

# The Tobacco Deal: Myths and Misconceptions

by Robert A. Levy

The deal being forced on tobacco companies, whether it is the original negotiated agreement or one amended according to President Clinton's liking, is manifestly unconstitutional and nothing less than an attack on the rule of law.

In the original "Proposed Resolution," negotiated by a coterie of state attorneys general, plaintiffs' lawyers, and public health advocates, the industry agreed to disgorge \$370 billion in monetary damages to various parties, pay additional penalties if specified reductions in youth smoking do not occur, submit to Food and Drug Administration regulation of nicotine, cease all vending-machine sales of tobacco products, and rein in certain marketing practices allegedly targeted at children. In return, tobacco companies would be immune from punitive damages for their past conduct and from new class action lawsuits. Individuals could still sue, subject to a cap on compensatory damages. The settlement, if approved, would wipe out claims by more than three dozen state and local governments for Medicaid reimbursement.

In September, President Clinton weighed in with his version of the sweeping tobacco settlement. Clinton embraced parts of the deal but repudiated others. Specifically, the president wants the FDA to have more or less plenary regulatory authority over tobacco products. He also

wants tougher restrictions on advertising, greater disclosure of secret industry documents, and a stiffer price tag than the industry had bargained for. Instead of \$370 billion in tax-deductible payments—estimated to cause the price of a pack of cigarettes to rise by about 62 cents—Clinton proposed a \$1.50 per-pack increase over ten years. Part of the increase would arise from unspecified *nondeductible* payments by the industry; the rest would depend on penalties for not meeting targeted reductions in youth smoking. As to big tobacco's partial immunity from litigation, the president was uncharacteristically silent, apparently content to leave such legally and politically sensitive details to Congress.

Obviously overlooked in the president's evaluation is this troublesome complication: The deal in the making—either the "Proposed Resolution" or Clinton's adaptation—is unconstitutional. Indeed, no legislation in recent memory transgresses so many fundamental constitutional principles. Most important, the settlement expunges the industry's right to due process, about which more in a moment. Further, it punishes tobacco companies by legislative fiat despite the constitutional prohibition on bills of attainder. It abridges the industry's First Amendment rights of free speech, impermissibly obstructs litigants seeking redress through the courts, takes the property of cigarette vending-machine companies without just compensation, and delegates unprecedented legislative authority to the FDA. Moreover, the settlement intercedes in product liability cases that have

long been the prerogative of state government, thus exercising power beyond that enumerated in the Constitution and flouting our system of dual sovereignty.

Those are just a few of the problems. Meanwhile, the public seems blissfully unaware of the pernicious effects should the proposed settlement be approved. So here is a wake-up call. Perhaps it will dispel some of the myths and misconceptions surrounding the insidious deal with which the administration and Congress will be tinkering.

## Myth #1: We can ignore the constitutional infirmities if the industry consents to them.

The argument goes like this: If tobacco companies voluntarily enter into an agreement after extensive negotiations, why shouldn't we respect their decision? We shouldn't for two reasons: First, the settlement purports to bind parties who did not participate in the negotiations. Second, there can be no real consent at the point of a gun.

For starters, the proposed settlement affects future litigants, who had no representatives at the bargaining table. When parties are injured, the tort system permits them to seek recovery from those who caused the injury. While legislatures can alter the rules at the margin (for example, they can eliminate punitive damages), they cannot cut into the irreducible core that is our due-process right. The cumulative effect of immunities conferred by this settlement—no class actions, no punitive damages for past acts, a limit on compensatory damages—goes too far. By foreclosing adequate legal remedies, those restrictions have the practical effect of denying access to the courts.

Also without representation at the negotiations were vending machine operators, whose sales of tobacco products are precluded by the settlement; some nonparticipating tobacco companies; and, of course, yet-to-be-formed companies, which must either agree to the settlement or place substantial sums in escrow for 35 years to ensure that they will be able to pay damages if awarded against them. That "choice" raises obvious due-process concerns. Moreover, Con-

gress is simply not authorized to compel private companies to escrow funds for satisfaction of potential judgments arising out of state tort law. Any such statutory requirement makes a mockery of the principles of federalism and limited national government.

With respect to those tobacco companies that did participate in the settlement, their involvement and signatures by no means equate to consent. Either such companies could join the settlement or they could mount an expensive, time-consuming, and ultimately futile challenge to nearly 40 Medicaid recovery suits, litigated under a perverted system of law that effectively foreclosed every line of defense. Here's how that choice came about.

Over four decades, after thousands of claims, smokers had not collected one dollar of damages for a smoking-related illness. Juries understood—even if state attorneys general today do not—that we are free to use whatever legal products we wish, but if we assume the risk we must bear the consequences. As juries were reaffirming that basic rule of law—known as the "assumption-of-risk" doctrine—state Medicaid programs were coming under intense financial pressure. Of course, states were entitled to sue the tobacco companies for recovery of Medicaid outlays supposedly traceable to smoking; but the states bore the same burden of proof as the injured smoker and they were subject to the same defenses including assumption of risk. Unwilling to raise taxes and unable to prevail in court, the states came up with a creative solution: they simply eliminated assumption-of-risk as a defense in Medicaid recovery suits and, for good measure, applied the new rule retroactively so that it would affect cigarette sales made decades earlier.

While they were at it, to head off any possibility of an adverse jury verdict, the states abolished the requirement for proof of individual causation. Instead of demonstrating that a particular claimant's illness was caused by his smoking, all the states had to produce were aggregate statistics showing that certain injuries were more prevalent among smokers than non-smokers. Tobacco companies, under the new regimen, would thus have to pay for treating burn victims who fell asleep with a lit cigarette, cancer victims who never smoked, and even

Robert Levy is senior fellow in constitutional studies at the Cato Institute and author of the Cato Policy Analysis, "Tobacco Medicaid Litigation: Snuffing Out the Rule of Law."

Medicaid recipients who defrauded the system and weren't injured at all. Astonishingly, the states didn't have to furnish any corroborating evidence, just statistics.

What could possibly justify this abuse of power? Incredibly, the states contend that they are entitled to abrogate the assumption-of-risk defense and disregard proof of causation because, after all, the state as plaintiff never smoked. Imagine, analogously, that you are exceeding the speed limit by five miles per hour and hit another car driven by a Medicaid recipient; he is driving 80 miles per hour, intoxicated, and hurtles through a red light. When the state Medicaid program sues you for negligence, you properly respond that the other driver was 99 percent at fault. The state counters that the Medicaid recipient's behavior is irrelevant; the state doesn't drink, nor does it drive. Such arrant nonsense—the exact equivalent of “the state never smoked”—is unworthy of serious consideration.

Naturally, the states laughed off the charge that the new law wiped out the industry's defenses. One of Florida's lawyers said, for example, “It doesn't mean that the tobacco industry is defenseless. They [sic] can show that the state has unclean hands, that the state has participated in the activity somehow.”<sup>21</sup> Yes, “unclean hands” is a legitimate defense; but when the industry pointed to Florida's continued support for federal tobacco programs, its \$825 million pension investment in tobacco stocks, and its manufacture of cigarettes for sale to local jurisdictions and distribution to state prisoners, Florida attorneys filed a motion to suppress the evidence, and the state judge granted the motion.<sup>22</sup> So much for the unclean hands defense.

Faced with insurmountable legal hurdles in dozens of Medicaid suits patterned after Florida's, the industry decided to negotiate. Was the settlement consensual? Ask yourself why an industry would agree to fork over \$370 billion, subject itself to FDA regulation, overhaul its advertising, eliminate vending-machine sales, and pay large penalties if targeted reductions in youth smoking were not realized—all in return for partial immunity from litigation that had not cost a single dollar of damages in 40 years. To call this settlement consensual is consummate doublespeak.

## Myth #2: Tobacco is a special case. No other industries are at risk.

If the tobacco industry were the only victim, that would be bad enough; but the unhappy prospect is for yet more incursions by a paternalistic state with a boundless appetite for social engineering. Lamentably, American governments at all levels seem to have abandoned the principles of free choice and personal responsibility in favor of regulatory mandates and abolition for the consequences of our acts. And because we have socialized so many activities, like the provision of medical services, we should not be surprised when the government monitors our diet, exercise, recreation, and other lifestyle choices. Having created a system in which each of us has an incentive toward irresponsible behavior—paid for by the rest—the state then steps in to prohibit the behavior it has encouraged.

Mired in regulations, laws, taxes, and litigation, we look to Congress to extricate us from the mess that it helped create. Yet if Congress approves the ill-advised tobacco settlement, it will exacerbate the problem. Politicians from both the left and right will attack products deemed by them, our moral overseers, to be bad for us. There will be no shortage of candidates as the do-gooders take aim at the food industry, for example—from chocolate to sugar, dairy products, red meat, and French fries. Obesity, which causes 300,000 deaths each year from heart attacks and strokes, will be the new shibboleth; but it won't be the last. There's still coffee, motorcycles, sporting equipment; the list is endless.

Is that merely paranoia? You be the judge. Vice President Gore at a press conference this past July ventured that there is a “link between exposing children to massive levels of violence on television and violent behavior.” He asserted that the link is “just as well established” as the “link between tobacco smoking and lung cancer.” Then he prompted, “So how do we act on that?” And William J. Bennett, in a *New York Times* op-ed dated July 29, 1997, predicted: “If the liquor industry does not start acting in a more socially responsible way, it may soon find itself held in the same kind of esteem in which the tobacco companies are now held. The alco-

hol industry can act now. Or it can deny reality and pay later.”

Those threats must not be taken lightly. The hallmark of a free nation is whether it safeguards the rights of its least popular citizens. When it comes to tobacco, we have failed that test. We have tapped the industry's deep pockets in order to reward states that retroactively imposed new and unimaginable laws on a feckless and friendless defendant. Today it may be tobacco; tomorrow none of us will be secure.

## Myth #3: The administration and Congress should impose tougher sanctions.

The provisions of the tobacco settlement as originally drafted are misconceived, unworkable, and counterproductive. But if Congress adopts the Clinton version or, still worse, the draconian recommendations of antismoking zealots like former FDA commissioner David A. Kessler and former Surgeon General C. Everett Koop, the outcome will be even more destructive. Koop and Kessler want tougher FDA regulation, stiffer penalties imposed on the industry if the nation doesn't meet targeted declines in youth smoking, huge increases in cigarette taxes, tighter rules on smoking in public and work places, and export controls on industry access to foreign markets. That's all—just prohibition, without the label, and without the precursor to prohibition, which, as you will recall in the case of alcohol, was an amendment to the Constitution. Kessler and Koop object especially to a provision requiring the FDA to show that its regulations will not spawn black-market transactions. No wonder they regard that provision as a material limitation on the agency's powers. FDA restrictions on nicotine content, coupled with inflated retail prices to pay for the settlement, will lead ineluctably to a pervasive black market.

We never seem to learn. California, Maryland, Michigan, and New York hike their cigarette taxes and the result is rampant smuggling—not just from low-tax neighboring states, but from military bases, Indian reservations, even exports to Mexico that are smuggled back into the United States.<sup>23</sup> After Canada raised its

excise tax, smuggled cigarettes accounted for an estimated 30 to 50 percent of consumption; so Canada was forced to lower the tax to keep smuggled cigarettes away from children.<sup>24</sup> It doesn't take a rocket scientist, an FDA commissioner, or a surgeon general to know that the proposed tobacco settlement will inevitably foment illegal dealings dominated by criminal gangs hooking underage smokers on an adulterated product freed of all constraints on quality and price that competitive markets usually afford.

If the health imperative is to reduce smoking among teenagers, we have the requisite tools at our disposal. The sale of cigarettes to youngsters is illegal in every state. Those laws must be vigorously enforced. Retailers who violate the law must be prosecuted. Proof-of-age requirements are appropriate if administered objectively and reasonably. Vending-machine sales should be prohibited in areas like arcades and schools where children are the principal clientele. And minors—who are often held responsible as adults when charged with a serious crime—should at least be subject to parental notification and moderate punitive measures when caught smoking or attempting to acquire cigarettes.

## Myth #4: The industry and its customers owe the public for health costs due to smoking.

At the outset, one must ask why tobacco companies should be responsible for antismoking campaigns and programs to help smokers break their habit. After all, cigarettes are legal, and the choice to smoke is freely made. Claims that some consumers are hopelessly addicted, having relied on fraudulent information and deceptive advertising, not only strain credibility but require proof. Equally objectionable, the industry will be required to finance health care for uninsured children. By what possible logic can that problem be laid at the doorstep of the tobacco companies? Selling tobacco to children is illegal; but no one has shown that the tobacco companies have broken that law. To hold a single industry financially liable because some families are unable or unwilling to insure their

offspring is no more than a bald transfer of wealth from a disfavored to a favored group.

Even if tobacco companies were held accountable for all smoking-related public health costs—including publicly funded medical care, group life insurance, sick leave, nursing home care, and lost payroll taxes—the excise tax on cigarettes generates revenue to the government in excess of those costs. Thus, if any wealth transfer is justified, it would be from those smokers who are covered by Medicare and Medicaid to those smokers who are not. The typical smoker, who is not on public assistance, has paid his share of public health costs, and then some. By contrast, the nonsmoking taxpayer, presumably the financial beneficiary of the tobacco settlement, has not been burdened and should not, therefore, be rewarded.

The first comprehensive analysis of the social cost of smoking was published in the *Journal of the American Medical Association* in 1989 by a team of researchers from the RAND Corporation.<sup>5</sup> The RAND study established the framework for subsequent research, setting forth two key principles. First, if a smoker does not die from a smoking-related illness, he will die from something else. Accordingly, the relevant social cost is not the entire amount spent on his illness, but the difference between the amount spent and the amount that would otherwise have been spent if he had not smoked. Second, premature death from smoking can produce long-term financial benefits in the form of lower retirement costs and reduced nursing home care. Those benefits are an offset to outlays for medical care, sick leave, and group life insurance.

Researchers at RAND concluded that the public health cost of a pack of cigarettes in 1986 dollars was 15 cents. The Congressional Research Service updated that estimate to 33 cents, in 1993 dollars.<sup>6</sup> Smokers were then paying an average of 53 cents per pack in excise taxes—60 percent more than the costs they were imposing. In a separate study, Duke University economist W. Kip Viscusi reworked the RAND data and found that medical care, sick leave, and group life insurance cost approximately 51 cents per pack<sup>7</sup>—still lower than the excise tax, even without offsetting for retirement and nursing home savings. With all expenditures and savings factored in, the total external cost per

pack, according to Viscusi, was 25.3 cents—less than half of the prevailing 53-cent tax.

Thus, when it comes to reimbursing the public treasury for health costs associated with tobacco, the essential premise of the settlement is wrongheaded. Any fair-minded assessment of the public burden must take into account, first, the excise tax receipts that already compensate for smoking-related health costs and, second, the costs that the public would otherwise have incurred if the smoker had not smoked. Quite simply, tobacco companies and their customers have more than paid their way. Indeed, federal and state governments have benefited handsomely from excise tax collections, and therein lies one reason they have been unwilling to make cigarettes illegal.

### Myth #5: A legislated settlement is the only way to resolve this serious problem.

Disputes between private parties must not be resolved by legislative fiat. The settlement emerged after secret negotiations involving defendants with the boot of government resting on their necks, state attorneys general who seek to replenish their Medicaid coffers without imposing unpopular tax increases, and advocacy groups that have subordinated the rule of law to their professed health concerns. Our courts, not our legislatures, are constituted for the resolution of such disputes. They are the proper forum to adjudicate the one legitimate argument for holding a tobacco company liable notwithstanding a consumer's decision to smoke: a smoker is not free to choose if he relies on fraudulent advertising or if he is addicted as a minor and unable to quit once he is capable of appreciating the risks.

Weighing against that argument, however, is evidence that 46 million people have quit smoking. Moreover, as tobacco critic Richard Kluger concedes: "Whether one categorizes smoking as a . . . vice, a dependency, or an addiction, it was commonly known—and had been for decades—to be hard to stop once begun. Nor could anyone say for certain how much of a daily dose served to induce addiction; tolerance differed from person to person." Kluger concludes that there is no

basis to "claim that the cigarette makers had massively imposed an intentionally addicting product on an innocent public that had little knowledge or choice in the matter."<sup>8</sup>

The hazards of tobacco were well-documented as long as 400 years ago. Indeed, throughout this century incessant warnings have emanated from thousands of health publications, medical professionals, and government entities. By the 1920s, 14 states had actually prohibited cigarettes. Printed health warnings appeared on every pack of cigarettes lawfully sold in the United States for the past 30 years. To be unaware of the danger of tobacco is to have been hopelessly oblivious.

In any event, those are the claims and counterclaims that should be resolved in court. Our adversarial system—including evidence, trial, and jury verdict—must be permitted to function. Smokers, insurance companies, and the industry should fight it out, applying traditional principles of tort law. State Medicaid systems may sue like any other insurer; but they are subject to the assumption-of-risk defense and they must prove case-by-case causation and damages. If a plaintiff can show that he was defrauded, unaware of the risks, and addicted by the industry's deception, then he should prevail. But the rules must be objective and evenhanded—the same rules that are applied against any other defendant.

As for Congress, if it truly wants to discourage tobacco consumption, it can start by eliminating the industry's subsidies. There can be no rational explanation why the Department of Agriculture expends tax dollars in promoting an activity that the FDA is attempting to inhibit. Despite that unassailable proposition, we are treated to the spectacle of Dan Glickman, secretary of agriculture, announcing to the applause of North Carolina tobacco farmers—two

months after the parties signed the "Proposed Resolution"—that "[o]ur support for the tobacco program is as strong as ever."<sup>9</sup>

Regarding tobacco and its dangers, the private sector is capable of gathering and disseminating the requisite information. Then, based on that information, we can each decide whether to purchase a particular product. The controlling principle is the one laid down by former Senator George McGovern, who lost his daughter to alcoholism and thus knows firsthand what can transpire when a risky product is abused. Senator McGovern points to "those who would deny others the choice to eat meat, wear fur, drink coffee or simply eat extra-large portions of food." He cautions that "the choices we make may be foolish or self-destructive [but] there is still the overriding principle that we cannot allow the micromanaging of each other's lives.

. . . [W]hen we no longer allow those choices, both civility and common sense will have been diminished."<sup>10</sup> □

1. Richard Scruggs, remarks to the Federalist Society, National Conference on Civil Justice and the Litigation Process, September 12, 1996, transcript, p. 188.

2. Stephen Rothman, "Tobacco Industry Defense Move Curbed by Fla. Judge," Reuters, February 3, 1997.

3. Dwight R. Lee, *Will Government's Crusade Against Tobacco Work?* (St. Louis: Center for the Study of American Business, Washington University, 1997), pp. 2-4.

4. *Ibid.*, p. 4.

5. William G. Manning, et al., "The Taxes of Sin: Do Smokers and Drinkers Pay Their Way?" *Journal of the American Medical Association*, March 17, 1989, p. 1604.

6. Jane G. Gravelle and Dennis Zimmerman, *Cigarette Taxes to Fund Health Care Reform: An Economic Analysis* (Washington, D.C.: Congressional Research Service, 1994).

7. W. Kip Viscusi, "Cigarette Taxation and the Social Consequences of Smoking," in James Poterba, ed., *Tax Policy and the Economy* (Cambridge, Mass.: MIT Press, vol. 9, 1995), Table 5.

8. Richard Kluger, *Ashes to Ashes: America's Hundred-Year Cigarette War, the Public Health, and the Unabashed Triumph of Philip Morris* (New York: Alfred A. Knopf, 1996), p. 760.

9. "Washington Assures N.C. Tobacco Farmers," Reuters, August 27, 1997.

10. George McGovern, "Whose Life Is It?" *New York Times*, August 14, 1997, p. A35.

