



# Tobacco Public Policy Center at Capital University Law School

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## STATE SECURITIZATION OF TOBACCO MASTER SETTLEMENT AGREEMENT (MSA) PAYMENTS

### WHAT IS SECURITIZATION?

- Generally, securitization involves the selling of rights to an expected stream of revenue to investors in return for receiving a lump sum payment now.
- Specifically, securitization of tobacco settlement agreement payments involves a state selling its rights to future revenue from its share of dollars from the Master Settlement Agreement (MSA) to investment firms in exchange for an immediate influx of cash.<sup>1</sup> The investment firms later sell the revenue streams from the tobacco settlements by issuing settlement bonds.
  - In 1998, forty-six states (including Ohio) signed the MSA with the major U.S. cigarette manufacturers. The agreement ended litigation that had been brought against the industry by the state attorneys general. The attorneys general had filed suits against the cigarette manufacturers seeking to enforce state laws and recover the medical costs incurred in treating sick and dying cigarette smokers. The agreement required cigarette manufacturers to make annual payments to the settling states, which are to continue indefinitely into the future.

### WHICH STATES HAVE SECURITIZED TOBACCO DOLLARS?

- The following states have already securitized all or some part of their share of funds under the Master Settlement Agreement:
  - Alabama, Alaska, Arkansas, California, Iowa, Louisiana, Maryland, Michigan, Missouri, New Jersey, North Dakota, Oregon, Rhode Island, South Carolina, South Dakota, Virginia, Washington, Wisconsin, and the District of Columbia and Puerto Rico. New York City and some New York counties have also securitized some of their shares of New York State's tobacco settlement payments, as have some California counties.
  - A number of states have considered securitization and rejected it, including Illinois, Nevada, Vermont, West Virginia, and Colorado (twice).

### USES OF SECURITIZED TOBACCO REVENUE

- Although the MSA did not require that MSA payments be dedicated to tobacco prevention, the purpose of the lawsuits leading up to the MSA was to seek reimbursement for tobacco-related costs. The MSA payments, however, do not nearly cover tobacco-related costs imposed on the state. For example, total Ohio Medicaid costs for smoking-related illnesses and diseases equal \$1.1 billion annually (or \$458 million for the State Medicaid portion), and smoking-caused productivity losses in Ohio are \$4.14 billion each year. The only way for MSA payments to adequately address the costs of

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tobacco is for states to invest a substantial portion of MSA proceeds in a sustainable tobacco prevention program that will reduce tobacco use over time.

- Tobacco control is a sound investment for the future and one of the surest ways to enhance health and decrease health care costs. If revenue intended for tobacco control and the promotion of public health is diverted to other purposes, the state and its residents will have to pay more down the road toward health care for tobacco-related diseases.<sup>2</sup>

## **CAUTIONARY TALES FROM OTHER STATES: SECURITIZATION HARMS TOBACCO PREVENTION PROGRAMS**

**Wisconsin:**<sup>3</sup> In 2001, Wisconsin decided to securitize its MSA payments due to a large budget deficit. As a result of the transaction, Wisconsin received \$1.6 billion in up-front payments (annual MSA payments would have totaled \$5.2 billion). Wisconsin planned to use only \$350 million of the securitized amount to eliminate the budget deficit, with the remainder being used to create an endowment fund for tobacco control efforts. In 2002, however, the budget gap was greater than expected, and all remaining funds from securitization were used to balance the budget. No endowment for tobacco control was established. Said one state representative, "I'm terribly disappointed. Here is a pot of money that was supposed to pay medical costs and spread the message to teenagers that smoking is detrimental to their health, and it's gone."<sup>4</sup> Moreover, after using all of the proceeds for securitization to meet short-term needs, the state's overall bond rating actually declined. Now, Wisconsin's spending on tobacco prevention amounts to just 0.5% of the state's total annual health care costs directly caused by smoking (\$2.02 billion).

**California:**<sup>5</sup> In 2003, facing a \$17 billion deficit, the governor proposed a plan to securitize 50% of the state's share of MSA funds, resulting in a one-time payment of \$2.5 billion (annual payments would have totaled \$12.5 billion). None of the funds were dedicated toward tobacco control or public health measures. In FY 2003, California securitized the remainder of its settlement payments and received \$3 billion – all of which was allocated to the FY 2004 state budget. Following these shortsighted actions, high school smoking rates increased between 2004 and 2006, from 13.2 percent in 2004 to 15.4 percent in 2006.

**Rhode Island:**<sup>6</sup> In 2002, Rhode Island approved a plan to securitize the state's rights to \$1.19 billion in future tobacco settlement payments for a smaller, one-time payment of \$600 million. The funds were used to address budget shortfalls and pay capital and operating expenses in FY 2002-FY 2004. This securitization left Rhode Island with no tobacco settlement funding available for tobacco prevention and other purposes after FY 2004.

## **CUTS IN TOBACCO PREVENTION FUNDING TAKE A TOLL**

- Every year, tobacco companies spend more than \$12.5 billion marketing their products (more than \$666 million in Ohio alone), and 740,000 additional youth become new daily smokers.<sup>7</sup> Comprehensive tobacco control programs have proven to be highly successful in reducing smoking rates, but they must be sustained over time.<sup>8</sup> Cuts to program funding across the nation are taking their toll – reductions in youth smoking have stalled, and youth susceptibility to smoking is on the rise.<sup>9</sup>
- A 2005 study by the U.S. Centers for Disease Control and Prevention (CDC) found that kids are being exposed to fewer state-sponsored television ads that discourage them from smoking. The study used Nielsen television ratings data to measure the exposure of 12-17 year olds to anti-tobacco advertising in the 75 largest media markets. The study found that exposure to anti-tobacco

advertising among youth increased between 1999 and 2002, but declined in 2003.<sup>10</sup> These results are troubling because well-funded state tobacco prevention programs, including TV ad campaigns, have successfully reduced youth smoking rates across the country. In Ohio, for example, the youth smoking rate fell 40% between 2000 and 2006, due in part to the success of the **stand** campaign.

- Progress in reducing youth tobacco use can be reduced quickly if funding is cut or eliminated. For example, Minnesota experienced an increase in youth susceptibility to smoking just months after funding for its Target Market program was eliminated. Although Minnesota's program was successful right from the start, program funding was reduced from \$23.7 million to \$4.6 million in July 2003. Just six months later, awareness of the Target Market campaign among teens had already fallen from 84.5 percent to 56.5 percent and youth susceptibility to smoking increased by 22 percent.<sup>11</sup>

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<sup>1</sup> American Lung Association, *Securitization – Breaking the Promise*, <http://www.lungusa.org/atf/cf/%7B7A8D42C2-FCCA-4604-8ADE-7F5D5E762256%7D/SECURITIZATION.PDF>.

<sup>2</sup> *Id.*

<sup>3</sup> *Id.*

<sup>4</sup> Dennis Chaptman, *Tobacco Money is a Quick Fix; State's Planning Called Weak*, MILWAUKEE JOURNAL SENTINEL, May 5, 2002.

<sup>5</sup> American Lung Association, *Securitization – Breaking the Promise*, <http://www.lungusa.org/atf/cf/%7B7A8D42C2-FCCA-4604-8ADE-7F5D5E762256%7D/SECURITIZATION.PDF>.

<sup>6</sup> Campaign for Tobacco-Free Kids, *Special Report: State Settlement Section, Rhode Island* (Dec. 2006) <http://www.tobaccofreekids.org/reports/settlements/state.php?StateID=RI>.

<sup>7</sup> Campaign for Tobacco-Free Kids, *Youth Smoking Declines and Related Benefits from States Fully Funding Tobacco Prevention* (Feb. 24, 2005), <http://tobaccofreekids.org/research/factsheets/pdf/0273.pdf>.

<sup>8</sup> For example, "In four states that dedicated significant funding to tobacco control efforts, cigarette sales fell an average of 43 percent between 1990 and 2000 compared with an average of 20 percent for all other states. The four states were Arizona, California, Massachusetts and Oregon." Council of States Governments, *No Ifs, Ands or Butts: Proven Anti-Smoking Strategies for States* (December 2005), <http://www.healthystates.csg.org/NR/rdonlyres/31091518-EC7D-4295-9191-47E45801BE9D/0/SmokingBrief.pdf> (citing M. Farrelly, *et al.*, *The Impact of Tobacco Control Program Expenditures on Aggregate Cigarette Sales: 1981-2000*, 22 J. HEALTH ECON. 848-859 (2003)).

<sup>9</sup> Campaign for Tobacco-Free Kids, *The Impact of Reductions to State Tobacco Control Program Funding* (Nov. 2005), <http://tobaccofreekids.org/research/factsheets/pdf/0270.pdf>.

<sup>10</sup> G. Szczyepka, *et al.*, *Estimated Exposure of Adolescents to State-Funded Anti-Tobacco Television Advertisements --- 37 States and the District of Columbia, 1999–2003*, 54 MMWR 1077-1080 (Oct. 28, 2005).

<sup>11</sup> Centers for Disease Control and Prevention, *Effect of Ending an Antitobacco Youth Campaign on Adolescent Susceptibility to Cigarette Smoking – Minnesota, 2002-2003*, 53 MMWR 301-304 (April 16, 2004).