MSA TOBACCO PAYMENTS AND THE NON-PARTICIPATING MANUFACTURER (NPM) SETTLEMENT

(CONSENSUS FORECASTING GROUP)

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The Master Settlement Agreement

- The Master Settlement Agreement (MSA) resolved litigation brought by the States vs. major tobacco companies for costs incurred in treating smoking-related illnesses
- 52 States and Territories are collectively the "Settling States"
- The original, major tobacco companies that were sued are the "Original Participating Manufacturers" (OPMs)
- The tobacco companies that subsequently joined in the settlement are the "Subsequent Participating Manufacturers" (SPMs)

The Master Settlement Agreement

3

- OPMs and SPMs are subject to significant restrictions on advertising and marketing of tobacco products

- OPMs and SPMs have made and continue to make significant settlement payments to the Settling States

- The Commonwealth of Kentucky has received $117.59 million in FY19 and $2.198 billion in MSA payments in total

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4

Three types of payments to the States:

Initial Payments (1998 and 2000-2003)

- $12.7 Billion

Annual Payments (2000 - Perpetuity)

- $207.9 Billion through 2025
- $3.6 Billion to Kentucky through 2025
- Based on "Allocable Share" - For Kentucky – 1.76%

"Strategic Contribution Fund" payments

- $8.6 Billion in 2008-2017
- $50.7 Million to Kentucky in 2008-2017
- Not based on "Allocable Share" - For Kentucky – 0.75%

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5

Three potential adjustments to the payments:

Inflation adjustment

- Greater of CPI growth or 3%

Volume adjustment

- Based on reductions relative to base volume

Non-participating manufacturers (NPM) adjustment

What is the NPM Adjustment?

6

- Tobacco companies that don't join the MSA are "Non-Participating Manufacturers" (NPMs) and are free from MSA's marketing restrictions and the settlement payment obligations
- To prevent the NPMs from having a significant advantage in the marketplace, the Settling States each passed a "Qualifying Statute" requiring NPMs to make escrow payments for the cigarettes sold in each State
- The states are required to "diligently enforce" the provisions of the MSA, though "diligent enforcement " is not defined
- The reduction in payments is punitive – payments are reduced by triple the net market share loss above 2%

NPM Adjustment Settlement

7

- The Commonwealth entered into a settlement agreement with the OPMs and the SPMs in June, 2014
- Settled the issue of the 2003-2012 NPM Adjustments and 2014-2017 have been settled subsequently
- Eliminated the budgetary impact of the adverse 2003 NPM Adjustment decision
- Reduces the volatility in future annual MSA payments – OPMs agree to withhold significantly smaller portion of potential NPM Adjustment
- Eliminated the need for costly litigation for more than decade
- When litigation is required, the Commonwealth's case will be stronger than the current case for diligence for past years
- Thirty-eight States and Territories have entered into settlements of the NPM Adjustment issue

October 2019 – Revenue Estimates

8

Preliminary Estimates

Fiscal Year 2020	**$111.1 Million**
Fiscal Year 2021	**$106.9 Million**
Fiscal Year 2022	**$103.1 Million**