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THE WHITE HOUSE
WASHINGTON

May 12, 1998

MEMORANDUM FOR THE PRESIDENT

THE PRESIDENT HAS SEEN
5-14-98

FROM: Bruce Reed
Elena Kagan

SUBJECT: Tobacco Negotiations Status Report

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The key features of the manager's amendment under discussion are as follows:

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Sen. Conrad is worried that if we go this route, we will wind up with far less revenue than is necessary to fund what people expect from a tobacco bill. It is unclear, however, what Sen.

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Conrad would do to respond to the forthcoming CBO estimates. He seems to want to insist on an \$1.50 per pack excise tax, but CBO would score that as above \$2 as well, rendering this approach utterly impractical.

2. Lookbacks. As you recall, the McCain bill has industry-wide lookback penalties capped at approximately \$3.5 billion per year, with no company-specific penalties at all. We have gotten McCain and Hollings to agree to raise the cap on industry-wide penalties to \$4 billion. We have also gotten them to add a company-specific penalty wholly outside the cap of \$1000 per child for every child by which the company misses its youth smoking targets. This figure represents twice the lifetime profits that a company earns from any youth smoker. Finally, we have gotten McCain and Hollings to agree to strengthen the provision linking a 20 percent miss to the loss of liability protection. Under the current provision, when a company misses by more than 20 percent, the government must show that a company committed affirmative misconduct in order to trigger the loss of liability provisions. Under the new provision, when a company misses by this amount, the tobacco company will have to show 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.

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3. Liability. As you recall, the McCain bill provides for an annual liability cap of \$6.5 billion, while avoiding the question of whether this money comes from the annual industry payments or from other industry assets. McCain has now agreed to push the liability cap to \$8 billion, the exact amount of the Harkin-Chafee liability cap. (As you recall, you said you would sign Harkin-Chafee.) We have tentatively agreed that (1) half of the upfront payment that the industry makes will go to pay legal judgments and (2) when that amount is depleted, half the amount of judgments will come from the annual payments and half from other assets of the liable company(ies).

Another, perhaps even more tricky set of issues has arisen around other liability provisions in McCain. First, the legislation provides that suits for tobacco related disease can be brought only against a tobacco product manufacturer, and not against a wide variety of other parties, including their parents and affiliates; officers, directors, employees, agents, or attorneys; importers, distributors, wholesalers, and retailers; suppliers of component or constituent parts; growers; and insurers. We have succeeded in removing this liability protection for parents and affiliates. We do not think anyone cares about removing protection for growers, suppliers, or parties down the distribution chain. Conrad, however, has objected strongly to giving liability protection to attorneys, and we are trying to remove this provision. We may also try to remove

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8. Farmers. We agreed to give Sen. Hollings help in ensuring passage of the LEAF Act. Hollings is worried that he will lose a vote on the floor to substitute Sen. Lugar's farming plan for his own. As you know, Lugar's plan would buy out all tobacco farmers and then end the tobacco price support system; Hollings's plan would compensate tobacco farmers for any loss suffered as a result of legislation (through buyouts and/or subsidies), while keeping the price support system in place.

Please let us know if you have any thoughts on, or objections to, what we are doing in these negotiations.

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