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DATE: July 13, 2000

****AS PASSED BY THE LEGISLATURE****
CHAPTER #: 2000-128, Laws of Florida

HOUSE OF REPRESENTATIVES
AS FURTHER REVISED BY THE COMMITTEE ON
FINANCIAL SERVICES
FINAL ANALYSIS

BILL #: CS/HB 1721
RELATING TO: Tobacco settlement proceeds
SPONSOR(S): Committee on Financial Services and Representative Lacasa
TIED BILL(S):
ORIGINATING COMMITTEE(S)/COMMITTEE(S) OF REFERENCE:

- (1) FINANCIAL SERVICES YEAS 10 NAYS 0
- (2) GOVERNMENTAL RULES AND REGULATIONS (W/D)
- (3) FINANCE & TAXATION YEAS 14 NAYS 2
- (4) GENERAL APPROPRIATIONS (W/D)

I. SUMMARY:

CS/HB 1721 was the number assigned to the comprehensive approach developed by the Legislative Conference Committee appointed to resolve the differences in the House and Senate versions of bills relating to the protection of the tobacco settlement proceeds and the disposition of the resulting funds. Please see Part VI of this analysis for a chronicle of CS/HB 1721 and related Senate bills. Also, please see Part V for related comments.

This bill creates the Tobacco Settlement Finance Corporation, a non-profit, public-benefits corporation, for the purpose of purchasing the state's rights, interest and title to future tobacco settlement payments, subject to the Legislature's approval. The corporation would be governed by a board consisting of the Governor, the Treasurer, the Comptroller and the Attorney General (or designees) and two Senators appointed by the President of the Senate, and two Representatives appointed by the Speaker of the House. After January 7, 2003, the board would include the Chief Financial Officer (or designee), in place of the Treasurer and the Comptroller, as well as the Senate and House appointees. The executive director of the State Board of Administration would serve as the chief executive officer of the corporation.

The bill establishes The Task Force on Tobacco-Settlement Revenue Protection (the task force) to determine the need for and evaluate methods for protecting the state's settlement revenue from significant loss. The task force will consist of the Governor (as Chair), the Comptroller, the Insurance Commissioner, three members of the Senate appointed by the President, and three members of the House of representatives appointed by the Speaker. The task force will submit a recommendation report to the Senate President and Speaker of the House by November 1, 2000. A non-recurring sum of \$100,000 is appropriated from the General Revenue Fund to the SBA to support the operations of the task force.

To assist Florida tobacco farmers in reducing encumbered debt on stranded investment in equipment, the non-recurring sum of \$2.5 M is appropriated from the Tobacco Settlement Clearing Trust Fund to the Department of Agriculture and Consumer Services for the purchase of agricultural equipment used by tobacco farmers or tobacco-producing companies who intend to cease production of that crop, to be resold to anyone other than a person or company who produces tobacco in this state or who holds a quota to produce tobacco in this state. Additionally the University of Florida would receive \$2.5 M from the trust fund to provide on-farm direct assistance to growers in tobacco-producing counties affected by liquidation.

The bill creates s. 768.733, F.S., establishing that the amount of a bond or other surety required to stay the execution of punitive damages judgments in class-action suits pending appellate review shall be: (1) the amount of the punitive damage award plus twice the statutory rate of interest; or (2) ten percent of the net worth of the defendant prior to the judgement; provided that in no case shall the amount of the bond or other surety exceed \$100 million.

the state. Section 215.5601, F.S. Funds from the endowment will not be available for disbursement to state agencies until after July 1, 2000.

After Florida's settlement, the Big Four settled lawsuits with Texas, Mississippi, and Minnesota (collectively, estimated to be worth between \$25 billion to \$40 billion over the next 25 years), and they (along with the other producers who hold the other seven percent market share) have settled with the remaining states in what has been termed the Master Settlement Agreement² or AMSA². The unadjusted cost of the state settlements ranges between \$212 billion to \$246 billion over the next 25 years. The range is rather broad because these amounts are subject to numerous adjustments, from inflation to fluctuations in cigarette consumption and market share. Therefore, the amount may increase due to inflation, but may decrease if cigarette consumption decreases markedly. Other factors that may affect cigarette consumption include general population growth, cigarette price increases, changes in disposable income, youth consumption, health warnings, smoking bans in public places, nicotine dependence, advertising restrictions, and smoking trends over time.²

b. Legal issues and conflicting signals

Notwithstanding the restrictions and covenants negotiated in the various settlements, a sharply divided U.S. Supreme Court ruled March 21, 2000, that the Food and Drug Administration lacks the power to regulate tobacco products. The 5-4 opinion states that the FDA overstepped its authority in 1996, when it issued unprecedented, sweeping regulations involving cigarettes and smokeless tobacco. The tobacco companies anticipate federal legislation introduced in 2001, that would shift jurisdiction for tobacco from Congress to the FDA.

According to information posted on R. J. Reynolds' website, the states will be provided with up to \$246 billion over the next 25 years which can be used to design local solutions to address underage smoking and to enforce the settlement's new rules and restrictions on cigarette marketing.³ The Philip Morris website declares that

A...cigarettes are a legal product that many adults enjoy, notwithstanding the serious health issues surrounding smoking. Although it is appropriate for governments and health authorities to *encourage* people to avoid risky behaviors, we don't believe that they should *prohibit* adults from choosing to smoke. The decision as to whether or not to smoke should be left to individual adults (emphasis theirs).⁴

Despite the MSA (or perhaps because of it), and other settlements' requirements to educate about the dangers of smoking, tobacco companies are still active in recruiting. According to a Chicago PRNewswire story dated March 24, 2000, Philip Morris recently launched a \$40

²For instance, according to a report prepared by WEFA, Inc., (an international econometrics and consulting firm), on behalf of the Westchester Tobacco Asset Securitization Corporation, dated December 15, 1999, adult consumption of cigarettes declined 0.65% annually for the period 1965 to 1981, 3.31% for the period 1981 to 1990, and 2.47% for the period 1991 to 1998. According to these trends, consumption could decline from the roughly 530 billion cigarettes consumed in 1990, to under 200 billion cigarettes for the year 2040.

³<http://www.rjrt.com/common/pages/IndexDefault.asp>

⁴http://www.philipmorris.com/tobacco_bus/tobacco_issues/index.html

million advertising campaign called "Find your Voice" which portrays smoking as an alluring act of personal choice and is geared specifically towards women whose ethnicity is Latina, African American and Asian American, which reportedly is a largely untapped demographic for smoking.

What the tobacco companies (and the settling state governments) cannot factor in at this time is the estimated cost of dozens of individual suits and one certified class action (*Engle v. R.J. Reynolds, et. al.*, in Dade County, Florida) that are currently pending around the country.⁵ The presiding officers of the Legislature did request an opinion from the Attorney General on whether Florida law requires that compensatory damages be determined before punitive damages may be awarded. A lengthy response was received on March 27, 2000, and is referenced as AGO 00-21. While the tobacco settlement payments are to be made in perpetuity, there is concern by some that the companies may declare bankruptcy and default on their obligations.

c. Viability of the tobacco companies and the threat of bankruptcy

In a story dated March 26, 2000, the Associated Press reported that the National Association of Attorneys General retained a Los Angeles bankruptcy law firm to insure states receive a combined \$246 billion in tobacco settlements. According to the story, the nation's five biggest cigarette makers owe about \$10 billion this year, and also face a potentially record-setting punitive damages award in the *Engle* trial. The tobacco industry fears an estimated 500,000 sick Florida smokers may be awarded as much as \$100 billion or more – the amount being requested by the plaintiffs' counsel.

According to comments by Salomon Smith Barney, tobacco industry credit fundamentals make bankruptcy of a major manufacturer unlikely due to the significant domestic demand for the addictive product, the profitability of the industry, and the ability of the industry to pass additional costs to consumers in the form of higher prices.⁶ In fact, in a series of scenarios presented by WEFA included within the SSB materials projected an industry settlement three times the size of the MSA (approximately \$700 billion) resulting in a cigarette price increase of more than 50 percent causing a consumption decline of more than 14 percent. WEFA concluded that even in those "extreme and unlikely conditions" consumption is still projected to generate sufficient tobacco settlement revenues to meet the planned principal amortization schedule. While it appears that the industry could shoulder a tremendous hit that is amortized and paid out over time, it is unknown how the industry would react to a jury award of as much as \$100 billion or more that was upheld on appeal and immediately payable.

d. Securitization of tobacco settlement proceeds

To hedge against the uncertain continuation of tobacco settlement payments as a result of a vagarious marketplace, ongoing litigation, and potential bankruptcies, New York local governments securitized portions of tobacco settlement proceeds by issuing bonds through non-profit corporations three times, to date, with a fourth offering in the beginning stages. In

⁵For instance, in early 1999, Philip Morris lost a case in California for \$51.5 million (including punitive damages of \$50 million) and a case in Oregon for \$80.3 million (including punitive damages of \$79.5 million). The punitive damages awards in those cases have been reduced to \$26.5 million and \$32 million, respectively, and are on appeal.

⁶Opinions in Tobacco Settlement Securitization, dated February 29, 2000, page 19.

New York, Medicaid payments are split equally between the state and its counties so the Master Settlement divided New York state's settlement Ashare@between the state and other political subdivisions, and then again according to population and medical reimbursement. New York City had pursued its own lawsuit against the tobacco companies so it, too, was included within the settlement for New York state.

The separate offerings were issued for Nassau County, Westchester County, and New York City. A fourth, for Erie County, is in the beginning stages. For New York City (offering \$709 million) and Nassau County (offering \$295 million), the non-profit corporations were set up according to New York's existing corporation statutes. For Westchester County (offering \$104 million), an existing law authorizing a non-profit corporation and subsidiaries to own and operate the Westchester Medical Center was used as general authority to proceed with bonding.

Committee staff communicated with the transaction counsel for the Westchester County offering⁷ who provided some insight into the time spent (over one year, beginning immediately after the Master Settlement was reached and signed) structuring the bond issue so that it was finally approved with a favorable rating by the bond rating agencies. According to counsel, the offering was structured similarly to a securitization of receivables from credit card accounts or mortgages, and was very successful. Counsel also opined that there is a market for these securities at this time, but the situation could change if more and more political subdivisions securitize their settlement funds, and/or if the tobacco companies take a major Ahit@in a pending lawsuit, like *Engle*.

According to Bank of America, a proponent of securitization, other states considering this option include Alabama, Alaska, Colorado, Illinois, Indiana, Louisiana, Maine, New Mexico, Ohio, Oklahoma, South Carolina and Virginia. Salomon Smith Barney, another proponent, reports that the majority of states are interested and/or open to securitization, while Washington, Idaho, Montana, Wyoming, North Dakota, Minnesota, Indiana, Michigan, West Virginia, Maryland, New Hampshire, Maine and Mississippi are not interested.

e. Advantages and disadvantages of securitization

Generally, the advantages of securitization include transferring the risks associated with the receipt of future settlement payments to bond investors, and generating a large, up-front cash payment for a permanent trust fund or for new capital programs.

The disadvantages to securitization include having to discount the stream of future payments, and the implications for the state if there is a default on any bonds. Even though the bonding issues are not backed by the full faith and credit of the state, the bonds are still associated with the state, which creates a policy issue in the event of a default. This may have major implications for Florida because the Governmental Accounting Standards Board (GASB)⁸ requires that bonds of this type offered in the structure proposed by this bill must be reported as a blended component unit@of the state and as a bond payable in the Annual Financial Report.

⁷Hawkins, Delafield & Wood, New York, New York.

⁸The GASB is a group of private CPAs that standardized bond reporting requirements for states and municipalities, adherence to which provides consistency and comfort to investors.

2. Florida Tobacco Growers and State Divestiture

In 1933, the United States Congress passed the Agricultural Adjustment Act and since 1938, with the exception of one year, farmers in Florida produced tobacco under a federally controlled quota system that regulates the volume of production. There are now approximately 290 tobacco quota holders in the state. Florida tobacco farmers produce flue-cured tobacco which requires a large investment of capital to purchase quota as well as the infrastructure such as land and specialized equipment. Chapter 94-251, L.O.F., amended the "Medicaid Third-Party Liability Act" effectively removing defenses in tortious litigation by the state against tobacco companies. Since the time Florida settled with the Big Four in 1997, there has been a decline in demand for tobacco, and the Florida quota has been reduced 18 percent, 17 percent, and 18.5 percent, in 1998, 1999, and 2000 production years, respectively, dramatically reducing income opportunities for growers.

To ameliorate this hardship, a Phase II National Tobacco Grower's Settlement Trust was established with approximately \$4.3 million being mailed to Florida farmers and quota holders earlier this year, with an additional \$3.7 million expected to be distributed to farmers and quota holders from the United States Department of Agriculture during the 2000 growing season. Under the "Phase II agreement," Florida growers are scheduled to receive a total of \$58.5 million over a 12-year period. However, the Phase II Settlement proceeds are adjusted downward in anticipation of declines in the volume of cigarettes shipped for domestic consumption or in the event of bankruptcy. To date, there are no state programs to purchase *stranded* agricultural equipment from farmers who want to quit growing tobacco in favor of another, market-friendly crop.

On the state level, the College of Agricultural & Life Sciences, a part of the Institute of Food and Agricultural Sciences of the University of Florida (IFAS), is a statewide organization dedicated to teaching, research, and extension and serves the agricultural, human, and natural resources needs for the State of Florida.

Through a program called Florida FIRST, IFAS strives to develop knowledge in agricultural, human, and natural resources through teaching programs (environmental studies, agri-businesses, education, communications, engineering, social sciences, renewable natural resources, and pre-professional and professional programs), research through application of the natural, biological, and social sciences, and IFAS Extension, which provides Floridians with lifelong learning programs in partnership with county governments and the United States Department of Agriculture.

As many U.S. food, fiber, and other agricultural sectors continue to feel impacts of emerging product forms; shifting consumer preferences; heightened environmental, health and safety concerns; and changing lifestyles, alternative crops, value-added products, global competition, new processing technologies, and biotechnology will stimulate change and increase opportunities for growth.

3. Appeal from Civil Judgment - requirement for posting a supersedeas bond

In the case of a civil judgment resulting in an award of solely monetary damages, a party may obtain an automatic stay of execution pending review, without the necessity of a motion or order, by posting a good and sufficient bond equal to the principal amount of the judgment plus twice the statutory rate of interest on judgments on the total amount on which the party has an obligation to pay interest. Fla.R.App.P. 9.310(b); Fla Jur 2d, Sec. 161. On December 1 of each year beginning December 1, 1994, the Comptroller of the State of Florida shall set the

rate of interest that shall be payable on judgments or decrees for the year beginning January 1 by averaging the discount rate of the Federal Reserve Bank of New York for the preceding year, then adding 500 basis points to the averaged federal discount rate. Section 55.03, F.S.

C. EFFECT OF PROPOSED CHANGES:

1. The Tobacco Settlement

The corporation would be governed by a board consisting of the Governor, the Treasurer, the Comptroller, and the Attorney General (or designees) and two Senate members appointed by the President of the Senate, and two House members appointed by the Speaker of the House. After January 7, 2003, the board would include the Chief Financial Officer or its designee, in place of the Treasurer and the Comptroller, as well as the Senate and House appointees. The executive director of the State Board of Administration would serve as the chief executive officer of the corporation.

The bill establishes The Task Force on Tobacco-Settlement Revenue Protection (the task force) to determine the need for and evaluate methods for protecting the state's settlement revenue from significant loss. The task force will consist of the Governor (as Chair), the Comptroller, the Insurance Commissioner, three members of the Senate appointed by the President, and three members of the House of representatives appointed by the Speaker. The task force will submit a recommendation report to the Senate President and Speaker of the House by November 1, 2000. A non-recurring sum of \$100,000 is appropriated from the General Revenue Fund to the SBA to support the operations of the task force.

2. Florida Tobacco Growers and State Divestiture

To assist Florida tobacco farmers in reducing encumbered debt on stranded investment in tobacco agricultural equipment, the non-recurring sum of \$2.5 million is appropriated from the Department of Banking and Finance Tobacco Settlement Clearing Trust Fund to the Department of Agriculture and Consumer Services for the purchase of agricultural equipment used by tobacco farmers or tobacco-producing companies who intend to cease production of that crop, to be resold to anyone other than a person or company who produces tobacco in this state or who holds a quota to produce tobacco in this state.

In addition, a non-recurring appropriation of \$2.5 million from the Department of Banking and Finance Tobacco Settlement Clearing Trust Fund will be directed to the Institute of Food and Agricultural Sciences of the University of Florida to provide on-farm direct assistance to growers in the tobacco-producing counties affected by the state's tobacco liquidation. The vast majority of current tobacco farms are located in North/Central Florida area.

3. Appeal from Civil Judgment - requirement for posting a supersedeas bond

The bill creates s. 768.733, F.S., establishing that the amount of a bond or other surety required to stay the execution of punitive damages judgments in class-action suits pending appellate review shall be: (1) the amount of the punitive damage award plus twice the statutory rate of interest; or (2) ten percent of the net worth of the defendant prior to the judgement; provided that in no case shall the amount of the bond or other surety exceed \$100 million. This bond limitation could have an effect in the *Engle* class action, where an estimated 500,000 sick Florida smokers are seeking \$100 billion in punitive damages.⁹ In depositions taken in

⁹Reference Senate Journal page 1442 for Legislative intent.

May, 2000, Philip Morris' tobacco chief reported that his company could not afford to split even half of what Big Tobacco could be forced to shell out in a landmark smokers' case against the industry. Given that testimony, and without the bond limitation, it is unclear whether the tobacco companies could afford to appeal the verdict.

See, Part II.D., SECTION BY SECTION ANALYSIS, for more detail.

D. SECTION-BY-SECTION ANALYSIS:

Section 1. Creates s. 215.5600, F.S., providing definitions. This section also establishes the Tobacco Settlement Finance Corporation, a non-profit, public-benefits entity separate from the state. The purpose of the corporation is to purchase from the state its right, title and interest in and to any or all of the tobacco settlement agreement payments and will sell securities backed by the settlement payments, subject to the Legislature's approval. The proceeds from the bond sale will be used to pay the purchase price for the right to the payments. The total principal amount of bonds issued by the corporation shall not exceed \$3 billion, and the principal amount of bonds issued in any single fiscal year is limited to no more than \$1.5 billion, beginning with the 2001, 2002 fiscal year. The rate of interest on the bonds shall have a true interest cost rate of no more than four percent over the yield on U.S. Treasury obligations which have a maturity approximately equal to the average life of such series of bonds.

The corporation will be governed by a board consisting of the Governor, the Treasurer, the Comptroller, and the Attorney General (or designees), until January 7, 2003, at which time the board will include the Chief Financial Officer or its designee, in place of the Treasurer and the Comptroller. The executive director of the State Board of Administration (SBA) will serve as the chief executive officer of the corporation. The board members cannot be sued for any actions taken by them in the performance of their duties under the act. The corporation may elect, appoint, or employ such officers, agents, or employees as the corporation deems advisable. The officers, agents, or employees may be officers, agents, or employees of the state, as was done for the Inland Protection Financing Corporation (ss. 376.3071, 376.3075, F.S.), and the Investment Fraud Restoration Financing Corporation (ss. 517.1203, 517.1204, F.S.).

The corporation will be exempt from state and local taxation, and will not be deemed a special district for purposes of Chapter 189, F.S. (Special Districts), or a unit of government under Part III of Chapter 218, F.S. (Financial Matters Pertaining to Political Subdivisions). Neither the corporation, the purchase agreements entered into by the corporation, nor the bonds issued by the corporation, shall be subject to Chapter 120, F.S. (The Administrative Procedures Act), Part I of Chapter 287, F.S. (Procurement of Commodities, Insurance or Contractual Services), and ss. 215.57 through 215.83, F.S. (The State Bond Act within Chapter 215 - Financial Matters General Provisions). The corporation is authorized to validate any bonds issued pursuant to this act as provided by Chapter 75, F. S. The corporation may contract with the SBA to serve as trustee with respect to bonds issued, invest proceeds, or perform any other duty for the corporation as contracted. The Auditor General is authorized to conduct financial audits of the accounts and records of the corporation. The corporation would be required to use a competitive bidding process consistent with the rules adopted pursuant to the State Bond Act for the selection of service providers and underwriters.

The bonds are not to be construed in any manner as an obligation of the state or any of its agencies. The bonds can only be secured by payments received under the tobacco settlement agreement, and the corporation does not have the power to pledge the credit, the general revenues, or the taxing power of the state or of any political subdivision. The corporation is

prohibited from filing for voluntary bankruptcy until at least one year and one day after which no bonds of the corporation remain outstanding. If, however, the tobacco payments stop for any reason and the bonds go into default the state will not be held accountable to the bondholders. The state does covenant, however, that it will do nothing to impair the creditworthiness of those securities. The bonds that the corporation is authorized to issue are not to exceed a term of 40 years.

The Department of Banking and Finance is authorized, on behalf of the state, to assist the corporation in the execution of its responsibilities, including entering into one or more purchase agreements to sell to the corporation any or all of the state's right, title and interest in and to the tobacco settlement agreement. The department is authorized to covenant to take whatever actions on behalf of the corporation or holders of the bonds to enforce the provisions of the tobacco settlement agreement, and any remedies or rights thereunder. This language, suggested by the Division of Bond Finance, is to help secure a beneficial rate from the bond rating agencies who look favorably on provisions which allow a proxy (in this case the department) to enforce the agreement. The state, although it has sold its rights, still has a compelling interest in the bond residuals to keep the payments forthcoming.

Section 2 amends s. 17.41, F.S., conforming it to the changes in light of section 2, above, and clarifying that monies received by the state pursuant to any *residual* interest retained in the tobacco settlement are to be deposited in the clearing trust fund. However, *proceeds* of the sale of the state's right to tobacco settlement payments are to be deposited directly into the Lawton Chiles Endowment Fund. The administrative requirement that the State Board of Administration serve as cash manager for the clearing fund is removed.

Section 3 amends s. 215.5601, F.S., conforming it to the changes in light of section 2, above, and modifies current law appropriations to the endowment fund. The change would require that the \$200 million annually appropriated to the endowment fund during each of the next three fiscal years will be reduced on a dollar-for-dollar basis to the extent that securitization proceeds are deposited in the endowment fund. This essentially replaces the current law appropriation to the endowment with securitization proceeds. This also would assure that if, in FY 2000-2001, a securitization is executed then appropriations for programs from tobacco monies will not be adversely affected.

Section 4 creates s. 768.733, F.S., establishing that the amount of a bond or other surety required to stay the execution of punitive damages judgments in class-action suits pending appellate review shall be: (1) the amount of the punitive damage award plus twice the statutory rate of interest; or (2) ten percent of the net worth of the defendant prior to the judgement; provided that in no case shall the amount of the bond or other surety exceed \$100 million.

Section 5 establishes The Task Force on Tobacco-Settlement Revenue Protection (the task force) to determine the need for and to evaluate methods to protect the state's settlement revenue from significant loss. The options available for protecting the economic and non-economic assets include securitization, insurance, self-insurance, model statute, licensing of manufacturers, or a combination. The task force will consist of the Governor (as Chair), the Comptroller, the Insurance Commissioner, three members of the Senate appointed by the President, and three members of the House of representatives appointed by the Speaker. The task force will submit a recommendation report to the Senate President and Speaker of the House by November 1, 2000. Staff support for the task force will be provided by the State Board of Administration, and the term of the task force will expire on July 1, 2001.

Section 6. For the term of 2000-2001, a non-recurring sum of \$100,000 is appropriated from the General Revenue Fund to the SBA to support the operations of the task force.

Section 7. To assist Florida tobacco farmers in reducing encumbered debt on stranded investment in equipment, the non-recurring sum of \$2.5 million is appropriated from the Department of Banking and Finance Tobacco Settlement Clearing Trust Fund to the Department of Agriculture and Consumer Services for the purchase of agricultural equipment used by tobacco farmers or tobacco-producing companies who intend to cease production of that crop, to be resold by the Department of Management Services to anyone other than a person or company who produces tobacco in this state or who holds a quota to produce tobacco in this state. Proceeds of the resales, less administrative costs, will be deposited in the General Inspections Trust Fund of the Department of Agriculture and Consumer Services.

Section 8. Provides a non-recurring appropriation of \$2.5 million from the Department of Banking and Finance Tobacco Settlement Clearing Trust Fund to the University of Florida to provide on-farm direct assistance to growers in the tobacco-producing counties affected by the state's tobacco liquidation.

Section 9. Provides this bill will take effect upon becoming a law.

III FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT:

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

According to Economic & Demographic Research the fiscal impact of this bill is indeterminate and will depend on the amount of the future settlement payments, the size of the bond issue and the structure of the bond securitization.

2. Expenditures:

<u>FY 2000-2001</u>	<u>FY 2001-2002</u>
General Revenue Fund	\$ 100,000
Tobacco Trust Fund	\$5,000,000

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

See, Part III.A.1.and 2., above.

2. Expenditures:

See, Part III.A.1., above.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

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The impact is indeterminate, and depends on the amount of the future settlement payments, the size of the bond issue and the structure of the bond securitization.

Florida tobacco farmers attempting to change crop production from tobacco to another crop may receive assistance both in the purchase of their tobacco-agricultural equipment through the Department of Agriculture and Consumer Services, and in direct, on-farm assistance through the Institute of Food and Agricultural Sciences of the University of Florida.

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D. FISCAL COMMENTS:

N/A

IV CONSEQUENCES OF ARTICLE VII, SECTION 18 OF THE FLORIDA CONSTITUTION:

A. APPLICABILITY OF THE MANDATES PROVISION:

This bill does not require counties or municipalities to spend funds or to take an action requiring the expenditure of funds.

B. REDUCTION OF REVENUE RAISING AUTHORITY:

This bill will not reduce the authority of counties and municipalities to raise revenues.

C. REDUCTION OF STATE TAX SHARED WITH COUNTIES AND MUNICIPALITIES:

This bill will not reduce the total aggregate percentage of a state tax shared with counties and municipalities to below February 1, 1989 levels.

V COMMENTS:

A. CONSTITUTIONAL ISSUES:

The bonds would not be a debt or obligation of the state. If, after the securitization process, the tobacco payments stopped for any reason, the bonds would simply go into default and there would be no recourse against the state by bond holders.

B. RULE-MAKING AUTHORITY:

None is authorized under the bill.

C. OTHER COMMENTS:

During the 2000 legislative Session, the House and Senate considered legislative initiatives to protect the State's tobacco settlement revenues from significant loss and other tobacco-related consequences of the State's tobacco litigation - including the impact on the state's tobacco farmers and quota holders. The Senate appointed a Select Committee on Tobacco to examine the potentially substantial and imminent threats to the settlement proceeds. This Committee held extensive hearings during which a variety of witnesses gave testimony on the array of those threats (including the potential threat posed by the *Engle* case) and the need to address them.

Subsequently, comprehensive tobacco-related legislation was considered to protect the State's settlement proceeds and otherwise further the purposes of the tobacco settlement agreement, including: securitization of the settlement funds (HB 1721); prohibitions on the sale and transportation of "gray market" tobacco products (HB 1941); methods for dealing with the threat to recovery of settlement proceeds created by a potentially large punitive damage award in the *Engle v. R.J. Reynolds, et al.* class action, now pending in Miami (SB 1720); transition programs for tobacco farmers to alternative crops (SB 2446); passage of a tax on tobacco

manufacturers who are not signatories to the State's tobacco settlement (SB 1998); creation of the Task Force on Tobacco-Settlement-Revenue Protection (SB 2168); and funding of the Lawton Chiles Endowment Fund (SJR 1008). (Senate Journal pp. 810-812)

Ultimately, CS/HB 1721 was the number assigned to the comprehensive report developed by the Legislative Conference Committee appointed to resolve the differences in the House and Senate versions of bills relating to the protection of the tobacco settlement proceeds and the disposition of the resulting funds.

Passage of the Conference Committee's Report elicited specific explanations in both the House and the Senate. Section 4 of the bill addresses a potential constitutional defect with present law. Requiring a supersedeas bond in an amount which essentially prohibits a defendant from exercising its rights of appeal could result in a denial of the party's due process rights. If this issue was not legislatively addressed, it could result in the need for extensive litigation in cases such as the *Engle* case. Such litigation could lead to more confusion and uncertainty in regards to the ability of Florida to recover proceeds from the tobacco settlements or to securitize those proceeds. Senator Rossin's comments can be found in the Senate Journal on page 1442. The following statement was read by Representative Les Miller prior to the House vote on the Conference Report and may be found in tape recorded form in the House Clerk's Office.

REPRESENTATIVE L. MILLER: Thank you, Mr. Speaker. I'd like to read something -- a statement into the record before we vote on this bill. I think -- I want to congratulate and commend Representative Lacasa and Representative Gottlieb on the fine work that they've done on this Conference Committee. But, I think we need to read something into this statement -- to make something perfectly clear. With respect to Section 4 of the bill that deals with supersedeas bonds, I want to confirm that the language that includes --the language -- that this language includes the content of Senate Bill 1720 as it relates to supersedeas bonds; that to the extent that this applies, the "Whereas" clause of Senate Bill 1720 which was not included in this Conference Report explains the intent of the Legislature in passing this section; and that the provision is intended to apply to the current *Engle* case.

VI. AMENDMENTS OR COMMITTEE SUBSTITUTE CHANGES:

Disposition of the House Bill

HB 1721 was prefiled by Representative Lacasa on March 6, 2000, and introduced the following day. On March 10, 2000, the bill was referred to the Committees on Financial Services, Governmental Rules & Regulations, Finance & Taxation, and General Appropriations. The Financial Services Committee passed the bill out unanimously as a Committee Substitute on April 3, 2000. The original bill differs from the committee substitute in that the committee substitute version:

- C Caps the maximum interest rate for the bonds at 12 percent;
- C Replaces a broad exemption of the corporation from Chapter 215, F.S., with a narrowly defined exemption to include the provisions of the State Bond Act only;

- C Requires that selection of certain professional service providers be made in a manner consistent with rules of the State Bond Act, through a competitive bidding process;
- C Clarifies that the Auditor General may perform audits as deemed appropriate; and
- C Authorizes the department to covenant to take whatever actions are necessary on behalf of the corporation or holders of the bonds issued by the corporation to enforce the provisions of the tobacco settlement agreement.

The Bill was withdrawn from the Committee on Governmental Rules & Regulations on April 18, 2000. On April 26, the Committee on Finance & Taxation amended the CS and passed it out by a vote of 10 - 2. These amendments:

- C Modify the board of directors of the Tobacco Settlement Financing Corporation to include two members appointed by the President of the Senate, and two members appointed by the Speaker of the House. After the amendment, the board will be composed of four members of the executive branch and four members of the legislature. This will assure that the legislature is involved in decisions related to implementing a securitization.
- C Authorize the Corporation to purchase insurance or reinsurance products. This change is meant to allow for the purchase of insurance (if that is desirable) in addition to or as a supplement to the protection afforded by the securitization. This provision does not envision the purchase of insurance directly as an alternative to securitization as contemplated by the Senate's proposal. If the legislature wants to purchase insurance, it can do that directly without having to use the Finance Corporation as the mechanism to purchase insurance.
- C Limit the amount of debt that can be issued by the Corporation. This provision is intended to provide assurance to the legislature regarding the amount of the securitization to be implemented. In addition, this amendment replaces the maximum borrowing rate of 12% currently in the bill with a borrowing rate of no more than 4 percent over the yield on U.S. treasury bonds.
- C Make technical changes.
- C Provide language necessary for rating agency requirements in dealing with bankruptcy preference issues. These changes help the rating analysis and the resulting bond rating.
- C Make it explicit that securitization is a sale from a legal standpoint and not security for a borrowing which would be treated differently by the rating agencies. In addition, this amendment corrects a drafting error.
- C Modify current law appropriations to the endowment fund. The change would require that the \$200 million annually appropriated to the endowment fund during each of the next three fiscal years will be reduced on a dollar-for-dollar basis to the extent that securitization proceeds are deposited in the endowment fund. This essentially replaces the current law appropriation to the endowment with securitization proceeds. This also would assure that if, in FY 2000-2001, a securitization is executed then appropriations for programs from tobacco monies will not be adversely affected.
- C Explicitly state that no contract or other agreement entered into by the corporation, under the authority granted in this act, may be construed to bind or otherwise restrict the legislature.

The bill was withdrawn from the General Appropriations Committee on April 27, 2000. The bill passed the House, as amended, on May 3, 2000, by a vote of 88 - 29. The bill was sent to the Senate, where it was referred to the Committee on Governmental Oversight and Productivity.

On May 3, the Senate reconsidered the vote by which the Senate bill passed, and also voted to withdraw HB 1721 from the Senate Committee on Governmental Oversight and Productivity. The Senate then substituted the House Bill for CS/CS/SB 1998 and laid the Senate bill on the table. The Senate amended the House bill with the provisions of the laid Senate Bill and the provisions of several other tobacco settlement-related Senate bills (CS/SB 1720, SB 2168 & CS/SB 2446) which had passed in sequence with CS/CS/SB 1998 (SJ 811, 812). The amended bill was sent back to the House, which refused to concur on May 4, 2000. A conference committee was appointed. On May 5, 2000, the Conference Committee Report was received and adopted by the House. The amendments:

- C Establish The Task Force on Tobacco-Settlement Revenue Protection (the task force) to determine the need for and to evaluate methods to protect the state's settlement revenue from significant loss, and provide an appropriation of \$100,000 from the General Revenue Fund to the SBA to support the operations of the task force
- C Appropriate \$2.5 million from the Department of Banking and Finance Tobacco Settlement Clearing Trust Fund to the Department of Agriculture and Consumer Services for the purchase of agricultural equipment used by tobacco farmers or tobacco-producing companies who intend to cease production of that crop;
- C Provide a non-recurring appropriation of \$2.5 million from the Department of Banking and Finance Tobacco Settlement Clearing Trust Fund to the University of Florida to provide on-farm direct assistance to growers in the tobacco-producing counties affected by the state's tobacco liquidation; and
- C Create a new section in Chapter 768 (s. 768.733, F.S.), establishing that the amount of a bond or other surety required to stay the execution of punitive damages judgments in class-action suits pending appellate review shall be: (1) the amount of the punitive damage award plus twice the statutory rate of interest; or (2) ten percent of the net worth of the defendant prior to the judgement; provided that in no case shall the amount of the bond or other surety exceed \$100 million.

CS/HB 1721 was passed as amended by the Conference Committee Report by a vote of 115 - 0. The Senate received the bill as amended and passed the bill by a vote of 39 - 0.

Disposition of the Senate Bill:

Senate bill 1998 (Horne) was introduced on March 7, 2000, and referred to the Committees of Governmental Oversight and Productivity, Health, Aging and Long-term Care, and Fiscal Resource. On April 25, 2000, the Committee on Governmental Oversight and Productivity amended the bill and passed it unanimously as a Committee Substitute. The bill created a cigarette surtax, and provided an opportunity for tobacco manufacturers to be signatories to a specified settlement agreement and be participating manufacturers, thus exempting them from a state surtax on cigarettes not manufactured by a participating manufacturer, as defined by the act.

Among other technical changes, the committee substitute provided that:

- C All tobacco manufacturers that are signatories to the settlement agreement entered on August 25, 1997, in the case of *The State of Florida et. al. v. American Tobacco Company, et. al.*, and the settlement agreement entered on March 15, 1996, in the case of *State of West Virginia, State of Florida, State of Mississippi, Commonwealth of Massachusetts, and State of Louisiana v. Brooke Group Ltd. and Liggett Group, Inc.*, are participating manufacturers. Cigarettes produced by each such manufacturer that fully complies with the applicable settlement agreement and makes the annual payment required under the agreement by December 31 are exempt from the surtax on cigarettes imposed under s. 210.02(6) for the subsequent 12-month period.
- C Funds received from participating manufacturers will be deposited into the Department of Banking and Finance Tobacco Settlement Clearing Trust Fund.
- C The Legislature may not appropriate more than 85 percent of the revenue that is received from participating manufacturers or pursuant to s. 210.02, F.S., in any fiscal year and made available for appropriation in the subsequent fiscal year. Revenue received from participating manufacturers or pursuant to s. 210.02, F.S., in any fiscal year which is not appropriated by the Legislature must be deposited into the Lawton Chiles Endowment Fund.
- C For all fiscal years subsequent to fiscal year 2002-2003, a minimum of \$25 million is appropriated from the Department of Banking and Finance Tobacco Settlement Clearing Trust Fund to the Lawton Chiles Endowment Fund for Health and Human Services.
- C Beginning February 1, 2001, for cigarettes not manufactured by a participating manufacturer as defined in s. 215.5601, F.S., an additional surtax will be added to the amounts otherwise provided in the section. The division is required to calculate the surtax on January 1 of each year, and the surtax must apply on February 1. The per package surtax is calculated in the same manner as the amount that otherwise would be paid directly to the state by a participating manufacturer (per package rate based on the total annual payment due to the state pursuant to the settlement agreement in the case of *The State of Florida et. al. v. American Tobacco Company et. al.*, divided by the total number of packages of cigarettes delivered to wholesale dealers for sale in Florida by the four settling manufacturers during the previous 12 months, rounded to the nearest tenth of a cent).
- C The division is to certify to the Comptroller, month to month, the amount derived from the cigarette surtax imposed by s. 210.02(6), F.S., and that amount must be transferred from the Cigarette Tax Collection Trust Fund and credited to the Department of Banking and Finance Tobacco Settlement Clearing Trust Fund.

The bill was withdrawn from the Committee on Health, Aging and Long-term Care on April 26, 2000, and passed out unanimously by the Committee on Fiscal Resource that same day. On April 28, the bill was amended on the Floor of the Senate. The amendment added to the bill the House provision regarding the Tobacco Settlement Financing Corporation. The Senate passed the bill as amended by a vote of 40 - 0, on May 2, 2000.

On May 3, the Senate reconsidered the vote by which the Senate bill passed, and also voted to withdraw HB 1721 from the Senate Committee on Governmental Oversight and Productivity. The Senate then substituted the House Bill for the Senate Bill and laid the

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Senate bill on the table. The Senate amended the House bill with the provisions of the Senate Bill that was laid on the table and sent back to the House, which refused to concur on May 4, 2000. A conference committee was appointed. On May 5, 2000, the Conference Committee Report was received and adopted by the House. CS/HB 1721 was passed as amended by the Conference Committee Report by a vote of 115 - 0. The Senate received the bill as amended and passed the bill by a vote of 39 - 0.

VII SIGNATURES:

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