HOUSE BILL REPORT
ESB 5485

As Passed House:
April 25, 1999

Title: An act relating to a reserve account for tobacco product manufacturers not participating in the master settlement agreement.

Brief Description: Regulating certain tobacco product manufacturers.

Sponsors: Senators Thibaudeau, Deccio, McDonald, Snyder, Winsley, Kline, Oke and Costa; by request of Attorney General.

Brief History:
Committee Activity:
Health Care: 3/18/99, 4/1/99 [DP].
Floor Activity:
Passed Senate: 2/24/99, 40-8.
Passed House: 4/25/99, 77-19.

Brief Summary of Engrossed Bill

- Ensures that tobacco manufacturers not participating in the settlement cannot obtain an unfair market advantage.
- Provides the state Attorney General with adequate enforcement authority.

HOUSE COMMITTEE ON HEALTH CARE

Majority Report: Do pass. Signed by 11 members: Representatives Cody, Democratic Co-Chair; Parlette, Republican Co-Chair; Pflug, Republican Vice Chair; Schual-Berke, Democratic Vice Chair; Alexander; Boldt; Campbell; Conway; Edmonds; Mulliken and Ruderman.

Staff: Bill Hagens (786-7131).

Background:

On November 23, 1998, Washington State joined 45 other states in settling litigation brought against the tobacco industry for violations of state laws concerning consumer protection and antitrust. In doing so, Washington became part of the so-called Master Settlement Agreement, which had the effect of settling ours and all the states' suits against the industry.

Four of the country's largest tobacco manufacturers signed the agreement, and thus became bound by the following conditions: The companies agreed to significant curbs on their advertising and marketing campaigns; to fund a $1.5 billion anti-smoking campaign; and to open previously secret industry documents and disband industry trade groups. Further, they are prohibited from using cartoon characters in tobacco advertising, from targeting youth in ads and marketing, using billboards and transit advertising, and from selling and distributing apparel, backpacks and other merchandise which bear brand name logos.

The financial provisions of the Master Settlement Agreement include billions of dollars paid out to the settling states in perpetuity, beginning with up-front payments of more than $12 billion by 2003. Washington State could receive approximately $4.02 billion over 25 years. Annual payments will begin on April 15, 2000, and will result in Washington receiving approximately $323 million by the end of the 1999-2001 biennium.

Settlement negotiations originated with the four major tobacco companies; however, there are tobacco product manufacturers in business now and there could be those in the future who can sell products at a reduced price with no marketing or advertising restrictions because they are not bound by the Master Settlement Agreement.

States are encouraged to pass model statutes that create a reserve fund for nonparticipating manufacturers to pay future claims. The fund would serve as a source of compensation should these companies be found culpable in future litigation, and go bankrupt or out of business, rendering them judgment-proof. Requiring that nonparticipating companies pay into this fund also provides some protection against these companies selling their products at reduced rates, undercutting the market and making huge short-term profits.

Summary of Bill:

Any tobacco product manufacturer selling cigarettes to consumers in this state, whether directly or through intermediaries described in the bill, is required to either join the Master Settlement Agreement and perform its financial obligations, or place money into a qualified escrow fund. The funds placed in escrow can only be used to pay a judgment or settlement on any claim brought against the company, or to reimburse a manufacturer if an annual payment into this account is greater than the

payment required under the Master Settlement Agreement. The amount nonparticipating companies pay into escrow is based on their market share. If at the end of 25 years no funds are released for the two cited reasons, all funds, including interest, are released back to the manufacturer.

Any tobacco product manufacturer that elects to place money into the escrow account must annually certify compliance with the provisions of this act with the Attorney General. The state may bring civil action on behalf of the state against any tobacco product manufacturer that fails to comply.

Appropriation: None.

Fiscal Note: Available.

Effective Date: The bill contains an emergency clause and takes effect immediately.

Testimony For: This legislation is necessary for the state to receive the full amount of the tobacco settlement due Washington.

These payments are not a tax in the legal sense. The purpose of payments placed into escrow by nonparticipating tobacco manufacturers is not to raise revenues for the state, but to provide a contingency fund should the non-participating manufacturer engage in conduct deemed unlawful by the Master Settlement Agreement (MSA). Under the Model Statute, escrow funds are to be held by a qualified financial institution. Any payments into the fund in excess of those required under the MSA may be returned, and the balance of the escrow fund, with interest, is to be returned to the manufacturers after 25 years. The state can only access the escrow funds if it brings a claim against the manufacturer and either obtains a judgment or the case is settled. The escrow fund is more similar to bonding requirements established to ensure parties with claims can be paid.

Testimony Against: None.

Neutral Testimony: Essentially the bill requires a tax on the non-participating tobacco manufacturers, but it is not like a simple raise in the cigarette tax for Washington state because it is compensating and "leveling the playing field" between participating and non-participating manufacturers.

If every state passes this legislation, then any reduction in payments is allocated the same across the states according to the same distribution methods that allocate the dollars. If there is any state that has not passed this legislation, then that state is the first assessed by a reduction in dollars up to 65% of what it is owed.

The MSA sets up an incentive for every state to pass the legislation because states that do not will be left "holding the bag" because those are the states from which the non-participating adjustment will first come.

Testified: Elaine Rose and John Hough, Attorney General's Office.

(expert witness) Jonathan Gruber, MIT Department of Economics.