

MAINE STATE LEGISLATURE

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DAVID G. LEMOINE
Treasurer of State

State of Maine Office of the Treasurer of State

39 State House Station
Augusta ME 04333-0039

To: Members, Joint Standing Committee on Appropriations and Financial Affairs
Members, Joint Standing Committee on Health and Human Services
Fr: State Treasurer David Lemoine
On: December 2, 2009
Re: 2009 Tobacco Settlement Payments Report

Mandated Report: The State Treasurer is required to report the status of Maine's Tobacco Settlement Payments each December to the Joint Standing Committees on Appropriations and Financial Affairs and Health and Human Services. The report must summarize the activity in any funds or accounts directly related to the Fund for a Healthy Maine. *See 22 M.R.S.A s. 1511(8)*

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EXECUTIVE SUMMARY

In 1998, Maine, along with 45 other states and 6 U.S. Territories became creditors of Participating Cigarette Manufacturers (PMs) pursuant to a Master Settlement Agreement (MSA) made between the states and many cigarette manufacturers settling lawsuits brought by these states and territories. Florida, Minnesota, Texas and Mississippi had already reached individual agreements with the tobacco industry. The MSA exempted participating cigarette manufacturers from liability to the state governments arising from the claims alleged in the states' lawsuits, and provided those state governments with compensation for smoking related medical costs and the states' other monetary claims, and with funding to help reduce smoking in the United States through a national foundation. The MSA also limited the marketing and advertising practices of the cigarette manufacturers to further protect public health.

Maine's continuing receipt of Tobacco Settlement Payments hinges on three (3) key factors:

1. Enforceability: The continuing enforceability of the manufacturers' Master Settlement Agreement payment obligations.
2. Financial Capacity: The continuing financial capacity of the OPMs and SPMs to make timely Master Settlement Agreement payments.
3. Legal Actions: Legal actions which delay or alter Master Settlement Agreement Payment obligations.



PAYMENTS FORMULA AND REVENUE PROJECTION PROCESS

ELIGIBILITY: Maine will always receive 0.7693050% of the Annual Payments paid in perpetuity pursuant to the MSA. In addition, Maine will also receive 1.3281978% of the Strategic Contribution Payments during the years 2008 through 2017. Maine is eligible for these supplemental payments as a result of our early involvement in the work which resulted in the MSA. Payments are due in April each year.

PAYMENTS FORMULA: Annual settlement payments are driven by two key annual adjustments, the 1) inflation adjustment and the 2) volume of cigarettes sold nationwide. Under the Inflation Adjustment, the base annual payments will increase annually by the greatest of 3% or CPI, (the Consumer Price Index). Under the Volume Adjustment, the MSA tobacco payments due from the manufacturers are either reduced or increased depending on whether the Original Participating Manufacturer's national sales volumes for a given sales year are less than or greater than, respectively, the national cigarette sales volumes for 1997. Maine's Tobacco Settlement Payments are directly related to the shipments of cigarettes nationwide, without regard to increases or decreases in Maine cigarette sales.

REVENUE PROJECTION PROCESS: The Treasurer's Office organizes a meeting of the Maine Attorney General's Office, the State Budget Office and the Legislature's Office of Fiscal and Program Review in advance of each Revenue Forecasting Committee meeting in order to reach consensus on the revenue forecast. That meeting agenda includes a review of econometric models available from Global Insights and the National Association of Attorneys General that project domestic consumption of cigarettes. Each meeting also discusses the likely impacts on Maine's payments stream of any disputes pending under the MSA.

Under the MSA, a participating tobacco company may be entitled to a reduction in its annual payment obligation for the Non-participating Manufacturer Adjustment if two things are determined in its favor: First, an economic firm determines that the disadvantages imposed upon it by the MSA were a significant contributing factor in its loss of market share to non-participating manufacturers (NPMs), and; Second, recovery of this NPM Adjustment amount from an individual state is dependent on a) whether the state had a qualifying statute governing NPM escrow deposits in place during the relevant sales year and b) whether the individual state diligently enforced that qualifying statute.

Beginning in sales year 2003 and continuing through sales year 2008, the PMs have claimed that they are entitled to the NPM adjustment, which if true would result in a decrease in the amount the PMs owe under the MSA for those years. Maine asserts that it has had a qualifying statute in place for all relevant sales years and that it has diligently enforced that statute. If Maine's assertion is found to be correct in an MSA arbitration proceeding, Maine will not experience a reduction in its payment amount due to the NPM Adjustment. If, however, Maine is found not to have diligently enforced, the State's liability could be up to its entire annual payment amount.

Once the PMs dispute the calculated amount they owe by claiming entitlement to the NPM Adjustment, they have three options under the MSA. They may pay the contested amount to the State anyway, as Phillip Morris has done for sales years 2003-2008, or the PM may place the amount in a disputed payment account, which R.J Reynolds did for 2003-2007. To-date R.J. Reynolds has



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escrowed more than \$1.6 billion into the disputed-payments account for the NPM Adjustment for those years. Finally, the PMs may simply withhold the amount they dispute from their annual payments, and many PMs have done this.

If Maine is found to have diligently enforced its qualifying NPM escrow statute, the State will be entitled to the amounts still owed by R.J Reynolds and other PMs.

TOBACCO SETTLEMENT PAYMENTS, DEPOSITS, TRANSFERS, EARNINGS, AND FHM BALANCES

The State of Maine has received \$534,804,532 to date from the Tobacco Settlement. Each payment is deposited into the Fund for a Healthy Maine (the "Fund") where it is invested in the Treasurer's Cash Pool. All investment earnings on these funds are deposited back into the Fund.

A full history of Tobacco Settlement payment transactions is set forth in **Attachment A**.

Attachment A



Tobacco-FHM-
FY09.xls

ESTIMATED FUTURE TOBACCO SETTLEMENT PAYMENTS (AS REFLECTED IN THE DECEMBER 2009 REVENUE FORECASTING COMMITTEE'S REPORT)

Source	FY-10	FY-11	FY-12	FY-13
Base Payments	\$45,253,322	\$42,839,213	\$49,128,512	\$48,438,445
Strategic Contribution Payments	\$ 9,716,966	\$ 9,227,296	\$ 9,351,164	\$ 9,256,695
Racino Payments	\$ 5,276,923	\$ 5,382,971	\$ 5,624,388	\$ 5,905,608
Investment Income	\$ 21,142	\$ 11,953	\$ 17,256	\$ 19,632
Offsets	\$ 92,660	\$ 145,147	\$ 161,699	\$ 164,662
Total	\$60,175,693	\$57,316,286	\$63,959,621	\$63,455,718

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December 2009

Fund for a Healthy Maine
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Fiscal year	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	Total
Beginning Balance		61,280,943	43,892,730	43,464,808	8,674,690	4,045,268	5,081,373	5,260,296	3,619,946	7,959,654	
Add: Tobacco Settlement	63,176,643	47,819,280	56,292,287	55,807,033	48,952,964	49,033,129	45,011,759	47,113,687	58,219,190	63,378,561	534,804,532
Investment Earnings	1,604,300	3,605,927	1,233,998	681,756	54,830	91,444	124,780	297,803	64,695	49,819	7,809,353
Racino Revenue							1,771,173	3,538,805	3,735,774	4,981,163	14,026,914
AG Reimb/Other Income			25,475			220	39	217	25,080	192	51,224
Less: Legislative Transfer of Revenue & Others	(3,500,000)	(68,813,420)	(57,979,682)	(91,278,906)	(53,637,216)	(48,088,688)	(46,728,827)	(52,590,863)	(57,705,031)	(64,523,704)	(544,846,338)
Ending Balance	61,280,943	43,892,730	43,464,808	8,674,690	4,045,268	5,081,373	5,260,296	3,619,946	7,959,654	11,845,686	11,845,686

General Fund Cash Flow Support	24,700,000	20,000,000	24,700,000	20,000,000	33,000,000	24,200,000
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