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CHAPTER ONE

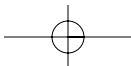
A New Way of Regulating Tobacco

CIGARETTE PRICES IN THE UNITED STATES vary a great deal with the quality of the brand and the state in which the sale occurs, but the price of leading brands has shot up everywhere in the past several years. In 1997 premium-brand cigarettes were selling at around \$1.90 per pack. Starting in 1997, however, major manufacturers raised the wholesale price of cigarettes fourteen times in five years.¹ By fall 2003 the price was approximately \$3.60 a pack, and it was much higher in states with steep excise taxes, such as California, Maine, Massachusetts, Michigan, New Jersey, New York, Rhode Island, and Washington.

The rise is not accounted for by an increase in the price of tobacco. Although tobacco is a very profitable crop for the farmers who grow it, yielding more income than other crops do, only a tiny fraction of the cost of a cigarette, less than 1 percent, is traceable to the manufacturers' tobacco purchases.² Nor is the rise accounted for by increases in production costs, which are relatively low because tobacco manufacturing is highly mechanized.

The place to hunt for an explanation of rising prices is not in the realm of economics but that of politics and law. Rather than searching in tobacco fields and factories, one should look to government offices, law firms, and courtrooms. Approximately 50 cents of the price increase is attributable to legal fees, plus the costs of a legal settlement the major cigarette manufacturers reached late in 1998 with state governments that had brought suit against them between 1994 and 1997, charging consumer fraud and unjust enrichment, among other offenses. This so-called Master Settlement Agreement (MSA) with forty-six states, along with settlements previously reached individually with Florida, Minnesota, Mississippi, and Texas, obliged the companies to pay an estimated \$246 billion to the state governments between 2000 and 2025. By the end of 2003, the forty-six MSA states had received more than \$29 billion.³

In effect, the settlement costs are an addition to the excise taxes on cigarettes that the state governments levy through legislation. And



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while the settlement costs were driving the price of cigarettes up, so were rises in both federal and state excise taxes. The federal excise tax per pack rose in 2000 from 24 to 34 cents, and in 2002 to 39 cents. The average state tax at the beginning of 2002 was approximately 44 cents, and in the following two years more than thirty states enacted increases.⁴

Of course, the companies have also increased prices to sustain their profits, and some industry analysts believe that these price increases have exceeded what was necessary to meet the extraordinary new legal costs. The companies had reason to believe—mistakenly, as it turned out—that the terms of their settlement with the state governments had protected them against price competition and hence a loss of market share.

• Shift in Policymaking Strategy •

How all this happened is the subject of this book, which analyzes a dramatic shift in the way governments make policy toward the tobacco industry. Between 1964 and 1993, governments practiced what I call “ordinary politics,” by which I mean that the principal arena of policymaking was elected legislatures, where the outcomes typically were compromises between contending interests—public health advocates opposed to tobacco use on one side, and the industry, consisting of manufacturers and growers, on the other side. Retailers and the broadcasting and advertising industries were sometimes allied with the latter. Litigation against the manufacturers was limited to individual cases and had little influence on public policy. Then the politics of tobacco suddenly underwent a fundamental change, in which policymaking was, at least for a time, largely removed from legislatures and instead made the subject of litigation.

The attorneys general of the state governments initiated the change. Starting with the attorney general of Mississippi, Mike Moore, they began filing suit in the summer of 1994. These suits were in general carried on without public appropriations, and their results, negotiated settlements between legal adversaries, were touted by the attorneys general as having advantages that could not be obtained through other means, including legislation. To finance them, nearly all attorneys general circumvented legislatures by signing contingency-fee contracts with private tort lawyers. Newly enriched with winnings from asbestos and other class-action suits against product manufacturers, these tort lawyers were able to invest some of their wealth speculatively in the suits against tobacco, in the hope that they would win and be still

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further enriched. The suits also benefited from legislative support. The legislatures of at least three states, Florida, Maryland, and Vermont, changed state law to ensure that their attorneys general would defeat the industry in the states' courts. What was sacrificed was not policy-making by legislatures but respect for law as an institution.

• Master Settlement Agreement •

The initial attempt by the state attorneys general and the major cigarette manufacturers to settle the lawsuits and create a new regulatory regime for tobacco was submitted to Congress for action. Completed in June 1997, this potential settlement alluded somewhat disingenuously to the inefficiencies of the many lawsuits, private as well as public, against cigarette manufacturers: "All of these civil actions are complex, slow moving, expensive and burdensome, not only for the litigants but also for the nation's state and federal judiciaries. . . . Only national legislation offers the prospect of a swift, fair, equitable and consistent result that would serve the public interest. . . ."5 National legislation, however, was not forthcoming. The Senate debated a bill but did not act, and the contending litigants resumed negotiations in June 1998.

The document they arrived at, the Master Settlement Agreement of November 1998, besides requiring the billions of dollars in payments to state governments, contained many prohibitions on marketing. It banned transit and outdoor advertising, including billboards and signs or placards larger than a poster in arenas, stadiums, shopping malls, and video game arcades. It banned cartoon characters in advertising, promotion, and packaging, putting an end to the infamous Joe Camel, a hip character that the R. J. Reynolds Company had created and popularized in the late 1980s. It banned the distribution and sale of nontobacco merchandise with brand logos, such as caps, T-shirts, and backpacks, except at tobacco-sponsored events. Other than allowing one event per year, it prohibited brand-name sponsorship of concerts, events with a significant youth audience, and team sports (football, basketball, baseball, hockey, and soccer).

The agreement also contained restrictions on the industry's political activity that were little remarked in journalistic accounts but are deeply problematic from the point of view of American political traditions. It disbanded the Tobacco Institute, the industry's lobbying organization. It prohibited the cigarette companies from lobbying against any of the terms of the MSA or challenging their constitutionality. It prohibited them from seeking bankruptcy. It also barred them from lobbying against various state and local legislative proposals, such as those

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limiting youth access to vending machines or penalizing youths for possession of tobacco.

• FDA Campaign •

The state governments' lawsuits were not the only attempts at bypassing legislatures in the late 1990s to expand the scope of tobacco regulation. Another was a campaign by David A. Kessler, commissioner of the federal Food and Drug Administration (FDA) between 1990 and 1997, to assert jurisdiction over the regulation of tobacco. Under Kessler the FDA, which earlier had denied that it had such authority, reinterpreted the law and in 1996 issued regulations with the backing of the Clinton White House. This action was overturned in the courts, although only by the narrowest of margins (5 to 4) in the Supreme Court, which ruled in spring 2000 that the FDA's historic interpretation was correct—it lacked statutory authority to regulate cigarettes.

Kessler's campaign gained momentum after the Republican capture of the House of Representatives in the 1994 midterm elections. It won crucial support within the Clinton White House precisely because it offered a way to pursue health policy objectives without legislation. Defeated in the courts, this campaign was ultimately less significant than the litigation brought by the state attorneys general, but both substantively and tactically the two efforts complemented one another. I therefore treat both of them, exploring in detail their origins and outcomes, including the failure of Congress to enact the terms of the 1997 settlement between the cigarette companies and the state governments.

• Purpose of the Book •

Before exploring the recent rise of extralegislative policymaking, I describe the legislation and litigation that took place in the years 1964–1993. I begin with the assumption that policymaking by elected, representative legislatures is preferable to litigation as a matter of constitutional principle. Self-government is at the core of the American Constitution: Here the people rule. Officeholders acquire the right to make decisions on behalf of the rest of us either by being elected or by being accountable to those who are elected. However, big governments, burdened with many responsibilities, test the principle of self-government.

As a practical matter, legislatures must make broad delegations of rulemaking authority to executive agencies. When these delegations are clear and agency rules fall within their bounds, such rulemaking fits more or less comfortably under my rubric of “ordinary politics.” Agency

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rulemaking in American government is long established, voluminous, heavily regulated by statutory law, and constantly subject to judicial scrutiny. On the other hand, statutory delegations are often vague and contestable, and the American system of separated powers, with a government in which the executive and legislative branches are independently constituted and often controlled by rival political parties, invites entrepreneurship by agency heads. The story told here of David Kessler's enterprise shows both how far a determined agency head can go in mounting initiatives without congressional sanction and how judicial review can constrain such conduct.

Policymaking through litigation, engaging as contestants the parties principally at interest, is more deeply problematic for democracy than agency rulemaking, especially when, as in the cases recounted here, out-of-court settlements are reached, so neither judges nor juries bring judgments to bear. Typical as a way of concluding lawsuits, negotiations between the contending parties do not feature public deliberation, as legislation ordinarily does in a democracy (even if legislative procedures are often less than transparent).

Believing that policymaking by elected, representative legislatures is the preferable form in our constitutional system, I believe also that those who would circumvent it should bear a heavy burden of justification, and one of my purposes is to see whether, or how, this burden was borne in the tobacco case.

Although this book is about how policy is made rather than what tobacco policy ought to be, how a reader reacts to the story is likely to depend on what he or she believes both about tobacco use and about the relation between government and its citizens. How far ought government to go in protecting citizens against their vices, and how far in regulating manufacturers of harmful products? At one extreme, governments in the United States might do nothing about tobacco, which historically was a staple crop of the South, helping to sustain the economy of a desperately poor region; at the other extreme, they could prohibit its growth, manufacture, and use.⁶ Since the danger of tobacco use was scientifically established and officially publicized in the mid-sixties, governments in the United States have sought to control tobacco consumption by occupying a middle ground, relying mainly on moderate taxation, warning labels and other public admonitions, limitations on place of use, prohibition of radio and TV advertising, and prohibition of sales to minors (a prohibition that historically has not been well enforced). Critics of tobacco are critics also of tobacco politics and regard this path of compromise as proof of the excessive power of the producers in legislative politics.

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It is of course tempting to judge policymaking processes by whether they produce the outcomes one prefers. However, by participating in a regime of constitutional democracy, one agrees to respect the preferences of others and of the polity as a whole, assuming that they are legitimately arrived at. For policy processes to be legitimate, at a minimum they need to be both broadly representative and plausibly public-regarding. Policy-makers need to take account of a wide range of interests (both organized and unorganized), combine and compromise them, and in the end transcend them to arrive at an outcome that serves no self-regarding interest alone or one that is above a broader public interest. This approach implies respect for public opinion but not an invariable deference to it. At any given time, it may or may not imply a need for action. In regard to tobacco control, Congress has more often than not implicitly preferred inaction to action, and critics have again taken this inaction as proof of Congress's subservience to producer interests.

Elected legislatures are designed to represent numerous constituencies and effectuate their preferences through policy choices that will be approved by a majority of the public, but many Americans appear to be skeptical of legislatures' ability to do this work well, partly because our elected politicians receive large campaign contributions from corporate donors such as cigarette manufacturers.⁷ The question raised here, however, is not whether legislatures are ideal instruments of policymaking; rather, it is how they compare with the litigation-centered alternatives to which Americans have an increasing propensity to resort. While pondering this question, we should remember that among all industries in the United States, including finance and real estate, pharmaceuticals, and tobacco, the largest contributors to election campaigns are lawyers and law firms.⁸

Politicization of the law is not a new story in this country, but it comes vividly to life in the contemporary politics of tobacco.

• Notes •

1. Pat Stith, "Upstart Brands Hurt Big Tobacco," *Raleigh News & Observer*, January 4, 2004, <http://newsobserver.com/front/story/3177143p-2862436c.html>, accessed January 14, 2004.
2. Tara Parker-Pope, *Cigarettes: Anatomy of an Industry from Seed to Smoke* (New York: New Press, 2001), 27. Parker-Pope's source was David Adelman, a tobacco industry analyst for Morgan Stanley Dean Witter, who estimated the breakdown of the cost of a pack of cigarettes purchased in New York City at \$3.50.
3. "President's Message: Fifth Anniversary of Landmark Tobacco Settlement," National Association of Attorneys General, <http://www.naag.org/news/presmsg-20031117-tobacco.php>, accessed January 8, 2004.

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4. "Cigarette Excise Tax per Pack, February 1, 2002," Centers for Disease Control, http://www.cdc.gov/tobacco/statehi/html_2002/excise.htm, accessed January 5, 2004; Gordon Fairclough, "Politicians Are Hooked on Cigarette Taxes," *Wall Street Journal*, February 20, 2002, A2; and American Heart Association, Campaign for Tobacco-Free Kids, American Cancer Society, and American Lung Association, *A Broken Promise to Our Children: The 1998 State Tobacco Settlement Five Years Later* (November 12, 2003), iv.
5. Carrick Mollenkamp et al., *The People vs. Big Tobacco* (Princeton, N.J.: Bloomberg Press, 1998), 270.
6. On the place of tobacco (and rice and cotton) in southern agriculture, see Pete Daniel, *Breaking the Land: The Transformation of Cotton, Tobacco, and Rice Cultures since 1880* (Urbana and Chicago: University of Illinois Press, 1985). Former president Jimmy Carter's wonderfully evocative portrait of the Depression-era rural South contains this description of Archery, a vanished town in which he spent his boyhood: "Archery . . . was never quite a real town. At the heart of it, a little more than a half-mile west of our farmhouse, were the homes of the Seaboard Airline Railroad section foreman and the six black employees who kept the rail bed in good repair. A half-mile farther west was a strong African Methodist Episcopal church congregation, across the road from the most notable landmark, a small store by the railroad that was sheathed completely in flattened Prince Albert tobacco cans." See Jimmy Carter, *An Hour Before Daylight* (New York: Simon and Schuster, 2001), 14–15.
7. On perceptions of Congress, see John R. Hibbing and Elizabeth Theiss-Morse, *Congress as Public Enemy: Public Attitudes toward American Political Institutions* (New York: Cambridge University Press, 1995).
8. The Web site of the Center for Responsive Politics (<http://www.opensecrets.org>, accessed January 16, 2004), which compiles campaign contributions by industry from records of the Federal Elections Commission, has ranked lawyers and law firms as the top-spending industry in all eight election cycles between 1990 and 2004.

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