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## **The Commerce Committee Manager's Package will Dramatically Reduce Youth Smoking**

The Commerce Committee manager's package contains significant improvements over the underlying bill which will help to reduce youth smoking and to protect the public health. With these improvements, the bill meets each of the President's principles for comprehensive tobacco legislation. The improvements include:

### **Tougher Lookback Surcharges:**

- The manager's amendment contains an uncapped company-specific surcharge of \$1,000 per youth smoker for every youth smoker by which the company misses its youth smoking targets. This surcharge represents twice the lifetime profits that a company earns from any youth smoker. The companies will not be able to pass these company-specific surcharges onto price, because any price differential between companies will dramatically affect their share of the adult market.

At the levels specified in the manager's amendment, company specific surcharges will reduce profits by \$640 million for every 10 points. The Treasury Department and OMB estimate that a 20-point miss in 2003 would represent one-third of total industry profits. By affecting their bottom line in this dramatic fashion, the company-specific surcharges in the manager's amendment will provide a significant incentive for tobacco companies to change their behavior and reduce sales to children.

- The manager's package also raises the cap on industry-wide lookback surcharges from \$3.5 billion per year to \$4 billion per year. The Treasury Department and OMB estimate that if targets are not met and the full \$4 billion industry-wide surcharge is levied, the price of a pack of cigarettes will rise by about 35 cents.

### **Enhanced Environmental Tobacco Smoke Protections:**

- The manager's package provides that a state can opt out of the national environmental tobacco smoke standard only if the state is able to demonstrate to OSHA that it has an ETS standard at least as protective of the public's health.

### **Spending:**

- The manager's package contains key provisions to fund important public health programs, health research, and assistance for farmers. It also provides funding to states to be used for a variety of programs, including child care.
- Approximately 22 percent of expected revenues from the legislation will go to fund research at NIH, CDC, and AHCPR. Another 22 percent will fund smoking cessation programs, prevention and education programs, international tobacco control efforts, and a variety of enforcement efforts at both the federal and state levels to minimize smuggling and crack down on retailers who sell tobacco products to children. All proceeds from lookback surcharges will go to prevention and education programs.

- Forty percent of expected revenues will go to states, with half unrestricted and half to be used for designated purposes -- the Child Care and Development Block Grant, the Safe and Drug-Free Schools Program, Eisenhower Grants, child welfare programs (Title IV-B), the Maternal and Child Health Bureau's Title V Program, Substance Abuse grant programs, and a limited match for the Children's Health Insurance Program. This entire list is directed at the health and well-being of children and families most in need of assistance.
- The remainder of expected revenues from the legislation will go to protect tobacco farmers and to provide assistance to their communities, through the mechanisms of the LEAF Act.
- Excess revenues will go to the Medicare program.

#### **Improved Liability Provisions:**

- The manager's package ensures that the bill's liability provisions (i.e., the settlement of state lawsuits and the annual damages cap) apply only to companies that agree to accept sweeping advertising restrictions and to comply with important provisions of the law (i.e., lookbacks and annual payments), even if those provisions are invalidated by the courts.
- The manager's package raises the annual liability cap from \$6.5 to \$8 billion (indexed for inflation), the same amount as the cap in the Chafee-Harkin bill. It also removes liability protections for parent companies and affiliates; ensures that the industry's attorneys will be subject to suit as under current law; and allows plaintiffs claiming injury from disease to use evidence of addiction in their lawsuits.
- The manager's package strengthens the provisions in the bill that link liability protections to the achievement of youth smoking targets. Under the amended legislation, a company that misses its targets by 20 percent or more has the burden of showing both that it did not engage in affirmative misconduct and that it used best efforts to reduce youth smoking in order to escape the loss of liability protections.

#### **Elimination of Antitrust Exemption:**

- The manager's package eliminates the blanket antitrust exemption contained in the underlying bill, which was not necessary to achieve the goals of the legislation and could have had anticompetitive effects.

### **Stronger Anti-Smuggling Provisions:**

- The manager's amendment will strengthen the anti-smuggling provisions in the bill, so as to prevent the emergence of contraband markets. The bill, as amended, will create a "closed distribution system" for tobacco products so that only licensed entities can sell or buy products; it will provide states with resources to establish or improve retail licensing systems; it will require manufacturers to mark packages for export to prevent their diversion; and it will establish and enforce strong penalties for violations. A very similar system has worked to control smuggling of alcoholic beverages for over sixty years.

## **Company-Specific Youth Lookback Surcharge will Change Industry Behavior**

The uncapped company-by-company surcharge of \$1,000 per youth smoker contained in the Commerce Committee manager's package will provide a significant incentive for tobacco companies to change their behavior and reduce sales to children. Industrywide surcharges are passed directly to price, and are designed to drive up the price to discourage teens from smoking. Company-specific surcharges are designed not to drive up the price of cigarettes, but to come straight out of the companies' bottom line if they sell to children. Companies cannot pass company-specific surcharges onto price, because any price differential between companies will dramatically affect their share of the adult market.

- Without a company-specific surcharge, any company can still make a profit by selling to kids. The \$1,000 per youth smoker surcharge contained in the manager's amendment will force a company to surrender twice the lifetime profits it makes from addicting a teen in the first place.
- This penalty is uncapped, and will take a large bite out of after-tax profits. The total after-tax profits of the domestic tobacco industry are \$5 billion (\$7.5 billion pre-tax). The Department of Treasury estimates that after-tax profits will drop to about \$3.4 billion by 2003 (in constant dollars) under the McCain bill. The company-specific surcharges reduce the companies profits by about \$640 million for every 10 points. A 30-point miss would reduce profits by over \$1.9 billion, which is more than half of projected profits. A 60-point miss would reduce profits by \$3.8 billion, which amounts to more than projected total profits.
- These penalties are large enough to prevent companies from being able to pass them onto price. Assume, for example, that the total volume of cigarettes sold in 2003 is 15 million packs (about halfway between CBO and OMB estimates). Because Philip Morris's market share is 50%, or 7.5 million packs, a 30-point miss would cost the company about \$1.2 billion. If Philip Morris passed that amount along to price, it would have to raise the price of Marlboros by 16 cents a pack, or \$1.60 a carton. A similar price differential between Philip Morris and RJR cigarettes in 1993 cost RJR so much of its adult market share that the company has never recovered.
- In addition, any company that misses its targets by more than 20% stands a significant chance of losing its liability protections altogether under the manager's amendment. As amended, the bill provides that a company that misses its targets by this amount has the burden of showing both that it did not engage in affirmative misconduct and that it used best efforts to reduce youth smoking in order to escape the loss of liability protections.

## Lookback Surcharges Are Constitutional

Opponents of lookback surcharges have argued that the Constitution -- principally, the substantive component of the Fifth Amendment due process guarantee -- prohibits collection of these surcharges unless the government:

- obtains company consent to the lookback regime, or
- exempts companies that have taken specified steps to discourage youth consumption of their products.

We believe that lookback surcharges can be imposed without consent or without a system for exempting companies who demonstrate that they took specified actions to reduce tobacco consumption by minors.

Congress possesses broad authority to enact legislation adjusting the "burdens and benefits of economic life"; the "burden is on the one complaining of a due process violation to establish that the legislature has acted in an arbitrary and irrational way." Usery v. Turner Elkhorn Mining Co., 428 U.S. 1, 15 (1976).

The McCain bill minimizes the risk of challenge by:

- Ensuring lookback provisions are primarily a mechanism for increasing prices in order to reduce underage demand and of generating revenues for programs to reduce underage smoking further and to combat its effects. If the government's purpose in imposing lookback surcharges is to increase prices and generate revenues, the refusal to permit an "innocent company" defense is plainly rational.
- Designing its provisions to make clear that altering tobacco company conduct is a secondary objective. If the government's primary purpose in imposing lookback surcharges was to induce tobacco companies to change their marketing and distribution practices, companies could plausibly (though we think incorrectly) argue that it is "arbitrary and irrational" to deny companies an opportunity to avoid surcharges by demonstrating that they took all reasonable steps to discourage youth consumption of their brands.

- Even a lookback scheme that did not allow an innocent company defense and that sought, as a primary objective, to alter company marketing and distribution practices ought to be sustained against a substantive due process challenge. Courts, under current doctrine, should accept the rationality of legislative judgments (1) that an innocent company defense would unduly undermine the deterrent effect of lookback incentives, or (2) that an innocent company defense should not be recognized because companies with excessive youth smoking rates could always do more, including imposing their own price increases, to reduce youth consumption. However, a constitutional defense along either of these lines would raise novel questions and we therefore believe that the risk of invalidation would be greater under this approach.
- Both company-specific and industry-wide surcharges can be imposed without consent. Company-specific surcharges would generate revenue (at the expense of those whose brands are used most heavily by minors) and might tend to increase price. Moreover, company-specific surcharges may be essential to the feasibility of the overall lookback scheme, since company-specific surcharges counter any incentive for individual companies to recruit new underage users at the expense of the entire industry. If company-specific lookback surcharges are designed to serve these purposes (and described accordingly), courts should not find that omission of an innocent company defense would render them arbitrary and irrational for purposes of the substantive due process doctrine.

## **Youth Smoking Survey**

### Methodology in McCain Bill Improves Upon Settlement

The ability to accurately measure youth tobacco use is an integral part of an effective system of reducing youth smoking.

The Commerce Committee Legislation contains a lookback surcharge system that is intended to ensure that, in the event that other measures contained in this Act prove to be inadequate to produce substantial reductions in tobacco use by minors, tobacco companies will pay additional assessments designed to lower youth tobacco consumption in a variety of ways: by triggering further increases in the price of tobacco products, by encouraging tobacco companies to work to meet statutory targets for reductions in youth tobacco consumption, and providing support for further reduction efforts.

As part of this system, there would be an annual survey of young people to determine the percentage that use cigarettes or smokeless tobacco. To be sure that any surcharge liability is fairly measured and not open to dispute, the Commerce Committee Legislation proposes that a new survey be conducted that would be far more accurate than current surveys that attempt to measure youth tobacco use.

As part of its June Settlement with the States Attorneys General, the tobacco industry agreed to a system of lookback surcharges where the industry's progress would be measured by a survey conducted at the University of Michigan called "Monitoring the Future." While this survey provides important data about youth tobacco use, it is not sufficient to serve as the basis of an effective lookback system.

- Because of low participation rates among schools, the results from the Michigan survey are much less reliable than those that would be produced by the survey contained in Commerce Committee Legislation.
- Because only a portion of the overall sample of the Michigan survey is used to measure cigarette use by brand, precise estimates of the number of youth people that use each manufacturer's brands of cigarettes are not possible. In addition, the Michigan survey does not collect brand data on smokeless tobacco use. The Commerce Committee Legislation will permit precise estimates of the number of young people that use each manufacturer's brands of cigarettes and smokeless tobacco.
- The survey contained in the Commerce Committee Legislation would use proven methodologies, such as computer-assisted technology, which increase respondent privacy and confidentiality. The Michigan survey does not employ such methods.

## Youth Monthly Tobacco Use is Appropriate Measure of Youth Smoking

The public health community believes that youth tobacco use should be measured based on tobacco use within the last month. This is an appropriate standard that captures a significant amount of youth tobacco use that occurs on a routine, but not daily, basis.

- Data on youth tobacco use indicate that a significant percentage of youths who are occasional users will become addicted smokers, some while they are still teens and others in early adulthood.
- Surveys indicate that about 30% of 12-17 year olds who smoked just 2-9 times in the previous 30 days had become everyday smokers 4 years later.

If we fail to capture these patterns of use when we measure youth tobacco use, the tobacco companies would have little incentive to discourage experimentation and occasional use.

In fact, the tobacco industry may find ways to game the system by targeting their ads in ways that encourage occasional use by older teens on the assumption that these teens will not progress to daily use until after age 17. The industry has demonstrated quite well its ability to target ads to segments of the youth market.

## **The Commerce Committee's Manager's Package Funds Critical Public Health, Health Research, Farmers, and State Programs**

The Commerce Committee's manager's package funds critical funding for public health, health research, farmers and farming communities, and states, including significant funds for child care.

### **Public Health Programs: 22 percent of funds (about \$14 billion/5 years)**

The bill funds critical public health programs, including tobacco prevention and education programs, cessation programs, counter-advertising, Indian health services, international tobacco control efforts, and a variety of enforcement efforts at both the federal and state levels to minimize smuggling and crack down on retailers who sell tobacco products to children.

### **Health Research Programs: 22 percent of funds (about \$14 billion/5 years)**

The bill provides 22 percent of funds for research at the National Institutes of Health, the National Science Foundation, the Centers for Disease Control, and the Agency for Health Care Policy and Research. The bill would also fund a demonstration to permit Medicare beneficiaries to participate in certain federally sponsored cancer clinical trials.

### **Farmers and Communities: 16 percent of funds (about \$10 billion/5 years)**

The bill provides 16 percent of funds to assist the transition of both flue-cured and burley tobacco growers and their communities. The bill contains \$28.5 billion for tobacco farmers and their communities over 25 years, including payments for lost tobacco quota; payments for sale of quotas; payments for community economic development block grants; a worker transition program; and higher education assistance programs.

### **Grants to States: 40 percent of funds (about \$26 billion/5 years)**

Recognizing the important role states have played in enabling this legislation, the manager's amendment provides that 40 percent of funds be transferred to the states, \$196.5 billion over 25 years, with half unrestricted and half to be used for designated programs for the health and well-being of children and families most in need:

- Child Care and Development Block Grant
- Maternal and Child Health Block Grant
- Child welfare (Title IV-B)
- Substance Abuse and Mental Health Services Administration grants
- Safe and Drug-Free Schools
- Professional Development (Eisenhower) grants
- Match for the Children's Health Insurance Program (limited to 6 percent of restricted funds)

If states were to spend their restricted funding in proportion to current federal expenditures, and use 6% for the Children's Health Insurance Program, at least 40% of the funds, or over \$5 billion over five years, would go to child care.

### **Medicare: Additional Revenues**

In the event that the bill generates more receipts than estimated, the balance of funds will be directed to the Medicare HI Trust Fund.

**The Manager's Amendment Narrows  
the Scope of Liability Protections  
for the Tobacco Industry**

Senator McCain's Manager's Amendment contains key improvements in the bill's civil liability provisions. As amended, the bill establishes a higher, \$8-billion-per-year cap on damages, which will be available only to tobacco companies that finally change the way they do business by agreeing to restrict advertising to youth and abide by the terms of the legislation rather than tying it up in court. The new version of the bill also removes special protections for parent companies of tobacco manufacturers.

**The Manager's Amendment significantly improves on the bill reported out of the Commerce Committee by:**

- Ensuring that the bill's liability provisions -- i.e., the settlement of state lawsuits and the annual damages cap -- apply only to companies that agree to accept sweeping advertising restrictions and to comply with the key terms of the law, even if those provisions are struck down;
- Raising the annual liability cap from \$6.5 billion to \$8 billion (the same amount as in the Chafee-Harkin-Graham bill), with all damage judgments to be paid by the industry;
- Strengthening the provisions in the bill that link liability protections to the achievement of youth smoking targets, by removing liability protections from a company that misses its targets by 20 percent or more unless it proves that it used best efforts to reduce youth smoking;
- Permitting suits against parent companies and affiliates of tobacco manufacturers, as well as their attorneys;
- Ensuring that individuals with tobacco-related disease can use evidence of their addiction in suits against tobacco companies; and
- Ensuring that tobacco companies cannot escape their obligations by making fraudulent transfers or declaring bankruptcy.

**Moreover, the Manager's Package retains important features of the bill reported out of Committee:**

- The bill contains no limits on class action lawsuits and does not limit the amount that anyone can recover from a tobacco company; and
- The bill assists plaintiffs who have minimal resources in suing big tobacco companies by recognizing two well established facts -- that nicotine is addictive, and that the use of tobacco causes a wide array of diseases.

## **The Commerce Committee Manager's Package Contains Tough Anti-Smuggling Provisions**

The Commerce Committee manager's package creates a strong licensing and enforcement system that will minimize smuggling by creating a closed distribution system for tobacco products, labeling all products for export, and imposing tough penalties on manufacturers and other firms involved in smuggling.

***An Effective Licensing System is the Key to a Closed Distribution System:*** To prevent black market activity, the manager's package regulates tobacco products in a manner similar to the way the federal government has regulated alcoholic beverages for over 60 years.

Under this closed distribution system, only manufacturers, wholesalers, exporters, importers, and distributors that hold a federal license would be allowed to engage in those businesses. Licenses would be issued based on certain specified criteria and could be revoked or suspended for certain specified violations. Those conducting business without a permit would be subject to civil monetary penalties of up to \$10,000 per offense, a prison term of up to five years, and property forfeiture. Tobacco companies implicated in smuggling would lose their liability protections. Licensed entities would be authorized to sell tobacco products only to other licensed entities. Licensing of retailers would be done by the states.

Additionally, all tobacco product packages would be marked with a serial number to facilitate tracking, and all exported packages will be labeled FOR EXPORT FROM THE UNITED STATES to prevent them from being smuggled back into the U.S. and sold illegally.

***A Closed Distribution System will Prevent Black Market Activity:*** A closed distribution system will ensure that products moving outside the legal channels of distribution can be easily earmarked and targeted for prosecution. This system would drastically limit smugglers' ability to enter products into a legitimate distribution channel. Potential black marketeers would not be able to move products through legitimate wholesalers or distributors. Nor would they be able to sell products to retail consumers at local convenience stores or other licensed retail outlets. Instead, without a way to place contraband in the market legally, smugglers would have to sell cigarettes outside channels of legitimate distribution. This would be very risky and criminal provisions and penalties would act as a significant deterrent to persons contemplating the unlawful diversion of tobacco products.

***Funding for Enforcement:*** The manager's amendment authorizes funding for anti-smuggling enforcement as part of the public health spending account and enables the Secretary of the Treasury to collect fees to cover enforcement costs.

## **Comprehensive Tobacco Legislation will Not Cause Bankruptcy**

Claims by the tobacco companies that the McCain bill will drive them into bankruptcy are not convincing for two key reasons. First, the legislation is designed to facilitate the pass-through of manufacturer payments to the prices of tobacco products, minimizing the impacts on the profits of the manufacturers themselves. Second, the industry has a significant cash flow and net assets to absorb the reduced volume as prices rise.

***The Payments are Made by Tobacco Consumers, Not Tobacco Manufacturers:*** The primary goal of comprehensive tobacco legislation is to reduce youth tobacco use. The single most effective means of accomplishing this goal is to raise the price of tobacco products. As a result, the McCain legislation and other bills facilitate the pass-through of industry payments to the price of tobacco products. Mechanisms such as the allocation of industry payments by market share, and volume adjustments which reduce industry payments as volumes fall, will ensure that these payments are made by consumers, not manufacturers.

***Payments Made by Tobacco Consumers Have Modest Impact on Manufacturer Profitability:*** The opinion of the objective experts at the Federal Trade Commission is that even large price increases will have little impact on profits. They find that the AG settlement, which raised prices by 62 cents, lowered the profitability of the tobacco industry by only about 15%. By their method, the \$1.10 price increase in the McCain bill would lower profitability by less than 25%.

***The Tobacco Industry Has Substantial Financial Resources:*** The U.S. tobacco industry is large, well-diversified, and financially strong; the operating earnings for the top five tobacco manufacturers was \$23.6 billion. The industry leader, Philip Morris, is particularly well positioned to absorb decreases in their domestic tobacco earnings:

- Their stock is currently valued at almost \$100 billion.
- They had \$4.7 billion in domestic tobacco operating profits in 1997.
- They also had operating profits of \$4.6 billion on their international tobacco business.
- They are also a well diversified company that has operating profits of almost \$5 billion from other lines of business such as food and beer.

Even the most vulnerable in this industry, RJR Nabisco, has substantial financial resources:

- For 1997, RJR Nabisco's domestic tobacco business had operating profits of \$1.5 billion
- The company also has a rapidly growing international business which had \$670 million in operating profits in 1997.
- In addition to their tobacco businesses, RJR Nabisco has a substantial asset: its holdings of 80 percent of Nabisco, valued at almost \$10 billion dollars. This exceeds by \$5 billion the company's outstanding debt (excluding Nabisco).

## **The McCain Bill's Price Increase will Substantially Reduce Youth Smoking and Prevent Premature Death**

The single most important step we can take to reduce youth smoking is to raise the price of a pack of cigarettes significantly. The Treasury Department analysis has found that the \$1.10 price increase in the McCain bill will, by itself, reduce youth smoking by 32% in 2003. Taken in conjunction with a conservative estimate of the impact of the other non-price provisions in the legislation, such as access and marketing restrictions, the overall impact is an average 42% reduction in youth smoking and premature deaths in every state.

### **Why do we need to significantly increase the price of cigarettes to prevent youth smoking?**

According to the Treasury Department, the per-pack price increase in the McCain bill combined with advertising and access restrictions will result in an average reduction of 42 percent in underage teenage smoking in the year 2003. The percentage reductions in underage teen smoking and resulting premature deaths range from 33-36 percent in states like Washington, Massachusetts, and Michigan, to 47-51 percent in states like Wyoming, Tennessee, and Kentucky. Fifteen states will see reductions above 45 percent in 2003.

Over the next five years, the number of young people kept from smoking would be about 3 million young people for the country as a whole. Individual states will see reductions ranging from a few thousand in the smaller states up to about 248,000 in California and 205,000 in Texas. And about a million young people will be saved from premature death, including 56,000 in Florida, 57,000 in Ohio, 37,000 in Michigan, 83,000 in California, and 24,000 in Missouri.

### **Can one million lives really be saved over 5 years if Congress passes comprehensive legislation?**

The Treasury Department's analysis shows that the McCain bill's price increase of \$1.10 per pack over five years coupled with sales and advertising restrictions will reduce underage smoking by nearly half, stopping 3 million teens from smoking and saving a million lives over the next five years. This analysis includes a conservative estimate that advertising and access provisions will reduce teen smoking by 15 percent. The rest of the reduction is attributable to the price increase.

### **Don't some experts say a price increase will have no effect on young people's behavior?**

In fact, there is a substantial consensus in the economics literature that price increases have a dramatic impact on youth smoking. The model used by the Treasury Department reflects that consensus. Indeed, an independent analysis from the Congressional Budget Office recently reviewed the literature and concluded that youth smoking is very responsive to price.

**Doesn't the international evidence contradict this contention?**

Again, the clear consensus of the U.S. literature, as confirmed by CBO, is that youths are very responsive to price in their decisions to smoke. International comparisons are much less informative for the response of youths in the U.S. to price changes. If one insists on international comparisons, perhaps the best one to use is Canada, where a doubling of the price of cigarettes over the 1981 to 1991 period led to a 50% fall in youth smoking -- almost exactly what would have been predicted by Treasury's model.

## Background on Youth Smoking Elasticity Estimates

### The Treasury Model

- The Treasury model of youth smoking starts from a participation elasticity of -0.7 at the current price level of about \$1.95 — which means that a 10% increase in price above its current level would reduce the number of teen smokers by 7%.
- But this relationship only holds for very small price changes. For larger and larger price increases, the Treasury model predicts somewhat smaller proportional reductions in teen smoking. This reflects the fact that the teens most likely to respond to price signals are also the first to be discouraged from smoking by a price increase.
- Using this model, a \$1.10 increase in the real price of cigarettes is projected to reduce youth smoking by 32%. Since a \$1.10 increase in the real price in 2003 represents a 53% rise, the associated “average” elasticity is actually -0.6.<sup>1</sup>

### Previous Academic Studies

- A number of studies have attempted to estimate the responsiveness of youth smoking in the U.S. to price changes — the participation elasticity, or the change in the number of teen smokers due to price changes. This literature is based on comparisons of youth smoking rates in high and low tax states, and on changes in youth smoking within states as tax rates change.
- The CBO recently summarized this literature by stating that most of the evidence points to participation elasticities ranging from -0.50 to -0.75. **The Treasury estimate is in the range used by the CBO.**
- The results from this literature are shown in the Table below. Because differences in elasticity estimates may be less intuitive, the table shows — for each analysis of youth smoking — the projected reduction in teen smokers from a \$1.10 price increase (along with the Treasury estimates). This approach recognizes the fact that the Treasury model allows the elasticity to decline for larger price increases.

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<sup>1</sup>The semi-logarithmic demand function underlying this analysis is based on a standard model used to predict overall cigarette demand. Under it, every dime (\$0.10) increase in price reduces demand by the same *percent*, but since it is doing so from a smaller and smaller base at each step, the *absolute* reduction in teen smoking from each 10 cent increment declines slightly.

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Study of Teen Smoking	Percent Reduction in Teen Smoking from \$1.10 Real Price Increase
Lewit, Coate, and Grossman (1981)	65%
DeCicca et al. (1998)	46%
Grossman et al. (1983)	41%
Chaloupka and Grossman (1996)	36%
CBO (midpoint)	34%
<b>Treasury</b>	<b>32%</b>
Evans and Huang (1997)	28%
Wasserman et al. (1991)	0-9%

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- It is clear that the Treasury estimate is within the range of professional consensus on this question. Indeed, our estimates are more conservative than what most of the recent work in this area would suggest.
- One study which estimates a very different response from the remainder of the literature (Wasserman et al.) focuses exclusively on the late 1970s. During this period some surveys indicate that youth smoking fell precipitously without a price increase. We believe a more appropriate interpretation of the data during the late 1970s is that youth smoking was driven down by the broader dissemination of facts about smoking's dangers. According to one major survey, only half of 12th graders saw a great risk in smoking a pack or more of cigarettes a day in 1975 — the lowest level in the survey — but this number increased by nearly 25% between 1975 and 1980. Thus, rather than indicating that price does not affect youth smoking, we believe this data shows that other things can influence teens *in addition to* price.
- This same problem has led to a misinterpretation by some of the Evans and Huang paper. As Professor William Evans of Maryland pointed out in a recent letter to the Commerce Committee, the findings of his paper have been misquoted. *As noted in the Table above, the estimate that Evans stands behind is very close to the Administration estimate.* The confusion over his findings arises from the fact that his estimates which include data from the late 1970s show a smaller youth elasticity than his estimates which focus on the 1980s and 1990s. As Prof. Evans has noted, however, the data are less reliable for this earlier period; in addition, as noted above, this was an era when non-price factors were driving teen smoking down in the face of constant prices.

## The Cornell Study

- Some have cited the recent study by DeCicca et al. as refuting the previous literature. In fact, this study finds higher estimates than the remainder of the literature when standard estimation techniques are used on their full sample of 8th-12th graders.<sup>2</sup>
- The study does find smaller effects when they choose the particular sample of 12th graders who weren't smoking in 8th grade, and try to model whether they start smoking. But there is no obvious explanation for this anomalous result; after all, removing from their model a population that is more addicted to cigarettes — individuals smoking from 8th to 12th grade — should *raise*, not *lower*, the elasticity estimate. It is troubling that dropping only 5% of their sample — the 5% of teens that are most addicted — reduces their estimate so dramatically.
- The likely explanation for this anomalous finding is problems with their empirical methodology. A recent re-analysis of their data by Professors Thomas Dee of Georgia Tech and William Evans of Maryland has found these results to be very sensitive to the particular sample restrictions imposed by the Cornell authors. As these experts note, “The results appear to be purely an artifact of the way that the authors constructed the analysis sample”. When a broader sample of observations is used, there is a very significant effect of taxes on youth smoking in their onset model - indeed, the results are quite comparable to the previous literature.
- This partly explains why the results of the Cornell study are so statistically imprecise. For example, in this particular model, they estimate that a \$1.10 price rise would reduce smoking onset by only 7%. However, given the level of statistical imprecision in their model, their findings would be equally consistent with a reduction in youth onset of 50% or more from this \$1.10 price increase — a range which encompasses the Treasury estimate, as well as their own estimates using a more straightforward methodology.
- One criticism levied by DeCicca et al. against the earlier literature is that it does not control for differences across states at a point in time that might determine youth smoking propensities; low tax states may have high smoking because of other regulatory or cultural factors. But their approach does not solve this problem; it still relies on point-in-time comparisons of smoking onset across states, making it difficult to separate out other differences across those states. Other studies address this problem much more directly. Chaloupka and Grossman (1996) do so by including a variety of state characteristics, including state anti-tobacco regulations. Evans and Huang (1997) address the problem even more directly by examining only the effect of within-state price changes on youth smoking. The fact that these estimates are so similar to that used by Treasury highlights the robustness of the conclusions, and indicates why the previous scientific consensus is not undermined by one set of anomalous results.

## International Evidence

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<sup>2</sup>The estimate cited in our Table is an average of their elasticities for 8th, 10th, and 12th graders.

- There has also been much recent attention paid to the fact that youth smoking remains high in other countries with much higher cigarette prices. In particular, Wall Street analyst Martin Feldman noted in his testimony of March 19th that youth smoking rose in the U.K. between 1988 and 1996, despite a 26% rise in the real price of cigarettes. The inference that is often drawn from this type of evidence is that higher prices won't deter youth smoking in the U.S.
- But *these international comparisons do not tell us much of anything about the response of youth in the U.S. to price changes.* The fact that youth smoking rates remain high in other countries reflects other cultural factors that influence youth to smoke, and is not a rejection of the fundamental relationship between price and demand. And increased smoking among youth in the U.K. between 1988 and 1996 may have more to do with other factors, such as a recession which raised youth unemployment rates by 25% over this period, than with changes in the price of cigarettes.
- In light of this concern, it is certainly preferable to rely on careful, controlled analysis of U.S. teen smoking than on this type of anecdotal international evidence.
- Nevertheless, if one is going to make international comparisons, then the most appropriate one would be to Canada, since it is more similar to and faces many of the same cultural influences as the U.S. The two economic studies which estimate the effects of cigarette prices on Canadian teens are both consistent with the findings in the U.S. literature — teens are not only responsive to price changes, but they are more responsive than adults. In fact, the Canadian youth elasticity estimates are higher than those for the U.S.
- Moreover, the pattern of youth smoking in Canada confirms the sensitivity of youth to price changes. In 1981, Canada had a youth smoking rate that was about 50% higher than that in the U.S. *Over the next decade, Canada raised its cigarette prices by over 100%, and teen smoking fell by almost half.* During this period there were no substantial change in teen smoking rates in the U.S., so by 1991 Canada's teen smoking rate was lower than ours. The implied Canadian elasticity of -0.42 is very close to the estimate that would be computed by the Treasury model (which allows the price responsiveness to fall as the magnitude of the price increase grows) for this large a price rise, which is an elasticity of -0.48.
- Teen smoking then rose again in Canada between 1991 and 1994, as Canada lowered dramatically its federal excise taxes. Of course, teen smoking was on the rise in the U.S. over this period as well, so it is not as easy to attribute all of the rise in Canada over this time period to price impacts. But the fact remains that *for the country most comparable to the U.S., teen smoking rates fell as prices rose, and rose as prices fell.*

## **Affirming FDA Authority to Prevent Advertising and Marketing to Children**

By reaffirming the full authority of the FDA to regulate tobacco products, S.1415 will prevent the tobacco industry from advertising and marketing to children, and establish tough access restrictions on tobacco products to stop sales to children.

***Reaffirms 1996 Rule:*** Many of the measures to reduce teen smoking and protect the public health contained in S.1415 are in the 1996 FDA rule, but have not yet gone into effect because of pending litigation. The bill would put these provisions into effect immediately, protecting American children from the dangers of smoking. These provisions include: 1) banning outdoor advertising within 1000 feet of schools and playgrounds; 2) restricting advertising to black-and-white text only except in adult only facilities or publications with predominantly adult readership; 3) prohibiting the sale or giveaway of promotional products with brand names or logos; 4) prohibiting brand-name sponsorship of sporting or entertainment events; 5) setting the minimum age for purchase of tobacco products at 18 years and requiring age verification for anyone age under 27.

***Creates a Separate Chapter for Regulating Tobacco:*** S.1415 creates a separate chapter in the Food, Drug and Cosmetic Act that gives the FDA explicit authority over access to and advertising of tobacco products, in order to ensure that FDA regulation of tobacco does not impinge on the regulation of other products.

***Establishes New Standard for Regulating Tobacco:*** Instead of requiring tobacco products to meet the traditional safety and efficacy standard required of drugs and devices, S.1415 imposes a new standard which would require FDA regulation of tobacco products to be “appropriate for the protection of public health”. This standard better meets the characteristics of tobacco products and allows the FDA to take the addiction of over 40 million Americans into account in making decisions about how to regulate these products.

***Provides Necessary Flexibility:*** Full FDA authority to regulate tobacco products provides the agency with the flexibility it needs to protect the public health. However, any FDA effort to eliminate any particular class of tobacco products or eliminate nicotine cannot go into effect for two years in order to provide Congress with an opportunity to weigh in and vote on the measure.

***Preserves State and Local Authority:*** S.1415 makes clear that except as expressly provided, states and localities may adopt and enforce tobacco product requirements that are in addition to, or more stringent than, requirements established under the Food, Drug and Cosmetic Act for tobacco products.

***Provides Full Enforcement Authority:*** S.1415 provides for the same civil and criminal penalties that the agency may use in enforcing device law.

## Summary of FDA Provisions in S.1415

- **Overview of FDA Provisions:** S. 1415 creates a separate chapter in the FDCA that explicitly gives FDA authority over access to and advertising of tobacco products. In nearly all respects this authority is comparable to the authority that FDA asserted in its 1996 rule, which asserted FDA jurisdiction over tobacco products on the ground that nicotine is an addictive drug and that cigarettes and smokeless tobacco products are combination drug/device products under the Federal Food, Drug and Cosmetic Act (FDCA). S.1415, however, created a separate chapter in order to respond to concerns raised by medical device companies that tobacco statutory interpretations and other policies issued under the device provisions of the FDCA could adversely affect those companies.

The most significant difference between S. 1415 and current law is the standard that products must meet in order to be marketed. Under current law the standard is “reasonable assurance of safety and effectiveness.” This standard obviously does not fit tobacco products because tobacco products are inherently unsafe. Therefore, S. 1414 adopts the standard of “appropriate for the protection of the public health,” which allows FDA to take into account the fact that over 40 million Americans are addicted to tobacco in making decisions about how to regulate the product.

- **1996 FDA Tobacco Rule in Effect:** S. 1415 provides that the tobacco regulation that FDA finalized in 1996 will remain in effect as though it were issued under the new law. Because the effective date of certain portions of the regulation has been delayed due to the industry’s judicial challenge to the rule, the bill would authorize FDA to establish effective dates for those provisions not yet in effect.
- **Access Restrictions:** S. 1415 authorizes FDA to establish restrictions on the sale or distribution of tobacco products. By affirming the 1996 rule’s access restrictions, the bill sets the minimum age of purchase at 18 years; requires age verification by photo ID for anyone 26 or younger; requires face-to-face sales (except for mail order sales); bans vending machines and self-service displays except in facilities where only adults are permitted; prohibits the sales of single cigarettes or “loosies”; bans free samples; and sets the minimum package size at 20 cigarettes. However, S. 1415 constrains FDA from prohibiting the sale of tobacco products in face-to-face transactions by specific categories of retail stores (such as a ban on sale of cigarettes by gas stations).
- **Advertising Restrictions and Warning Labels:** S. 1415 expressly authorizes FDA to establish restrictions related to the advertising and promotion of a tobacco product. By affirming the 1996 rule’s advertising restrictions, the bill bans outdoor advertising within 1000 feet of schools and public playgrounds; restricts advertising to black-and-white text only (publications, outdoor, point of purchase, direct mail, etc.), except in publications with a predominant adult readership or at adult only facilities; prohibits the sale or giveaways of products like caps or gym bags that carry cigarette or smokeless tobacco product brand names or logos; and prohibits brand-name sponsorship of sporting or entertainment events, but permits it in the corporate name.

S. 1415 also requires stronger and larger warning labels than existing law on tobacco

products (to replace the “Surgeon General’s warning”), and provides authority for FDA to modify the text, format, and type size requirements of these statements.

- **Submission of Health Information to the Secretary:** S. 1415 requires tobacco product manufacturers and importers, within 6 months of enactment (and annually thereafter), to submit to FDA specific categories of information relevant to FDA regulation of tobacco products.
- **Good Manufacturing Practice Requirements:** Authorizes FDA to issue regulations requiring that the methods used in, and the facilities and controls used for, the manufacture, of a tobacco product conform to good manufacturing practice (GMPs). The bill also makes explicit that the Secretary has the authority to grant either temporary or permanent exemptions or variances from a GMP requirement.
- **Performance Standards:** S. 1415 confirms FDA’s authority to issue standards for tobacco for tobacco products (for example limiting the amount of certain ingredients) if FDA determines that a standard is appropriate for protection of the public health. This authority is the same as that for devices.
  - In issuing a performance standard, FDA must consider the health effects on tobacco users as well as potential users (such as children).
  - In order to give Congress a chance to vote on any standard that eliminates all cigarettes, all smokeless tobacco products, or any similar class of tobacco products, or requires the reduction of nicotine yields of a tobacco product to zero, such a standard will not go into effect until two years after the President has notified Congress of such a standard.
- **Testing and Reporting of Tobacco Smoke Constituents:** S. 1415 directs the Secretary to issue regulations to require the testing, reporting, and disclosure of tobacco smoke constituents (e.g., tar, nicotine and carbon monoxide) and ingredients that “the Secretary determines should be disclosed to the public in order to protect the public health.”
- **Reduced Risk Tobacco Products:** S. 1415 contains a provision that allows FDA to designate a product as a “reduced risk tobacco product” if it finds that “the product will significantly reduce harm to individuals caused by a tobacco product and is otherwise appropriate to protect the public health.”

- **Preservation of State and Local Authority:** S. 1415 makes clear that except as expressly provided, states and localities may adopt and enforce tobacco product requirements that are in addition to, or more stringent than, requirements established under FDCA for tobacco products.
  - State and local requirements related to access and advertising are not preempted by the FDCA.
  - State and local requirements related to performance standards, good manufacturing practices, and other similar FDCA requirements, are preempted, but States and localities may apply for exemptions pursuant to procedures that parallel provisions in device law.
  - S.1415 modifies the Federal Cigarette Labeling and Advertising Act in order to ensure that restrictions on advertising imposed under State laws are not preempted.
- **Full Enforcement Authority:** S. 1415 provides for the same civil and criminal penalties that the agency may use in enforcing the device law. The bill also provides that FDA may issue, after an administrative hearing before an Administrative Law Judge, a no tobacco sale order prohibiting the sale of tobacco products at a particular retail outlet based on repeated violations by that outlet. The bill also imposes the same requirements for the export of tobacco products that do not meet the requirements of the FDCA that apply to devices.

## **REGULATORY AUTHORITY OVER TOBACCO PRODUCTS IS APPROPRIATELY PLACED AT FDA**

- The Food and Drug Administration (FDA) is the leading public health agency with authority to protect public health and to provide regulatory oversight of products that affect the human body, such as foods, drugs, and medical devices.
  - There are other federal public health agencies and there are other federal regulatory agencies. But FDA is the only agency that has extensive experience in both areas. This experience, combined with its recent development of the tobacco access and advertising regulations, makes it the only federal agency that can hit the ground running to implement the regulatory program to combat youth tobacco use in S. 1415.
- Under S. 1415, tobacco products fit appropriately into the regulatory framework that FDA has had in place for over sixty years.
- The scientific and regulatory expertise that resides within FDA is uniquely suited to provide the oversight that will be needed to protect the public health from the hazards of nicotine products. FDA's medical experts already evaluate and approve nicotine replacement drug and device products. In addition, regulatory offices within the agency are experienced in industry-wide product regulation.
- FDA's enforcement authorities, which S. 1415 expressly extends to tobacco products, are essential in order to protect public health. Enforcement actions are necessary to ensure that manufacturers and retailers comply with requirements such as those in the final rule issued in 1996 to protect young people from the hazards of tobacco products, and to protect the public from future violations.
- A distinctive feature of FDA's regulatory authority is the flexibility inherent in the Federal Food, Drug, and Cosmetic Act, and in the new provisions added to that Act by S. 1415, that enable FDA to swiftly and effectively address problems linked to the products for which it is responsible. As tobacco companies design new marketing campaigns or develop new products, FDA has a great amount of flexibility to respond to industry actions that could harm public health.

## **ID'S OF PURCHASERS UNDER THE AGE OF 27 MUST BE CHECKED**

- Under the FDA rule, a retailer must not sell cigarettes or smokeless tobacco to anyone under 18. Therefore, purchasers must be 18 or older.
- Under the FDA rule, retailers must require customers under the age of 27 to present a photo ID (any photo ID with a birth date is acceptable).
  - FDA's rule contains this requirement because the evidence compiled by the agency during its rulemaking showed that it is very difficult to judge the age of many teenagers and young adults simply from their appearance, partly because young people mature at different rates. To ensure that older-looking teenagers are asked for ID, it makes sense to set the requirement to check identification somewhere above 18.
  - FDA's requirement is consistent with a report prepared by twenty-six State Attorneys General recommending that the age for photo ID should be significantly higher than the minimum age of sale.
  - In addition, materials developed and distributed to retailers by the tobacco industry and leading retailer organizations specifically recommended that retailers card anyone who appears to be under 26.
- Under the FDA rule, a retailer is not required to check the ID's of regular customers who are known to be at least 18 years old every time they buy tobacco products. Retailers must check a customer's photo ID at least once to ensure that the customer is at least 18 years old.

**S. 1415 PROVIDES AMPLE OPPORTUNITY FOR CONGRESS  
TO REVIEW ANY FDA DECISION TO ELIMINATE NICOTINE  
OR A CLASS OF TOBACCO PRODUCTS**

- Because of the importance of any decision by FDA to eliminate all cigarettes, all smokeless tobacco products, or any similar class of tobacco products, or to require the reduction of nicotine yields to of a tobacco product to zero, S. 1415 recognizes that it is appropriate for Congress to have the opportunity to review such a decision and enact legislation to override it.
- S. 1415 recognizes this by requiring that FDA may not begin implementing any such standard until at least *two years* after the President notifies Congress that a final regulation imposing the restriction has been issued.
- S. 1415's provision ensures that Congress will have sufficient time and opportunity to review the standard and, if desired, vote on whether the standard should be rejected.
- FDA has no plans to use this authority, but scientific developments in the future may make its use appropriate.
- FDA has demonstrated that it would administer its authority to eliminate nicotine reasonably.
  - Although FDA had the authority to reduce or eliminate nicotine at the time it issued its tobacco regulations, the agency did not do so, because, among other reasons, there was not a sufficient scientific basis to conclude that reducing or eliminating nicotine from tobacco products would reduce tobacco use.
  - FDA's refusal to ban cigarettes or smokeless tobacco products was based in part on the significant weight the agency accorded to the risks that a black market would be created and that addicted tobacco users would suffer as a result of sudden withdrawal from nicotine-containing products.
  - FDA is required under S.1415 to take these same factors into account in promulgating any standard eliminating nicotine from tobacco products.
- S. 1415 imposes many procedural requirements on FDA before the agency can issue a performance standard eliminating nicotine from tobacco products.
  - FDA must issue a notice of proposed rulemaking, containing a finding with supporting justification that the performance standard is appropriate for protection of the public health.
  - The notice must contain proposed findings with respect to the risk of illness or injury that the standard is intended to address.

- FDA must invite interested persons to submit an existing or draft performance standard.
  - FDA must invite participation from informed persons, including industry representatives.
  - FDA must consider the risks to the health of tobacco users and non-users from elimination of nicotine, including the risk that a black market will be created.
  - FDA must, at the request of an interested party, refer the proposed standard to an advisory committee.
- A performance standard eliminating nicotine could not be issued in the absence of scientific evidence that such elimination would significantly reduce the risks of illness or injury from tobacco products.
    - Development of such evidence would require reliable information showing that elimination of nicotine would reduce the risks of tobacco use, and that the benefits of this reduction in use were not outweighed by the risks of a black market or of precipitous withdrawal by addicted tobacco users.

## S. 1415 APPROPRIATELY MAKES EXPLICIT FDA'S AUTHORITY TO RESTRICT TOBACCO PRODUCT ADVERTISING

- S. 1415 expressly provides that FDA may by regulation require that a tobacco product be restricted to sale, distribution, or use upon such conditions, *including restrictions on the access to and the advertising and promotion of the tobacco product*, if FDA determines that such regulation would be appropriate for the protection of the public health.
  - This provision has no effect on FDA's regulation of drugs and devices.
- Advertising restrictions are a critical component of FDA regulation of tobacco products.
  - Two recent, comprehensive analyses by the National Academy of Science's Institute of Medicine and the Surgeon General found that tobacco advertising plays a significant role in the decisions of young people to use cigarettes and smokeless tobacco.
    - The two studies are the Institute of Medicine's Report, *Growing Up Tobacco Free, Preventing Nicotine Addiction in Children and Youth* (1994), see especially chapter 4; and the Department of Health and Human Services' Centers for Disease Control and Prevention's Report, *Preventing Tobacco Use Among Young People, A Report of the Surgeon General* (1994), see especially chapter 5.
    - The Institute of Medicine's 1998 Report, *Taking Action to Reduce Tobacco Use* (1998) reaffirms the 1994 IOM Report.
  - In addition, the nation's largest psychological association, the American Psychological Association, concluded that tobacco advertising "plays directly to the factors" that are most appealing to youth.
  - During its rulemaking, FDA found, based on the evidence and comments received, that comprehensive advertising restrictions are necessary to ensure that the access restrictions on access are not undermined by the product appeal that advertising for these products creates for young people.
    - Otherwise, tobacco companies will continue to use advertising to appeal to kids, associating tobacco with fun, sex, glamour, and sports. As long as the tobacco companies are allowed to advertise to kids and create a demand for tobacco products, it will be impossible to effectively address the problem of youth tobacco use.

- FDA also concluded that *both* access *and* advertising restrictions are necessary to meet public health goals because they are complementary —
  - The effectiveness of access restrictions on youth access would be substantially diminished if the manufacturers were free to entice children and adolescents to circumvent the access restrictions.
- Because advertising restrictions are so critical, the agency's authority in this area should not be left ambiguous and open to lengthy court challenges.

**S. 1415 ENSURES THAT FDA WILL ADEQUATELY CONSIDER WHETHER A PROPOSED REGULATORY ACTION WILL RESULT IN HEIGHTENED DEMAND FOR CONTRABAND**

- S. 1415 requires that FDA find that regulations to be imposed on a tobacco product “are appropriate for the protection of the public health.”
  - In making this finding, FDA is directed to consider the risks and benefits to the population as a whole, including users and nonusers of the tobacco product, and
  - Taking into account the increased or decreased likelihood that: (1) existing users of tobacco products will stop using such products, and (2) those who do not use tobacco products will initiate use.
  - FDA is to weigh a variety of consequences resulting from possible new regulations on tobacco products, *including the use of contraband products and the development of black markets*, and consider the effects of the regulation on both users and nonusers of the products.
  - This standard is not be applied to any other product regulated under the Federal Food, Drug, and Cosmetic Act.
- Requiring FDA to affirmatively *find* that a particular regulatory action will not result in the heightened demand for contraband would severely restrict the Agency’s authority as it would be forced to prove an unknown.
  - It could be very difficult to prove a negative—that a black market will not occur.
  - If FDA makes the finding, its decision would be delayed by extended litigation.
- FDA’s 1996 tobacco rule reflects the agency’s consideration of the contraband issue:
  - Considering the large number of Americans who are currently addicted to nicotine, FDA determined that a ban on cigarettes and smokeless tobacco would unlikely be effective in protecting consumers from the serious risks of these products. FDA found that black markets and smuggling could develop, offering products that likely “would be even more dangerous than those currently marketed.”

- FDA concluded that, to address effectively the death and disease caused by cigarettes and smokeless tobacco, addiction to these products must be eliminated or substantially reduced.
- FDA found that this goal could be achieved best by preventing minors from beginning use of tobacco products, and not by banning the products.

**GREGG AMENDMENT MAKES IT HARDER TO STOP TOBACCO ADVERTISING  
AND HARDER TO CHANGE THE WAY TOBACCO COMPANIES DO BUSINESS**

- **The McCain Bill Gives No Immunity to Tobacco Companies**

The bill passed by the Senate Commerce Committee did away with most of the major liability limitations of the June 20th settlement between the tobacco companies and the attorneys general, which had banned class action lawsuits and punitive damages. The manager's amendment went even further, by eliminating special protections for tobacco parent companies and affiliates, ensuring that the industry's attorneys will be subject to suit as under current law, and allowing plaintiffs claiming injury from disease to use evidence of addiction in their lawsuits. Under the McCain bill, anybody can sue the tobacco companies, and get whatever damages a jury will award.

- **The Cap Is Available Only to Companies that Agree to Make Sweeping Advertising Restrictions and Comply with the Law, not Challenge It in Court**

No company will be eligible for the annual damages cap unless it agrees to sweeping changes in the way it does business. To be eligible, a company must sign a binding protocol that requires it to:

- **Accept sweeping restrictions on advertising that would otherwise be unconstitutional under the First Amendment. Tobacco advertising is one of the most important factors in luring young people to start smoking. A recent study in the Journal of the American Medical Association estimated that 34% of young people start smoking because of tobacco advertising and marketing. The First Amendment limits what government can do to stop the tobacco companies' harmful advertising practices without the companies' consent. To qualify for the cap in the McCain bill, a tobacco company must agree to give up advertising that contains any human or animal image or cartoon character, all outdoor advertising, advertising on the Internet, and much more. The protocol in the McCain bill is the only way to get rid of the Marlboro Man, and ensure that Joe Camel never comes after our kids again.**
- **Comply with the terms of the legislation, not tie in up in court. Tobacco legislation will be far more successful in its central goal -- reducing youth smoking -- if the companies cooperate instead of tying the bill up in court for decades. Under the protocol in the McCain bill, a company must agree to abide by the rules of the legislation, not file endless legal challenges to thwart its intent. Participating companies must agree to make payments and lookback surcharges even if those provisions are struck down in court.**

- **The Cap Is a Powerful Incentive for Companies to Change Their Behavior, Because Any Company That Doesn't Play by the Rules Will Lose Eligibility.**

Without any incentive to sign onto the protocol, companies are bound to go to court to strike down every part of the tobacco bill they can. But under the McCain bill, once a company has signed the protocol, the government will have a powerful tool to make that company change its ways or lose liability relief altogether. A participating company will lose eligibility for the cap if it violates the protocol. For example:

- **A Company Must Make Dramatic Reductions in Youth Smoking or Lose Eligibility for the Liability Cap.** The manager's amendment strengthened the provisions in the bill that link liability protection to the achievement of youth smoking targets. Under the amended legislation, a company that misses its youth smoking targets by 20 percent or more has the burden of showing both that it did not engage in affirmative misconduct and that it used best efforts to reduce youth smoking in order to escape the loss of liability protections. **The cap is in effect a powerful company-specific penalty to ensure that youth smoking goes down.**
- **Any Company Caught Smuggling Will Lose Eligibility for the Cap.** Most anti-smuggling experts agree that it would be extremely difficult for smuggling to occur on a massive scale without the company's knowledge. Under the McCain bill, if a company's management is found guilty of taking part in a smuggling scheme, the company will lose any liability relief. This will serve as a powerful and necessary incentive to keep tobacco companies from orchestrating a black market.
- **The Cap in S. 1415 Is Even Tougher on Tobacco Companies than the Cap in the Highly-Regarded Chafee-Harkin-Graham Bill**

Senators Chafee, Harkin, and Graham sponsored a tough, comprehensive tobacco bill that also includes an \$8 billion liability cap as a way to get tobacco companies to stop marketing to children. Under that bill, tobacco companies were able to pay \$4 billion a year in judgments out of their annual payments to the government. Under the McCain bill, the tobacco companies would have to pay every penny of damage awards -- up to \$8 billion a year, indexed for inflation -- on top of their annual payments.

## TALKING POINTS ON WHAT'S NOT IN TITLE XIV

### \* **Title XIV Does Not Limit The Tobacco Companies' Liability**

Participating manufacturers who comply with the rigorous restrictions in the protocol and the other requirements of Title XIV have their liability limited to \$8 billion per year. If they owe more than \$8 billion in a given year, they will simply have to pay the additional amount in the next year.

### \* **The Bill Does Not Prevent or Limit Anyone From Recovering**

Every dollar that a person wins in a lawsuit against the tobacco industry will be paid. The bill does not limit the amounts that people can win. It only postpones payment until the next year if the tobacco companies owe more than \$8 billion in a given year.

### \* **The Bill Does Not Limit A Person Who Claims that They Are Addicted From Recovering**

The bill provides for extensive smoking cessation and other public health programs. The bill eliminates lawsuits against participating manufacturer only if those suits seek to create public health programs, such as smoking cessation programs. It does not limit any person from recovering any damages that they themselves have suffered.

### \* **The Bill Does Not Limit the Evidence that May Be Discovered or Introduced Against Tobacco Companies**

The Manager's Amendment removed provisions that would prevent plaintiffs from discovering or introducing in court evidence of reduced-risk tobacco products

### \* **The Bill Does Not Limit Tobacco Companies' Obligation to Produce Documents in Litigation**

The Manager's Amendment removed a provision that might have allowed the tobacco industry to avoid its obligation to produce documents in lawsuits. Under the Manager's Amendment, a person wishing to sue a tobacco company may review documents publicly disclosed under Title IX of the bill and may seek documents in discovery

### \* **The Bill Does Not Protect Attorneys, Advertising Agents, or Parent Companies**

The Manager's Amendment expressly allows lawsuits against tobacco manufacturers and their parent companies. It does not change current law with respect to suits against attorneys and advertising agents, and thus does not preclude such suits.

### \* **The Bill Allows Class Actions and Third-party Claims to Go Forward**

### \* **The Bill Does Not Limit Recovery for Punitive Damages**

## **Low Income Groups See Smallest Rise in Spending and Greatest Benefits from McCain Bill**

### ***Lower Income Adults Are Most Responsive to Price***

- Two recent studies have evaluated the effect of cigarette prices on smoking participation (the decision to smoke at all), and have documented an important fact: the smoking participation decision of lower income adults is much more responsive to price than that of higher income adults. In particular, both studies find that those individuals at the median income or below are *more than four times as likely* to not smoke in response to price increases as are those individuals above median income.<sup>3</sup>
- The professional consensus is that for every 10% rise in cigarette prices, there is a roughly 4.5% decline in the total number of packs of cigarettes consumed. These studies find that individuals at the median income or below are more than 50% more responsive to price in their smoking decisions than the overall average. This implies that every 10% rise in cigarette prices will cause the number of packs consumed to fall by about 7%.<sup>4</sup>
- Using this elasticity, estimates show that there is a 33% reduction in smoking for those at the median income or below from the \$1.10 price increase, as compared to the 23% reduction on average, and only about an 8% reduction above median income.

### ***So Lower Income Families Will See Only a Modest Increase in Spending on Cigarettes***

- The implications of this finding are that the price increases in the McCain legislation will not cause a significant increase in cigarette spending for lower income individuals. This is because, on average across individuals at or below the median income, for every two packs on which this group spends an extra \$1.10, there will be one pack on which they save the \$2 base price.
- These effects roughly cancel, resulting on net in only a small increase in spending on cigarettes in this population. In particular, total spending on cigarettes, on average, for a median income family will rise by only about 3%. This is only about \$20 per year for a median income smoker.

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<sup>3</sup>Ringel, J. and W. Evans, "Public Finance Aspects of the Global Tobacco Settlement", Working Paper, University of Maryland, 1998; Farelly, M., J. Bray, T. Pechacek, and T. Woolery, "The Response to Increases in Cigarette Prices by Race, Income, and Age Groups," Working Paper, Research Triangle Institute, 1998.

<sup>4</sup>These studies focus only on the smoking participation decision. But a conservative assumption is that the number of packs per smoker will follow the same income relationship. This is conservative because it is likely that the first source of response by lower income smokers will be to reduce packs rather than to quit altogether.

### ***Lower Income Groups Will Benefit Disproportionately from Cessation Spending***

- An important use of the funds raised by the McCain bill is to fund increased cessation spending so that those smokers who want to quit this addictive habit can do so.
- Unfortunately, cessation treatment can be expensive - more expensive in the short run than the cost of cigarettes. As a result, it is low income individuals who are least likely to avail themselves of cessation treatment.
- Thus, increased cessation spending should benefit lower income groups the most, since these are the individuals who cannot afford cessation treatments now.
- Cessation programs have been shown to be effective in reducing smoking. This reduction will produce further savings for lower income groups in particular, since they will not be spending their hard-earned income on cigarettes.

### ***Low Income People Will Gain More in Health Terms:***

- As noted above, recent evidence indicates that lower income individuals are more responsive to price increases than are those above median income. As a result, they will benefit disproportionately from the health benefits that come from reduced smoking.
- In particular, the number of packs smoked in families with incomes below the median income will fall by 33 %, while the number of packs smoked by families with incomes above the median will fall by only 8%. This means that the *health benefits will be 4 times as large* for lower income families as for higher income families.
- Moreover, lower-income individuals spend a higher percentage of their income on health costs. They therefore stand to gain the most from reducing smoking-related health costs.

**FORD APPROACH IS BEST FOR PUBLIC HEALTH, PROTECTS FARMERS,  
AND AVOIDS HANDING A WINDFALL PROFIT TO TOBACCO INDUSTRY**

- **Lugar Bill Would Require Drastic Cuts in Health Spending**

The Lugar bill requires the government to “buy-out” farmers from the quota program over a three-year period (FY1999 through 2002). The cost of this buy-out over the three years is \$18 billion dollars. **If the Lugar farmer spending is added and state spending is kept the same, the McCain Manager’s Amendment spending on health research and public health programs would have to be cut by 69 percent to make up the difference.** (See chart below). In contrast, the Ford-Hollings approach costs \$2.1 billion a year during those years and has no effect on the levels of spending in the McCain Amendment for NIH research, cessation, prevention, education and enforcement efforts.

- **Ford Limits Amount of Tobacco Grown; Lugar Dramatically Increases U.S. Production**

Senator Ford’s bill (LEAF Act) maintains limits on the amount of tobacco that can be grown in the United States. Under the competing Lugar approach, very large producers would quickly expand their production. A U.S. Department of Agriculture analysis concludes production of flue-cured tobacco is likely to increase by as much as 50% and burley tobacco is projected to increase by as much as 20%. That is one reason why the Campaign for Tobacco-Free Kids, the American Cancer Society, and the American Heart Association support continuation of the tobacco program.

- **Ford-Hollings Protects Small and Minority Farms**

The increased production with lower profit margins under the Lugar approach will benefit large corporate farmers, however, the legislation would have a disproportionately adverse impact on minority and limited-resource tobacco producers. Market uncertainties and reduced margins on small sales will destabilize many family farming operations. This will have a particularly harsh effect on small African-American farms -- fully 90% of African-American farms have sales of less than \$25,000.

- **Lugar Leads to a Financial Windfall for Companies**

The creation of a free market in tobacco production will dramatically lower the prices the companies will pay to buy tobacco. USDA estimates that under the Lugar bill, the price of flue-cured tobacco would fall from \$1.72 a pound to \$1.15, and the price of burley would plummet from \$1.89 to \$1.35. Given that the companies average almost 1.5 billion pounds of purchases a year, USDA estimates a financial windfall by the companies of at least \$800 million annually or \$20 billion over 25 years. The Ford approach is consistent with the overall tobacco control legislation. It avoids generating windfall profits for the tobacco companies with which the companies will offset the payments designed to force them to reduce youth smoking rates.

## Lugar Bill Cuts Health Spending by 69 Percent

	NIH and Other Research	Public Health, including Cessation, Prevention, Education, and Enforcement
<b>Total, FY 1999-2001</b>		
<b>Ford-Hollings</b>	\$8.6 billion	\$8.6 billion
<b>Lugar</b>	\$2.7 billion	\$2.7 billion
<b>Percent Reduction</b>	- 69%	- 69%

	FY99	FY00	FY01	FY02	FY03	FY99-03
Ford-Hollings	2.5	1.8	2.0	2.0	2.2	10.5
Lugar	6.0	6.0	6.0	0.0	0.0	18.0

Based on estimates of revenue from S. 1415. Calculations assume the funding for states remains \$15.6 billion over three years under either farm proposal.

RECORD TYPE: PRESIDENTIAL (NOTES MAIL)

CREATOR: Elena Kagan ( CN=Elena Kagan/OU=OPD/O=EOP [ OPD ] )

CREATION DATE/TIME:21-MAY-1998 20:10:19.00

SUBJECT: Re: Here's the compilation of all our tobacco fact sheets

TO: Cynthia A. Rice ( CN=Cynthia A. Rice/OU=OPD/O=EOP @ EOP [ OPD ] )

READ:UNKNOWN

TEXT:

make sure chief of staff's office has. thanks.

RECORD TYPE: PRESIDENTIAL (NOTES MAIL)

CREATOR: Elena Kagan ( CN=Elena Kagan/OU=OPD/O=EOP [ OPD ] )

CREATION DATE/TIME:26-MAY-1998 15:22:28.00

SUBJECT: Re: MAY 26-POVERTY MEASUREMENT MEETING

TO: Andrea Kane ( CN=Andrea Kane/OU=OPD/O=EOP @ EOP [ OPD ] )

READ:UNKNOWN

TEXT:

yes.

RECORD TYPE: PRESIDENTIAL (NOTES MAIL)

CREATOR: Elena Kagan ( CN=Elena Kagan/OU=OPD/O=EOP [ OPD ] )

CREATION DATE/TIME:27-MAY-1998 15:50:26.00

SUBJECT: Re: Diana Fortuna

TO: Paul J. Weinstein Jr. ( CN=Paul J. Weinstein Jr./OU=OPD/O=EOP @ EOP [ OPD ] )  
READ:UNKNOWN

TEXT:  
she told me; i forget if she set a date.

Paul J. Weinstein Jr.  
05/27/98 03:31:41 PM

Record Type: Record

To: Bruce N. Reed/OPD/EOP, Elena Kagan/OPD/EOP  
cc:  
Subject: Diana Fortuna

Has Diana mentioned to either of you here decision to leave? Did she tell you a date?



**Assisted Suicide Update.** Next week we plan on releasing the Justice Department interpretation that concludes that the Drug Enforcement Agency (DEA) has no legal authority to prohibit physicians from prescribing drugs with the intention of hastening death. As you will recall, Senator Hatch and Congressman Hyde had requested that the DEA/Justice determine if there was any Federal authority to address Oregon's assisted suicide law, which permits physicians to provide medications for the purposes of aiding in an assisted suicide. Consistent with your instructions, we will release this interpretation, but will also make clear that you maintain your longstanding position of opposition to assisted suicide and remain open to workable legislative approaches that address this issue. We expect that Senator Hatch and Congressman Hyde will respond by introducing legislation that provides DEA the explicit authority to press charges against physicians who assist in suicide. As you know, we believe that a DEA approach is ill-advised. We will carefully roll out the announcement of your position on this issue with both Members and interested organizations, such as the Catholic Health Association and the American Medical Association and will keep you advised of legislative developments.

**HCFA Letter to Ravenswood Hospital in Chicago.** Last week, 15 year old Christopher Sercye died of gunshot wounds just 35 feet from Ravenswood Hospital in Chicago, where friends had brought the young man for help. Hospital workers did not leave their posts and apparently would not even give police officers a stretcher to help the young man. In response, the Health Care Financing Administration sent out a letter to the President of Ravenswood Hospital on Friday stating that the hospital will lose its Medicare funding on June 19, 1998, unless the facility takes steps to ensure that the events that led to the tragic death of Christopher Sercye will not be repeated. You released a statement to highlight the Administration's strong action. In addition, your statement urges all hospitals to follow the recently released guidance by the American Hospital Association that advise hospitals to change any policies that prevent taking appropriate actions in a medical emergency.

**Medicare Commission.** Next Monday, the Medicare Commission will be holding another meeting to respond to its Members concerns that they have not had enough time to have intensive discussions about the major issues of benefits, costs, eligibility, administration, and financing. Senator Breaux, concerned about the perception of the Commission's irrelevance, has asked Senators Lott and Daschle to open up the meeting with words of encouragement on the charge and the potential of this Commission. The Democrats, including our Commission members, are becoming increasingly nervous that the Commission's staff and Congressman Thomas are focusing much too heavily on highly speculative, numbers-driven policy and much too little time on how best to reform the Medicare program to respond to the delivery challenges it faces in the next century. They therefore can be expected to urge the Commission to dedicate as much time to program design as to program financing. Our members are increasingly seeking answers from us as to how comfortable we are in allowing them to engage in serious discussions about controversial policy reforms on benefits (both in requiring higher cost sharing and more benefits like prescription drug coverage), eligibility age changes, income-related means-testing, and the possibility of putting new revenues on the table. In general, we believe that at this point it would be constructive for the Commission to engage in general discussions on all of these issues with the exception of new revenues. As for revenues, we believe our members should only address this issue until it becomes clear that traditional saving approaches alone will be insufficient to

satisfactorily address the program's financing challenges. We are working closely with Gene Sperling and the NEC to assure we have a coordinate message.

**Long Term Care.** Long term care is an issue that the aging and disability advocates are increasingly raising as a major issue that cannot continue to go unaddressed. The demographic changes in the population make clear that, in the absence of major new breakthroughs in cures and treatments, there will be an extraordinary increase in demand for services targeted to the nation's aging and disability population. Because of cost and other limitations, both the public and private sectors have been slow to develop responses to this challenge. Although comprehensive solutions are politically and financially unrealistic, we believe that we should begin a series of targeted policy options to begin to address this problem. These could include, requiring FEHBP to offer (but not pay for) private long-term care policies, educating Medicare beneficiaries that Medicare does not cover long term care and advising them of other options, developing policy options that provide more flexibility to states to provide home and community-based personal care options for Medicaid elderly and disabled eligibles, and developing possible tax incentive approaches that could potentially increase the purchase of private long-term care policies. We believe that you may want to move in this area relatively soon and capture at least part of an issue that has extraordinary political and policy dimensions.

RECORD TYPE: PRESIDENTIAL (NOTES MAIL)

CREATOR: Elena Kagan ( CN=Elena Kagan/OU=OPD/O=EOP [ OPD ] )

CREATION DATE/TIME:29-MAY-1998 15:57:29.00

SUBJECT: riggs bilingual

TO: Laura Emmett ( CN=Laura Emmett/OU=WHO/O=EOP @ EOP [ WHO ] )  
READ:UNKNOWN

TEXT:  
please print

----- Forwarded by Elena Kagan/OPD/EOP on 05/29/98 03:57  
PM -----

Michael Cohen  
05/29/98 03:55:57 PM  
Record Type: Record

To: Elena Kagan/OPD/EOP  
cc:  
Subject: riggs bilingual

===== ATTACHMENT 1 =====  
ATT CREATION TIME/DATE: 0 00:00:00.00

TEXT:  
Unable to convert ARMS\_EXT:[ATTACH.D80]MAIL43326615W.126 to ASCII,  
The following is a HEX DUMP:

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DRAFT

May 29, 1998

MEMORANDUM FOR THE PRESIDENT

FROM: BRUCE REED

SUBJECT: Riggs Bilingual Education Bill

On Thursday May 21 the House Subcommittee on Early Childhood, Youth and Families reported H.R. 3892, the English Fluency Act, introduced by Rep. Frank Riggs. This bill raises many of the same programmatic issues and political dynamics as the Unz Initiative in California, as well as additional civil rights enforcement concerns. We expect the bill to be taken up at the full committee either on June 4 or June 11.

The purpose of this memo is to update you on our strategy for addressing this bill. Because few members have focused on this bill yet, the political context in which it will be considered is still quite fluid. The Unz vote in California next week as well as the mark-up shortly after the recess will focus attention on this issue, and we will reassess the situation and our strategy after these and other significant events.

**I. Summary and Analysis of the Proposed Legislation**

The bill would eliminate the existing Bilingual Education and Emergency Immigrant Education programs and (1) establish a formula block grant program to states to provide assistance to LEP and immigrant students in English language instruction, (2) require states to withdraw funding from local programs in cases where students do not master English within two years; (3) set a 3-year limit for serving any individual student with these program funds; (4) require parental consent before a student could be placed in a program that uses native language instruction; and, (5) prohibit states from exempting LEP students who have been in the same school system for 2 years from statewide testing in academic subjects in English, by withdrawing funds under this program from states that do not follow this policy.

In addition, the bill would void existing compliance agreements between the Department's Office for Civil Rights (OCR) and States and local school districts, if those agreements require those States and school districts to develop, implement, provide, or maintain any form of bilingual education. Similarly, the bill requires OCR to publish in the Federal Register all enforcement guidelines and compliance standards that relate to the provision of English language

instruction to students with limited English proficiency. OCR would be prohibited from entering into any new compliance agreements based on those guidelines or standards until those guidelines and standards, themselves, are approved by a subsequent statute.

This bill is seriously flawed in a number of respects, even though it attempts to promote the more rapid mastery of English. Like Unz, its punitive approach is likely to result in fewer rather than more students mastering English. It is simply unrealistic to expect that all students, or even a large proportion of them, will master English within 2 years. And in cases where this timetable is not achieved, the sole remedy is to cut off funds. The bill makes no provisions to provide extra help to individual students who lack English proficiency after two years. Nor does it provide a mechanism or resources to strengthen local programs that do not meet the two year standard.

The proposed state block grant would replace the existing discretionary grant program that targets funds to the local school systems with the greatest need and highest quality proposals. There would be no formula for allocating funds to local school districts within each state. Under this arrangement, funding would be less effectively targeted to communities with the greatest need, especially large cities such as Los Angeles, San Francisco, New York and Chicago. These communities generally receive less than their fair share of funds in other programs (e.g., Goals 2000 and the Technology Literacy Challenge Fund) that allow states to distribute funds on a discretionary rather than formula basis. In addition, the bill lacks maintenance of effort and supplement-not-supplant provisions to prevent States and school districts from substituting federal funds for state and local funds.

The Riggs bill is likely to exacerbate the current shortage of qualified bilingual education and ESL teachers nationwide. It would eliminate the professional development program which helps strengthen the skills of existing teachers and train new ESL and bilingual education teachers. In contrast to your FY 1999 proposal to double funding for teacher training, this bill would limit state use of funds for teacher training and force teacher training to compete for funds for service delivery at the local level.

Finally, the civil rights provisions could effectively end--or at least seriously delay--enforcement of Title VI of the Civil Rights Act of 1964, as it applies to the education of language minority children, through the use of voluntary compliance agreements. The use of compliance agreements is one of OCR's most important (and, by far, the most commonly used) enforcement tools regarding the provision of appropriate educational programs for such children.

Title VI, itself, requires OCR to attempt to resolve all compliance problems under it, including those relating to the education of language minority children, through voluntary means before employing other, more adversarial, means, such as funding terminations--preceded by administrative litigation--and referral to the Department of Justice for court litigation. If H.R. 3892 were enacted, OCR enforcement of Title VI as it applies to the education of language minority children would necessarily have to rely far more on litigation than it currently does, and States and school districts would necessarily endure far more costly and time-consuming

litigation, not only with the Department of Education and the Department of Justice, but with private parties, as well, because States and school districts would no longer be able to rely on voluntary agreements with OCR as evidence of their compliance with Title VI.

## **II. Congressional Outlook and Strategy**

The bill was reported out of subcommittee on a party-line vote. We expect the bill to be taken up at full committee shortly after recess, on either June 4 or June 11. We expect Democrats will remain uniformly opposed to the bill at committee.

The Congressional Hispanic Caucus is adamantly opposed to the Riggs bill. Shortly before subcommittee mark-up they met with Secretary Riley and pressed him very hard for a veto threat from the Administration. While Secretary Riley would in fact recommend a veto of this bill, he told the Caucus that a veto threat would need to be accompanied by an alternative bill, in order to reinforce the Administration's principles for strengthening bilingual education articulated in his statement opposing the Unz Initiative, and to provide cover to Democrats voting against Riggs. However, Caucus members are also firmly opposed to the introduction of any alternative bill, and we will have difficulty gaining strong Democratic support for our alternative over the opposition of the CHC. They prefer to delay consideration of changes in the program until next year's scheduled reauthorization. In addition, they are not comfortable with the prospect of translating our 3-year goal for students to become proficient in English into legislation. For subcommittee mark-up, the CHC preferred that we stay silent on the bill rather than signalling opposition short of a veto threat, or coupling a veto threat with an alternative bill. We did not comment on the bill before subcommittee mark up, but will need to take a position before full committee.

We have been working with Mr. Gephardt's office to gauge the bill's prospects on the House floor. However, few members beyond the subcommittee and the Hispanic Caucus have focused on it, so it is difficult to predict how this will play out. While the civil rights provisions may help keep Democrats together, we expect that many conservative Democrats, particularly those without sizeable Hispanic constituencies, will find it difficult to oppose this legislation, especially in the wake of the anticipated Unz vote, without some alternative to vote for.

There is no indication at present that the Senate Education and Labor Committee intends to take up the Riggs bill. While there is always a chance of a floor amendment, we think the odds that such a move would succeed are quite slim. Thus, it is very unlikely that a bill to overhaul bilingual education will pass the Congress this session.

Our primary objective therefore is to oppose Riggs while avoiding the appearance of defending the status quo. We also have an opportunity to set the stage for the reauthorization of the bilingual education program in the next Congress, if we can effectively advocate for our own reform approach without splitting Democrats on the issue. Our effectiveness toward these ends depends in part on our ability to gain Hispanic Caucus support for our alternative. This in turn will

depend heavily on the extent to which other Democrats express the need for an alternative bill, the extent to which the Caucus continues to want a strong veto threat on this bill, and our willingness to condition a veto threat on CHC support for our alternative legislation.

To accomplish our objectives, we will stay in close touch with the CHC and with Mr. Gephardt's office, and are planning the following steps:

- **Prepare an alternative legislative proposal.** The Education Department is drafting legislation, in the form of amendments to the existing bilingual education program, based on the principles articulated by Secretary Riley's statement of opposition to Unz. While the legislation can be ready shortly, we have not yet determined the best time to introduce the bill. As indicated above; if an alternative were introduced at committee mark-up next week, we could not count on broad Democratic support due to CHC opposition. We believe the situation could well change when the bill comes to the floor, when many Democrats may feel the need for an alternative to vote for in order to vote against Riggs. If this situation materializes, we believe the Hispanic Caucus will likely change its position and support our alternative. If not, we would again face the prospect of offering a bill that is opposed by a significant number of Democrats, and would recommend against taking this step.
- **Continue to link the possibility of a veto threat to support for our alternative proposal, at least through full committee mark-up.** In our conversations with the Hispanic Caucus leading up to the full committee mark-up, we will continue to take the position that we cannot issue a veto threat unless we also put our alternative on the table, with their support. In the short run, the most likely result of this approach is that we indicate our "strong opposition" to the Riggs bill before mark-up, rather than issuing a veto threat, though the outcome of the Unz vote could affect how caucus members view the value of an alternative bill, even before the mark-up. When the bill goes to the floor we will be able to better gauge the desirability of a veto threat and alternative legislation, and will reassess our strategy accordingly.
- **Consider nonlegislative steps to highlight your commitment to reforming bilingual education.** In order to ensure that your opposition to Riggs is not equated with a defense of the status quo, we are exploring several steps you could take to underscore your commitment to reform. One would be to issue a directive to the Education Department or NPR, to identify models of effective approaches to helping kids become proficient in English within your 3-year goal. A second approach would be to begin to reframe the debate over bilingual education. In addition to stressing the necessity of LEP kids becoming proficient in English within 3 years, you could also call for efforts to help more native English speakers become proficient in a second language, in order to be competitive in the global economy. In California, each of the gubernatorial candidates has taken this approach, stressing the value of all students leaving school fluent in English and another language.

Your June 13 commencement address at Portland state, focused on immigration, could be forum for addressing these nonlegislative steps, or, if necessary, announcing our legislative proposal.

- **Veto Threat for Full Committee.** Secretary Riley will send a letter just before mark-up, indicating that he will recommend a veto if this bill comes to you. This would be a strong signal that would help hold the Democrats together in committee and on the floor. The rationale for the veto would stress our problems with the civil rights enforcement provisions, but would also raise our objections to the programmatic features of the bill. The veto threat would be coupled with a reiteration of the principles for how to strengthen bilingual ed you approved in the context of the decision to oppose Unz, and an indication that Administration will develop legislation fully in accord with these principles, without specifying when such legislation would be transmitted. The letter could also highlight your budget comittment to bilingual education, including particularly teacher training.

RECORD TYPE: PRESIDENTIAL (NOTES MAIL)

CREATOR: Elena Kagan ( CN=Elena Kagan/OU=OPD/O=EOP [ OPD ] )

CREATION DATE/TIME:29-MAY-1998 22:13:04.00

SUBJECT:

TO: GENE (Pager) #SPERLING ( GENE (Pager) #SPERLING [ UNKNOWN ] )

READ:UNKNOWN

TEXT:

reminder: weekly due tomorrow at 12:00, we can do over phone in morning;  
try to call marchik and hilley

RECORD TYPE: PRESIDENTIAL (NOTES MAIL)

CREATOR: Elena Kagan ( CN=Elena Kagan/OU=OPD/O=EOP [ OPD ] )

CREATION DATE/TIME:29-MAY-1998 22:13:04.00

SUBJECT:

TO: GENE (Pager) #SPERLING ( GENE (Pager) #SPERLING [ UNKNOWN ] )  
READ:UNKNOWN

TEXT:

reminder: weekly due tomorrow at 12:00, we can do over phone in morning;  
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RECORD TYPE: PRESIDENTIAL (NOTES MAIL)

CREATOR: Elena Kagan ( CN=Elena Kagan/OU=OPD/O=EOP [ OPD ] )

CREATION DATE/TIME:30-MAY-1998 14:13:00.00

SUBJECT: Public charge

TO: Bruce N. Reed ( CN=Bruce N. Reed/OU=OPD/O=EOP [ OPD ] )  
READ:UNKNOWN

TEXT:

are you ok with this?

----- Forwarded by Elena Kagan/OPD/EOP on 05/30/98 02:12  
PM -----

Diana Fortuna

05/21/98 10:50:12 AM

Record Type: Record

To: Elena Kagan/OPD/EOP, Christopher C. Jennings/OPD/EOP  
cc: Julie A. Fernandes/OPD/EOP, Jeanne Lambrew/OPD/EOP, Laura  
Emmett/WHO/EOP  
Subject: Public charge

Julie, OMB, and I are opposing INS and the State Department actions that are endangering our efforts to sign up as many children for Medicaid as possible and to restore food stamps and other benefits to legal immigrants. A formerly obscure feature of immigration law requires the INS or State to bar people from the U.S. who are likely to be a "public charge." Because of crackdowns by INS/State since welfare reform passed, word has spread in immigrant communities that signing up yourself or your children for Medicaid or other benefits puts you at risk with the INS -- and while these fears are exaggerated, they are not crazy. For example, legal immigrants with green cards who leave the country for more than 6 months are not permitted to re-enter the country if they are currently on Medicaid.

The INS wants to issue guidance that current receipt on SSI, TANF, Medicaid, or sometimes food stamps automatically makes you a public charge -- even though you're legitimately eligible for benefits -- preventing you from adjusting your immigration status or leaving the U.S. for more than 6 months. (They say this is current policy, but that's quite murky.) The advocates are starting to jump on this issue. We have enlisted Rob Weiner of WH counsel and James Castello at DOJ to help us figure out whether the law will allow us to rescue just Medicaid or whether we can go even further to say the INS shouldn't consider receipt of benefits in determining public charge, but simply look at income, assets, etc. The further we go, the more we will enrage Lamar Smith. The INS is fearful of provoking him, and feels that some of the options we're considering fly in the face of the common sense meaning of the term "public charge." The State Department appears baffled that we are concerned about this issue and dug-in to their position.

Just wanted to make sure you're aware and on board. Chris, Bruce Bullen of Massachusetts has written you on this issue.

# Withdrawal/Redaction Marker

## Clinton Library

DOCUMENT NO. AND TYPE	SUBJECT/TITLE	DATE	RESTRICTION
001. email	Elena Kagan to Richard Socarides re: Repeal (1 page)	05/30/1998	P6/b(6)

### COLLECTION:

Clinton Presidential Records  
Automated Records Management System [Email]  
OPD ([From Elena Kagan])  
OA/Box Number: 250000

### FOLDER TITLE:

[05/21/1998-06/18/1998]

2009-1006-F  
bm110

### RESTRICTION CODES

#### Presidential Records Act - [44 U.S.C. 2204(a)]

- P1 National Security Classified Information [(a)(1) of the PRA]
- P2 Relating to the appointment to Federal office [(a)(2) of the PRA]
- P3 Release would violate a Federal statute [(a)(3) of the PRA]
- P4 Release would disclose trade secrets or confidential commercial or financial information [(a)(4) of the PRA]
- P5 Release would disclose confidential advice between the President and his advisors, or between such advisors [(a)(5) of the PRA]
- P6 Release would constitute a clearly unwarranted invasion of personal privacy [(a)(6) of the PRA]

C. Closed in accordance with restrictions contained in donor's deed of gift.

PRM. Personal record misfile defined in accordance with 44 U.S.C. 2201(3).

RR. Document will be reviewed upon request.

#### Freedom of Information Act - [5 U.S.C. 552(b)]

- b(1) National security classified information [(b)(1) of the FOIA]
- b(2) Release would disclose internal personnel rules and practices of an agency [(b)(2) of the FOIA]
- b(3) Release would violate a Federal statute [(b)(3) of the FOIA]
- b(4) Release would disclose trade secrets or confidential or financial information [(b)(4) of the FOIA]
- b(6) Release would constitute a clearly unwarranted invasion of personal privacy [(b)(6) of the FOIA]
- b(7) Release would disclose information compiled for law enforcement purposes [(b)(7) of the FOIA]
- b(8) Release would disclose information concerning the regulation of financial institutions [(b)(8) of the FOIA]
- b(9) Release would disclose geological or geophysical information concerning wells [(b)(9) of the FOIA]

RECORD TYPE: PRESIDENTIAL (NOTES MAIL)

CREATOR: Elena Kagan ( CN=Elena Kagan/OU=OPD/O=EOP [ OPD ] )

CREATION DATE/TIME: 8-JUN-1998 10:47:22.00

SUBJECT: weekly

TO: Cynthia Dailard ( CN=Cynthia Dailard/OU=OPD/O=EOP @ EOP [ OPD ] )

READ:UNKNOWN

TEXT:

1. Tobacco -- Senate Update: The Senate passed two amendments to the McCain bill this week. The first, sponsored by Senator McCain and approved by voice vote, provides \$3 billion over five years to the Veterans Administration to assist veterans with smoking-related illnesses. The second, approved by a 66-29 vote, greatly increases the surcharges imposed on individual companies that fail to meet youth smoking targets. This amendment, supported by most Democrats as well as by those Republicans who want to kill tobacco legislation (on the theory that a lack of balance will bring the bill down), would impose penalties equaling or exceeding anticipated industry profits on a company that has a significant youth market and misses its youth reduction targets by 20 percent.

Next week, the Senate is scheduled to consider a proposal by Senator Gramm to use tobacco revenues for a tax cut to all married couples earning less than \$50,000 per year (whether or not they now pay a marriage penalty). A prior version of this proposal would have decimated just about all other spending immediately, but Gramm reportedly is phasing in his amendment to avoid this result. The latest version would cost \$13 billion over the first four years (28 percent of total receipts), an additional \$30 billion in the next five years (42 percent of total receipts), and \$225 billion in the remaining years of the bill (78 percent of total receipts). Even this scaled back version of the amendment, of course, is incompatible with our and the Democratic Caucus's spending priorities. For this reason, Senator Daschle has prepared an alternative tax amendment, which would provide relief for those married couples earning less than \$60,000 per year who now pay a marriage penalty, as well as accelerating the deductibility of health insurance costs for the self-employed. This alternative proposal would cost \$11 billion over the first four years and would continue to consume between 20 and 25 percent of total revenues throughout the lifetime of the bill. It is conceivable that McCain and Senator Kerry will strike a deal with Gramm next week that splits the difference between these two proposals. Such a compromise certainly would grease Senate passage of the tobacco bill, but at some cost to our public health and research priorities.

The Senate also is expected to vote next week on an amendment offered by Senators Craig and Coverdell, which would allocate about \$2 billion each year to anti-drug efforts, again cutting into the funding available in the bill for public health and research. The Craig-Coverdell amendment also includes a permanent prohibition on the use of federal monies for needle exchange and a program to allow education vouchers to students who have been the victims of school violence. We are working to draft a modified version of the Craig-Coverdell amendment that spends less money on anti-drug efforts and eliminates the amendment's poison pills. We hope that we will be able to convince a bipartisan group of Senators, including McCain and Kerry to support this modified anti-drug amendment.

Cloture votes are scheduled for Tuesday and Wednesday, but because Senator Lott strenuously opposes cutting off debate at this time, no one expects these motions to pass. We are hopeful that by the end of the

week, the Senate will have dealt with the tax and drug issues, as well as the two Republican substitute bills and the farmers provisions, and that it then will be ready to vote for final passage.

RECORD TYPE: PRESIDENTIAL (NOTES MAIL)

CREATOR: Elena Kagan ( CN=Elena Kagan/OU=OPD/O=EOP [ OPD ] )

CREATION DATE/TIME: 8-JUN-1998 10:47:42.00

SUBJECT: INS Mtg

TO: Laura Emmett ( CN=Laura Emmett/OU=WHO/O=EOP @ EOP [ WHO ] )  
READ:UNKNOWN

TEXT:  
----- Forwarded by Elena Kagan/OPD/EOP on 06/08/98 10:47  
AM -----

LESLIE  
BERNSTEIN  
06/08/98 08:55:34 AM

Record Type: Record

To: Karen Tramontano/WHO/EOP, Elena Kagan/OPD/EOP  
cc:  
Subject: INS Mtg

Maria Echaveste is having a naturalization meeting with MALDEF and about 10 other folks . She would like you both to weigh in. Julie Fernandes will also be in attendance.

Please let me know how 6/10 at 10:30a works.

Thanks.

RECORD TYPE: PRESIDENTIAL (NOTES MAIL)

CREATOR: Elena Kagan ( CN=Elena Kagan/OU=OPD/O=EOP [ OPD ] )

CREATION DATE/TIME: 8-JUN-1998 17:28:06.00

SUBJECT: Options paper

TO: Laura Emmett ( CN=Laura Emmett/OU=WHO/O=EOP @ EOP [ WHO ] )  
READ:UNKNOWN

TEXT:  
please print now.

----- Forwarded by Elena Kagan/OPD/EOP on 06/08/98 05:27  
PM -----

Rebecca M. Blank  
06/08/98 05:08:04 PM  
Record Type: Record

To: See the distribution list at the bottom of this message  
cc: See the distribution list at the bottom of this message  
Subject: Options paper

Attached is the final options paper for the Principal's meeting on poverty measurement. Sally Katzen's office will be scheduling this meeting in the near future. Note that the Appendix on program effects has been substantially edited, after extended negotiation between OMB and HHS.

Message Sent

To: \_\_\_\_\_  
Joseph J. Minarik/OMB/EOP  
Sally Katzen/OPD/EOP  
Elena Kagan/OPD/EOP  
pruggles @ osaspe.dhhs.gov @ inet  
Katherine K. Wallman/OMB/EOP

Message Copied

To: \_\_\_\_\_  
Mark A. Wasserman/OMB/EOP  
Cecilia E. Rouse/OPD/EOP  
Andrea Kane/OPD/EOP  
Paul Bugg/OMB/EOP  
Richard B. Bavier/OMB/EOP  
===== ATTACHMENT 1 =====  
ATT CREATION TIME/DATE: 0 00:00:00.00

TEXT:  
Unable to convert ARMS\_EXT:[ATTACH.D73]MAIL47558395R.126 to ASCII,  
The following is a HEX DUMP:

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June 8, 1998

DRAFT BACKGROUND MEMORANDUM FOR EOP PRINCIPAL'S MEETING

FROM: REBECCA BLANK  
ELENA KAGAN  
SALLY KATZEN  
JOE MINARIK

Subject: Meeting on Income and Poverty Measures

**Purpose of the Meeting**

In early 1999, the Census Bureau will publish alternative measures of poverty based on the proposals contained in the 1995 National Research Council (NRC) report, *Measuring Poverty: A New Approach*. The current official poverty measure dates back to the 1960s, and while it has been an important contributor to public debate and policymaking, the NRC report reflects a broad consensus that the measure is out-of-date and in need of revision.

Poverty measurement involves two concepts: (1) A definition of family income; and (2) A "threshold" against which income is compared to determine if a family is poor. Changes in these two concepts will have a direct impact on statistics used by the public for informational purposes. Changes will also likely have an effect on Federal programs as well.

Because of the importance of an independent statistical system, the Census Bureau plays the major role in deciding technical issues regarding poverty measurement. However, because of the important policy and political implications of the poverty concept, Census has asked for advice from the EOP (because OMB, through OIRA's Statistical Policy Office, is the statutory arbiter of the "official" poverty measurement methodology) on the upcoming report.

In response to Census' request, CEA, DPC, NEC, and OMB formed a policy working group. (Among the agencies, only the Deputy Assistant Secretary for Human Services Policy at HHS was invited to participate because of her expertise on poverty measurement.) This working group has held a series of meetings, and prepared the attached memo to outline its tentative guidance to Census. The meeting of EOP Principals is intended to review the working group's conclusions before they are transmitted to Census. It is important to emphasize that we are only being asked to give advice to the Bureau of the Census; what it actually publishes is its decision.

There are four global issues to be decided; the first two are most pressing because we need to give guidance to Commerce as soon as possible:

1) Should the Census Bureau select or highlight a single alternative poverty measure, or present several equally in its forthcoming report? Do the principals have a single preferred measure that

they would like to see replace the current official measure? Would anointing a single measure at this time be premature, and prejudice the analytical process? Would it raise ire in the Congress? If we do not anoint a single preferred measure at this time, will it be difficult to select one later should we want to switch the “official” definition to one of the proposed alternatives?

2) There are also two technical issues (policy options 1 and 4 in the background memo) that require careful consideration.

- Should we advise Census to benchmark the new poverty measure to the old poverty rate in the current year (so that the number of people classified as poor would remain the same, although the distribution would change)? Should Census implement the NRC recommendations, which would result in a higher poverty rate (e.g., 18% rather than 13.7% in 1996)?
- If there is only one measure reported by Census, should it account for differences in medical out-of-pocket (MOOP) expenditures among households in the way recommended by the NRC, namely, subtracting them from income before a family’s poverty status is calculated? (An alternative choice is to add them to the thresholds -- which of these methodologies should be used is a technical choice best left to Census.) If we believe that several measures should be equally reported by Census, should one of them account for medical expenditures using a different methodology?

3) How should the Administration proceed toward a new official measure of poverty? Should it proceed along a timetable to replace the current official measure before the end of this Administration? If so, what process do we need to establish to move forward on this in a timely fashion? Or, should the Administration proceed more cautiously, letting a consensus build around a preferred measure among the community of users of poverty statistics, but possibly lessening the chances that the official measure is ultimately changed?

4) In addition to OMB’s designation of the “official” poverty measurement, HHS also issues administrative poverty guidelines, used in certain program eligibility calculations. If revised poverty thresholds are adopted as part of a new poverty measure, would the Administration continue the old administrative poverty guidelines, or make them consistent with the new threshold measure? If the guidelines are made consistent, would the Administration make programmatic changes to mitigate the effects on eligibility and spending of switching to the new guidelines?

## TECHNICAL BACKGROUND ON INCOME AND POVERTY MEASURES

### The Current Poverty Measure

The methodology by which current poverty thresholds are determined was developed in the early 1960s by Mollie Orshansky, a staff economist at the Social Security Administration. She developed a set of poverty thresholds that vary with the number of adults, the number of children, and the age of the family head. These thresholds represent the cost of a minimum diet multiplied by 3 to allow for non-food expenditures. The multiplier of 3 was chosen because the average family in 1955 spent one-third of its after-tax income on food. Since the late 1960s, the thresholds have simply been updated annually to adjust for price inflation -- i.e., the measure of poverty has remained virtually unchanged for 35 years, despite substantial changes in family behavior and government policy.

The NRC panel identified several weaknesses in the current poverty measure:

- The current poverty measure takes no account of changes in taxes (i.e., the expansion of the EITC) or in-kind benefits (i.e., Food Stamps).
- The current measure does not distinguish between the needs of working and non-working families. In particular, it does not reflect the cost of child care and other work expenses for working low-income families.
- The current poverty measure takes no explicit account of medical care costs, which vary significantly across families and have increased substantially since the current poverty measure was developed.

### The NRC Recommendations

In order to understand the NRC panel's recommended revisions, one must understand the basics of determining poverty. A family is considered poor when its resources fall below a predetermined poverty line or threshold. Therefore, one must develop a methodology for estimating family resources and for defining the threshold resource level below which a family is considered poor.

#### 1. Defining Family Resources

Under the current poverty calculation, the definition of family resources is cash income. The NRC recommendations would estimate family resources as:

Family resources = Cash income + Near-money in-kind benefits - Taxes - Child care costs - Work expenses - Child support payments - Out of pocket

medical care expenditures (including health insurance premiums)

The rationale for subtracting taxes, work and medical expenses from family resources is that these expenditures are typically not discretionary and reduce the family income available to achieve a basic quality of life.

There is near consensus among researchers that adjusting for near-money in-kind benefits (primarily Food Stamps and housing subsidies) and taxes would be an improvement in how poverty is measured. There is slightly less agreement on whether child care costs, work expenses, and child support payments should also be deducted because an unknown proportion of these expenses is likely discretionary. (The NRC proposes to cap the amount of child care and work expenses that can be subtracted to deal with this problem.) As discussed below, the adjustment for out-of-pocket medical care expenditures is more controversial.

## 2. Defining a Poverty Threshold

A threshold must be determined against which to compare a family's resources. The NRC panel recommends basing the threshold on expenditures on "necessities" (food, shelter, and clothing) plus a little more. Specifically, the NRC panel recommends selecting the 30th to 35th percentile in the distribution of annual expenditures on food, shelter, and clothing among families of four (two adults and two children), and then multiplying this expenditure level by between 1.15 and 1.25. Thresholds for other family sizes and types would be determined by an equivalency scale calculation.

The NRC recommends adjusting these thresholds to take into account geographic variation in cost of living, based on differences in housing costs by region and by city-size. It also recommends adjusting the thresholds over time by recalculating them from expenditure data on an annual basis.

## OPTIONS FOR DISCUSSION

### 1. **Recommendation regarding determining the level of the poverty threshold.**

The NRC panel acknowledges that the actual level at which the poverty threshold is set (and hence the final poverty rate) is inherently arbitrary and cannot be determined on the basis of purely statistical judgements. There are two primary options:

A. The NRC alternative. As described above, the NRC panel recommends establishing a threshold based on the 30th-35th percentile in the distribution of annual expenditures for a family of four, with a small multiplier to account for additional small personal expenditures. As shown in Tables 1 and 2, column 3, this would raise the 1996 poverty rate from 13.7% to 18%, and increase poverty among all subgroups. In addition, (as described further in Option B) this change

will alter the composition of poverty among various subgroups.)

B. Benchmarking. The NRC panel also considered poverty estimates that benchmark the alternative poverty rate to equal the old poverty rate in a given year. The Census has done a number of such benchmarked calculations for 1996, as shown in Tables 1 and 2, column 2. (The report issued early next year would benchmark to 1997.) Benchmarking would assure that the aggregate poverty rate is identical for the official and the alternative measure in the benchmark year. But the distribution of poverty among subgroups within each measure would differ (see Table 2). In general, working families and families with large out-of-pocket medical expenses become poorer and non-working families with substantial in-kind benefits become less poor. This has geographic as well as subgroup poverty rate implications. Similarly, both historical and future trends would differ. For instance, the alternative measure is identical in 1996 but higher in 1991. (The faster fall using the alternative measure is largely due to the expansion in the EITC.)

*Pros of using the NRC measure:*

- Incorporates the recommendations of the NRC panel, based on their professional judgement from the best available evidence.
- Generates dollar threshold levels that are quite similar to the current dollar thresholds (although the resources to which the thresholds would be compared are quite different).

*Cons of using the NRC Measure:*

- Results in a higher poverty rate (although the trends over time are similar.)

*Pros of Benchmarking:*

- May provide an easier transition to the new methodology because there will not be a change in the overall level of poverty.
- Focuses the arguments on the relative distribution of who is poor rather than how many people are poor.

*Cons of Benchmarking:*

- Violates the NRC recommendation that the threshold should be based on the 30th-35th percentile in the expenditure distribution. In order to benchmark, the threshold falls to (about) the 25th percentile of expenditures on food, shelter, and clothing.

## **2. Recommendation regarding updating the thresholds over time**

Currently the poverty threshold is updated annually using the CPI. This, however, does not allow for adjustments that reflect changes in underlying consumption patterns that might affect the revised thresholds. For instance, food prices have decreased relative to other goods over time,

while housing prices have increased. There are two options:

(A) Recalculate the thresholds annually as a share of consumption on food, shelter, and clothing. (This is recommended by the NRC panel.)

(B) Update the thresholds on a year-to-year basis using a price index (preferably one based only on food, shelter and clothing). Implement a regular process (every 5-10 years) of reviewing the poverty measure and recalculating the thresholds.

*Pros of Re-calculating the Thresholds:*

- Regular recalculation will allow the poverty thresholds to reflect more accurately changes in consumption patterns and standards of living.
- Without an expectation that the thresholds will be re-calculated regularly, it may be hard to update them at all.
- Under certain data circumstances, recalculation could move the threshold a large amount or in an unexpected direction. This might raise substantive and political concerns.

*Pros of Updating Using the CPI:*

- Using the NRC methodology, the poverty thresholds are somewhat relative (i.e., they are affected by changes in the distribution of household expenditures.) As a result, they are a moving target and do not provide an absolute standard of need. A CPI adjustment would make it easier to compare poverty from year-to-year against a constant standard.
- Because consumption patterns and standards of living change slowly, it may be better to take them into account periodically rather than annually.
- An update with a CPI for necessities only (food, clothing, and shelter) may capture most of the relevant changes and would make it easier in the short run to understand the updating procedure.
- The data may not be good enough for an annual re-calculation of the thresholds.

NOTE: The EOP Policy Working Group recommends Option (B).

**3. Recommendation as to whether thresholds should be adjusted for geographic variation.**

The NRC panel recommended adjusting the poverty thresholds for cost-of-living differences across regions and by city size. Census proposes to make such adjustments based on housing

cost differences (which have much greater regional/city size variation than food or clothing.)

*Pros of Adjusting for Geographic Variation in Cost of Living:*

- Most statisticians and economists agree that such adjustments should be made if data are available.

*Cons of Adjusting for Geographic Variation in Cost of Living:*

- There is no one “right” way to make such adjustments and the issue could be highly politicized.
- The data available to make such adjustments are limited and may not be entirely reliable.
- Implementing such an adjustment in the poverty line threshold could lead to pressure to provide regional cost adjustments in a wide variety of other government programs, from Social Security benefits to tax payments.

NOTE: The EOP Policy Working Group recommends against geographic price adjustments.

#### **4. Recommendation regarding how to account for medical care expenditures.**

Since the mid-1970s, analysts have been concerned that the official poverty rate overstates the extent of poverty among beneficiaries of Medicare, Medicaid, and private health insurance. At the same time, the official poverty rate may understate the extent of poverty among populations with large medical expenditures. Most analysts agree that, in principle, medical care “needs” should be incorporated into the calculations of the threshold and family resources (i.e., families with higher medical needs should have higher thresholds; those with more generous medical benefits should be considered to have more resources; and those who must spend more to achieve “good health” should have those expenses subtracted from their resources). However we cannot observe a family’s medical need. In addition, it is not clear that one can simply impute the cash value of insurance benefits and add this to income. The “extra” benefits received from insurance to cover expensive medical services do not provide income that can be used for any other purpose.

To understand the difficulties, consider including medical benefits into the income calculations. Adding medical benefits to income, without also adjusting the poverty threshold, has the perverse effect of making sicker individuals appear better off. Other proposals to adjust the poverty threshold (without also adjusting resources) run into similar problems.

In the end, the NRC panel recommended subtracting all medical out-of-pocket (MOOP) expenses (including health insurance premiums) from income, without trying to value health insurance as a part of income or medical need as a part of the thresholds. Hence, family

resources are measured net of MOOP. Those individuals with good insurance will have few out-of-pocket expenses; those without insurance who face health problems will have lower measured incomes as they pay more for medical care.

This adjustment accounts for the larger poverty rates using the NRC methodology. For example, in 1996 the poverty rate was 13.7% using the current methodology; it would have been 18% using the NRC methodology, but only 13.2% using the NRC methodology without the medical expenses adjustment. This adjustment nearly doubles the poverty rate for the elderly, raising it almost to the rate for children. This adjustment is one of the most controversial of the NRC recommendations.

There is general agreement that ignoring medical care and medical expenses entirely is not a good idea, particularly given the rapid increase in medical costs in the past 30 years, the extent of uninsurance among the low-income population, and this Administration's concern with it. In addition, if we do not adjust for medical care (in some way) now, it may be much harder to do so in a few years when we will have better data (because the change will be so dramatic it will be viewed as another big methodology change).

There are three approaches to incorporating medical care and expenses:

(A) Follow the NRC recommendation and subtract MOOP from family resources. This makes families with unreimbursed medical expenses less well-off than other families.

(B) MOOP could be added to the thresholds rather than subtracted from resources. (The choice between options (A) and (B) is a technical decision that Census should address.)

(C) Try to impute the value of health insurance to resources, so those with insurance have higher resources. Health insurance should then also be imputed into the thresholds.

*Pros of Adjusting for MOOP (either options (A) or (B)):*

- While not perfect, under the NRC recommended adjustment families with higher unreimbursed medical expenditures will be "poorer." The NRC recommended adjustment would also be sensitive to changes in health care financing that would decrease MOOP and thereby increase disposable income and reduce poverty.

*Cons of Adjusting for MOOP (either options (A) or (B)):*

- The data that are currently available are out-of-date (but we should have updated information available in a more timely fashion within another year.)
- The NRC recommended approach relies on the controversial assumption that all medical care expenditures are nondiscretionary. (This concern could be mitigated to some extent by imposing a cap on the amount of medical expenses.)

*Pros of Imputing the Value of Health Insurance into Resources and Thresholds:*

- Provides a more complete accounting of all medical resources available to a family.

*Cons of Imputing the Value of Health Insurance into Resources and Thresholds:*

- There is no accepted “correct” way to do this. The data here are probably more unreliable than the data needed to impute the value of MOOP to families.
- Many analysts agree with the NRC panel that the value of health insurance is quite different than (say) the value of food stamps, which are far more fungible. Mixing in health insurance coverage with economic need causes interpretational and conceptual problems to a measure of economic need.
- To date, Census has been following the NRC recommendation. If we asked them to switch to this approach, it might require substantial additional work and seriously delay their report.

NOTE: The EOP Policy Working Group recommends that Census incorporate medical care in some way and recognizes that option (A) is the most practical and realistic for the short term. However, the group strongly recommends that Census thoroughly investigate the impact of option (B), and continue work on other approaches to incorporating medical care and expenditures, such as by valuing medical health insurance (option (C)).

**5. Recommendations regarding which alternatives Census should publish and/or how they should be presented.**

The current plan is to publish a small number (maybe 3) of alternatives. For instance, the Census could publish a 1997-benchmarked poverty rate and a NRC-alternative poverty rate, providing two alternatives. Or it could publish a 1997-benchmarked poverty rate including all of the NRC recommendations, and then publish the same thing without MOOP, or without geographical price variation. (There will be extensive appendices in this report that will report a wide variety of different poverty calculations, to demonstrate the statistical properties of the poverty measurement recommended by NRC.)

- Will it be confusing to publish multiple (even a small number of) alternatives, as opposed to only one alternative? How will this affect how the report is received? How should these be presented?
- What problems will it create to have multiple alternatives if at some future point we want to redefine the official poverty rate to one of these improved alternative measures?

Table 1. Poverty Rates and Thresholds under Alternative Measures, 1991-96, CPS

	Official measure	Benchmarked to 1996	NRC Experimental
<b>Poverty Rates</b>			
1991	14.2	14.5	18.9
1992	14.8	15.3	19.6
1993	15.1	15.7	20.2
1994	14.6	14.7	19.0
1995	13.8	13.8	18.2
1996	13.7	13.7	18.0
<b>Thresholds for 2 adults and 2 children (in dollars)</b>			
1991	13,812	11,891	13,891
1992	14,228	12,249	14,309
1993	14,654	12,616	14,738
1994	15,029	12,938	15,115
1995	15,455	13,305	15,543
1996	15,911	13,698	16,002

Table 2. Poverty Rates under Alternative Measures, 1996, CPS

	Official measure	Benchmarked NRC to 1996	Experimental
<b>All persons</b>	<b>13.7</b>	<b>13.7</b>	<b>18.0</b>
Children	20.5	18.1	23.8
Nonelderly adults	11.4	11.5	15.0
Elderly	10.8	15.6	20.4
White	11.2	11.8	15.6
Black	28.4	25.2	32.0
Hispanic origin	29.4	28.5	37.7
One or more workers	9.5	10.0	13.6
Persons in family of type:			
Married couple	6.9	7.8	11.1
Female householder	35.8	32.3	40.4
Geographic regions:			
Northeast	12.7	14.3	18.8
Midwest	10.7	10.3	13.8
South	15.1	14.2	18.3
West	15.4	16.1	21.0
Metro/CC	19.6	19.2	24.7
Not CC	9.4	10.6	14.1
Nonmetro	15.9	13.5	17.5

**APPENDIX**  
**The Effect of the Poverty Measure on Program Eligibility and Benefits**

The Congressional Research Service has identified 26 programs that are affected by the measure of poverty. Many of the program connections to the poverty definition are unique, and many are highly complex. Hence, we do not yet have a precise estimate of how program costs or coverage would be affected.

We should not leap to the conclusion that this large number of programs would dictate a large Federal cost impact of a new measure of poverty. Many of the affected programs are small, and many of the programs may be affected to only a limited degree by even a change in the measured aggregate incidence of poverty. Some of the programs are discretionary, meaning that their aggregate cost is set by appropriation; a change in the measure of poverty would affect only the geographic distribution of those funds (though that could, in itself, be a matter of political concern, if such reallocations should prove to be significant). However, where at least a few large programs are involved, it is essential to investigate the potential impact carefully.

There are two schools of thought on the potential budgetary or allocational effect of a change in the definition of poverty.

Gordon Fisher, the analyst at HHS who oversees the production of the poverty guidelines used in some programs, presents one perspective in a recent paper:

A number of people believe that the poverty guidelines affect many big entitlement programs. That belief is an exaggeration of the actual situation. Most of the Federal programs using the guidelines are medium-sized or small, with only a few big programs. Moreover, most...are discretionary programs...Only a few programs using the guidelines are mandatory: Medicaid, the Food Stamp Program, and child nutrition programs (mainly the National School Lunch Program).<sup>1</sup>

Offering a different perspective, a recent issue of *Focus*, the periodical of the Institute for Research on Poverty, notes:

For example, the NRC study panel proposed that the measure take into account work-

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<sup>1</sup>G. Fisher, "Disseminating the Administrative Version and Explaining the Administrative and Statistical Versions of the Federal Poverty Measure." Clinical Sociology Review, vol. 15 (1997), p. 165.

related expenses in families where at least one person is employed. Such a change could have important implications for the allocation of federal funds between local areas where the proportions of working and nonworking families differ. Including geographic variations in housing costs might have similar far-reaching effects. Before introducing a new property measure for program purposes, policy makers must determine whether the resulting redistribution of resources will be more equitable, or will have unexpected and capricious effects.

As Fisher suggests, the discretionary - mandatory distinction is important. As noted above, the issue for discretionary programs is not the amount of funding, which is determined by appropriations (though Congress could change future appropriations under the influence of a changed measure of poverty), but rather the geographic allocation of a fixed amount of appropriations. The geographic allocation of relevant discretionary program funds can depend upon the incidence of poverty in particular locations. Therefore, these programs are affected by the actual poverty measure, based on the official thresholds and income concept. The ties between these programs and poverty vary considerably, and staff are undertaking the task of determining how much effect a change in the poverty concept could have. These allocations may or may not change by much, depending upon the extent to which the new poverty measure reallocated poverty geographically; the role of poverty in the allocation of the discretionary funds (some programs use poverty as only one of several indexes by which to distribute funding); the lag between the measurement of poverty and the actual effect on the program (some programs use poverty as measured in the decennial census); and other factors that can be determined only through a program-by-program search.

Besides the official poverty thresholds and the income definition, there are poverty guidelines. The Federal poverty guidelines are the version of the official poverty measure used for program purposes. They are issued by HHS annually, and are based on a simplified and updated version of the previous year's Census poverty measure.

Staff are in the process of determining the potential effects of a change in the poverty measure on the two largest programs affected by the poverty measure, Medicaid and the Food Stamp Program, as well as the smaller programs. In Medicaid, while most recipients qualify for coverage because of their participation in other means-tested programs such as TANF and SSI (programs that do not use the poverty line in their eligibility criteria), changes in poverty thresholds could affect at least three major Medicaid eligibility groups: women, infants and children up to age 6 with family incomes below 133 percent of poverty and children from age 6 to 18 with incomes at or below the poverty level (this provision is being phased in for all poor children under age 19 by FY 2002); families, children and other uninsured in the Medicaid waiver States that have extended coverage beyond current law requirements based on income in relation to the poverty guidelines; and new groups of low-income Medicare beneficiaries who qualify for partial coverage under Medicaid. In all, people whose eligibility for Medicaid is related to the poverty line are estimated to account for about 20 percent of Medicaid recipients. Since most are in families with incomes well below the specified level, only a small fraction

would actually be affected by a poverty line change. Further, most of the new enrollees would be children, whose average health care costs are low. Still, Medicaid is such a large program that even a small proportionate change in costs could involve a significant number of dollars.

The poverty guidelines are used in the Food Stamp Program to set gross income eligibility--only families with gross incomes below 130% of the poverty line are eligible for food stamps. Actual food stamp benefits are calculated based on net income, however--income after deductions for work expenses and various other things. Net income is compared to a specific benefit allotment, determined nationally for each family size, and that benefit is reduced by 30 cents for every dollar of net income the family receives. In practice, the benefit allotment for most families with incomes near the gross income eligibility limit would be small. Many families would be eligible only for zero benefits. Even where families are eligible for some positive benefits, take-up rates among those eligible for small amounts of food stamp benefits tend to be low--the hassle of getting and using food stamps exceeds their value for most such eligibles. Thus, the gross income eligibility cut-off for food stamps is more theoretical than real--families at or near 130% of the poverty line will almost always be eligible only for very low or zero benefits, and are unlikely to participate in the program. For these reasons, we would expect the effect on Food Stamp costs to be smaller than that for Medicaid.

RECORD TYPE: PRESIDENTIAL (NOTES MAIL)

CREATOR: Elena Kagan ( CN=Elena Kagan/OU=OPD/O=EOP [ OPD ] )

CREATION DATE/TIME: 9-JUN-1998 16:59:29.00

SUBJECT: Child Cust Let. Pls review ASAP

TO: Laura Emmett ( CN=Laura Emmett/OU=WHO/O=EOP @ EOP [ WHO ] )  
READ:UNKNOWN

TEXT:

----- Forwarded by Elena Kagan/OPD/EOP on 06/09/98 04:59 PM -----

William P. Marshall  
06/09/98 12:14:45 PM  
Record Type: Record

To: See the distribution list at the bottom of this message  
cc:  
Subject: Child Cust Let. Pls review ASAP

This time I attached the letter.

Message Sent

To: \_\_\_\_\_  
Sylvia M. Mathews/WHO/EOP  
John Podesta/WHO/EOP  
Charles F. Ruff/WHO/EOP  
Ann F. Lewis/WHO/EOP  
Maria Echaveste/WHO/EOP  
Elena Kagan/OPD/EOP  
Audrey T. Haynes/WHO/EOP  
Peter G. Jacoby/WHO/EOP  
Tracey E. Thornton/WHO/EOP  
Robin Leeds/WHO/EOP  
Lisa M. Brown/OVP @ OVP  
Neera Tanden/WHO/EOP  
Nelson Reyneri/WHO/EOP  
June G. Turner/WHO/EOP

===== ATTACHMENT 1 =====  
ATT CREATION TIME/DATE: 0 00:00:00.00

TEXT:

Unable to convert ARMS\_EXT: [ATTACH.D86]MAIL45889406L.126 to ASCII,  
The following is a HEX DUMP:

FF57504394040000010A020100000002050000009617000000020000BC101290B7E5BE2D103E2D  
991F977731356234DABEB696F5B18D84CEE6263335D9E52F80A62173CF4A28BD4FD1178E39537C  
8B8BC7ECAF184773672B36832DFC3E47538A88BE6D817A5FF0EE2D613F79F16E3A02B63ACFCD95  
943FD3928581D94A3EDDF8E12811BE438ACDD7555165CB31E125D33DD6147170A2F44E8E9F02D  
4551F50CF92E8B44B4DEE12200217C56628B1C104595E847D79A835740A6FDB3BEEB6F34487C85  
841E291AF9A7F2E5F9B04C9EE62974FA31955003C5F11943C654049F4F4E05C57A726468C60CBC

Dear

The Administration would support properly crafted legislation that would make it illegal to transport minors across state lines for the purposes of avoiding parental involvement requirements. The Administration appreciates the concerns of the sponsors of S. 1645 about fostering parental and family involvement in a minor's decision to obtain an abortion and their concerns about overbearing and sometimes predatory adults who improperly influence minors' abortion decisions. The Administration believes, however, that changes must be made to ensure that S. 1645 is appropriately targeted at these important goals. If these changes are not made, senior advisors would recommend a veto.

First, S. 1645 must be amended to exclude close family members from criminal and civil penalty. Under the legislation, grandmothers, aunts, and adult siblings could face criminal prosecution for coming to the aid of a relative in distress. Even a mother or father could be exposed to criminal penalty if she or he resides in a state which requires the consent or notification of both parents. Imposing criminal and civil sanctions on family members for helping their relatives, however, does not further the interests of healthy family communications.

Subjecting family members to criminal or civil sanction, moreover, would also further isolate the minor by discouraging her from seeking advice and counsel from those closest to her. Finally, creating a civil action which allows family members to sue each other when a minor within that family has an abortion does not serve the goal of fostering strong families.

Second, S. 1645 must be amended to prevent punishing persons who simply provide information, counseling, referral, or medical services to the minor. The bill as written, for example, could potentially subject a telephone receptionist to civil or criminal liability merely for informing an unnamed caller about the availability of abortion services. Holding such persons criminally or civilly liable, however, does not further the interests in promoting family communication or deterring those who would inappropriately transport minors across state line to obtain abortions.

The Justice Department has also identified a number of constitutional concerns that inhere in particular aspects of the legislation. The Department will forward their concerns subsequently and would be pleased to work with the sponsors in crafting legislation that remedies those defects and the other matters noted above.

The Administration is concerned that S. 1645, as written, represents a novel intrusion into federalism and the rights of states to regulate matters within their own boundaries. The Administration believes, however, that legislation which reflects the concerns noted above, and is carefully targeted towards punishing non-relatives who transport minors across state lines for the purposes of avoiding parental involvement requirements, would serve to minimize the federalism concerns.

S/  
OMB

RECORD TYPE: PRESIDENTIAL (NOTES READ RECEIPT)

CREATOR: Elena Kagan ( CN=Elena Kagan/OU=OPD/O=EOP [ OPD ] )

CREATION DATE/TIME: 9-JUN-1998 17:01:20.00

SUBJECT: RECEIVED: LABOR Report on HR2661, H.R. 2869, and H.R. 2873--DEADLINE IS COB TODAY

TO: Melissa N. Benton ( CN=Melissa N. Benton/OU=OMB/O=EOP [ OMB ] )

READ:UNKNOWN

TEXT:

RETURN RECEIPT

Your Document:

LABOR Report on HR2661, H.R. 2869, and H.R. 2873--DEADLINE IS COB TODAY

was successfully received by:

CN=Elena Kagan/OU=OPD/O=EOP

at:

06/09/98 04:55:33 PM

RECORD TYPE: PRESIDENTIAL (NOTES MAIL)

CREATOR: Elena Kagan ( CN=Elena Kagan/OU=OPD/O=EOP [ OPD ] )

CREATION DATE/TIME: 9-JUN-1998 16:56:13.00

SUBJECT: food safety

TO: Mary L. Smith ( CN=Mary L. Smith/OU=OPD/O=EOP @ EOP [ OPD ] )  
READ:UNKNOWN

TO: Thomas L. Freedman ( CN=Thomas L. Freedman/OU=OPD/O=EOP @ EOP [ OPD ] )  
READ:UNKNOWN

TEXT:

fyi- Laura

----- Forwarded by Elena Kagan/OPD/EOP on 06/09/98 04:55  
PM -----

Barry J. Toiv

06/09/98 03:45:14 PM

Record Type: Record

To: See the distribution list at the bottom of this message  
cc: Michelle Crisci/WHO/EOP  
Subject: food safety

I trust you saw yesterday's Washington Times piece quoting Republicans  
opposing food safety initiatives.

Message Sent

To: \_\_\_\_\_  
Rahm I. Emanuel/WHO/EOP  
Ann F. Lewis/WHO/EOP  
Bruce N. Reed/OPD/EOP  
Elena Kagan/OPD/EOP  
Stacie Spector/WHO/EOP

RECORD TYPE: PRESIDENTIAL (NOTES MAIL)

CREATOR: Elena Kagan ( CN=Elena Kagan/OU=OPD/O=EOP [ OPD ] )

CREATION DATE/TIME:14-JUN-1998 13:25:43.00

SUBJECT: Re: Self-assessment guide

TO: Bruce N. Reed ( CN=Bruce N. Reed/OU=OPD/O=EOP [ OPD ] )

READ:UNKNOWN

TEXT:

fyi

----- Forwarded by Elena Kagan/OPD/EOP on 06/14/98 01:25  
PM -----

Sylvia M. Mathews

06/13/98 03:37:33 PM

Record Type: Record

To: Edward W. Correia/WHO/EOP

cc: See the distribution list at the bottom of this message

bcc:

Subject: Re: Self-assessment guide

I agree with the recommendation. Let's pull the plug.

Edward W. Correia

06/11/98 01:52:01 PM

Record Type: Record

To: Charles F. Ruff/WHO/EOP, Sylvia M. Mathews/WHO/EOP, Maria Echaveste/WHO/EOP

cc: Peter Rundlet/WHO/EOP, Tanya E. Martin/OPD/EOP, Robert M.

Shireman/OPD/EOP, Scott R. Palmer/PIR/EOP

Subject: Self-assessment guide

We met with the civil rights groups this morning to discuss the draft guide on affirmative action for higher education. Representatives of DOJ and OCR were there as well.

There have always been some underlying difficulties in drafting this document. Unlike other areas, e.g., benchmarking, federal hiring, and DOT rulemaking, this has not been an exercise in our "mending" our own affirmative action policies. Instead, the idea has been to state the law as it now stands in order to provide guidance to universities.

However, as the groups argued, it is impossible to state the law clearly and completely, given that there are so many unanswered questions. The more specific the document, the more we have to put our own interpretation on the Court's cryptic statements in this area, and the more we make it difficult for others to argue their interpretations. On the other hand, if we issue a highly general statement, the document is not really useful, and it certainly does not provide a "mend it, don't end it" message.

As a result, there is a consensus among White House and agency staff that, for the time being at least, we should abandon the effort to

issue a document that purports to set out the law of affirmative action in this area. We should continue doing what we have already been doing, which is providing technical assistance to universities at conferences and in other informal settings. This decision was somewhat painful given that DOJ and OCR staff have spent hundreds of hours in drafting. However, they agree with this approach, too. In addition, we believe that we should look for an opportunity to get out this basic message: the administration believes that affirmative action in higher education is constitutional and strongly supports it. That message can be conveyed in other ways, for example, in a statement by the POTUS this fall.

Consequently, our advice is not to issue this document and to tell the civil rights groups informally of our decision. I will wait to hear from you before I contact them.

Message Copied

To: \_\_\_\_\_

Charles F. Ruff/WHO/EOP

Maria Echaveste/WHO/EOP

Peter Rundlet/WHO/EOP

Tanya E. Martin/OPD/EOP

Robert M. Shireman/OPD/EOP

Scott R. Palmer/PIR/EOP

Elena Kagan/OPD/EOP

RECORD TYPE: PRESIDENTIAL (NOTES READ RECEIPT)

CREATOR: Elena Kagan ( CN=Elena Kagan/OU=OPD/O=EOP [ OPD ] )

CREATION DATE/TIME:15-JUN-1998 13:24:02.00

SUBJECT: RECEIVED: URGENT: Tobacco Letters

TO: Kate P. Donovan ( CN=Kate P. Donovan/OU=OMB/O=EOP [ OMB ] )

READ:UNKNOWN

TEXT:

RECORD TYPE: PRESIDENTIAL (NOTES READ RECEIPT)

CREATOR: Elena Kagan ( CN=Elena Kagan/OU=OPD/O=EOP [ OPD ] )

CREATION DATE/TIME:15-JUN-1998 11:26:14.00

SUBJECT: RECEIVED: Need clearance -- Revised tobacco letter

TO: Kate P. Donovan ( CN=Kate P. Donovan/OU=OMB/O=EOP [ OMB ] )  
READ:UNKNOWN

TEXT:



June 11, 1998

MEMORANDUM FOR THE PRESIDENT

FROM: Bruce Reed  
Elena Kagan

SUBJECT: DPC Weekly Report

**1. Tobacco -- Senate Update:** The Senate passed several important amendments to the McCain bill this week. The Craig-Coverdell amendment, approved by a 52-46 vote, authorizes about \$2 billion per year for anti-drug efforts. Although we support most of these efforts, the money for them would come out of the funds previously reserved for public health programs: if the appropriators were to provide the full amounts authorized for these anti-drug efforts, funding for smoking cessation, education, and counteradvertising programs would decrease by about 80 percent. The amendment also prohibits the use of federal monies for needle exchange and allows states to give education vouchers to students who have been the victims of school violence.

The Senate also passed by a vote of 50-48 the Gramm tax-cut amendment. The Gramm amendment would cost \$16 billion over the first four years and an additional \$30 billion in the next five years; in these years, all the cost would come out of tobacco revenues. After 2008, the estimated cost of the proposal would increase dramatically to over \$10 billion each year; one-third of all tobacco revenues would go to pay for this tax cut, with other revenues (presumably the surplus) accounting for the rest. The amendment would provide all couples with annual incomes below \$50,000 a new tax deduction of \$825 this year, rising to \$3,300 in 2008, and would provide full deductibility of health insurance for the self-employed.

Finally, the Senate passed by a vote of 66-33 an amendment sponsored by Senators Kerry and Bond to require states to spend 25 percent of the funds they receive under the bill on child care subsidies. (States would have to spend another 25 percent of their funds on the menu of programs we negotiated with the NGA, which includes child care subsidies; states could do whatever they wished with the remaining 50 percent of their funds.)

As a result of these votes, key groups have expressed concern about the diminishing dollars available to them. The Governors have drafted a letter objecting to the state financing section of the bill because the funding level has dropped below the \$196.5 billion over 25 years originally provided in the bill (the same level contained in the June 20 settlement). The Governors also may object to the further restrictions placed on state spending by the passage of the Kerry-Bond amendment. At the same time, public health groups such as the Campaign for Tobacco Free Kids, the American Cancer Society, and the American Heart Association are

deeply concerned that sufficient funding will not be available for anti-smoking programs. Erskine, Secretary Shalala, and we met with them on Friday to explain that the bill would not move through the Senate without funding for tax cuts and anti-drug programs, and to urge them to work hard over the next few days to achieve final passage.

With the addition of a tax cut and anti-drug programs, Republicans should find it more difficult to oppose the bill. Many Republican Senators, however, harbor a very deep hostility to this legislation, and they read new polls to suggest that obstructing it will have little electoral consequence. Senator Lott sharply criticized the bill on this Sunday's talk shows and indicated that it would not pass the Senate. He noted that the Senate still had not dealt with the issues of tobacco farmers or attorneys' fees and that either issue could cause the legislation to explode. (Actually, the Senate has rejected two amendments to cap attorneys' fees -- one limiting fees to \$250 per hour and the other limiting fees to \$1,000 per hour -- but apparently Lott believes this issue remains open.) He also indicated that while there were not 50 votes in the Senate to defeat the legislation, there also were not the 60 votes necessary to pass it.

You will be speaking on Monday to 150 high school Presidential scholars and can use the event to urge swift passage of the tobacco legislation.

**2. Education -- National Testing: The National Academy of Sciences (NAS) released an interim report last week, as required by last year's Labor-HHS-Education appropriations bill, on the feasibility of linking scores from existing commercial and state reading and math tests to each other and/or to NAEP. The NAS concluded that it is not technically feasible to compare student scores on different tests to each other and/or to the NAEP standards. This conclusion of course undermines Rep. Goodling's argument that existing tests could be used to accomplish the purpose of a national test in reading and math. We do not expect, however, that this report will dampen his opposition to our testing initiative. Indeed, earlier this week, he received assurances from the Republican leadership about supporting an anti-testing rider on this year's appropriations bill. (The leadership provided these assurances when they decided to remove an anti-testing provision, as well as a sweeping education block grant provision, from the conference report on the Craig-Coverdell education tax bill; as you know, they believe that removing these provisions will make it harder for you to veto the bill.)**

**3. Crime -- PRIDE Study: The National Parents' Resource Institute for Drug Education (PRIDE) will release on Thursday its annual survey on teen drug use and violence for the 1997-98 school year. We have not yet seen the data on drug use among teens, but PRIDE has shared with us some of its findings on school violence. The study finds that the percentage of students who reported carrying a gun to school decreased by over a third since the 1993-94 school year -- from 6 percent to 3.8 percent (or nearly 1 million students). Of those students who brought a gun to school, almost half did so six or more times, over half threatened to harm a teacher, and nearly two-thirds threatened to harm another student. Drug use was very high among students carrying guns: 30 percent used cocaine in the month prior to**

carrying a gun to school; 32 percent used stimulants such as methamphetamine; and 31 percent used hallucinogens. Perhaps most important, the survey reaffirms the effectiveness of involving kids in after-school programs and school activities. Students who did not bring guns to school were 53 percent more likely to be involved in after-school programs and 34 percent more likely to be active in school activities (such as band and sports teams) than those who carried guns.

**4. Child Care -- House Legislation: The First Lady and Secretary Shalala joined House Democrats last week as they unveiled a comprehensive child care bill that includes all the pieces of your child care initiative, plus a tax credit for families with a stay-at-home parent and children under four years of age. The \$20 billion package will be sponsored by more than 100 members. The proposal does not specify funding sources.**

**5. Child Care -- After-School Event: You are currently scheduled to announce on Wednesday \$40 million in grants for after-school programs. These grants, the first awarded under the new 21st Century Learning Centers Program, will allow 315 schools in 36 states to establish or expand after-school initiatives. You also will release a new report, titled *Safe and Smart: Making the After-School Hours Work for Kids* and jointly authored by the Departments of Justice and Education, which finds that quality after-school programs decrease juvenile crime and improve the academic performance of participating children. This event, also involving the First Lady and Vice President, will support our efforts to expand the 21st Century Learning Centers Program in this year's appropriations process.**

**6. Health -- Patients' Bill of Rights: Larry Stein and Chris Jennings met with Rep. Dingell last week to discuss patients' bill of rights legislation. Dingell said he would work closely with the Administration in the event that he and Rep. Norwood begin to talk seriously about developing a unified bill to be brought to the floor by way of a discharge petition. For the moment, Dingell believes (and we agree) that he should stand firmly behind his bill as written, including its state-court liability enforcement provisions, rather than signal any willingness to compromise. Dingell noted, however, that the CBO may soon issue a high estimate of the costs associated with his bill's enforcement provision. We have heard that the Republican leadership has insisted on reviewing the CBO's estimate before it is released and is subjecting the CBO staff to relentless pressure. We will talk with Dingell about an appropriate response when we learn more about the CBO's estimate.**

**7. Health -- Vice President's Announcement of the Quality Forum: The Vice President is scheduled to unveil on Wednesday a planning committee to establish a "Quality Forum," a private sector entity that will develop and disseminate uniform standards for high-quality health care. Your Quality Commission recommended establishing this Forum, and you asked the Vice President to oversee the process. In conjunction with this announcement, we are releasing a report that highlights the many shortcomings of the current system: the report will note, for example, one study's estimate that preventable errors in hospital care lead to 180,000 needless deaths**

each year. **Developing uniform measures of quality and encouraging health plans to adopt these measures has great potential to improve health outcomes, increase confidence in the health care system, and save costs. We will describe this effort as the natural complement to our patients' bill of rights proposal in the effort to promote health care quality.**

**8. Health -- FDA Commissioner:** We plan to announce the nomination of the new FDA commissioner, Jane Henney, as soon as the Senate completes consideration of the McCain bill. (We do not think it would be helpful either to confirming Henney or to passing the tobacco bill to announce her nomination in the middle of the current debate in the Senate.) So far, advance word of her nomination has prompted neither major objections nor strong support. It is possible that Republicans will try to portray Henney as a David Kessler protégé essentially chosen by Senator Kennedy. One positive development is that Senator Domenici has agreed to accompany Henney on courtesy visits to Republican members of the Senate Labor Committee.

**9. Housing/Welfare Reform -- Welfare-to-Work Housing Vouchers:** The Senate Appropriations Subcommittee for VA and HUD last week voted in favor of a demonstration program that would give \$40 million to seven cities or counties for 7,000 "self-sufficiency" housing vouchers targeted to people moving from welfare to work. The seven sites chosen were New York City, Los Angeles, Cleveland, Miami-Dade County, Anchorage, Charlotte, and Prince George's County. Although the Subcommittee provided substantially fewer welfare-to-work vouchers than the Administration requested -- 7,000 instead of 50,000 -- the vote is a good first step for the Administration's initiative. The Chair of the VA/HUD Subcommittee in the House (Jerry Lewis) has expressed interest in the program, and we are hopeful that he will support a greater number of vouchers.

**10. Welfare Reform -- Portland Study:** HHS is preparing to release an evaluation of Portland, Oregon's mandatory welfare reform program which shows that the program has led to increased employment and earnings and reduced welfare expenditures. The study, conducted by Manpower Demonstration Research Corporation as part of HHS's national evaluation of welfare-to-work strategies, tracked over 5,500 recipients from 1993 through mid-1996. The study found that after two years, participants in the program had earnings that were 35 percent higher and employment levels that were 11 percent higher than comparable individuals in the control group. Participants also received 17 percent less in welfare payments than people in the control group; 41 percent of program participants still received welfare after two years, as compared with 53 percent in the control group. The program had a measurable positive impact both for people with few barriers to employment and for people considered harder to place.

Portland required all welfare recipients with children older than one year to participate in its program and sanctioned 21 percent of recipients for failure to

comply with program rules. (The sanction rate is in the mid-range for comparable programs.) The program generally had a strong employment focus, but a significant number of participants also participated in short-term education and training activities. The staff emphasized child care arrangements in their case management, and the program had relatively high child care usage and costs. The program, however, did not increase overall welfare costs.

**11. Welfare Reform -- New Jersey Family Cap Study:** Secretary Shalala has sent you a memo on the draft Rutgers University study issued last week which concluded that New Jersey's family cap policy has resulted in a "small but non-trivial" effect on abortion rates (an estimated additional 240 abortions per year). As the memo relates, both New Jersey and HHS have raised serious questions about the study's methodology and findings. Rutgers is currently revising the study in response to these criticisms. A total of 22 states have adopted a family cap policy since the passage of the welfare law (up from 15 states that had waivers to implement this policy).

**12. Disabilities -- Bunning-Kennelly Legislation:** The House last week passed legislation, sponsored by Reps. Bunning and Kennelly and supported by both the Administration and the disability community, to move SSDI and SSI beneficiaries into the workforce by using a "pay for performance" approach. People on the SSDI and SSI rolls currently get rehabilitation services through state vocational rehabilitation agencies, which receive reimbursement for their costs. Under Bunning-Kennelly, beneficiaries could choose their own rehabilitation providers from among a number of public and private entities. Providers that successfully assist beneficiaries to leave the rolls and return to work would receive a percentage of the disability benefits saved. These payments would continue as long as the person remained off the rolls, up to a maximum of five years. The premise of the bill is that providers will have a greater interest in their clients' long-term success if they are rewarded for results rather than reimbursed for costs. **Notwithstanding widespread support for this approach, the bill's fate in the Senate is uncertain. Senators Jeffords and Kennedy may not want to move the bill unless it is paired with their proposal to extend Medicare and Medicaid benefits to those leaving SSDI or SSI. We have a number of problems with the Jeffords-Kennedy bill, including its cost (estimated at over \$1 billion each year) and complexity. We are meeting this week with staff for the Senators to discuss these issues, as well as the possibility of moving the Bunning-Kennelly bill forward.**

RECORD TYPE: PRESIDENTIAL (NOTES MAIL)

CREATOR: Elena Kagan ( CN=Elena Kagan/OU=OPD/O=EOP [ OPD ] )

CREATION DATE/TIME:16-JUN-1998 10:29:58.00

SUBJECT: Save the Date - Susan Liss Going Away

TO: Laura Emmett ( CN=Laura Emmett/OU=WHO/O=EOP @ EOP [ WHO ] )  
READ:UNKNOWN

TEXT:

please schedule

----- Forwarded by Elena Kagan/OPD/EOP on 06/16/98 10:29 AM -----

Trooper Sanders @ OVP  
06/15/98 11:18:01 PM  
Record Type: Record

To: See the distribution list at the bottom of this message  
cc:  
Subject: Save the Date - Susan Liss Going Away

The going away party for Susan Liss will be June 30, 5-6p.m. (extact time TBD), VP Ceremonial Office. Please email me or Aimee Malnati with questions or rsvp. Thank you.

Message Sent

To: \_\_\_\_\_  
Sylvia M. Mathews/WHO/EOP  
John Podesta/WHO/EOP  
Thurgood Marshall Jr/WHO/EOP.  
Minyon Moore/WHO/EOP  
Lynn G. Cutler/WHO/EOP  
Audrey T. Haynes/WHO/EOP  
Maria Echaveste/WHO/EOP  
Dawn M. Chirwa/WHO/EOP  
Sally Katzen/OPD/EOP  
Betty W. Currie/WHO/EOP  
Heather M. Marabeti/OVP @ OVP  
Elena Kagan/OPD/EOP  
Ellen M. Lovell/WHO/EOP  
gbritton @ whitehousefellows.gov @ INET @ VAXGTWY  
Katharine Button/WHO/EOP  
Roberta W. Greene/WHO/EOP

RECORD TYPE: PRESIDENTIAL (NOTES READ RECEIPT)

CREATOR: Elena Kagan ( CN=Elena Kagan/OU=OPD/O=EOP [ OPD ] )

CREATION DATE/TIME:16-JUN-1998 20:27:13.00

SUBJECT: RECEIVED: URGENT: Need clearance - T/P Approps. letter

TO: Kate P. Donovan ( CN=Kate P. Donovan/OU=OMB/O=EOP [ OMB ] )

READ:UNKNOWN

TEXT:



June 16, 1998

The Honorable George Voinivich (CHECK SPELLING AND APPROPRIATE TITLES)  
Chair  
The Honorable Thomas Carper  
Vice Chair  
National Governors Association  
444 North Capitol Street  
Washington, D.C. 20001

Dear Governor Voinivich and Governor Carper:

In response to your request for clarification about my position to S. 1415, the National Tobacco Policy and Youth Smoking Reduction Act, I am writing to reiterate my strong opposition to actions by the Senate to further reduce the State Litigation Settlement Account or impose any additional restrictions to it. Since the beginning of the Senate floor debate, I have opposed amendments that reduce the original \$196.5 billion state allocation that was envisioned in the original Attorney Generals' Agreement.

OPTION 1 for 2nd paragraph:

It is my firm belief that we would not be having a debate on bipartisan comprehensive legislation without the efforts of the states and their attorney generals. As such, I will insist than any legislation adequately reflect the important state contributions to reducing the use of tobacco by our nation's children. I believe this commitment was illustrated by the joint agreement we reached regarding the level and uses of state funds that was included in the original McCain/Lott managers agreement. (NGA WANTS A SENTENCE LIKE THIS; ACTUALLY THEY WANT A REITERATION OF OUR SUPPORT FOR THE AGREEMENT, BUT I THINK THEY CAN LIVE WITH THIS. A difference way of saying same thing that may read a little better is outlined below)

OPTION 2 for 2nd paragraph:

It is my firm belief that we would not be having a debate on bipartisan comprehensive legislation without the efforts of the states and their attorney generals. It is for this reason that we worked so hard to reach the agreement that was included in the original McCain/Lott managers amendment regarding the level and uses of state funds. While the Senate has amended this agreement, you can be assured that I will insist than any final bill adequately reflects the essential contributions states have made toward reducing the use of tobacco by our nation's children.

As experienced lawmakers, I know you recognize that this bill will go through significant changes before final passage. I want to reiterate my strong commitment to working with you in the weeks ahead to ensure that a strong, equitable and comprehensive tobacco bill is enacted into law.

RECORD TYPE: PRESIDENTIAL (NOTES MAIL)

CREATOR: Elena Kagan ( CN=Elena Kagan/OU=OPD/O=EOP [ OPD ] )

CREATION DATE/TIME:16-JUN-1998 17:46:56.00

SUBJECT: Uniform Division Protest

TO: Laura Emmett ( CN=Laura Emmett/OU=WHO/O=EOP @ EOP [ WHO ] )

READ:UNKNOWN

TEXT:

----- Forwarded by Elena Kagan/OPD/EOP on 06/16/98 05:46  
PM -----

Jose Cerda III  
06/16/98 02:18:41 PM  
Record Type: Record

To: Karen Tramontano/WHO/EOP  
cc: Michelle Crisci/WHO/EOP, Elena Kagan/OPD/EOP, Christa  
Robinson/OPD/EOP, Leanne A. Shimabukuro/OPD/EOP  
Subject: Uniform Division Protest

Karen:

In talking about the Secret Service protest tomorrow at our staff meeting today, we thought we should probably do a Q&A for McCurry's brief tomorrow, and that you'd be the best suited to the task. Any chance you'll have a spare moment to do a few lines on this? If not, what guidance do you suggest we give the press office on this planned protest? I'm also going to check w/Rahm to see where he is on this.

Jose'



May 29, 1998

MEMORANDUM FOR THE PRESIDENT

FROM: Bruce Reed  
Elena Kagan

SUBJECT: DPC Weekly Report

**1. Tobacco -- Senate Update:** When the Senate returns from recess, it is scheduled to return to the McCain legislation and resume consideration of an amendment by Sen. Durbin to increase look back penalties and an amendment by Sen. Gramm to provide a tax cut for married couples with income of less than \$50,000 per year. Other potential amendments include: two complete substitutes (one by Senator Nickles and one by Senators Hatch and Feinstein), additional tax proposals (possibly including a slimmed-down version of the Gramm amendment, as well as a Roth-Boxer proposal for health care tax cuts), several anti-drug measures (see our separate memo on Monday), an anti-smuggling provision authored by Senator Leahy, a provision on the deductibility of tobacco advertising costs by Senator Reed, and efforts to cut back on FDA jurisdiction. Senator McCain's strong preference is for an early cloture vote, which he believes he can win. Senator Lott opposes an early cloture vote, on the theory that his caucus will only harden if it feels jammed. Senator Daschle is still considering the question. We tend to agree with McCain, for fear that the bill will become weighed down with too many amendments and consideration of it will drag on forever. We and Larry will have further discussions of this question with the relevant Senate players this weekend.

**2. Tobacco -- Farmers:** The DPC and USDA are trying to ensure a favorable conclusion to the current dispute over providing assistance to tobacco farmers. As you know, the McCain bill now contains both Senator Lugar's and Senator Ford's proposals. The Ford measure, which we, public health groups, and most Democrats support, provides for an optional buy-out and preserves the price support program, at a cost of \$28.5 billion over 25 years. The Lugar measure, which most Republicans support, provides for a mandatory buy-out and ends the price support program (creating a free market in tobacco), at a cost of \$18 billion over three years. USDA calculates that Lugar would lead to an increase in the amount of tobacco grown in this country and a consequent decrease in its cost -- saving companies as much as \$20 billion over 25 years. In addition, OMB estimates that Lugar would displace 69 percent of the research and public health spending in the McCain bill in the first three years, assuming spending to the states were held constant. We have distributed this information widely, especially to moderate Republicans who should be concerned about the impact of Lugar on public health. We also have made clear to both sides our willingness to broker a compromise (for example, a phase-out of the price support program over 10 or 15 years, or

the creation of a commission to work out the best approach to this issue). As of now, however, both sides think they have the votes to defeat the other (which, in fact, they both might), and compromise discussions have not proved productive.

**3. Tobacco -- Minority Caucus Concerns:** DPC, OMB, and HHS will meet next week with members of the House Minority Caucuses to discuss their views of tobacco legislation -- especially the McCain bill's approach to public health spending. These members have concerns about the Senate bill's use of block grants to states for smoking prevention and cessation programs. They also are upset that the bill contains no direct grants to historically black and predominantly Hispanic colleges, universities, and medical schools. These members have sent us an alternative proposal for public health spending, but the agencies believe that it raises significant constitutional and administrative concerns. The proposal includes funding set-asides for minority groups that the Department of Justice believes run afoul of the Supreme Court's Adarand decision. In addition, the proposal's funding mechanism would create major administrative burdens for the Department of Health and Human Services. We anticipate holding several discussions with members of the Minority Caucuses to work out ways of making them more comfortable with the public health provisions of the legislation.

**4. Welfare Reform -- State Use of TANF Funds:** The NGA Fiscal Survey of States, released on May 27, contained some encouraging information about the way states are using welfare monies. The report showed that states are shifting funds from direct cash payments to work-related supports. Since 1996, spending for cash assistance has decreased 26 percent, while spending for child care has increased 85 percent and spending on work activities has increased 34 percent. Total welfare spending declined by 9 percent, but given caseload reductions, this figure represents increased spending per welfare recipient.

**5. Education -- GAO Report on National Testing:** In response to a request from Rep. Goodling, the GAO will issue a report next week on the roles played by NAGB and the Department of Education in developing the national tests in 4th grade reading and 8th grade math. The report finds that NAGB has full control over development of the tests, as required by law; it finds not a single instance of improper interference by the Department. In addition, the report finds no reason to criticize the procedures NAGB has used to award test development contracts. Although we do not expect the report to mitigate Rep. Goodling's adamant opposition to the tests, it should prevent him from making the claim that test development somehow remains under the influence of the Administration.

**6. Education -- Adult Education:** You recently asked what the Administration had accomplished with respect to adult education and whether we need to take additional steps. The Senate and House workforce investment bills, which Congress is expected to pass by July 1, provide for the reauthorization of all federal adult education programs. Your FY 1999 budget requests a \$16 million increase in grants to states for adult education programs. It also includes a request for funds to develop model English-as-a-second-language programs for adults, since 40 percent of adult education participants are in such programs. In addition,

the Department of Education has funded a PBS series, called "Crossroads Cafe," which is a kind of "Sesame Street" for adults learning English. The program is now shown in 35 states (and 50 foreign countries) and will be expanded shortly. DPC will begin a working group with NEC and the Education Department to explore how we can best highlight the efforts we already have underway, and what additional steps would be appropriate.

**7. Health -- Assisted Suicide:** The Department of Justice plans on releasing a letter next week, in response to an inquiry from Senator Hatch and Congressman Hyde, concluding that the Controlled Substances Act does not give the Drug Enforcement Agency (DEA) authority to take action against physicians who assist their patients to commit suicide. Consistent with your directions, this letter will include a restatement of your longstanding position opposing assisted suicide and an indication of your willingness to consider workable legislation addressing this issue. As you know, we expect that Hatch and Hyde will respond to the Department's letter by introducing a bill authorizing the DEA to take action against physicians for assisting suicide -- a legislative approach that we believe is ill-advised. We will work closely with DOJ to roll-out its letter, and will keep you advised of legislative developments.

**8. Health -- HCFA Letter to Ravenswood Hospital:** The Health Care Financing Administration (HCFA) sent a letter yesterday to Ravenswood Hospital of Chicago threatening it with loss of Medicare funding for policies posing a grave threat to the health and safety of patients. The letter followed an incident in which a 15 year-old died of gunshot wounds just 35 feet from the hospital door after hospital workers refused to leave their posts or even to give police officers a stretcher to bring the young man into the hospital. The HCFA letter states that the hospital will lose funding in three weeks, unless it provides credible evidence within that time of having reformed its emergency room policies and practices. We issued a statement in your name highlighting HCFA's action, as well as urging all hospitals to follow recently released guidance by the American Hospital Association on appropriate emergency procedures.

**9. Health -- Medicare Commission:** The Medicare Commission will hold a meeting on Monday, most of which will be devoted to discussions among the members on the major issues of benefits, costs, eligibility, administration, and financing. (We have told our members that they should feel free to talk openly about controversial policy reforms such as benefit changes, eligibility age changes, and means-testing proposals, but should avoid at this time any serious discussion of new taxes.) In general, the Democratic members are becoming nervous that the Commission's staff is focusing exclusively on questions of program financing, while ignoring issues of program design. They will use this meeting to urge the Commission to address ways of making the Medicare program more responsive to the needs of beneficiaries, at the same time as the Commission takes up the program's financing challenges.

**10. Health -- Long Term Care:** Aging and disability advocates are placing increased pressure on us to address the issues surrounding long-term care. Demographic changes will heighten the demand for these services greatly in the coming years, but cost considerations have deterred both the public and the private sectors from taking up this challenge. Although truly comprehensive approaches are politically and financially unrealistic, we can develop targeted policies that will begin to address the problem. These policies might include: requiring the Federal Employee Health Benefit Plan to offer (but not pay for) long-term care policies; informing Medicare beneficiaries that Medicare does not cover long-term care and advising them of other coverage options; giving more flexibility to States to use home- and community-based care options for elderly and disable people on Medicaid; and providing tax incentives to increase the purchase of private long-term care policies. We are setting up a working group to explore these and other ideas so that you begin to address this important issue shortly.

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CREATOR: Elena Kagan ( CN=Elena Kagan/OU=OPD/O=EOP [ OPD ] )

CREATION DATE/TIME:17-JUN-1998 19:51:33.00

SUBJECT: RECEIVED: URGENT: E&W Senate Floor SAP

TO: Kate P. Donovan ( CN=Kate P. Donovan/OU=OMB/O=EOP [ OMB ] )  
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Your Document:  
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CN=Elena Kagan/OU=OPD/O=EOP  
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06/17/98 07:44:36 PM

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CREATION DATE/TIME:18-JUN-1998 18:09:49.00

SUBJECT: RECEIVED: URGENT: 3:30pm Deadline: E&W HOUSE RULES SAP

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