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Case 19, Day 1, May 23, 2011

LO: Analyze the lead-up and catalyst of the Master Settlement Agreement and effects since.

Historic Settlement with Big Tobacco Did Not Leave a Strong Legacy in Tobacco Cessation and Provided No Durable Incentives for Cash-Strapped States to Promote Interventions

- "Cigarettes aren't going away. Nobody is about to ban tobacco, nor is anybody about to put cigarette companies out of business, much as they might like to."[1] (Joe Nocera, New York Times, June 18, 2006)
- "Altria Group Inc. posted a 15% rise in first-quarter profit, with its cigarette and smokeless-tobacco segments both pitching in despite slipping volumes. ... Altria reported a profit of $937 million, or 45 cents a share, up from $813 million, or 39 cents a share, a year earlier."[2] (Wall Street Journal, April 11, 2011, covering first quarter earnings of Altria Group Inc.)

***Abstract**: The historic 1998 Master Settlement Agreement (MSA) between the major U.S.-based tobacco companies and 46 states attorneys general and U.S. territories has failed to impact tobacco control because it did not bind states to use settlement funds for tobacco cessation and treatment activities. The tobacco industry was not significantly harmed, nor has the MSA led to clear actions by states to meaningfully control tobacco product sales. Since the agreement was reached, tobacco companies have, overall, increased promotional spending for products that are linked to the deaths of 443,000 Americans annually.[3,4] Most states have failed to direct the billions of dollars from the settlement to tobacco intervention programs at levels suggested by the U.S. Centers for Disease Control (CDC). The fiscal well-being of states today is more firmly connected to tobacco product sales, through the sale of bonds tied to MSA funds paid to states and through tobacco product taxes that fund basic government services—all indicating states' unwillingness to reduce the sale and consumption of tobacco products that kill hundreds of thousands of their citizens annually.*

Introduction: High School instructor Miles Smith's rude encounter with realities of an industry that kills nearly half a million Americans annually leaves him wondering how tobacco firms are still thriving, despite the still ballyhooed[5] legal settlement in 1998 known as the MSA. That landmark agreement created a whopping $206 billion in funding to be shared with 46 states and 5 U.S. territories over 25 years, while the 4 other states (Florida, Minnesota, Mississippi, and Texas) had already settled with tobacco manufacturers for $40 billion. Smith believes the funding should have created campaigns to counter smoking, though he still sees ads that he thinks target youth. Smith is apparently unaware of the most recent profits statement by Altria[2], purveyor of the Phillip Morris brand of products such as Marlboro, and a scathing report by the Campaign for Tobacco-Free Kids that shows states have slashed support for tobacco prevention and cessation activities programs to their lowest level since 1999, despite continued payouts from the MSA.[4] Both are evidence that the settlement failed to deliver a knock-out blow to Big Tobacco, as was optimistically hoped by some public health advocates in 1998. What's more, recession-battered states are now more reliant than ever on the sale of lethal tobacco products to help balance their general budgets.[1]

Regulating a Lethal and Legal Product: Though still exceedingly profitable, large U.S. tobacco companies in the 1990s were on the defensive. Since the 1950s, cigarette smoking had become viewed as socially unacceptable as a result of incremental steps showing the dangers of smoking and tobacco use.[6] In 1964, after the publication of 7,000 articles highlighting the

dangers of smoking, the U.S. Surgeon General issued a warning that "cigarette smoking is a health hazard of sufficient importance in the United States to warrant appropriate remedial action."[6] (See appendix 1.) Congress passed the Federal Cigarette Labeling and Advertising Act in 1965 and the Public Health Cigarette Smoking Act in 1969, which required a health warning on cigarette packages, banned cigarette ads by the broadcast media, and called for an annual health report on the impact of smoking. The ban on tobacco advertising by broadcast media began in 1971. Cigarette ads were removed from television or billboards, and states implemented regulations to control marketing to youth. Smoking was banned from airplanes. By 1999, 42 states had set restrictions on smoking at government workplaces, while 20 states had set similar bans at private work sites.[6] But the biggest threat facing the industry came not from the public health officials or medical experts or the thousands of peer-reviewed studies on the dangers of tobacco and smoking by researchers, but from trial lawyers.

For decades prior to the MSA, Big Tobacco successfully fought off all lawsuits in the courts. The companies prevailed in quashing most public health efforts by containing government regulation at the state level, where public health advocates had little clout to force any controls beyond advertising bans and label requirements.[7] By the end of the 1990s, however, the industry faced financial disaster because of mounting pressure in the state courts. A coalition of trial lawyers and states attorneys general coordinated a strategy that rested on a new and potentially successful legal argument. Its premise was because of the growing costs for smoking-related illnesses, among many persons who received Medicaid, state taxpayers who had not chosen to voluntarily smoke were being asked to cover mounting costs. Thus states could seek to recover those costs for smoking-related illnesses.[7] Mississippi was the first to launch a suit, followed by 17 states in 1996, and then 39 by 1997.[7] Damning evidence was released showing tobacco companies had conspired to repress information on the dangers of their products, and states invoked Racketeer-Influenced Corrupt Organization (RICO) statutes that threatened to multiply damages in the billions for each state. (Michael Mann's critically acclaimed 1999 film called *The Insider* highlights this dense back story.) "It was a moment when the cigarette companies were exceedingly vulnerable, and serious reform could have been imposed by the federal government," writes New York Times columnist Joe Nocera. "But that didn't happen."[1]

Congress Falls Short: The MSA, as Nocera notes, must be seen as a result of the failure by Congress to control tobacco use.[1] In 1998, the stars were aligning for decisive federal intervention against tobacco companies under a Democratic President, Bill Clinton, and a Republican-controlled Congress. Sen. John McCain (R-Ariz.) sponsored the 1998 Tobacco Control Bill (see table 1[8]). Yet as John McKinlay and Lisa Marceau note in their study of this legislative fight, the industry launched a surprisingly inexpensive lobbying campaign costing $40 million, when there was likely sufficient bipartisan backing in Congress, buy-in from the public health community, presidential support, and widespread public support (60%) to garner a congressional win. Instead, public health victory turned into defeat on June 17, 1998,

Table 1: **Provisions of the failed 1998 Tobacco Control Bill in Congress:**

- Cost tobacco companies $516 billion over 25 years.
- Raise cigarette prices $1.10 a pack over 5 years.
- Levy $7 billion on tobacco industry if youth smoking did not meet targets.
- Allow FDA to regulate nicotine.
- Force tobacco companies to make research documents public.
- Restrict tobacco industry's ability to advertise to minors.

due to a U.S. Senate filibuster and the successful media strategy of the five largest tobacco companies.[8,9]

The Settlement: The industry was then able to turn to the mounting litigation with the states attorneys general through the MSA. Faced with possibly bankruptcy[7], Brown & Williamson Tobacco Corp., Lorillard Tobacco Co., Philip Morris Inc. (which later changed its name to Altria), R.J. Reynolds Tobacco Co., Commonwealth Tobacco, and Liggett & Myers moved to settle the pending state lawsuits with the 25-year, $206 billion settlement on Nov. 23, 1998, the largest civil litigation settlement in U.S. history and the largest financial recovery in legal history.[5,10] It settled "all antitrust, consumer protection, common law negligence, statutory, common law and equitable claims for … relief alleged by any of the settling states."[10]

Table 2, highlights of the MSA:

- $206 billion to the states over 25 years.
- A $1.5 billion payment over 10 years to support state antismoking measures.
- A $250 million payment to fund research into reducing youth smoking.
- Permanent limitations on cigarette advertising.
- A ban on using cartoon characters (such as Joe Camel) in advertising.
- A ban on cigarette "branded" merchandise.
- Limits on tobacco industry sponsorship of sporting events (such as the Virginia Slims tennis tournament).
- The dissolution of tobacco trade groups

Numerous concessions were imposed on how cigarettes were to be advertised to minors, with the goal of decreasing youth smoking nationally (See table 2[7]). A separate Smokeless Tobacco Master Settlement Agreement (STMSA) also was signed with the 46 states and U.S. territories and the smokeless tobacco industry to limit the marketing of smokeless tobacco products with similar terms to the MSA.[11]

A Missed "Golden Opportunity"[7]: According to a review of the effectiveness of the MSA by Walter Jones and Gerard Silvestri, it was originally assumed that the states would be willing to spend the revenues from the MSA on smoking-related illnesses and on educing underage smoking, though no provision was written into the MSA requiring that MSA funds had to be spent on tobacco control. "For a brief historical moment, the air was filled not with smoke, but with optimism that soon all states would mount credible, comprehensive tobacco control programs."[7] But Jones and Silvestri conclude that the consensus of researchers is that the MSA has not "significantly harmed" the tobacco industry. While the largest allocation of MSA funds did go to state health care programs, the funds did not focus on smoking-related treatments or youth anti-smoking efforts.[7] The MSA has not led to "clear and straightforward intensification" of state tobacco control efforts, mainly because MSA funds from Big Tobacco have been diverted to other state policy activities.[7]

In many cases, MSA funds were seen by state lawmakers as a cookie jar for all state spending, with health and "general purpose" spending accounting for most MSA expenditures. This has been exacerbated by economic downturns twice since 1998, leaving many states strapped for raising revenues to cover all government activities. MSA disbursements have varied widely by state[7]:

- North Carolina, a tobacco growing state, used much of its funds to support tobacco farmers and their communities.
- North Dakota used 45% of its MSA funds on flood control projects.

- Alabama used more than a more than $1 million in MSA funds for juvenile boot camps.
- A study in 2006 found that in 15 states, no MSA funds were being spent on tobacco control.

One critic of the MSA, Anne Landman of PRWatch, writes: "In the absence of some mandate (backed by a strong enforcement mechanism) saying MSA funds must be spent on tobacco control, throwing a billion-dollar windfall to legislators was bound to create a free-for-all, pork-barrel feeding frenzy. It's hard to believe that the high-level state attorneys at the National Association of Attorneys General couldn't have foreseen that legislatures would divert the windfall to other causes."[12] She argues most of the real gains against the tobacco industry have been made by high cigarette taxes and workplace smoking bans that end smoking in bars and restaurants. Jones and Silvestri agree that "overwhelming evidence" shows the most important factor to deter youth initiation to tobacco use is high prices, including through taxes.[7]

The MSA 12 Years Later: For its part, Washington State's Office of the Attorney General praises the MSA for its bans on advertising and marketing cigarette products, for prohibiting tobacco advertising to those under 18 years, and for releasing classified tobacco industry documents to the public. The release of documents has also been credited for helping a global effort to combat the promotion of tobacco products.[13] The Office of Attorney General notes that the Legacy Foundation, which was created by the MSA, launched a highly successful truth campaign that was linked to a 22% decline in overall youth smoking rates from 2000 to 2002, leading to 300,000 fewer smokers.[5] (The foundation has been attacked by some critics, however, for wasting resources on executive salaries topping $500,000 annually and diverting funding to real-estate acquisitions that do not promote smoking cessation.[14])

However, Washington state like many other states is coming up short in meeting the CDC's recommended spending levels for tobacco prevention, according to a 2011 analysis of the MSA's impacts by the Campaign for Tobacco-Free Kids. The CDC recommends the evergreen state spend $67.3 million annually, while the state as of 2011 has allocated only $13.4 million and has cut state tobacco prevention programs by 50% in the last 2 years.[4] What's more, no new anti-tobacco media ads are being created, and the state's quit line has reduced services.[4] The report by the Campaign for Tobacco-Free Kids further notes that all states, and not just Washington, have cut tobacco prevention to their lowest levels since 1999, when the first MSA funds were disbursed. Other key findings in the report show[4]:

- States are spending only 2% of their MSA revenue on programs to prevent youth from smoking or to help smokers quit, and have cut programs with those services by 28% in the last 3 years.
- State spending for tobacco prevention amounted to just $518 million in FY2011, compared to the $25.3 billion raised from the settlement and tobacco taxes (see appendix 1)
- Only 2 states, Alaska and North Dakota (both resource-rich states with healthy state reserves) are funding tobacco prevention programs at CDC-recommended levels.
- Tobacco companies, whose marketing spending has generally increased since 1999 (see appendix 1), spend nearly $25 to market tobacco products for every $1 states spend to prevent smoking or help smokers quit. (Product placements in movies alone since the MSA have generated the U.S. tobacco companies an additional $900 million in profits.[7])

The report claims prevention programs remain "woefully underfunded" compared to the scope of the health problems associated with tobacco use. The group cites the CDC's estimate that cigarette smoking alone costs the nation $193 billion in annual economic losses.[4]

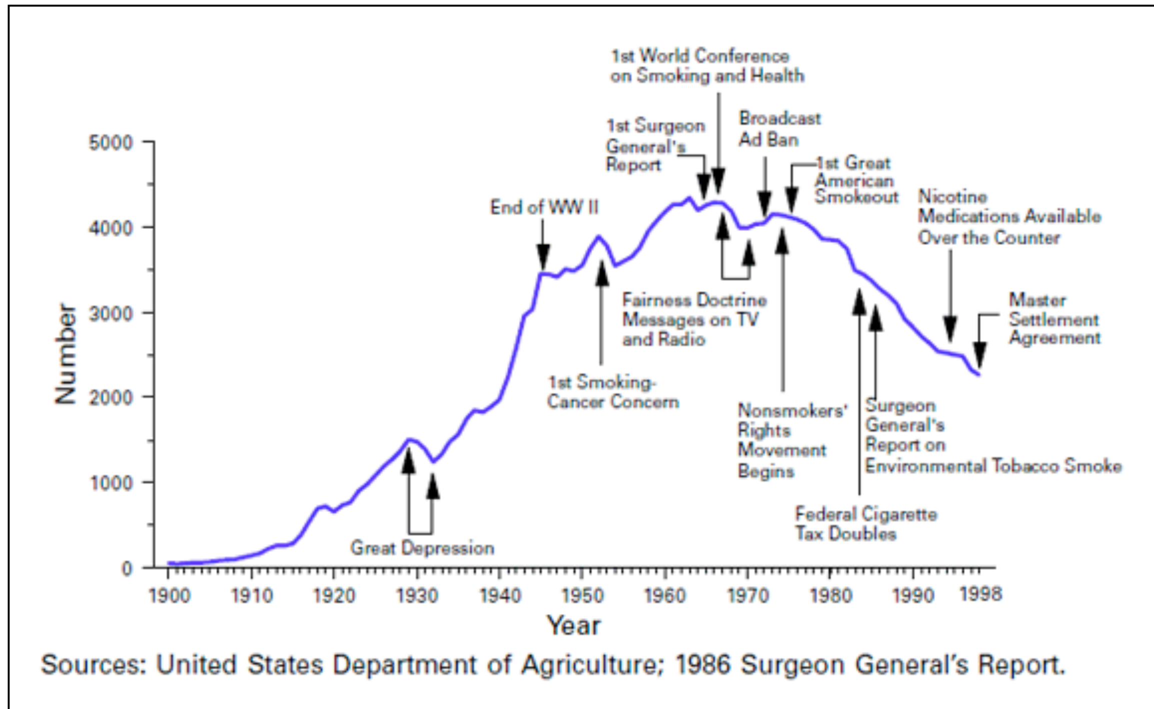
Strange Bedfellows: In an odd twist, states have now aligned themselves to the success of tobacco companies by securitizing MSA payments to raise revenues. MSNBC reports that some MSA payments that are not due for 20 years have already been spent through bonds created by the now-defunct trading firm Baer Stearns and other Wall Street brokerage houses.[15] This unforeseen consequence began immediately after the settlement with the first bonds sold in 1999. Thus, if Big Tobacco fares poorly, states will be liable for large billion-dollar loans. As of 2010, U.S. states have raised more than $107.6 billion in outstanding bonds backed by the 1998 settlement, according to data compiled by Bloomberg News.[16] The trend is worrisome, according to some analysts, given MSA payments to states fell 16% in 2010 and are declining 5.6% this year, and California, Ohio and Virginia are using reserve funds this year to pay interest and principal on bonds backed by the MSA payments.[16] Based on the amount of tax revenues generated from cigarette taxes (see appendix 1) and bond indebtedness of states tied to MSA payments, states are at best ambivalent in wanting to see the industry disappear entirely from the marketplace or in advancing the cause of tobacco prevention and cessation further.[7]

Back to the Case: Our concerned science teacher is enthusiastic that an anti-tobacco campaign aimed at preventing or reducing tobacco use among Central District youth may be productive. He should be concerned, too. Between 2000 and 2009, smoking rates among high school students fell by 39% (from 28% to 17.2%) and by 53% among middle school students (from 11% to 5%), but those declines have leveled off since 2006, as funding for smoking cessation activities dropped.[17] His strategies involve techniques that may have proven effective already in smoking cessation since the MSA was signed. However, Mr. Smith may realize better outcomes to curb the prevalence of tobacco use among youth by trying more upstream advocacy, which could include pushing for stricter state regulations of tobacco products (smoking and nonsmoking) and for raising cigarette taxes even higher. He also may not wish to learn how his state has drastically cut smoking cessation programs and how it likely needs future smokers like these youth to raise revenues that are needed to plug holes in the state budget—now experiencing a $5 billion deficit.

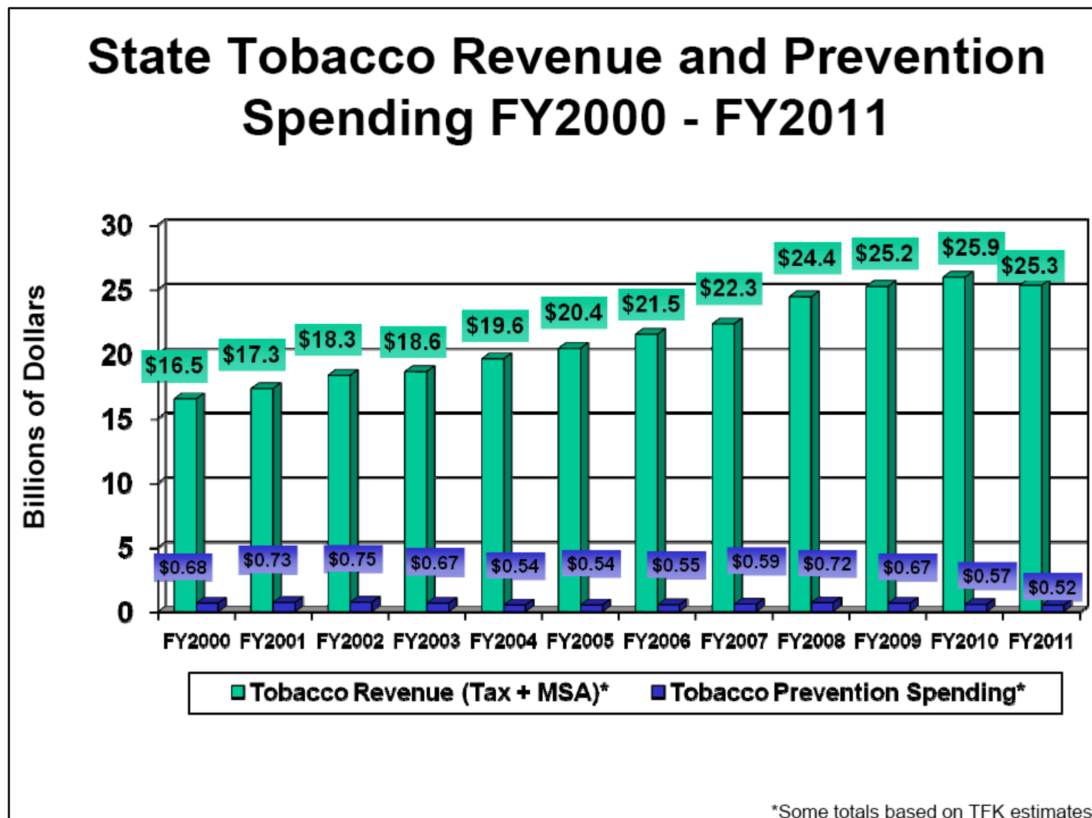
1. Has the securitization of MSA funds by states, including large ones like New York and California, been acknowledged or understood by public health experts in their efforts to develop effective campaigns to curb tobacco use?
2. Are states so beholden to tobacco taxes that their economic self-interest requires that they keep tobacco cessation underfunded, as that is defined by groups such as the Campaign for Tobacco-Free Kids?

Appendix 1:

Annual adult per capita consumption of cigarettes and major smoking health events in the United States 1900-1998.[6]



State tobacco revenue collections and prevention spending since FY 2000.[4]



Marketing expenditures by U.S.-based tobacco firms since the signing of the Master Settle Agreement in 1998.[4]

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