

NLWJC - KAGAN

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CM014 258307SS

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CM014

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258307 SS
cm014
THE PRESIDENT HAS SEEN
46-98

THE WHITE HOUSE
WASHINGTON

March 30, 1998

MEMORANDUM FOR THE PRESIDENT

FROM: Bruce Reed
Elena Kagan

SUBJECT: Tobacco Update

Senator McCain announced a comprehensive tobacco bill today for mark-up on Wednesday in the Senate Commerce Committee. The bill is not perfect, and we will continue to seek improvements. But it represents real progress (see the attached chart comparing the McCain bill with the June 20th settlement and your positions), and it should enhance the prospects for enacting comprehensive tobacco legislation in this session of Congress.

The Commerce Committee is likely to pass the bill this week with bipartisan support. Among Republicans, Senators Stevens, Gorton, Hutchison, Snowe, and Frist are likely to vote yes; Senators Burns and Ashcroft are likely to vote no; Senators Abraham and Brownback are undecided; and Senator Lott probably will recuse himself. Among Democrats, Senators Hollings, Wyden, Breaux, and Kerry are likely to vote yes; Senators Rockefeller and Dorgan will vote no; and Senators Bryan, Inouye, and Ford are undecided. The mainstream public health groups (Heart Association, Cancer Society, etc.) called the bill an encouraging step forward, but Drs. Koop and Kessler probably will criticize the bill because it contains some liability limits and increases the price of cigarettes less than they would like. The industry responded to McCain's announcement by saying that it would not agree to the legislation, but many observers believe that the industry has taken this position only to prevent the price from increasing still further.

Erskine gave the Administration's response to the bill in your absence. At a previously scheduled speech at the Center for National Policy (given before McCain made the liability provisions of the bill more acceptable to the public health community), Erskine said that the bill laid a good foundation for future efforts, but had room for improvement. In addition to praising Sen. McCain's leadership and process, Erskine lauded the legislation for raising the price of tobacco products substantially, giving the FDA full authority to regulate tobacco products, and including a strong plan to protect tobacco farmers. Erskine criticized the bill for having inadequate lookback penalties, and noted that it did not contain a comprehensive plan for using tobacco revenues to protect the public health and assist children. Erskine said he would not address the liability issues because the rest of the legislation did not yet meet your principles.

The bill emerged from a weeks-long process in which McCain consulted with the Attorneys General, Wall Street analysts, public health leaders, and the Administration. As noted above, at the last moment, McCain changed the liability provisions of the bill -- removing the bar

PHOTOCOPY
WJC HANDWRITING

on class actions and probably on punitive damages -- to get the support of at least some members of the public health community. The final bill, which we summarize more fully below, addresses many of your concerns and offers an opportunity for bipartisan accomplishment.

1. Funding and Per-Pack Price Increase. The McCain bill essentially uses your budget numbers, raising approximately \$70 billion over five years (including a \$10 billion up-front payment) and generating a \$1.10 increase in the price of a pack of cigarettes by 2003. The bill prevents the real price of tobacco products from increasing after the fifth year by including a volume adjustment on annual payments. Some in the public health world, as well as a number of liberal Democrats, will criticize the price rise as insufficient, arguing that an almost immediate \$1.50 increase is required to reduce youth smoking dramatically. Your own plan, however, contains the same price increase, and we have estimated that it will help reduce youth smoking by over 40 percent in five years.

2. FDA Regulation. The bill provides full authority to the FDA to regulate tobacco products. To respond to concerns from pharmaceutical companies about the effect of regulating tobacco under normal "drug and device" authority, we agreed to set up a separate chapter in the Food Drug and Cosmetic Act for tobacco products. We managed to do so, however, without ceding any of the authority the FDA has claimed over tobacco. This victory was hard-fought -- Senators Hatch and Jeffords argued strenuously for language defining the FDA's authority more narrowly -- and will be subject to challenge on the floor. Senators McCain and Frist, however, have committed to fighting off weakening amendments, so we are in the best position possible (given a Republican Congress hostile to the FDA) to emerge from the Senate with full FDA authority.

3. Farmers. The bill contains a plan to protect tobacco farmers and their communities, which has the support of Senators Hollings, Ford, and Robb. We do not yet know the full details of this piece of the legislation, but it is designed to address the concerns of both burley and flue-cured tobacco farmers. Needless to say, it will contain funds fully sufficient for these purposes, and accordingly meets your demand to protect tobacco farmers.

4. Lookback Penalties. The bill provides for non-deductible industry-wide lookback penalties capped at \$3.5 billion per year. The industry will have to pay \$80 million for each percentage point by which it misses youth smoking targets between 0 and 5 percent, \$160 million for each percentage point between six and ten percent, and \$240 million for each percentage point over 11 percent. The industry will hit the \$3.5 billion cap at about a 20 percent miss, so any larger miss will be "free." There are no monetary penalties on individual companies for failing to meet youth smoking targets. The bill does contain a provision for taking away the liability protections of any company that misses the youth smoking targets by more than 20 percent, but this provision has a very large loophole and probably will have little effect as currently drafted.

As Erskine noted in his speech, the penalty provisions are the weakest part of the McCain

bill. We have raised serious concerns about both the \$3.5 billion cap and the absence of any company-specific penalties. We also will try to tighten the provision that makes liability protections contingent on success in reducing youth smoking. We assume that such amendments should not come in committee, but during debate on the floor.

5. Liability Provisions. As late as Sunday, Senator McCain intended to include liability provisions very close to those in the proposed June 20 settlement. These provisions included a \$6 billion cap on annual liability payments (with any judgments beyond the cap rolled over to the next year), as well as prohibitions on class actions and punitive damages. By Monday morning, however, the public health community (including the mainstream groups) had made clear to McCain that they would denounce the bill if it contained these provisions. McCain accordingly modified the legislation to permit class actions. We think the legislation now allows punitive damages as well, but we have not received the new language and are not entirely certain. Drs. Koop and Kessler and some liberal Democrats will oppose the bill because of the remaining liability limits.

A simple cap on damages -- without any limitations on class actions or punitive damage claims -- is the least objectionable form of liability protection for the industry. We will try, however, to raise the cap beyond the level set in the McCain legislation; you should note, for the sake of comparison, that the Harkin-Chafee bill's cap stands at \$12 billion.

6. Budget Issues. The biggest issue left unresolved by the McCain bill is how to allocate tobacco funds. Although the bill takes care of tobacco farmers, and also provides money for smoking cessation, counteradvertising, and some research, it leaves other spending issues for the Senate floor. Senator Domenici's budget resolution would reserve all tobacco funds for Medicare, not even allowing the spending on farming and public health contained in the McCain bill. The Senate will take up amendments to this resolution tomorrow to make tobacco funds available for class size, child care, NIH, farmers, and other purposes. Many Republicans have raised concerns about the Domenici approach, but they may decide to vote for it, on the theory that as long as they have 60 votes for a tobacco bill, they can waive the budget rules anyway.

When the time comes to engage in serious negotiations over how to allocate tobacco funds, we expect bipartisan consensus on 75-80 percent of the spending (\$10 billion over 5 years for farmers; \$10 billion for cessation, counteradvertising, and other public health programs; \$10-15 billion for NIH; and \$20-25 billion for states). The battle will be over how to divide up the remaining \$15 billion or so. Senate Republicans will seek money for Medicare; House Republicans may push Rep. Archer's proposal for health care tax deductions for small business and the self-employed; and Democrats will push for everything from child care to school construction.

* * * * *

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bipartisan support, and it is close to meeting your principles. We should continue, however, to press for real improvements -- particularly in the bill's penalty and liability provisions. Tomorrow, Erskine, Larry, and we will have meetings with Senators McCain, Hollings, and Daschle about how to move forward to enact the strongest possible tobacco legislation.

Comparison of Tobacco Proposals

March 30, 1998

| | Attorneys General | McCain | President |
|---|------------------------------|---------------|--|
| Substantial Price Increase | No | Yes | Yes |
| Strong Industry and Company Penalties | No | No | Yes |
| Full FDA Authority | No | Yes | Yes |
| Strong Advertising and Access Provisions | Yes | Yes | Yes |
| Protections of Tobacco Farmers | No | Yes | Yes |
| Comprehensive Plan to Use Tobacco Revenue to Protect Public Health and Assist Children | Yes | No* | Yes |
| Strong Environmental Tobacco Smoke Provision | Yes | No | Yes |
| Liability Protections for Industry: | | | |
| 1. Liability Cap | Yes | Yes | Only if bill meets President's public health principles. |
| 2. Bar on Class Actions | Yes | No | Only if bill meets President's public health principles. |
| 3. Bar on Punitive Damages | Yes | Uncertain | Only if bill meets President's public health principles. |

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TIME OF TRANSMISSION: _____

~~SECRET~~

TIME OF RECEIPT: _____

[Document is not classified. Stamp used in error]

Ry 5/14/09

**WHITE HOUSE
SITUATION ROOM**

PRECEDENCE: _____

IMMEDIATE
PRIORITY
ROUTINE

RELEASER: _____
DTG: _____

MESSAGE NO: _____ CLASSIFICATION: ~~SECRET~~ PAGES: 23
(Including Cover)

FROM: PHIL CAPLAN 202-456-2702 GR FL/WW
(NAME) (PHONE NUMBER) (ROOM NO.)

MESSAGE DESCRIPTION: ERSKINE BOWLES DAILY REPORT WITH REED/KAGAN
TOBACCO UPDATE AND CEA NUMBERS.

| <u>TO (AGENCY)</u> | <u>DELIVER TO</u> | <u>DEPT/ROOM NO.</u> | <u>PHONE NUMBER</u> |
|--------------------|-------------------------|----------------------|---------------------|
| | SYLVIA MATHEWS (FOR THE | PRESIDENT | |
| | cc: CHERYL MILLS | | |
| | DOUG SOSNIK | | |
| | KRIS ENGSKOV | | |
| | | | |
| | | | |
| | | | |
| | | | |

PLEASE DELIVER BY 6:30 A.M. DO NOT WAKE ANYONE TONIGHT.

REMARKS:

THE WHITE HOUSE
WASHINGTON

March 30, 1998

MEMORANDUM FOR THE PRESIDENT

'98 MAR 30 PM 10:33

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Elena Kagan

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258307

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March 30, 1998

MEMORANDUM FOR THE PRESIDENT

98 MAR 30 4:10:13

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WHITE HOUSE STAFFING MEMORANDUM

Date: 3/30/98 ACTION / CONCURRENCE / COMMENT DUE BY: --

Subject: Tobacco Update

| | ACTION | FYI | | ACTION | FYI |
|----------------|--------------------------|-------------------------------------|----------|--------------------------|-------------------------------------|
| VICE PRESIDENT | <input type="checkbox"/> | <input checked="" type="checkbox"/> | McCURRY | <input type="checkbox"/> | <input checked="" type="checkbox"/> |
| BOWLES | <input type="checkbox"/> | <input checked="" type="checkbox"/> | McGINTY | <input type="checkbox"/> | <input type="checkbox"/> |
| McLARTY | <input type="checkbox"/> | <input type="checkbox"/> | NASH | <input type="checkbox"/> | <input type="checkbox"/> |
| PODESTA | <input type="checkbox"/> | <input checked="" type="checkbox"/> | REED | <input type="checkbox"/> | <input type="checkbox"/> |
| MATHEWS | <input type="checkbox"/> | <input checked="" type="checkbox"/> | RUFF | <input type="checkbox"/> | <input checked="" type="checkbox"/> |
| RAINES | <input type="checkbox"/> | <input checked="" type="checkbox"/> | SMITH | <input type="checkbox"/> | <input type="checkbox"/> |
| BEGALA | <input type="checkbox"/> | <input checked="" type="checkbox"/> | SOSNIK | <input type="checkbox"/> | <input type="checkbox"/> |
| BERGER | <input type="checkbox"/> | <input type="checkbox"/> | SPERLING | <input type="checkbox"/> | <input checked="" type="checkbox"/> |
| BLUMENTHAL | <input type="checkbox"/> | <input type="checkbox"/> | STEIN | <input type="checkbox"/> | <input checked="" type="checkbox"/> |
| ECHAVESTE | <input type="checkbox"/> | <input checked="" type="checkbox"/> | STERN | <input type="checkbox"/> | <input type="checkbox"/> |
| EMANUEL | <input type="checkbox"/> | <input checked="" type="checkbox"/> | STREETT | <input type="checkbox"/> | <input type="checkbox"/> |
| GIBBONS | <input type="checkbox"/> | <input type="checkbox"/> | VERVEER | <input type="checkbox"/> | <input type="checkbox"/> |
| IBARRA | <input type="checkbox"/> | <input type="checkbox"/> | WALDMAN | <input type="checkbox"/> | <input type="checkbox"/> |
| KLAIN | <input type="checkbox"/> | <input type="checkbox"/> | YELLEN | <input type="checkbox"/> | <input type="checkbox"/> |
| LEWIS | <input type="checkbox"/> | <input type="checkbox"/> | _____ | <input type="checkbox"/> | <input type="checkbox"/> |
| LINDSEY | <input type="checkbox"/> | <input type="checkbox"/> | _____ | <input type="checkbox"/> | <input type="checkbox"/> |
| MARSHALL | <input type="checkbox"/> | <input type="checkbox"/> | _____ | <input type="checkbox"/> | <input type="checkbox"/> |
| | | | _____ | <input type="checkbox"/> | <input type="checkbox"/> |

REMARKS: This has been forwarded to the President.

RESPONSE:

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SUBJECT: Tobacco Update

Senator McCain announced a comprehensive tobacco bill today for mark-up on Wednesday in the Senate Commerce Committee. The bill is not perfect, and we will continue to seek improvements. But it represents real progress (see the attached chart comparing the McCain bill with the June 20th settlement and your positions), and it should enhance the prospects for enacting comprehensive tobacco legislation in this session of Congress.

The Commerce Committee is likely to pass the bill this week with bipartisan support. Among Republicans, Senators Stevens, Gorton, Hutchison, Snowe, and Frist are likely to vote yes; Senators Burns and Ashcroft are likely to vote no; Senators Abraham and Brownback are undecided; and Senator Lott probably will recuse himself. Among Democrats, Senators Hollings, Wyden, Breaux, and Kerry are likely to vote yes; Senators Rockefeller and Dorgan will vote no; and Senators Bryan, Inouye, and Ford are undecided. The mainstream public health groups (Heart Association, Cancer Society, etc.) called the bill an encouraging step forward, but Drs. Koop and Kessler probably will criticize the bill because it contains some liability limits and increases the price of cigarettes less than they would like. The industry responded to McCain's announcement by saying that it would not agree to the legislation, but many observers believe that the industry has taken this position only to prevent the price from increasing still further.

Erskine gave the Administration's response to the bill in your absence. At a previously scheduled speech at the Center for National Policy (given before McCain made the liability provisions of the bill more acceptable to the public health community), Erskine said that the bill laid a good foundation for future efforts, but had room for improvement. In addition to praising Sen. McCain's leadership and process, Erskine lauded the legislation for raising the price of tobacco products substantially, giving the FDA full authority to regulate tobacco products, and including a strong plan to protect tobacco farmers. Erskine criticized the bill for having inadequate lookback penalties, and noted that it did not contain a comprehensive plan for using tobacco revenues to protect the public health and assist children. Erskine said he would not address the liability issues because the rest of the legislation did not yet meet your principles.

The bill emerged from a weeks-long process in which McCain consulted with the Attorneys General, Wall Street analysts, public health leaders, and the Administration. As noted above, at the last moment, McCain changed the liability provisions of the bill -- removing the bar

on class actions and probably on punitive damages -- to get the support of at least some members of the public health community. The final bill, which we summarize more fully below, addresses many of your concerns and offers an opportunity for bipartisan accomplishment.

1. Funding and Per-Pack Price Increase. The McCain bill essentially uses your budget numbers, raising approximately \$70 billion over five years (including a \$10 billion up-front payment) and generating a \$1.10 increase in the price of a pack of cigarettes by 2003. The bill prevents the real price of tobacco products from increasing after the fifth year by including a volume adjustment on annual payments. Some in the public health world, as well as a number of liberal Democrats, will criticize the price rise as insufficient, arguing that an almost immediate \$1.50 increase is required to reduce youth smoking dramatically. Your own plan, however, contains the same price increase, and we have estimated that it will help reduce youth smoking by over 40 percent in five years.

2. FDA Regulation. The bill provides full authority to the FDA to regulate tobacco products. To respond to concerns from pharmaceutical companies about the effect of regulating tobacco under normal "drug and device" authority, we agreed to set up a separate chapter in the Food Drug and Cosmetic Act for tobacco products. We managed to do so, however, without ceding any of the authority the FDA has claimed over tobacco. This victory was hard-fought -- Senators Hatch and Jeffords argued strenuously for language defining the FDA's authority more narrowly -- and will be subject to challenge on the floor. Senators McCain and Frist, however, have committed to fighting off weakening amendments, so we are in the best position possible (given a Republican Congress hostile to the FDA) to emerge from the Senate with full FDA authority.

3. Farmers. The bill contains a plan to protect tobacco farmers and their communities, which has the support of Senators Hollings, Ford, and Robb. We do not yet know the full details of this piece of the legislation, but it is designed to address the concerns of both burley and flue-cured tobacco farmers. Needless to say, it will contain funds fully sufficient for these purposes, and accordingly meets your demand to protect tobacco farmers.

4. Lookback Penalties. The bill provides for non-deductible industry-wide lookback penalties capped at \$3.5 billion per year. The industry will have to pay \$80 million for each percentage point by which it misses youth smoking targets between 0 and 5 percent, \$160 million for each percentage point between six and ten percent, and \$240 million for each percentage point over 11 percent. The industry will hit the \$3.5 billion cap at about a 20 percent miss, so any larger miss will be "free." There are no monetary penalties on individual companies for failing to meet youth smoking targets. The bill does contain a provision for taking away the liability protections of any company that misses the youth smoking targets by more than 20 percent, but this provision has a very large loophole and probably will have little effect as currently drafted.

As Erskine noted in his speech, the penalty provisions are the weakest part of the McCain

bill. We have raised serious concerns about both the \$3.5 billion cap and the absence of any company-specific penalties. We also will try to tighten the provision that makes liability protections contingent on success in reducing youth smoking. We assume that such amendments should not come in committee, but during debate on the floor.

5. Liability Provisions. As late as Sunday, Senator McCain intended to include liability provisions very close to those in the proposed June 20 settlement. These provisions included a \$6 billion cap on annual liability payments (with any judgments beyond the cap rolled over to the next year), as well as prohibitions on class actions and punitive damages. By Monday morning, however, the public health community (including the mainstream groups) had made clear to McCain that they would denounce the bill if it contained these provisions. McCain accordingly modified the legislation to permit class actions. We think the legislation now allows punitive damages as well, but we have not received the new language and are not entirely certain. Drs. Koop and Kessler and some liberal Democrats will oppose the bill because of the remaining liability limits.

A simple cap on damages -- without any limitations on class actions or punitive damage claims -- is the least objectionable form of liability protection for the industry. We will try, however, to raise the cap beyond the level set in the McCain legislation; you should note, for the sake of comparison, that the Harkin-Chafee bill's cap stands at \$12 billion.

6. Budget Issues. The biggest issue left unresolved by the McCain bill is how to allocate tobacco funds. Although the bill takes care of tobacco farmers, and also provides money for smoking cessation, counteradvertising, and some research, it leaves other spending issues for the Senate floor. Senator Domenici's budget resolution would reserve all tobacco funds for Medicare, not even allowing the spending on farming and public health contained in the McCain bill. The Senate will take up amendments to this resolution tomorrow to make tobacco funds available for class size, child care, NIH, farmers, and other purposes. Many Republicans have raised concerns about the Domenici approach, but they may decide to vote for it, on the theory that as long as they have 60 votes for a tobacco bill, they can waive the budget rules anyway.

When the time comes to engage in serious negotiations over how to allocate tobacco funds, we expect bipartisan consensus on 75-80 percent of the spending (\$10 billion over 5 years for farmers; \$10 billion for cessation, counteradvertising, and other public health programs; \$10-15 billion for NIH; and \$20-25 billion for states). The battle will be over how to divide up the remaining \$15 billion or so. Senate Republicans will seek money for Medicare; House Republicans may push Rep. Archer's proposal for health care tax deductions for small business and the self-employed; and Democrats will push for everything from child care to school construction.

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The emergence of the McCain bill is a very positive development. It will attract

bipartisan support, and it is close to meeting your principles. We should continue, however, to press for real improvements -- particularly in the bill's penalty and liability provisions. Tomorrow, Erskine, Larry, and we will have meetings with Senators McCain, Hollings, and Daschle about how to move forward to enact the strongest possible tobacco legislation.

Comparison of Tobacco Proposals
March 30, 1998

| | Attorneys General | McCain | President |
|---|------------------------------|---------------|--|
| Substantial Price Increase | No | Yes | Yes |
| Strong Industry and Company Penalties | No | No | Yes |
| Full FDA Authority | No | Yes | Yes |
| Strong Advertising and Access Provisions | Yes | Yes | Yes |
| Protections of Tobacco Farmers | No | Yes | Yes |
| Comprehensive Plan to Use Tobacco Revenue to Protect Public Health and Assist Children | Yes | No* | Yes |
| Strong Environmental Tobacco Smoke Provision | Yes | No | Yes |
| Liability Protections for Industry: | | | |
| 1. Liability Cap | Yes | Yes | Only if bill meets President's public health principles. |
| 2. Bar on Class Actions | Yes | No | Only if bill meets President's public health principles. |
| 3. Bar on Punitive Damages | Yes | Uncertain | Only if bill meets President's public health principles. |

* Does not attempt to address most spending issues.