

Tobacco Settlement Revenue Update
Presented to Tobacco Settlement Revenue Oversight Committee
November 6, 2014
Peter B. van Moorsel, Chief Economist, Legislative Finance Committee

Overview

- Master Settlement Agreement (MSA) revenue decreased in FY14 due to a reduction in the settlement payment pursuant to a successful challenge by participating manufacturers (PMs) of New Mexico's enforcement of the MSA.
- The FY14 payment of \$21.2 million was below the \$39.3 million received in FY13.
- MSA revenue in FY15 is projected to be \$39.9 million, and revenue in FY16 is estimated to be \$40.1 million.
- The forecast remains subject to uncertainty surrounding the nature and timing of any subsequent challenges by PMs of New Mexico's enforcement of the MSA.
- This forecast does not assume a reduction in the MSA payments for FY15 and FY16.
- The General Appropriation Act of 2014 includes contingency language to ensure programs funded with tobacco MSA funds are kept whole in the event of revenue reductions pursuant to a challenge. Any shortfall in MSA funds would be made up with a transfer from the Tobacco Settlement Permanent Fund (TSPF).

Background

- Signed in 1998, settlement of lawsuits over smoking-related deaths
- 46 states participated
- Payments made in perpetuity by participating manufacturers (PM's)
- There are restrictions on advertising, marketing and promotion
- The goal is to reduce smoking – especially among the youth

Key Statutory Provisions

- All manufacturers selling cigarettes in NM must either make MSA payments (PM's) or pay equivalent amounts into escrow for settlement of future claims (Non-participating manufacturers or NPMs).
- MSA payments are deposited in Tobacco Settlement Permanent Fund (TSPF).
- Since 2003, 50 percent of MSA revenue has been distributed to the Tobacco Settlement Program Fund to fund health care, research and tobacco use cessation programs.
- Between FY09 and FY13, the other 50 percent of the MSA payment were also transferred to the Tobacco Settlement Program Fund as part of the general fund solvency initiatives. This provision expired in FY14.
- However, the 2013 Legislature made additional changes to the distribution of Tobacco MSA revenues:
 - 25 percent of the transfer to the TSPF to the lottery tuition fund for lottery scholarships; and
 - 25 percent of transfer for appropriation for direct services provided by early childhood care and education programs administered by CYFD.
- After the 2013 session, the arbitration panel ruled in favor of the tobacco manufacturers that New Mexico did not diligently enforce the provisions of the compact. The ruling would result in a reduction in the FY14 transfer to the TSPF, estimated by the Attorney General's office to range

from \$12- million to \$24 million. The LFC estimated the reduction to be \$20 million for budgeting purposes, and adjusted its tobacco revenue estimate to \$19.5 million.

- \$39 million in appropriations had been made, so the Legislature made efforts to backfill these appropriations in the face of the reduced tobacco revenue, including:
 - Transferring from the TSPF the difference between the appropriation and the transfer to the TSPF;
 - Transferring the 25 percent of tobacco revenue to the Lottery Tuition Fund back to the TSPF (however, this language was vetoed); and
- New language replacing the appropriation to CYFD with TANF funds.
- In FY15, 50 percent of the MSA revenue is transferred to the Tobacco Settlement Program Fund; the remainder is transferred to the permanent fund.

MSA Payment Determination

- Base payment increased annually for inflation factor – greater of CPI or 3 percent.
- Payments are reduced if participating manufacturers lose market share.
- Some PM’s began withholding payments in 2006, arguing the states are not enforcing the MSA: PM withholding has ranged from \$3 million to over \$6 million per year.
- Settlement/litigation risks: ongoing litigation is a negative risk to annual payments.

MSA Revenue Forecast Assumptions

- Inflation factor = 3 percent (IHS/Global Insight forecast of inflation is below 3 percent)
- Volume adjustment -2.2 percent
- PM withholding: \$4.4 million per year in FY15.

MSA Revenue Forecast Summary

	FY12	FY13	FY14	FY15	FY16
	Actual	Actual	Actual	Forecast	Forecast
Net Revenue	\$39.3	\$39.0	\$21.1	\$39.9	\$40.1

MSA Revenue Budget Challenge

- MSA revenue is unpredictable.
- Actual revenue is not known until April and not distributed until the end of the fiscal year.
- Appropriations must be determined prior to actual amounts being available.