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STATE SPENDING OF TOBACCO SETTLEMENT REVENUES

HEARING

BEFORE THE

COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION UNITED STATES SENATE

ONE HUNDRED EIGHTH CONGRESS

FIRST SESSION

NOVEMBER 12, 2003

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SENATE COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION

ONE HUNDRED EIGHTH CONGRESS

FIRST SESSION

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STATE SPENDING OF TOBACCO SETTLEMENT REVENUES

WEDNESDAY, NOVEMBER 12, 2003

U.S. SENATE,
COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION,
Washington, DC.

The Committee met, pursuant to notice, at 9:30 a.m. in room SR–253, Russell Senate Office Building, Hon. John McCain, Chairman of the Committee, presiding.

OPENING STATEMENT OF HON. JOHN McCAIN, U.S. SENATOR FROM ARIZONA

The CHAIRMAN. Good morning. Today's hearing gives the Committee an opportunity to learn more about how states are spending revenues derived from the $247 billion Master Settlement Agreement, MSA, that was reached in 1998 between the states and the Nation's four largest tobacco companies. As this month marks the 5-year anniversary of the MSA, now is an appropriate time to revisit the effects of the agreement.

I would like to have our witnesses come forward now.

In the U.S. alone, an estimated 400,000 people die each year as a result of a smoking-related illness, which equates to approximately 1,200 smoking-related deaths per day. Nearly 2,000 children start smoking each day. Sixty percent of smokers in this country begin before the age of 14, and nearly 90 percent become addicted by age 19. While the Surgeon General estimates that 75 percent of smokers want to quit, only slightly over 2 percent actually succeed each year. Globally, the World Health Organization estimates that eight out of a hundred people who are currently alive will die from smoking.

These statistics underscore the importance of both investing in tobacco prevention programs and preventing targeted tobacco marketing designed to allure our children. The MSA settled lawsuits filed by numerous states seeking reimbursement for decades of healthcare expenditures on tobacco-related illnesses and deaths. While the MSA does not direct how states allocate their settlement payments, one of the most recurring and dominant refrains of state officials pursuing litigation was the critical need to reduce the use of tobacco products by our youth. In fact, several of the recitals set forth in the beginning of the MSA expressly indicate the settling state's intention to dedicate significant MSA fundings to the reduction of youth smoking.

In addition, in a resolution that was passed in 1999 and 2001 by the members of the National Governors Association, the Nation's

Governors committed to spending, "a significant portion of the settlement funds on smoking-cessation programs." However, the state legislatures have committed their settlement revenues for other purposes. The NGA's promises have eroded over time. This fact is most apparent in its 2003 resolution that omits any reference to spending settlement funds on smoking-cessation programs.

The Campaign for Tobacco-Free Kids is expected today to release a report that confirms that the vast majority of states are failing to live up to their promises to fund tobacco-related programs. The report will show that only four states are funding tobacco prevention programs at the minimum recommended level suggested by the U.S. Centers for Disease Control, a level that typically amounts to only a fraction of a state's overall tobacco revenue. Despite the nearly $20 billion the states expect to receive from the MSA in Fiscal Year 2004, states will spend less than 3 percent of that total on tobacco prevention programs, which is less than half the CDC's recommended funding level.

We are all fully aware of the budget shortfalls that are being experienced by the states, but isn't an ounce of prevention better than a pound of cure, from both a long-term economic perspective and a moral perspective? I'd like to better understand why states are, to a large degree, ignoring the problem of youth smoking.

The Surgeon General testified in the year 2000, before this Committee, that smoking prevention programs work and that proper funding of these programs could cut smoking rates in half by 2010. I believe that the MSA settlement revenues may be our best chance to dramatically reduce smoking rates, especially among our children.

Before we proceed any further, I want to mention my disappointment that the U.S. Department of Health and Human Services declined our invitation to have the CDC appear today. Perhaps that's an indication of the Department of Health and Human Services' involvement and interest in this issue.

[The prepared statement of Senator McCain follows:]

PREPARED STATEMENT OF HON. JOHN MCCAIN, U.S. SENATOR FROM ARIZONA

Good morning. Today's hearing gives the Committee an opportunity to learn more about how states are spending revenues derived from the $247 billion Master Settlement Agreement (MSA) that was reached in 1998 between the states and the Nation's four largest tobacco companies. As this month marks the five-year anniversary of the MSA, now is an appropriate time to revisit the effects of the agreement.

In the U.S. alone, an estimated 400,000 people die each year as a result of a smoking-related illness, which equates to approximately 1,200 smoking-related deaths per day. Nearly 2,000 kids start smoking each day. Sixty percent of smokers in this country begin before the age of 14, and nearly 90 percent become addicted by age 19. While the Surgeon General estimates that 75 percent of smokers want to quit, only slightly over two percent actually succeed each year. Globally, the World Health Organization estimates that eight out of 100 people who are currently alive will die from smoking. These statistics underscore the importance of both investing in tobacco prevention programs, and preventing targeted tobacco marketing designed to lure our children.

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In addition, in resolutions passed in 1999 and 2001 by the members of the National Governors Association (NGA), the Nation's Governors committed to spending "a significant portion of the settlement funds on smoking cessation programs." However, as state legislatures have committed their settlement revenues for other purposes, the NGA's promises have eroded over time. This fact is most apparent in its 2003 resolution that omits any reference to spending settlement funds on smoking cessation programs.

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Before we proceed any further, I want to mention my disappointment that the U.S. Department of Health and Human Services (HHS) declined our invitation to have the CDC appear today. I thank the witnesses for being here and I look forward to your testimony.

The CHAIRMAN. Our witnesses today are the Honorable Mike Moore, Attorney General of the State of Mississippi; Mr. Matt Myers, President of Campaign for Tobacco-Free Kids; Mr. Raymond C. Scheppach, the Executive Director of the National Governors Association; the Honorable Deborah Hudson, Delaware State Legislature; and Dr. Carol Healton, President and CEO of the American Legacy Foundation.

Dr. Healton, we'll begin with you.

STATEMENT OF DR. CHERYL G. HEALTON, PRESIDENT AND CEO, AMERICAN LEGACY FOUNDATION

Dr. HEALTON. Chairman McCain, Senator Hollings, and other distinguished Members of the Committee, I deeply appreciate this opportunity to testify on behalf of the American Legacy Foundation.

Our mission is to build a world where young people reject tobacco and anyone can quit. Every day in America, 1,200 lives are lost to tobacco-related disease. On that same day, 4,400 young people under the age of 18 smoke their first cigarette.

We are the national foundation born of the Master Settlement Agreement and funded through dollars directed to us by the states. Among the members of our Board are two—of directors—are two representatives each, designated by the National Association of Attorneys General, the National Governors Association, the National Conference of State Legislatures. I am especially pleased to serve on a panel with these organizations.

Governor Napolitano, of Arizona, currently serves as one of the NGA representatives on our board, and she sends her special greetings to you, Chairman McCain.

We are here, not to lobby today, but rather to assist the Committee in its oversight responsibilities by sharing our insights and experiences regarding the use of the MSA funds by the states. Perhaps because of our board's structure, Legacy is sensitive to the Solomon-like choices that must be made by states facing unprecedented budget deficits and escalating demands for resources. Nonetheless, we must add our voice to the public-health chorus that would remind states of the long-term consequences of today's decision to rob Peter to pay Paul. The tobacco epidemic costs the U.S. $158 billion a year and hundreds of thousands of lives needlessly lost.

Because only a small proportion of the original funds disbursed to the states via the MSA have been spent by the states to prevent or reduce tobacco use, and because of recent budget shortfalls, Legacy has become a de facto safety net at the national level. It is a role that will be increasingly difficult for Legacy to fulfill.

At a time when state programs are critically wounded or disappearing, including some of the most effective, like those in California, Florida, Massachusetts, or Oregon, Legacy is faced with its own funding cliff, which is shown on the charts here.

Payments would be made to Legacy under the agreement only if the participating manufacturers controlled 99.05 percent of the market share of tobacco sales nationally. Last April, Legacy received what it believes to be its last major payment, pursuant to the MSA, and that payment would be $330 million, so the wound is quite critical.

In 2001 alone, the tobacco industry spent a record $11.2 billion marketing their products, up by $5 billion since the MSA was signed, and outspending Legacy's national public-education campaign 200-to-one.

So far, Legacy, along with others, has been able to hold its ground in the David-versus-Goliath struggle, and youth smoking is now at its lowest level in 28 years. We are proud of the role Legacy has played in this life-saving effort. Programs like our award-winning Truth Youth Counter-Marketing Campaign have been cited as one of the reasons for the sharp and accelerating declines in youth smoking. Circle of Friends, another of our signature programs, provides social support for women smokers, 70 percent of whom want to quit. I am wearing a Circle of Friends pin, which symbolizes my support for the 20-million-plus women who are struggling to quit smoking. The encouraging trends in youth smoking rates and the number of people who have quit smoking could end tomorrow, but they don't have to end.

I'd like to conclude my testimony by issuing four challenges to the Committee and a pledge from Legacy. We must recommit, as a Nation, to youth smoking prevention. The American Legacy Foundation pledges to partner with the states to fund programs like Truth. Already, Legacy has spent over $3 million in coops with the state and has committed six million next year of our own foundation funds for cooperative agreements with 15 states, including some of those Committee Members represent.

We must turn our attention to the 47 million Americans who are smokers, most of whom want to quit, and the 177 million remaining Americans who should help them. Over the course of the coming year, the American Legacy Foundation is committed to leading a consortium of partners to raise $100 million, about $2 per smoker, to assist the states and the Nation in motivating and helping smokers to quit.

We must encourage new and expanded public-private partnerships to help increase the lifesaving benefits of prevention programs and smoke-free workplaces throughout the country. Legacy proudly salutes those private sector partners that have already joined with us, including Avon, QVC, Novartis, the BlueCross/BlueShield Association, and the Entertainment Industry Foundation.

Finally, Legacy urges this Committee and the U.S. Congress to continue your oversight responsibilities, tracking the progress of the MSA, and encouraging the Federal Government to find appropriate avenues to become a more direct partner in tobacco prevention and cessation programs at the national level.

Legacy's role as a crucial funding and strategic counterweight against the tobacco industry will continue. We pledge that our efforts to partner with those states and organizations that are genuinely committed to the moral contract they made in the MSA will be redoubled in the months and years ahead.

Mr. Chairman, I commend you for holding today's important oversight hearing, and thank you for including the American Legacy Foundation on the panel. I would be pleased to respond to questions.

[The prepared statement of Dr. Healton follows:]

PREPARED STATEMENT OF DR. CHERYL G. HEALTON. PRESIDENT AND CEO, AMERICAN LEGACY FOUNDATION

Chairman McCain, Senator Hollings, and other distinguished Members of the Committee, I deeply appreciate this opportunity to testify on behalf of the American Legacy Foundation. Our mission is to build a world where young people reject tobacco and anyone can quit.

We are the national foundation borne of the Master Settlement Agreement (MSA) and funded through dollars directed to us by the states. Our Board of Directors includes among its members two representatives each designated by the National Association of Attorneys General, the National Governors Association, and the National Conference of State Legislatures. I am thus especially pleased to serve on a panel with representatives from those organizations. Governor Napolitano of Arizona currently serves as one of the NGA representatives on our Board and she sends her special greetings to you Chairman McCain.

Chairman McCain and Members of the Committee, let me say at the outset that Legacy is prohibited from lobbying pursuant to the terms of the MSA. Today, we are here not to lobby, but rather to assist the Committee in its oversight responsibilities, by sharing our insights and experiences regarding the use of MSA funds. Because of the unique circumstances of our birth, the American Legacy Foundation is a creature of the states. Therefore, we feel well qualified to share our views regarding the significant progress that has been made at the state level as a result of the MSA. And, we are equally qualified to point out where states have fallen short—despite the infusion of funds by the MSA—because of competing fiscal priorities.

The Centers for Disease Control (CDC) issued their Best Practices for Comprehensive Tobacco Control Programs guidelines in August of 1999, with a call to action on the percentage of funds that should be spent by each state for tobacco control programs. These recommendations became an important benchmark for the public health community. In 2003, the states will spend only 8 percent of the total tobacco settlement revenues they are expected to receive this year. *That translates to just $682 million dollars that are committed to tobacco control programs of $8.7 billion total.* Most states have failed to meet the minimum recommendations set forth by the CDC to promote tobacco prevention programs, let alone the ideal funding level which could aggressively address the epidemic of tobacco-related death and disability.

Every day in America, 1,200 lives are lost to tobacco-related disease. On that same day, 4,400 young people under the age of 18 take their first puff of a cigarette, steering many of them down the road to a lifetime of tobacco addiction. Because lives are at stake, advocates from the tobacco control, medical and public health communities in the states are understandably disappointed that so few of the MSA dollars have been devoted to tobacco control programs. And the alarming trend shows no sign of abatement. Compounding the problem, some of the most effective state programs have already been lost or critically wounded, including California, Massachusetts, Oregon and Florida. Many feel strongly that the States have squandered an unprecedented opportunity to save lives and have argued that decisions to direct all—or virtually all—MSA dollars to other programs are especially short sighted in economic terms since smoking cessation dramatically reduces the enormous sums needed to treat sick and dying smokers in the long term and greatly curtails productivity losses. The tobacco epidemic costs the U.S. 158 billion dollars a year.

Perhaps because of our board structure, Legacy is uniquely sensitive to the Solomon-like choices that often must be made by states that are facing unprecedented budget deficits and escalating demands for resources. However, we must nonetheless add our voice to the public health chorus that would remind States of the long term consequences of today's decision to rob Peter to pay Paul—including millions of lives needlessly lost and billions of dollars spent on preventable death and disease.

Because only a small portion of the original sums disbursed to the States via the MSA have been spent by the states to prevent or reduce tobacco use, Legacy has become a *de facto* safety net at the national level to fill many of these gaps. It is a role that will be increasingly difficult for Legacy to fulfill.

Notably, at a time when state programs are disappearing, Legacy is facing its own funding cliff as a result of what was in essence a "sunset provision" in the MSA. That cliff is shown on the chart here.

Specifically, Legacy was only guaranteed major payments from the states via the participating manufacturers for the first five years. Thereafter, payments would be made to Legacy only if the participating manufacturers controlled 99.05 percent market share of tobacco sales nationally. Because of the number of small companies not participating in the MSA, the 99.05 threshold was never met—although there were strong incentives built in to join the agreement. Last April, Legacy received what it believes will be its last major payment pursuant to the MSA.

The sun is setting at a time when the industry is spending more than ever before on its marketing and advertising campaigns. In 2001 alone, the tobacco industry spent a record $11.2 billion dollars marketing their products—up by 5 billion dollars since the MSA was signed. Although Legacy does its share of counter marketing through the **truth**® campaign and other programs, the industry routinely outspends us by 200 to 1.

So far, Legacy—along with others—has been able to hold its ground in this David vs. Goliath battle. But the threat of litigation haunts any successful tobacco-control advertising campaign—as you have witnessed in the State of California—and as the American Legacy Foundation currently finds itself engaged in the State of Delaware. Simply put, our foundation is working to save lives and the tobacco companies are in business to sell cigarettes. Effective efforts to reduce smoking that significantly decrease industry marketshare, have been met with long-term litigation that serves to distract us from our mission, rob us of limited resources and if successful, can ultimately silence our work and close our doors.

Smoking is at its lowest level in 28 years. The American Legacy Foundation is proud of this achievement by the community as a whole, including the states.

We are also proud of the role Legacy has played in securing this success through our programs, such as **truth**® our award-winning youth counter marketing campaign that has been cited as one of the reasons for the sharp declines in youth tobacco use. We are also proud of "Great Start," our innovative cessation program for pregnant women, which was the brainchild of the former First Lady of Utah, Jackie Leavitt. The program worked with 20 First Ladies to spread the word to women about the benefits of quitting before and during pregnancy and staying smoke free.

"Circle of Friends" is another signature foundation campaign designed to provide social support for women smokers, 70 percent of who want to quit but need strong social support to be successful in the long-term. I am wearing a Circle of Friends pin today, which symbolizes my support for the over 20 million women who are struggling to quit smoking.

Mr. Chairman, on the anniversary of the MSA, we are at a crossroads. The encouraging trends in the number of people who have quit smoking and the number of youth who never start could end tomorrow. *But they don't have to end.* The MSA still has decades left to achieve the vision of a smoke free society—and the American Legacy Foundation is committed to staying the course, to help shape a society where all young people reject tobacco and anyone can quit.

The past five years have taught us a great deal about what works in the effort to get the **truth**® about tobacco to the American people—especially our youth. We've also learned that it takes a partnership between states, Federal agencies, and private organizations such as Legacy to address the nationwide tobacco epidemic. We are working aggressively to forge partnerships with our colleagues in tobacco-control and public health as well as states, national organizations and corporate America, who share in our conviction that working together, we can eliminate tobacco addiction and achieve healthier and longer lives for all Americans. But, these partnerships require the states to remain committed to the spirit of the MSA and require all of us to remain actively engaged.

I'd like to end my testimony by issuing four challenges to the Committee and a pledge from Legacy:

(1) We must re-enforce and renew our commitment as a nation, and in the individual states, to youth tobacco prevention. The American Legacy Foundation pledges to partner with the states in funding programs like **truth**®. Already, Legacy has spent over $3 million—with a commitment to spend $6 million—of our own foundation funds on cooperative agreements with 15 states from coast to coast, like Alaska, Arkansas, Indiana, Kentucky, New Mexico, New York and Wisconsin, to leverage state dollars with Legacy funds to provide sustainable state-led efforts.

(2) We must turn our attention to the 47 million Americans who are smokers, most of whom want to quit, and the 177 million remaining Americans who need to help them quit. Over the course of the coming years, the American Legacy Foundation is committed to leading a consortium of partners in raising 100 million dollars—about $2 per smoker—to assist the states and our Nation in motivating and assisting smokers to quit.

(3) We must encourage new and expanded public/private partnerships between business, unions, communities, states and the Federal Government that will help us expand the life-saving benefits of prevention programs and smoke-free workplaces throughout the country. Legacy proudly salutes those private sector partners that have already joined us including Avon, QVC, Novartis, the Blue Cross Blue Shield Association, the Entertainment Industry Foundation and others. We need more businesses, associations and organizations to join us in these efforts.

(4) Finally, Legacy urges this committee and the United States Congress to continue your oversight responsibilities, tracking the progress of the MSA and encouraging the Federal Government to find appropriate avenues to become a more direct partner in tobacco prevention programs at the national level. Here, as well, Legacy pledges our support and full partnership with you.

We are putting our faith in the proven power of partnership to help us achieve the promise of a smoke-free future. Legacy's role as a crucial funding and strategic counter-weight against the tobacco industry will continue, and I pledge to this committee that our efforts to partner with those states and organizations who are genuinely committed to the moral contract they made in the MSA will be redoubled in the months and years ahead.

Mr. Chairman, smoking is the number one killer in America today and all of these deaths are *completely* preventable. The American Legacy Foundation offers our resources, depth of knowledge and fierce determination to help states, and the Nation as a whole, meet these challenges. We commend you for holding today's important oversight hearing and thank you for including The American Legacy Foundation's on the panel.

The CHAIRMAN. Thank you very much.

Mr. Myers?

STATEMENT OF MATTHEW MYERS, PRESIDENT, CAMPAIGN FOR TOBACCO-FREE KIDS

Mr. MYERS. Mr. Chairman and Members of the Committee, first I want to thank you very much for holding this hearing. The spotlight you shine on how the tobacco settlement money is one of the most important public health issues of our time.

Let me briefly summarize our testimony. As you correctly said, when the states sued the tobacco industry and when they settled, they said that they were both suing and settling for very specific purposes. They were trying to stop an epidemic of tobacco use among children, and they were trying to stop the crushing rise in Medicaid costs the states were experiencing due to tobacco-related diseases.

These quotes are typical. Pennsylvania Attorney General Mike Fisher, "Emphysema, heart disease, cancer, more than 20,000 Pennsylvanians die from tobacco-related diseases each year. This money will not bring back those who have died, but it may be used to keep others from starting this deadly habit."

West Virginia Attorney General Darrell McGraw, "The reason we got into this fight was to protect public health and prevent underage smoking. A significant portion of this money should go toward these curses."

When the states came to this Committee and to Congress in 1999 and asked you to waive any potential right the Federal Government had to direct the spending of that money, or to its share of that money so that the Federal Government would have more funds to fight this battle, they also made specific promises. You correctly quoted the National Governors Association's resolution. But in May 1999, the National Governors Association said something else, and I quote, "States are already spending state funds on smoking-cessation programs and will substantially increase funding as the effectiveness of these programs is established."

Mr. Chairman and Members of the Committee, as I will note later on in our report, the effectiveness of these programs has been established, and the states have done just the opposite.

Three years ago, you held a hearing. At that time, you were harshly critical, as were we, of the fact that the states were only spending 9 percent of the tobacco settlement money at that time on tobacco prevention programs. Well, today we and the American Cancer Society, the American Heart Association, and the American Lung Association are issuing a new report entitled, "A Broken Promise To Our Children." What it shows is that the case has become substantially worse. The amount of money the states are now spending on tobacco prevention has dropped by 28 percent in the last 2 years. It is now down to $541.1 million out of a total of that the states have received this year from tobacco excise taxes and tobacco settlement money of over $19 billion.

Mr. Chairman and Members of the Committee, we can't win this war if we don't wage it, and currently we are not waging it.

The situation is even worse in another respect. The cuts in tobacco spending have decimated some of the most effective programs this Nation has ever seen, programs whose effectiveness is beyond debate, programs that have already saved lives, programs in California, Massachusetts, and Florida, which have proven they can dramatically drive down tobacco-use rates. And yet today, Massachusetts and Florida's programs barely exist, and California's program has been cut in half.

This tragedy comes about at a time when the need for strong action is greater, not less than it was 5 years ago. We had hoped that the tobacco industry would take advantage of the Master Settlement Agreement to decrease their targeting of young people and young people's exposure to tobacco marketing. The data shows that they have done just the opposite of that. There's a chart in our report that shows that in the 3 years after the Master Settlement Agreement, tobacco marketing actually increased by 66 percent to a record $11.5 billion. What does that mean today? It means that today the tobacco industry is spending $20 marketing this product for every dollar the states are spending to prevent the sale of its product. What it means is that in 3 weeks, the tobacco industry spends more money marketing its products than all of the states combined spend in an entire year.

What does that mean? The variation from state to state is dramatic. States like Maine and Delaware, that have committed substantial funds to this program, are only being outspent three to one, and it's the reason we're seeing results in those states. But a state like Florida, whose program was a model for the Nation when it was created, whose program resulted in the most dramatic decrease in youth tobacco use in history over a 4-year period, is now being outspent 655 to one by the tobacco industry. We're already seeing smoking rates among the youngest kids in Florida turn around. It isn't an accident that it's happening.

And that's the critical fact, Mr. Chairman. We're not asking the states to spend money on unproven programs. We're asking the states to spend money on programs that are scientifically based, that have been fully evaluated, and that have been found to reduce tobacco use.

Attorney General Moore, at the end, today, will talk about what's going on in Mississippi, but Mississippi is not an isolated case. In Maine, they used the Master Settlement money to fund comprehensive tobacco prevention programs, increased excise taxes, and expanded clean indoor air. Maine went, in 4 years, from a state with the worst youth smoking rates to one of the best, from over 39 percent to 20 percent.

Mr. Chairman, we have—we have an antidote to lung cancer. We know how to prevent lung cancer from ever happening if we would only spend the money that the states promised to spend. We know that budget times are tight. But when you compare the results of our study with the published data from the states, what you find is that in this fiscal year the states are spending more money on tobacco farmers than they're spending on tobacco prevention.

Our organization has worked with tobacco farmers. We want to help them. But it is a tragedy beyond comprehension, it is political malpractice, for a nation to be spending its money this way. They're hard choices. That's why we elect public officials, to make hard choices. These funds came for a specific purpose. We don't need to spend all of them. If the states will spend just 8.2 percent of the tobacco revenue they're receiving on tobacco prevention and cessation programs, they can meet the minimum recommended by the CDC. This is not a partisan issue.

The current director of the CDC issued a report only 2 months ago that carefully evaluated the effectiveness of tobacco prevention programs and isolated the impact of tobacco prevention from smuggling, excise taxes, and other factors. And this is what the current director of the CDC said at that time, "This study provides our clearest evidence to date that tobacco control programs are an excellent investment in public health."

Mr. Chairman, we applaud this Committee for holding this hearing. Literally, the lives of millions of our children are at stake. We hope this hearing is the first step in a real focus in asking the question how we can ensure that the states spend the money that they say they received to deal with the problem of tobacco control to help protect our Nation's children.

Thank you.

[The prepared statement of Mr. Myers follows:]

PREPARED STATEMENT OF MATTHEW MYERS, PRESIDENT, CAMPAIGN FOR TOBACCO-FREE KIDS

Good morning Mr. Chairman, and members of the Committee. My name is Matthew Myers. I am the President of the Campaign for Tobacco-Free Kids, a national organization created to protect children from tobacco by raising awareness that tobacco use is a pediatric disease, by changing public policies to limit the marketing and sales of tobacco to children, and by actively countering the special interest influence of the tobacco industry.

Mr. Chairman, I want to thank you for your continued leadership on the issue of tobacco control. Many others and I are very grateful for your willingness to stand up for our kids, take on the tobacco companies, and hold the states accountable for living up to their commitment to spend a significant portion of the funds they received from the tobacco industry in settlement of their cases to prevent kids from starting to smoke and help adults to quit.

Summary of Key Points

Let me summarize my key points:

(1) When the states sued the tobacco industry and then again when they settled their cases against the tobacco industry, they said they were doing so because of what they described as a tragic epidemic of tobacco use among children and the crushing and rising burden of tobacco-related disease on state Medicaid expenditures. Their goal and their promise was to insure that the states had adequate funds to address these problems.

(2) When the states came to Congress in 1999 and asked the Federal Government to waive its claim to a portion of these funds, the leaders of the National Governors Association pledged to spend *"a significant portion of the tobacco settlement funds on smoking cessation programs, health care, education and programs benefiting children"* if Congress agreed to waive its right to any of these funds.

(3) Over three years ago you held a hearing on the use of revenues from the tobacco settlement. This hearing took place before the states faced serious budget crises. At that hearing we released a report that showed the states were not then living up to their promise. Today we are releasing an update of that report and the picture has become significantly worse. The report released today by the Campaign for Tobacco-Free Kids, the American Cancer Society, the American Heart Association and the American Lung Association demonstrates that far fewer states are spending a significant amount of their tobacco settlement money on tobacco prevention and cessation. As of October 2003, 24 states have cut their funding for tobacco prevention and cessation, including several of the programs that have proven most successful at reducing youth tobacco use, such as the programs in California, Massachusetts and Florida. It appears, sadly, that there is no relationship between success and continued funding.

(4) The failure of the states to do as they promised will have tragic consequences for the health of our Nation's children and the amount taxpayers are forced to pay in the future to cover the costs of tobacco-related Medicaid expenditures. The scientific evidence is now conclusive-comprehensive tobacco prevention programs have been proven to be effective in reducing tobacco use, particularly among our Nation's children.

Every state that has implemented a well-funded tobacco prevention program in accordance with the guidelines issued by the Centers for Disease Control and Prevention (CDC) has experienced a significant reduction in tobacco use. The data from California, Washington, Oregon, Arizona, Minnesota, Alaska, Maine, Mississippi, Florida, New York, Massachusetts and Indiana all tell the same story. These programs work.

As the current Director of the CDC, Dr. Julie Gerberding, said just two months ago in conjunction with the release of the most authoritative study ever done on the impact of tobacco control programs, "This study provides our clearest evidence to date that tobacco control programs are an excellent investment in public health."

Thus, the failure of the states to do what they promised their citizens and Congress is having very real world consequences. We too often think of tobacco in statistical terms. To tobacco victims-parents, children, grandchildren, husbands, wives and siblings tobacco's victims are not statistics. A couple of examples from our website, "Voices Against Tobacco" show that:

> Ever since I was 3 there was a big green oxygen tank sitting in the front room of my house and a small portable one sitting next to it. They were there to help my mother breathe because she was dying from emphysema, a smoking disease. My family was never able to do the things that most families could do, like go on vacations and weekend camping trips because we always had to worry about my mom. When I was 9 she died, at the age of 49, it was hard growing up without a mother. She wasn't there for the mother daughter talks that all my friends were having with theirs. I promised myself that I will never let that happen to me.
>
> Joyce R., West Valley City UT, November 10, 2003
>
> On March 23, 2000, l lost my sister, Mary, to lung cancer. She started smoking at age 13 and stopped when she was 32. She had a lot of stress in her life when she was diagnosed with lung cancer. She was 46 years old. She was 47 years old when she passed away. Watching her wither away and suffer through the inability to breathe was very painful. It's something you never forget. I miss her a lot.
>
> Eileen R., Dimondale MI, November 10, 2003
>
> I lost my father to a tobacco-related heart attack. It was just 10 days after my 13th birthday in 1996. I was home getting ready to go to my Boy Scouts meeting and watching TV and my mom and myself received the phone call that my dad had died that day. He was just 48 yrs old when he died. I lost more than just a father because anyone can be a father but it takes someone special to be a dad and I lost my dad. Everyday I think about my dad and wonder if he would be proud of me. April 30th, 2003 will be 7 years I have had to live without my dad because he smoked cigarettes. Is that fair?
>
> Ray L., Punta Gorda FL, May 29, 2003

The funds from the Master Settlement Agreement gave the states an historic opportunity to improve the lives of their citizens. Former U.S. Surgeon General David Satcher who testified at your hearing three years ago concluded that investing tobacco settlement dollars in these comprehensive prevention programs represented the greatest opportunity in public health since the polio vaccine. Unless the public officials who make the decisions about how these funds or the funds from state tobacco excise taxes are used, literally millions of citizens will die prematurely from wholly preventable tobacco-caused deaths. We can do better and we must hold our public officials accountable.

Background

Mr. Chairman, as you know, between 1994 and 1998 every state sued the tobacco companies. In state after state Attorneys General indicated that the primary purpose for filing the lawsuits was that far too many children were smoking, the tobacco companies were targeting minors with their marketing campaigns and the states could no longer afford the rising costs from tobacco-related Medicaid expenditures. Something had to be done to address these problems, these public officials said, and these lawsuits were the answer.

On November 23, 1998, 46 states settled their lawsuits against the major tobacco companies to recover tobacco-related health care costs, joining four states (Mississippi, Texas, Florida and Minnesota) that had reached earlier, individual settlements. These settlements required the tobacco companies to make annual payments to the states in perpetuity, with total payments over the first 25 years estimated at $246 billion. The multi-state settlement, known as the Master Settlement Agreement (MSA), also imposed limited restrictions on the marketing of tobacco products.

At the press conference announcing the settlement, the tobacco settlement was presented as an historic opportunity to attack the enormous public health problem posed by tobacco use in the United States. As described by state Attorneys General and Governors, the promise of the settlement was two-fold: It would significantly increase the amount of money the states were spending on programs to prevent kids from starting to use tobacco and help those already addicted to quit, and it would greatly reduce youth exposure to tobacco marketing.

Mr. Chairman, while the multi-state settlement did not dictate how states should spend the money, state Attorneys Generals and Governors from across the Nation pledged that they would use the tobacco companies' own money to address the tobacco problem.

Why did we think these cases were about reducing the death toll from tobacco? Listen to what our public officials said:

> *New Jersey Governor Christine Whitman: "Every penny of these funds should be used for health purposes including prevention programs and counter advertising to protect kids, cessation programs and community partnerships to serve those who have already put their health at risk by smoking, in addition to existing important health programs such as charity care and Kidcare"*
>
> *Indiana Governor Frank 0'Bannon: "This money can go a long way toward preventing Hoosier Kids from ever getting hooked on tobacco and toward helping our citizens stop smoking and recover from smoking-related illness."*
>
> *Utah Attorney General Jan Graham: "Utah has a moral duty to invest a good part of this money in keeping our kids away from cigarettes. One-third of kids who start smoking will die of smoking caused disease"*
>
> *Pennsylvania Attorney General Mike Fisher: Emphysema, heart disease, cancer more than 20,000 Pennsylvanians die from tobacco-related diseases each year." "I sued the tobacco industry because it conspired to increase the addictive properties of tobacco products and suppressed vital information about the deadly nature of tobacco. This money will not bring back those who have died, but it may be used to keep others from starting this deadly habit."*
>
> *West Virginia Attorney General Darrell V. McGraw: "The reason we got into this fight was to protect public health and prevent underage smoking. A significant portion of this money should go toward these causes."*
>
> *North Carolina Governor Jim Hunt: the consent decree gives North Carolina "a balanced approach" to allocate tobacco settlement money. "It will address our efforts to crack down on underage smoking and to protect the health and well-being of North Carolinians."*

State officials made similar promises to Congress less than a year later. Shortly after the settlement, the Health Care Financing Administration (HCFA) notified the states that Medicaid related recoveries would be subject to recoupment under Medicaid third party recovery provisions.

The Clinton Administration indicated a willingness to let the states keep all of the funds but wanted to require the states to spend a portion of the funds on reducing teenage smoking among others things. Instead, the states pressed Congress to change the existing Medicaid law to allow them to keep the Federal Government's share of the settlement without any strings attached. The states promised Congress that they would do the right thing with the funds and that they were committed to reducing tobacco use.

In order to persuade Congress, the states made explicit promises. The National Governors' Association, the National Conference of State Legislators and others stated

> **"[We] are committed to spending a significant portion of the tobacco settlement funds on smoking cessation programs, health care, education, and programs benefiting children."**

In May 1999, the National Governors Association told Congress,

> **"States are already spending state funds on smoking cessation programs and will substantially increase funding as the effectiveness of these programs is established."**

Some made an even more explicit commitment according to Washington State Attorney General Christine Gregoire. According to Attorney General Gregoire,

> **"The representations we (the states) made to them (Congress) were that states would use not less than 50 percent of the money for health and anti-tobacco causes."**

Five years after the November 1998 state tobacco settlement, we find that most states have failed to keep their promise to use a significant portion of the settlement funds to reduce tobacco's terrible toll on America's children, families and communities. We also find that the settlement's marketing restrictions have done little to reduce the tobacco companies' ability to market their products aggressively in ways effective at reaching and influencing our children.

Disturbingly, in the past two years the states have cut funding for their tobacco prevention programs by more than a quarter, and several states have completely eviscerated some of the most successful and promising tobacco prevention and cessation programs in history. Remember the program in Florida that received so much publicity because it reduced tobacco use by 35 percent among high school students and by 50 percent among middle school students in just four years? In 2003 Florida's governor and legislature virtually eliminated it. Massachusetts is another case in point. In the 10 years its program was in existence, cigarette consumption dropped by 36 percent versus just 16 percent in the rest of the country. Nonetheless, in the last two years Massachusetts' governor and legislature also virtually wiped out the program and with this decision, we can expect to see a decade of progress gradually eroded.

As the report we release today details, the states lack credible excuses for their failure to do more to protect our children from tobacco. They are collecting record amounts of tobacco revenue from the tobacco settlement and tobacco taxes. To protect our children states only need to spend a small portion—20 to 25 percent per state and an even smaller percentage of a state's total tobacco revenues from the tobacco settlement and tobacco taxes—of those funds on tobacco prevention and cessation programs to meet the minimum levels recommended by the CDC.

The findings for this year:

- Only four states—Maine, Delaware, Mississippi and Arkansas—currently fund tobacco prevention programs at minimum levels recommended by the CDC. Last year Maryland and Minnesota were in this category, but both cut funding.
- Only eight other states are funding tobacco prevention programs at even half the minimum levels recommended by the CDC. Last year a total of 15 states fell into this category.
- Thirty-three states are spending less than half the CDC's minimum amount. Another five states—Michigan, Missouri, New Hampshire, South Carolina and Tennessee—and the District of Columbia allocate no significant state funds for tobacco prevention.
- In the current budget year, Fiscal Year 2004, the states cumulatively plan to spend $541.1 million on tobacco prevention programs. This amounts to just 33.8 percent of the CDC's minimum recommendations for all the states, which total $1.6 billion.
- Over the past two years, the states have cut total annual funding for tobacco prevention by 28 percent, or $209 million (from a high of$749.7 million in Fiscal Year 2002 to $674.4 million in Fiscal Year 2003 and $541.1 million in Fiscal Year 2004).These cuts have decimated three of the Nation's longest standing and most successful tobacco prevention programs, in Florida, Massachusetts and Oregon, and they have seriously hampered some of the Nation's most promising new programs, including those in Indiana, Maryland, Minnesota, Nebraska and New Jersey.
- While many states have cut funding for tobacco prevention, the tobacco industry increased its marketing expenditures to record levels, up 66 percent in the three years after the settlement to a record $11.45 billion a year, or $31.4 million a day, according to the Federal Trade Commission's most recent annual report on tobacco marketing. While the FTC report was for calendar year 2001, there is strong evidence that tobacco industry marketing expenditures have continued to increase. Based on the latest FTC figures, the tobacco companies are spending more than twenty dollars marketing their deadly products for every dollar the states spend to prevent tobacco use. Put another way, the tobacco compa-

nies spend more in three weeks marketing their products than all 50 states spend over a full year trying to prevent tobacco use.

The settlement included important restrictions on tobacco marketing, but since the settlement, the tobacco companies have simply shifted their resources and increased spending on other forms of marketing that appeal to kids, especially promotions in convenience stores and other retail outlets. These include payments for highv·isibility store placements and displays, price discounts that make cigarettes more affordable to kids, and free gifts with purchase. The settlement's restrictions on tobacco marketing, thus, did not succeed in reducing the tobacco companies' ability to market their products aggressively to either children or adults. The need for the states to act is no less today than it was when the settlement took place five years ago.

- The states this year will collect $19.5 billion in tobacco-generated revenue from tobacco taxes and the tobacco settlements. It would take just 8.2 percent of this total for every state to fund tobacco prevention programs at the minimum levels recommended by the CDC ($1.6 billion for all the states). The states are spending only about one-third of what the CDC recommends for tobacco prevention, amounting to only 2.8 percent of their total tobacco revenue. (Looking only at settlement money, the National Conference of State Legislatures recently reported that in Fiscal Year 2004 states are spending just three percent of their tobacco settlement money on tobacco prevention.)
- At least 20 states and the District of Columbia have also sold to investors, or securitized, their rights to all or part of their future tobacco settlement payments for a much smaller, up-front payment, or have passed laws authorizing such action. Several states used the revenue generated to balance budgets for just one year. Securitization eliminates or reduces the amount of settlement money available to fund tobacco prevention and meet other needs in the future.

Why States Should Increase Funding for Tobacco Prevention Programs

The states' funding of tobacco prevention and cessation is woefully inadequate given the magnitude of the tobacco problem. The amount the states are spending on tobacco prevention today pales in comparison to the enormity of the problem. Tobacco use is the number one cause of preventable death in the United States, claiming more than 400,000 lives every year. The annual cost of treating tobacco-caused disease exceeds $75 billion. Despite recent progress in reducing youth smoking rates, more than a quarter of high school seniors (26.7 percent) still graduate as smokers, and every day another 2,000 kids become regular, daily smokers, one-third of whom will die prematurely as a result. These children are the tobacco companies' valued "replacement smokers."

The evidence is conclusive that state tobacco prevention and cessation programs work to reduce smoking, save lives and save money. Every scientific authority that has studied the issue, including the National Cancer Institute, the Institute of Medicine and the U.S. Surgeon General, has concluded that when properly funded and implemented, these programs reduce smoking among both kids and adults.

For example, the 2000 Surgeon General's report, *Reducing Tobacco Use,* provides an in depth analysis of tobacco intervention strategies. This report offers a science-based blueprint for achieving the goal of reducing tobacco use among both adults and children. A key conclusion of the Report is that the Federal Government's Healthy People 2010 objectives with regard to tobacco can be achieved, but only if comprehensive tobacco prevention and cessation approaches to tobacco control are implemented.

In September 2003 a study conducted jointly by the Research Triangle Institute, the CDC, and the University of Illinois published in the *Journal of Health Economics,* provided the most powerful evidence yet of the effectiveness of comprehensive tobacco prevention programs. The study found that states with well-funded, sustained tobacco prevention programs during the 1990s—Arizona, California, Massachusetts and Oregon—reduced cigarette sales more than twice as much as the country as a whole (43 percent compared to 20 percent). This is the first study to compare cigarette sales data from all the states and to isolate the impact of tobacco prevention program expenditures from other factors by controlling for changes in excise taxes, cross-border sales and other state specific factors. The study shows that the more states spend on tobacco prevention, the greater the reductions in smoking, and the longer states invest in such programs, the larger the impact. The study concludes that cigarette sales nationwide would have declined by twice as much as they did between 1994 and 2000 had all states fully funded tobacco prevention programs.

These studies are buttressed by the real life examples of every state that has committed significant funds to tobacco prevention in accordance with the CDC guidelines. A case in point: In 1997, Maine had one of the highest youth smoking rates in the country at almost 40 percent. That year, Maine increased its cigarette tax and used a portion of the funds to establish a comprehensive tobacco prevention program known as the Partnership for a Healthy Maine. Maine subsequently expanded its program with settlement money to meet the CDC's minimum funding level and has now achieved dramatic results. Between 1997 and 2003, smoking among Maine's high school students declined by an astounding 48 percent, falling from 39.2 percent to 20.5 percent. Smoking among middle school students declined by 59 percent, from 21 percent to 8.7 percent. This report ranks Maine first in the Nation in its funding of tobacco prevention.

Mississippi, which has also used settlement funds on a comprehensive program and ranks third among the states in funding tobacco prevention, reduced smoking by 48 percent among public middle school students and by 29 percent among public high school students between 1999 and 2002. As Mississippi Attorney General Mike Moore often states, "What state has an excuse to not fund tobacco prevention when we have done it in Mississippi, one of the poorest states."

Maine and Mississippi's experience is similar to what happened in other states. Programs in Washington, Alaska, Oregon, Arizona, Florida, Minnesota, New York, California, Massachusetts and Indiana all have reduced tobacco use. The only place these programs haven't worked is where they haven't been seriously tried.

Florida is a very visible example of the power of these programs to save lives and what happens when a state guts a successful program. Florida's once innovative and successful program served as a model around the country. Despite the program's success, the Florida legislature and Governor cut the funding for the program each year since the program's inception and then virtually eliminated the program in 2003. Florida's kids are already paying a price for the decision to dismantle a program that reduced high school smoking by 35 percent and middle school smoking by 50 percent in four years. In 2002 there was no decline in smoking among middle school students. Even more disturbing, smoking between 6th and ih grades and between 7th and 8th grades rose in 2001 and the increases in smoking between 6th and 7th grades persisted in 2002. There is no excuse and there can be no excuse for Florida's decision to abandon a program whose results were proven and universally applauded.

The evidence also shows that when sustained over time, comprehensive, well-funded tobacco prevention programs also save lives and money. Two recent studies show that California, which started the Nation's first tobacco prevention program in 1990, has saved tens of thousands of lives by reducing smoking-caused birth complications, heart disease, strokes and lung cancer. Other studies have shown that California and Massachusetts, which started their tobacco prevention programs in 1990 and 1993 respectively, have saved as much as $3 in smoking-caused health care costs for every dollar spent on tobacco prevention.

The states have a clear source of revenue to address the problem. Despite their recent budget shortfalls, the states are actually collecting more tobacco-generated revenue than ever before from the tobacco settlement and tobacco taxes. That is because 32 states and DC have increased tobacco taxes since January 1, 2002. Altogether, the states this year will collect $19.5 billion in tobacco-generated revenue. It would take just 8.2 percent of this tobacco revenue, about $1.6 billion, for every state to fund tobacco prevention programs at the minimum levels recommended by the CDC. That leaves plenty of tobacco revenue to balance budgets and meet other needs. But the states are spending barely a third of what the CDC recommends.

Assessing Other Aspects of the Tobacco Settlement

Mr. Chairman, the news is not all bad. Smoking rates, particularly among children, are down. While the tobacco settlement has failed to deliver on its promises to provide significant funding for state tobacco prevention programs or to curtail tobacco marketing, it has contributed to the significant reductions in tobacco use over the last five years. First, the settlement led the major cigarette companies to increase their prices by more than $1.10 per pack between 1998 and 2000. Part of these increases was used to pay the states, but about half of the price increases bolstered the tobacco companies' profits.

Second, the settlement included about $300 million a year in industry payments over five years to create a new national foundation, the American Legacy Foundation, to conduct public education campaigns to reduce tobacco use. Both the settlement-related price increases and the Legacy Foundation's campaigns along with the states that have implemented their own programs have contributed significantly to the reduction in youth smoking rates in the last several years.

While tobacco price increases are effective at reducing smoking, especially among children, they are not a substitute for prevention and cessation programs. The research shows that tobacco price increases are most effective when part of a comprehensive approach that includes prevention and cessation programs and smoke-free workplace policies. In addition, the benefits of price increases are difficult to sustain over time prices erode with inflation and can be undermined by tobacco industry price reductions.

The Legacy Foundation's programs have been highly effective, but it will lose a large portion of its funding after this year because of a loophole in the settlement that lets the major tobacco companies cease payments after 2003. In addition, Legacy's programs were always intended to enhance and not to replace state tobacco prevention efforts.

Today we are at a critical juncture in determining the settlement's long-term impact. Our hope is that this hearing will make a difference. Our nation has made important progress in recent years in reducing youth tobacco use. Continued progress will not occur unless more states use more of the billions of dollars they are receiving from the tobacco settlement, and from tobacco taxes, to fund comprehensive tobacco prevention and cessation programs based on the recommendations of the CDC. If they do, the 1998 state tobacco settlement could yet mark a historic turning point in the battle to reduce tobacco's terrible toll. If they do not, it will be a tragic missed opportunity for the Nation's health.

In conclusion, Mr. Chairman and Members of the Committee, our policy makers in the states are in a rare position on this issue.

We know exactly what the problem is—that tobacco use is the cause of more than 400,000 preventable deaths and millions of illnesses each year.

We have also identified an evidence-based solution to the problem that we know will work when implemented.

We have a clear source of revenue to implement the solution.

And, we have the support of the voters as 86 percent of Americans support spending a significant portion of tobacco settlement funds on tobacco prevention and cessation.

We simply have no excuses for not exercising the political will to spend tobacco money on tobacco prevention. Thank you.

The CHAIRMAN. Thank you.

Ms. Hudson, welcome.

STATEMENT OF HON. DEBORAH HUDSON, CHAIR, REVENUE AND FINANCE COMMITTEE, DELAWARE HOUSE OF REPRESENTATIVES, ON BEHALF OF THE NATIONAL CONFERENCE OF STATE LEGISLATURES

Ms. HUDSON. Thank you very much. Good morning. It's very nice to be here.

Chairman McCain and distinguished Members of the Committee, I'm Deborah Hudson, a member of the Delaware House of Representatives, where I serve as Chair of the Revenue and Finance Committee, and I'm also on the Delaware Health Fund Advisory Committee, which was established in 1999 to make recommendations to the Governor and our General Assembly about how to spend Delaware's allocation of the tobacco settlement funds. But I am here today on behalf of the National Conference of State Legislatures to discuss the states' use of tobacco settlement funds.

On November 23, 1998, the Attorneys General and other Representatives of 46 states, Puerto Rico, U.S. Virgin Islands, American Samoa, the Northern Marianna Islands, Guam, and the District of Columbia signed an agreement with the five largest tobacco manufacturers, ending a 4-year legal battle between the states and the industry, a battle that began in 1994, when Mississippi became the first state to file suit. The settlement funds became available in 2000, and I am honored to be a part of this distinguished panel today to talk about the settlement.

In keeping with the rules, I will be as brief as possible, but I need to make four points. One, the states have dedicated the largest percentage of tobacco funds to healthcare services and programs. Second, a growing number of states are securitizing their tobacco settlement funds, and many more are expressing interest in securitization. Third, the number of nonparticipating tobacco manufacturers is growing. And, fourth, Federal legislation is needed to help some states in key areas.

It is really difficult to discuss all of the programs that the states currently support with tobacco settlement funds. It's even more difficult to compare and contrast among the states. But the Master Settlement Agreement provided no direction to states and imposed no restrictions regarding the allocation of the tobacco settlement funds. So, as such, these funds are treated as state revenue and are subject to regular appropriations. Most states, like Delaware, do receive continuing feedback from citizens regarding the allocation of these tobacco funds. And, as a result, state tobacco settlement fund expenditures, by and large, reflect the priorities established by citizens of each state. Delaware has dedicated the majority of its tobacco settlement funds to healthcare. We are very comfortable with our decision, but would not venture to second-guess the other states that have made different decisions.

I've been asked to talk about other states. NCSL has tracked states' tobacco expenditures since FY–2000 and has divided the expenditures into nine categories: health services, long-term care, tobacco use and prevention, research, education, children and youth services, tobacco farmers, endowment and budget, and the other category of "other."

In nearly 5 years since the beginning of the historic settlement, much has changed, though. State fiscal conditions have eroded, tobacco manufacturers are facing their own challenges.

So how have states spent the funds? Health services, as I said before, represents the largest single category of tobacco settlement fund expenditures. In FY–2000 and 2001, a third of the tobacco settlement funds went toward healthcare services. Today, these expenditures represent 28 percent of the total fund expenditures.

The kind of health services vary by state. For instance, in Arizona, our Chairman's state, the people, in 2000, voted for Proposition 204, which directed the state to use tobacco settlement funds to expand eligibility for the Arizona Healthcare Cost Containment System. That's the state's Medicaid program.

Now, South Carolina was one of the first states to securitize its tobacco settlement fund. The state received $791 million, and distributed the funds as following: 75 percent of the funds to the healthcare endowment, 15 percent to the community trust fund for farmers affected by the drop in tobacco demand and prices, 10 percent for economic development grants to the I–95 corridor of tobacco communities, and 2 percent for water and sewer projects in rural communities.

In my state, we established the Delaware Health Fund and the Health Fund Advisory Committee to make recommendations to the Governor, and this has worked very successfully.

The second largest category of expenditures was, until this year, endowments and budget reserves. The dramatic shift in funds allocated from endowments and budget reserves to the "other" program is very clear, and a dramatic illustration of the serious fiscal challenges facing states today.

While experts may differ on the adequacy and level of each state's expenditures for tobacco use and prevention, in the aggregate they remained constant at about 5 percent until the current Fiscal Year. This year, states increased the percentage of tobacco settlement funds that were allocated to education. Tobacco-producing states also increased the amount of funding allocated to tobacco farmers and as part of their commitment to provide economic and educational alternatives to tobacco farmers and the communities in which they live.

Now, in Delaware, as I said, we have a Health Fund Advisory Committee, which is chaired by our Secretary of Health and Social Services, which advises the Governor and the legislature of how to allocate the funds. I am a member of this committee. The committee has regular open, public meetings, and we maintain a Website where our advisory committee meetings are listed, and the minutes are listed, as well, so people can see our recommendations.

All of Delaware tobacco fund settlement money is dedicated to healthcare programs and services and to tobacco prevention and control. But, like many other states, we have reduced our reserve funds this year, but only to assure full funding for state healthcare priorities. We've slightly increased funding for tobacco prevention and control, as people want us to, and have provided level funding for most other ongoing programs. We are happy that we were able to maintain this.

But now some states choose to securitize their settlement funds. Securitization is the process by which states sell their revenue streams of the tobacco settlement payments for a set number of years in return for a single up-front payment. Although the up-front payment is less than the normal sum of the annual payment, the state receives a lump sum, and the funds are immediately available. It is comparable to receiving a lump-sum payment instead of an annuity.

There has always been a level of uncertainty regarding whether tobacco funds would continue into perpetuity, so initial interest in securitization was popular among states that feared bankruptcy of one or more of the tobacco manufacturers. Now, decreasing state revenues, continuing class-action litigation against manufacturers, makes this a more vulnerable to bankruptcy, and, therefore, decreasing tobacco sales.

To date, sixteen states have securitized all or part of their tobacco settlement funds. We've seen a dramatic decline in the volume of cigarettes shipped by participating manufacturers. It is due, in part, to lower demand for cigarettes, but much of the decline can be attributed to the growing number of nonparticipating manufacturers who have entered the market and who sell their products at a deep discount. These deeply discounted products are more attractive to children, because they are often sold over the Internet and, therefore, are more available. This represents a serious problem for states and for people who support reducing youth access to tobacco. In addition, there is a reduction in the volume of cigarettes shipped by participating manufacturers.

Five years ago, the most immediate task for state legislators related to the Master Settlement Agreement was the model statute. This statute was designed to provide a level playing field between participating and nonparticipating manufacturers by creating a reserve fund into which nonparticipating manufacturers are to pay future claims. Since the signing of the Settlement Agreement, we have found that the model act needs some fine-tuning to close loopholes in the participating manufacturers. NCSL is working with the National Association of Attorneys General to close these loopholes in existing state laws.

The National Council of State Legislators and individual legislators are also working with Congress to enact Federal legislation that would strengthen the Jenkins Act and provide states with additional tools to enforce both the Jenkins Act and existing state laws. This legislation will help states reduce youth access to tobacco products and to collect state tobacco tax revenue that is not currently being collected.

A recent Government Accounting Office report advised that states would lose approximately——

The CHAIRMAN. Ms. Hudson, if you——

Ms. HUDSON. Yes.

The CHAIRMAN.—could——

Ms. HUDSON. Yes.

The CHAIRMAN.—complete your statement. We usually——

Ms. HUDSON. I certainly could.

The CHAIRMAN.—give 5 minutes for——

Ms. HUDSON. I'm talking about the part where we would like to cooperate with you, and we would like to do that the best way we can to make sure that this program is the most effective that it can be.

And we thank you for your time today.

[The prepared statement of Ms. Hudson follows:]

PREPARED STATEMENT OF HON. DEBORAH HUDSON, CHAIR, REVENUE AND FINANCE COMMITTEE, DELAWARE HOUSE OF REPRESENTATIVES, ON BEHALF OF THE NATIONAL CONFERENCE OF STATE LEGISLATURES

Good morning Chairman McCain, Senator Hollings and Members of the Committee:

I am Deborah Hudson, a member of the Delaware House of Representatives where I serve as chair of the Revenue and Finance Committee. I also serve as a member of the Delaware Health Fund Advisory Committee, which was established in 1999 to make recommendations to the governor and to the General Assembly regarding the allocation of Delaware's tobacco settlement funds.

I am here today on behalf of the National Conference of State Legislatures (NCSL) to discuss the states' use of tobacco settlement funds. On November 23, 1998 the Attorneys General and other representatives of 46 states [1], Puerto Rico, the U.S. Virgin Islands, American Samoa, the Northern Mariana Islands, Guam and the District of Columbia signed an agreement with the five largest tobacco manufacturers, ending a four-year legal battle between the states and the industry. A battle that began in 1994, when Mississippi became the first state to file suit. The settlement funds became available to states in 2000. I am honored to be a part of such a distinguished panel on a day so close to the fifth anniversary of the historic tobacco settlement agreement.

[1] Florida, Minnesota, Mississippi and Texas had previously settled with tobacco manufacturers for $40 billion.

In keeping with the rules of the Committee, my oral statement will be limited to five minutes. I am submitting my written statement to be included in the hearing record. Today I will focus on the following observations:

(1) States have dedicated the largest percentage of tobacco funds to health care services and programs.
(2) A growing number of states are securitizing their tobacco settlement funds and many more are expressing interest in securitization.
(3) The number of non-participating tobacco manufacturers is growing.
(4) Federal legislation is needed to help states in some key areas.

It is difficult to discuss the myriad programs that states currently support with tobacco settlement funds. It is even more difficult to contrast and compare among the states. The Master Settlement Agreement (MSA) provided no direction to states and imposed no restrictions on states regarding the allocation of their tobacco settlement funds. As such, these funds are treated as state revenue and are subject to the regular appropriation process. Most states, like Delaware, receive continuing feedback from citizens regarding the allocation of tobacco settlement funds. As a result, state tobacco settlement fund expenditures by and large reflect the priorities established by the citizens of each state. Delaware has dedicated the majority of its tobacco settlement funds to health care. We are comfortable with our decision, but would not venture to second-guess states that have made other choices.

State Tobacco Settlement Expenditures

I have been asked to provide an overview of how states have spent and are spending their tobacco settlement funds. NCSL has tracked state tobacco settlement expenditures since FY 2000 and has divided expenditures into nine categories: health services, long term care, tobacco use prevention, research, education, children and youth services, tobacco farmers, endowments and budget, and other. In the nearly five years since the signing of the historic tobacco settlement agreement, much has changed.

State fiscal conditions have eroded and tobacco manufacturers are facing their own financial challenges. How have states spent the funds? What are the trends? Below is a summary of what we have observed.

Table 1.—Allocation of Tobacco Settlement Funds by Category, FY 2000–FY 2004

[Dollar figures represent total allocation for the fiscal year]

	FY 2000/FY 2001 ($10.97 billion)	FY 2002 ($10.97 billion)	FY 2003 ($9.83 billion)	FY 2004 ($7.9 billion)
Health Services	33%	29%	29%	28%
Long Term Care	3%	7%	8%	6%
Tobacco Prevention	5%	5%	5%	3%
Education	4%	8%	3%	5%
Research	3%	6%	3%	3%
Children & Youth Services	4%	2%	3%	3%
Tobacco Farmers	3%	3%	2%	4%
Endowments and Budget Reserves	29%	24%	18%	2%
Other	16%	16.2%	29%	47%

Source: National Conference of State Legislatures, Health Policy Tracking Service, 2003

Trends in State Expenditures

Health Services represents the largest single category of tobacco settlement fund expenditures. In FY 2000/FY 2001 a third of the tobacco settlement funds went toward health care services. Today these expenditures represent 28 percent of total expenditures. The kinds of health services vary considerably by state. For instance in Arizona, the chairman's state, the people in 2000 voted for Proposition 204 which directed the state to use the tobacco settlement funds to expand eligibility for the Arizona Health Care Cost Containment System (AHCCCS), the state's Medicaid program. South Carolina was one of the first states to securitize its tobacco settlement funds. The state received $791 million and distributed the funds as follows: (a) 75 percent of the funds to the Health Care Endowment[2]; (b) 15 percent to the Community Trust Fund for farmers affected by the drop in tobacco demand and prices; (c) 10 percent for economic development grants to the I–95 corridor of tobacco communities; and (d) 2 percent for water and sewer projects in rural communities. We established the Delaware Health Fund and the Delaware Health Fund Advisory Committee to make recommendations to the Governor and General Assembly regarding the allocation of Delaware's tobacco settlement funds.

The second largest category of expenditures was, until this year, endowments and budget reserves. The dramatic shift in funds allocated to endowments and budget reserves between FY 2003 and FY 2004 to the "Other" program category is a very clear and dramatic illustration of the serious fiscal challenges facing the states. While experts may differ on the adequacy of each state's expenditures for tobacco use prevention, the level of expenditures for tobacco use prevention in the aggregate remained constant at about 5 percent until the current Fiscal Year. This year states increased the percentage of tobacco settlement funds that were allocated to education. Tobacco-producing states also increased the amount of funding allocated to tobacco farmers as part of their commitment to provide economic and education alternatives to tobacco farmers and the communities, in which they live and work.

Delaware Health Fund

The Delaware Health Fund Advisory Committee, a twelve member board, chaired by the Secretary of the Delaware Health and Social Services Department, advises the governor and the legislature on how to allocate the state's tobacco settlement funds. I am a member of the advisory committee. The committee has regular, open meetings and maintains a website where advisory committee meeting minutes and the advisory committee recommendations can be read and downloaded. All of Delaware's tobacco settlement funding is dedicated to health care programs and services and to tobacco prevention and control. Like many other states we have reduced our reserve fund this Fiscal Year to provide funding for state health care priorities. We have slightly increased funding for tobacco prevention and control and have provided level funding for most ongoing programs. We are happy that we are able to maintain this commitment despite the fiscal challenges we face. (See Table 2 for details).

Securitization of State Tobacco Funds

Securitization is the process by which states sell the revenue stream of its tobacco settlement payments, for a set number of years, in return for a single, up-front payment. Although the up-front payment is less than the sum of the annual payments, the state receives a lump sum payment and the funds are immediately available. It is comparable to receiving a lump sum payment instead of an annuity. There has always been a level on uncertainty regarding whether the tobacco funds would in fact continue into perpetuity. Initial interest in securitization was among states that feared that the bankruptcy of one or more of the tobacco manufacturers would undermine the settlement agreement. Decreasing state revenues, continuing class action litigation against tobacco manufacturers that may in fact make tobacco manufacturers vulnerable to bankruptcy, and decreasing tobacco sales, have increased the interest among states in the securitization of tobacco settlement funds. To date, 16 states[3] have securitized all or part of their tobacco settlement funds. (See Table 3 for details)

Growing Number of Non-participating Tobacco Manufacturers

The dramatic decline in the volume of cigarettes shipped by participating manufacturers is due in part lower demand for cigarettes, but much of the decline can be attributed to the growing number of non-participating manufacturers who have entered the market and who sell their products at a deep discount. These deeply discounted products are more attractive to children and because they are often sold over the Internet, are more available to children. This represents a serious problem for states and for people who support reducing youth access to tobacco. In addition, the reduction in the volume of cigarettes shipped by participating manufacturers can result in an overall decrease in state tobacco settlement fund allocations.[4]

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[2] The initial awards from the endowment supported the state's pharmaceutical assistance program.

[3] Alabama, Alaska, Arkansas, California, Connecticut, Iowa, Louisiana, New Jersey, New York, North Dakota, Oregon, Rhode Island, South Carolina, South Dakota, Washington, Wisconsin

[4] Under the provisions of the MSA, if the total aggregate market share of the participating manufacturers decreases more than 2 percent and an economic consulting firm determines that

Continued

Five years ago, the most immediate task for state legislatures related to the Master Settlement Agreement was the consideration and enactment of the "Model Statute" included in the settlement agreement. This model statute was designed to provide a level playing field between participating and non-participating tobacco manufacturers by creating a reserve fund into which non-participating manufacturers are to pay future claims. Since the signing of the settlement agreement, we have found that the Model Act needs some fine-tuning to close some loopholes the non-participating manufacturers have discovered. NCSL is working with the National Association of Attorneys General (NAAG) to close these loopholes in the existing state laws.

We are also working with Congress to enact Federal legislation that strengthens the Jenkins Act and provides states with additional tools to enforce both the Jenkins Act and existing state laws. This legislation will help states reduce youth access to tobacco products and to collect state tobacco tax revenue that is not currently being collected. A recent Government Accounting Office (GAO) report advised that states would lose approximately $1.5 billion in tax revenues by the year 2005 if the current state of Internet tobacco sales continues. As you know, the Senate Judiciary Committee recently reported S. 1177, the Prevent All Cigarette Trafficking Act (PACT Act), a bill that amends both the Jenkins Act [5] and the Contraband Cigarette Trafficking Act.[6] A related piece of legislation, H.R. 2824, amends the Jenkins Act and is pending in the House Judiciary Committee. NCSL looks forward to working with you to work towards passage of this important legislation.

I thank you for this opportunity to share NCSL's thoughts and observations with you. I would be happy to answer questions.

Table 2.—Delaware Health Fund Appropriations State FY 2002–FY 2004

[in thousands]

Initiative	FY 2002	FY 2003	FY 2004
Continuing Initiatives			
Strategic Reserve	6,025	9,843	5,291
DE Prescription Drug Assistance	5,150	7,213	7,500
Tobacco Prevention/Control	5,005	5,009	5,072
Medical Coverage for SSI Transition	1,485	1,485	4,485
DHCC Uninsured Action Plan	1,000	885	500
Chronic Disease Pilot	500	500	500
Medicaid Increase for Pregnant Women	409	408	408
Public Access Defibrillation	375	141	134
Substance Abuse Transitional Housing	200	200	200
Lesser-Known Illnesses	150	100	100
DHCC Staff Assistance	57	57	57
Heroin Residential Program	500	500	500
Attendant Care	340	430	430
Breast & Cervical Cancer Treatment	150	150	150
Cancer Care Connection		150	150
The Wellness Community		200	200
DE Breast Cancer Coalition	40	40	40

the provisions of the MSA were a significant factor contributing to the market share loss, the payments to states may be reduced based on that loss. This reduction in state payments is called the non-participating manufacturers (NPM) adjustment. This analysis is done annually. A state's enactment of the model statute is significant because if there is an NPM adjustment in any year, a specific state's share of the funds from the payment in question will not be reduced at all if that state has passed and has in force the model statute.

[5] The Jenkins Act (18 U.S.C. 375) requires any person who sells and ships cigarettes across state lines to anyone other than a licensed distributor, to report the sale to the buyer's state tobacco tax administrator, allowing state and local governments to collect the taxes due. The current penalty for violating the Act is a misdemeanor.

[6] The Contraband Cigarette Trafficking Act (CCTA) (18 U.S.C. 2342) makes it unlawful for any person to ship, transport, receive, possess, sell, distribute, or purchase contraband cigarettes.

Table 2.—Delaware Health Fund Appropriations State FY 2002–FY 2004—Continued

[in thousands]

Initiative	FY 2002	FY 2003	FY 2004
Delaware School survey (Statewide)			48
New Nurse Formation Programs		750	1,297
Disease Cost Containment Initiatives		500	500
Perinatal Association		200	200
Southbridge Community Health Outreach		120	
University of Delaware/Drug & Alcohol Studies		48	
Instruments for TB & Metabolic Disorders	150	150	
Fire Suppression Program	500	750	
Support for People with Cancer	200		
Gift of Life	105		
Resource Mothers	200		
Council on Cancer Inc. & Mortality			4,938
DE Ecumenical Council			100
Total Initiatives	*$20,325*	*$19,986*	*$24,509*
Total Program and Reserves	*$26,391*	*$29,829*	*$29,800*

Source: Delaware Health and Social Services Department, Delaware Health Fund Advisory Committee (*http://www.state.de.us/dhss/healthfund.html*)

Table 3.—Securitized State Tobacco Settlement Funds

State	Year	Amount	Purpose
Alabama	2000	$50 million	Industrial bonds to attract new jobs
Alaska	2000, 2001	$242 million	Remodel and build new schools, rehabilitate buildings at the University of Alaska and update several port facilities
Arkansas	2001	$60 million	Biomedical research facilities
California	2002, 2003	$4.2 billion	Deficit
Connecticut	2003	$300 million	General revenue
Iowa	2001	$644 million	Retire capital debt to free up general fund revenue for health care services
Louisiana	2001	$1.2 billion	Millennium Fund (endowment) to be used for health care, education and scholarships
New Jersey	2002	$1.8 billion	Deficit
New York	2003	$4.2 billion	Deficit
North Dakota	2000	$32 million	Debt service on water resource and flood control projects
Oregon	2002	$200 million	Deficit
Rhode Island	2002	$685 million	Retire capital debt, deficit
South Carolina	2000	$934 million	73% to the Health Care Endowment [7], balance for rural infrastructure and tobacco farmers
South Dakota	2002	$278 million	Education endowment
Washington	2002	$518 million	Deficit
Wisconsin	2001	$1.6 billion	Deficit

[7] The initial awards from the fund supported the state's pharmaceutical assistance program.

The CHAIRMAN. Thank you very much. Thank you for coming to help us in this very difficult issue.

Mr. Scheppach, welcome.

STATEMENT OF RAYMOND C. SCHEPPACH, EXECUTIVE DIRECTOR, NATIONAL GOVERNORS ASSOCIATION

Mr. SCHEPPACH. Thank you, Mr. Chairman and Members of the Committee. I thank you for the opportunity to represent the Nation's Governors before this Committee today.

The MSA was reached on behalf of the attorney generals of 46 states, five commonwealths and territories, and the District of Columbia in 1998. That agreement, worth $206 billion over 25 years, is actually worth $246 billion, when combined with the other four states.

The MSA did not require set-asides. There was a fundamental difference between the settlement reached and the proposals being promoted in the late 1990s involving Federal legislation. In fact, on May 21, 1999, President Clinton signed into law the measure PL 106–31, recognizing that decisions about how to spend the tobacco settlement dollars were more appropriately made at the state level, where Governors and legislators could be the most responsive to the unique needs and circumstances of their citizens.

Over the 2000 to 2003 period, I think states have received about $37 billion from the Master Agreement. Over this period, there has been substantial stability in the allocation of these revenues. About 36 percent went to healthcare services and long-term care, another 4 percent to tobacco use prevention, 12 percent went to research, education, and services for children. Also, states allocated 3 percent to tobacco farmers for crop diversification and efforts to reduce the state's dependence on tobacco production. The remainder went to endowments, budget reserves, and other programs.

One area that did witness a major change over the last 3 years was in the percent allocated to endowments and budget reserves, which went from 29 percent in 2000 to 18 percent in 2003, and to 2 percent in 2004.

Throughout the last 2 years, due partly to the budget crisis, as well as concerns regarding bankruptcy of tobacco firms, 16 states have securitized their tobacco settlement revenues, for total proceeds of about $13 billion.

The tobacco settlement funds are allowing states to develop a significant number of innovative programs in biotechnology and economic development, smoking cessation, early childhood and prevention healthcare. This period of innovation and experimentation, which helped states develop best practices, will pay great dividends over time.

The most important issue facing states today is the dismal fiscal situation. States are enduring the worst fiscal crisis since the second world war. And although the national economy is beginning to recover, state revenue growth has not yet responded.

The fiscal situation is driven by two major factors—an obsolete tax base and lower revenues, and exploding Medicaid and other healthcare costs. Unfortunately, in 2001 states witnessed both a reduction in total state revenues of 5 percent, at the same time Medicaid exploded to grow 13 percent per year. Medicaid has now become the Pac-Man of state budgets, gobbling up every additional dollar of revenues. Medicaid growth rate has average 10 percent per year during the past two decades and now represents 21 percent of the average state budget, up from 12.5 in 1990. Other healthcare costs represent another 10 percent of state budgets. The major reason for the Medicaid continued growth is that it serves to supplement the Medicare program for many services Medicare beneficiaries do not obtain other places.

It is shocking to note that the Medicaid's 50 million beneficiaries, the six million who are dual-eligible for Medicare and Medicaid, account for 42 percent of the Medicaid budgets. Prior to year 2001, state spending over those previous two decades was growing about 6.5 percent per year. For the last 3 years, spending essentially has been flat or negative, essentially no growth.

This fiscal crisis has had several major impacts—number one, on the allocation of funds from the Master Settlement Agreement, two, the cost of tobacco products, and, three, total spending on healthcare.

First, settlement dollars that originally were to be placed in rainy day funds or specific endowment funds were utilized to balance state budgets. Second, a larger number of states were forced to securitize part of their funds. Third, funds for tobacco prevention from the MSA were reduced. And, fourth, a large number of states enacted significant increases in excise taxes on cigarettes, which should have a huge impact on smoking, over time. Since January 2002, 28 states plus the District have increased cigarette taxes, some as high as over a dollar a pack. The median has increased to 58 cents from 28 cents, over a hundred-percent increase. We have not seen yet the impacts of these tax increases.

Finally, Medicaid spending growth at 10 percent per year, all states have enacted changes to moderate the growth of Medicaid.

I would say, Mr. Chairman, this is about hard choices. And, unfortunately, Governors and state legislatures have had to look at the potential of pushing as many as a million to two million women and children off the rolls of Medicaid, and compare that to smoking cessation programs. That's what's going on, in terms of hard choices, when you have virtually no revenue growth.

In conclusion, given the long history of state expenditures for smoking-related illnesses and the fiscal pressures facing states, the financial flexibility provided to states in the MSA is not only appropriate, but vitally necessary. The state fiscal crisis will continue, and, without flexible use of MSA funds to target emerging priorities, states will be forced to cut education spending and make painful cuts in Medicaid expenditures for prescription drugs and other programs.

Thank you, Mr. Chairman. I'd be happy to answer any questions.

[The prepared statement of Mr. Scheppach follows:]

PREPARED STATEMENT OF RAYMOND C. SCHEPPACH, EXECUTIVE DIRECTOR, NATIONAL GOVERNORS ASSOCIATION

Chairman McCain, Senator Hollings, and members of the Committee, my name is Ray Scheppach and I'm the Executive Director of the National Governors Association. Thank you for the opportunity to represent the Nation's Governors before this committee today.

The tobacco Master Settlement Agreement (MSA) was reached on behalf of the Attorneys General of forty-six states, five commonwealths and territories, and the District of Columbia on November 23, 1998. That agreement, worth $206 billion over a 25-year period, is actually worth $246 billion when combined with previous settlements on behalf of Florida, Minnesota, Mississippi, and Texas.

The MSA Contains Many Important Provisions to Discourage Smoking

Two major programs in the settlement are dedicated to reducing teen smoking and educating the public about tobacco-related diseases. A total of $250 million was used to fund the creation of the American Legacy Foundation, a national charitable organization, to support the study of programs to reduce teen smoking and substance abuse as well as prevent diseases associated with tobacco use. An additional $1.45 billion was utilized to create a National Public Education Fund to counter youth tobacco use and educate consumers about tobacco-related diseases.

In addition, the price of tobacco has increased. Immediately after the MSA, the price of tobacco products jumped by 40 to 50 cents per pack. Additional price increases have occurred as companies attempt to maintain profit margins and make settlement payments. These price increases will substantially reduce smoking over time.

The settlement agreement also has a significant number of restrictions on advertising and promotion. The settlement prohibits targeting youth in tobacco advertising, including a ban on the use of cartoon or other advertising images that may appeal to children. The settlement also prohibits all outdoor tobacco advertising, tobacco product placement in entertainment or sporting events, and the distribution and sale of apparel and merchandise with tobacco company logos. Further, the settlement places restrictions on industry lobbying against local, state, and Federal laws. These restrictions on tobacco companies' ability to market their products to children and young adults will eventually have a major impact on smoking.

The MSA Did Not Require Set-Asides

There is a fundamental difference between the settlement we reached and the proposals being promoted in the late 1990s involving Federal legislation. For that reason, Congress acted wisely in 1999 in declaring that decisions about the MSA funds should be made at the state and local level.

In the original lawsuits, states filed complaints that included a variety of claims, such as consumer protection, racketeering, antitrust, disgorgement of profits, and civil penalties for violations of state laws. Medicaid was not mentioned at all in a number of cases and was only one of a number of issues in many others. Further, the state-by-state allotments were determined, not based on Medicaid expenditures, but on an overall picture of health care costs in a given state.

It is important to note that, ultimately, the master settlement agreement bore no direct relationship to any particular state lawsuit. The master settlement agreement represents a global settlement approach that encompassed states who sued for Medicaid, states that had Medicaid claims thrown out of court, and other states that simply did not sue at all. The attorneys general were attempting to obtain a fair monetary recovery for all states considering the variety of claims and requests for relief and the common goals of the multistate settlement process.

The Federal Government was invited to participate in the state lawsuits, but declined. Therefore, states were forced to bear all of the risk initiating the suits and the entire fiscal burden of carrying forth the unprecedented lawsuits against a well financed industry that had never lost such a case before. It was not until after state victory was ensured that the Federal Government began to pay renewed attention to state activities.

Simply put, the master settlement agreement negotiated between the Attorneys General and the tobacco companies is separate and distinct from the agreement that was proposed in the 105th Congress. That proposal would have represented almost 50 percent more money, $368 billion compared to the current settlement of $246 billion. That agreement was much more comprehensive, representing both state and Federal costs and requiring congressional approval. In the context of the negotiations over the $368 billion amount, the Federal Government may have had a legitimate claim to a share of the settlement, but the proposal's inability to garner enough votes for passage in Congress fundamentally changed the debate. Without passage of supporting legislation, states were forced to proceed with their own lawsuits and negotiate settlements based on nonfederal claims.

Congress Acted Definitively to Give States Spending Authority

On May 21, 1999, President Clinton signed into law a measure (P.L. 106–31) recognizing that decisions about how to spend the tobacco settlement dollars were most appropriately made at the state level, where Governors and legislators could be the most responsive to the unique needs and circumstances of their citizens. Championed by a large bipartisan group of Senators led by Sen. Kay Bailey Hutchison (R-Tex.) and Sen. Bob Graham (D-Fla.), the provision was successfully added to the FY 1999 Emergency Supplemental Appropriations bill.

State Spending

Over the 2000 to 2003 period, states have received $37.5 billion from the Master Settlement Agreement. Over this period there has been substantial stability in the allocation of revenues. About 36 percent went to health services and long-term care. About four percent went to tobacco use prevention. Another 12 percent went to research, education, and services for children. Also, states allocated three percent to tobacco farmers for crop diversification efforts to reduce their states' dependence on tobacco production. The remainder went to endowments, budget reserves, and other programs.

The one area that witnessed a major change over the three year period was the percent allocated to endowments and budget reserves, which went from 29 percent in 2000 to 18 percent in 2003 and then two percent in 2004. This was caused by the worst state fiscal crisis since World War II. Regardless of this crisis, 37 states continued to spend funds on health services and about 33 maintained their commitment to tobacco use prevention.

Throughout the last two years, due partly to the budget crisis as well as concerns regarding the bankruptcy of tobacco firms, 16 states have securitized their tobacco settlement revenues. The proceeds from this securitization were about $13 billion.

Innovative Programs

The tobacco settlement funds allowed states to develop a significant number of innovative programs in biotechnology and economic development, smoking cessation, early childhood, and preventive health care. This period of innovation and experimentation, which helped states develop "best practices", will pay dividends for a long time. States are proud of the smoking cessation initiatives and other programs they've developed with the tobacco settlement funds.

There are several innovative programs designed to prevent maternal smoking that are showing great promise. Smoking during pregnancy is currently responsible for 20 percent of all low-birth weight babies, 8 percent of preterm births, and 5 percent of all perinatal deaths. Several states have invested a portion of its tobacco settlement to target smoking cessation among pregnant women. These include both classes and one-on-one counseling on the dangers of smoking; effective protocols for breaking the smoking habit; statewide quit lines, and media campaigns aimed at women of childbearing age. Besides traditional cessation education and counseling, these services address a range of barriers to cessation, including weight gain, by providing support such as free enrollment in sports clubs.

Other states have used portions of the settlement to develop unique approaches to enhance education opportunities for low-income and disadvantaged students; strengthening foster care and child welfare initiatives; and expanding options for early childhood development and Healthy Start programs.

Many states have used tobacco settlement funds to make critical investments in pharmaceutical assistance programs for seniors and home and community-based care programs for people with disabilities. As many as 16 states have invested funds in biomedical research or research on cancer and other tobacco-related illnesses. The dividends that these investments pay will benefit all the other states as well.

Finally, the largest investment has been in traditional health care. States have invested billions in funds for indigent care programs, primary care, increasing insurance coverage for the working poor, for hospital charity care, community health centers as well as Medicaid and the State Children's Health Insurance Program (S–CHIP).

Fiscal Condition of the States

The most important issue facing the states today is the dismal fiscal situation. States are enduring the worst fiscal stress since World War II, and although the national economy is beginning to recover, state revenue growth has not responded, and historically has lagged Federal recoveries by upwards of 18 months. In fact, the current state crises are likely to endure well into Fiscal Year 2005. These fiscal conditions are driven by two major factors, sagging revenues and exploding Medicaid costs.

States have responded sensibly to these difficult conditions. Although the need for services has increased rapidly, state spending has only increased by 1.6 percent over the last two years, and our estimates for 2004 are that state spending will actually decrease by 2–3 percent State spending will have been essentially flat for three years.

On the spending side, the program that has been responsible for the deteriorating fiscal condition is Medicaid, the state-federal health care entitlement for the poor, the elderly, and the disabled. Now larger than Medicare in terms of total population, total expenditures, and annual growth rate, Medicaid has become the "Pac-Man" of state budgets, gobbling up every additional dollar of revenue. Medicaid's growth rate has averaged 10 percent per year during the past two decades and now represents 21 percent of the average state budget, up from 12.5 percent in 1990.

The major reason for Medicaid's continued growth is that it quietly serves to supplement the Medicare program for the many services Medicare beneficiaries can not obtain anywhere else. Medicaid pays for the prescription drugs and long-term care that Medicare does not cover, and subsidizes the significant cost-sharing burdens that Medicare places on its poorest beneficiaries.

It is shocking to note that of Medicaid's 50 million beneficiaries, the six million people eligible for both programs (the "dual eligibles") account for 42 percent of Medicaid's budget. Therefore, 42 percent of a $280 billion budget is being spent on people who are already receiving the FULL Medicare benefits package. State budgets simply cannot sustain this growing cost shift.

The 2001–2004 state fiscal crisis has had major impacts on:

- The allocation of funds from the Master Settlement Agreement;
- The cost of tobacco products in the states; and
- Total spending on health care.

First, settlement dollars that originally were to be placed in rainy day funds or specific endowment funds were utilized to balance state budgets. Second, a larger number of states were forced to securitize part or all of their funds. Third, funds for tobacco prevention from the MSA were reduced. Fourth, a large number of states enacted significant increases in excise taxes on cigarettes which should have a huge impact on smoking cessation over the next 20 years. The proceeds from some of these taxes went into other endowment funds that are being used for smoking cessation. Finally, with Medicaid spending growing at 10 percent per year all states enacted changes to moderate the growth in Medicaid.

Tobacco Prevention and Control is Important to the States

The Federal and state governments have always had the responsibility of ensuring and protecting the public health of its citizens. Smoking, as the leading cause of preventable death and disease, results in $150 billion in direct and indirect medical costs per year.

In 2001, 22.8 percent of the population were reported to be smokers, a reduction from 25 percent reported in 1993. Progress continues to be made in meeting national goals related to reduction in the percentage of the population who smoke. States are leaders in these efforts—through direct program efforts and changes to public policy.

- Twenty states increased funding in Fiscal Year 2003 for tobacco prevention.
- Forty three states have laws restricting smoking in public places, 45 restrict smoking in government buildings, and 25 have laws restricting smoking in private work places.
- Five states have comprehensive laws with statewide restrictions on indoor smoking in restaurants, bars, and other public places.
- Between 1990 and 2000, cigarette sales fell 20 percent.

Since January 2002, 28 states and the District of Columbia have implemented or enacted new cigarette tax increases. These increases are as high as $1.01 per pack in Connecticut and are more than 50 cents per pack in a dozen states. This raises the median tax rate to 58 cents per pack, an increase from 28 cents in July 2002.

Conclusion

The nation's Governors feel strongly that the states are entitled to all of the funds awarded to them in the tobacco settlement agreement without Federal restrictions. The master settlement agreement is fundamentally different from the earlier proposals considered by Congress. It is a global settlement of myriad claims.

Given the long history of state expenditures for smoking related illnesses and the fiscal pressures facing states, the financial flexibility provided to states in the MSA is not only appropriate, but vitally necessary. The state fiscal crisis will continue, and without flexible use of MSA funds to target emerging priorities, states will be forced to cut education spending and make painful cuts in Medicaid expenditures for prescription drugs and long-term care as well as other public health and health promotion activities.

I thank you again for the opportunity to appear before the Committee, and I would be happy to answer any questions you may have.

Cigarette Tax Increases Since January 2002

Rank	State	Increase Per Pack	Effective Date
1	Connecticut	$1.01	April3, 2002 and March 15, 2003
2	Massachusetts	0.75	July 25, 2002
2	Vermont	0.75	July 1, 2002 and July 1, 2003
4	New Jersey	0.70	July 1, 2002
4	New Mexico	0.70	Jul1, 2003
6	Pennsylvania	0.69	July 15, 2002
7	Oregon	0.60	November 1, 2002
7	Washington	0.60	January 1, 2003
9	Arizona	0.58	November 25, 2002
10	Kansas	0.55	July1, 2002 and July 1, 2003
11	Montana	0.52	May 1, 2003
12	Michigan	0.50	August 1, 2002
12	Rhode Island	0.50	May 1, 2002 and July 1, 2003
14	Wyoming	0.48	July 1, 2003
15	lllinois	0.40	July 1, 2002
15	Indiana	0.40	July l, 2002
17	New York	0.39	April 3, 2002
18	West Virginia	0.38	May 1, 2003
19	District of Columbia	0.35	January 1, 2003
20	Maryland	0.34	July 1, 2002
21	Ohio	0.31	July 1, 2002
22	Hawaii	0.30	October 1, 2002 and July 1, 2003
22	Nebraska	0.30	October 1, 2002
24	Idaho	0.29	June 1, 2003
25	Arkansas	0.25	June 1, 2003
26	South Dakota	0.20	March 18,2003
27	Utah	0.18	May6, 2002
28	Louisiana	0.12	August 1, 2002
29	Tennessee	0.07	July 15, 2002

Source: Federation of Tax Administrators and news reports

State Excise Tax Rates on Cigarettes, 2003

Rank	State	Cents Per Pack	Rank	State	Cents Per Pack
1	Connecticut	151.0	26	Idaho	57.0
1	Massachusetts	151.0	27	Indiana	55.5
3	New Jersey	150.0	28	Ohio	55.0
3	New York	150.0	28	West Virginia	55.0
3	Rhode Island	150.0	30	South Dakota	53.0
6	Washington	142.5	31	New Hampshire	52.0
7	Hawaii	130.0	32	Minnesota	48.0
8	Oregon	128.0	33	North Dakota	44.0
9	Michigan	125.0	34	Texas	41.0
10	Vermont	119.0	35	Iowa	36.0
11	Arizona	118.0	36	Louisiana	36.0
12	Alaska	100.0	37	Nevada	35.0
12	Maine	100.0	38	Florida	33.9
12	Maryland	100.0	39	Delaware	24.0
12	Pennsylvania	100.0	40	Oklahoma	23.0
16	Illinois	98.0	41	Colorado	20.0
17	New Mexico	91.0	41	Tennessee	20.0
18	California	87.0	43	Mississippi	18.0
19	Kansas	79.0	44	Missouri	17.0
20	Wisconsin	77.0	45	Alabama	16.5
21	Montana	70.0	46	Georgia	12.0
22	Utah	69.5	47	South Carolina	7.0
23	Nebraska	64.0	48	North Carolina	5.0
24	Wyoming	60.0	49	Kentucky	3.0
25	Arkansas	59.0	50	Virginia	2.5

Source: Campaign for Tobacco-Free Kids, May 2003

The CHAIRMAN. Thank you.
Attorney General Moore, welcome.

STATEMENT OF HON. MIKE MOORE, ATTORNEY GENERAL, STATE OF MISSISSIPPI

General MOORE. Thank you, Senator McCain. And it's great to see my friend, Senator Lautenberg, back again, and Senator Durbin, Senator Nelson, and my hometown Senator, Senator Lott. It's good to be with you.

I will just talk from my heart a little bit today. Some of the information that I've just heard just grieves me just a little bit, and I think we might ought to rewind history a little bit and remember what this was all about.

I know the courage that Senator McCain showed, and Senator Lott and others, who worked with us to put this bill in the Commerce Committee back in 1997. People seem to forget about that, that there was really an original settlement that came before Congress that turned into the McCain bill. It had FDA jurisdiction in it, something that a lot of the naysayers said, "Oh, we'll get that through the courts." Well, we didn't. It had, eventually, $550 billion worth of dollars in there, some that would go to the Federal Government, some that would go the State Government. It had advertising and marketing restrictions way beyond anything any public-health person had ever even thought about.

In my opinion, had the McCain bill passed the United State Senate, we would have seen a 50 percent or greater reduction in teen smoking in this country by this point. We certainly wouldn't be having this argument with the states about how they're spending the money. But, unfortunately, we're not there.

In 1997, Mississippi settled its case that it had fought for about 4 years. Florida followed, settling its case. Texas followed, and Minnesota. Later on, Plan B, which was the 46-state settlement, which didn't have the same type advertising and marketing restrictions, and much less money, because the leverage had changed in those years.

All those things that the naysayers said were going to happen didn't happen. We lost FDA. A lot of the states' cases were lost. And so by the time of the 1998 settlement, basically the leverage was lessened.

My point about that is, if you rewind history a little bit, a couple of things come to mind. When we settled our case and Florida settled their case, the tobacco companies gave us an extra amount of money while the bill was pending in Congress. To do what? To start prevention programs. I got $62 million extra, on top of my settlement, to immediately start a pilot program to find out what worked on prevention. Florida got $200 million. Texas got above $200 million.

Mississippi, one of the poorest states in America, and Florida, started their programs. We began to see immediate reduction in teen smoking and even adult smoking in our states over the first two or 3 years. The plan was for us to use that as a template for all the other states, should there be a national settlement.

Texas—it hasn't been pointed out, but I'll point out—never even used the $200 million that they were given, on top of their settlement, for prevention programs statewide. They expended it in just a few counties. They put the money in the bank, even though their settlement said they "shall have a prevention program." And, unfortunately, that didn't occur.

So, fast forward. The settlement occurs in 1998, the MSA that everybody talks about. And then all of a sudden we start getting letters. Senator Lott will remember this, because I think that was the first phone call I made. Donna Shalala sent me a letter and said she wanted 80 percent of my money, in Mississippi. And I remember what happened. The Governors of the country, the legislators of the country, and attorneys general of the country, what we said together was, "The states fought this fight. The Federal Government didn't fight this fight, even though we invited them in. They thought we were foolish and we didn't have a chance to win." I'll never forget them telling me that when I went to see them in 1994. So what we did is, we asked Congress, the House and the Senate, "Please pass a bill, let the states keep all the money. And, if you do, so there won't be any Medicaid claim, trust us"—I remember it, because I was one of the messengers going to each and every one of your offices and saying this—"trust us, we'll spend the money on prevention and public health matters." Trust us. The Governors said that, the national legislative groups said that. Trust us. There was even a debate—Senator Lott, you will remember, "I don't know if we can trust the states or not, maybe we ought to have a set-aside," and Senator Lott—I guess I can say it now—was helping us, "Maybe we should have as much as a 25 percent set-aside." Some wanted 50 percent. But, "No," we heard from the Governors and others, "let the states decide how to spend this money. But, trust us, we'll spend it on this prevention program."

This was a tobacco lawsuit. It didn't have anything to do with highways. It didn't have anything to do with sewers. It didn't have anything to do with creating a morgue out in North Dakota. It didn't have anything to do, in Michigan, for creating college scholarships for middle- and upper-class students. This was about the number one public health problem in America. Now, whether people believe it or not, more people die from this cause than any other cause in this country.

And I was glad to hear my friend, Matt Myers and Senator McCain, say that now only 2,000 kids start smoking a day. When we were debating this in Congress, it was 3,000 kids start smoking a day, and it was 430,000 people die. Now it's only 400,000 people a year die from tobacco-related disease.

My point to you is, if you know that more people die from one thing than anything else in this country—I remember the debate. You guys debated this for a solid year on the floor of the Senate and the House, and I didn't hear, one time, people talking about budget deficits. What I heard was, "We need—help our children, protect our children. Prevent the tobacco companies from hooking them into a horrible addiction that will turn out to lung cancer and heart disease and emphysema." And I heard about all the great things that Senator Lautenberg did, and Senator Durbin, Senator Wyden, and all these courageous people before us that did this. It was just a great cause. It was the number one story on every newspaper, TV show. It was a great thing, and people were really going to do something. We were going to change the public health of this country.

And then guess what happened? We settled the cases. We got the money to do it. Not a little bit of money. $246 billion. To do what? To clean up the mess.

And are we cleaning up the mess? I've been to 44 states giving a speech called "Spend The Money On What The Fight Was About." And one of the analogies I use, and I'll say it very quickly, is, what if, in Alaska, when the Exxon Valdez ship crashed, and the oil spilled out into the beautiful, pristine Sound and all the little oily fish and oily birds and the pristine environment was destroyed—what if the Governor and the legislature in Alaska had said, "You know, when we get this money from Exxon, we need some new schools. You know, we need to build some new roads. You know, we have a budget deficit this year. We've got a hole in our budget. Leave the mess out there. Leave the oil out there." You see, everybody in this country and the world would have been in an outrage. Why? Because you can see the mess. I mean, you can see the birds and the fish and all the terrible environmental disasters that are occurring, so of course they had to clean up the mess.

I'm not talking about oily fish here, Senator. I'm not talking about little floppy birds. I'm talking about 400,000 grandmas and grandpas and uncles and aunts, and I'm talking about 2,000 real children who are beginning a life that, one third of them, are going to die from it. And I'm talking about having the antidote, having the penicillin, having the substance that we can inject and make a change.

Some say I'm in the poorest state in America in Mississippi. Sometimes I think we're the richest state in America. Who has an excuse in this room? Mississippi takes all of its money from the tobacco settlement, places 100 percent in a healthcare trust fund, by statute. On top of that, we've spent over $20 million on a prevention program. And, Senator Lott knows this, we've reduced teen smoking in Mississippi by over 30 percent. We've reduced middle-school smoking by 50 percent. We've reduced adult smoking by 20 percent. That's the astounding number. We have 70 percent more smoke-free homes now than we had when we started.

The only place that prevention programs don't work are where they're not being tried. I've used some strong words in my speeches across the country. I call it "moral treason." I remember why we filed these cases. With all due respect to the Governors and the legislators in this country who are making decisions about this, this money didn't fall out of heaven. It really didn't fall out of heaven. It has a connection with a lawsuit that we filed that was real. And if it wasn't real, we wouldn't have settled, we wouldn't have won this money.

Governor Chiles, in Florida, God rest his soul, would turn over in his grave today if he knew what had happened in Florida to his program. Tremendous gains. And then all of a sudden, well, we're successful, so let's quit doing it.

Every single state in this country that's doing the right thing, including Delaware, by the way, are making a difference. So if I sound like I've got a hollow place in my belly about this, I do. I'm proud of my state, and we're doing good, and we—Senator McCain, we lived up to what I told you. I told you, “Trust us. You let us keep all the money, and we’ll do the right thing.” But the majority of the states in this country, frankly, think the money fell out of heaven, and I really wish that Congress would do something about this injustice. We had one chance to change the public health of this country for the better, and I think we’re wasting it.

Don’t tell me about the budget deficits. Don’t tell me about needs coming Mississippi. I’m going to have a $700 million budget deficit next year, in Mississippi. $700 million bucks. That’s a lot of money. They’re not going to attack my prevention program. Do you know why? Because in the long run, every dollar you invest in prevention in tobacco saves you three dollars.

All this woe about the Medicaid program? Why do you think we filed this lawsuit? The majority of people who smoke are the folks who are on Medicaid. They’re the poorest people in this country. If you reduce the number of people that are the poorest from smoking, you will stop heart disease and lung cancer and emphysema and all those things, and you will, therefore, reduce your Medicaid budget tremendously.

So it is shortsighted thinking to securitize your money, to sell off the future of your children and your people. It is shortsighted thinking to take the money that you have and spend it on other things because you have a budget deficit. My question to the Governors and the legislators today is, What would you have done if we didn’t have a tobacco settlement?

Thank you, Senator.

[The prepared statement of Attorney General Moore follows:]

PREPARED STATEMENT OF HON. MIKE MOORE, ATTORNEY GENERAL, STATE OF MISSISSIPPI

Good morning, Chairman McCain and Members of the Senate Commerce Committee.

It is my pleasure to again appear before you and address the important public health issues concerning the historic tobacco settlement. I remember very well the days, weeks, months, and years put into the historic battle with the tobacco companies. I remember the legal battles, the political battles, and the legislative battles.

Mississippi filed the first case against the Tobacco Industry in May of 1994. We claimed the tobacco companies were killing 430,000 people a year, attracting 3,000 new teenage smokers every day by their marketing and advertising, and costing our state millions of dollars a year in the medical treatment for those indigent citizens in our health care programs.

The industry responded that the use of their product did not cause death and disease, that nicotine was not an addictive drug and they certainly didn’t advertise and market to children. They were proven wrong on all counts. In June of 1997 a historic settlement was announced among all the states Attorneys General and the Tobacco Industry. That settlement provided Food and Drug Administration (FDA) regulation over nicotine, $368 billion for the states and various Federal programs, major marketing and advertisement restrictions and much more. This Committee with the leadership of Senator McCain brought forward the settlement in legislation, held hearings, added many refinements and strengthened the original settlement. Unfortunately, that fell a few votes short of the requisite 60 votes needed to pass the Senate. In the interim between June of 1997 and June of 1998 the landscaped had changed. Mississippi, Florida, Texas, and Minnesota settled their cases, taking away some of the toughest cases against the industry. Some of the states had legal setbacks, FDA regulation looked shaky and thus leverage had shifted. In November of 1998 a settlement of $206 billion that included some of the advertising and marketing provisions of the original settlement was announced by the remaining 46 states. Known as the Master Settlement Agreement (MSA) this settlement did not require any Congressional approval and settlement dollars began to flow to all the states in the next year. A huge public health victory-we had what we needed to immediately impact the number one cause of death in this country.

Since the Tobacco Settlements I have been in 44 states giving a speech called "spend the money on what the fight was about." I have discovered that some governors and state legislators must believe that the tobacco settlement dollars fell out of heaven . . . that the dollars have no connection to the public health lawsuit that we brought. The money is being spent on one-time budget deficits, college scholarships, tobacco warehouses, roads, anything but prevention, cessation, and improving public health of this country.

If tobacco really kills 430,000 people a year in America-If tobacco related disease really is the number one cause of preventable death in America-then why is it we get $246 billion to do something about the problem and only a few states are using the money at a substantial level to make a difference. Comprehensive tobacco prevention programs work. They have worked everywhere they have been implemented. The only place they don't work is where they have not been tried.

In Mississippi, one of the poorest states in this country, we take all the money from our tobacco settlement and place it by law in our Health Care Trust Fund. These dollars can only be spent on public health matters. We spend $20 million a year on a prevention/cessation program call the Partnership for a Healthy Mississippi. It is truly a successful comprehensive program. In the first few years we have reduced the number of public high school students smoking by more than 20 percent and middle school students smoking by almost 50 percent. That means that there are 28,000 fewer kids smoking in Mississippi since the start of the program. We have dramatically reduced adult smoking by 20 percent and changed attitudes across our state about the importance of clean indoor air increasing the number of smoke-free homes by 63 percent since 2000—that means 406,000 people are no longer exposed to second-hand smoke in their homes.

I have heard all the arguments by those states that have chosen not to live up to the purposes of the tobacco fight.

1. That the settlement documents don't say we have to spend the money on tobacco prevention and cessation. To them I say the preamble of the settlement provides ample language that public health improvements, protection of our children, and the reduction of death and disease from tobacco form the basis of the agreement. When did doing the right and moral thing have to be spelled out? These same public officials promised Congress in 1999 that if Congress would prevent the Department of Health Human Services from requiring the states to reimburse the Federal Government the Federal percentage of Medicaid from the tobacco settlement dollars they would spend appropriate amounts on tobacco prevention and cessation. Governors and legislators all over the country rallied and lobbied to keep Secretary Donna Shalala from seizing the Federal share, promising they would do the right thing-I was there, I heard it, they said 'trust us'. Congress agreed, passed the appropriate legislation and most of the states have not lived up to word.
2. I also hear "we have a budget problem-a hug deficit, so we need this money to fill the hole." This short-term thinking makes little sense when compared with the dollars saved by a long term investment in reducing deaths and disease from tobacco use and preventing our children from starting. We have had the capability to reduce the deaths, disease and the billions spent in health care costs by half. This public health campaign should have begun in every state in American in 1999 but unfortunately it has not.

I congratulate all those states like Maine who just announced dramatic reductions in youth smoking this month. Florida, Massachusetts, and California all had great results but have now been cut back. I know we can do better. The Attorneys General of this country fought long and hard to achieve this important public health victory, I hope that this committee will take action to make sure that this victory does not tum into another defeat by Big Tobacco.

Senator NELSON. Mr. Chairman, may I take a point of personal privilege to commend the attorney general of Mississippi, who was one of the great leaders in this fight, and I was aware of it at the time, as a statewide elected official in Florida, where Florida and Mississippi, our two attorneys general, Bob Butterworth and Mr. Moore, consulted so frequently. And there is a tale of two states. The State of Mississippi today, that all that tobacco money is being spent as it was intended, on prevention, and the State of Florida, the chart that makes that chart pale by comparison, having $840 million a year coming in, and they are spending on prevention now one million dollars. It's a sad commentary.

Thank you, Mr. Chairman.

The CHAIRMAN. Well, thank you very much.

I'd like to mention that Senator Lott was the Majority Leader at the time we passed this bill through this Committee with a vote of 13 to 1. He was the one that allowed us to spend weeks on the floor of the U.S. Senate in an effort to get that bill passed. And I'm grateful for his support. And I understand why we had to pull the bill. And so I want to personally thank him and all others who were involved in this issue.

You know, Mr. Scheppach, my beloved friend, Mo Udall, used to have a saying. He said, "There's a politician's prayer that goes, 'May the words that I utter today be tender and sweet, because tomorrow I may have to eat them.' "

[Laughter.]

The CHAIRMAN. Here's what our public officials said at the time of the MSA. New Jersey Governor Christine Whitman, quote, "Every penny of these funds should be used for health purposes, including prevention programs and counter-advertising to protect kids, cessation programs, and community partnerships to serve those who have already put their health at risk by smoking, in addition to existing important health programs, such as Charity Care and Kid Care." New Jersey now ranks 30th amongst the states.

Indiana Governor Frank O'Bannon, "This money can go a long way toward preventing Hoosier kids from ever getting hooked on tobacco and toward helping our citizens stop smoking and recover from smoking-relating illness." They now rank 26th.

It goes on and on. It's really disturbing, because Attorney General Moore and others came to us and said, "Stay out of this. Don't make the states devote any money to prevention and treatment of tobacco illness. Trust us. Trust us."

North Carolina Governor Jim Hunt, the consent decree gives North Carolina, quote, "a balanced approach to allocate tobacco settlement money. It will address our efforts to crack down on underage smoking and to prevent the health and well-being—protect the health and well-being of North Carolinians." They now rank 33rd in the country.

Dr. Healton described what's going on here.

My first question is to you, Mr. Scheppach, and I know you'll spout the party line, just as you did in your opening statement, but how do you answer Attorney General Moore's statement, if Mississippi can do it, the poorest nation in the country, why is it that other states in this country can't live up to the promises and commitments they made to their citizens and to Congress when they made this deal?

Mr. SCHEPPACH. Well, I'm sorry it wasn't somewhat better, in all honesty. I mean, the—I wish the percentage was 8 to 10 percent, rather than 4 percent, in this particular area. I do, however, say that it does take us awhile—yes, I think we do know what our effective programs are now, but I don't know that we knew that, necessarily, 3 or 4 years ago.

Plus, this fiscal crisis has really been impacted very differentially across the states. When I say, “This is the worst fiscal crisis since the second world war,” I mean it. In 2001, revenues were down over 5 percent. We have never had a year of negative revenue growth for states since the second world war. We’ve had quarters, but we’ve never had a year. We were down negative five percent. Medicaid growth over the boom period, 1995 through year 2000, was down to 5 percent. Those are the baselines we were working with. Medicaid jumped, in 2001, to 13 percent growth, and other healthcare, which is another 10 percent of the budget, jumped, as well. So I think states were caught in a very, very difficult situation. And it was differential. Places like New Jersey, New York, and California were hit extremely hard, where other states were hit less hard.

So I wish it was better. My hope is that, as revenues turn around and begin to grow, that larger amounts of money go into these particular programs. States have experienced when they’ve taken money from trust funds in the past that they have, in fact, replenished them when revenues did grow.

The CHAIRMAN. Well, I thank you, Mr. Scheppach, and I understand what your job is, and I appreciate you coming here today, unlike the Department of Health and Human Services.

But I just—and I don’t—it’s not useful for me to keep kicking you around, but a resolution adopted by your members in 1999 states, “The Nation’s Governors are committed to spending a significant portion of the settlement funds on smoking cessation,” unquote. In a 2001 NGA resolution, the same commitment is repeated. In 2003, silence. This is what gives politicians a bad name.

Ms. Hudson, securitization, I understand that you think that that’s a good idea. Is that right?

Ms. HUDSON. I do not.

The CHAIRMAN. You do not. Isn’t this—and maybe the other witnesses—well, I’m about out of time—isn’t this, sort of, a commitment to keep the use of tobacco products as a viable way of continuing revenue?

Ms. HUDSON. Well, I just think that states should have done what Delaware did, and put it into an account and spend it for health. Securitization is so risky, and it really hasn’t been that successful. And it doesn’t necessarily solve the problem, in that it’ll be spent in the right way when they do have it to spend. I also think it would be good if states would pass a clean indoor-air bill, so that there wouldn’t be an opportunity to smoke in indoor public places, that would go with all of this, and many states are doing that.

The CHAIRMAN. Thank you.

Dr. Healton, do you want to comment on that?

Dr. HEALTON. On securitization?

The CHAIRMAN. Yes.

Dr. HEALTON. Well, I think securitization is the penultimate example of robbing the—you know, robbing the fund and making the chance that a poor decision during a fiscal crisis can be changed in the future. I think that’s the great tragedy. And I also think—I don’t know the exact percentage—but it’s fiscally foolish, given the amount that’s being paid on the dollar at this juncture, given the liability situation and the litigation situation for the tobacco industry.

The CHAIRMAN. Senator Lautenberg?

STATEMENT OF HON. FRANK R. LAUTENBERG, U.S. SENATOR FROM NEW JERSEY

Senator LAUTENBERG. Thanks, Mr. Chairman. And I thank you for your interest in resolving this dispute over tobacco. You've been a staunch supporter.

My work on tobacco began here, and Dick Durbin was on the other side of the Capitol. We did it together, started in 1986, it was our activity in 1987, we got a bill passed. And it's very disappointing to see the reduction in prevention funds that we are regularly dealing with.

I want to say this, as kind of a start. First, Mr. Chairman, I want to ask consent that my full statement be included in the record.

The CHAIRMAN. Without objection.

[The prepared statement of Senator Lautenberg follows:]

PREPARED STATEMENT OF HON. FRANK R. LAUTENBERG, U.S. SENATOR FROM NEW JERSEY

Mr. Chairman:

I know that you and I both are dedicated to protecting Americans—especially our youth—from the dangers of tobacco. I applaud your leadership in this regard and thank you for holding this important hearing.

Today, five years after the settlement agreed to by 46 states and five major tobacco companies, tobacco control *remains* one of America's most pressing public health issues.

It is estimated that direct medical expenditures attributed to smoking now total more than *75 billion dollars* per year.

I used to smoke—a lot. Fortunately, my daughter, when she was a young girl, convinced me to quit. Since then, I have been fighting the tobacco industry. I'm proud to say that my work on the public health side of the tobacco debate started long before tobacco control became a mainstream issue.

I authored the law banning smoking on airplanes, which protected people from deadly secondhand smoke. That law changed our culture's attitudes about smoking in public places.

I also wrote the laws banning smoking in all federally-funded places that serve children. And I have consistently supported higher tobacco taxes to pay for expanding health coverage for children and the uninsured.

We have made progress over the past several years but we still have so much further to go. Tobacco use continues to be the No. 1 leading cause of *preventable* death and disease. Each year, tobacco claims over 400,000 lives here in the United States.

According to the Centers for Disease Control (CDC), if current tobacco use patterns persist in the United States, an estimated *6.4 million children* will die prematurely from a smoking-related disease. Every day, nearly 5,000 young people try cigarettes for the first time. On a positive note, smoking among adults has slowly but steadily declined since 1993; however, 46.5 million American adults still smoke.

After the flawed "Global Tobacco Settlement" proposal failed, and Chairman McCain's good tobacco bill was killed by the industry, the states struck their own, separate settlement with the tobacco industry.

While this "master settlement" did not tell states how they should spend the money, the governors and other officials from many of the States promised that they would use the funds for tobacco prevention and anti-smoking campaigns targeted to children.

At the time I was skeptical of the state settlement because it did not earmark funding for health. Unfortunately my doubts proved correct.

A study by the Campaign for Tobacco Free Kids found that only four states currently fund tobacco prevention programs at the level recommended by the CDC.

This is deeply disturbing. Especially when you consider that tobacco companies continue to spend more than 20 times as much to market their deadly products as the States spend to protect kids from tobacco.

The states are facing their biggest fiscal crisis since World War II or, in some instances, the Depression. It's no surprise that financially-strapped State officials are diverting tobacco settlement funds. But it's disappointing and it's short-sighted. Spending settlement money on tobacco control now will save *money* down the road by reducing health care costs. More important, spending settlement money on tobacco control now will save *lives* down the road as well.

Thank you, Mr. Chairman.

Senator LAUTENBERG. And that is that we suffer from a depletion of funds. And, you know, Attorney General Moore and Matt Myers and—we had a lot of contact. It's been several years since I've seen you. You're looking well.

And also, oh, for those days when we were constantly on the press and doing the right thing, and we thought that this was a role that was going to really curb smoking, and we wind up dealing with what I'll say is an opposition that never stops writhing, never stops fighting back, in such devious ways, at times, we don't recognize what's happening.

But I do want to say that the reduction in Federal funding in the states has caused us great distress. And I don't approve of what New Jersey did, and I don't approve of what other states have done, either. But some of it is to reduce pollution, which causes lots of lung problems, and some of it is designed to reduce accidents, which causes death and destruction. None of them have the impact, however, of tobacco.

And a dear friend of mine, who stopped smoking 30 years ago, just in the last couple of months was diagnosed with a lung cancer that evolved from his smoking days, and the future is bleak. Even though he's a mature man, the fact is that he was in the good state of life.

Matt Myers, I want to ask, should the FDA—should we continue to fight that fight and see if we can get tobacco regulated under the FDA? Can we trust them to do the job? What do you think?

Mr. MYERS. Senator Lautenberg, thank you for your question. We need a comprehensive approach. We need the states living up to their promise and spending tobacco settlement money on tobacco prevention. But we also need to regulate tobacco. It remains the least regulated consumer product in this Nation. We need to do both.

It's shocking that if Philip Morris sells macaroni and cheese, they have to test the ingredients, notify consumers of the ingredients, label the ingredients. If they put a known carcinogen in Marlboro, they don't have to do any of those things. We need to do that, and we need to do it soon.

But it's also not a substitute for states doing the right thing. I mean, Mike Moore said it correctly. If states as poor as Maine and Mississippi can find a way to protect their children from tobacco, every state can find a way to protect their children from tobacco.

Senator LAUTENBERG. I think that's fair to say. Again, not defending state action and not doing these things, but the states are in a pinch that has not been seen, perhaps, for 50 to 60 years.

Mr. MYERS. You know, while we all talk about that as a critical issue, and it is, tobacco has actually come to the rescue of revenue in over half the states in this nation, because they've increased their excise taxes, as did New Jersey. If the states would devote just a small percentage of those excise-tax increases, even after they securitize, we can protect our children. All we really need is them to spend about 8.2 percent of their tobacco revenue. This is money that came off of the backs of smoking so that we can do both. We shouldn't have to choose, in this country, between protecting our kids.

If we announced that, because of a budget crisis, we were going to withdraw polio immunization from our children, would anyone be saying, "Well, there's a budget crisis. That's OK"? That's what we've done with regard to tobacco.

Senator LAUTENBERG. That's a pretty good comparison. The problem is that it takes a long time for the impact of tobacco to——

Mr. MYERS. Actually, we see relatively rapid results in certain areas. For example, Massachusetts and California both targeted pregnant women. They reduced smoking among pregnant women by 50 percent, and paid for the entire cost of the program by doing so. They also reduced heart disease caused by tobacco within 12 months. That's not a 20 year lag time, as for lung cancer. Tobacco-prevention programs begin to pay dividends immediately.

Senator LAUTENBERG. Mr. Chairman, there is lots more that we'd like to hear from our witnesses. It's an excellent panel, and we thank you, but time is up. I don't know whether you intend to——

The CHAIRMAN. Sure.

Senator LAUTENBERG.—go around again.

The CHAIRMAN. Be glad to, Senator.

Senator LAUTENBERG. Thank you.

The CHAIRMAN. Senator Lott?

STATEMENT OF HON. TRENT LOTT, U.S. SENATOR FROM MISSISSIPPI

Senator LOTT. Well, first, thank you, Mr. Chairman, for having this hearing and having this very good panel here this morning. And thanks to all of you for being here. I apologize for not directing a lot of questions to the other four panelists, but he is from my home state and my hometown, so I'm going to address most of my questions to our attorney general from Mississippi.

And I want to say we appreciate the job you have done. You know, if people want to know why Mississippi was able to put this money where it needed to go and handle it in the right way, the simple answer is because Mike Moore wouldn't let them do otherwise. But you did also, I guess, we'd have to say, have cooperation from the state legislature to set it up in the way that it was done, and I'm very proud of how our state is handling it.

As a matter of fact, those funds are being used in ways that do some things that would need to be done by regular funding from the state if they didn't have this fund, so it's not a zero-sum game. We're taking some of the programs that needed funding and are taking care of it.

But let me ask you some specific questions for the benefit of those that have not been as wise as Mississippi. What did you do to make sure it was handled this way in Mississippi? Other than being a watchdog and snarling at anybody that started breathing heavily on it. What did you and the state legislature and the Governor do to set it up the way it was done?

[Laughter.]

General MOORE. Well, if you'll remember, we didn't get a lot of cooperation from the Governor. The Governor actually sued me to try to stop the lawsuit, so we—that wasn't going to work. The Governor at the time was opposed to it. So the first thing we did was, I got it written in our court order that settled our case, that the money should just be used for healthcare and prevention programs. And that could be challenged, the legislature could have challenged that, but when presented with a court order, let's just say they were cajoled very easily into saying that we ought to spend—pass a law that says create a healthcare trust fund, put all the money in there, and the original idea was just to spend the interest on expanded healthcare programs in Mississippi. And that worked for the first two or 3 years. The last couple of years, one of the things they could spend some money on is the expansion of new programs for Medicaid, so they took some money out to spend on Medicaid.

But separate and apart from that, we also put in a court order the establishment of the Partnership for a Healthy Mississippi, which is our comprehensive prevention program, and that has remained unchallenged through the years. Part of it is cooperation, Senator Lott. Truthfully, part of it is its success. Had it been a failure, had numbers not gone down in Mississippi, I guarantee you I would have had folks challenge me in court about the validity of the court order, and they would have tried to dismantle the Partnership for a Healthy Mississippi. But because it's been just a remarkable success, you know, we don't believe in shutting down success in Mississippi when you get it going, like some of the other states have done. I think Senator Nelson mentioned that, in Florida.

Senator LOTT. But the legislature did pass the legislation to set up the——

General MOORE. The healthcare trust fund, absolutely.

Senator LOTT. What is it being spent on? Other than, you know, the prevention programs, the programs that have been targeted at children, trying to make sure they understand that they shouldn't be smoking. You mentioned some of the Medicaid programs. Could you give me just two or three examples?

General MOORE. Sure. We've expanded some Medicaid programs, covering more folks, which was the original intention of the settlement. Matt will remember this, when we were in discussions with the White House and others, part of this money—Senator Lautenberg and—or, he's gone—Senator Durbin, you will remember—to fund the extra part of children's healthcare, the match for the Federal—and we're using part of our money—matter of fact, the first 2 years, we took $6 million from the interest that funded the entire match for Mississippi to expand our children's healthcare by 50,000 folks. We set up trauma centers in hospitals that didn't have any trauma centers, a lot of things for the disabled. So it's been—it's done very well.

Senator LOTT. OK. All right. So we have a problem, though, in all these other states that have not followed your example and our example. What is the solution? And is this going to be resolved again in the courts? Do we need to come back and address it again at the Federal level?

General MOORE. Well, you know, for years—and you and I have talked, Senator McCain and I have talked—about the possibility, and especially when you had the hearing 3 years ago—I always, in these speeches, tell folks, you know, what Congress gives, Congress can take away. You know, you gave an exemption for the expenditure of this tobacco money, basically saying that there wouldn't be any Medicaid claim. I would certainly hope that Congress didn't do that, but it might be that this statute ought to be revisited and take a look at how the states are spending their money, because it was a deal.

I mean, the reason I remember it is, I was up here every single day, walking into offices, talking to legislators, saying, "Believe me, trust us, we're going to do this the right way." And we met with the Governors Association, met with the legislators, and they just wanted autonomy, but they said, "Trust us." If they'd never said that, you would have never passed that bill. Kay Bailey Hutchison, in your body, and Chairman Bilirakus, in the other body, never would have gotten those things passed had we not said, "Trust us, we'll spend the money the right way."

So I'm saying most of the states have reneged on the deal they made with the U.S. Congress to get that historic change in the Medicaid law. Maybe we should revisit it.

Senator LOTT. Well, thank you for being here. I'm proud to hear the statistics that you've given about, you know, what's happened in our State of Mississippi. It's been a good week, with this information and beating Auburn, too.

[Laughter.]

General MOORE. That's exactly right.

Senator LOTT. We're on a roll. Let's keep it going.

General MOORE. Six-and-oh, Senator, and we're—and thank you, again, too, for the leadership that you provided to us and the help behind the scenes, especially with this issue.

The CHAIRMAN. In all due respect to the great State of Mississippi, isn't it true that Mississippi has been noted as the poorest state in America; and it is the poorest people, generally speaking, lowest income people, that are addicted to smoking.

Senator LOTT. Right.

The CHAIRMAN. So, therefore, what's been achieved in Mississippi is truly remarkable, when put in that context. Is that right, Mr. Myers?

Mr. MYERS. That's exactly right, Your Honor, and—I mean—Your Honor——

[Laughter.]

Mr. MYERS.—Mr. Chairman. You like that, too.

The CHAIRMAN.—you're talking to Senator Lott.

[Laughter.]

Mr. MYERS. That's exactly right. And when we talk about crushing Medicaid burden, that's what we have to understand, is that states like Mississippi and Maine and several others have proved that we can literally lift that burden off our poorest citizens, who can least afford it, and that's a burden that falls on every taxpayer, because it translates into billions of Medicaid dollars that are needlessly spent.

We can do something about state budgets if we lower smoking rates among the poorest citizens. And programs like the program in Mississippi, the program that originally existed in Florida, were doing just that.

The CHAIRMAN. Senator Durbin?

STATEMENT OF HON. RICHARD DURBIN, U.S. SENATOR FROM ILLINOIS

Senator DURBIN. Mr. Chairman, thank you for inviting me here. I'm not a Member of this Committee, and I came to testify, and you were kind enough to let me come take a seat. Bill Nelson was kind of enough to let me precede him in questioning. And I'd like to make my statement part of the record, with your permission.

The CHAIRMAN. Without objection. You're welcome here, Senator Durbin.

[The prepared statement of Senator Durbin follows:]

PREPARED STATEMENT OF HON. RICHARD DURBIN, U.S. SENATOR FROM ILLINOIS

Mr. Chairman, Ranking Member Hollings, and Members of the Committee, thank you for holding this important hearing on how states have allocated their settlement revenues since signing the 1998 Master Settlement Agreement (MSA). I would like to commend you, Mr. Chairman, for your work 6 years ago to try to enact comprehensive legislation to hold the tobacco industry accountable for the harm it has caused to so many millions of Americans. While it was an assignment you might not initially have sought, you worked valiantly to promote a public health-oriented solution. And while your bill did not become law, I think it is fair to say that the Master Settlement Agreement between the states and the tobacco companies would not have been as strong as it was without your efforts.

I also salute you, Senator Hollings, for standing up for public health and accountability with a position that must have required a deft handling of some of your constituents back home.

I am sure that a lot will be said today about the importance of holding states to their commitment to use a significant portion of the settlement funds to attack the enormous public health problem posed by tobacco use in the United States. As we reach the 5th anniversary of the MSA, I agree that states have a responsibility to adequately fund these prevention programs.

The Institute of Medicine, the Surgeon General, and the National Cancer Institute have all issued reports on reducing youth tobacco use. These reports signal that state funds spent on tobacco prevention and cessation will produce important results for the health of our country. In fact, in its August 2000 report, the Surgeon General found that the United States could make unprecedented progress and reduce tobacco use by 50 percent in one decade through the implementation of nationwide prevention and cessation programs.

Clearly, state tobacco programs play a vital role in decreasing tobacco use among youth, and it is critical that we take a close look at how states have been using the settlement funds. However, we must also recognize that an overwhelming majority of states, facing severe budget constraints, have turned to settlement funds to provide essential services, such as health care. I would hope that as the economy improves and the gaps in states' budgets are filled in, they will devote more of their MSA funds to launch tobacco prevention programs. But, we cannot ignore the fact that the ultimate responsibility of reducing youth tobacco use rests with the tobacco industry.

It is no accident that more than 80 percent of adult smokers today started smoking before the age of 18 and over half before the age of 16. Despite claims that their products are intended for adults, for years tobacco companies have targeted kids and have been deceptive about their alleged efforts to reduce youth tobacco consumption.

Eighteen months prior to the signing of the MSA, the tobacco industry claimed, during negotiations on a broader proposed agreement, that youth smoking would decline by approximately 40 percent over a 5-year period and 67 percent over a 10-

year period. If those targets weren't reached, the industry agreed to be subject to penalties. The tobacco industry appeared to be committed to these goals. However, when I offered an amendment to include these "lookback" provisions in the tobacco settlement bill and hold individual companies accountable for their share of the reductions to which they agreed the previous year, these same companies opposed my amendment.

So, here we are, five years later. Has the tobacco industry followed through on its promise, on its commitment to our Nation's children? The answer to this question, I am sad to say, is a resounding NO.

While youth smoking has decreased, we have not reached the goals that would have been established in the *lookback.* The decline has largely been the result of cigarette tax increases despite the industry's insistence that youth smoking is not price sensitive. Five years have passed, yet we find ourselves still fighting the same battle, youth smoking.

So, let's take a look back. Since 1998, tobacco companies have launched youth anti smoking campaigns, buying full page ads in the *Washington Post,* the *New York Times,* and the *Wall Street Journal,* saying that they adamantly oppose the sale of tobacco to kids. Hearing these claims, one would assume that the tobacco industry had turned over a new leaf, finally committing itself to reducing youth smoking. But, a California judge thought differently, and just a year ago, fined R. J. Reynolds $20 million for continuing to target kids through their advertisements in youth oriented magazines ads, which directly violate the MSA.

So, why would tobacco companies continue to advertise their products in magazines with high youth readership when their products are intended for adults? The answer is so simple that I will quote directly from a 1981 Philip Morris report:

> *"Today's teenager is tomorrow's potential regular customer, and the overwhelming majority of smokers first begin to smoke while still in their teens."*

It is no surprise that in the first year after the MSA was signed, advertising in youth-oriented magazines, especially for the three brands most popular with youth, increased by 15 percent, jumping from $58.5 million in 1998 to $67.4 million in 1999.

We can no longer tum a blind eye to what is going on. The tobacco companies have continued to wage a war against our communities, and our youth are the most innocent of its victims. Clearly, as the system stands today, the tobacco industry continues to benefit from youth smoking. There is no incentive for the tobacco industry to truly work to prevent kids from smoking, so we must get rid of that profit motive that makes teen smoking attractive to them.

We cannot ignore the critical foundation that was laid five years ago by the state attorneys general in fighting youth tobacco use, and I agree that we must hold states accountable for their use of settlement funds. But we must broaden this discussion to include holding the tobacco industry to its promises as well.

I hope that out of this hearing today, we will develop a plan to successfully tackle this problem of youth smoking. I think it is time resurrect the lookback mechanism to hold each company accountable for its share of youth smoking. We owe it to our nation, our communities, and especially to the 5 million kids who are regular smokers and find themselves facing a deadly addiction.

I commend this Committee for taking the first step in that important direction. Again, thank you Mr. Chairman. I appreciate the opportunity to share my views. It is important that we continue to monitor this issue, and I look forward to working with you in that regard.

Senator DURBIN. Thank you.

Mr. Chairman, let me start by saying thank you. We don't talk about tobacco anymore around this place. There hasn't been a good conversation about tobacco on Capitol Hill in a long, long time. Thank goodness you're an exception and are willing to step out and continue to lead on this issue. It really is a matter of life and death. And the fact that you're showing this political leadership is not lost on this Senator and a lot of your colleagues and people who are following these hearings.

Tobacco has been an important part of my life, personally and politically. When I was a sophomore in high school, my father died of lung cancer. He was 53 years old. I didn't stand by his bedside as he gave his last breath and say, "I'll get even with those bastards," but when I was elected to Congress and started facing these tobacco issues, whether it was wasted money on the so-called "safe cigarette" research or some of the things we're doing to promote tobacco in other places, it wasn't lost on me that there were a lot of people around America who shared the same life experience that I did and my family did. And that's why I joined Senator Lautenberg—and we were successful many, many years ago now, Frank—in banning smoking on airplanes, and why I stood and watched, with real admiration, Senator McCain, as you led the way in trying to show some Federal leadership on this issue.

Today, we are discussing the obvious. We are not putting money into tobacco prevention, and more children are becoming addicted, and those addicted children will ultimately—at least one out of three of them—die from this addiction. That's the simple fact of the matter.

We've talked about the lack of money that's there. But, in my mind, it is not so much a depletion of revenue, but a depletion of resolve. A depletion of resolve at the State and Federal level.

Attorney General Moore, thanks for your leadership. You have been a national leader on this issue. And, Matt Myers, you and I have been colleagues on this for a long, long time. I would just say your Prince William Sound Exxon Valdez analogy—I'd take it a step further, for Mr. Scheppach and the Governors. How many of these Governors are willing to walk away from earmarked funds, from gasoline taxes, and highway trust funds, and say, no, we're going to spend those on Medicaid? You know what would happen in my state capital and most others? The contractors and the labor unions and the mayors would all be there screaming bloody murder, "Wait a minute. That money was for highways. That money's not for Medicaid." And yet when it comes to the tobacco money to save the lives of people in those states and to prevent death and disease among children, there isn't this same level of anger.

And at the Federal level, I was afraid, when Senator Hutchison offered her amendment, that we'd be sitting here today, 5 years later, saying, "They didn't keep their word." The states didn't spend the money as they were promising they would, and we let them off the hook. We let them off the hook here on Capitol Hill, and that is sad and unfortunate.

Dr. Healton, I want to tell you something. I really admire what Legacy's done. And I watch those Truth ads and think, "Right on." If we could get those ads on the air on the right program and across America, it'll have as great an impact as raising the cost of the product does with children.

I read your testimony and hear that you may be going away. Is that a fact?

Dr. HEALTON. Well, our revenue source has declined by 90 percent because of a provision in the Master Settlement Agreement. It required that the participating manufacturers collectively represent 99.05 percent of the market for us to receive a payment. If they represent 99.04, we do not receive a payment, which, in essence, is a sunset clause, though Mike Moore may want to comment a little more on it.

So our existence is threatened. But, because the board wisely set aside some of the payments to us, we will operate at a level, but it will be so substantially below the current level that we will be unable to provide a national ad campaign.

And I would just comment, Senator Durbin, that I want to thank you for coming to the event that we had here on the Hill for staffers about the Truth Campaign, and just also point out that presently spending about $75 million in the advertising marketplace for the Truth Campaign and bringing it to the highest risk kids, it has been enormously successful, and it's probably responsible for about half of the decline that has been observed in youth smoking.

If the rates stayed where they were in 1997, when you folks were talking about this issue here on the Hill, two million more young people would be regular smokers than are today. So I think we should all collectively be proud of the successes we have had, while we remain vigilant about what still needs to be done. And I thank you for your interest in the program and your support for, at times, a controversial campaign that's intended to grab the hearts and minds of our most at-risk adolescents.

Senator DURBIN. Mr. Chairman, the voice of Truth, the voice of the Legacy campaign, is a small voice against the roar of tobacco advertising, but it's so good that we can't let it go away. I don't know what I can do. I hope that you'll join me, Frank Lautenberg, and Bill Nelson, and any other Senator. We can't let this go away. If this is all that we make a commitment to do, we can't force Governors to spend this money at this point, but we can't let this go away. And I hope we can find a way to find the revenue to keep you on the air.

Thank you, Mr. Chairman.

Mr. SCHEPPACH. Mr. Chairman, can I make a comment?

The CHAIRMAN. Yes, sir.

Mr. SCHEPPACH. Since everybody's talking about the commitment of the Governors, I just want to read from our resolution that was longstanding, and it was that they're committed to——

The CHAIRMAN. In what year, Mr. Scheppach?

Mr. SCHEPPACH. Well, this goes all the way back, I believe—it's been in existence from probably 1997 or so.

But the commitment was to spend a significant portion of the settlement funds on smoking cessation, healthcare, education, and programs benefiting children. Now, I think that that depends upon what you define as significant, but I think 45 percent of the money is, in fact, going to those areas. Now, everybody has focused on cessation, and, you know, our hopes are that that can be increased over time. But as far as I remember, that was our commitment. Now, I can't speak for any individual Governor, but as far as the organization is concerned, I think that's been our commitment.

The CHAIRMAN. Well, I guess that deserves a response. Mr. Moore?

General MOORE. What I know is that, you know, it's great to put something down on a piece of paper and have a vote and read it. The people who came up here and lobbied Congress, we would have never gotten Congress to pass the exemption that they passed with a, you know, "We'll spend a little money," or, "Don't worry about it, we'll take care of it." I mean, it was—you remember, President Clinton and Donna Shalala, from the Administration, were against this bill, and they were only for it if the states spent the money on prevention programs and expansion of children's healthcare and had four categories that he was for. So I can't imagine that we would have been successful without the cohesiveness of Governors and legislators and others at least telling a convincing story that, "Trust us, we'll spend the money the appropriate way."

And I understand all the excuses. I've heard them all. I live in Mississippi. I hear all the excuses about needs and deficits and all those kind of things. But this was a lawsuit against tobacco. This had nothing to do with any of those other things.

Mr. MYERS. Mr. Chairman, could I just also respond to—because I think it's important to note—and it's very disturbing—that when the National Governors Association was seeking the waiver, they came forth with a resolution to contain the commitment. But when Congress stopped looking, they revised the resolution, and they took out that paragraph, that promise.

I don't think that was a promise for 2 years or 3 years. That money is coming in in perpetuity. I thought that was a long-term promise that the states and the Governors made to Congress, not that they would change the second that no one was looking.

The states do face hard choices. But, in 2000, they spent 43 percent of the money on health, now it's down to 28 percent. In 2000, they spent 9 percent on tobacco prevention, now it's down to 3 percent.

If we're going to solve the problem with tobacco, it requires a straight-up, honest commitment of a long-term and sustained nature, not that we go somewhere else as soon as someone stops looking. I don't think we can afford to see this continued diversion of funds if we're going to protect our kids.

The CHAIRMAN. Mr. Scheppach, I don't want—again, I don't want to continue this debate, because I think facts will take care of this argument. But these two statements, of 1999 and 2001, clearly they are talking about healthcare and education as related to tobacco. That's why policy position tobacco settlement funds policy. I mean, when you read the entire statement, in 1999 and 2001, you draw the obvious conclusion we're not talking about taking care of Medicare. We're talking about tobacco-related illnesses. That's certainly the way that I read this statement.

Now, you can draw out—say, "Oh, healthcare, so it's OK for us to spend the money on our Medicaid programs," but that's not the way that reads in its context, at least from my viewpoint and that of others.

And I also, again, want to repeat, I know that you are here to defend your organization, and I appreciate that. But I can't let it go, just say, "Well, we said that it would be healthcare." It's clear that this statement is about health-related illness—tobacco-related illnesses and could be—I don't see how you could interpret it any other way.

And, in interest of fairness, please, you respond if you would like to.

Mr. SCHEPPACH. Yes. I mean, you have the advantage of, in report language and other things, of knowing what the debate was. I think I was there at the time and listened to the debate. We did a lot of analysis on the effectiveness of cessation programs at the time, and the feeling was you couldn't put $8 billion or $10 billion a year of additional money in cessation programs and make them effective. So I think——

The CHAIRMAN. Well, I——

Mr. SCHEPPACH.—we were talking more broadly.

The CHAIRMAN. Are you talking about treating health-related illnesses, too—tobacco-related illnesses?

Mr. SCHEPPACH. Well, you get into problems, I think, of defining what is specifically tobacco related. I think, you know, you've got to deal with those in the broader programs that we've got.

The CHAIRMAN. Well, I guess I wish that I had been in there when the debate and discussion took place, because then I would have had a different position about earmarking funds that—and making it mandatory that it be spent for certain purposes. And I thank——

General MOORE. Senator, if I could respond for just 1 second?

The CHAIRMAN. Yes, sure.

General MOORE. Just very quickly. I don't want anybody to be confused. In 1999, when this decision was made, the California results had been in for years and years and years and years, about the reduction in their program. The Florida numbers had come in that year, humongous reduction. Massachusetts numbers were in. We knew, in this country, what worked. And the reason I know that is, we modeled our program in Mississippi, starting in 1998, on the successful programs of Florida and Massachusetts and California and others.

And another point, and I'll quit, is that we're not talking about if a state receives $100 million a year, to take that $100 million and spend it on TV anti-tobacco. What we're saying is if you even spent 20 percent of that money—if you took 20 million out of that hundred and take the 80 and do whatever it is you want to do with it—if you took 20, you could have a huge impact on this problem. But what we're doing is, we're taking 3 percent nationwide, and that's just not—it's not good.

The CHAIRMAN. Senator Nelson?

STATEMENT OF HON. BILL NELSON, U.S. SENATOR FROM FLORIDA

Senator NELSON. Mr. Chairman, what we've heard here is shocking to me; it's not surprising. And I must say that I am chagrined, Mr. Chairman, that the states being in the fiscal distress that they are, and we had in front of this Congress, earlier this year on the tax bill, a question of how much money we were going to send to the 50 states who are in fiscal distress. What ultimately emerged in the package was $20 billion to the states, close to a billion dollars going to my state alone. There was an amendment that I voted for, $40 billion to help the states in their fiscal distress. And yet what we're hearing today, shockingly, is the money that came from the tobacco settlement, which was clearly stated at the time that a certain portion of this was going to go for prevention so that ultimately the states would have less healthcare costs through Medicaid, that that money is not being spent. That's unconscionable.

And, again, I go back with great commendations for Mississippi and the attorney general, who's with us today, of where the recommended spending by the CDC that Mississippi today, years later, over half a decade later, after the settlement, that Mississippi is exceeding that in spending on tobacco prevention.

And then, sadly, I turn to the page on Florida. Florida, having settled its case one month after Mississippi, a much bigger state than Mississippi, with a lot more dollars coming in, and lo and behold, what the CDC's recommended spending on tobacco prevention—Florida today is spending 1 percent of the CDC's recommendation. And yet we send $20 billion to the states, and I voted for a version that was to send $40 billion to the states because of their fiscal distress. So it distresses me.

You know, Mr. Scheppach, one of the things that the Governors ought to be asking themselves is how much of the dollars that they are spending for smoking-related illnesses—how does that compare to what you're spending for prevention? Are the Governors asking themselves that?

Mr. SCHEPPACH. I would probably disagree that, in the short run, there would be significant savings. Medicaid, most of that money is going into nursing homes, and people generally are going to end up there at some point in time. Women and children are relatively inexpensive. Most of the money is in long-term care, drugs, it's for the so-called dual-eligibles for Medicare and Medicaid. That's where all the money is.

Senator NELSON. Well, do you know what's happening in Florida right now? Now that you brought up nursing homes? What's happening—under Florida law, a person who is in a nursing home, under Medicaid, pays their income to the State of Florida in return for being treated. But there are certain exceptions that the State of Florida is to deduct for their income—how much they pay out for health insurance, how much they pay out-of-pocket healthcare costs for deductibles and co-pays. And do you know that the State of Florida, right now, is not deducting that money, but, instead, is taking that money from the senior citizens to the average of $125 a month, or, for 15,000 seniors in Florida that are affected, that's $35 million a year that seniors on Medicaid in nursing homes are paying that they're not supposed to be paying, under the eligible law, because Florida, the State of Florida, is not adhering to the Federal law. So when you start talking about nursing homes, you've just hit a hot button of mine.

I want to get back to tobacco.

Mr. MYERS. Senator, could I also just—a quick comment on getting some facts straight. You do see a quick turnaround in Medicaid costs. Over half the pregnant women who smoke in this country are on Medicaid, because it is so directly related to poverty. A low birth weight baby, due to smoking, costs an additional $60,000 in healthcare costs. If you can dramatically reduce that, not only do you improve the life of our youngest, most vulnerable children, you save immediate taxpayer dollars, let alone the huge taxpayer dollars that you will save over the long run. It's not just shortsighted. It's wrong to think that tobacco prevention doesn't save money quickly.

Senator NELSON. I believe that that's true. I mean, it just is common sense to understand what you just said. But even if it weren't true, to save those 2,000 children a day that are beginning to get hooked every day, and the long-term healthcare costs to the country and to the states? That's worth it, right there.

Mr. MYERS. There's no question about that.

Senator NELSON. You know, this is something that we shouldn't be divided on. The tobacco companies, I would think, are on the same side of this issue of what we're arguing. And yet the tobacco settlement is not being implemented in the way that it was supposed to, with the understanding and the promises.

Mr. MYERS. To quote a tobacco industry lobbyist this year in the state legislature, "You know, my job would be a lot easier if my state had spent the money on roads and other things, like other states had." And I fear that that's true. They recognize that tobacco prevention programs work and make an immediate difference. We can't afford not to treat this problem seriously.

Senator NELSON. Amen.

Mr.——

The CHAIRMAN. Senator——

Senator NELSON.—Chairman, that light is red, and I've got a couple more questions that I need to ask, so I'll wait.

The CHAIRMAN. Senator Lautenberg?

Senator LAUTENBERG. Thanks, Mr. Chairman.

This settlement-lite, which is what we got, as compared to the tobacco industry—and, by the way, just to make sure that people understand where the industry is going, you know, we see the ads that say, "Buy nourishing food, and this is where you get it," and all that stuff, but lurking behind there, I suspect, is a lot of tobacco revenue still coming in there. And what do we do further to acquaint the public with the fact—when they buy a cigarette lite, that the fact is that, in many cases, they're damaging their health even more than if they smoked the regular cigarettes? And one of the things, Dr. Healton, that we see—and Senator Durbin adequately, I think, described our dismay at the fact that your voice isn't out there. How do we get these messages across, when the companies are spending, what, $7 billion a year, I think it is, on marketing?

Mr. MYERS. That's now up to 11 and a half billion dollars, 31 million dollars a day. The answer is, we need a sustained public-education campaign, both from Truth and from the Federal Government and in each state. The scientific evidence is now conclusive. Lite and low-tar cigarettes are not safer or less hazardous than regular cigarettes. Millions of smokers have switched to these products thinking that they were reducing their risk, and we now know it's not true.

We need a sustained media campaign to educate every consumer before they make that mistake and to help every consumer understand that the only safe cigarette is the one you don't smoke.

Senator LAUTENBERG. We look at the cost—and I thought Senator Nelson was going there some—and that is, the costs of the deferrals of investment in the smoking-cessation programs, have we—is there a way to calculate that? That we say, look, this thing that you don't do today will not get you out of a financial obligation, no matter what, that these costs are inherently there, and you're going to just get them. Is there anything that you see that has a—that can attract the kind of attention that we'd like to see put into this that says, “Hey, if you don’t spend the money today, you’re going to spend it tomorrow,” because I agree with much of what was said here about the irresponsibility of the states, and mine included, that says, “Hey, spend it on other things. Spend it on debt forgiveness.” There are other ways that we could generate revenues, but, instead, it’s—I guess it’s easier to give away something that people don’t see for awhile.

General MOORE. I think yours is a salient question. The best way I can describe it for you is that, you know, we just talked about the numbers—3,000, we used to say, kids start smoking a day, and now, 7 years later, we’re at 2,000 a day. The best way to say what the cost would be is, what if it was a thousand a day? What if we had actually reduced it down to a thousand a day? Then your cost is, for not acting, there are a thousand new kids a day who are going to start an addiction, and at least we know one third of them are going to die, so 333 kids a day times 365 days a year. Those are real lives that will be lost, and we forget about that. I mean, statistics—you know what statistics are. People just—the numbers go over your heard. But they’re real people, Senator Lautenberg. I mean, all that you’ve done, all that this Committee’s done, all that this settlement has done, we save lives.

The other thing is the saving in the money. What I don’t understand—and, you know, you talked about polio—or was it you or—what if we had the polio vaccine, and we had a lot of folks that are infected with polio virus, and we had it here, and we said, “You know, we’re going to put all this money into a trust fund, and we’re going to wait a few years before we innoculate folks.” Well, what would be the result? People would die from polio, right? Or they would suffer illness, disability from polio. It’s the same very thing. The longer you wait to apply the serum to this problem, the more people who are going to be addicted, the more people who are going to have lung cancer and heart disease and the like.

It is just unfathomable to me that we’re waiting to use the funds, when we know exactly what works to solve the problem, but we’re not doing it. And then our excuses are so weak, “Well, we need to spend money in another area.” That’s so weak, when we’re talking about real lives. We’re not talking about somebody getting injured and recovering. We’re talking about somebody starting a behavior that will kill them.

I mean—and the other thing I’ll mention to you—boy, times have changed. When we began this lawsuit, you know, we were telling—the tobacco companies were still lying, they were testifying before Congress in March 1994 that, “No, nicotine is not an addictive drug,” and, “No, it doesn’t cause cancer, and we certainly don’t market and advertise to children.” That was in March 1994. Every day, you turn on the TV, and there’s Philip Morris with their little, you know, message, “Cigarette smoking causes cancer, cigarette smoking is addictive.” I mean, of course, they’re doing that for a reason, and the reason is because they’ve got lawsuits pending and they want to, you know, invade the populace out there and maybe even infect the jury pool. I’d do the same thing. But——

So the tobacco companies are saying it. I mean, Philip Morris is saying, “This will kill you if you do it.” We’ve got $246 billion out here to impact the problem. And are we doing it? No, we’re not. I mean, even—it's not just the Matt Myers of the world telling us that it's bad for you, it's now the tobacco companies who are saying, "This will kill you." And, in America, what we're saying is, "We don't care."

Senator LAUTENBERG. Yes, it's an obtuse kind of thing, because it gets their name out there. They look like good citizens, but they know that those people who are hooked, they are staying hooked, and the more they stay hooked, the more the cash register rings, and that's the ultimate mission. It's like saying, you know, "If you speed, get up to crazy speeds, it can kill you." Does that stop people from speeding? I don't think anybody who is making the decision says, "You know what? If I do this, it could kill me."

Mr. MYERS. That's why youth prevention programs are so critical. The way to stop this problem is to get them before they start. If we do that, we can save a generation of American children from dying.

Senator LAUTENBERG. If the members of the board of these companies, or the executives of the companies, were wearing a white, kind of, dress with a turban, we'd have the FBI and the DEA and the Marine Corps and everybody else in there, "They're out to kill 400,000 Americans? What is going on here?" The rest is in your imagination, which——

Mr. MYERS. Senator, you asked an economic question, though, and we do have data. You know, we know several things. We know that the programs in Florida—in Massachusetts, in California, saved between two and three dollars in healthcare costs for every single dollar they spent. That's an enormous savings to our country. We can calculate the reduction in healthcare costs from a reduction in smoking in any state. And we have often provided that information to state legislators. What we need to do is get across the immediacy of it. This isn't a long-term problem. We have to stop our kids from starting today.

Dr. HEALTON. I'd like to embellish that a little bit. That report that Matt is talking about is a report that was produced by the Legacy Foundation and co-branded with many leading public-health groups, including Tobacco-Free Kids. It did a state-by-state analysis of the additional Medicaid revenues that would accrue for a 25 percent and a 50 percent decline in smoking within the 50 states. And it demonstrated the advantages. It excluded adolescents and kids and newborns, and we are now producing another report that will be out shortly that very compellingly makes the case that Medicaid savings accrue very, very rapidly, because approximately one in ten babies in NICUs are there because of tobacco-related—low birth weight or other tobacco-related complications, not to count the thousands upon thousands of asthma incidents, asthma attacks, otitis media, surgeries, and bed days related to that problem. And the one in four fire deaths—one in four of all fire deaths in the United States are caused by tobacco. The medical care costs associated with that are enormous. Controlling smoking in the home can take a huge bite out of that. You don't hear a lot about it.

And I want to just mention one more thing, for the record. The Philip Morris ad campaign does not say the product will kill you.

And I've pointed that out to Steve Parrish, that that's one item that is not mentioned in any of their ads.

General MOORE. They do say it causes cancer.

Dr. HEALTON. That's right.

The CHAIRMAN. Senator Nelson?

Senator NELSON. Mr. Chairman, there have been a lot of accolades coming your way. I want to add to that, because the multi-state agreement had placed some limits on tobacco product advertising and marketing, but it didn't go far, as far as your bill. And so what we're left with is that the multi-state agreement does not restrict print advertising, it does not restrict Internet advertising, or marketing and advertising inside of retail stores, it does not include any provisions limiting youth access to tobacco products, nor does it provide for the enforcement of Federal and state minimum-age-of-sale laws, and if fails to address the FDA regulation of tobacco products, indoor smoking restriction, and smoking cessation.

Now, I'm curious, Dr. Healton, tell me—the agreement was to restrict advertising on television, but there seems to be a lot of advertising of tobacco products going on in movies these days. Now, it's one thing, under freedom of speech, to accurately portray whoever the actor or actress is portraying and whatever brand of cigarette, but it's another thing if the cigarette companies are paying for the placement of that. Your organization recently did a study on this. Would you share with us your conclusions?

Dr. HEALTON. Yes. I would start by saying that we are not in a position, though I think the attorneys general are, to prove whether or not money exchanged hands or any form of a quid pro quo exists, both of which would be a violation of the MSA agreement and possibly also of the FTC reporting requirements, because they are indicating that such exchanges are not occurring.

The findings in the study were highly provocative. What we did is, we looked at the prevalence of smoking in R, PG–13, PG, and G movies, and we found proportional declines in the presence of smoking across each of the ratings, such that it looks as if there's a quota for how much smoking. But, more importantly, and the area that I think needs serious evaluation is the ads for the movies that are 30- and 60-second spots that are televised and that are highly salient to adolescents. I have two adolescents and one 22-year-old. They look up when a movie ad starts, because it's the coming attraction.

A very substantial proportion of those 30- and 60-second spots have a smoking scene in them. In the typical movie, only about 2 to 4 minutes include smoking if it has smoking in the movie. So it's, first of all, statistically bizarre that so many of these televised commercials include smoking. But what's more important and what I think may, in fact, be a "smoking gun" is that if there is a brand appearing in a movie, the probability that there will be smoking in the televised ad is fourfold.

Senator NELSON. Very interesting. But you, at this point, do not have any proof of the actual exchange of remuneration in return for that, in effect, cigarette advertising in the movie promotion.

Dr. HEALTON. Right, because obviously I'm not in the position of doing that type of research. But, of course—because that's a legal matter, in my view. However, you, of course, know that for many years that practice was legal and did occur. And the tobacco documents, which, thanks to the work of attorneys general like Mike Moore, have become available, and the endowment that the Legacy Foundation gave to UCSan Francisco to make those forever available to scholars, has unearthed a very large number of communications related to product placement practices, and I think that they begin to lay out the roadmap, as do documents that are provided to the FTC on an annual basis, what the companies themselves represent. We've been in a dialogue with the FTC about that information, and we do have some information available to us.

But, again, what I find most curious is that there's a steady increase in the amount of smoking that is occurring, there's a steady increase in the amount of smoking on television. I mean, I'll be perfectly frank, the new show where Whoopi Goldberg appears, who's an actress whose talents, I think, are enormous, she is holding a pack of Marlboros in every show. Maybe it's a coincidence. Maybe she just decided to smoke Marlboros on an NBC show. But I think it's pretty extraordinary, and that's, by no means, the only example.

A few years ago, a movie came out called "The Smokers," and it's about a gang of five adolescent girls, who literally had a cigarette in their hand for the entire duration of the film. It was shown on HBO over and over and over again over the last 2 years. So there's definitely something going on. The question is, what is it? And I know that the AGs are looking into it. A coalition of 26 of them have begun a dialogue with Jack Valenti, which isn't a moment too soon, in my view.

Senator NELSON. Do you think the FTC is an appropriate agency to further look into this?

Dr. HEALTON. Well, I think they are. They look into it every year, when they ask some very specific questions. And I would point out, as I think Mike Moore probably knows, after the settlement, the nature of the questions that the FTC asked of the industry tightened up considerably, such that it covers a broader range of activities, including a wink on the golf course. So I think it's fairly interesting, and they would certainly be one venue. But I don't think they're the only one. I think that there was—there was very strong language in the Master Settlement Agreement, and I'm—as I often say, one of my favorite movies involved cutting out all the kisses, and it was a, you know, terrific European film in which, at the end, the young man looks at all the kisses that the town priests had removed.

I am a great defender of the First Amendment. I don't think this has anything to do with the First Amendment. I think it has to do with maintaining market share in some fashion. Now, I'm speculating, and maybe it's inappropriate to do so, but I think it deserves serious consideration, particularly given the most recent study in *The Lancet* that, very convincingly—and it's my understanding Jack Valenti actually agreed that the science was clear and did not debate the science—that 50 percent of adolescent uptake of smoking is related to the depictions of smoking in film.

Senator NELSON. General Moore and Mr. Myers, you all are familiar with the agreement, and certainly the settlements in your state. Was it clearly your intent that paid advertising for cigarettes be banned from television advertising?

Mr. MYERS. Actually, that was done by Congress, in 1969. The Master Settlement Agreement addressed the issue of paid advertising for product placement in movies, and explicitly banned it. If it were happening, the state attorney generals would have an opportunity to take strong—and I would hope would, in fact, take very strong and quick action. Finding it is the key.

Senator NELSON. And so if you found such evidence, General Moore, of payment in return for product placement in a movie or in a promotional for a movie, what would be the response of the attorney general of Mississippi?

General MOORE. We are in a dialogue right now with the motion-picture industry. I'm not going to prejudge it, but I'm not sure that it's going to bear fruit. There's supposed to be a meeting very soon with Jack Valenti to begin a discussion about how and what is going on. Of course, they think that they should have the freedom to do this. The thing that they cannot do is to pay money, such as the Brown & Williamson documents revealed, that Sylvester Stallone, for example, was paid by Brown & Williamson to—you know, on one occasion, a half a million dollars to smoke their brands in his particular movies. That's what they're prohibited from doing.

We've got some ramifications from the settlement that we can take on in fines, penalties, and I think you would see AG's file litigation against the industry if we found them doing that. It's absolutely a direct violation of the agreement, but it—to me, it's also even more egregious than that. If we catch them doing that, then there'll be a whole new series of litigation that we won't settle until the very end.

I think Dr. Healton mentioned something that's worth saying, that 50 percent of the folks who begin smoking are impressed by the smoking in the movies. When that move, the "Titanic" came out and, you know, the cute young fellow on the front of the boat was smoking a cigarette the whole time, that did more to set us back on teen smoking than just about anything that could happen, because Leonardo Di Caprio was up there, and all the little girls were, you know, saying, "Oh, I want to be—you know, be like him," or, you know, whatever it might be. It's just such an image, it's hard for us to impact that.

And then this idea that they don't advertise, Matt's right, they got rid of advertising on TV, promoting the brands, but every day you can see, whether it's Philip Morris or somebody else, telling us how good they are to us, you know, "We're also Kraft Foods, and we give to the poor, and we donate money to domestic violence, and we do this, and we do that." They spend more on building themselves up in the minds of the public than they do on the prevention programs that they ask for so much acclaim for. So I——

And then a group comes in my office every single day—it might be the 4–H Clubs or the Boy Scouts or whoever it might be, and they're telling me that, "Well, do you think we ought to take this money from Philip Morris? They're going to give us some money, several million dollars, to do so and so." And I said, "What do you have to do for it?" "Well, they want us to—they say really nothing," but really what they want is, they want to be able to advertise that the Boy Scouts of America or the 4–H Clubs of America have been endorsed and supported by Philip Morris Tobacco Company.

Again, that hurts us in our effort to demonize them, as you will, so that people don't take up smoking. So it's hard, it's very hard. We've got a little bitty small message going out there that says, "Don't smoke," and they have a humongous message that's really overpowering us, saying, "Do smoke."

And that's why this whole hearing is important, Senator McCain. It's an unfair fight. I mean, it's still an unfair fight. We thought we had leveled the playing table, but it—their spending has increased and increased and increased, and the state spending has been diminished and diminished and diminished. And, you know, but for Legacy's loud message nationwide in a few spots around the country, there's not another message that says, "Don't smoke."

There are no prevention programs in schools anymore, like there used to be. You remember the days of the drug and alcohol abuse programs? If you look around this country, those programs have slowly gone away, too. So there are very few programs left that tell our kids, at a very early age, to stay away from this product.

So I'm extremely concerned that—in 1997 we had a peak in teen smoking, and we've gone down, and we're headed that way. I'm afraid that it may go back up if the loud message continues.

Mr. MYERS. That's a very important message. There is good news. We have seen youth smoking rates decrease every year since 1997. The question is, what would have happened had the states spent the money properly? And the best available data says they would have dropped by twice that rate.

And then the second question is, Now that we know actually how to impact these things, will we put our political will behind the scientific knowledge we have? We do have the opportunity, in the next 10 years, if we spend the money wisely, literally to decrease the number of kids in this country who become addicted to tobacco to a very small number, and it's solely a matter of political will.

The CHAIRMAN. Dr. Healton wanted to comment.

Dr. HEALTON. I just wanted to add two comments. One, that the last time I looked at it, which was about 2 years ago, Kraft spends about a billion, with the networks and magazines alone, and I'm certain also spends a considerable amount in product placement in film for Kraft products. And I believe the same, in a letter that I just looked at that R.J. Reynolds penned to their product placement firm. They, too, at least at that time, had Lifesavers and Planters as two products that they were having placed. And there was significant discussion in that letter, which I can make available to you, about where they were able to get products appearing in film.

So I think it's a very complicated web of relationships that one would have to look at. And as the final note, my understanding of the MSA language—and I may have it wrong, but I was at a meeting with the attorneys general preparing for the meeting with Jack Valenti—I believe that it isn't just paid product placement that would be literally a check in exchange for a placement. I think any form of quid pro quo also is implied in that.

The CHAIRMAN. I want to thank——

Please, Mr. Scheppach.

Mr. SCHEPPACH. Just one comment, Mr. Chairman. We seem to be saying that all the decrease in smoking is due to cessation programs. I think we underplay the fact that we're in a market economy, and actually the Master Agreement did raise the price of cigarettes quite considerably. And, second of all, I think the tax increases that states have just done are important, and I suspect some of that, in that there is probably some interaction between raising of prices and cessation programs. So I think the evidence is that at least that group of children that we're trying to hit, the young teens, are fairly responsive to the tax increases.

So I don't think it is a one-way street.

The CHAIRMAN. And I assume that the states that raised taxes did it because they said, "Gee, we'd like to stop kids from smoking, so we'll raise these taxes."

Mr. SCHEPPACH. Oh, I think it was both, Mr. Chairman.

The CHAIRMAN. I don't think so.

Ms. Hudson, you've been strangely unpummeled here.

[Laughter.]

The CHAIRMAN. I would like to allow you to speak, but I would also like, before you do, to say that I think you should be proud of what Delaware has done, but you are here representing, as I understand it, the National Conference of State Legislatures. I don't think you can be proud of what the state legislatures have done. Please go ahead.

Ms. HUDSON. I am not. And that's what I wanted to say. It makes me feel very awkward here. But what I think is important is that legislators realize what we did today was discuss with you our successes and our failures, and they need to know your frustration and disappointment with the states that are not spending the money on tobacco cessation and health-related issues.

And I will recommend to the National Conference of State Legislatures that they have sessions on this at their conferences and they put something, a really good article, in their magazines to let legislators know that they really are wrong, and perhaps we need to step up our language with them and let them know just how serious we are.

The CHAIRMAN. Thank you. I hope they would invite our witnesses, all of them, including Mr. Scheppach, to these deliberations so that they can hear all sides of this issue.

We try very hard in these hearings, despite the bias that I may bring to it, to allow the other side to be heard. And, Mr. Scheppach, I think you have earned your considerable salary this morning at this——

[Laughter.]

The CHAIRMAN.—at this hearing.

Mr. SCHEPPACH. You've never seen it, Senator, so——

[Laughter.]

The CHAIRMAN. I do thank you for appearing this morning, and I mean that, on behalf of the National Governors Association.

Attorney General Moore, it's always a pleasure to see you again. Mr. Myers, thank you for your dedicated efforts. Ms. Hudson, thank you for being here. And, Dr. Healton, I hope we can do something to keep your program alive, and I'll work with others in trying to see that that happens.

I thank you all, and this hearing is adjourned.

[Whereupon, at 11:25 a.m., the hearing was adjourned.]

A P P E N D I X

PREPARED STATEMENT OF JOHN R. SEFFRIN, PH.D., CHIEF EXECUTIVE OFFICER, AMERICAN CANCER SOCIETY

On behalf of the millions of volunteers and supporters of the America Cancer Society, I thank you, Mr. Chairman, and your Committee colleagues for the opportunity to submit testify on the fifth anniversary of the multi-state agreement, the Master Settlement (MSA), with the tobacco companies.

Tobacco is highly addictive and causes more than 440,000 deaths each year in the United States, including approximately 150,000 cancer deaths. Put another way, we know that one out of every three cancer deaths in this country is caused by tobacco use. That is an unacceptable fact.

Shortsighted states with budget crises and other priorities have frustrated the heroic efforts of tobacco advocates to get states to commit substantial funds for comprehensive tobacco prevention and cessation programs. Out of $11.6 billion the states received in Fiscal Year 2003, states spent only $682.3 million on tobacco prevention and cessation. Over the past year, funding levels have fallen even further and successful programs in states like Oregon, Florida, Massachusetts, and California have suffered major cuts.

The American Cancer Society has long been at the forefront of efforts to educate the public about the dangers of smoking and to advocate on behalf of policies, including regulation, to reduce disease, suffering, and death caused by tobacco use.

It is impossible to evaluate the success or failure of the 1998 Master Settlement Agreement without awareness that the MSA was the aftermath of the failed effort by the state attorneys general to bring about broad comprehensive public health change through the settlement of their lawsuits against the tobacco companies in June 1997. That settlement led to the comprehensive national tobacco control bill proposed by Senator John McCain, as the chairman of the Senate Commerce Committee.

The McCain bill, launched by a 19–1 vote of the Senate Commerce Committee, proposed landmark tobacco control goals far beyond the reach of the MSA. However, a combination of tobacco industry opposition and a splintered public health community resulted in the bill's demise. While the tobacco companies fiercely opposed the McCain bill, so did many tobacco control advocates, but not because of its public health provisions, which addressed almost every policy objective dreamed of by tobacco control advocates over the past 30 years. They opposed the McCain bill because it set a "cap" at $8 billion on the amount of product liability damages the cigarette companies could be forced to pay out in a single year. This concession to the tobacco companies would protect them against a possibility some advocates considered highly likely—that, as Dr. Stanton P. Glantz, a leading opponent, predicted, "given patience and hard work, the tobacco industry will lose enough of these cases to be brought to their knees."

The tobacco companies and their supporters in the Senate greeted the public health community's opposition as a welcome opportunity to delay the bill's passage. By the time the Senate was prepared to vote on the McCain bill, the *New York Times* reported that the eight-week national advertising blitz the tobacco industry launched in the interim "has been remarkably successful in turning what tobacco opponents view as a bill that would discourage teenage smoking into a tax issue and an assault on working stiffs who cannot afford to pay more for cigarettes."

Even so, the bill came within just three votes of the 60 needed to override a tobacco industry-spawned filibuster on the Senate floor. But those three missing votes were enough. Few observers of the White House and the Congress believe we shall soon again, if ever, see a serious piece of legislation with the same potential for saving lives as the McCain bill embodied.

Innovative lawsuits against the tobacco companies brought by state attorneys general led by Mike Moore of Mississippi, Christine Gregoire of Washington, and Hubert Humphrey III of Minnesota, had forced the companies to agree to the June 1997 settlement that laid the foundations for the McCain bill. The bill's death, the failure of the public health community to support the state attorneys general initial settlement efforts, and independent settlements by four states that changed the situation dramatically for all the state attorneys general. Some feared losing at trial. Others remained deeply concerned about the public health impact of their cases. But the vast majority cared only about the amount of money they could bring home to their state. Now the state attorneys general, not the tobacco industry, felt the pressure to settle.

With this shift in leverage, it was not surprising that what emerged from the 1998 Master Settlement Agreement negotiations bore no resemblance to the scope of the 1997 settlement or to the McCain legislation. Public health advocates were united in their concern about its flaws and limited scope. Even the attorneys general who negotiated the MSA were quick to acknowledge that it accomplished far less than the changes proposed only a year earlier, although they still argued that it would bring about meaningful progress.

It is in this setting that we should view the MSA and the efforts of tobacco control advocates to make the most of the settlement. What was lost when the McCain bill died? Has the MSA lived up to its promise of change?

The core of the MSA focused on marketing restrictions on the tobacco industry, funding for the states, and the creation of the independent American Legacy Foundation. The agreement's stated goals were to curtail marketing to children, to provide the funds necessary for sustained comprehensive tobacco prevention and cessation efforts, and to better address the health problems caused by tobacco. It also funded a long-term national public education campaign through the American Legacy Foundation.

Comparing the MSA to the 1997 settlement and the McCain legislation exposes startling contrasts. For example, the McCain bill contained comprehensive restrictions on tobacco marketing that would have sharply curtailed the tobacco industry's ability to reach kids. Since the industry has easily thwarted the MSA's limited restrictions in this area, despite the enforcement efforts of the state attorneys general.

True, cigarette billboards have disappeared, along with promotional materials like t-shirts and caps with company logos. But the tobacco industry's marketing expenditures have increased each year since the MSA and the results continue to bombard our children.

Through a penalty scheme that few tobacco control advocates had dared dream of, the McCain bill held the tobacco companies responsible if youth tobacco use did not fall dramatically: penalties up to $2 billion annually if the companies failed to reduce youth smoking by 30 percent in five years; 60 percent in ten years. The MSA contained no such provision.

The McCain bill and the 1997 settlement specifically earmarked more than $2.5 billion every year for tobacco prevention and cessation-on top of revenue from the uncommitted funds each state was to receive. Unfortunately, states' budget crises and other priorities have frustrated the heroic efforts of tobacco advocates to get states to commit substantial funds to comprehensive tobacco prevention and cessation programs.

The earlier provisions also proposed permanent funding for public education about tobacco prevention and cessation without restrictions as to its content. By contrast, the MSA's funding of the American Legacy Foundation prohibits the Foundation from "vilifying" tobacco companies. Further, the MSA guarantees funding for the Foundation's public education for only five years. As a result, funding for the Legacy's education campaign is about to end and the Foundation faces continuing attacks by the tobacco companies.

Most important, the McCain bill granted the U.S. Food and Drug Administration broad power to regulate every aspect of tobacco product manufacturing, distribution, and marketing. It authorized a Federal agency, for the first time, to regulate the tobacco product itself; it forced the tobacco companies to disclose the ingredients in tobacco products and what they knew about the products. Five years later, regulation of tobacco remains an unmet priority.

Another advantage of the 1997 settlement and the McCain bill was the ability to impose additional costs on all tobacco manufacturers. The MSA applied only to the specified defendants. The upshot? Other manufacturers can sell cigarettes at far lower prices. Some adult smokers who might have quit because of the increased cost can still buy low-priced cigarettes. This very likely has reduced the impact of our efforts on both youth starting to smoke and adult consumption.

The 1997 settlement would have provided funding to charities to replace the dollars they would have received from the cigarette companies, so that worthy causes would no longer be forced to choose between their desperate need for funds and their integrity. But the failure of the 1997 settlement and the McCain bill left open a critical window of opportunity for the tobacco companies to resurrect their reputations through a big-budget propaganda campaign, focused on their philanthropy and new-found acknowledgement of tobacco's risks. At the same time, they continue to buy the silence of many worthy causes that must now rely indefinitely on tobacco money.

From the beginning, the MSA was a missed opportunity to make historic change; it is not surprising that, five years later, its achievements pale compared to the promise of the 1997 settlement and the McCain bill. To date, the MSA has not lived up even to the limited advances it promised.

The tobacco control movement has nevertheless made significant progress in the last five years. And that progress has come from the remarkable level of effective advocacy and action from a movement that picked itself up and fought on heroically. We have made huge strides in raising tobacco excise taxes, expanding clean indoor air protection, and—yes, even in bleak times increasing funds for tobacco prevention and control programs. And we have proven to the world that comprehensive programs work.

A significant number of states funded their programs substantially and these states have achieved powerful results. As one inspiring illustration, Indiana, a state notably lackluster in its tobacco control until the MSA settlement. Tobacco control advocates in Indiana—a notoriously fiscally conservative state—persuaded the state legislature to allocate $32.5 million to tobacco control for Fiscal Year 2002 and 2003. Under the direction of veteran tobacco control leader Karla Sneegas, Indiana launched a comprehensive, state-of-the-art tobacco control program. By the fall of 2002, when the program conducted the state's first adult tobacco survey, 193,000 Indiana adults had quit smoking. Overall cigarette consumption had fallen 18 percent.

And Maine, with ample funding, has gone from the state with the highest teen smoking rate to one of the lowest. Maine has cut smoking among kids literally in half.

Finally, we need to give the MSA credit for two signal achievements. First, it changed the debate about what adequate spending is for tobacco control. With the MSA and the publication of Center for Disease Control and Prevention's Best Practices, even half hearted state legislators now acknowledge that meaningful comprehensive tobacco prevention costs more than they assumed-much more.

The high cost and lack of access to effective smoking cessation therapies are among the biggest obstacles to achieving the Nation's *Healthy People 2010* goal of reducing smoking rates from 23 percent today to 12 percent by 2010.

In August 2002, Health and Human Services Secretary Tommy Thompson created a Subcommittee on Cessation of the Interagency Committee on Smoking and Health. He appointed 16 tobacco policy experts as committee members. The Subcommittee was charged with developing a series of broad-based recommendations to substantially increase tobacco cessation in the United States. He asked the Subcommittee to look at action steps that could be employed by the Federal Government as well as the private sector to reduce the number of people who smoke. I was privileged to serve as a member ofthe Subcommittee.

The Subcommittee considered the existing body of scientific evidence regarding effective tobacco dependence strategies and policies. Numerous effective treatments exist today to treat tobacco dependence. These treatments can double, triple or even quadruple the likelihood that a smoker will be able to quit. There are also proactive policies that are being employed to assist smokers in their efforts to quit such as, telephone quitlines, paid media campaigns, cigarettes excise tax increases, and reducing out of pocket costs for cessation treatment.

The report entitled *Preventing Three Million Premature Deaths, Helping Five Million Smokers Quit: A National Action Plan for Tobacco Cessation,* was submitted to the Interagency Committee on Smoking and Health for its approval. The full Committee voted unanimously to accept the recommendations and to transmit the report in its entirety to the Secretary. The success of our efforts was due in large part to the tremendous work of many organizations and individuals who attended the public hearings, submitted comments, and provided visibility for the Committee's activity.

I want to highlight just two of the ten recommendations.

The Subcommittee's first recommendation was to establish a federally-funded National Quitline network by 2005 that will provide universal access to evidence-based counseling and medications for tobacco cessation. This quitline would work with existing state or regionally managed quitlines. Research has shown that quitlines are a very effective tool in assisting smokers to quit. To date thirty-four states provide some level of quitline service.

The American Cancer Society provides Quitline services through our call center in Austin, Texas. The center receives approximately 12,000 calls per year from people of all walks of life with one thing in common—they recognize that they need help to quit smoking. The trained counselors who answer the quitline work with the callers to set a quit date and provide them with materials and other support to help them in their efforts. It is important to remember that tobacco is addictive. Therefore, the most successful cessation strategies and policies combine counseling with FDA-approved pharmacotherapies. Studies have shown that the combination of counseling and drugs substantially increases the likelihood that a smoker will quit.

The second recommendation of the Subcommittee was to increase awareness by launching an ongoing, extensive paid media campaign by Fiscal Year 2005 to help Americans quit using tobacco products.

The American Legacy Foundation's truth® campaign has been a success, supported by rigorous evaluation. The Foundation has shown that an aggressive, well-executed, well funded public education campaign can make a difference at the national level, and it has helped drive down youth tobacco-use rates. Whether or not the Foundation gains new financing, its experience gives us a powerful argument for future major national investment in tobacco control.

This otherwise dismal history offers lessons to us all. Perhaps the most painful, in the words of the ancient Taoist poet Lao-Tzu, is "that we know, but never learn." Windows of opportunity can slam shut; the passion for the perfect can sabotage the attainable near perfect.

But there are affirming lessons, too: A civic movement deeply grounded in a passionate vision for a future free of preventable misery and death can recover from internal dissension and setbacks, renew its pursuit of the common good, and continue to march toward that vision.

SUBMISSION FOR THE RECORD

This article can be found in Journal of Health Economics 22 (2003) 843–859 and online at *www.sciencedirect.com*

THE IMPACT OF TOBACCO CONTROL PROGRAM EXPENDITURES ON AGGREGATE CIGARETTE SALES: 1981–2000

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PREPARED STATEMENT OF SHEILA M. ROSS, WASHINGTON REPRESENTATIVE, ALLIANCE FOR LUNG CANCER ADVOCACY, SUPPORT AND EDUCATION (ALCASE)

Mr. Chairman:

The Alliance for Lung Cancer Advocacy, Support and Education appreciates this opportunity to make a statement for the record on the hearing you are holding today on how the 46 states that were parties to the 1998 Master Settlement Agreement (MSA) with the Nation's five largest tobacco companies are allocating their settlement revenues since the signing of the MSA.

We thank you, Mr. Chairman, and commend you for holding this hearing.

ALCASE was founded in 1995 to help lung cancer patients and their families, to educate the public and to advocate for a change in public health policy on lung cancer. It is the only national organization dedicated to those goals. I present this testimony on behalf of ALCASE, as a survivor of two bouts of lung cancer and as a former Hill staffer for nearly 20 years.

The MSA was negotiated with, to best of our knowledge, no input from those most affected by tobacco: lung cancer patients and their caregivers and families. Indeed, we cannot ascertain that even a single dollar of the $213 billion settlement has gone to lung cancer research.

The primary reason is this: The mortality rate of lung cancer is so high that not enough people remain alive long enough to establish a grass roots organization with sufficient political clout to demand more attention and funding.

Lung cancer kills more people each year than breast, prostate and colon cancers combined. Yet it receives a miniscule amount of Federal research funding and that inequity is reflected in the statistics. Since the passage of the Cancer Act of 1971 the five year survival rate for breast cancer has risen to 88 percent and for prostate cancer to 97 percent. Thirty years ago the 5 year survival rate for lung cancer was

12 percent. Today it is 15 percent. The cancers with the highest survival rates and the largest advocacy groups consistently receive the most funding, up to ten times as much per death as lung cancer.

In a recent study, even the National Cancer Institute conceded that lung cancer is being funded far below its public health impact. (Progress Review Report on Lung Cancer, August 2001.)

At the state level, lung cancer research lost out again when the MSA funds were allocated, again for lack of political support. Ironically the pay outs to the states are predicated on prospective tobacco sales. Followed to its logical conclusion, unless states want to reduce their anticipated, and in many cases already appropriated revenues, it is in their interest that cigarette sales be at least maintained.

In this surreal world of the MSA settlement, the states did set aside or earmark hundreds of millions of dollars for tobacco cessation programs. So much money was spent so fast that many of these programs have been of dubious success. The sheer number of these programs has also unfortunately served to stigmatize lung cancer as a life style choice rather a disease, which stimatization, in turn, has become a convenient fig leaf to hide the addiction of the state legislatures to tobacco money.

The fact is, Mr. Chairman, that over 60 percent of new lung cancers are being found in former smokers, people who quit smoking, many of them years ago, or in people who have never smoked. U.S. women have the highest lung cancer mortality in the world. Since 1988 more women in the United States have been dying each year from lung cancer than breast cancer and the number is increasing so rapidly that by 2006 lung cancer deaths among women will be double that of breast cancer. People are not being told these statistics.

The sad truth is that by the time symptoms, such as a cough, occur, it is already too late. The only hope is to find it early and treat it early. Finally we can do that Advances in spiral CT and computer assisted diagnostic technology can detect small nodules in the lungs even before they become cancerous.

We must research these nodules and early disease management now. We must leap at this opportunity to finally make a dent in lung cancer mortality. 438 people are dying from lung cancer every day in the United States. We cannot allow this to continue. These facts cannot be covered up any longer.

We recognize, Mr. Chairman, that the Federal Government cannot dictate to the states how they should allocate their revenues. However, with the Federal suit against big tobacco still in utero in the Department of Justice, and with this opportunity for a breakthrough on lung cancer finally at hand, the Federal government can suggest and encourage the states to put some of the MSA money into lung cancer research and treatment.

And hopefully, Mr. Chairman, in the FY 05 budget, the Federal government will do its part by directing money and a mandate to its agencies to turn these promising breakthroughs in to better outcomes with dispatch and urgency.

Please speak for us, Mr. Chairman. We need your voice.

AMERICAN LEGACY FOUNDATION
November 14, 2003

Hon. JOHN MCCAIN,
Chairman,
U.S. Senate Committee on Commerce, Science, and Transportation,
Washington, DC.

Dear Senator McCain:

It was an honor to have the opportunity to testify before the Senate Commerce Committee on November 12 and to share the American Legacy Foundation 's insights on States' use of Tobacco Master Settlement Agreement Funds. I wish to thank you again for your leadership in holding this hearing. After the hearing, several Senators requested detailed information about Legacy's funding situation and the threat it poses to the continuation of our **truth**® youth counter marketing campaign. We are pleased to provide you with the information below.

As I stated during my testimony, Legacy has become the *de facto* safety net at the national level for youth tobacco prevention programs. In most states, **truth**® television ads are the only tobacco prevention messages that young people see.

Legacy is facing an alarming funding cliff as a result of a sunset clause in the MSA. Legacy received what it believes will be its last major payment of approximately $300 million from participating cigarette manufacturers pursuant to the MSA in April of this year. While Legacy has prepared for this "rainy day," the sharp decline in funding means that we will be forced to sharply reduce, if not eliminate, many of our programs. Although Legacy will do all it can to preserve **truth**®, the fact is that an effective national counter marketing campaign cannot be staged with less than $40–60 million for media placement.

It is worth noting that the youth market is among the most expensive segments to buy. It is also a significant consideration that this $40–60 million figure does not include the cost of cultural immersion and study required for creative development, which is the heart of **truth**®. Nor does it include our aggressive and innovative grass roots and web based outreach efforts. Today, these efforts are combined with state based youth empowerment grants and all of this work is the subject of the unprecedented evaluation of the campaign's impact on youth smoking. These non-media efforts, again at a minimum, would cost an additional $30–40 million.

To put this into context, Legacy is already on a glide path to a greatly reduced overall operating budget, which is reflected on the attached funding cliff. By 2008, we expect our *overall* operating budget to be $30–$35 million in *today's* dollars. Consequently, even if Legacy were to shut down every other program, **truth**® as we know it would ultimately be silenced.

Youth smoking rates are at their lowest level in 28 years. Evidence suggests that **truth**® is responsible for a very substantial proportion of that decline. Included with this letter is an MMWR report from the Centers for Disease Control that was released today. It provides some of the most recent data on youth smoking rates, as well as an analysis of **truth®'s** contribution to those declines.

What is most alarming is that the loss of **truth**® is coming at a time when States, for whatever reason, have backed away from their commitments to fund comprehensive tobacco control pro rams, including youth prevention. We know that 90 percent of smokers . start before their 19th birthday. It is estimated that the steady decline in youth smoking since 1997 has prevented over 2 million teenagers from becoming adult smokers and thus saved a minimum of 700,000 lives. Thus, if we can continue to inoculate young people with a dose of **truth**®, millions of lives will be saved in the long term.

Senator McCain, I commend you again for holding the hearing and thank you for allowing me to testify. Should you or your staff require any additional information about the American Legacy Foundation or our **truth**® counter marketing campaign, please do not hesitate to contact me at (202) 454–5547.

Sincerely,

CHERYL G. HEALTON, DR.P.H.
President and CEO.

enclosures

TOBACCO USE AMONG MIDDLE AND HIGH SCHOOL STUDENTS—UNITED STATES, 2002

Each day in the United States, approximately 4,400 youths aged 12–17 years try their first cigarette (*1).* An estimated one third of these young smokers are expected to die from a smoking-related disease(£). The National Youth Tobacco Survey (NYTS), conducted by the American Legacy Foundation, provides estimates of usage among U.S. middle and high school students for various tobacco products (*i.e.,* cigarettes, cigars, smokeless tobacco, pipes, bidis [leaf wrapped, flavored cigarettes from India], and kreteks [clove cigarettes]). This report summarizes tobacco use prevalence estimates from the 2002 NYTS and describes changes in prevalence since 2000. Both tobacco use and cigarette smoking among students in high school (*i.e.,* grades 9–12) decreased by approximately 18 percent during 2000–2002; however, a decrease among students in middle school (*i.e.,* grades 6–8) was not statistically significant. The lack of progress among middle school students suggests that health officials should improve implementation of proven antismoking strategies and develop new strategies to promote continued declines in youth smoking.

Sampling frames for the 2002 NYTS were stratified by U.S. Census Bureau region; black, Hispanic, and Asian students were oversampled. A partial panel design was used (*i.e.,* comprising a newly drawn sample and a sampling of schools that participated in the 2000 NYTS). The sampling frame for the drawn sample consisted of all public and private schools in the United States. A total of94 primary sampling units (PSUs) (*i.e.,* large counties or groups of counties) were selected in the first stage of the sampling, and 215 schools were selected from these PSUs in the second stage of the sampling; 83 additional schools were selected randomly for the panel sample. Of these 298 eligible schools, 246 (83 percent) participated in the 2002 NYTS. Approximately 125 students were then drawn from each school by selecting classes randomly, depending on the average class size of each school, from a required subject area (*e.g.,* English or social studies). Participation was voluntary and anonymous, and school parental permission procedures were followed; students recorded their responses on a computer-scannable sheet.

Among youths attending the 246 participating schools, 26,119 (90 percent) (*i.e.,* 12,581 middle school students and 13,538 high school students) completed the survey, resulting in an overall response of75 percent. Data were weighted to be nationally representative. STATA 7 was used to compute 95 percent confidence intervals for prevalence estimates, which were used to identify differences among populations. Current use of a specific tobacco product was defined as having used that product on at least one occasion during the 30 days preceding the survey. Current use of any tobacco product was defined as having used any of the listed products on at least one occasion during the 30 days preceding the survey.

In 2002, a total of 13.3 percent of middle school students reported current use of any tobacco product (*Table* 1). Cigarettes (10.1 percent) were the most commonly used product, with no statistically significant differences in usage by sex. Cigars (6.0 percent) were the second most commonly used tobacco product, followed by smokeless tobacco (3.7 percent), pipes (3.5 percent), bidis (2.4 percent), and kreteks (2.0 percent). Males were more likely than females to use all tobacco products except for cigarettes. No significant differences were found for any type of tobacco use by race/ethnicity.

Among high school students, 28.4 percent reported current use of any tobacco product (Table 2). Cigarettes (22.9 percent) were the most commonly used product, with no difference by sex; however, white students were more likely to use cigarettes than black, Hispanic, or Asian students. Cigars (11.6 percent) were the second most common tobacco product, followed by smokeless tobacco (6.1 percent), pipes (3.2 percent), kreteks (2.7 percent), and bidis (2.6 percent). Males were more likely than females to use all tobacco products except for cigarettes. Asian students were less likely to use cigars) and white students were more likely to use smokeless tobacco than students in other racial/ethnic groups.

During 2000–2002, current use of any tobacco product among high school students decreased from 34.5 percent to 28.4 percent; cigarette use decreased from 28.0 percent to 22.9 percent, cigar use from 14.8 percent to 11.6 percent, bidi use from 4.1 percent to 2.6 percent, and kretek use from 4.2 percent to 2.7 percent (*Iable* 2). However, no significant change was found among middle school students in the prevalence of tobacco use (Table 1).

Reported by: JA Allen, MA, D Vallone, PhD, ML Haviland, DrPH, C Healton, DrPH, American Legacy Foundation, District of Columbia. KC Davis, MS, MC Farrelly, PhD, Research Triangle Institute, Research Triangle Park, North Carolina. CG Husten, MD, T Pechacek, PhD, Office on Smoking and Health, National Center for Chronic Disease Prevention and Health Promotion, CDC.

Editorial Note

The declines in cigarette smoking and overall tobacco use among high school students reflect downward national trends since 1997 (3,*4*). The declining use of cigars) bidis) and kreteks and the unchanged use of smokeless tobacco and pipes among high school students suggests that students are not substituting other tobacco products for cigarettes and that efforts to reduce cigarette smoking might be reducing use of all tobacco products. However, the lack of any statistically significant decline in tobacco usage among middle school students is cause for concern.

The findings in this report are subject to at least two limitations. First) these data apply only to youth who attended middle school or high school and are not representative of all youths in these age groups. Nationally, approximately 5 percent of youths aged 16–17 years were no longer in school (4). Second, the data were from self-reports of survey participants. Although underreporting of tobacco use by youths has been minimal in previous surveys (5), recent declines in the acceptability of smoking might have led to increased underreporting.

Why middle school and high school students appear to be responding differently to the current antismoking environment is not clear. Factors expected to discourage youth from smoking include increases in cigarette prices (*i.e.,* approximately 88 percent from December 1997 to December 2002) *(6);* implementation of smoke-free laws and policies; restrictions on tobacco advertising; and local, state) and national antitobacco campaigns (*e.g.,* the truth® campaign) (7). However, spending on tobacco industry marketing doubled during 1997–2001 *(8),* and tobacco industry-sponsored media campaigns have been determined to reduce the impact of public health campaigns *(7)*.

The data in this report suggest that further refinements in evidence-based strategies will be needed to decrease tobacco use among middle school students. Efforts might focus on (1) devising more targeted and effective media campaigns, (2) reducing depictions of tobacco use in entertainment media *(9),* (3) instituting campaigns to discourage family and friends from providing cigarettes to youths, (4) promoting smoke-free homes, (5) instituting comprehensive school based programs and policies in conjunction with supportive community activities, and (6) decreasing the number of adult smokers (*e.g.,* parents) to present more nonsmoking role models.

Because tobacco use is the leading cause of preventable death in the United States, efforts to reduce tobacco use must remain a public health priority. Preventing tobacco use among youth is essential to reduce future smoking-related illness and associated costs. However, in 2003, states cut spending for tobacco use prevention and control programs by $86.2 million (11.2 percent) *(10).* For the decline in tobacco use among youth in the United States to continue, such funding must be restored and perhaps expanded.

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Table 1.—Percentage of &tudents in middle school {i.e., grades 6–8) who were current users* of any tobacco product. by product type, sex, and race/ethnicity—National Youth Tobacco Survey, United States, 2002 and 2000

	Any tobacco†		Cigarettes		Cigars		Smokeless tobacco		Pipes		Bidis		Kreteks	
Characteristic	%	(95% CI§)	%	(95% CI)	%	(95% CI)	%	(95% CI)	%	(95% CI)	%	(95% CI)	%	(95% CI)
Middle school, 2002														
Sex														
Male	14.8	(±1.6)	10.2	(±1.3)	7.9	(±1.1)	5.6	(±1.3)	5.1	(±0.8)	3.1	(±0.6)	2.7	(±0.6)
Female	11.8	(±1.4)	10.0	(±1.4)	4.1	(±0.7)	1.8	(±0.4)	1.9	(±0.4)	1.7	(±0.4)	1.1	(±0.3)
Race/Ethnicity														
White	13.3	(±1.9)	10.4	(±1.6)	5.5	(±1.0)	4.0	(±1.1)	2.8	(±0.6)	1.8	(±0.4)	1.5	(±0.4)
Black	13.6	(±2.4)	9.4	(±2.4)	7.3	(±1.7)	2.9	(±1.1)	3.9	(±1.4)	3.1	(±1.0)	2.3	(±0.9)
Hispanic	12.5	(±1.9)	9.1	(±1.6)	6.3	(±1.1)	2.9	(±0.7)	4.4	(±0.9)	2.9	(±0.7)	2.6	(±0.7)
Asian	8.6	(±3.2)	7.4	(±3.2)	4.8	(±2.8)	3.6	(±2.7)	4.4	(±2.7)	2.9	(±2.1)	3.6	(±2.8)
Total	13.3	(±1.4)	10.1	(±1.2)	6.0	(±0.7)	3.7	(±0.8)	3.5	(±0.5)	2.4	(±0.3)	2.0	(±0.3)
Middle school, 2000														
Sex														
Male	17.6	(±2.2)	11.7	(±1.7)	9.7	(±1.5)	5.7	(±1.8)	4.3	(±0.7)	3.4	(±0.6)	2.7	(±0.5)
Female	12.7	(±1.5)	10.2	(±1.3)	4.6	(±0.8)	1.5	(±0.3)	1.8	(±0.4)	1.4	(±0.3)	1.5	(±0.3)
Race/Ethnicity														
White	14.3	(±1.9)	10.8	(±1.6)	6.1	(±1.1)	3.9	(±1.3)	2.7	(±0.5)	1.9	(±0.4)	1.9	(±0.4)
Black	17.5	(±3.0)	11.2	(±2.0)	9.8	(±2.5)	2.4	(±0.7)	2.2	(±0.7)	2.9	(±0.8)	1.7	(±0.5)
Hispanic	16.0	(±2.0)	11.4	(±1.7)	8.8	(±1.4)	2.9	(±0.7)	5.3	(±1.1)	3.6	(±0.9)	2.6	(±0.8)
Asian	7.5	(±2.6)	5.3	(±2.3)	4.1	(±1.9)	1.7	(±1.2)	2.8	(±1.5)	2.9	(±1.7)	2.3	(±1.4)
Total	15.1	(±1.5)	11.0	(±1.2)	7.1	(±1.0)	3.6	(±0.9)	3.0	(±0.4)	2.4	(±0.4)	2.1	(±0.4)

* Used tobacco on at least one occasion during the 30 days preceding the survey.
† Cigarettes. cigars. smokeless tobacco, pipes. bidis (leaf-wrapped, flavored cigarettes from India), or kreteks (clove cigarettes).
§ Confidence interval.

Table 2.—Percentage of students in high school (i.e., grades 9–12) who were current users* of any tobacco product, by product type, sex, and race/ethnicity—National Youth Tobacco Survey, United States, 2002 and 2000

	Any tobacco†		Cigarettes		Cigars		Smokeless tobacco		Pipes		Bidis		Kreteks	
Characteristic	%	(95% CI§)	%	(95% CI)	%	(95% CI)	%	(95% CI)	%	(95% CI)	%	(95% CI)	%	(95% CI)
High school, 2002														
Sex														
Male	32.9	(±2.3)	24.6	(±2.1)	16.9	(±1.4)	10.8	(±2.0)	5.0	(±0.9)	3.7	(±0.8)	3.5	(±0.7)
Female	23.9	(±1.8)	21.2	(±1.8)	6.2	(±0.9)	1.4	(±0.4)	1.4	(±0.4)	1.5	(±0.4)	1.8	(±0.5)
Race/Ethnicity														
White	31.1	(±2.1)	25.5	(±1.8)	11.8	(±1.0)	7.4	(±1.4)	2.8	(±0.6)	2.2	(±0.5)	2.7	(±0.6)
Black	21.8	(±2.9)	14.3	(±2.8)	12.0	(±1.9)	2.3	(±0.8)	3.8	(±1.2)	3.4	(±1.1)	1.9	(±0.8)
Hispanic	24.5	(±2.7)	20.5	(±2.5)	10.8	(±1.5)	3.8	(±1.3)	4.6	(±1.1)	3.5	(±0.9)	3.0	(±0.8)
Asian	15.0	(±3.9)	12.8	(±3.5)	5.4	(±2.3)	2.3	(±1.5)	2.7	(±1.5)	2.9	(±1.7)	2.7	(±0.5)
Total	28.4	(±1.7)	22.9	(±1.6)	11.6	(±0.9)	6.1	(±1.1)	3.2	(±0.6)	2.6	(±0.5)	2.7	(±0.5)
High school, 2000														
Sex														
Male	39.1	(±2.2)	28.8	(±1.9)	22.0	(±1.5)	11.8	(±1.7)	5.2	(±0.7)	5.4	(±0.6)	5.3	(±0.7)
Female	29.8	(±1.9)	27.3	(±2.0)	7.3	(±0.9)	1.4	(±0.4)	1.4	(±0.3)	2.8	(±0.4)	3.0	(±0.5)
Race/Ethnicity														
White	38.0	(±2.3)	31.8	(±2.1)	15.1	(±1.2)	8.2	(±1.2)	3.3	(±0.5)	3.6	(±0.5)	4.5	(±0.6)
Black	26.5	(±3.6)	16.8	(±3.0)	15.3	(±2.9)	2.6	(±0.9)	2.2	(±0.8)	4.9	(±1.0)	2.2	(±0.7)
Hispanic	28.4	(±2.5)	22.6	(±2.4)	13.6	(±1.6)	4.0	(±1.2)	4.2	(±0.9)	5.7	(±1.1)	4.0	(±0.8)
Asian	22.9	(±3.7)	20.6	(±3.5)	7.4	(±2.1)	1.9	(±0.9)	2.5	(±1.1)	3.0	(±1.3)	3.2	(±1.4)
Total	34.5	(±1.9)	28.0	(±1.7)	14.8	(±1.1)	6.6	(±0.9)	3.3	(±0.4)	4.1	(±0.4)	4.2	(±0.5)

* Used tobacco on at least one occasion during the 30 days preceding the survey.
† Cigarettes. cigars. smokeless tobacco, pipes. bidis (leaf-wrapped, flavored cigarettes from India), or kreteks (clove cigarettes).
§ Confidence interval.

Arizona

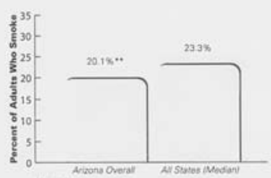
Legacy

State Rankings

- Arizona ranks 27 out of 50 states and the District of Columbia in tobacco-related deaths.
- In 2003, Arizona received $101,600,000 in tobacco settlement revenue.
- During FY03 Arizona spent $18,300,000 on tobacco prevention. That's 65.7% of the CDC Best Practices minimum recommendation of $27,790,000.
- Arizona ranks 11 out of 50 states and the District of Columbia on dollars spent for tobacco prevention.
- Arizona has not securitized all or part of its MSA dollars.

Tobacco Usage

ADULT CIGARETTE USE



**Ranked 46 of 51 states.
Source: Behavioral Risk Factor Surveillance System, 2000

YOUTH TOBACCO USE

Grades 6-8

	Current Cigarette Smoking	Current Any Tobacco Use
National†	10.1%	13.3%
AZ††	11.4%	17.1%
Boys††	10.2%	14.8%
Girls††	10.0%	11.8%

Grades 9-12

	Current Cigarette Smoking	Current Any Tobacco Use
National†	22.9%	28.4%
AZ††	n/a	n/a
Boys††	24.6%	32.9%
Girls††	21.2%	23.9%

Current Cigarette Smoking=smoked cigarettes on ≥ 1 of the 30 days preceding the survey.
Current Any Tobacco Use=current use of cigarettes or smokeless tobacco or pipes or bidis or cigars or kreteks on ≥ 1 of the 30 days preceding the survey.
Source: † National Youth Tobacco Survey 2000, †† Arizona Youth Tobacco Survey 2001

State Laws 2002‡

- Does Arizona have a sales tax on tobacco products?
  Yes, $1.18/pack.
- Does the state have public smoking bans?
  Yes, bans in schools. Smoking restrictions in public places and workplaces.
- Does the state have youth access laws?
  Yes, minimum age requirements, packaging restrictions, photo ID requirements, unannounced random inspections, statewide enforcement agency.
- Does the state laws preempt federal laws?
  No.

Source: ‡ American Lung Association, State of Tobacco Control

Legacy in Arizona

- Governor Janet Napolitano currently serves on our Board of Directors.
- Gary Gearheart currently serves on our Youth Advisory Panel.
- Legacy has awarded $1,024,893 in grants to projects in Arizona.

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ALTRIA GROUP INC.
Washington, DC, November 24, 2003

Hon. JOHN MCCAIN,
Chairman,
Committee on Commerce, Science, and Transportation,
Washington, DC.

Dear Mr. Chairman:

Attached hereto is written testimony from Philip Morris USA that we respectfully request be included in the record of proceedings before the Committee on Commerce, Science, and Transportation conducted on November 12, 2003 to consider State use of tobacco settlement funds.

During the course of that hearing, two issues in particular were discussed that believe warrant further information be provided to the Committee. Thus, the attached statement discusses the position of PM USA on the use of cigarettes in movies, as well as the company's current marketing and promotion practices and expenditures. Should the Committee desire additional information on these matters, beyond that contained in our statement, please do not hesitate to have your staff contact this office.

Thank you for your consideration of this request.

Sincerely,

JOHN F. SCRUGGS,
Vice President,
Government Affairs.

cc. Senator Ernest F. Hollings
Ranking Minority Member,
Committee on Commerce, Science, and Transportation

ATTACHMENT

WRITTEN COMMENTS OF PHILIP MORRIS USA

Philip Morris USA is pleased to submit these comments regarding the Committee's November 12, 2003 hearing on the use of tobacco settlement funds. That hearing was held to discuss, among other things, the issue of whether states are devoting enough tobacco settlement funds to youth smoking prevention efforts.

We want to express our appreciation to the Committee and to Chairman McCain for holding a hearing on this subject. As we have stated over the years, Philip Morris USA encourages the states to spend a significant portion of the tobacco settlement funds on youth smoking prevention efforts. We share the disappointment expressed by many at the November 12 hearing that more states have not taken advantage of the opportunity to use these funds to support programs that can help reduce youth smoking. Indeed, there is no question that support for youth smoking prevention efforts is a worthy and appropriate use for the tobacco settlement funds. For our part, as the manufacturer of a product intended for adults that causes serious disease in smokers such as lung cancer, emphysema, and heart disease, and which is addictive, we believe we have a responsibility to help prevent youth smoking. In fact, with a dedicated Youth Smoking Prevention staff and an annual budget of over $100 million, we support positive youth development programs, research, and communications aimed at helping parents talk to their kids about not smoking. We believe there is a great opportunity for the States to increase their support for these kinds of activities. For Philip Morris USA, youth smoking prevention is a long-term commitment, and we stand ready to work with members of the Committee, as well as other interested stakeholders, in making progress on this important policy issue.

Philip Morris USA would like to take this opportunity to address two other issues that were raised during the hearing.

Product Placement and Smoking Scenes in Movies and Television Shows

We share the concern raised by a number of the hearing participants about the incidence of smoking in motion pictures and television shows. In connection with our marketing activities generally, Philip Morris USA conducts extensive training and continuously monitors compliance with our obligations under the Cigarette Advertising and Promotion Code (the "Ad Code")-a voluntary agreement originally entered into by the major domestic manufacturers in 1964 and most recently updated in 1990-as well as our internal guidelines and the terms of the Master Settlement

Agreement (the "MSA"), which collectively address issues with respect to the content and placement of our cigarette advertising.

With regard to product placement in particular, our policy for more than a decade has been to deny all third party requests for permission to use, display or make reference to our cigarette brand names, products, packages, or advertisements in media such as motion pictures or television shows produced for viewing by the general public, irrespective of whether the target audience is adults or minors. Since that policy was implemented, Philip Morris USA has not made, or caused to be made, any payment, or given other consideration to any person or entity to use, display or make reference to or use as a prop our cigarette brand names, products, packages or advertisements in any form of media covered by the policy, including movies or television shows produced for viewing by the general public.

This policy is consistent with the terms of the MSA, which, as Attorney General Moore correctly noted in his remarks, prohibits participating manufacturers from paying for product placements in movies, television shows, or other performances or video games.[1] Philip Morris USA has been in full compliance with the MSA and the Ad Code, including all provisions relating to product placement prohibitions. Moreover, no Attorney General has taken any enforcement action against us with respect to these provisions. If any State believes that there is any evidence suggesting that there is any question about our compliance, we stand ready to address those concerns. In fact, we recently received an inquiry from the California Attorney General on the topic of smoking in movies. In response, we provided information on our policy and practices 1related to this topic and included copies of letters—referenced below—that we sent to the heads of movie studios encouraging them to take action on this issue.

The fact that we do not pay for product placement, and the fact that we deny all requests to use our brands and brand imagery in movies and television shows, does not mean, of course, that our products never appear in movies or television shows. The fact of the matter is that some producers and directors of motion pictures and television shows do use or depict Philip Morris USA brands in their works *without* seeking or obtaining our permission. This is a frustrating situation for us, since our position is clear we do not want our brands or brand imagery to be depicted in movies and television shows. Among other things, such usages of our brands and brand imagery perpetuate the misunderstanding in the minds of some that we pay for or otherwise encourage these depictions, when, in fact, we are legally barred from doing so, and have followed a strict policy for more than a decade that prohibits such activity. However, irrespective of our views or our business practices, current law clearly *allows* the "fair use" of our brands or brand imagery-even without our permission which hinders our ability to take proactive steps to prevent usages of our brands or brand imagery in movies and television shows.

Nevertheless, we have joined others in encouraging the motion picture industry to reduce or eliminate smoking scenes from movies targeted towards kids, and, in addition, to cease using cigarette brands or brand imagery in *all* movies. As Howard Willard III, Senior Vice President of Philip Morris USA's Youth Smoking Prevention Department, stated in an October 17, 2003 letter to a group of motion picture producers:[2]

> I am writing to express Philip Morris USA's support of the proposal by 25 State Attorneys General encouraging the motion picture industry to reduce or eliminate smoking scenes in movies that are directed towards kids. In addition, consistent with Philip Morris USA's policy of denying permission for the use of our products or trademarks in films, we also want to strongly encourage the motion picture industry to voluntarily refrain from portraying or referring to cigarette brands or brand imagery in any movies.
>
> Youth smoking prevention is a serious commitment for Philip Morris USA. Our Youth Smoking Prevention (YSP) Department has a dedicated staff of 20 people and a budget in excess of $100 million. We focus our efforts in the following four areas: (i) communications and education for parents to help and encourage them to talk to their kids about not smoking; (ii) grants to support youth smoking prevention and positive youth development programs; (iii) support for youth access prevention programs and (iv) research to help us understand the latest developments in youth smoking prevention.

[1] The Master Settlement Agreement creates a few narrow exceptions to this rule, for media that are not intended to be distributed to the public or are intended to be viewed in Adult-Only Facilities or instructional media for adult smokers regarding non-conventional cigarettes.

[2] Letter from Howard Willard to heads of major U.S. motion picture studios, dated October 17, 2003. Copies attached.

In May 2003, an American Legacy Foundation study found that smoking was depicted in 64 percent of PG–13 and 37 percent of PG movies included in their analyses.[3] Research suggests that youth exposure to smoking in movies has an impact on their attitudes and behaviors related to smoking. For example, researchers found that children who had the highest exposure to smoking in movies were almost three times more likely to start smoking than were children who had the lowest exposure to smoking in movies.[4] I have attached a brief summary of this and other relevant research on this issue.

At Philip Morris USA we are committed to helping prevent youth smoking. We welcome the opportunity to work with others who share our goal. We have significant resources available in our YSP programs and YSP research groups that could provide you with support as you tackle this issue. Please contact me if we can be of assistance.

In short, we believe it is appropriate for the motion picture and television industry to reduce or eliminate depictions of cigarettes and smoking from movies and shows aimed at kids, and to refrain from using cigarette brands and brand imagery in any movies.

Changes in Cigarette Advertising, Marketing and Promotional Expenditures

During the hearing, a number of comments were made regarding changes in industry expenditures on cigarette advertising, marketing and promotional efforts since the MSA was signed. Contrary to what some at the hearing implied, Philip Morris USA has dramatically reduced its expenditures on newspaper, magazine, and point of sale advertising in every year since the MSA was signed in 1998. Traditional brand image advertising represented less than 8 percent of the Company's total expenditures in 2001, the most recent year for which the FTC has published aggregate industry expenditures, continuing a four-year decline from 21 percent of spending in 1998. And these downward trends have continued through to the present.

The $11.5 billion figure reported by the FTC that was cited at the hearing is an aggregate industry figure for an FTC designated expense category that includes not only expenditures on brand advertising (which for us has been dramatically reduced) but also expenditures on price promotions. Philip Morris USA has expanded the breadth and depth of its price promotions following its commitment to the MSA in order to compete effectively in the marketplace, particularly in light of the deep discount prices charged by competitors that did not sign the MSA and recent drastic increases in state excise taxes. A significant percentage of our marketing and promotional expenditures are for price promotions. Yet, despite our use of price promotions to remain competitive, the price of our products is still among the highest in the industry. Recently, some tobacco control advocates have implied that the substantial level of expenditures on price promotions constitutes an increase in brand advertising. That is simply not the case. We not only disagree with that characterization; we believe it reflects a misunderstanding of current industry dynamics, which require manufacturers to compete on price to remain competitive in a rapidly changing industry.

For its part, Philip Morris USA is meeting that challenge responsibly. For example, Philip Morris USA's marketing and promotional expenditures include promotional allowances we pay to retailers who agree to take significant steps to help reduce youth access to tobacco products and to otherwise responsibly merchandise the cigarette category. Philip Morris USA offers retailers the highest level of promotional incentives for a non self-service environment, no displays or signage on the counter and implementing the *We Card* program, which trains retail employees to comply with minimum age laws.

As the testimony at the hearing made clear, the extra costs imposed by the MSA on participating manufacturers—which have been exacerbated by dramatic increases in State excise taxes in the past several years—have spurred considerable growth over the last few years of the "deep discount" segment of the domestic cigarette market. Manufacturers that don't compete effectively on price will continue to lose share to those manufacturers that have not agreed to comply with the terms of the MSA. This trend clearly *undermines* the goals of those who want to reduce

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[3] American Legacy Foundation. "Big Tobacco on the Big Screen" (Press Release). May 31, 2003.

[4] Dalton, Madeline A., Sargent, James D., *et al.,* "Effect of viewing smoking in movies on adolescent smoking initiation: a cohort study" *The Lancet* 362 (2003): 281–285; published online *http://image.thelancet.com/extras/03art1353web.pdf* (June 10, 2003).

the visibility of cigarette advertising, because those manufacturers are *not* bound by the MSA's marketing restrictions.

Not only have we reduced the amount that we spend on traditional cigarette brand advertising, we have also significantly changed the *nature* of our marketing and advertising practices to further reduce the profile of our advertising. Part of this change is compelled by the MSA, which prohibits participating manufacturers such as Philip Morris USA from marketing its brands through billboards, mass transit, and most other forms of outdoor advertising, and which imposes other important restrictions on the way we communicate with adult smokers. But the changes we have experienced go above and beyond what the MSA, or other applicable laws require, and include restrictions that we have voluntarily adopted to better align our practices with society's expectations. For example, three years ago Philip Morris USA withdrew all of our advertising from the back covers of all magazines. We have also set voluntary standards that prohibit us from advertising in any magazine with significant youth readership in particular, in any publication in which readers younger than 18 years of age constitute 15 percent or more of the total readership of the magazine or that is read by more than two million persons younger than 18 years of age. These readership standards are the same as those contained in the tobacco rules proposed by the Food and Drug Administration. However, having severely restricted the amount of print advertising we run, our current print advertising practices go well beyond these standards.

Conclusion

We thank the Committee for the opportunity to submit these written remarks, and we would be happy to provide further detail or clarification regarding our practices and positions.

PHILIP MORRIS U.S.A.
New York, NY, October 17, 2003

Hon. DENNIS ECKHART,
Senior Assistant Attorney General,
Office of the Attorney General,
State of California,
Sacramento, CA.

Dear General Eckhart:

I have attached copies of the letters I recently sent to the major movie studios expressing Philip Morris USA's support of the proposal by 25 State Attorneys General encouraging the motion picture industry to reduce or eliminate smoking scenes in movies that are directed towards kids, as well as our request that the motion picture industry voluntarily refrain from portraying or referring to cigarette brands or brand imagery in any movies. I have been committed to communicating with the movie studios on this issue since our correspondence in August. However, prior to sending the letters we conducted a review of the relevant research to both better inform our communication and to share with the movie industry executives.

I am hopeful that our efforts will help contribute to continued declines in youth smoking rates.

Sincerely yours,

HOWARD A. WILLARD III,
Senior Vice President,
Youth Smoking Prevention.

Attachments

ATTACHMENTS

PHILIP MORRIS U.S.A.
New York, NY, October 17, 2003

JONATHAN DOLGEN,
Chairman,
Paramount Pictures,
Los Angeles, CA.

Dear Mr. Dolgen:

I am writing to express Philip Morris USA's support of the proposal by 25 State Attorneys General encouraging the motion picture industry to reduce or eliminate smoking scenes in movies that are directed towards kids. In addition, consistent with Philip Morris USA's policy of denying permission for the use of our products or trademarks in films, we also want to strongly encourage the motion picture industry to voluntarily refrain from portraying or referring to cigarette brands or brand imagery in any movies.

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At Philip Morris USA we are committed to helping prevent youth smoking. We welcome the opportunity to work with others who share our goal. We have significant resources available in our YSP programs and YSP research groups that could provide you with support as you tackle this issue. Please contact me if we can be of assistance.

Sincerely yours,

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cc: Jack Valenti, President, Motion Picture Association of America
Senior Assistant California Attorney General Dennis Eckhart, w/encl.
Denise Keane, Senior Vice President and General Counsel, Philip Morris USA.

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PHILIP MORRIS U.S.A.
New York, NY, October 17, 2003

MICHAEL D. EISNER,
Chief Executive Officer,
The Walt Disney Company,
Burbank, CA.

Dear Mr. Eisner:

I am writing to express Philip Morris USA's support of the proposal by 25 State Attorneys General encouraging the motion picture industry to reduce or eliminate smoking scenes in movies that are directed towards kids. In addition, consistent with Philip Morris USA's policy of denying permission for the use of our products or trademarks in films, we also want to strongly encourage the motion picture industry to voluntarily refrain from portraying or referring to cigarette brands or brand imagery in any movies.

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PHILIP MORRIS U.S.A.
New York, NY, October 17, 2003

HARVEY WEINSTEIN,
Co-Chairmen,
Miramax Films,
Los Angeles, CA.

Dear Mr. Weinstein:

I am writing to express Philip Morris USA's support of the proposal by 25 State Attorneys General encouraging the motion picture industry to reduce or eliminate smoking scenes in movies that are directed towards kids. In addition, consistent with Philip Morris USA's policy of denying permission for the use of our products or trademarks in films, we also want to strongly encourage the motion picture industry to voluntarily refrain from portraying or referring to cigarette brands or brand imagery in any movies.

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PHILIP MORRIS U.S.A.
New York, NY, October 17, 2003

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Miramax Films,
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PHILIP MORRIS U.S.A.
New York, NY, October 17, 2003

STEVEN SPIELBERG,
Chairman and Chief Executive Officer,
Dreamworks,
Glendale, CA.

Dear Mr. Spielberg:

I am writing to express Philip Morris USA's support of the proposal by 25 State Attorneys General encouraging the motion picture industry to reduce or eliminate smoking scenes in movies that are directed towards kids. In addition, consistent with Philip Morris USA's policy of denying permission for the use of our products or trademarks in films, we also want to strongly encourage the motion picture industry to voluntarily refrain from portraying or referring to cigarette brands or brand imagery in any movies.

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PHILIP MORRIS U.S.A.
New York, NY, October 17, 2003

JOHN CALLEY,
Chairman and Chief Executive Officer,
Sony Pictures Entertainment,
Culver City, CA.

Dear Mr. Calley:

I am writing to express Philip Morris USA's support of the proposal by 25 State Attorneys General encouraging the motion picture industry to reduce or eliminate smoking scenes in movies that are directed towards kids. In addition, consistent with Philip Morris USA's policy of denying permission for the use of our products or trademarks in films, we also want to strongly encourage the motion picture industry to voluntarily refrain from portraying or referring to cigarette brands or brand imagery in any movies.

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PHILIP MORRIS U.S.A.
New York, NY, October 17, 2003

ALEX YEMENIDIJAN,
Chairman and Chief Executive Officer,
MGM Pictures,
Santa Monica, CA.

Dear Mr. Yemenidijan:

I am writing to express Philip Morris USA's support of the proposal by 25 State Attorneys General encouraging the motion picture industry to reduce or eliminate smoking scenes in movies that are directed towards kids. In addition, consistent with Philip Morris USA's policy of denying permission for the use of our products or trademarks in films, we also want to strongly encourage the motion picture industry to voluntarily refrain from portraying or referring to cigarette brands or brand imagery in any movies.

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PHILIP MORRIS U.S.A.
New York, NY, October 17, 2003

STACEY SNIDER,
Chief Executive Officer,
Universal Pictures,
Universal City, CA.

Dear Ms. Snider:

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PHILIP MORRIS U.S.A.
New York, NY, October 17, 2003

BARRY MEYER,
Chief Executive Officer,
Warner Brothers Studios,
Burbank, CA.

Dear Mr. Meyer:

I am writing to express Philip Morris USA's support of the proposal by 25 State Attorneys General encouraging the motion picture industry to reduce or eliminate smoking scenes in movies that are directed towards kids. In addition, consistent with Philip Morris USA's policy of denying permission for the use of our products or trademarks in films, we also want to strongly encourage the motion picture industry to voluntarily refrain from portraying or referring to cigarette brands or brand imagery in any movies.

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References

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PHILIP MORRIS U.S.A.
New York, NY, October 17, 2003

JIM GIANOPULOS,
Co-Chairmen,
Fox Filmed Entertainment,
Los Angeles, CA.

Dear Mr. Gianopulos:

I am writing to express Philip Morris USA's support of the proposal by 25 State Attorneys General encouraging the motion picture industry to reduce or eliminate smoking scenes in movies that are directed towards kids. In addition, consistent with Philip Morris USA's policy of denying permission for the use of our products or trademarks in films, we also want to strongly encourage the motion picture industry to voluntarily refrain from portraying or referring to cigarette brands or brand imagery in any movies.

Youth smoking prevention is a serious commitment for Philip Morris USA Our Youth Smoking Prevention (YSP) Department has a dedicated staff of 20 people and a budget in excess of $100 million. We focus our efforts in the following four areas: (i) communications and education for parents to help and encourage them to talk to their kids about not smoking; (ii) grants to support youth smoking prevention and positive youth development programs; (iii) support for youth access prevention programs and (iv) research to help us understand the latest developments in youth smoking prevention.

In May 2003, an American Legacy Foundation study found that smoking was depicted in 64 percent of PG-13 and 37 percent of PG movies included in their analyses.[1] Research suggests that youth exposure to smoking in movies has an impact on their attitudes and behaviors related to smoking. For example, researchers found that children who had the highest exposure to smoking in movies were almost three times more likely to start smoking than were children who had the lowest exposure to smoking in movies.[2] I have attached a brief summary of this and other relevant research on this issue.

At Philip Morris USA we are committed to helping prevent youth smoking. We welcome the opportunity to work with others who share our goal. We have significant resources available in our YSP programs and YSP research groups that could provide you with support as you tackle this issue. Please contact me if we can be of assistance.

Sincerely yours,

HOWARD A. WILLARD III

cc: Jack Valenti, President, Motion Picture Association of America
Senior Assistant California Attorney General Dennis Eckhart, w/encl.
Denise Keane, Senior Vice President and General Counsel, Philip Morris USA.

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1. American Legacy Foundation. "Big Tobacco on the Big Screen" (Press Release). May 31, 2003.

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PHILIP MORRIS U.S.A.
New York, NY, October 17, 2003

TOM ROTHMAN,
Co-Chairmen,
Fox Filmed Entertainment,
Los Angeles, CA.

Dear Mr. Rothman:

I am writing to express Philip Morris USA's support of the proposal by 25 State Attorneys General encouraging the motion picture industry to reduce or eliminate smoking scenes in movies that are directed towards kids. In addition, consistent with Philip Morris USA's policy of denying permission for the use of our products or trademarks in films, we also want to strongly encourage the motion picture industry to voluntarily refrain from portraying or referring to cigarette brands or brand imagery in any movies.

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SUMMARY OF RESEARCH AND PERSPECTIVES ON THE PORTRAYAL OF TOBACCO IN THE MOVIES IN AN EFFORT TO HELP PREVENT YOUTH SMOKING

Prepared by Philip Morris USA's Youth Smoking Prevention Department as an enclosure to its letter to U.S. movie industry executives—October 17, 2003

Prevalence of Smoking/Tobacco Use in Movies

American Legacy Foundation Analysis (2003) covered 216 movies and their trailers [1]

—67 percent of the movies and 14 percent of the trailers depicted smoking
—The survey found that smoking was depicted in the following:

- 85 percent of R-rated movies
- 64 percent of PG-13 movies
- 37 percent of PG-rated movies

—Television-aired trailers were more likely to include smoking imagery if the movie being promoted showed a specific brand

- If a brand appeared in the movie, there was a 45 percent incidence of the trailer including tobacco imagery
- If the movie included smoking with no brand appearance, there was only a 15 percent incidence of the trailer including smoking

STARS Project (American Lung Association) Study (2003) reviewed 145 movies playing between May 31, 2002 and May 26, 2003 [2]

—106 of the 145 movies (73 percent) that made the box office weekly Top 10 featured tobacco use
—The study found that tobacco use was depicted as follows:

- 76 percent of R-rated movies
- 82 percent of PG-13 movies
- 39 percent of PG-rated movies

—Reviewers classified segments according to perceived tobacco messages:

- 30 percent did not portray tobacco use or depicted the negative consequences of its use
- 39 percent either used numerous pro-tobacco or glamorous portrayals
- 20 percent used specific brand depictions and/or showed a minor or pregnant women use tobacco

Massachusetts Public Interest Research Group (MASSPIRG) (2002) reviewed PG-13 films and compared the amount of tobacco use in 1996–97 (pre-MSA) and 1999–2000 (post-MSA). The top 10 grossing films and top 5 video rentals in America during the specified years were reviewed. [3]

—Tobacco use remains prevalent in PG-13, youth oriented movies

- 82 percent of post-MSA movies
- 80 percent of pre-MSA movies

—From the perspective of total film time, tobacco use is up 50 percent in post-MSA films

- 1.35 minutes of tobacco use post-MSA
- .89 minutes of tobacco use pre-MSA

—Most films portray smokers and smoking in a positive or neutral light

- 83 percent of post-MSA movies with tobacco use conveyed the perception that smoking is acceptable and even "cool" (no comparison to pre-MSA made)

—Fewer films feature negative statements about tobacco use

- Before the MSA, 31 percent of movies showed tobacco use as a negative; post-MSA that number fell to 17 percent

Impact of the Depiction of Smoking/Tobacco Use in Movies

Although there are a limited number of studies in this area, academic research has increased recently and preliminary findings indicate that exposure to cigarette smoking in movies has an impact on youth attitudes and behaviors related to smoking. A number of peer-reviewed studies have suggested that children may be influenced to smoke by watching movies that portray smoking:

- Dalton, *et at.* (2003)—"After controlling for baseline characteristics, adolescents in the highest quartile of exposure to movie smoking were 2.71 times more likely to initiate smoking compared to those in the lowest quartile. The effect of exposure to movie smoking was stronger in adolescents with non-smoking parents than in those whose parents smoked . . . Our results provide strong evidence that viewing smoking in movies promotes smoking initiation among adolescents." [4]
- Sargent, *et al.,* (2002)—"Our research documents a strong relationship between viewing tobacco use in movies and more positive attitudes toward smoking among adolescent never-smokers . . . This is consistent with the idea that viewing tobacco depictions in movies softens adolescents' resistance to peer offers, enhances their perceptions of the positive benefits of smoking, and makes them more likely to consider trying smoking in the future." [5]
- Pechmann and Shih (1999)—". . . smoking (versus nonsmoking) scenes positively . . . enhanced their [youth] perceptions of smokers' social stature, and increased their intent to smoke. However, youths' opinions were malleable, and showing them an antismoking advertisement before the film effectively repositioned the smoking from forbidden to tainted, thereby nullifying the aforementioned effects." [6]
- Distefan, *et at.* (1999)—"We conclude that there is a relationship between adolescents' choice of favorite movie actors and actresses and their smoking status. Favorite movie stars may provide normative behavior models that are emulated or used to justify subsequent smoking . . . the recent increase in the portrayal of smoking in the movies is alarming, particularly as it has been associated with a large increase in smoking among adolescents." [7]

Perspectives on the Subject of the Depiction of Smoking/Tobacco Use in Movies

"Movies are rated on the basis of language, violence, sexual content, and drugs . . . The MPAA does not consider smoking -the most widely used additive drug that kills the most people—in assigning ratings."

> Stanton Glantz, Professor of Medicine at the University of California, San Francisco and founder of the Smoke Free Movie project, Excerpt from an Editorial entitled *Rate Movies with Smoking "R"* [8]

"Substantial research indicates that exposure to cigarettes and smoking in movies has a measurable impact on youth . . . The appearance of tobacco in PG and PG–13 movies has steadily increased . . .! invite the film industry's cooperation in reducing the amount of tobacco and smoking in movies by eliminating the appearance of tobacco except where absolutely integral to a scene. I think it is reasonable to expect that cigarette brand names not appear at all . . ."

> Bill Lockyer, Attorney General, State of California, Letter to Jack Valenti, President of Motion Picture Association of America [9]

". . . not everyone supports the claim that movies are an important influence on children's smoking behaviors. Moreover, the evidence supporting this claim is limited to a few observational studies; and all such research faces the difficult challenge of disentangling the effect of movies from adolescent personalities and parenting characteristics."

> Steven Woloshin, MD, MS and Lisa Schwartz, MD, MS; Excerpt from an Editorial entitled *Smoke-Free Movies: Sense or Censorship?* [10]

Recommendations from the Public Health Community

The World Health Organization,[11] American Medical Association, American Legacy Foundation, and others—including the Los Angeles Department of Public Health and U.S. Public Interest Research Group—have endorsed the following four policies:

—*Certify No Pay-Offs*

The producers should post a certificate in the credits at the end of the movie declaring that nobody on the production received anything of value (cash money, free cigarettes or other gifts, free publicity, interest-free loans or anything else) from anyone in exchange for using or displaying tobacco.

—*Require Strong Anti-Smoking Ads*
Studios and theaters should require a genuinely strong anti-smoking ad (not one produced by a tobacco company) to run before any film with any tobacco presence, regardless of its MPAA rating.

—*Stop Identifying Tobacco Brands*
There should be no tobacco brand identification nor the presence of tobacco brand imagery (such as billboards) in the background of any movie scene.

—*Rate New Smoking Movies "R"*
Any film that shows or depicts tobacco should be rated "R." The only exceptions should be when the presentation of tobacco clearly and unambiguously reflects the dangers and consequences of tobacco use or is necessary to represent smoking of a real historical figure.

—*The American Legacy Foundation[12] also recommends adding:*
Eliminate the practice of portraying smoking in aired movie trailers.

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