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**MINUTES
of the
FIFTH MEETING
of the
TOBACCO SETTLEMENT REVENUE OVERSIGHT COMMITTEE**

**November 6, 2014
State Capitol, Room 321
Santa Fe**

The fifth meeting of the Tobacco Settlement Revenue Oversight Committee (TSROC) was called to order by Senator Cisco McSorley, co-chair, on November 6, 2014 at 9:30 a.m. in Room 321 of the State Capitol in Santa Fe.

Present
Sen. Cisco McSorley, Co-Chair
Rep. Jim R. Trujillo
Rep. Monica Youngblood

Absent
Rep. Elizabeth "Liz" Thomson, Co-Chair
Sen. John C. Ryan
Sen. John Arthur Smith

Advisory Members
Rep. Kelly K. Fajardo
Sen. Linda M. Lopez*
Sen. Mary Kay Papen

Rep. Paul C. Bandy
Rep. Gail Chasey

* Senator Lopez was appointed by Senate President Pro Tempore Papen as a voting member to constitute a quorum.

Staff
Caela Baker, Staff Attorney, Legislative Council Service (LCS)
Michelle Jaschke, Researcher, LCS
Julio Garcia, Intern, LCS

Guests
The guest list is in the meeting file.

Handouts
All handouts and other written testimony are in the meeting file.

<u>Thursday, November 6</u>

Welcome and Introductions
Senator McSorley welcomed committee members and guests.

Tobacco Settlement Permanent Fund (TSPF) Asset Allocation

Steven K. Moise, state investment officer, State Investment Council (SIC), and Vince Smith, deputy state investment officer, SIC, presented TSPF investment performance information and recommendations for TSPF asset allocation. Mr. Moise reported that TSPF assets amounted to $192.1 million as of September 30, 2014 and that the fund had an investment return rate of 11.88 percent for the year ending September 30, 2014. He observed that this represents a growth of $13.5 million in the fund over the last 12 months. A total of $29.4 million was distributed from the fund in June 2014, a total of $8.2 million above the reduced annual settlement amount. Mr. Moise informed the committee that this is the first time that the corpus of the fund has been used to satisfy appropriations.

Mr. Smith reviewed the fiscal year (FY) 2014 TSPF investment performance and provided data projecting that investment returns will drop dramatically over the next 10 years. He stated that if the committee is willing to move the fund in another direction, the TSPF will get better returns by diversifying assets and allocating more to private equity investments. Mr. Smith identified the reserve status of the fund and the uncertainties that remain with regard to pending tobacco settlement litigation as major issues affecting TSPF returns on investment. He also noted that no new funds have been added to the TSPF since FY 2008 and that the practice of zero contributions makes it difficult to grow the corpus of the fund.

Several options to improve the health of the TSPF were discussed by the committee. Mr. Smith reported that the SIC suggests that the fund be removed from reserve status and managed as a true permanent fund. In addition, the SIC recommends reinvesting fully half of the proceeds from the tobacco settlement revenue into the corpus of the TSPF and creating a revenue stream, perhaps from tobacco surcharges or taxes, to feed the corpus of the fund. These changes would require legislative action, according to Mr. Smith.

Peter B. van Moorsel, chief economist, Legislative Finance Committee (LFC), responded to members' questions regarding repayment of TSPF funds "borrowed" by the general fund. Mr. van Moorsel reported that for a period of five years (FY 2009 through FY 2013), 50 percent of the Master Settlement Agreement (MSA) funds that feed the TSPF were used to satisfy general fund obligations, a diversion of approximately $100 million. Ms. Baker presented a report on TSPF appropriations showing fund outflows, including nonrecurring program costs in FY 2014 and prior years. She reported that much of the TSPF money that was diverted during that five-year period was used to ensure Medicaid solvency.

Committee members and the SIC panelists discussed where the fund would be if the 50 percent of fund proceeds that were to have fed the fund had not been diverted, including calculating the income that would have been earned from the diverted $100 million. The committee also sought to include in its calculation the lost future returns on investment as efforts are made to restore the fund and the additional amount needed for the corpus of the fund to enable restoration of certain funding cuts that have been made in program appropriations.

Members and the SIC representatives discussed a plan to add $53 million per year to the corpus of the TSPF over a period of five years to restore the fund. Mr. Smith reported that the

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SIC estimates that with restoration of the fund and enactment of the proposed statutory changes to the TSPF, the fund has a 50 percent chance of maintaining a 6.6 percent rate of return over time. Panelists agreed that the relatively high rates of return previously enjoyed by the fund are not projected to continue. Members discussed possibilities for sponsorship of the proposed legislation, and the co-chair asked that the likely sponsors meet with the LFC and the SIC to discuss proposals to restore the fund, to change the reserve status of the TSPF and to modify the fund's asset allocations.

Tobacco Settlement Permanent and Program Funds; Revenue Projections

Mr. van Moorsel presented a tobacco settlement revenue update and projections for FY 2015 and FY 2016. He reported that the MSA revenue that flows to the TSPF decreased in FY 2014 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 FY 2014 payment of $21.2 million was below the $39.3 million received in FY 2013. MSA revenue in FY 2015 is projected to be $39.9 million, and revenue in FY 2016 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.

The General Appropriation Act of 2014 included contingency language to ensure that programs funded with tobacco MSA funds are kept whole in the event of revenue reductions pursuant to a legal challenge. Any shortfall in MSA funds would be made up with a transfer from the TSPF. Mr. van Moorsel observed that the MSA revenue amounts are unpredictable and present a budgeting challenge because appropriations must be determined prior to knowing the actual amount of MSA revenue that will be available.

Proposed Legislation for Committee Endorsement

Ms. Baker presented two versions of legislation to prohibit the sale of electronic nicotine delivery devices to minors. One of the bills was a duplicate of House Bill 15 from the 2014 legislative session. The co-chair asked Ms. Baker to address the differences between the two bills. Ms. Baker stated that the bills differ in that one defines and uses the term "e-cigarette" whereas the other bill defines "tobacco product" to include e-cigarettes. In addition, one bill would provide an exemption for the use of tobacco products in connection with the practice of cultural or ceremonial activities by Native Americans and would also restrict vending machine sales of tobacco products to age-controlled locations where minors are not permitted, eliminating other venues for vending machine sales. Representative Youngblood reported that the legislation that she will sponsor is unchanged from last year, and she asked for the committee's endorsement of that version of the bill over the newly presented legislation. Following further discussion, Representative Youngblood agreed to include the exemption for the use of tobacco products in connection with the practice of cultural or ceremonial activities by Native Americans and the changes concerning vending machines.

The co-chair asked for public comment on the proposed legislation. Chris Croom, representing an e-cigarette trade organization, asked that e-cigarettes not be labeled as tobacco products. He observed that 36 other states have banned sales to minors without defining

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electronic cigarettes as tobacco products. Scott Scanland, representing Altria, stated that defining electronic cigarettes as tobacco products may help to remove stumbling blocks that prevented the legislation from passing last year. Sandra Adondakis, American Cancer Society Cancer Action Network, spoke in support of the new definition of electronic cigarettes as tobacco products, noting that the federal Food and Drug Administration has already stated that it is planning to come out with a ruling next spring that will establish this definition at the federal level.

Stephen Beckers, representing another trade organization that represents more than 125,000 e-cigarette users, stated that he has been in business since 2009 and that the industry is opposed to sales to minors. He reported that the industry's products offer the potential to use nicotine products, but only about one-third of users actually use the products for nicotine delivery. Mr. Beckers asserted that it is the chemicals and other cancer-causing agents in cigarettes and not necessarily the nicotine contained therein that make cigarettes addictive and a risk to health.

On a motion made and seconded, the committee voted three to one to endorse Representative Youngblood's version of the proposed legislation, amended to include the exemption for the use of tobacco products in connection with the practice of cultural or ceremonial activities by Native Americans and the changes related to vending machines.

On a motion made and seconded, the committee considered endorsement of the other proposed bill to prohibit the sales of electronic delivery devices to minors. The motion failed on a vote of two to two.

Ms. Baker presented proposed legislation that would amend the Tobacco Products Tax Act to impose a tax on nicotine products and require nicotine content labeling for nicotine products. The name of the act would be changed to the Tobacco and Nicotine Products Tax Act (TNPTA). The proposed act defines "electronic delivery devices" and the nicotine products used in such devices. The TNPTA would impose a tax of $0.04 per milligram of nicotine contained in nicotine products.

Mr. Croom objected to the proposed taxation as excessive and prohibitively expensive for users. Ms. Adondakis reported that by her calculation, the tax amounts to only one-half of that imposed on other tobacco products. Hector Dorbecker, economist, LFC, clarified that the proposed level of taxation is gauged to reflect the same level of taxation as that currently imposed on tobacco products, based on a comparison of the amount of nicotine in the products. Discussion ensued about how the tax would be calculated, and the co-chair noted that the tax is based only on the amount of nicotine contained in the nicotine products, not on the total volume of the product. The co-chair stated that he would sponsor the proposed legislation in the upcoming legislative session. Mr. Beckers expressed support for the legislation but asserted that the industry would like to see the tax revenue go directly to fund cancer projects.

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On a motion made and seconded, the committee voted unanimously to endorse the proposed legislation. The co-chair agreed to work with interested parties to finesse the language of the bill to ensure appropriate labeling requirements and to address related stakeholder concerns.

Pamelya Herndon, executive director, Southwest Women's Law Center, presented information on the Breast and Cervical Cancer Early Detection Program (BCCEDP). She explained that new 3-D mammography provides important and potentially life-saving early detection opportunities. Ms. Herndon asked for the committee's support for a $1.2 million increase in funding for the BCCEDP for a period of at least one year to enable access to the new technology for low-income women served by the project.

Members discussed the constraints of the TSPF budget as they attempted to adjust funding to meet the request for additional resources for early detection of breast and cervical cancer. Ms. Baker informed the committee that funding for the Family Infant Toddler Program is a new request for FY 2016 funding. On a motion made and seconded, the committee voted unanimously to recommend the same funding levels as last year with the following adjustments: move $1 million in funding from the Medicaid line item to the BCCEDP line item for 3-D mammography; and add $5 million in funding for the Family Infant Toddler Program for FY 2016.

On a motion made and seconded, the committee voted unanimously to approve the minutes of the meeting of October 14, 2014.

Adjournment

There being no further business before the committee, the fifth meeting of the TSROC for the 2014 interim adjourned at 1:05 p.m.

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