\$8,194,049.54
Annual Payments	between April and June 2000	\$21,890,915.46
	April 2001	\$23,638,672.09
	April 2002	\$28,383,145.58
	April 2003	\$28,651,761.36
	April 2004	\$23,912,967.90
	April 2005	\$23,912,967.90
	April 2006	\$23,912,967.90
	April 2007	\$23,912,967.90
	April 2008	\$24,387,539.93
	April 2009	\$24,387,539.93
	April 2010	\$24,387,539.93
	April 2011	\$24,387,539.93
	April 2012	\$24,387,539.93
	April 2013	\$24,387,539.93
	April 2014	\$24,387,539.93
	April 2015	\$24,387,539.93
	April 2016	\$24,387,539.93
	April 2017	\$24,387,539.93
	April 2018	\$27,327,155.20
	April 2019	\$27,327,155.20
	April 2020	\$27,327,155.20
	April 2021	\$27,327,155.20
	April 2022	\$27,327,155.20
	April 2023	\$27,327,155.20
	April 2024	\$27,327,155.20
	April 2025	\$27,327,155.20
	TOTAL	\$668,903,056.53

- **TIMING OF UP-FRONT PAYMENT:** On December 28, 1998, the tobacco companies paid an up-front payment into escrow as part of the agreement. No legislation is required for Alaska to receive its up-front payment, which will be disbursed to Alaska only when 80 percent of the states' lawsuits are dismissed without any appeal, or on June 30, 2000, whichever comes first. Right now, there are appeals in California and New York, so the anticipated receipt of the up-front payment will probably come closer to June 30, 2000.
- **TIMING OF ANNUAL PAYMENTS:** The first annual payment will be available no later than June 30, 2000. No legislation is required for Alaska to receive its annual payments. Alaska's first annual payment could come as early as April 2000, if 80 percent of the states' lawsuits are dismissed without any appeal, but in any case will be made no later than June 30, 2000. Beginning in 2001, the annual payments will be made to the state on April 15 each year.
- **ATTORNEYS' FEES:** The State of Alaska was represented in the tobacco litigation by the law firm of Hagens & Berman, which represented all the Northwest states. The settlement agreement allows the state's outside counsel to seek payment from the tobacco companies without affecting Alaska's share of the settlement. Hagens & Berman requested reimbursement directly from the tobacco companies, which agreed to pay \$10 million as full payment for the firm's representation of Alaska. This payment did not affect Alaska's share of the settlement. However, when compared to the state's settlement of \$668,903,056.53, the Hagens & Berman fee is approximately 1.5 percent.

THREAT TO SETTLEMENT FROM HCFA

- **FEDERAL RECOUPMENT:** The U.S. Health Care Finance Administration (HCFA) has taken the position that as much as half of the funds recovered through the national settlement are subject to the agency's right of recoupment. HCFA apparently bases its position on an interpretation of §1903(d)(2)(A-B) of the Social Security Act, which states that reimbursements to a state by a third party are "overpayments" from which HCFA may claim a pro-rata share.
 - The agency's position is based on the assumption that the state was specifically suing to collect state and federal dollars under a Medicaid reimbursement theory. One estimate shows that HCFA's interpretation of §1903(d) could result in a loss to the State of Alaska of \$400 million over 25 years. The Department of Law is working through Alaska's congressional delegation and other states to solve this problem, and it will defend the state's right to settlement funds in court if necessary. HCFA has represented

that it will assert its claim against annual state payments beginning after the Year 2000 payment.

- **ALASKA'S RESPONSE TO THREAT: Alaska's Objectives** - The State had four primary objectives when it brought suit against the tobacco industry: (1) to end the industry's targeting of Alaska's children as new consumers for its products; (2) to force the industry to disclose the harmful effects of smoking and decades of research demonstrating that tobacco kills; (3) to thwart the industry's apparent efforts to prevent the development of a safer product; and (4) to require the industry to pay for the harm it already has caused and, in the future, fund public health programs directed at alleviating the related public health concerns.
- **Alaska Sued to Protect Alaskans:** Alaska brought suit to protect Alaskans and to protect the fiscal integrity of the state's Medicaid program against future smoking-related treatment costs. Unlike other states, Alaska did not specifically plead a federal Medicaid recoupment claim in state superior court. Collecting federal dollars is the responsibility of HCFA and the U.S. Department of Justice. The U.S. Department of Justice declined to sue the tobacco industry on behalf of HCFA, and HCFA provided no support to the states during the litigation.
 - **First Proposed Settlement and Congress vs. State Settlement:** The first settlement was signed by the states and tobacco industry on June 20, 1997. It called for the tobacco industry to make payments to the states and fund federal enforcement programs totaling \$368.5 billion over 25 years. This settlement also required congressional approval, which did not occur. Accordingly, the states returned to litigation and resumed negotiations with the industry on their own. The litigation and resumed negotiations resulted in the second state settlement of November 23, 1998. HCFA could have acted along with the states to protect its rights during the second settlement process, but chose not to.
 - **Use of Settlement Funds:** A key provision of the McCain Bill in the 105th Congress provided that if states directed 50 percent of the settlement money (of the proposed 1997 settlement) to supplement but not supplant existing health care programs, HCFA could not assert its claim for recoupment. While the states take the position that all settlement dollars are state funds, many states are abiding by the provisions of the McCain Bill (spending no less than 50 percent to supplement health care-related programs) to protect against recoupment by the federal government.
 - **Recent Development: SB 346:** On February 3, 1999, U.S. Senator Frank Murkowski and U.S. Senator Kay Bailey Hutchinson co-sponsored SB 346. SB

346 would protect all the states' settlement dollars from HCFA's attempted recoupment.

LEGISLATION

- **MODEL STATUTE:** The state is not required to pass the model statute included in the settlement to receive settlement payments. However, if the state does not pass the model statute, the state will risk a possible reduction in payments under the nonparticipating manufacturers' payment (NPM) reduction formula of the settlement. The settlement provides for an adjustment to the state's payments if the participating manufacturers experience a disadvantage and lose market share for sales of their tobacco products to other nonparticipating manufacturers as a result of the marketing restrictions, payments, and other restrictions in the settlement agreement.
- **NPM Risk Low In Alaska** - At this point, the risk to Alaska of a non-participating manufacturer reduction is minimal, given that many of the very small tobacco product manufacturers have decided to sign on to the settlement, which reduces the risk that they will take market share away from the largest companies. The risk is further lowered by the fact that the small tobacco products manufacturers only represent 1-2 percent of the U.S. market, making it unlikely that sales of their products will trigger the nonparticipating manufacturer reductions.
- **NPM Risk Can Be Eliminated** - The risk of nonparticipating manufacturer reductions can be eliminated by passage of the model statute. Under the terms of the settlement agreement, if the state passes the model statute and enforces it, the state will be exempt from any payment reductions even if the settlement was a significant factor contributing to the participating manufacturers' loss of market share.

CONCLUSION

In the upcoming months, Law will be working closely with the Alaska Departments of Revenue and Health and Social Services, and the federal Alcohol, Tobacco and Firearms investigators to assure full compliance with state tax laws. Law is also working closely at the direction of the governor with members of Alaska's congressional delegation to protect the state settlement from HCFA.