

Prepared Testimony of Jeffrey A. Modisett Attorney General of Indiana
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Mr. Chairman and members of the House Subcommittee on Health and Environment, I appreciate the opportunity to address you regarding the historic tobacco settlement and its impact on the public health of our nation. I have testified in the Senate regarding the impact of the settlement on tobacco growers and believe it important that Congress possess the best information on all facets of the deal as it makes decisions that will change an industry and the lives of countless Americans. As I testify before this Subcommittee, I cannot help but recognize that there is much confusion in many quarters about the goals of the state attorneys general in litigating and then agreeing to settle the states' cases against the tobacco industry.

Each attorney general who brought suit did so to protect children from the industry's unlawful practices and to promote the public health. Thus, nearly all the suing attorneys general brought, on behalf of our respective states, lawsuits based on state-law claims in state courts. Each of us did so to make the industry accountable to the children, addicted tobacco users, and taxpayers of his or her state. Given the states' substantial investments of time and money in devising, litigating, and settling these lawsuits, the states are entitled to the vast majority of the settlement proceeds.

In these remarks, I will address three aspects of financing the proposed tobacco settlement. First, I will discuss the June 20th Settlement Agreement and the payments to be made under the settlement by the tobacco industry. Second, I will explain that the principles behind the distribution of settlement funds are consistent with the states' lawsuits and that states, therefore, should receive a majority of those funds. Finally, I will assert that H.R. 2938, the bill sponsored by Chairman Bilirakis, is an appropriate mechanism to help ensure those principles are served.

By way of introduction, my background is in law enforcement. I was an Assistant United States Attorney in Los Angeles for nearly six years. I then worked for Indiana Governor Evan Bayh and served, among other roles, as the Governor's drug coordinator for the State of Indiana. I quickly learned that underage smoking was often the beginning of a lifelong addiction to nicotine and, in many cases, premature death from smoking-related disease. I next served as the Marion County Prosecutor in Indianapolis for four years. In short, I consider myself a relatively conservative, law-enforcement Democrat.

On February 19, 1997, I filed suit against the tobacco industry on behalf of the State of Indiana. I was involved in some of the negotiations with the industry toward the end of that process. A few weeks before the settlement was reached and announced on June 20, 1997, I was asked to

study aspects of the settlement's financing as it related to the allocation of the industry payments. A subcommittee of attorneys general has conferred several times over the past months to discuss the allocation, and I have continued to discuss the matter periodically with individual attorneys general.

As I point out later in these remarks, I believe there is consensus among the attorneys general on two issues important to this Subcommittee: the relation between the lawsuits and the settlement; and the proper way to calibrate the distribution of funds between the federal and state governments. In determining the propriety of legislation affecting the distribution of tobacco settlement proceeds, it is important to understand the proposed tobacco settlement.

Throughout the negotiating process that culminated in the historic Tobacco Settlement on June 20, 1997, the principal motivation of the attorneys general to settle their lawsuits against the tobacco industry evolved from the same concern that prompted them to initiate those suits -- to protect our children and to promote public health by requiring the industry to disclose its secrets, reform its practices, and pay for its misdeeds. In accomplishing those aims, we always knew that more than money would be required. We pushed hard for advertising restrictions, counter-marketing and cessation programs, compliance checks, retail licensure, stronger FDA enforcement, and the unprecedented Youth Lookback provision. We left the financing of the deal as the final piece of the settlement puzzle; it was not discussed until the final round of negotiations. Yet, the settlement proceeds are also important to public health both in terms of compensating state governments for injuries done to them by the tobacco industry and for a progressive attack on the perils of cigarette addiction and youth consumption. The terms of the June 20th Settlement contemplate these purposes and provide for a distribution of monies to the federal government and the states.

As illustrated by the table below [*table omitted*], over a 25-year period the states are to receive direct payments of \$193.5 billion (represented by the total of column 7) which includes the "up-front" payment. The remaining \$175.5 billion (the total of columns 3-6) is earmarked for the federal government and other purposes national in scope.

While the June 20th Settlement served as a baseline for a national tobacco control program -- a baseline that can and should be strengthened -- the principles behind any distribution of settlement funds should be the same regardless of the final shape of the legislation. In addition to providing a national tort fund for persons harmed or killed by tobacco use, it is sensible that the federal government receive a reasonable portion of the settlement proceeds to administer certain national programs.

Thus, the Food & Drug Administration, the Department of Health and Human Services, and other appropriate federal agencies should receive funds to administer smoking cessation and counter-marketing programs. Moreover, a sizable federal trust is to be established for the benefit of public health. These federal uses of the settlement proceeds would not have been forthcoming without the states' initiative. Thus, limited distributions to the federal government are

appropriate for these narrow purposes, but state governments should receive the bulk of funds derived from the settlement. The emphasis on state control of the settlement proceeds is appropriate in light of the nature of the lawsuits states brought against the tobacco industry.

The national settlement constitutes the compromise of the states' ability to sue the tobacco industry for its many past transgressions. The gravity of the states' compromise of claims cannot be overstated. This is no less than the release of the states' sovereign power to sue an industry whose deceit and greed unnecessarily has caused and is causing the premature death of millions of Americans. Obviously, the states would never have pledged to concede their rights to sue the tobacco industry without being convinced that the benefits to be conferred on them -- as states -- made the concession worthwhile. The commitment of the attorneys general to ensure their states receive the benefit of their bargain is stronger than ever.

The industry's remarkable public-health and monetary concessions are a direct result of the states' lawsuits and strong positions during settlement negotiations. The states seek, among other things, money damages in their lawsuits. Some of these damages were compensatory in nature, owing to the injuries to state-funded health-care programs and other state interests because of smoking-related illnesses. Most states also sought damages -- including punitive damages, treble damages, and/or severe penalties -- for unfair trade practices, consumer protection violations, and racketeering. Many states, including Indiana, brought claims of public nuisance and contributing to the delinquency of a minor.

A number of state attorneys general and certain members of Congress encouraged the federal executive branch to sue the tobacco companies for federal Medicare monies spent to treat smoking-related diseases, but the federal government declined to do so. Therefore, the states are entitled to retain or otherwise maintain control over the settlement proceeds they worked diligently and tirelessly to garner and for which they have given up the right to seek damages and equitable relief.

After the states' announced the proposed settlement and its unprecedented monetary sanctions exacted from the tobacco industry, agents of the federal government declared on several occasions that most if not all of that money is to fill federal and not state coffers. Indeed, it is widely reported that the Health Care Financing Administration has already sought to take a sizable portion of the settlement funds realized by Florida and Mississippi. In light of the nature of the litigation and settlement processes discussed above, it is not too strong a characterization to say that state governments are incredulous to the notion that they have been spending their time and resources to secure a recovery for the federal government.

On this point, the state attorneys general and the National Governors' Association are unified: the states want the benefit of their bargain. The assertion, championed most vigorously by the career bureaucrats in the Department of Health and Human Services, that the settlement encompasses mostly "federal money" is patently wrong. First, the settlement is a result of the compromise of state claims. The federal government retains the right to sue or negotiate a

settlement with the industry for injuries the federal government believes it has suffered to programs such as Social Security, Medicare, Medicaid, and veterans' benefits.

The states, on the other hand, will give up their right to sue by settling. It is incongruous to enrich the federal government on the backs of state governments that have compromised their claims. Second, while the federal government may, under present federal law, exact a Medicaid lien for overpayments recovered by states, Medicaid claims constitute at most a small part of states' lawsuits. Indeed, some states do not even maintain Medicaid claims in their litigation.

Moreover, the financing structure of the proposed settlement bears no relation to recovery for Medicaid claims, but is better characterized as compensation for money damages states have sought including a sizable amount of punitive damages. Thus, the compromise of Medicaid claims constitutes a small part of the overall settlement picture. Third, since the federal government is already receiving substantial funds under the settlement to administer important facets of the settlement, it would be harmful to the beneficiaries of the settlement plan for the federal government to attempt to exact additional funds from settlement proceeds for unstated federal purposes.

Because HHS and HCFA have threatened to wage a battle with states over the tobacco-settlement proceeds, and because the true federal character of the settlement proceeds is minimal, legislation like that proposed by Chairman Bilirakis is quite desirable. I believe that H.R. 2938 is the right approach to ensure that the executive branch of the federal government does not embroil the states in unfortunate litigation over the settlement recovery. I also believe Congress should go further and resolve not to deprive the states in any other fashion of the \$193.5 Billion in direct payments from the tobacco industry over the first twenty-five years of the settlement. There is every reason to think states will make appropriate use of funds they receive.

Tobacco-related illness and use trends differ among the states and regions of our country. I personally favor directing most or all of the money to public health, but am not receptive to a federal mandate or attachment of strings to the money. I have already begun discussions with my governor and state legislators about potential public health uses of the settlement proceeds should the settlement be passed. Ultimately, state governments, and not the federal government, are in the best position to determine the proper uses of the majority of the settlement funds. Yet we are also committed to have the settlement proceeds fund certain national programs to be administered by the federal government

The attorneys general also have been working on a method of allocating monies received from the tobacco settlement by the states. In a nutshell, the subcommittee of attorneys general I chair has recommended a compensatory model that is based on past harms to the states caused by the tobacco industry. We chose this type of model because of the commonality of certain claims throughout the states' cases. (The evidence and methods of proof required at trial, as well as the claims, vary significantly from state to state.) The variables used to allocate the settlement

proceeds are proxies for states' costs of smoking related illness and for the tobacco companies' various unlawful business practices. The formula allocates settlement proceeds among all fifty states, the District of Columbia, and all five U.S. Territories.

In conclusion, the attorneys general could not be more steadfast in their belief that the states ought to receive the benefit of their bargain. We undertook this massive litigation and settlement process to promote the public health and to produce a meaningful structure for protecting our children from the tobacco industry. For the federal government to exact money from the state portion of the settlement proceeds is not only unfair but is likely to be counterproductive.