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**Testimony in Support of Senate Bill 255
An Act Concerning Sales of Cigarettes and Tobacco Products**

**Presented to the Senate Committee on Judiciary
By Assistant Attorney General Jordan Brewer, Tobacco Enforcement Unit**

March 17, 2015

Chairman King and Members of the Committee:

The Office of the Attorney General respectfully submits the following testimony to the Committee in support of Senate Bill 255, an Act concerning sales of cigarettes and tobacco products.

As a brief background, the State of Kansas ("Kansas"), along with 51 other states and territories, entered into the Master Settlement Agreement ("MSA") in 1998 to resolve lawsuits filed against certain tobacco manufacturers. The tobacco manufacturers that have signed the MSA are known as Participating Manufacturers ("PMs"). All other tobacco manufacturers are known as Non-Participating Manufacturers ("NPMs"). As required per the MSA, Kansas enacted a "qualifying statute" for MSA enforcement in 1999. Since then, Kansas has enacted "complimentary legislation" to aide in enforcing the MSA. These MSA statutes are found in the Kansas MSA Escrow Statutes, K.S.A. § 50-6a01, *et seq.* Other changes have been made to the MSA Escrow Statutes over time, most recently in 2009.

Under the MSA, Kansas is tasked with "diligently enforcing" its "qualifying statute." In 2003, the PMs challenged several states' MSA diligent enforcement efforts in arbitration. In 2012, Kansas, along with 19 other contested states and two uncontested states, settled the matter outside of arbitration ("2003 NPM Adjustment Settlement and Term Sheet"). Subsequently, two more states have settled with the PMs and have adopted the Term Sheet. The parties to the settlement are presently finalizing a formal settlement agreement.

By virtue of this settlement, Kansas agreed to make certain changes regarding diligent enforcement of the MSA. Kansas also resolved MSA enforcement liability for calendar years 2003-2014. Of the states that did not settle and had their diligent enforcement efforts contested, six were deemed non-diligent by the arbitration panel, including Missouri. Each of the non-diligent states is required to pay back tens of millions of MSA dollars in future payments (subject to appeal), *e.g.* Indiana (\$83,000,000), Kentucky (\$72,000,000), Maryland (\$92,000,000), Missouri (\$93,000,000), New Mexico (\$24,000,000) and Pennsylvania (\$235,000,000). These figures will be eventually be multiplied by the number of years that these states are found to have not diligently enforced the MSA between 2004 and the present. Through the arbitration rulings, Kansas was able to learn what the arbitration panel deemed important for diligent enforcement purposes. The panel listed the following eight factors:

1. Collection Rate
2. Lawsuits Filed
3. Gathering of Reliable Data
4. Resources Allocated to Enforcement
5. Preventing Non-Compliant NPMs from Future Sales
6. Legislation Enacted
7. Actions Short of Legislation
8. Efforts to be Aware of National Association of Attorneys General (NAAG) and Other States' Enforcement Efforts

In recent years, Kansas has received approximately \$60,000,000 per year from the MSA, although that figure is expected to trend slightly lower due to decreased tobacco sales and other factors. In order to help ensure that Kansas continues to receive its full annual payment under the MSA, Kansas needs to make amendments to the MSA Escrow Statutes as well as changes to Kansas's enforcement efforts.

Using the 2003 NPM Adjustment Settlement and Term Sheet and the arbitration panel rulings as directives, the Attorney General's Office has submitted the proposed legislation amending the MSA Escrow Statutes relating to the directory and certification of tobacco product manufacturers, disclosure of information and criminal penalties.

The amendments proposed in Senate Bill 255 focus on the MSA Escrow Statutes and not the Cigarette and Tobacco Products Act, K.S.A. § 79-3301, *et seq.* The Office of Attorney General has submitted Senate Bill 255, as introduced, to the PMs, and they have confirmed that if enacted these changes would result in Kansas maintaining a "qualifying statute" under the MSA (See attachment 1). The second requirement is for Kansas to "diligently enforce" its qualifying statute, and the Department of Revenue has proposed additional changes to the Cigarette and Tobacco Products Act in Senate Bill 203 making recommendations to strengthen enforcement going forward.

The overall purpose of most of these amendments is MSA enforcement through increased escrow requirements under the definition of "units sold," annual manufacturer certifications, directory maintenance, increased penalties for violations and disclosure of information.

The following are descriptions of the specific section amendments in Senate Bill 255:

Section 1. Section 1 amends the definition of "units sold" to require escrow payments by NPMs on all FET-paid sales for which Kansas has the authority to tax (includes internet sales and sales on tribal lands). This escrow requirement is part of the 2003 NPM Adjustment Settlement and Term Sheet.

Section 2. Section 2 includes several amendments and additions. First, it makes it a violation of the MSA Escrow Statutes for a person to sell, offer, possess for sale or import into this state cigarettes of a tobacco product manufacturer brand family not included in the directory. The directory refers to the directories of compliant PMs and NPMs as maintained by the Attorney General. Second, it adds the

authority for the Attorney General to remove a tobacco product manufacturer from the directory of approved manufacturers if found guilty of a felony sale or taxation crime or if removed from the directory of another state under certain circumstances. Third, it requires NPMs to include in their annual certification the identity of all stamping agents to whom the NPMs sold cigarettes or believed or had reason to believe purchased or received any cigarettes from another source during the preceding year. The purpose of this change is to better identify and track the channel through which cigarettes are sold in this state. Fourth, it requires NPMs to declare that all sales or shipments made by the NPMs and their importers and stamping agents into this state are made to stamping agents or retailers licensed by the state. Fifth, it requires all tobacco product manufacturers include on their annuals certifications that they have a valid federal tobacco manufacturer permit and that they are in compliance with all requirements of the Prevent All Cigarette Trafficking Act (“PACT Act”). The manufacturers are required to submit copies of both the permit and PACT Act reports. Additionally, all manufacturers must pay an annual directory fee of \$500.

Section 3. This section adds definitions of “Indian tribe” and “tribal land.”

Section 4. Section 4 authorizes the Attorney General to request invoices and documentation of sales of all NPMs. Currently, such authority is granted to the Director of Taxation.

Section 5. Section 5 includes two amendments. First, it adds the ability for the Director of Taxation and the Attorney General to share certain information with other agencies, the data clearinghouse and counsel for the PMs as required by the 2003 NPM Adjustment Settlement and Term Sheet. Second, it provides that any tobacco sales data provided to the Director, Attorney General or data clearinghouse for MSA and MSA-related agreements enforcement purposes shall be confidential.

Section 6. This section increases the criminal penalties, including enhancing second and subsequent violations to felonies, for selling or possessing cigarettes in Kansas in violation of the MSA Escrow Statutes. Currently, the criminal penalties are minor: Class B misdemeanors with fines up to \$1,000. The purpose of felony enhancements is to deter the smuggling of cigarettes into the State.

Section 7. This is the only amendment that occurs outside of the MSA Escrow Statutes and adds the authority for the Director of Taxation and the Attorney General to share certain information with other agencies, the data clearinghouse and counsel for the PMs as required by the 2003 NPM Adjustment Settlement and Term Sheet (similar to Section 5). This section concerns licensure, registration and taxpayer information from stamping agents and retailers.

Thank you for the opportunity to present this testimony on behalf of the Office of the Attorney General and I stand for any questions that the Committee may have.

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February 17, 2015

VIA EMAIL

Jordan Brewer
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120 SW 10th Avenue, 2nd Floor
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Re: Proposed Kansas Legislation

Dear Jordan:

I am writing on behalf of the Original Participating Manufacturers under the Master Settlement Agreement (“MSA”) to confirm that, if the enclosed proposed legislation is enacted, Kansas will continue to have in full force and effect a Model Statute and a Qualifying Statute, as these terms are defined in MSA Section IX(d)(2)(E).

Sincerely,

/s/ Alexander Shaknes

Alexander Shaknes

enclosure