Department of Legislative Services
Maryland General Assembly
2019 Session

FISCAL AND POLICY NOTE
First Reader

House Bill 1159 (Delegate Rosenberg)
Appropriations

Cigarette Restitution Fund - Establishment of Account

This bill establishes a separate account within the Cigarette Restitution Fund (CRF) that consists of payments received by the State from litigation by participating manufacturers related to the State's diligent enforcement of its qualifying statute for the Master Settlement Agreement (MSA). The bill restricts the uses of most of the available funding from the account by specifying that 75% of any appropriation from the account must be used for enumerated public health purposes, of which 25% must be used for substance use treatment. Up to $20.0 million may be appropriated from the account in any fiscal year. **The bill takes effect July 1, 2019.**

Fiscal Summary

State Effect: The bill is not anticipated to materially affect State expenditures or revenues but may redirect future spending, as discussed below.

Local Effect: The bill does not materially affect local finances.

Small Business Effect: Minimal.

Analysis

Bill Summary: In each fiscal year for which appropriations from the account are made, 75% of the appropriations must be made for (1) the Tobacco Use Prevention and Cessation Program; (2) the Cancer Prevention, Education, Screening, and Treatment Program; and (3) other programs that serve specified purposes including various tobacco cessation measures, tobacco production alternatives, enforcement of tobacco sales laws, and substance use treatment and prevention programs. The bill also requires that, of this funding, 25% must be used for substance use treatment.

These uses are already authorized in statute. By specifying that 75% of the account must be used for the public health purposes listed above, the bill limits use of funding available in the account for "any other public purpose" and also for Medicaid.

The bill also repeals the current law authorization to use CRF for the Maryland Health Care Foundation, which no longer exists in statute.

Current Law/Background:

Cigarette Restitution Fund: Chapters 172 and 173 of 1999 established CRF, which is supported by payments made under MSA. Through MSA, the settling manufacturers pay the litigating parties – 46 states, five territories, and the District of Columbia – substantial annual payments in perpetuity. The distribution of MSA funds among the states is determined by formula, with Maryland receiving 2.26% of MSA monies, which are adjusted for inflation, volume, and prior settlements.

The use of CRF is restricted by statute. Activities funded through CRF include the Tobacco Use Prevention and Cessation Program; the Cancer Prevention, Education, Screening, and Treatment Program; substance use treatment and prevention; the Breast and Cervical Cancer Program; Medicaid; tobacco production alternatives; legal activities; and nonpublic school textbooks. CRF use is also generally authorized for "any other public purpose." For each fiscal year in which appropriations are made from CRF, at least 50% of the appropriations must be made for specified core public health uses, including substance use treatment and prevention programs. Additionally, at least 30% of the appropriations must be made to Medicaid.

Nonparticipating Manufacturer Adjustment: Among other conditions, MSA required states to take steps toward creating a more "level playing field" between participating manufacturers (PMs) to MSA (those subject to annual payments and other restrictions) and nonparticipating manufacturers (NPMs) to MSA. PMs have long contended that NPMs have avoided or exploited loopholes in state laws that give them a competitive advantage in the pricing of their products. If certain conditions are met, MSA provides a downward adjustment to the contribution made by PMs based on their MSA-defined market share loss multiplied by three. This adjustment is known as an NPM adjustment. The agreement also allows PMs to pursue this adjustment on an annual basis.

Under MSA, PMs must meet three requirements to prevail and reduce their MSA payments: (1) have a demonstrable loss of market share of more than approximately 2%;

(2) show that MSA was a significant factor contributing to that loss of market share; and (3) show that a state was not diligently enforcing its qualifying statute.

Litigation regarding the NPM adjustment started in 2005, beginning with the NPM adjustment for sales year 2003. Arbitration regarding the "diligent enforcement" issue for 2003 commenced in July 2010. Maryland was 1 of 15 states that did not settle with PMs during the arbitration process and was 1 of 6 states that were found to not have diligently enforced its qualifying statute. Among the findings made by the arbitration panel were that Maryland lacked dedicated and trained personnel to conduct enforcement efforts and that the Comptroller's Office failed to meaningfully participate in enforcement efforts.

Based on the arbitration panel's finding, Maryland not only forfeited $16 million that PMs placed in escrow for the 2003 sales year but, under the MSA arbitration framework, also saw its 2014 payment reduced by $67 million based on the arbitration panel's assessment that those states that settled before arbitration could not be found as nondiligent. However, subsequent litigation reduced the payment loss to $13 million.

Those states that did settle with PMs realized a one-time cash windfall with the release of funds from disputed payments escrow accounts for sales years 2003 through 2012. However, under the terms of the settlement, PMs were given credit for future payments from those states (*i.e.*, reducing the payments to those states), and those states had to enact new legislation and will be held to an enhanced standard in NPM adjustment disputes beginning with 2015.

PMs sought a multistate arbitration related to sales year 2004 for Maryland and other states that did not settle the 2003 sales year litigation. Arbitration on sales year 2004 began in fall 2018, with eight or nine states involved (New Mexico's participation in the current arbitration proceedings is under litigation in that state). No decision on the arbitration will be made until all of the arbitration proceedings for each state have concluded.

For each disputed year since 2004, with some exceptions, an amount has been withheld and deposited into a disputed payments account. As of April 2018, there was $202 million in that account. If the State is found to have diligently enforced the statute in subsequent years, at least this amount could be realized in revenue. When that funding could be available depends on whether PMs continue to pursue annual sales year litigation or whether they try to bring all states back into realignment by pursuing multi-year settlements with the states currently still in arbitration and also what strategies individual states pursue.

Exhibit 1 shows the disputed payments held in escrow (and that are subject to release) for dispute years 2004 through 2015. Amounts actually released and the timing of their receipt depend on the outcomes of future litigation.

Exhibit 1
Disputed Payments from Nonparticipating Manufacturer Adjustment
Dispute Years 2004-2015
($ in Millions)

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Total	$16.0	$0	$12.0	$13.0	$20.0	$20.0	$20.0	$17.0	$19.0	$19.0	$20.0	$22.0

Notes: Numbers are approximate. Dispute year 2005 payments have already been received as part of the 2003 arbitration. Payment information for 2016 and beyond have yet to be determined.

Source: Office of the Attorney General

State Fiscal Effect: The bill directs disputed payments that are released from escrow to a new account within CRF and authorizes an appropriation of up to $20.0 million in each fiscal year from the account primarily for specified public health and substance use treatment services. As of April 2018, there was $202 million in the account. As mentioned above, depending on the involvement of New Mexico in arbitration proceedings, and when any disbursement is made, the earliest the State may receive any released payments is April 2019. Further, the State may choose to settle payments from multiple years at one time, resulting in the release of a lump sum to the State. However, it is also possible that Maryland receives no portion of these funds. As noted previously, the portion and timing of payment release depend on the outcome of future litigation.

The bill does not affect the amount or timing of any such special fund revenues that may be received. Rather it redirects such revenues to a separate account and specifies how they may be used. The Governor's proposed fiscal 2020 budget assumes that the $16 million held in escrow from the 2004 sales year is released during fiscal 2020. The bill redirects these funds to the newly created account in CRF and requires the funds to be used for specified purposes, which may not supplant existing State funding. The projected CRF revenues available for fiscal 2020, assuming receipt and use of the amount held in escrow, total $157.1 million. Of this available funding, $67.3 million is appropriated for Medicaid and $21.5 million is appropriated for substance use treatment. Thus, both Medicaid and substance use treatment are receiving more than the minimum required funding under current law and the bill, so the redirection of a portion of the special funding from CRF under the bill is not expected to materially change State expenditures. Rather, the bill is intended to ensure that specified funding is met in future years.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Office of the Attorney General; Comptroller's Office; Maryland State Treasurer's Office; Maryland Department of Health; Department of Legislative Services

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mm/jc

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