Approved: 2/29/00
Date

MINUTES OF THE HOUSE TAXATION COMMITTEE.

The meeting was called to order by Chairperson Wagle at 9:00 a.m. on February 15, 2000, in Room 519-S of the Capitol.

All members were present except: Rep. Tedder - excused
Rep. Tomlinson - Excused
Rep. Edmonds - excused

Committee staff present: Chris Courtwright - Legislative Research Department
April Holman, Legislative Research Department
Don Hayward, Revisor of Statutes
Shirley Sicilian, Department of Revenue
Ann Deitcher, Committee Secretary
Edith Beaty, Taxation Secretary

Conferees appearing before the committee: Kansas Attorney General, Carla Stovall
Deputy Attorney Genera, John Campbell

The Attorney General's staff passed out copies of testimony. (Attachment 1 through 34).

The day's entire testimony was taken verbatim by a court reporter. These minutes are attached. (Attachment 35).

The meeting was adjourned at 10:20 a.m. The next meeting is scheduled for Wed., February 16, 2000.

State of Kansas
House of Representatives

Susan Wagle

February 2, 2000

Honorable Carla Stovall
Kansas Attorney General
120 SW 10th Avenue
Memorial Hall
Topeka, Kansas 66612-1524

Dear Attorney General Stovall:

Thank you for allowing John Campbell, Deputy Attorney General, brief tax leadership yesterday on tobacco litigation.

I plan on having informational/investigative hearings during the week of February 14th. I am hopeful that you will allow John Campbell to brief the Tax Committee on the history of the tobacco litigation on Monday, February 14th, and Tuesday, February 15th. On Wednesday, February 16th, I would like to give Representative Tony Powell an opportunity to brief the Tax Committee on the merits of his bill to tax the attorneys' fees at 50%. I am hopeful that on Wednesday after Representative Tony Powell has defended his bill, you would address the Tax Committee on your position.

The Tax Committee will start at 9:00 a.m. I would like to give both Representative Powell and you 30 minutes to address the Tax Committee and then open the issue up for questions. If you are unable to attend the hearing on Wednesday, I am hopeful you will send John Campbell or any other representative you desire on your behalf.

Thank you for your cooperation in this matter.

Sincerely,

Susan

Susan Wagle
Tax Committee Chairperson

REPRESENTATIVE, 99TH DISTRICT
BUTLER/SEDGWICK COUNTIES
14 SANDALWOOD
WICHITA, KANSAS 67230

House Taxation
Date 2/15/00
Attachment # 1

State of Kansas
House of Representatives

Susan Wagle

January 26, 2000

Honorable Carla Stovall, Attorney General
Kansas Attorney General's Office
120 SW Tenth Avenue
Topeka, Kansas 66612-1597

RE: Document's Request

Dear Attorney General Stovall:

I am writing to request that you provide to my Committee documents relating to the hiring of private counsel for the purpose of assisting the State in its pursuit of litigation involving the tobacco industry. This information will be needed so that the Committee may conduct a proper investigation as to how the law firm of Entz and Chanay was selected.

Thank you in advance for your cooperation in this matter. We would appreciate receiving this information within seven days.

Very truly yours,

Susan Wagle
Chairperson, Committee on Taxation

REPRESENTATIVE, 99TH DISTRICT
BUTLER/SEDGWICK COUNTIES
14 SANDALWOOD
WICHITA, KANSAS 67230

House Taxation
Date 2/15/00
Attachment # 2

STATE OF KANSAS

236 N. EAGLE ROAD
HEALY, KANSAS 67850
(316) 398-2238
380-W STATE CAPITOL
TOPEKA, KS 66612-1504
(785) 296-2302

STATE REPRESENTATIVE
117TH DISTRICT
HODGEMAN, LANE, NESS
RUSH AND FINNEY COUNTIES

Speaker of the House

Robin Jennison

February 14, 2000

The Honorable Carla Stovall, Attorney General
Office of the Attorney General
120 SW 10th Ave
Topeka, KS 66612

Dear Attorney General Stovall:

During the course of the last several weeks the Chairperson of the Committee on Taxation, has requested records or documents from you concerning your actions in hiring counsel for the purpose of assisting the state in pursuit of litigation involving the tobacco industry. A letter was received from Mr. Campbell, Senior Deputy Attorney General, discussing several topics but not providing records or documents. Chairperson Wagle then wrote again to you asking for public records in the possession of the Office of the Attorney General which relate to this matter. In return, Chairperson Wagle was provided with documents similar to those obtained by the Legislative Post Audit Committee under an audit of water rights litigation and procedures for selecting attorneys.

Frankly, there are a number of legislators who have information which make it appear that Chairperson Wagle has not received from you all the documents and records in possession of your office on this matter. This matter should not drag on any further or need to involve any more formal procedures like subpoena for the legislature to obtain this information. The legislature has business to conduct and it is in our mutual interests to resolve this issue and move on. In this regard, I am requesting from the Office of the Attorney General a copy of the signed and dated contract or contracts entered into by you on behalf of the state of Kansas with the law firm of Entz and Chanay and any other law firm, including national counsel, relating to tobacco litigation and any correspondence, memoranda, documents and any other records in any form which relate to any negotiation with or consideration of the hiring of the Entz and Chanay firm or the hiring of or failure to hire any other law firm in the tobacco litigation cases.

To make this clear, I am requesting:

(1) A copy of any contract entered into by the Office of the Attorney General with Entz and Chanay and any other lawyer or law firm relating to the tobacco litigation (signed and dated copy);

(2) the names of any other law firm or lawyers considered by the Attorney General as possible attorneys for the state in the tobacco litigation prior to hiring the firm of Entz and Chanay;

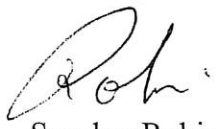
(3) a copy of all records, correspondence, memoranda, documents and any other records in any form which relate to negotiations with the Entz and Chanay law firm or any other law firm or lawyer, whether hired or not, as part of the process of selecting a law firm to represent the state in the tobacco litigation.

(4) A copy of each billing from the Entz and Chanay law firm or other law firm pursuant to the contract or contracts you entered into with any law firm on this matter.

If you have this information please provide it by 3:00 p.m. on Tuesday, February 15. If you have this information but refuse to provide it to me, please specify what information you possess and the reason for the refusal. If you do not have this information, say so and provide me a list specifying the information requested above which you do not have.

Your speedy cooperation in this matter will be appreciated.

Sincerely,



Speaker Robin Jennison

State of Kansas
Office of the Attorney General
120 S.W. 10th Avenue, 2ND FLOOR, TOPEKA, KANSAS 66612-1597

CARLA J. STOVALL
ATTORNEY GENERAL

MAIN PHONE: (785) 296-2215
FAX: 296-6296

January 31, 2000

The Honorable Susan Wagle
Representative, District 99
Room 170-W, Capitol
Topeka, KS 66612
Fax: 8-6365

RE: House Bill 2386

Dear Chairperson Wagle:

I am in receipt of your letter of January 26, 2000 in which you request us to, ". . . provide to my Committee documents relating to the hiring of private counsel for the purpose of assisting the State in its pursuit of litigation involving the tobacco industry." This letter is written in response and in preparation for our meeting of tomorrow.

As you know, in 1997 the Legislative post audit conducted an extensive investigation of this same issue. As part of that investigation, three auditors were given unlimited access to the RJ Reynolds and Brooke Group Limited, case files for four months. Therefore, they should have the documents you have requested, but I will double check on this. In the meantime should you or your staff wish to have the same access, please contact me and arrangements will be made.

As an attorney for the State, I must sound a note of caution. Post Audit obtained the above-described documents pursuant to K.S.A. 46-1101 *et seq.*, by which the attorney client and attorney work product privileges were maintained. If these documents are distributed to the Committee or other persons and discussed in an open session, those privileges will be waived. Such a waiver could have serious consequences.

Tobacco litigation is not over. Currently the State of Kansas is a party in the case, *PTI, Inc. et al. v. Philip Morris, et al.*, Central District of California Case No. 99-08235. In addition, eight states are currently being sued by individuals harmed by tobacco products who are not being compensated by the funds received in the settlement. It would not surprise me if Kansas is added to that number. Finally, the Shawnee County District Court retains enforcement jurisdiction over the injunctive relief granted under the Master Settlement Agreement (MSA). In the event that it

House Taxation
Date 2/15/00
Attachment # 4-1

appears that the tobacco companies have returned to their past practices, such as marketing cigarettes to children, the suit would be reactivated and most likely discovery ordered.

Once the privilege is waived, it could be gone for every internal communication the State has now and in the future with relation to tobacco litigation. This could seriously jeopardize future enforcement of the MSA and the collection of the $1.6 billion that the State is entitled to under that agreement.

Further it is unlikely that other states will wish to continue sharing confidential information with us if such a waiver occurs. An example of the cost of such a decision can be found in the PTI suit. Currently the State of California is representing all of the states sued in that action. Not having to retain local California counsel, prepare separate pleadings, and appear and argue in California does save Kansas money.

Also of concern are the documents held by Post Audit relating to *Kansas v. Colorado*, U.S. Supreme Court 105 Original. As you know, this case is still in active litigation before a special master. Any release of materials from that case would constitute a waiver of privilege and subject Kansas to extraordinary discovery by Colorado. At best this would increase the cost of the litigation.

I strongly advise you to review the matter of privilege with the Revisor of Statutes. I have not discussed this matter with Mr. Furse so you will be getting a fresh evaluation from a lawyer I know you trust. It may well be that the Revisor thinks I am overly cautious and that waiver is not a problem, or he may have some suggestions as to how your Committee's needs and the State's litigation goals can both be served.

I hope the above satisfies your request of January 26th. I look forward to our meeting tomorrow. Should you or your staff require additional information or assistance please contact me.

Sincerely,

OFFICE OF THE ATTORNEY GENERAL
CARLA J. STOVALL

John W. Campbell
Senior Deputy Attorney General

JWC:dsw
cc: Post Auditor

State of Kansas
Office of the Attorney General
120 S.W. 10th Avenue, 2ND FLOOR, TOPEKA, KANSAS 66612-1597

CARLA J. STOVALL
ATTORNEY GENERAL

MAIN PHONE: (785) 296-2215
FAX: 296-6296

February 4, 2000

The Honorable Susan Wagle
Representative 99th District
Room 170 -W
State Capitol
66612-1510

RE: Re: HB 2683

Dear Chairperson Wagle:

I am in receipt of your letter of February 4, 2000. As I understand it, you do not want to take advantage of my offer for either you or your staff to have complete access to the tobacco litigation files nor do you wish to take responsibility for possibly waiving the state's attorney client and/or work product privilege. Instead you ask us basically to repeat Post Audit works of 1997 and make the call as to if the document requested contains any confidential or privileged information which would endanger the State's privileges.

It appears to me that all of your requests are contained in the second paragraph of your letter. I will break down those requests below and respond accordingly:

1. "a copy of the contract entered into by you [attorney general] on behalf of the state of Kansas with the law firm of Entz and Chanay relating to the state tobacco litigation, . . . " Parenthetical supplied:

No request for a copy of this contract has ever been declined. A copy of the contract is attached.

2. "the names of any other law firms considered by the Attorney General prior to entering into the contract with Entz and Chanay, . . . "

Enclosed is page 21 of the Legislative Post Audit's report on its investigation of the hiring of Entz and Chanay. It lists all of the firms that were considered.

House Taxation
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Attachment # 5-1

3. "and all correspondence, memoranda, documents and any other records in any form which relate to the hiring of private counsel to assist the state in the pursuit of litigation involving the tobacco industry including all correspondence, memoranda, documents and any other records in any form relating to any negotiation with or consideration of the Entz and Chanay firm or any firm other than Entz and Chanay firm with regard to this matter."

As you know, three auditors took four months to look through the files for such information, as well as information relating to the hiring of *Kansas v. Colorado* and other legal counsel. I will do my best to duplicate their work with regard to the tobacco litigation prior to the February 14 hearings. I have set aside when ever possible, my work on current cases, other legislative requests, etc., and will continue to do so as needed to compile this information, as well as another legislator's request for the organizing the RJR and Liggett court files for "quick and easy access" to the pleadings in RJR and Liggett cases. In addition, I am compiling a time line on the history of tobacco litigation which I hope will be of benefit to the committee.

4. "I am also requesting a copy of each billing from the Entz and Chanay firm pursuant to the contract to which you entered into with this law firm on the tobacco litigation matter."

The State was never billed by Entz and Chanay for any of the tobacco litigation, thus there are no documents which satisfy this request.

I hope the above is a satisfactory response to your request. If it is not or if you need more information, please contact me.

Sincerely,

OFFICE OF THE ATTORNEY GENERAL
CARLA J. STOVALL

John W. Campbell
Senior Deputy Attorney General

JWC:dsw

STATE OF KANSAS
OFFICE OF THE ATTORNEY GENERAL
CARLA J. STOVALL

ENGAGEMENT AND CONTINGENCY AGREEMENT

THE AGREEMENT, effective the 1st day of August, 1996 between the **STATE OF KANSAS BY CARLA J. STOVALL, ATTORNEY GENERAL,** (herein the "Attorney General"), and the law firms of **ENTZ & CHANAY, P.A.; SCRUGGS, MILLETTE, LAWSON, BOZEMAN & DENT, P.A.;** and **NESS, MOTLEY, LOADHOLT, RICHARDSON & POOLE, P.A.,** (herein "Counsel"), is as follows:

WHEREAS, cigarette smoking kills approximately 400,000 individuals each year in the United States; more than the number of deaths caused by guns, drug use and automobile accidents combined; and,

WHEREAS, the cost to the State of Kansas and its citizens for health care and related expenditures for smoking related diseases exceeds tens of millions of dollars each year; and,

WHEREAS, any litigation involving tobacco-related industries is likely to entail numerous complex factual and legal issues; and,

WHEREAS, any such litigation will require the expenditure of substantial resources and attorney time; and,

WHEREAS, the Attorney General seeks to avoid the expenditure of state resources for direct costs and attorney time in any such litigation; and

WHEREAS, the Attorney General plans to bring an action against tobacco companies and related entities pursuant to her authority the Common Law and Kansas Statutes Annotated;

NOW, THEREFORE, IT IS AGREED BY AND BETWEEN THE ATTORNEY GENERAL AND COUNSEL AS FOLLOWS:

Section 1 - Engagement of Counsel

1.1 Counsel is retained to provide legal services to the State of Kansas for the purpose of seeking injunctive relief, monetary relief (including, without limitation, damages and civil penalties) and other relief against tobacco industry companies and related entities ("Defendants") in litigation arising from the advertising, marketing, manufacturing, promotion, sale and/or distribution of cigarettes and other tobacco products (hereinafter "the Litigation"). Counsel shall provide sufficient resources, including attorney time, to prosecute the Litigation faithfully and with due diligence.

1.2 The Attorney General, as the Chief Legal Officer of the State of Kansas shall retain final authority over all aspects of the Litigation. As provided herein, Counsel is authorized to take appropriate legal steps to prosecute the Litigation and participate in all settlement negotiations and the State of Kansas and the Attorney General hereby further agrees not to settle this action without prior consultation with Counsel. However, the Attorney General specifically reserves the right to settle the Litigation without the approval of Counsel.

1.3 The Attorney General may appoint members of her staff to monitor the prosecution of the Litigation. Counsel shall consult in advance with and obtain the prior approval of the Attorney General, or her designee, concerning all significant matters related to the Litigation. Regular status meetings shall be held as requested by either the Attorney General or Counsel.

1.4 It is specifically agreed by the parties that neither Counsel nor any third party employed whose services or products are used by either the State of Kansas or Counsel in furtherance of this agreement or its goals, is considered, or paid as a State employee, but is an independent contractor.

1.5 It is specifically agreed by the parties that any documents or any other tangible objects produced by Counsel, or any third party employed pursuant to this Agreement, which were produced or procured solely in the performance of this agreement, shall be the property of the State of Kansas.

1.6 Counsel shall communicate with state agencies through the Attorney General, unless alternative arrangements are made in advance with the Attorney General. Where written communications from Counsel to state agencies are authorized, the Attorney General shall be provided copies of those communications.

Section 2. Designation of Counsel

2.1 The Attorney General, by this agreement designates Scruggs, Millette, Lawson, Bozeman & Dent, P.A., and Ness, Motley, Loadholt, Richardson & Poole, P.A., as "Lead National Counsel" and Entz & Chanay, P.A. as "Lead Local Counsel" in the Litigation. The Attorney General retains the right, after a showing of just and good cause to revoke such designations and make new designations at any time.

2.2 It is anticipated that additional private law firms may be needed in the representation of the State of Kansas in the Litigation. The Attorney General, after consultation with and agreement by Counsel, retains the right to engage additional counsel to participate in the Litigation. All such added Counsel shall be bound by the terms of this Agreement.

Section 3. Contingent Fee

3.1 Counsels' fees are contingent upon the State receiving funds as a result of claims asserted in the Litigation. If the State receives nothing, no fees are due from the State to Counsel. If the State receives funds by reason of settlement, legislation, judgment in litigation or by any other form or process for resolution of the litigation, Counsel shall be

paid a fee ("counsel Fees"). Counsel Fees shall be determined in accordance with this Agreement, 1995 Kan. Ct. R. Annot 226, MRPC 1.5, by the terms of any settlement agreement or as provided in any other resolution process. Counsels' Fees to Lead National Counsel shall not exceed Twelve and One-Half Percent (12.5%) and Counsel Fees to Lead Local Counsel shall not exceed Twelve and One-Half Percent (12.5%) of funds received by the State as a result of claims asserted in the Litigation.

3.2 The sole contingency upon which compensation is to be paid to Counsel is the recovery and collection by Counsel, on behalf of the State of Kansas, of monies in the Litigation, whether by settlement or judgment.

3.3 Compensation on the foregoing contingency as set forth in Paragraph 3.2, above, shall be made in accordance with 1995 Kan. Ct. R. Annot. 226, MRPC 1.5 and shall not exceed 12.5% to Lead National Counsel and 12.5% to Lead Local Counsel of the amount of money recovered by the State of Kansas in the Litigation.

3.4 In accordance with 1995 Kan. Ct. R. Annot. 226, MRPC 1.5(d), Litigation and other expenses shall be deducted from any recovery before the Contingency Fee is calculated.

3.5 Settlement, for purposes of this Agreement, may include any structure, type or form of settlement of issues raised in the Litigation, including state or federal legislation, state or federal Court multi-party settlement structures or any other structure, means of device to settle and resolve the claims of a nature as alleged in original Petition and any amendments thereto for damages asserted therein or which could have been asserted therein.

3.6 In the event the Litigation is resolved, by settlement or judgment, under terms involving the provision of goods, services or other "in-kind" payment, the parties hereto agree to seek, as part of any such settlement, compensation for Counsel equivalent to the said Contingency Fee and expenses to which Counsel would be entitled under this Agreement. In the event the Attorney General is unable to secure such compensation for Counsel as part of any "in-kind" settlement, the Attorney General agrees to petition the legislature to appropriate funds to reasonably compensate Counsel in accordance with the terms and provisions of this Agreement for both fees and expenses.

Section 4. Expenses of Litigation

4.1 Lead National Counsel shall advance all expenses of the Litigation except those expenses paid by funds appropriated by the legislature of the State of Kansas for said purpose.

4.2 If recovery is obtained, all expenses advanced by Counsel will be paid to said firms advancing the same before the computation of attorney's fees. During the pendency of the litigation the Attorney General retains the right to petition the Kansas legislature for funds needed for expenses in the litigation. In the event no recovery is made by the State of Kansas, Counsel agree to waive any legal claim that they may have against the State of Kansas or any of its officers or employees for reimbursement of costs, expenses and attorney's fees, but may submit the same to the Joint Committee on Special Claims against the state for determination by the legislature. The Attorney General agrees to support Counsel's claims. As to the Court ordered expenses and costs, monies actually recovered from the Defendants for expenses and costs advanced by Counsel shall be the property of Counsel. It is the intent of the parties that such money as is recovered from the Defendants be used to offset the expenses and costs due to Counsel and that only such reasonable expenses and costs not recovered as such from the Defendants be deducted by Counsel from the recovery prior to the calculation of the Contingency Fee.

4.3 Counsel shall, to the extent allowed under the laws of the State of Kansas and subject to approval of the Attorney General, attempt to recoup all expenses, costs and fees due them or the State of Kansas from the Defendants in the Litigation.

4.4 As used in this Agreement the term "expenses" shall include travel, lodging, telephone charges, copying charges, fax charges, deposition costs, investigator costs, messenger service costs, mailing costs, mediation expenses, computer research fees, medical or nursing consultation fees, expert witness fees, consultant's fees, printing costs and all other costs incurred in relation to or as a result of the pendency and prosecution of the Litigation.

4.5 Counsel are not required to maintain time records, but shall maintain expense records. It is understood and agreed by the Attorney General that Lead National Counsel bring to the Litigation thousands of hours of legal work and research regarding tobacco litigation in other states, and the State of Kansas will benefit from such legal work, which Lead National Counsel agree to share with the State of Kansas.

Section 5. Miscellaneous

5.1 Counsel agrees to abide by the provisions of Kansas Statute Annotated 46-239(c). Counsel agrees to notify the Attorney General in the event K.S.A. 46-239(c) is applicable and to assist the Attorney General in filing her reporting requirements.

5.2 The provisions found in the contractual provisions (Form DA-146a) attached hereto, are hereby incorporated in this contract and made a part hereof. In addition, Counsel shall incorporate the provisions of Form DA-146a into any contract with any third party.

IN WITNESS WHEREOF, the parties have hereunto set their hands the day and year first above written.

THE STATE OF KANSAS

CARLA J. STOVALL
Attorney General of Kansas
Kansas Judicial Center, 2nd Floor
Topeka, Kansas 66612
(913) 296-2215
(913) 296-6296 (fax)

By _____

LEAD NATIONAL COUNSEL

SCRUGGS, MILLETTE, LAWSON
BOZEMAN & DENT, P.A.
734 Delmas Avenue
P.O. Box 1425
Pascagoula, Mississippi 39568-1425
(601) 762-6068
(601) 762-1207 (fax)

By _____

LEAD LOCAL COUNSEL

ENTZ & CHANAY, P.A.
3300 S.W. Van Buren
Topeka, Kansas 66611
(913) 267-5004
(913) 267-7106 (fax)

By _____

LEAD NATIONAL COUNSEL

NESS, MOTLEY, LOADHOLT,
RICHARDSON & POOLE, P.A.
151 Meeting Street, Suite 600
P.O. Box 1137
Charleston, South Carolina 29402
(803) 577-6747

By _____

APPROVED:

John W. Campbell
Sr. Deputy Attorney General

Neil A. Woerman
Director of Budget and Special Projects
Office of the Attorney General

...ment of Administration
...ion of Accounts and Reports
DA-146a (Rev. 7-97)

Agency No. _____ Contract No. _____

CONTRACTUAL PROVISIONS ATTACHMENT

Important: This form contains mandatory contract provisions and must be attached to or incorporated in all copies of any contractual agreement. If it is attached to the vendor/contractor's standard contract form, then that form must be altered to contain the following provision:

"The provisions found in Contractual Provisions Attachment (form DA-146a), which is attached hereto, are hereby incorporated in this contract and made a part hereof".

The parties agree that the following provisions are hereby incorporated into the contract to which it is attached and made a part thereof, said contract being the _____ day of _____, 19_____.

1. TERMS HEREIN CONTROLLING PROVISIONS
It is expressly agreed that the terms of each and every provision in this attachment shall prevail and control over the terms of any other conflicting provision in any other document relating to and a part of the contract in which this attachment is incorporated.

2. AGREEMENT WITH KANSAS LAW
All contractual agreements shall be subject to, governed by, and construed according to the laws of the State of Kansas.

3. TERMINATION DUE TO LACK OF FUNDING APPROPRIATION
If, in the judgment of the Director of Accounts and Reports, Department of Administration, sufficient funds are not appropriated to continue the function performed in this agreement and for the payment of the charges hereunder, State may terminate this agreement at the end of its current fiscal year. State agrees to give written notice of termination to contractor at least 30 days prior to the end of its current fiscal year, and shall give such notice for a greater period prior to the end of such fiscal year as may be provided in this contract, except that such notice shall not be required prior to 90 days before the end of such fiscal year. Contractor shall have the right, at the end of such fiscal year, to take possession of any equipment provided State under the contract. State will pay to the contractor all regular contractual payments incurred through the end of such fiscal year, plus contractual charges incidental to the return of any such equipment. Upon termination of the agreement by State, title to any such equipment shall revert to contractor at the end of State's current fiscal year. The termination of the contract pursuant to this paragraph shall not cause any penalty to be charged to the agency or the contractor.

4. DISCLAIMER OF LIABILITY
Neither the State of Kansas nor any agency thereof shall hold harmless or indemnify any contractor beyond that liability incurred under the Kansas Tort Claims Act (K.S.A. 75-6101 et seq.).

5. ANTI-DISCRIMINATION CLAUSE
The contractor agrees: (a) to comply with the Kansas Act Against Discrimination (K.S.A. 44-1001 et seq.) and the Kansas Age Discrimination in Employment Act (K.S.A. 44-1111 et seq.) and the applicable provisions of the Americans With Disabilities Act (42 U.S.C. 12101 et seq.) (ADA) and to not discriminate against any person because of race, religion, color, sex, disability, national origin or ancestry, or age in the admission or access to, or treatment or employment in, its programs or activities; (b) to include in all solicitations or advertisements for employees, the phrase "equal opportunity employer"; (c) to comply with the reporting requirements set out at K.S.A. 44-1031 and K.S.A. 44-1116; (d) to include those provisions in every subcontract or purchase order so that they are binding upon such subcontractor or vendor; (e) that a failure to comply with the reporting requirements of (c) above or if the contractor is found guilty of any violation of such acts by the Kansas Human Rights Commission, such violation shall constitute a breach of contract; (f) if the contracting agency determines that the contractor has violated applicable provisions of ADA, that violation shall constitute a breach of contract; (g) if (e) or (f) occurs, the contract may be cancelled, terminated or suspended in whole or in part by the State Department of Administration.

Parties to this contract understand that subsections (b) through (e) of this paragraph number 5 are not applicable to a contractor who employs fewer than four employees or whose contracts with this agency of the Kansas state government total $5,000 or less during this fiscal year.

6. ACCEPTANCE OF CONTRACT
This contract shall not be considered accepted, approved or otherwise effective until the statutorily required approvals and certifications have been given.

7. ARBITRATION, DAMAGES, WARRANTIES
Notwithstanding any language to the contrary, no interpretation shall be allowed to find the State or any agency thereof has agreed to binding arbitration, or the payment of damages or penalties upon the occurrence of a contingency. Further, the State of Kansas shall not agree to pay attorney fees and late payment charges beyond those available under the Kansas Prompt Payment Act (K.S.A. 75-6403), and no provision will be given effect which attempts to exclude, modify, disclaim or otherwise attempt to limit implied warranties of merchantability and fitness for a particular purpose.

8. REPRESENTATIVE'S AUTHORITY TO CONTRACT
By signing this document, the representative of the contractor thereby represents that such person is duly authorized by the contractor to execute this document on behalf of the contractor and that the contractor agrees to be bound by the provisions thereof.

9. RESPONSIBILITY FOR TAXES
The State of Kansas shall not be responsible for, nor indemnify a contractor for, any federal, state or local taxes which may be imposed or levied upon the subject matter of this contract.

10. INSURANCE
The State of Kansas shall not be required to purchase, any insurance against loss or damage to any personal property to which this contract relates, nor shall this contract require the State to establish a "self-insurance" fund to protect against any such loss or damage. Subject to the provisions of the Kansas Tort Claims Act (K.S.A. 75-6101 et seq.), the vendor or lessor shall bear the risk of any loss or damage to any personal property in which vendor or lessor holds title.

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5-11

Representation for the Tobacco Lawsuit Was Divided Between a Mississippi Firm, A South Carolina Firm, and a Kansas Firm After Discussions Were Held With Several Other Law Firms

In early Spring 1996, the Attorney General held preliminary discussions with three Kansas law firms about representing the State in tobacco litigation. The lawsuit was to be filed against several national tobacco companies. Those firms were Hutton & Hutton of Wichita, Morrison & Hecker of Kansas City, and Don Barry of Topeka. At the time of those preliminary discussions, it was anticipated the firm selected would handle the entire case, and would be paid on a contingency fee basis if the case were won. The firm selected also would have to finance any up-front legal expenses, which at the time were estimated could run several million dollars.

Two firms withdrew over issues related to expenses, and negotiations with a third firm stalled over the fee arrangement. Two of the firms—Don Barry and Morrison & Hecker withdrew from the negotiations because they didn't want to be responsible for paying the up-front costs of the lawsuit. Throughout the Spring and early Summer of 1996, negotiations with Hutton & Hutton continued. According to the correspondence, the sticking point of those negotiations was a disagreement over the fee amount. The firm wanted the contract to state that fees would be a fixed percent of whatever the State was awarded. (Draft contracts indicated the firm wanted 25%, although the percent was reportedly somewhat negotiable.) The Attorney General's Office wanted the fee to be established by the Court up to a maximum of 25%. The Attorney General's staff indicated the fee a court actually awarded could vary greatly, depending on the size of any damages awarded to the State.

The Attorney General decided to hire Mississippi and South Carolina firms as the lead national counsel on the case. While the negotiations with Hutton & Hutton were continuing, the Attorney General's Office held discussions with a Mississippi law firm—Scruggs, Millette, Lawson, Bozeman & Dent, P.A.—that was representing several other states in tobacco litigation. Ultimately the Attorney General decided to hire Scruggs, et al. and a South Carolina firm—Ness, Motley, Loadholt, Richardson & Poole, P.A.—to jointly serve as national counsel for the lawsuit.

The State still needed to find local counsel capable of providing support to the national firms, and capable of reviewing and providing a repository for the thousands of documents that would be generated by the case. The Attorney General's Office went back to Morrison & Hecker to see if the firm would be interested in serving as local counsel for the lawsuit, with up-front expenses to be negotiated with the national firms. Morrison & Hecker declined, citing the appearance of a conflict of interest. The Attorney General's Office didn't talk with Mr. Barry or with Hutton & Hutton about serving as local counsel.

In June, about a month after she'd heard they were interested in the case, the Attorney General contacted the law firm of Entz & Chanay (her former employer) about the possibility of serving as local counsel. It is unclear when serious negotiations with Hutton & Hutton stopped, but an internal memorandum dated June 28 from the Attorney General to her chief deputy informs him of Entz & Chanay's interest, and refers to the need to back out of arrangements with Hutton & Hutton.

During the summer, Entz & Chanay and Scruggs et al. negotiated terms that called for the two national firms to pay up-front expenses of the case and to receive a contingency fee of up to 12.5%. Entz & Chanay also would receive a contingency fee of up to 12.5%. On August 8, 1996, the Attorney General and the three law firms signed the contract.

State of Kansas
House of Representatives

Susan Wagle

February 4, 2000

The Honorable Carla Stovall
Office the Attorney General
120 SW 10th Ave
Topeka, KS 66612

Dear Attorney General Stovall:

Previously, I requested information from you on behalf of the House Committee on Taxation relating to your actions in hiring a private counsel for the purpose of assisting the state in the pursuit of litigation involving the tobacco industry. I received back from Mr. John W. Campbell, Senior Deputy Attorney General, a letter discussing a post audit investigation, the possibility of future tobacco litigation and the *Kansas v. Colorado* water litigation. In addition, Mr. Campbell referred to information obtained by the Legislative Post Audit Committee under the post audit act. I would emphasize to you that I am not seeking to obtain information under the post audit act (K.S.A. 46-1101 *et seq.*) nor am I interested at this time in information relating to the *Kansas v. Colorado* water litigation. I am making this request pursuant to the Kansas open records act (K.S.A. 45-215 *et seq.*).

Pursuant to the Kansas open records act, I request that you provide to me a copy of the contract entered into by you on behalf of the state of Kansas with the law firm of Entz and Chanay relating to the state tobacco litigation, the names of any other law firms considered by the Attorney General prior to entering into the contract with Entz and Chanay, and all correspondence, memoranda, documents and any other records in any form which relate to hiring private counsel to assist the state in the pursuit of litigation involving the tobacco industry, including all correspondence, memoranda, documents and any other records in any form relating to any negotiation with or consideration of the Entz and Chanay firm or any firm other than the Entz and Chanay firm with regard to this matter. I am also requesting a copy of each billing from the Entz and Chanay law firm pursuant to the contract to which you entered into with this law firm on the tobacco litigation matter.

I wish to make it clear that I am not asking for any kind of confidential or privileged information relating to litigation strategy in the tobacco cases subsequent to the entering into the contract with the law firm of Entz and Chanay. My request for the information is for all records and documents which relate to selecting the law firm of Entz and Chanay to represent the state in the tobacco litigation and which relate to negotiations with other law firms which were not selected.

REPRESENTATIVE, 99TH DISTRICT
BUTLER/SEDGWICK COUNTIES
14 SANDALWOOD
WICHITA, KANSAS 67230

House Taxation
Date 2/15/00
Attachment # 6-1

I would note in passing that prior attorney generals have been very supportive of open public records as the public policy of this state. I would hope that you would continue this support by your cooperation in the matter of my request.

Sincerely,

Representative Susan Wagle

State of Kansas
Office of the Attorney General
120 S.W. 10th Avenue, 2ND FLOOR, TOPEKA, KANSAS 66612-1597

CARLA J. STOVALL
ATTORNEY GENERAL

MAIN PHONE: (785) 296-2215
FAX: 296-6296

February 8, 2000

HAND DELIVERED

The Honorable Susan Wagle
Representative 99th District
Room 170 -W
State Capitol
Topeka, Kansas 66612-1510

RE: Re: HB 2683

Dear Chairperson Wagle:

Please find enclosed the following documents in regard to your request of February 4, 2000, which indclude:

> ". . . all correspondence, memoranda, documents and any other records in any form which relate to the hiring of private counsel to assist the state in the pursuit of litigation involving the tobacco industry including all correspondence, memoranda, documents and any other records in any form relating to any negotiation with or consideration of the Entz and Chanay firm or any firm other than Entz and Chanay firm with regard to this matter."

With the limited exception of those documents that are viewed by those persons not holding employment or office with the State, the government of Kansas has not and will not waive any of its attorney client privileges or the attorney work product privileges in this or subsequent tobacco

House Taxation
Date 2/15/00
Attachment # 7-1

related litigation. No person or entity, be it public or private, should view the distribution of this material as such a waiver under K.S.A. 60-426 or any Kansas, state or federal statute: or any court rule or the common law, federal or state.

Sincerely,

OFFICE OF THE ATTORNEY GENERAL
CARLA J. STOVALL

John W. Campbell
Senior Deputy Attorney General

JWC:dsw
Enclosures

ARBITRATION PANEL
CONVENED UNDER KANSAS COUNSEL
FEE PAYMENT AGREEMENT

IN RE:

ATTORNEYS' FEE APPLICATION BY KANSAS PRIVATE OUTSIDE COUNSEL

OPINION

The Kansas Outside Counsel fee arbitration was heard by the Panel of arbitrators on November 13, 1999 in Houston, Texas. In advance of the hearing, the Panel received written submissions from Kansas Outside Counsel and the Settling Companies. This was the ninth arbitration before the Tobacco Arbitration Panel arbitrators, established to award attorneys' fees to Private Outside Counsel in connection with the settlement of the Attorney General Medicaid cases against the tobacco industry. This arbitration proceeding awards attorneys' fees to Private Outside Counsel for the State of Kansas pursuant to the Master Settlement Agreement ("MSA"). The MSA is the November 1998 global settlement of the Attorneys General litigation involving 46 states and a number of U.S. territories and Participating Tobacco Manufacturers. The State of Kansas' share in the financial proceeds of the MSA will exceed an estimated $1,767,000,000 billion. The Participating Manufacturers also agreed to pay full reasonable attorneys' fees to Counsel representing the sates over and above the settlement proceeds under the MSA. The contract governing this proceeding, the Kansas Fee Payment Agreement, charges the Panel with

the responsibility of awarding Kansas Private Outside Counsel "a full reasonable fee," taking into consideration the 'totality of the circumstances."

There was a contingent fee contract between Kansas Private Outside Counsel and the State of Kansas providing for counsel to be paid attorneys' fees "up to 25%" of the amounts recovered, with that amount being divided between Kansas local counsel and Kansas national counsel "up to 12.5%" each. Kansas National Private Counsel were responsible for all of the out-of-pocket expenses in order to prosecute this case, totaling approximately $1,000,000 or higher."

As we have noted before, each state's application has presented unique questions and there cannot be a cookie-cutter approach to determining the attorneys' fees. Kansas filed suit in August of 1996 and was the eleventh state to file suit. The Attorney General of Kansas was one of the first attorney's general to bring suit who was a member of the Republican party. The entry of Kansas into the litigation fray demonstrated that the litigation was a bipartisan effort and helped to create a "critical mass" for the litigation. Given the political atmosphere in the state of Kansas, it appears that the Kansas Attorney General took a courageous step in commencing litigation against the settling companies. Kansas was actively involved in the negotiations of the Liggett II settlement.

Two Parallel Cases in Kansas:

The main case was filed in August 1996, after the Liggett I Settlement. This main case was stayed most of the time. However, the second case — to enforce the provisions of the Liggett II Settlement — was where all of the court's activity took place. This second case was

also before the same judge as the main case. It is in the second case that the favorable decision on joint defense privilege was obtained.

The new challenge posed for the arbitrators in awarding full, reasonable compensation to Outside Counsel for Kansas is the extent to which Outside Counsel is to be rewarded for pursuing issues related to the applicability of the joint defense privilege to the documents which were to be turned over by Liggett to the states pursuant to the Liggett II settlement. Kansas (the only state to do so) commenced an ancillary suit against Liggett and was successful initially in obtaining a ruling pursuant to Kansas law that no joint defense privilege protected those documents from production. As the Kansas Court stated in one of the hearings in the second case:

> The Court never stayed discovery in the Liggett case. Discovery was stayed in the part of the other case. We're not talking about discovery issues in the Liggett case. The only issue is whether or not these interested defendants are entitled to insert a so-called joint defense privilege and there's, of course, a collateral issue, which is, if they are, has the issue been, — or has the privilege been waived.... And let me say, so that we all understand each other, the issue I want to take up — issues I want to take up are: Does Kansas recognize the so-called joint defense privilege and, if so, has it been waived, given the circumstances in this case?" (*Kansas Tobacco Arbitration hearing, p. 45-46)*

Kansas Outside Counsel asserts that this ruling in Kansas enabled national counsel to convince courts in other states to release the disputed Liggett documents to the states. We must resolve how to reward Kansas Outside Counsel for the work done relating to the privilege issue.

At the hearing, there was conflicting testimony concerning the importance of Kansas Outside Counsels' pursuit of the privilege issue. Outside Counsel argues that Kansas was the only state in which a claim could be made that no joint defense privilege existed and that

the Kansas Outside Counsel opened an additional front of attack on the Settling Companies by pursuing that argument. Outside Counsel argues that their work on the privilege issue served all states by increasing the pressure on the Settling Companies and that the additional pressure was one of the factors which brought the Settling Companies to the bargaining table. Mississippi Attorney General Michael Moore appeared before the Panel and testified, as did National Counsel Scruggs and Rice, that the attack on the joint defense privileges was part of a coordinated national strategy. The industry, in its pleadings in opposing the breaking of the joint defense privilege decision, called the Kansas case "unique." It also admitted the Kansas decision could affect future cases, even though not a single document was turned over to Plaintiffs because of the Kansas decision. However, it could have had a major impact on the national litigation if enforced and hundreds of thousands of documents were eventually turned over.

The Settling Companies, in contrast, argue that the dispute over the privilege issue had no effect on the main case against the Settling Companies. The Settling Companies point out that nothing happened in the litigation against the Settling Companies in Kansas once the suit was filed. There was no ruling on the industry's motion to dismiss, there was no discovery, no expert designations, no depositions and no trial date was set. The Settling Companies further assert that the ruling on the joint defense issue by the trial court clearly was in error and would have been reversed by the Kansas Supreme Court and that, in fact, no documents were ever produced as a result of the Kansas trial court's ruling.

No one will ever know the outcome since as Attorney General Moore testified under cross-examination by the industry lawyers:

Industry Lawyer: Did the states get documents?
Moore: Out of "the Kansas" case?

No, you guys — y'all folded. You settled the case. You must have given up...."[1]

---

1. While no documents were actually produced into the court records in Kansas or elsewhere by the time of the MSA, Kansas local counsel was probably the first Plaintiffs' counsel to review the 2,500 Liggett-only privileged documents which were physically delivered to the Kansas courthouse pursuant to the second Kansas case. Kansas' local counsel then sent memoranda of what he had reviewed to other Plaintiffs' counsel even though he could not send copies of the documents he had revealed. Kansas' local counsel testified at the hearing:

> To the best of our knowledge, I am the first person outside the tobacco industry to ever view those documents. I personally read every single page of those documents and generated five reports regarding what those documents revealed.... Among the distinct projects that Kansas' local counsel worked on through its document review was we charted the relationship between the tobacco industry lawyers and outside company operations. We charted the work of the Tobacco Institute and its Committee of Council. We charted the Liggett's so-called safer cigarette research, and we charted the attorney-controlled funds that financed the operation of the Council for Tobacco Research.
>
> The quality and value of these Liggett only privileged documents was so impressive that Kansas counsel determined that the release of the remaining documents filed under seal was of critical importance. ... Yet, rather than starting from the premise that these documents were protected under the joint defense privilege and that the documents were discoverable only after a document-by-document crime-fraud review, we started a detailed study of whether the joint defense privilege could even be asserted at all in our state.
>
> After intensive research into the question, we reached the conclusion that the joint defense privilege does not exist in Kansas. We asserted this never-before-litigated theory in connection with a motion to have all documents that were filed under seal released to Kansas' counsel through the enforcing of the Liggett II Settlement. Although the specific challenge would reach only the 2,500 documents that remained under seal, the potential impact could have affected a pool of nearly 680,000 documents that were present in the underlying litigation. Thus, while the first case was under a discovery stay, we were laying the groundwork for the wholesale release of the industry's most sensitive secrets.

(Kansas Tobacco Arbitration hearing, pp. 82-84)

One of the criteria in determining a full, reasonable fee award is the element of risk. If "risk" is the most important criteria, the political risk and the legal risk at the time Outside Counsel was engaged was very high and the industry offered no evidence to the contrary. Attorney Generals Stovall of Kansas and Moore of Mississippi, and national counsel Scruggs, said the risk was substantial and that filing of Kansas' lawsuit was a risky and courageous thing to do. Attorney Generals Stovall and Moore, and National Counsel testified to the importance of bringing in Kansas, a Republican state, into the tobacco fray, particularly with GOP presidential nominee and Kansas native Senator Dole, who had made public comments expressing skepticism about the dangers of tobacco.

Looking at a lodestar as a starting point, Kansas counsel did not provide an estimate or an accounting of hours worked on the cases. This failure hampered the deliberations of the Panel. The industry estimated that there were 10,000 hours worked on the Kansas cases, and Kansas counsel estimated that this was a low number of hours actually worked. The role of National Counsel in this state was very prominent and active. Attorney General Moore and National Counsel Scruggs sought out Kansas, and National Counsel Ness Motley was instrumental in providing counsel and monetary support for the Kansas effort. Local counsel did not have any out-of-pocket expenses, for example, and were a small 4-5 person law firm selected by Kansas AG Stovall after several Kansas counsel refused to take the case. National Counsel Rice, however, testified that there was more work spent by National Counsel in Kansas than in several other states. That does not take away the effort or contribution of the Kansas case, as the appearance and testimony of AG Moore, National Counsel Scruggs and Rice at the Kansas hearing will illustrate. It does, however, clarify that National Counsel provided most of the personnel power and resources for the Kansas effort.

In addition, National Counsel, played a key role in the negotiations which led to the June 20 Agreement. In these circumstances, we believe that it is appropriate to reward Outside Counsel principally for the work that was done on the national scene with a much smaller portion of the fee award being based on the work that both national and local counsel actually did in the Kansas action.

In arriving at this decision, the undersigned analyzed the role of Outside Counsel, using the factors listed in the Johnson case. The Johnson factors are identical to the criteria used by the ABA and virtually every court when called upon to determine fees to be awarded in all manner of cases. Given our prior discussions of those factors, we do not feel it would be useful to set out an extended discussion of those factors or the weight given those factors.

The undersigned have reviewed the totality of the circumstances utilizing those factors set out in Johnson and in the ABA ethics rules in consideration of what fees should be awarded to Kansas Outside Counsel.

As noted above, it was estimated that Kansas private counsel — not including National Counsel — spent a minimum of 10,000 hours working on the case. Applying a generous hourly rate in Kansas, and applying a modest multiplier to this amount, the Panel began with this analysis. It also took into consideration the fact that there was a contingency fee contract validly entered into, and negotiated at arms' length, but that such contingent fee contract provided only maximums, *i.e.*, "up to 25%." To the lodestar calculation was added a substantial amount for the compensation of the work done by National Kansas Counsel, utilizing a percentage calculation to arrive at a number.

Utilizing all of these factors, the Panel took into account the totality of the circumstances, including the lodestar calculation and a reasonable percentage for national counsel, in the setting of full, fair reasonable compensation.

The Panel thus concludes and awards a fee of $54,000,000 as full, fair reasonable compensation for Kansas outside private counsel.

S/_____
John Calhoun Wells, Chairman

S/_____
Hon. Charles B. Renfrew

S/_____
Harry Huge, Esq.

Dated: January __, 2000.

Contact:
Eric Berman
Kekst and Company
212-521-4894

FOR IMMEDIATE RELEASE

TOBACCO FEE ARBITRATION PANEL ANNOUNCES UNANIMOUS KANSAS DECISION

NEW YORK, January 31, 2000 – The Tobacco Fee Arbitration Panel announced today a unanimous decision regarding attorneys' fees for outside counsel retained by the State of Kansas in the 1998 state tobacco litigation settlement.

In this case, the Panel determined that full, reasonable compensation for these attorneys is $54,000,000.

These fees, which will be paid by the tobacco companies, are separate from – and in addition to – the $1.767 billion financial recovery Kansas will receive through its settlement with the tobacco industry over the next 25 years, and additional payments in perpetuity.

The Kansas State Fee Payment Agreement specifically granted the Panel the authority to award a fee either lower or higher than the contract stipulates. The Panel's findings are final and not appealable by any party.

The arbitrators for the Kansas case included the Panel's two permanent members – Dr. John Calhoun Wells, the Panel's chairman, and former U.S. District Court Judge Charles Renfrew, the industry-appointed member – and Harry Huge, Esq., the Kansas counsel-appointed member. Dr. Wells is the consensus selection of both parties and is permanent chairman.

During its consideration of the Kansas application, the Panel conducted a hearing in Houston, TX on November 13, 1999. Both parties also presented written submissions to the arbitrators.

The Panel has previously announced fee determinations for attorneys representing the states of Florida, Texas, Mississippi, Massachusetts, Hawaii, Illinois and Iowa. It is also announcing a determination today for attorneys representing the state of Louisiana. The Panel will continue its work for those states choosing to enter the arbitration process. To date, some states have opted not to enter arbitration and have reached separate agreements with the industry on attorneys' fees.

###

8-10

Kekst & Company

437 Madison Avenue, 19th Floor
New York, New York 10022
212-521-4800
Fax: 212-521-4900

FAX TRANSMISSION COVER SHEET

To:	*Attorney General Stovall – URGENT*
Firm:	*Office of the Attorney General*
Sender:	*Eric Berman*
Fax:	*785-296-6296*
Phone:	*785-296-3751*
Date:	*January 31, 2000*

YOU SHOULD RECEIVE __ PAGE(S), INCLUDING THIS COVER SHEET. IF YOU DO NOT RECEIVE ALL THE PAGES, PLEASE CALL 212-521-4894

State of Kansas
Office of the Attorney General
301 S.W. 10TH AVENUE, TOPEKA 66612-1597

CARLA J. STOVALL
ATTORNEY GENERAL

MAIN PHONE: (913) 296-2215
CONSUMER PROTECTION: 296-3751
FAX: 296-6296

Q & A

1. Why is Attorney General Carla Stovall filing suit against the tobacco industry?

No person or company is above the law, including the tobacco industry. We are filing suit because the tobacco industry has engaged in unlawful conduct, including negligence, civil conspiracy, and deceptive consumer practices, and has violated state antitrust laws. As a direct result of these violations, their products have killed more Kansans than AIDS, homicide, suicide, automobile accidents, and alcohol and drug abuse combined. Each year more than 4,000 Kansans die from tobacco-related causes.

The tobacco industry has addicted its customers by manipulating nicotine impact levels in its tobacco products. The industry's products slowly kill its customers, and then the industry targets children through advertising to recruit a new bumper crop of life-long smokers. No Kansan is spared from the costs associated with smoking-related illnesses. It's time the tobacco industry reimburses the taxpayers for its deceit and conspiracy. It's time for the industry be held accountable for its conduct.

2. What is the state seeking in the lawsuit?

The suit aims to end the industry's practice of directing advertising toward children. It also seeks to recover the many millions that Kansas taxpayers have had to pay in taxes to treat sick and dying indigent Kansans. These patients are covered by Medicaid and other taxpayer-financed health care programs. Who should pay for their treatment: innocent taxpayers or the manufacturers of the product that is killing them? The suit also seeks to prohibit the defendants' unlawful business activities.

3. What is the basis of the lawsuit?

The suit alleges that the tobacco industry misrepresented and suppressed important information in their conspiracy to sell unsafe products. It further alleges that the companies

misled Kansans about the adverse health effects of tobacco, while conspiring to keep safer, alternative products off the market. The tobacco industry has also addicted its customers by manipulating nicotine impact levels in its cigarettes, and has callously targeted children in its advertising. Because of this conspiracy, Kansas taxpayers have borne the burden of increased health costs under Medicaid and other taxpayer-funded programs.

4. Why aren't the Attorney General's staff attorneys handling this case?

Our attorneys will have a substantial role in this litigation, as in any other case this office prosecutes. However, to prosecute a case of this magnitude against a multi billion dollar industry, it will cost millions of dollars up front in legal expenses. Every state which has filed similar litigation against the industry has contracted with outside attorneys. By utilizing, on a contingency fee basis, lawyers experienced in this type of litigation, the state puts itself in the optimum position. If the state prevails in court, it will recover its Medicaid costs plus additional damages. If the lawsuit fails, then the state suffers no monetary loss.

If the state is successful, the outside attorneys will receive no more than 25 percent of the award, which is lower than the typical contingency fee percentage of 33 percent - 40 percent. All attorneys fees in this case are subject to review by the Court for approval and reasonableness.

5. If Kansas wins this lawsuit, how will the people of Kansas benefit?

Money that is annually drained from taxpayer pockets to pay for the medical treatment caused by the tobacco industry will be paid by the perpetrators themselves. The state is asking for damages in the same amount as Kansas taxpayers have paid in smoking-related Medicaid claims over the past decades. That amount has not yet been determined but is in the millions of dollars. A substantial portion of the money will go back into the state general fund for distribution by the Kansas Legislature.

6. But don't the tobacco companies indirectly pay for government health care programs through the assessment of taxes on tobacco products?

The truth is that tobacco companies themselves pay very little in state taxes. Distributors pay the bulk of state excise taxes, which are passed on to consumers. Consumers also pay state sales taxes for cigarettes, not tobacco companies. The amount of revenue generated by these sales and excise taxes are only a small fraction of the dollar value of the harm caused by the tobacco industry.

7. Why is the Attorney General just suing the tobacco industry? Aren't there other unsafe consumer products on the market?

The use of tobacco is unique. It is the only product which, if used as the manufacturer intends, will eventually cause mass addiction, disease and death. Plus, the essence of the state's suit is that the tobacco companies conspired in violation of Kansas laws.

8. Is this an anti-business lawsuit?

Absolutely not. Any business that violates the law in Kansas will be prosecuted. Legitimate businesses should support this action. They make up the majority of our economy, but suffer along with consumers when there is deceit and conspiracy committed by members of the business community. Also, business unfairly bears the brunt of many tobacco-related illnesses through increased health insurance premiums.

9. Would you settle this lawsuit? If so, for how much?

We have filed suit to hold the tobacco industry accountable. We are not interested in settlements that do not provide substantial relief to Kansas citizens. It's time for the industry to come clean and meet its responsibility. If a proposed settlement meets our goals and serves the best interests of Kansas, then I would certainly consider it.

10. Are you trying to put the tobacco companies out of business?

Not at all. But no business is above the law. If the industry were to conduct business in a legal manner, then there would be no need for litigation. Unfortunately, that has not been the case. As Attorney General, I will enforce the law against any person or entity that violates it.

11. What effect, if any, will the settlement by the Liggett Group have on your lawsuit?

The Liggett Group settlement represents the recognition by the tobacco industry of its culpability. Up until this settlement, the industry was fond of bragging that it had never paid a dime in damages. That empty statement no longer applies. The wind is shifting -- it's time the industry paid for its illegal actions. We will begin immediately to negotiate with the Liggett Group to have the terms of the original settlement apply to Kansas. If these negotiations are unsuccessful, Liggett will be added as a defendant in this case.

12. Isn't it true that the tobacco industry has never lost a lawsuit?

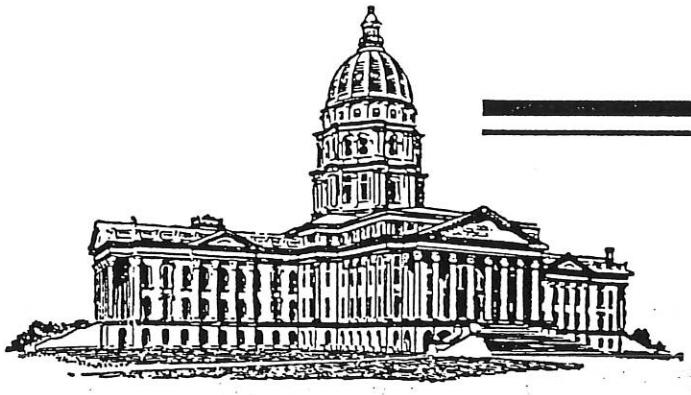
No. The industry has been successful in individual smoker cases, but with some exceptions. For example, in *Cipollone v. Liggett Group, Inc.*, a New Jersey jury awarded the widower of a smoker $400,000. On appeal, however, the tobacco industry managed to overturn the damages. The U.S. Supreme Court ruled in 1992 that the husband had the authority to sue the tobacco industry and sent the case back to the trial court. According to some estimates, the industry spent $75 million to fight this case As a result, the widower did not have the resources to proceed with the litigation.

Just two weeks ago, a Florida jury in *Carter v. Brown & Williamson Tobacco Corp.* awarded a smoker $750,000 in damages based upon some of the same legal theories that the State of Kansas is pursuing in this litigation. The tide is clearly turning against the tobacco industry.

13. How did you choose counsel for the State of Kansas?

We have sought the assistance of both local and national counsel in this lawsuit. Entz & Chanay, P.A., Attorney General Stovall's former law firm, was chosen because it is a leading expert on Medicaid reimbursement and holds Attorney General Stovall's utmost trust in protecting the interests of Kansas taxpayers. The law firms of Scruggs, Millette, Lawson, Bozeman & Dent, P.A. of Pascagoula, Mississippi, and Ness, Motley, Loadholt, Richardson & Poole, P.A. of Charleston, South Carolina, were chosen because they are national leaders in state-sponsored Medicaid recoupment litigation against the tobacco industry.

-30-



PERFORMANCE AUDIT REPORT

Reviewing the Attorney General's Expenditures For Water Rights Litigation and Procedures For Selecting Attorneys

A Report to the Legislative Post Audit Committee
By the Legislative Division of Post Audit
State of Kansas
October 1997

97-59

Legislative Post Audit Committee

Legislative Division of Post Audit

THE LEGISLATIVE POST Audit Committee and its audit agency, the Legislative Division of Post Audit, are the audit arm of Kansas government. The programs and activities of State government now cost about $8 billion a year. As legislators and administrators try increasingly to allocate tax dollars effectively and make government work more efficiently, they need information to evaluate the work of governmental agencies. The audit work performed by Legislative Post Audit helps provide that information.

We conduct our audit work in accordance with applicable government auditing standards set forth by the U.S. General Accounting Office. These standards pertain to the auditor's professional qualifications, the quality of the audit work, and the characteristics of professional and meaningful reports. The standards also have been endorsed by the American Institute of Certified Public Accountants and adopted by the Legislative Post Audit Committee.

The Legislative Post Audit Committee is a bipartisan committee comprising five senators and five representatives. Of the Senate members, three are appointed by the President of the Senate and two are appointed by the Senate Minority Leader. Of the Representatives, three are appointed by the Speaker of the House and two are appointed by the Minority Leader.

Audits are performed at the direction of the Legislative Post Audit Committee. Legislators or committees should make their requests for performance audits through the Chairman or any other member of the Committee. Copies of all completed performance audits are available from the Division's office.

LEGISLATIVE POST AUDIT COMMITTEE

Representative Eugene Shore, Chair
Representative Richard Alldritt
Representative Doug Mays
Representative Ed McKechnie
Representative Dennis Wilson

Senator Lana Oleen, Vice-Chair
Senator Anthony Hensley
Senator Pat Ranson
Senator Chris Steineger
Senator Ben Vidricksen

LEGISLATIVE DIVISION OF POST AUDIT

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The Legislative Division of Post Audit supports full access to the services of State government for all citizens. Upon request, Legislative Post Audit can provide its audit reports in large print, audio, or other appropriate alternative format to accommodate persons with visual impairments. Persons with hearing or speech disabilities may reach us through the Kansas Relay Center at 1-800-766-3777. Our office hours are 8:00 a.m. to 5:00 p.m., Monday through Friday.

LEGISLATURE OF KANSAS
LEGISLATIVE DIVISION OF POST AUDIT

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September 30, 1997

To: Members, Legislative Post Audit Committee

Representative Eugene Shore, Chair
Representative Richard Alldritt
Representative Doug Mays
Representative Ed McKechnie
Representative Dennis Wilson

Senator Lana Oleen, Vice-Chair
Senator Anthony Hensley
Senator Pat Ranson
Senator Chris Steineger
Senator Ben Vidricksen

This report contains the findings, conclusions, and recommendations from our completed performance audit, *Reviewing the Attorney General's Expenditures for Water Rights Litigation and Procedures for Selecting Attorneys.*

The report also contains appendices showing amounts paid to specific outside attorneys and experts involved with the water rights litigation, and providing information about all contracts with outside attorneys approved by Attorney General Stovall since she took office in January 1995.

This report includes recommendations for modifying the process for selecting outside attorneys. We would be happy to discuss these recommendations or any other items in the report with any legislative committees, individual legislators, or other State officials.

Barbara J. Hinton

Barbara J. Hinton
Legislative Post Auditor

10-3

EXECUTIVE SUMMARY

LEGISLATIVE DIVISION OF POST AUDIT

Question 1: How Much Money Has the Attorney General's Office Spent To Date on Water Rights Litigation With the State of Colorado, and Have Those Payments Covered the Full Cost of the Litigation?

In fiscal years 1984 through 1997, the Attorney General's Office spent more than $12 million on the *Kansas v. Colorado* lawsuit. *Payments to attorneys and water experts who are not State employees have accounted for 87% of the money spent. Outside experts have been paid more than $5.9 million, and outside attorneys have been paid more than $4.5 million. Experts include hydrologists, computer modeling experts, historians, economists, and specialists in crop requirements. The available cost data don't include salary costs of State employees who've done work related to the lawsuit. We estimated those costs exceeded $100,000 for the past two years combined and could be several times that over the life of the lawsuit.*

..... page 3

Much of the lawsuit was funded through supplemental appropriations because of the difficulty in predicting costs in advance. *Because of the extremely technical nature of the lawsuit and difficulties in predicting lawsuit activities and developments a year in advance, in recent years the Governor and Legislature have decided to fund significant portions of the cost through the supplemental appropriation process, when more accurate lawsuit budget projections were available. To pay bills when they came due, the Attorney General's Office has spent about $1.6 million that was originally in accounts other than the one designated for water rights litigation moneys, but much of that money was replaced after the Office received supplemental appropriations.*

..... page 6

The Attorney General's Office estimates it could take up to four years and $3 million to finish the lawsuit with Colorado, excluding post-judgment monitoring costs. *The costs for monitoring Colorado's compliance with the Supreme Court's eventual decision in this case will depend on the Court's ruling as to how Colorado's future compliance is to be determined. Any moneys received from Colorado as a result of the lawsuit are to be distributed according to a complex formula enacted by the 1996 Legislature. The Attorney General will ask the Legislature to decide whether to file a similar lawsuit against Nebraska over waters in the Republican River, which could cost as much as $20 million. Litigation over the Missouri River is also possible but isn't being planned.*

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The 98% increase in the Attorney General's budget from fiscal year 1995 to 1998 was caused mostly by increases in federal grant programs for victims. *Of the increase, 68% came from federal grant funds. The federally mandated Medicaid Fraud and Abuse Division, which also is funded mostly by federal dollars, accounted for 10% of the increase. Costs related to the water rights litigation account for only 6% of the increase.*

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Question 2: What Contractual Agreements Has The Attorney General's Office Made With Private Attorneys?

Most of the Attorney General's contracts with private attorneys were awarded because conflicts of interest prevented the Office from handling particular cases. *About 42% of the cases were contracted out because the Attorney General's staff has a conflict of interest and couldn't represent one of the parties. About 31% were contracted to take advantage of an attorney's or firm's expertise. Occasionally an agency head or agency counsel will request a specific private attorney; the Attorney General typically honors those requests.*

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The Attorney General's Office uses a standard contract for nearly all the cases involving outside counsel. Most have fixed fees and a maximum amount that can be paid under the contract. The standard rate of pay is $85 per hour. The contracts clearly specify what out-of-pocket expenses can be charged to the State. The contracts also state that outside counsel must get approval from the Attorney General's Office to hire experts for the case. We noted that about one-third of the contracts we looked at were amended one or more times to increase the maximum payable.

The Attorney General's contract with law firms representing Kansas in the tobacco litigation could become moot if Congress approves a national settlement with the tobacco companies. The three firms—two national law firms and a local law firm—took the contract on a contingency basis. That contract requires the national firms to pay all up-front expenses and gives the three firms a combined 25% maximum of any amount recovered on the State's behalf.

The Attorney General has a new billing review system that should help ensure the State pays outside counsel only for reasonable costs. *New billing guidelines were adopted for fiscal year 1998. Under these guidelines, for example, a firm will be paid for only one attorney attending a deposition and won't be paid for basic legal research. Outside attorneys electronically submit their bills to Examen, Inc., a California billing review firm. The Office will determine next Spring whether the guidelines save money for the State.*

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There's little consistency in the contractual arrangements State agencies make with outside attorneys. *In their contracts with outside attorneys, State agencies use a wide variety of provisions, depending on their legal needs. Other agencies' contracts for outside counsel vary as to the reasons outside counsel is hired, the rate of pay, whether the contract includes a cap, whether a primary attorney is specified, and whether the outside attorney is allowed to hire experts. We didn't see anything to indicate that the rates or other contractual provisions contained in the Attorney General's contracts were out of line.*

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Question 3: Does the Attorney General's Office Follow Adequate Procedures To Prevent Potential Conflicts of Interest When it Hires Private Attorneys and Law Firms?

The Office has no written procedures for awarding contracts; the Attorney General selects which outside counsel to contract with based on the recommendations of the deputy. *The Senior Deputy Attorney General recommends an attorney or firm based on factors including whether the attorney or firm has successfully worked with the Attorney General's Office in the past, has skill in an area particularly relevant to the case, and whether the quality of the work is known by someone in the Office.* ..... page 19

We looked specifically at the selection process for attorneys for the water rights litigation and for the tobacco lawsuit. The first lead attorney on Kansas v. Colorado *was chosen after a search within Kansas by the Attorney General's Office and outside the State by the chief engineering firm for the case. His successor had been assisting with the case and was the obvious choice because of the successor's experience and strong credentials. For the tobacco lawsuit, the Attorney General held preliminary discussions with three Kansas firms. The Office hired a firm from Mississippi and a firm from South Carolina as joint national counsel and the Attorney General's former law firm as local counsel.*

We didn't find any violations of the State's conflict-of-interest laws for cases contracted to outside counsel. *Kansas conflict-of-interest laws prohibit State offices and employees from contracting on the State's behalf with firms they or their immediate family members own or have a substantial interest in. According to forms they submit annually to the Commission on Governmental Standards and Conduct, neither the Attorney General nor her Senior Deputy owns or has a substantial interest in any private law firm.* ..... page 22

Some contracts were awarded to former associates and to campaign contributors. One contract was awarded to the Attorney General's former law firm, and five were awarded to former staff members of the Attorney General's Office, for appropriate reasons. About two-thirds of the firms that received contracts had contributed to the Attorney General's 1994 campaign. Half of those firms also had contributed to her opponent, and many more firms and attorneys made contributions than were awarded contracts.

For cases that need to be contracted, some State agencies have adopted procedures that can help minimize the appearance of favoritism and increase the pool of interested and qualified attorneys. *Several agencies maintain lists of qualified attorneys that are interested in being considered for outside contracts. Some have adopted approaches to contracting that allow the work to be rotated among interested attorneys.* ..... page 23

For specialized cases, other agencies generally follow the same practices as the Attorney General's Office in selecting outside counsel. *Officials from other agencies said that they, like the Attorney General and her staff, identify qualified outside counsel for cases requiring* ..... page 24

special expertise by talking with colleagues, law schools, and other professionals in the field and then hire based on interviews and professional judgment.

The Attorney General's Office could do more, for major cases, to ensure that it identifies and considers a broad pool of qualified firms and that it documents the rationale for selecting outside counsel. Although it appeared that for the water rights case and for the tobacco litigation that the Office made efforts to identify or advertise for, interview, compare, and select firms staff thought could do the best job for the State, it has no systematic procedures for doing so.

This audit was conducted by Cindy Lash, Jill Shelley, and Alice Alexander. If you need any additional information about the audit's findings, please contact Ms. Lash at the Division's offices. Our address is: Legislative Division of Post Audit, 800 SW Jackson Street, Suite 1200, Topeka, Kansas 66612. You also may call (785) 296-3792, or contact us via the Internet at: **LPA@mail.ksleg.state.ks.us.**

Reviewing the Attorney General's Expenditures for Water Rights Litigation and Procedures for Selecting Attorneys

Since the beginning of the century, there has been an ongoing controversy between Kansas and Colorado with regard to the use of water from the Arkansas River. In 1985, then-Attorney General Stephan filed suit, alleging Colorado had violated the Arkansas River Compact (an agreement formed to protect each state's rights to water in the river.)

The current lawsuit originally sought a decree commanding that the waters of the Arkansas River be delivered in accordance with the provisions of the Compact. However, in 1987, the U.S. Supreme Court ruled that monetary damages could be recovered in water compact enforcement cases. Then-Attorney General Robert Stephan filed a motion to amend the State's complaint and was allowed to include monetary damages.

In 1995, the Supreme Court upheld the finding that Kansas should prevail in the lawsuit on the liability issue. In September 1997, the Special Master appointed by the Supreme Court issued a report that concluded Kansas should be allowed to seek damages for depletions of 420,000 acre-feet of water. This is an estimate of the additional amount of water that would have passed into Kansas at the State line, had Colorado complied with conditions of the Compact from 1950 to 1994.

The Supreme Court will hear arguments on this issue (the amount of water lost to Kansas) in early 1998. The final stage of the lawsuit will be to determine whether Colorado repays the judgment in water, money, or some combination of the two, and whether Colorado also is liable for prejudgment interest on the amount to be repaid.

Recently legislators have raised questions about the amount of money being spent on the lawsuit, who is being paid to perform work for the litigation, and how that work is being funded. Specifically, legislators are concerned that the Attorney General is using operating moneys to fund the lawsuit, thereby creating the need to come back to the Legislature with supplemental requests for operating moneys.

In addition, concerns have been raised about what types of contractual agreements the Attorney General's Office has with private law firms it contracts with for representation, particularly with regard to litigation against the tobacco companies. Finally, questions have been raised about whether the Attorney General's Office takes adequate steps to prevent the appearance of favoritism in its selection of private attorneys and law firms to represent the State. To address these concerns, this audit answers the following questions:

1. **How much money has the Attorney General's Office spent to-date on water rights litigation with the State of Colorado, and have those payments covered the full cost of the litigation?**

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2. **What contractual agreements has the Attorney General's Office made with private attorneys?**

3. **Does the Attorney General's Office follow adequate procedures to prevent potential conflicts of interest when it hires private attorneys and law firms?**

To answer these questions, we reviewed and analyzed appropriations, budgets and payment vouchers for water rights litigation, and interviewed officials in the Attorney General's Office and the Division of Water Resources about the history of the lawsuit. We also reviewed the entire agency budget for 1995 through 1998 to see what factors have caused the budget to increase so dramatically in recent years.

We reviewed all contracts with outside attorneys entered into since January 1995, when Attorney General Stovall took office, to identify reasons for contracting and the types of conditions included in the contracts. We also talked with several other State agencies about the types of contractual arrangements they make with outside attorneys. Finally, we looked at the Attorney General's process for selecting outside attorneys, reviewed campaign contributions by attorneys who received contracts from the Office and by those who didn't, and talked with other State agencies about how they select outside attorneys.

In conducting this audit, we followed all applicable government auditing standards. One of the standards states that individual auditors should be free from impairments to independence, and should maintain an independent attitude and appearance. Although staff of the Attorney General's Office have acted as legal counsel for the Division of Post Audit on several occasions, we are confident that no impairments to independence occurred.

How Much Money Has the Attorney General's Office Spent To-Date On Water Rights Litigation with the State of Colorado, and Have Those Payments Covered the Full Cost of the Litigation?

Since fiscal year 1984, the Attorney General's Office has spent slightly more than $12 million on *Kansas v. Colorado*. That amount doesn't include significant amounts of salary and benefit costs of State employees who also worked on the lawsuit. In the past two years alone, we estimate those costs have exceeded $100,000. Nearly 50% of the total amount spent on the lawsuit has been paid to experts such as hydrologists, computer modeling specialists, historians, and economists, while 38% has been for fees and expenses of outside attorneys. Budgeting for the lawsuit has been difficult because of uncertainty about how quickly the trial would progress and what resources would be needed. In recent years, the Governor and the Legislature have chosen to fund part of the lawsuit through supplemental appropriations as the costs became more clearly known. In addition, moneys from other agency funds were transferred or used directly from other accounts in five years when expenses exceeded the amount immediately available. The Attorney General estimates it will take several years and $3 million to finish the lawsuit.

In Fiscal Years 1984 Through 1997, The Attorney General's Office Spent More Than $12 Million on the *Kansas v. Colorado* Lawsuit

Kansas v. Colorado, filed in 1985, alleges that Colorado has violated the Arkansas River Compact. The Legislature has appropriated money since fiscal year 1984 to prepare for and present this lawsuit. The graphic on page 4 provides a brief history of events leading up to the lawsuit and shows major events in the case from fiscal year 1984 to the present. The bottom of the graphic also shows cumulative expenditures for the lawsuit since fiscal year 1984.

The table at the top of page 5 shows annual expenditures the Attorney General has reported for the water rights litigation. We checked those expenditures and found them to be accurate.

Payments to outside attorneys and water experts have accounted for 87% of the money spent on the lawsuit to-date. As the table shows, from fiscal year 1983 through fiscal year 1997 outside attorneys had been paid a total of approximately $4.5 million. Two lead attorneys have handled this case over time. The first was Richard Simms, who was with the firm of Hinkle, Cox, Eaton, Coffield & Hensley when he was initially hired; later he and a partner formed Simms & Stein. Mr. Simms was hired by then-Attorney General Stephan in July 1984, and he resigned in a disagreement over funding for the case in 1991. He was succeeded by John Draper of Montgomery & Andrews, who continues as lead attorney. Both of these water rights litigation experts are based in Santa Fe, New Mexico.

These lead attorneys are allowed by contract to hire necessary experts—hydrologists, computer modeling experts, historians, economists, specialists in crop re-

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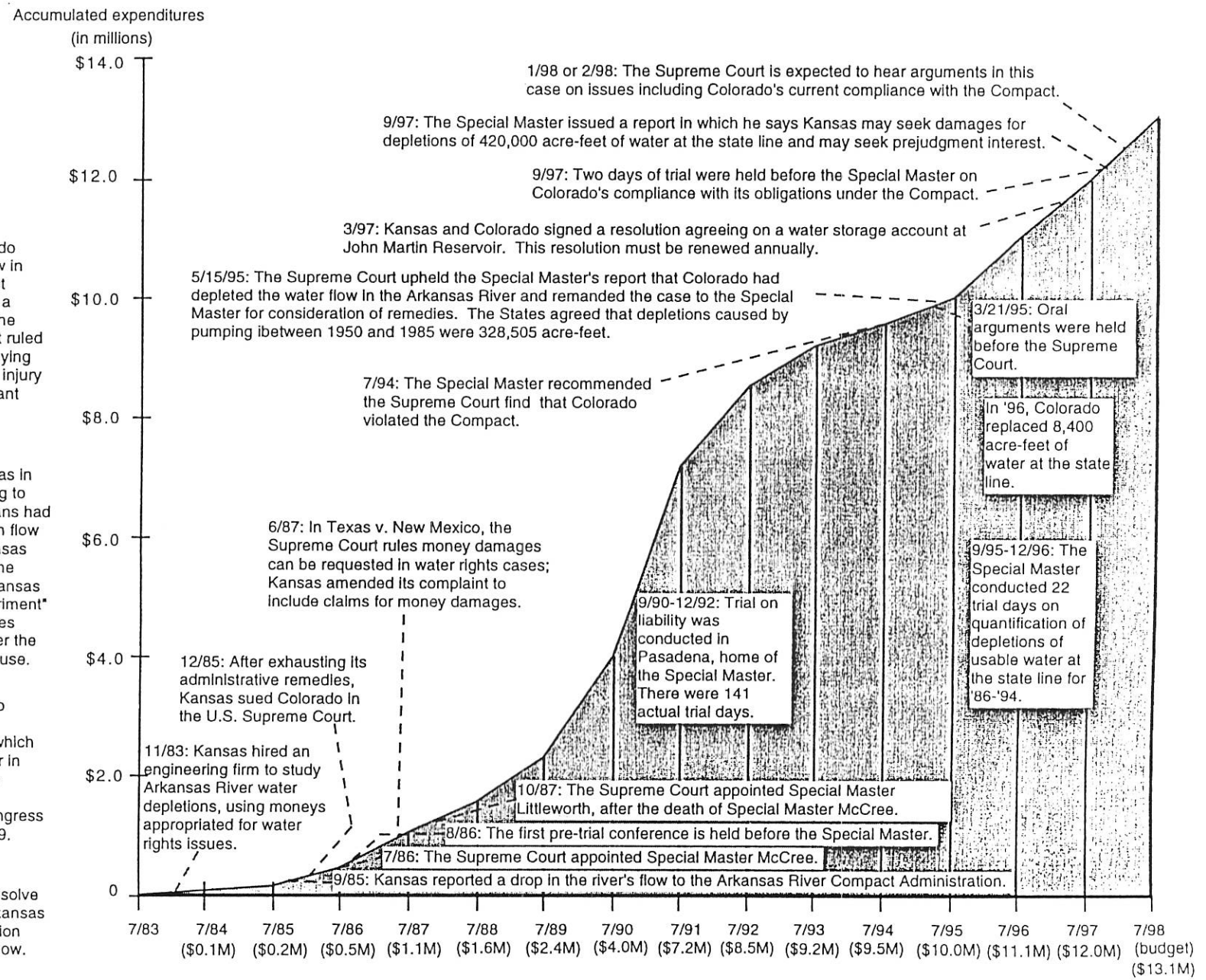
Major events in and cumulative expenditures for *Kansas v. Colorado*
Fiscal Years 1984-1997



1901: Kansas sued Colorado over decreased stream flow in the Arkansas River, the first interstate controversy over a stream to be accepted by the Supreme Court. The Court ruled against Kansas in 1907, saying Kansas had failed to prove injury substantial enough to warrant disruption of the upstream economy.

1928: Colorado sued Kansas in the Supreme Court, seeking to stop lawsuits private Kansans had filed over decreased stream flow in the Arkansas River. Kansas counterclaimed. In 1943, the Supreme Court held that Kansas failed to prove "serious detriment" and recommended the states settle their differences under the Constitution's Compact Clause.

1948: Kansas and Colorado representatives signed the Arkansas River Compact, which equitably apportioned water in the Arkansas River and the benefits of the John Martin Reservoir in Colorado. Congress ratified the Compact in 1949.

1982: Kansans asked the Attorney General to help resolve disagreements with the Arkansas River Compact Administration over depletions of stream flow.

Kansas v. Colorado Expenses

Fiscal Year	Attorney fees & expenses *($ paid to outside expert attorneys)*	Expert fees & expenses *($ paid to outside hydrologists, economists, geologists, historians, etc.)*	State expenses *($ paid for State employee travel, special studies, etc.)*	Special Master fees *(Kansas' share of fees for the Special Master)*	Other expenses *($ paid for hotel costs, equipment rental, etc.)*	TOTAL
1984		$55,100	$40,932			$96,032
1985	$38,000	$32,424				$70,424
1986	$140,369	$139,653	$1,302			$281,324
1987	$82,449	$564,853	$4,147			$651,449
1988	$98,281	$332,327	$4,492	$40,385	$35,560	$511,045
1989	$391,640	$346,159	$6,499		$2,192	$746,490
1990	$792,110	$817,140	$6,562	$40,000		$1,655,812
1991	$1,254,948	$1,241,601	$33,998	$240,000	$442,528	$3,213,075
1992	$398,861	$758,819	$15,722	$60,000	$80,541	$1,313,943
1993	$242,482	$307,925	$37,613	$60,876	$6,164	$655,060
1994	$168,203	$92,685	$1,473	$90,000	$2,096	$354,457
1995	$227,813	$200,957	$14,058	$60,000	$3,422	$506,250
1996	$347,615	$606,807	$17,067	$50,000	$21,199	$1,042,688
1997	$325,035	$471,676	$20,637	$75,000	$29,452	$921,800
TOTAL	$4,507,806	$5,968,126	$204,502	$716,261	$623,154	$12,019,849

quirements, and the like— and to bill the State for those costs. The table shows that outside experts had been paid more than $5.9 million through fiscal year 1997. Major experts the lead attorneys have hired include the following:

- Spronk Water Engineers—serves as Kansas' main consultant and provides expert witness testimony. Spronk, with expertise in Colorado water rights and knowledge about irrigation in the Arkansas River valley, was responsible for data collection and analysis.
- Hydrologic Consultants, Inc.—provides hydrologic modeling, consulting, and expert testimony. (The model was used to determine how much water Colorado had withheld and may continue to be withholding.)
- S.S. Papadopulos & Associates—provides hydrologic modeling, consulting, and expert testimony.

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Records weren't available to determine the exact amount paid to each firm before fiscal year 1991. However, a breakdown of amounts paid to each of the major experts employed on this case in fiscal years 1991 through 1997 is shown in Appendix A.

The available cost data don't include salary costs of State employees who've done work related to the lawsuit. Although outside attorneys and experts have done most the work associated with the lawsuit, staff in several State agencies also have been involved. For example:

- In the Attorney General's Office, the attorney who is now Senior Deputy Attorney General was heavily involved in the early years of the lawsuit, and since 1987 he has spent about 5%-10% of his time on it. Three successive assistant attorneys general have worked extensively since 1990 with outside counsel.

- In the Department of Agriculture's Division of Water Resources, the chief engineer has provided technical expertise over the years, the legal counsel has served as legal liaison between Division staff and others, and other staff have been involved as needed. During the liability phase of the trial, for example, nine Division staff helped process data from geographic information systems, develop exhibits for trial, and the like in fiscal year 1991.

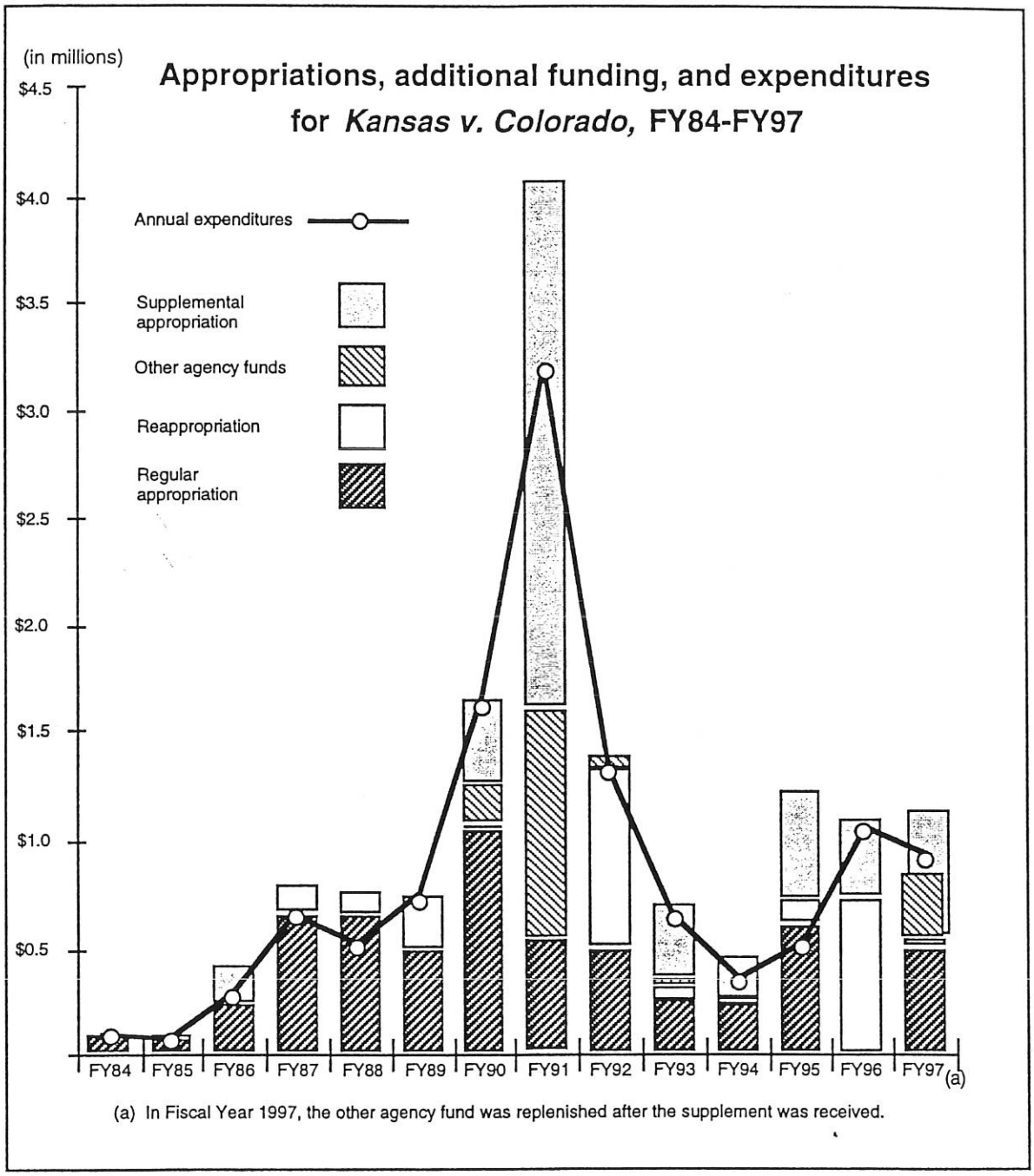
- The Department of Health and Environment, the Kansas Water Office, and the U.S. Geological Survey at the University of Kansas also have provided limited, occasional consultation.

Complete time records weren't available from all agencies to allow us to determine the actual number of hours State employees have spent on the lawsuit. However, we estimated that, in the past two years, the State has spent approximately $106,000 on salary and benefits for employees who spent at least 5% of their time on the lawsuit. If similar amounts were spent in earlier years, the total cost of State employee time could be hundreds of thousands of dollars, if not more. Appendix B shows key staff in the Attorney General's Office and the Division of Water Resources and the time periods in which they worked on the lawsuit plus time periods when key attorneys, experts, and others were involved.

Much of the Lawsuit Was Funded Through Supplemental Appropriations Because of the Difficulty in Predicting Costs in Advance

Expenses associated with this lawsuit have been variable over the years, ranging from a few hundred thousand dollars in some years to several million dollars in others. Nearly all are paid from a water rights account in the Attorney General's Of-

fice, the account used for appropriations specifically directed toward *Kansas v. Colorado*. The chart below shows the expenditures each year and the sources of the money used to fund those expenditures.



As the chart illustrates, regular appropriations and amounts carried over from previous years generally were sufficient to cover the lawsuit's expenses through fiscal year 1989. In 1986 and in fiscal years 1990 and later (except in fiscal year 1992), the Attorney General received supplemental appropriations from the Legislature to cover

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those expenses. In several years—most notably 1990, 1991, and 1997—the Attorney General had to transfer moneys from other operations within the Office to fund the lawsuit until a supplemental appropriation could be obtained. In fiscal year 1995, although the Attorney General didn't request it, the Governor and Legislature provided $500,000 in supplemental funding, intended to be used in the following fiscal year.

When this audit was requested, legislators asked why the lawsuit's costs couldn't be more accurately predicted, so that the Attorney General wouldn't have to request supplemental appropriations to fund the legal costs. They also asked how much of the cost was funded with moneys intended for other aspects of the Attorney General's operation.

Officials in the Attorney General's Office told us that supplemental appropriations were necessary for several reasons:

- *Because budget requests are prepared about a year in advance, it was difficult to predict expenditures accurately when those requests were submitted.* Attorney General officials told us that staff most involved with the lawsuit tried to project the activities that would occur during the coming fiscal year. Very few interstate water rights cases have been brought to the Supreme Court, making it even more difficult to determine from precedent when activities "should" occur. Actual activities on the case have depended on such things as how quickly Colorado provided certain materials to Kansas and how quickly the Special Master moved the case along.

- *Unexpected events sometimes caused significant delays in the case.* For example, during 1990, an important witness became ill and couldn't testify. The Special Master granted Kansas a seven-month delay in the trial so that it could find a new expert and correct problems in its hydrologic model.

- *The extremely technical nature of the suit made certain costs hard to predict.* This was particularly true during the liability phase of the lawsuit, when Kansas had to prove Colorado had taken more water than it was allowed under the Arkansas River Compact. It was difficult to know how much information expert witnesses would have to provide and what the associated costs would be.

- *For several years, the Governor and the Legislature made a conscious decision not to fund the full amount requested for the lawsuit until a more accurate amount could be determined through the supplemental appropriation process.* For fiscal years 1994 through 1997, the Governor recommended and the Legislature funded a total of less than one-third of the amount the Attorney General had estimated the lawsuit would cost.

Over the years, the Attorney General's Office, in consultation with the Legislative leadership and the Governor, has spent about $1.6 million that was originally in accounts other than the one designated for the water rights litigation, but much of that money was replaced after the Office received supplemental appropriations. Appendix C shows how much money was used from other accounts to pay for the water rights litigation and that 75% of it was replaced. For example, officials in the Attorney General's Office told us that, in fiscal year 1997, after the Attorney General consulted with legislative leadership, the Office borrowed

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$300,000 from the unrestricted operating expenditures account and used it for the lawsuit. These moneys were replaced from the supplemental appropriation the Attorney General received for 1997. A similar situation occurred in fiscal year 1991, when $900,000 of operating funds was used and replaced with a supplemental appropriation to that account.

The Attorney General's Office Estimates It Could Take Up to Four Years And $3 Million To Finish the Lawsuit with Colorado, Excluding Post-Judgment Monitoring Costs

These time and cost estimates aren't hard-and-fast, but Attorney General staff indicated they were the best currently available, based on projected activities. During fiscal years 1998 and 1999, officials expect to prepare and present arguments before the Supreme Court on Colorado's compliance modeling, to prepare for and present arguments before the Special Master on Colorado's compliance and future monitoring, to prepare expert opinions on remedies, and to conduct additional activities. They also expect assessments of $150,000 in fees for the Special Master.

In addition, State officials expect Kansas to incur costs for monitoring Colorado's compliance with the Supreme Court's eventual decision in *Kansas v. Colorado*. The type and cost of that monitoring will depend on the Court's ruling as to how Colorado's future compliance is to be determined. If that determination depends on complicated adjustments to the hydrological model, outside expertise may be necessary. If adjustments to the model are relatively simple and not time-consuming, Division of Water Resources officials said, current staff in the Division could perform those duties.

Any moneys received from Colorado as a result of the lawsuit are to be distributed according to a complex formula enacted by the 1996 Legislature. According to that formula, the Attorney General must certify how much the State has spent on *Kansas v. Colorado*. If Kansas receives money, as it has requested, the amount certified is to be deposited into an interstate water litigation fund. The first use of that fund will be to reimburse private parties who donated funds for the lawsuit. Appropriations from the fund then can be used for preparing for or conducting an interstate water rights lawsuit or for monitoring or enforcing compliance with an interstate agreement or judgment. Any interest earned on moneys in the water rights litigation fund is to be credited to the State General Fund.

If there is no such lawsuit or monitoring or enforcement action at the end of fiscal year 2001, the fund will be abolished, and the remaining moneys in it will be transferred to the State General Fund. If Kansas receives more money than it spent on *Kansas v. Colorado*, the additional money is to be divided—one third will go to the State Water Plan Fund for use on water conservation projects and two-thirds will go to a Water Conservation Projects Fund.

10-16

The Attorney General will ask the Legislature to decide during the 1998 session whether to file a similar lawsuit against Nebraska over the Republican River, which could cost as much as $20 million. The Republican River begins in eastern Colorado and flows through northwest Kansas and southwest Nebraska before it returns to Kansas. It joins with the Smoky Hill River below Milford Reservoir to form the Kansas River. Kansas and Nebraska have a compact governing prospective allocation of water in the Republican River. That compact was intended to allow a certain amount of water development and to allocate water rights accordingly.

Division of Water Resources officials think Nebraska is overusing its allocation, at least in part because Nebraska doesn't regulate groundwater wells near the river. If a lawsuit were to be filed and experts determine the waters of the Ogallala Aquifer also are involved, that lawsuit could be even more complicated than *Kansas v. Colorado*, officials in the Attorney General's Office told us.

The Attorney General's Office estimates that a lawsuit with Nebraska over the Republican River could cost perhaps $20 million. Although the State can apply much of what it learned in *Kansas v. Colorado* regarding time expectations, expertise required, and budget, the Republican River Compact differs substantively from the Arkansas River Compact in its primary scheme for allocating water, so that much of the legal precedent of *Kansas v. Colorado* will not be applicable.

The 1997 Legislature appropriated $200,000 to study this issue in fiscal year 1998. That money is being used in part to pay experts—including Kansas' lead attorney for *Kansas v. Colorado*—to study the feasibility of a lawsuit against Nebraska.

Kansas also could face litigation over the waters of the Missouri River at some point; no decision on whether to file suit has been made and no cost estimates have been developed. Kansas, along with several other states, several Indian nations, and federal agencies such as the Corps of Engineers and the Bureau of Reclamation, is a member of the Missouri River Basin Association. The Association's mission is to provide advice on how the River should be operated, to resolve disputes, and to serve as a coordinating body.

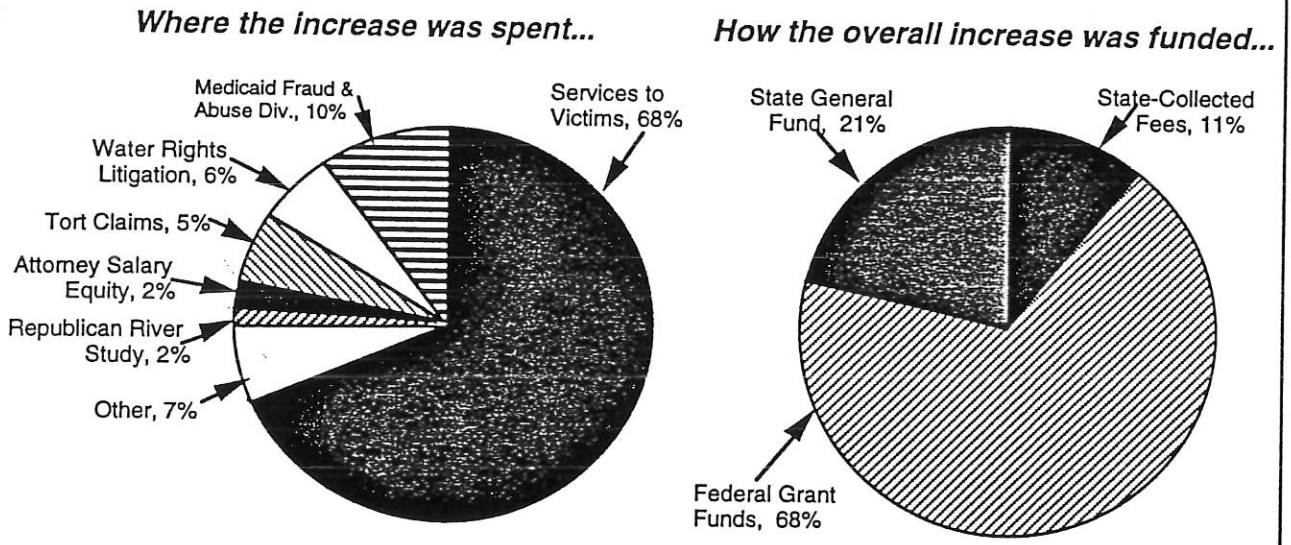
Recently, the Corps has proposed changes in how federal reservoirs in the upper basin (Montana, North Dakota, and South Dakota) will be operated. These changes have the potential to affect recreation, hydroelectric power, navigation, and other beneficial uses in downstream states and Indian nations.

Missouri already is suing the Corps over its operating plan. Missouri's main concern is maintaining sufficient water flows for barge traffic (30,000 cubic feet per second). Kansas' chief concern is maintaining sufficient water flow at Kansas City for basic water needs (5,000 cubic feet per second).

The 98% Increase in the Attorney General's Budget From Fiscal Year 1995 to 1998 Was Caused Mostly by Increases in Federal Grant Programs for Victims

One of the questions legislators had raised for this audit was why the Attorney General's Office's budget had increased so rapidly in recent years and whether those increases were related to the lawsuit. The Office's budget has risen by $8.8 million

Reasons for Increases in the Attorney General's Budget, and Sources of Those Funds—Fiscal Years 1995-1998



over the past three years—from $9 million in fiscal year 1995 to $17.8 million for fiscal year 1998.

The accompanying pie charts illustrate what the additional money is being spent on and where it comes from. As the charts show, costs related to the water rights litigation account for only 6% of the increase in the Attorney General's costs over the past three years. By far the biggest area of increase—accounting for 68%—was in victim services programs, which receive much of their funding from federal grants. Victims of Crime Act moneys, formerly administered by the Department of Social and Rehabilitation Services, and Safe and Drug-Free Schools and Communities Grants, formerly in the Governor's Office, were moved to the Attorney General's Office beginning in fiscal year 1996. These programs are financed mostly with federal funds.

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The pie charts also show that the Medicaid Fraud and Abuse Division accounts for a substantial portion of the increase—about 10%. This unit was created by a federal mandate in fiscal year 1996, and to-date has been mostly funded with federal dollars. Tort claims, which accounted for about 5% of the increase, are paid as a result of legal settlements and judgments against the State. Funding for two additional positions also is included in that funding increase. Tort claims are paid from the State General Fund.

In addition, several other employees have been added to the Attorney General's Office over the past three years. These additional positions, which accounted for approximately 3% of the increase, were as follows:

- 2 were added for sexual predator work
- 2 were added for death penalty work
- 1 accounting position was added
- 2 special projects positions were added in consumer protection

What Contractual Agreements Has the Attorney General's Office Made with Private Attorneys?

Since she took office in January 1995, the Attorney General has awarded 55 contracts to private attorneys or law firms to perform legal work on behalf of the State. Most of those firms were hired because of conflicts of interest that prevented the Attorney General's staff from prosecuting or representing defendants. Nearly all contracts were based on flat hourly fees, with rates of pay ranging from $75-$85 per hour for more routine cases up to $255 per hour for one expert case. New billing guidelines adopted by the Attorney General's Office for fiscal year 1998 should help control the cost of using outside attorneys. Finally, we found that State agencies' practices in contracting for outside attorneys varied so widely that we couldn't make meaningful comparisons. These and other findings are described in the sections that follow. Issues about which attorneys or firms the Office has contracted with and how they were selected are discussed in question 3.

Most of the Attorney General's Contracts with Private Attorneys Were Awarded Because Conflicts of Interest Prevented The Office from Handling Particular Cases

During this audit, we reviewed all 55 contracts for outside attorneys the Office entered into from January 1995—when Attorney General Stovall took office—through fiscal year 1997. When a case continues across fiscal years, the Attorney General's Office signs a new contract for each year. For our purposes, however, we counted a contract as new only once, regardless of how many years it spanned.

The Office contracts out very few cases to private attorneys. In fiscal year 1997, for example, the Attorney General entered into contracts with 13 private law firms to assist with 14 of the 1,664 case files opened by the Civil Litigation Division that year (less than 1%).

Officials in the Attorney General's Office told us they contract with outside counsel in the following types of situations:

- In-house staff have a conflict of interest and can't represent the defendant. This happens most often when a case has multiple defendants; the Attorney General's Office normally can represent only one of the defendants and must hire outside counsel for the others. (Multiple defendants may have different defenses that could conflict with each other.)

- In-house staff don't have the expertise to most efficiently handle the case. Outside counsel often are used when the case requires a specialist in a particular area of law. Also, former staff may be hired as outside counsel to handle appeals of cases they handled while on the Attorney General's staff. This practice allows knowledge gained during the original trial to be carried over for the appeal.

- In-house staff don't have time to take on the case. Attorney General staff said this has become less of a problem since the 1995 Legislature authorized two additional assistant attorneys general for the Civil Litigation Division.

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In addition, agency heads or their chief counsel occasionally request a specific private attorney for a case. The Attorney General typically honors these requests.

About 42% of the cases contracted out were because of a conflict-of-interest, while about 31% were contracted to take advantage of an attorney's or firm's expertise. The table below shows how many of each type of case the Attorney General has contracted out. It also provides basic information about the provisions contained in those contracts. More detailed information about amounts spent on each case from fiscal year 1995 through fiscal year 1997 can be found in Appendix D.

Reasons for Contracting Cases and Fee Structures
1/1/95 through 6/30/97

Reason for Contracting	No. of Cases	Fee Type	Attorney Rate of Pay
Conflict of interest	23	Fixed Fee	$75/hr - $85/hr.
Time	9	Fixed Fee	$75/hr - $85/hr.
Multiple reasons	5	Fixed Fee	$85/hr.
Other	1	Contingency	Fees and expenses as awarded by the Court
Specialized	17	Fixed Fee (13) Contingency (4)	$75/hr - $255/hr
Examples of specialized cases:			
Sexual Predators		Fixed Fee	$139/hr - $255/hr
Water Rights - Colorado		Fixed Fee	$115/hr - $145/hr
Tobacco		Contingency	If case is heard and won in State court: •out-of-pocket expenses will be reimbursed •national and local counsel can each get up to 12.5% of the remainder of the State's award (25% maximum) If case is heard and lost in State court: •no fees or expenses have to be paid, but attorneys can petition the Joint Committee on Special Claims for payment

One concern expressed when this audit was requested was that attorneys on the water rights lawsuit would receive part of the damages awarded to Kansas, even though they'd been paid at an hourly rate. As the table shows, the contract on this lawsuit calls for a fixed hourly rate of $115-$145 per hour. No provisions of the contract or law allow the attorneys to share in any damage award the State may receive.

The Attorney General's Office uses a standard contract for nearly all the cases involving outside counsel. The contract clearly specifies what out-of-pocket expenses can be charged to the State, including long distance calls, photocopies, special delivery mail, travel and lodging (economy class when available), and mileage. The contract also states that outside counsel must get approval from the Attorney General's Office to hire experts for the case.

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The contracts also include a cap, or maximum amount to be paid under the contract. Each year, we noted that about one-third of the contracts were amended one or more times to increase the maximum payable. The Senior Deputy Attorney General said caps are written into contracts to give outside counsel an idea of how much the Office expects to spend on the case. However, he also said that on defense cases the Office can't know for sure how much the attorney will need to spend—if the plaintiff wants an extensive discovery phase, or the judge makes rulings the defense attorney thinks should be challenged, the costs will rise accordingly. If outside counsel want to exceed the cap written into the contract they must discuss the increase with the Senior Deputy, and the increase must be approved by the Attorney General.

The Attorney General's contract with law firms representing Kansas in the tobacco litigation could become moot if Congress approves a national settlement with the tobacco companies. In 1996, the Attorney General contracted with two national law firms and a local law firm to file suit against the tobacco companies. The suit was to recover money the State has spent over the years because of health problems Kansans have suffered by smoking.

The three firms took the contract on a contingency basis, which requires them to pay all up-front expenses and gives them a combined maximum of 25% of any amount recovered on the State's behalf. Under the contract, the actual fees each firm receives will be determined by the district court after all out-of-pocket expenses had been reimbursed.

In July 1997, after 39 states and Puerto Rico filed similar suits, the tobacco companies offered a $368.5 billion national settlement to be paid out over 25 years. If that settlement is adopted by Congress, it will wipe out all the individual state suits. It's likely a national arbitration board will be appointed to determine the fees and expenses for all attorneys involved and the tobacco companies would be required to pay their compensation.

Thus, although the attorneys could make a great deal of money if the case goes to trial and Kansas receives a large judgment, it's not clear how much the attorneys might receive if the national settlement is approved by Congress. Even if the case did go to trial and Kansas won, there's no guarantee the court would award the full 25% allowed by the contract.

The Attorney General Has a New Billing Review System That Should Help Ensure the State Pays Outside Counsel Only for Reasonable Costs

In the past, the Attorney General's Office didn't have a strong system for ensuring the State paid outside attorneys only for reasonable costs. The Office's main attempts to hold down costs were twofold: the establishment of a standard $85-per-hour fee, and a billing review by the Deputy Attorney General for Litigation, assisted by accounting staff, to check for mathematical accuracy and reasonableness of the

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time and amounts charged. However, no specific guidelines had been established for such things as how many attorneys would be paid for attending a deposition, which staff members could be billed to a case, and the like. This left the State at higher risk of paying for services that weren't provided in a cost-effective manner.

In fiscal year 1997, after reviewing the Legislative Post Audit report on contracting for professional services, the Attorney General began working with Examen, Inc., a California billing review firm, to develop billing guidelines for contracted legal services. Examples of some of the guidelines, which were adopted beginning in fiscal year 1998, are as follows:

- firms won't be paid for more than one attorney attending depositions
- firms won't be paid for basic legal research—the State is paying for the existing expertise of the contractor
- firms won't be paid for subscription and on-line charges for computerized legal research services (these are considered to be overhead). They can be paid for the time of a staff person doing specialized computer research
- firms can only be paid for a team of up to two attorneys and one paralegal on any case, and payment will be made only for people named as team members
- firms won't be paid for time spent by replacement personnel to learn the basic facts of a case, or for inexperienced staff using the case as a training ground
- firms are encouraged to staff cases at the lowest effective economic level (for example, when appropriate, associates should be used rather than partners in the firm.)
- firms won't be paid for administrative or supervisory conferences among firm personnel

Outside attorneys submit monthly invoices to Examen, Inc., on an electronic basis. Each invoice must show such things as the date of each service performed, a full description of the service rendered, the name of the person performing the service and his or her hourly rate, and the amount of time spent on the service. Expenses must be itemized, and although documentation isn't required to be submitted, it may be requested by the Office at any time. Officials said they may begin requiring documentation in the future.

Examen, Inc., receives a fee equal to 3% of the billings it processes. In Spring 1998, the Office will compare the estimated cost savings to the cost of the contract to determine whether the guidelines are saving money for the State.

If this system had been in place during fiscal year 1997, the Attorney General's Office may have reduced its contract costs. To get an idea of what effect the guidelines might have, we looked at 32 contracts in effect during fiscal year 1997 to see how many of them used more staff than would have been allowed under the new guidelines. (This was the only aspect of the guidelines we could readily check against the type of billing data we collected.)

Our review showed that 11 firms billed the Office on 15 contracts for either more attorneys or more paralegals than would have been allowed if the current system had been in place. For example, the State paid for 10 attorneys under one contract, and for three to seven attorneys on 11 other contracts. It seems likely that if the

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firms had been limited to two attorneys on these contracts, the total number of attorney hours billed to the State would have been lower.

There's Little Consistency in the Contractual Arrangements State Agencies Make With Outside Attorneys

We interviewed officials in several State agencies that contract for outside counsel to find out what types of contractual arrangements they use. The following table compares those contract provisions for both cases that are part of the agency's normal workload and specialized types of cases that may come up only rarely for a particular agency.

Contractual Arrangements with Outside Counsel in Selected State Agencies

Type of case/ Agency	Rate of Pay	Cap?	Is Primary Attorney Specified?	Allowed To Hire Experts?
Cases that are part of the agency's normal workload				
Attorney General	$75 - $85/hr	Yes, varies	Usually	Agency must approve
Insurance Dept.	$60/hr	$2,500	Yes	Agency must approve
Indigents' Defense	negotiated	n/a	Yes	Board selects
Dept. of Transportation				
Property damage	Contingency	25%	No	Attorney selects
Specialized cases				
Attorney General	$95 - $255/hr	Yes, varies	Yes	Agency must approve
KCC	$75 - $185/hr	Yes, varies	Yes	Agency selects
Dept. of Revenue				
Single taxpayer case	$300/hr	Yes	Yes	Agency selects
Dept. of Transportation				
Land condemnation	$100 - $125/hr	Yes, varies	Yes	Agency must approve
Copyright/patent	$5,000/case	n/a	Yes	Agency must approve
Constitutional law	$150/hr	Yes, varies	Yes	Agency must approve
Employment law	$90/hr	Yes, varies	Yes	Agency must approve
Retirement System				
Direct placement	Contingency	% smaller as award increases	Yes	Agency must approve

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As the table shows, these agencies use a wide variety of contractual provisions, depending on their legal needs. It's difficult to draw meaningful comparisons from the data because the agencies differ significantly in the types of legal work they contract out. For example, the Attorney General's own staff might normally handle a constitutional law case with in-house staff, whereas the Department of Transportation might consider such a case to be a "specialized" case to be contracted out. Also, an agency such as the Board of Indigents' Defense Services contracts out only criminal cases, whereas the Attorney General's Office is contracting out civil cases. None of the other contractual provisions contained in the Attorney General's contracts were out of line.

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Does the Attorney General's Office Follow Adequate Procedures To Prevent Potential Conflicts of Interest When It Hires Private Attorneys and Law Firms?

The Attorney General's Office has no formal procedures for awarding contracts to outside counsel. Attorneys or firms are selected by the Attorney General, based on such factors as the firm's previous successful work for the Office, its geographic closeness to the case, and its expertise. We didn't find any violations of the State's conflict-of-interest laws for cases contracted to outside counsel, but contracts were awarded to former associates and campaign contributors. Because public moneys are being awarded, such practices can create at least an appearance of favoritism. Some other State agencies follow procedures that could help minimize these concerns, while also providing greater assurance that attorneys who are interested in and qualified for such work have an equal chance of being considered. In contracting for large and complex cases, the Office and other State agencies we talked with generally follow the same practices, but we thought more could be done to ensure the Office identifies and considers a broad pool of qualified firms, and documents the rationale for selecting outside counsel. These and other related findings are discussed in more detail in the sections that follow.

The Office Has No Written Procedures for Awarding Contracts; The Attorney General Selects Which Outside Counsel To Contract With Based on the Recommendations of the Deputy

Because the Office has no written procedures in this area, we interviewed Office staff about how private attorneys and law firms were selected for the 55 contracts that had been awarded from January 1995 through June 1997. (As noted earlier, although contracts are renewed each year, we counted a contract with a firm only once, regardless of how many years it spanned.) Those counsel and the cases they've been hired for are shown in Appendix D.

Like other State agencies, the Attorney General's Office isn't required to competitively bid contracts for legal services. The Senior Deputy Attorney General told us that, when a case comes to the Office that can't be handled in-house, he recommends an attorney or firm to the Attorney General based on the following factors:

- the attorney or firm has successfully worked with the Attorney General's Office in the past
- the attorney or firm is in the geographic area where the case was filed
- the attorney or firm has skill in a particular area relevant to the case
- the quality of work produced by the attorney or firm is known by someone in the Attorney General's Office
- the attorney's office has an adequate infrastructure for handling the case (for example, adequate support staff, equipment, library, and the like)

In explaining the Office's selection process, the Senior Deputy told us that "litigation is a very personal thing to the defendant who faces possible dire financial,

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political, and social consequences. Thus, the selection process is open only to the individuals and firms known and trusted by the Attorney General, who she can professionally recommend as counsel for the State agency, official, or employee being sued."

The Attorney General then approves a firm, taking the Deputy's recommendation into consideration. The Office doesn't document the actual selection process, or the basis for the decisions made.

In determining how the Office has selected contract attorneys, we also interviewed staff and firms and reviewed the information available for two of the Office's largest ongoing cases—the water rights litigation case, and the tobacco litigation case. The selection process for those two cases is described below.

Consulting Engineers Who Worked On the Water Rights Case Recommended the Attorney Who Initially Was Hired to Handle the Case

During Summer 1983, the Attorney General's Office approached federal agencies and private engineering firms about doing a study of reduced water flow in the Arkansas River. In the early 1980s, the Office began exploring concerns that Colorado was depleting water supplies in the Arkansas River before the water reached Kansas. In July 1983, the Attorney General's Office approached federal agencies—including the Corps of Engineers and the Bureau of Reclamation—about conducting a study to determine whether Colorado was using more than its fair share of water. Those federal agencies declined to do the study.

The Office also asked officials from the Division of Water Resources, the Kansas Water Office, and members of the Kansas Compact Administration to suggest the names of firms that might have the expertise to conduct such a study. A number of firms were contacted, and six firms from five states submitted proposals. Those proposals were reviewed by the Kansas Water Office, the Kansas Geological Survey, and the Division of Water Resources. Although documentation from this time period was limited, it appears there was strong support among the agencies for the Colorado consulting firm of Simons, Li & Associates, which then-Attorney General Stephan subsequently hired.

The consulting engineers who did the water study for Kansas helped in the search for legal counsel to represent the State in the lawsuit. In late 1983 and early 1984, both the Attorney General's Office and the consulting engineers solicited law firms to serve as the lead counsel for the lawsuit. The Attorney General's Office tried to identify firms within Kansas that might be qualified, while Simons, Li & Associates conducted a broader search. The Attorney General's Office reviewed the law firms that submitted proposals and in late Spring 1984 selected Richard Simms (then of Hinkle, Cox, Eaton, Coffield and Hensley), one of the attorneys suggested by Simons, Li & Associates.

When the first attorney withdrew from the case, an attorney who was already working on the case was chosen as the replacement because of his experience and familiarity with the case. In 1991, Richard Simms withdrew as legal counsel on the case because of disputes with the Attorney General's Office over delays in paying his fee and the amount of money the State was allocating to the lawsuit. John Draper of Montgomery and Andrews was selected to replace Mr. Simms. Mr. Draper had been assisting with the case for two years and reportedly was regarded as the obvious choice because of his experience and his strong credentials. There was no documentation that any other candidates were considered as a replacement for Mr. Simms.

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Representation for the Tobacco Lawsuit Was Divided Between a Mississippi Firm, A South Carolina Firm, and a Kansas Firm After Discussions Were Held With Several Other Law Firms

In early Spring 1996, the Attorney General held preliminary discussions with three Kansas law firms about representing the State in tobacco litigation. The lawsuit was to be filed against several national tobacco companies. Those firms were Hutton & Hutton of Wichita, Morrison & Hecker of Kansas City, and Don Barry of Topeka. At the time of those preliminary discussions, it was anticipated the firm selected would handle the entire case, and would be paid on a contingency fee basis if the case were won. The firm selected also would have to finance any up-front legal expenses, which at the time were estimated could run several million dollars.

Two firms withdrew over issues related to expenses, and negotiations with a third firm stalled over the fee arrangement. Two of the firms—Don Barry and Morrison & Hecker withdrew from the negotiations because they didn't want to be responsible for paying the up-front costs of the lawsuit. Throughout the Spring and early Summer of 1996, negotiations with Hutton & Hutton continued. According to the correspondence, the sticking point of those negotiations was a disagreement over the fee amount. The firm wanted the contract to state that fees would be a fixed percent of whatever the State was awarded. (Draft contracts indicated the firm wanted 25%, although the percent was reportedly somewhat negotiable.) The Attorney General's Office wanted the fee to be established by the Court up to a maximum of 25%. The Attorney General's staff indicated the fee a court actually awarded could vary greatly, depending on the size of any damages awarded to the State.

The Attorney General decided to hire Mississippi and South Carolina firms as the lead national counsel on the case. While the negotiations with Hutton & Hutton were continuing, the Attorney General's Office held discussions with a Mississippi law firm—Scruggs, Millette, Lawson, Bozeman & Dent, P.A.—that was representing several other states in tobacco litigation. Ultimately the Attorney General decided to hire Scruggs, et al. and a South Carolina firm—Ness, Motley, Loadholt, Richardson & Poole, P.A.—to jointly serve as national counsel for the lawsuit.

The State still needed to find local counsel capable of providing support to the national firms, and capable of reviewing and providing a repository for the thousands of documents that would be generated by the case. The Attorney General's Office went back to Morrison & Hecker to see if the firm would be interested in serving as local counsel for the lawsuit, with up-front expenses to be negotiated with the national firms. Morrison & Hecker declined, citing the appearance of a conflict of interest. The Attorney General's Office didn't talk with Mr. Barry or with Hutton & Hutton about serving as local counsel.

In June, about a month after she'd heard they were interested in the case, the Attorney General contacted the law firm of Entz & Chanay (her former employer) about the possibility of serving as local counsel. It is unclear when serious negotiations with Hutton & Hutton stopped, but an internal memorandum dated June 28 from the Attorney General to her chief deputy informs him of Entz & Chanay's interest, and refers to the need to back out of arrangements with Hutton & Hutton.

During the summer, Entz & Chanay and Scruggs et al. negotiated terms that called for the two national firms to pay up-front expenses of the case and to receive a contingency fee of up to 12.5%. Entz & Chanay also would receive a contingency fee of up to 12.5%. On August 8, 1996, the Attorney General and the three law firms signed the contract.

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We Didn't Find Any Violations of the State's Conflict-of-Interest Laws For Cases Contracted to Outside Counsel

Kansas' conflict-of-interest laws prohibit State officers and employees from contracting on the State's behalf with firms they or their immediate family members own or have a substantial interest in. State law also prohibits any State officer or employee, upon leaving State service, from immediately accepting employment with a firm he or she participated in awarding a contract to in the previous two years. Employees can't join such a firm for two years after leaving State service or until two years after the contract has been completed, whichever comes first.

Our reviews of statement of substantial interest forms showed that the two officials primarily involved in selecting contract attorneys—the Attorney General and the Senior Deputy Attorney General—don't own or have a substantial interest in any of the private law firms hired by the Office.

We did note that the Office has no systematic procedure for checking these statements to ensure that no conflict exists. In addition, in one instance during the period we reviewed, an assistant attorney general had recommended a firm to handle a case. Because this attorney wasn't required to file a statement of substantial interest, we couldn't determine whether a conflict of interest existed.

Although not a violation of law, contracts were awarded to former associates and to campaign contributors. Because these contracts involve public moneys, such practices can raise questions about favoritism or political patronage. These situations are described below:

- *One contract was awarded to the Attorney General's former law firm.* After talking with several other law firms about the case, the Attorney General eventually hired her former employer to serve as local counsel for the State's lawsuit against the major tobacco companies. The box on page 19 describes the steps the Attorney General's Office took in making this selection. Regardless of the firm's qualifications, this situation is bound to create at least an appearance of favoritism.

- *Five contracts were awarded to four former staff members of the Attorney General's Office.* In all five contracts, there appeared to be appropriate reasons for contracting with former employees. Three involved appeals of cases those attorneys had handled successfully while on the Attorney General's staff. The fourth contract involved the reopening of a case the attorney had worked on while at the Office. In the fifth case, the State agency being sued specifically asked to be represented by the former employee.

- *About two-thirds of the firms the Attorney General has contracted with had contributed to the Attorney General's 1994 campaign.* In looking at campaign finance records, we focused only on the 29 attorneys or firms involved in the 35 contracts that had been newly awarded under the current Attorney General. (We counted a firm as a contributor if at least one attorney in the firm had made a contribution.) In all, 20 of these 29 outside counsel (69%) had made contributions. Their contribu-

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tions ranged from $50 to nearly $6,500. Those 20 firms received 27 of the 35 contracts that were awarded, or about 77%. Information about these contracts can be found in Appendix D.

Because it's not uncommon for certain people or businesses who do work for the State to make contributions to both sides during an election campaign, we looked to see if that was the case for these contributors in 1994. We found that 10 of the 20 firms had contributed to both General Stovall and to her opponent in either the primary or general election.

Finally, we reviewed the number of attorneys or firms who'd contributed to the Attorney General's 1994 campaign but hadn't received a contract from the Office. We identified members of 75 firms and about 140 other attorneys who made contributions but didn't receive contracts. (Not all these firms or individual attorneys may have been eligible for or interested in contracting with the Office.) In all, attorneys made 26% of the total contributions to Attorney General Stovall's campaign.

Selecting attorneys to handle lawsuits for the State is clearly a professional judgment call. During our discussions with officials in the Attorney General's Office, they clearly stated that the Office's decisions were based on an attorney's qualifications and expertise, and on the confidence they had in that attorney's ability to present an effective strategy and win the case. But any elected official in a position to direct State work to private firms or individuals likely will be subject to charges of favoritism if some connection can be made between the official and the individuals being hired.

Such concerns may be minimized if, whenever possible, procedures were established to ensure that attorneys who are interested in and qualified for such work have an equal chance of being considered. The sections that follow discuss some of the things the Attorney General's Office could consider in this area.

For Cases That Need To Be Contracted, Some State Agencies Have Adopted Procedures That Can Help Minimize the Appearance of Favoritism and Increase the Pool of Interested and Qualified Attorneys

Some cases the Attorney General's Office contracts out could be handled by any number of qualified law firms. These include cases the Office would handle with a staff attorney if there weren't a conflict of interest or time constraints.

During this audit, we contacted the Insurance Department, the Board of Indigents Defense Services, and the Department of Transportation to see how their procedures for selecting outside counsel compared to the Attorney General's. All three agencies contract out a significant amount of legal work.

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In general, we found that these agencies had established some procedures the Attorney General's Office might be able to apply to some of the cases it contracts out. Those procedures are as follows:

- *Both the Board of Indigents Defense Services and the Insurance Department have processes for soliciting attorneys who want to do legal work.* The Board issues a request for proposals for attorneys who are interested in handling cases its staff can't handle. Interested attorneys submit a proposal, resume, and references. Qualified attorneys then are interviewed by the agency director, who makes a recommendation to the Board.

  Similarly, attorneys who are interested in handling Second Injury Fund cases for the Insurance Department send a letter of interest and resume to the Insurance Commissioner and are interviewed by staff attorneys. If the Department determines they are qualified, they are put on a list of attorneys who may be given cases.

- *The Insurance Department also has a method for rotating work among interested and qualified attorneys.* Those who are added to the Department's roster have their names placed in alphabetical order, by geographic region. When a case is filed against the Second Injury Fund, the attorneys from the region in which the case was filed are contacted in alphabetical order to see if they are available and want to take the case.

The maintenance of qualified attorney lists such as the Board of Indigents Defense Services or the Insurance Department uses can help to ensure that all interested and qualified attorneys are considered for work to be contracted out. Rotating the work among the interested and qualified firms also appears to be desirable because it can give more firms an opportunity to participate in State business. The Insurance Deparment's alphabetical approach to rotating cases for the Second Injury Fund wouldn't be appropriate for the Attorney General's Office to use because of significant differences in the types of cases involved, but the concept of rotating cases among qualified firms may be able to be implemented on some other type of basis.

For Specialized Cases, Other Agencies Generally Followed The Same Practices as the Attorney General's Office In Selecting Outside Counsel

According to records provided by the Attorney General's Office, about 31% of the contracts signed by the current Attorney General since January 1995 were for cases that required a high level of expertise in certain areas. Few firms may have the expertise needed to handle such cases. These can include such major cases as the water rights lawsuit and the sexual predator lawsuit They also can include cases that are being appealed, where the attorney who initially handled the case has a tremendous amount of knowledge and expertise about that specific case.

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The Senior Deputy Attorney General told us the Office generally follows the same process outlined on page 17 in selecting attorneys to handle these expert cases. (The box on pages 18-19 described the selection process followed for the water rights litigation and the tobacco lawsuit.) These processes show the Attorney General's Office relies heavily on staff's professional judgment in selecting outside counsel.

During this audit, we asked general counsel in a number of other agencies how they selected counsel for the most technical and specialized litigation they contract out. These include litigation such as the single-taxpayer case (Department of Revenue), lawsuits to recover investment losses (KPERS), constitutional law and patent issues (Department of Transportation), and utility regulation (Kansas Corporation Commission.)

Officials from these other agencies said they commonly identified qualified outside counsel by talking with colleagues, law schools, and other professionals in the field. After interviewing several candidates, they said they'd make their selection based on their professional judgment as to which attorney or firm could best handle the case. Because of the major issues or dollars involved in these "specialized" cases, they said, they wanted the very best attorney they could afford, and sometimes cost wasn't even a consideration.

The Attorney General's Office could do more for major cases to ensure that it identifies and considers a broad pool of qualified firms, and that it documents the rationale for selecting outside counsel. With major lawsuits, attorneys may be paid very large sums to represent the State. Taxpayers deserve assurance that the Office has identified qualified firms, has some rational basis for comparing their qualifications and expertise, and has used good professional judgment in selecting the "very best attorney" they could hire. Documenting the basis for selecting an attorney or firm also would help reduce concerns that counsel were selected on the basis of their connections or contributions, rather than their qualifications.

Although it appeared in the two cases we reviewed that the Office made efforts to identify or advertise for, interview, compare, and select firms they thought could do the best job for the State, it has no systematic procedures for doing so.

Conclusion

When people think of conflicts of interest in awarding State contracts, they tend to include such things as awarding contracts to friends, business associates, or political contributors. While such contract awards don't fall under the definition of conflict of interest contained in State law, they can create at least the appearance of favoritism.

Given the nature of many professions, it would be difficult for any elected official to avoid making contracts with individuals or firms they've worked with in the past, or who've made contributions to their campaigns. The current Attorney General's Office is no exception. A significant num-

ber of the contracts the Attorney General has awarded went to former associates or campaign contributors. On the other hand, we also found that contracts weren't awarded only to campaign contributors, and that a large number of attorneys who'd made campaign contributions hadn't gotten any State contracts.

Unless and until State laws are changed in this area, such situations will continue, and it will be up to each elected official to demonstrate that such State contracts weren't awarded on the basis of patronage or favoritism. By establishing reasonable procedures related to such things as identifying qualified attorneys or firms, evaluating those firms' qualifications, and documenting their rationale for selecting outside counsel, the Attorney General's Office could take a large step in this direction.

Recommendations

1. The Attorney General's Office should establish reasonable procedures to ensure that its contracting process is as open as possible, and that all attorneys who are interested in and qualified to handle legal work for the Office have an equal chance of being considered. Among the procedures the Office should consider are the following:

a. Periodically announcing that attorneys or firms who are interested in contracting with the Office for legal work should provide the Office with their qualifications, location, areas of expertise, and any other pertinent information.

b. Establishing some objective criteria for evaluating the qualifications of attorneys or firms that express an interest in doing contracted legal work, and evaluating their qualifications through record reviews and discussions with the attorneys themselves and with others familiar with them. Those criteria established might include such things as the number of similar types of cases handled by the firm, the backgrounds and number of years of experience of attorneys who would be assigned to contracted cases, the level of support services the firm could provide, and the like.

c. Maintaining a list of individuals or firms the Office has determined to be qualified and suitable to handle contract cases, by area of specialty and by geographic area, and informing them when legal work is to be contracted out. For some types of cases, it also may be possible to consider rotating the work among qualified attorneys on that list.

d. Clearly documenting the rationale for selecting the firm or firms chosen for each State contract.

2. To ensure that it can verify it is complying with statutory conflict-of-interest requirements, the Office should require all professional staff to complete annual statements of substantial interest.

APPENDIX A

Amounts Paid to Outside Attorneys and Experts, Fiscal Years 1991-1997

The State paid approximately $7.3 million to outside attorneys and experts in fiscal years 1991- 1997.

Firm name	Amount paid	% of all spent on experts*	Type of work performed
Simms & Stein	$1,451,076	19.9	lead attorney 1984-1991
Montgomery & Andrews	$1,969,589	27.1	lead attorney 1991-present
Spronk Water Engineers	$1,920,232	26.4	Kansas' main water consultant
Hydrologic Consultants, Inc.	$696,702	9.6	hydrologic modeling, consulting, & expert testimony
S.S. Papadopulos & Asociates	$617,992	8.4	hydrologic modeling, consulting, & expert testimony
Littlefield Research	$96,849	1.3	historical research on the Arkansas River Compact and its framers' intents
Clearwater Consulting Corp.	$68,835	1.0	Kansas' main economics consultant
Groeneveld Resource Management	$60, 596	0.8	research and testimony on water uptake by plants
Prickett & Associates	$56,592	0.8	calibration of the hydrologic model, consulting, and expert testimony
Franzoy Consulting Inc.	$43,658	0.6	consulting and expert witness testimony on crop requirements
others	$67,189.27	1.0	consulting on crops, irrigation, computer code, Supreme Court briefs, etc.

* This column does not add to 100% because it does not account for $87,890 spent on temporary services and $138,984 spent to purchase items. These were included as money spent on experts for this analysis because they were paid through the lead attorney.

Of the amounts spent with the lead attorney firms, most was spent on the services of the lead attorneys.

	Amount	% of the total amount spent with attorney firms
lead attorneys (Richard Simms of Simms & Stein and John Draper of Montgomery & Andrews)	$1,755,810	51.3
other attorneys	$571,698	16.7
legal assistants	$340,734	10.0
clerical	$7,224	0.2
expenses	$745,383	21.8

Note: The categories used in this analysis differ from those used by the Attorney General's Office for its budget table, which is reproduced on p. 5; therefore, the total shown as paid to outside attorneys and experts differs.

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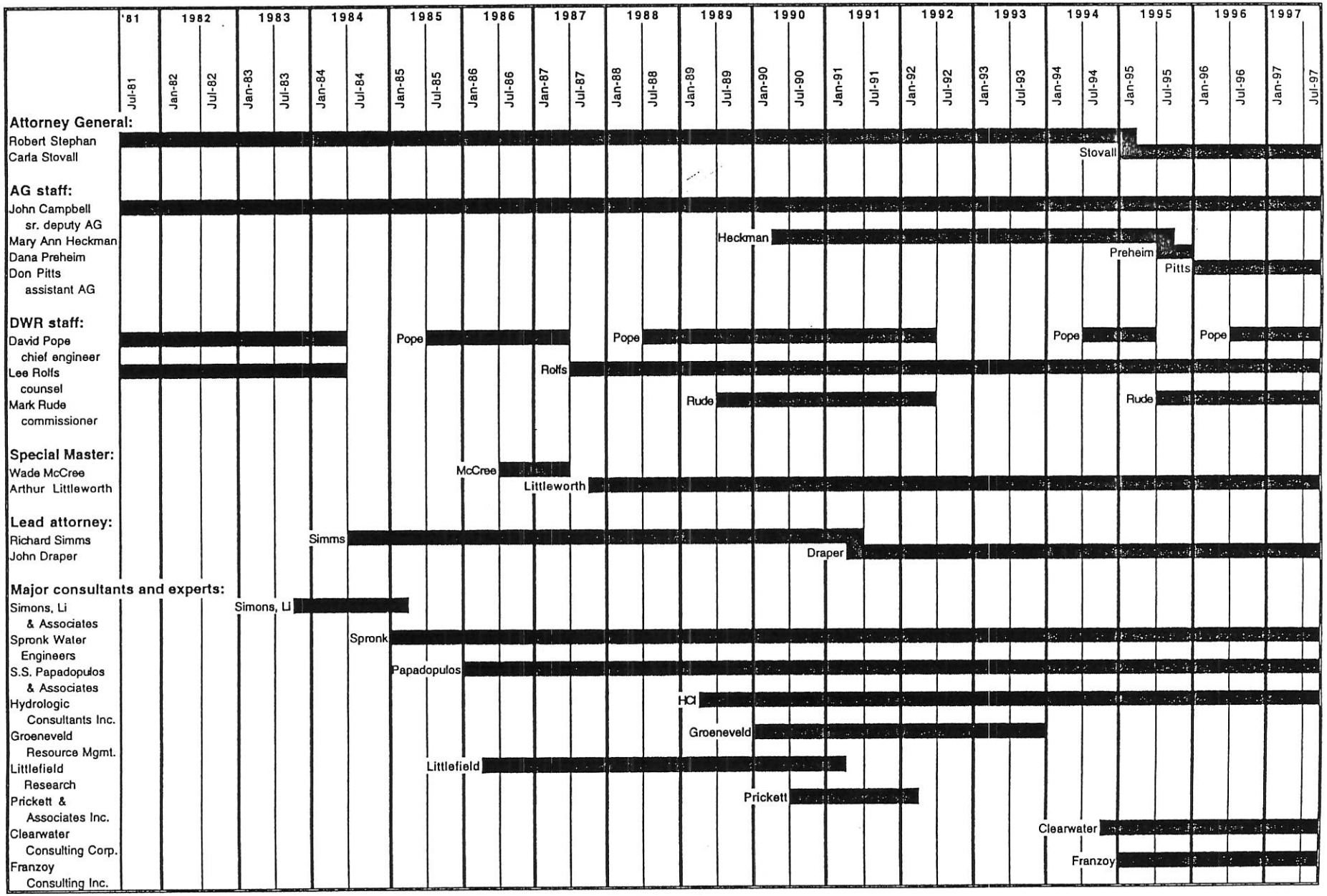
APPENDIX B

Major Participants in *Kansas v. Colorado*

This appendix identifies State officials and employees, as well as outside attorneys and experts, who have had significant involvement with the lawsuit over the years. Appendix F describes the type of work performed by the outside experts shown in this table.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Attorney General:
Robert Stephan
Carla Stovall
Stovall
AG staff:
John Campbell
sr. deputy AG
Mary Ann Heckman
Heckman
Dana Preheim
Preheim
Don Pitts
assistant AG
Pitts
DWR staff:
David Pope
chief engineer
Pope
Pope
Pope
Pope
Lee Rolfs
counsel
Rolfs
Mark Rude
commissioner
Rude
Rude
Special Master:
Wade McCree
McCree
Arthur Littleworth
Littleworth
Lead attorney:
Richard Simms
Simms
John Draper
Draper
Major consultants and experts:
Simons, Li
& Associates
Simons, Li
Spronk Water
Engineers
Spronk
S.S. Papadopulos
& Associates
Papadopulos
Hydrologic
Consultants Inc.
HCI
Groeneveld
Resource Mgmt.
Groeneveld
Littlefield
Research
Littlefield
Prickett &
Associates Inc.
Prickett
Clearwater
Consulting Corp.
Clearwater
Franzoy
Consulting Inc.
Franzoy

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APPENDIX C

Moneys Used On *Kansas v. Colorado* That Were Originally Budgeted for Other Purposes

In five fiscal years, the Attorney General's Office has used moneys for *Kansas v. Colorado* other than those specifically appropriated for the lawsuit. The amounts and the funds from which those moneys were spent are specified below. The Office replaced the two largest amounts ($900,000 in fiscal year 1991 and $300,000 in fiscal year 1997) in the fund of origin when supplemental appropriations were received.

Fiscal Year:

1990

$147,000 was transferred into the water rights litigation fund:
- $30,000 from other operating expenses
- $40,000 from salaries and wages
- $27,000 from the litigation costs fund
- $50,000 by executive order from an unused litigation fund

$45,777 was used from the tort claims fund to defend counterclaims Colorado made

1991

$900,000 was transferred into the water rights litigation fund from the salaries, wages, and other operating expenses fund. Early in the 1991 legislative session, a supplemental appropriation of $900,000 repaid that fund.

$112,500 was used from the court cost fund. That amount had been donated for *Kansas v. Colorado* by ditch associations, an individual, and a company.

$61,133 was transferred into the water rights litigation fund from a fund for other operating expenditures for antitrust litigation

1992

$50,000 from salaries, wages, and other operating expenses was used to pay the Special Master

$10,000 from the litigation costs fund was used to pay the Special Master

1993

$5,000 from the litigation fund was spent on water rights litigation

1997

$300,000 was "borrowed" (moved using a journal voucher rather than a formal transfer) from operating expenditures and replaced when a supplemental appropriation was received

$1,631,410 total

APPENDIX D

Contracts Approved, 1/1/95 through 6/30/97

This appendix lists the contracts with outside attorneys approved since Attorney General Stovall took office in January 1995. Many of the contracts were originally entered into by the previous Attorney General, Robert Stephan, and the firms simply were retained by Attorney General Stovall to complete the case. Contracts initiated under Attorney General Stovall are shown in italicized typeface.

The appendix shows the reason the case was contracted, the rate of pay for the outside attorney, the name of the firm handling the case, and the case name. It also shows the amount paid to the law firms in fiscal years 1995, 1996, and 1997, and contributions the firm or its members made to Attorney General Stovall's 1994 election campaign.

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Contracts Approved, 1/1/95 through 6/30/97

Reason for Contracting Case	Hourly Rate of Pay	Name of Firm	Case	Total paid per case, FY95 - FY97	Total paid per firm, FY95 - FY97	*****Contributions****** from the firm	from members	total
Firms that contributed to Carla Stovall in the 1994 election:								
Conflict	*85*	*Advocates Group, The*	*Tonkovich v. Kansas Board of Regents et al.*	*94,093.85*	*94,093.85*	*0*	*250*	*250*
Conflict	*85*	*Bennett, Lytle, Wetzler, Martin & Pishny, L.C.*	*Tonkovich v. Kansas Board of Regents et al.*	*113,530.54*	*114,290.29*	*1,210*	*1,550*	*2,760*
Expertise	75	Bennett, Lytle, Wetzler, Martin & Pishny, L.C.	Rice v. Garrison District Court	759.75				
Conflict	*85*	*Carpenter, P.A.*	*Jacka v. Board of Agriculture*	*8,745.97*	*8,745.97*	*1,000*	*2,000*	*3,000*
Conflict	*85*	*Depew & Gillen, L.L.C.*	*Jimmy Jestes v. Robert C. Hannigan*	*6,446.84*	*6,446.84*	*0*	*693*	*693*
Expertise	*255*	*Dickstein, Shapiro, Morin & Oshinsky*	*State of Kansas v. Leroy Hendricks*	*63,350.81*	*63,350.81*	*500*	*1,000*	*1,500*
Conflict	*85*	*Entz & Chanay*	*Tonkovich v. Kansas Board of Regents et al.*	*31,855.33*	*31,855.33*	*3,442*	*3,000*	*6,442*
Expertise	*Contingency*	*Entz & Chanay; Scruggs et al.; Ness, Motley et al.*	*Kansas v. R.J. Reynolds Tobacco Company*	*contingency*				*0*
Conflict	*85*	*Foulston & Siefken, L.L.P.*	*Luckey v. Jerry & University of Kansas*	*38,906.84*		*0*	*500*	*500*
Conflict	*85*	*Foulston & Siefken, L.L.P.*	*Tonkovich v. Kansas Board of Regents et al.*	*57,162.81*	*96,069.65*			
Time	75	Gilliland & Hayes P. A.	Russell Geis v. Kansas Parole Board	0.00		0	225	225
Time	75	Gilliland & Hayes, P.A.	Charles M. Torrence v. Kansas Parole Board	133.50				
Time	*75*	*Gilliland & Hayes, P.A.*	*Kennedy v. Neuenschwander & Laws Zidek*	*5,149.47*	*5,282.97*			
Time	85	Goodell, Stratton, Edmonds & Palmer	Karr v. Adjutant General of the State	1,300.50	1,300.50	1,000	400	1,400
Conflict	75	Ireland, Lawrence	Marsh v. Koenig et al.	3,441.66	3,441.66	0	2,400	2,400
Time	75	Jeter & Moran	Schbley v. Fort Hays State University et al.	243.61	243.61	0	50	50
Conflict	*85*	*Martin, Pringle, Oliver, Wallace & Swartz, L.L.P.*	*Kansas State Troopers Assn. et al. v. Frahm et al.*	*7,234.19*		*500*	*300*	*800*
Conflict	*85*	*Martin, Pringle, Oliver, Wallace & Swartz, L.L.P.*	*Tonkovich v. Kansas Board of Regents et al.*	*38,113.73*	*45,347.92*			
Conflict	*85*	*Mayfield, Bruce D.*	*Tonkovich v. Kansas Board of Regents et al.*	*33,825.87*	*33,825.87*	*0*	*50*	*50*
Conflict	*85*	*McAnany, Van Cleave & Phillips, P.A.*	*O'Connor & Co. et al. v. KS Public Employees Retirement*	*22,371.26*		*0*	*210*	*210*
Time	*75*	*McAnany, Van Cleave & Phillips, P.A.*	*Johnson v. Kansas Supreme Court*	*8,072.71*				
Conflict	*85*	*McAnany, Van Cleave & Phillips. P.A.*	*Kansas State Troopers Assn. et al. v. Frahm et al.*	*19,044.71*	*49,488.68*			
Conflict	*85*	*Morris, Laing, Evans, Brock & Kennedy, Chtd.*	*Little & Miller, Chtd. v. Sebelius & Workers Comp. Fund*	*47,367.94*		*0*	*700*	*700*
Conflict	*85*	*Morris, Laing, Evans, Brock & Kennedy, Chtd.*	*UKMC Heart Transplant Program*	*256,435.07*	*303,803.01*	*0*	*0*	
Expertise	*135*	*Morrison & Hecker*	*University of Kansas & KUMC (Pedicle Screw)*	*193,609.61*	*193,609.61*	*100*	*787*	*887*
Conflict	*85*	*Perry, Hamill & Fillmore, L.C.*	*Tonkovich v. Kansas Board of Regents et al.*	*60,728.50*	*60,728.50*	*959*	*1,100*	*2,059*

Expertise	*85*	*Polsinelli, White, Vardeman & Shalton, A.P.C.*	*Crandall v. Pierce, et. al.*	*0.00*		1,500	4,424	5,924
Expertise	*85*	*Polsinelli, White, Vardeman & Shalton, A.P.C.*	*KNRC v. Browner*	*81,929.29*	*81,929.29*			
Conflict	75	Porter, Fairchild, Wachter & Haney, P.A.	Marsh v. Koenig	5,996.85				0
Conflict	*85*	*Porter, Fairchild, Wachter & Haney, P.A.*	*Peters*	*1,839.25*	*7,836.10*	*0*	*0*	
Combination	85	Sloan, Listrom, Eisenbarth, Sloan & Glassman, L.L.C.	Kathy L. Kaul v. Robert T. Stephan	6,946.79		2,000	500	2,500
Combination	*85*	*Sloan, Listrom, Eisenbarth, Sloan & Glassman, L.L.C.*	*McCue v. Kansas Dept. of Human Resources et al.*	*92,646.76*				
Combination	85	Sloan, Listrom, Eisenbarth, Sloan & Glassman, L.L.C.	Phelps et al. v. Hamilton et al. (Phelps I)	216,275.52				
Conflict	*85*	*Sloan, Listrom, Eisenbarth, Sloan & Glassman, L.L.C.*	*Hamilton Case No. A6577*	*21,370.51*				
Conflict	85	Sloan, Listrom, Eisenbarth, Sloan & Glassman, L.L.C.	Marsh v. Koenig et al.	9,204.36				
Expertise	85	Sloan, Listrom, Eisenbarth, Sloan & Glassman, L.L.C.	Hobart Hayes v. Kansas Department	586.50	347,030.44			
Interest	*Contingency*	*Sprague, Dale & Thomas Brill*	*NASDAQ Market-Markers Antitrust Litigation*	*contingency*		*0*	*950*	*950*
Combination	85	Wright, Henson, Somers, Sebelius, Clark & Baker	Connelly et al. v. State of Kansas et al.	15,964.35		0	200	200
Expertise	*95*	*Wright, Henson, Somers, Sebelius, Clark & Baker*	*William G. McShane, Kansas Civil Service Board appeal*	*9,986.50*	*25,950.85*			
Firms that didn't contribute to Carla Stovall in the 1994 election:								
Conflict	*Expenses*	*Arent, Fox, Kinter, Plotkin & Kahn*	*Tonkovich v. Kansas Board of Regents et al.*	*8,336.14*	*8,336.14*	*0*	*0*	*0*
Expertise	*Contingency*	*Berger & Carmody*	*Estate of Lester L. Copley, Deceased*	*contingency*		*0*	*0*	*0*
Conflict	85	Glaves, Irby & Rhoads	Fritts & Fritts v. Horner	5,722.95	5,722.95	0	0	0
Conflict	75	Harper, Hornbaker, Altenhofen & Opat, Chtd.	Workers Compensation Claim of Fletcher Bell	1,067.03	1,067.03	0	0	0
Expertise	85	Holbrook, Heaven & Fay	Parra v. Board of Regents	5,072.80	5,072.80	0	0	0
Expertise	*85*	*James L. Daniels, Richard L. Colbert & Associates*	*Kansas Animal Health Dept. v. McCall*	*2,634.80*		*0*	*0*	*0*
Expertise	*85*	*James L. Daniels, Richard L. Colbert & Associates*	*Rice v. Behavioral Sciences Regulatory Board*	*4,452.63*	*7,087.43*			
Expertise	*235*	*Mayer, Brown & Platt*	*Zipper et al. v. Todd et al.*	*177,380.21*	*177,380.21*	*0*	*0*	*0*
Expertise	*150*	*McAllister, Steve - KU School of Law*	*State of Kansas v. Leroy Hendricks*	*65,310.74*	*65,310.74*	*0*	*0*	*0*
Expertise	145	Montgomery & Andrews	Kansas v. Colorado	1,802,084.02	1,802,084.02	0	0	0
Expertise	*Cont*	*Peck, Martin J*	*KS v. Network Billing Centers*	*contingency*		*0*	*0*	*0*
Combination	85	Reals & Weber	Schbley v. Fort Hays State University et al.	3,549.60	3,549.60	0	0	0
Expertise	*85*	*Rowe & Anstaett*	*Blue Cross and Blue Shield of Kansas v. Stovall*	*22,998.24*	*22,998.24*	*0*	*0*	*0*
Time	75	Sebelius & Griffiths	Steven Wickwire v. Kansas Parole Board	896.72	896.72	0	0	0
Time	250/case	Sebelius & Griffiths	Kansas Parole Board	0.00				
Time	85	Smithyman & Zakoura, Chtd.	Ballou v. KU Medical Center	807.50	807.50	0	0	0

italics indicate contracts initiated under Attorney General Stovall
plain type indicates contracts initiated under Attorney General Stephan that continued under Attorney General Stovall

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APPENDIX E

Agency Response

On September 19th, we provided a copy of the draft audit report to the Attorney General's Office. The Attorney General's response is included as this appendix.

State of Kansas
Office of the Attorney General
301 S.W. 10TH AVENUE, TOPEKA 66612-1597

CARLA J. STOVALL
ATTORNEY GENERAL

September 26, 1997

MAIN PHONE: (913) 296-2215
CONSUMER PROTECTION: 296-3751
FAX: 296-6296

The Honorable Eugene Shore
Chairman, Legislative Post Audit Committee
6788 E. Road 24
Johnson, Kansas 67855

Barbara Hinton, Legislative Post Auditor
Legislative Division of Post Audit
800 SW Jackson Street, Suite 1200
Topeka, Kansas 66612-2212

RE: Legislative Post Audit Report of Attorney General's Expenditures for Water Rights Litigation and Procedures for Selecting Attorneys, 97PA59

Dear Mr. Chairman and Post Auditor:

As you know, for the last four months the Post Audit Division has been auditing the Attorney General's Office. Scores of interviews have been conducted; tens of thousands of documents have been examined; events and records dating back 15 years have been reviewed. It has been a very exhaustive process. The findings of Post Audit Division's draft report are as I could have predicted on the day the audit was commenced -- no evidence of wrongdoing or conflict of interest in the manner in which I have awarded legal contracts exists.

While specific comments regarding the report follow below, I would especially note these Post Audit findings:

1. In the *Kansas v. Colorado* litigation, **none** of the attorneys or experts have ever contributed a **dime** to my political campaign.

2. The increase in the Attorney General's Office budget over the last three years was caused primarily by increases in **Federal grant programs** for crime victims and children, and were grants Governor Graves authorized me to administer.

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3. The Attorney General's Office contracts out very few cases to private attorneys -- **less than 1 percent** of the total cases for which I am responsible.

4. I have instituted a **new billing review system** which I predict will help reduce the amount the State pays outside counsel.

5. **No hint of violation** of the State's conflict-of-interest laws has been found.

6. **More than a third** of the private law firms hired since I took office contributed to my political **opponents**.

7. **More than 90 percent** of the attorneys and law firms that did make campaign contributions to me did not receive State contracts.

8. Most of the money paid by my Office to outside counsel went to lawyers who have **never contributed** to my political campaign.

9. The draft report recommends that we establish an **expensive bureaucratic process** to select attorneys; I believe the citizens of Kansas elect the Attorney General to exercise professional legal judgment in determining who will defend and prosecute for the State.

10. The process recommended by the draft report is designed to help attorneys seeking State business; I believe instead **my duty as the Attorney General is to the State and its taxpayers, not the attorneys.**

As to the specifics of the report, I will address them by category.

KANSAS V. COLORADO

I would note the most important fact - **WE ARE WINNING!** For nearly a century Colorado had been stealing water and, despite years of effort, no one could stop them -- until the Attorney General's Office sued them in the United States Supreme Court. That stopped them! To succeed it has taken not just this Office, but the attorneys, hydrologists, engineers, economists, historians and farmers who worked directly on the case. It has also taken the four Governors who have supported this litigation *and* the legislative leadership who has supported this litigation. Elected officials like John Carlin, Mike Hayden, Bob Stephan, Charlie Angell, Bill Bunten, Gus Bogina and Dave Heinemann all were instrumental in securing this victory. Those current elected officials who sit on the House Appropriations Committee and the Senate Ways and Means Committee, as well as both houses' Energy and Natural Resources Committees, have continued that service and have consistently supported the case.

The cost of securing tens of thousands of acre feet of water each year from Colorado has not been cheap. In the first *Kansas v. Colorado* suit the United States Supreme Court ruled that such suits were a substitute for war. *Id.* at 185 U.S. 125 (1902). Modern water wars are expensive and time consuming, but the alternative is to stand by silently and allow another state to take our water to the detriment of the jobs and families depending on that water. To me this is not an acceptable alternative.

Since 1993 the Attorney General's Office budget requests for the *Kansas v. Colorado* litigation have been on target. The Governor's Budget Office and the Legislature, years before I came into office, adopted a policy of partially funding the litigation for the upcoming year with the clear understanding that the Office should come back for a supplemental appropriation in the following session. That policy allowed the Governor and Legislature to exercise more control over the suit and the budget as a whole. Considering the results of the litigation, I do not understand the reason for criticism. But if there is criticism, it should be directed at those who set the amount of appropriations. My predecessor and I have always asked for the full amount of funding the litigation was estimated to cost, but, of course, we had to accept partial funding and return for supplementals.

KANSAS V. NEBRASKA

As to the possible suit against Nebraska over its violations of the Republican River Compact, I will ask the Legislature for a joint resolution concurring that I file suit. I will submit a budget which assumes Nebraska will vigorously oppose our suit. I will continue to brief any Legislative committee or Executive Branch agency that wishes to examine the pros and cons of such litigation. I am scheduled to present information to the Energy and Natural Resources Committee on October 2nd detailing my recommendations regarding a lawsuit over this issue. Without a joint resolution ensuring the Legislature's willingness to fund the lawsuit, I will not file suit against Nebraska over its violations of the compact.

FEDERAL GRANTS
DOMESTIC VIOLENCE, CHILD ABUSE AND CRIME VICTIMS

For too long government's response to the victims of crime was sporadic and diffused. I strongly believe the victims of crime are entitled to the support of their government. Because of this I have been pleased to accept responsibility from Governor Graves for those federally funded programs which seek to aid our most victimized and vulnerable citizens. I knew this would cause growth in the Office and that it could be used against me politically, but the good that comes from a centralized program was too great to be overcome by political concerns.

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I have responsibility for administering the following grant programs, most of which are federally financed: Violence Against Women and Children, Safe and Drug-Free Schools and Communities, Victims of Crime Act, Protection from Abuse Fund, Family Violence and Prevention Services, Rape Prevention and Crisis Intervention Services, Rape Prevention and Education, Crime Victims Assistance Fund, Crime Victims Assistance Fund for Child Abuse and Neglect, and the Child Exchange and Visitation Center Program. These programs have helped thousands of Kansans who have been victimized by crime, and many of these programs can and do help in preventing crime.

In addition, I have maintained and strengthened the Attorney General's traditional role of prosecuting criminals. I have improved the prosecution capability of the Office. As a result of implementation of an attorney salary equity plan, my Criminal Litigation Division is now fully staffed with experienced career prosecutors. I have hired death penalty prosecutors and successfully prosecuted the first death penalty case in Kansas in decades. I have successfully defended the Sexually Violent Predator Act in the U.S. Supreme Court. Taking responsibility for these significant public policy enactments of the Legislature has cost money, but these expenditures have resulted, again, in success.

Another area in which my Office has seen growth is the federally mandated Medicaid Fraud and Abuse Division. This Division was created in response to federal legislation which threatened to stop the federal government's share of Kansas' Medicaid payments. Not creating the division could have cost the State hundreds of millions of dollars! Medicaid fraud and abuse divisions across the country consistently have been placed in the Offices of Attorneys General.

The Kansas Medicaid Fraud and Abuse Division was created in 1995 and is financed with both Federal and State dollars. It has already recovered more money for the State General Fund than the State has expended to fund it! I remain proud of this Division and will not be embarrassed that it has necessarily caused growth in my Office.

Nearly **80 percent** of the increase in my Office's budget has been financed with Federal grants and State-collected fees. While not every improvement can pay for itself like the Medicaid Fraud and Abuse Division, every increase in my budget has resulted in better service to the taxpayers.

SELECTION OF OUTSIDE ATTORNEYS

The State is subjected to various types of lawsuits. Hundreds of lawsuits in both Federal and Kansas courts are filed against it or its employees every year. These suits involve civil rights complaints, torts, contracts, bankruptcies, products liability, medical malpractice and challenges to the decisions of the Legislature, the Governor or Kansas courts.

In addition, the State sometimes must bring suit to protect its rights or enforce its laws. Such suits may be brought under the antitrust and consumer protection laws, the open meetings and records acts, numerous administrative regulations or even the Constitution itself. Finally, of course, the Attorney General can bring criminal charges against persons believed to have violated State criminal laws. Those cases include capital murder and drug trafficking.

In more than **99 percent** of the cases for which the Attorney General is responsible, a full-time Assistant Attorney General is assigned to the case. However, there are times when outside counsel must be retained. In FY 97, over 1,600 case files were opened in my Civil Litigation Division alone, while only 14 new contracts with outside law firms were entered into by the Office of Attorney General.

In more than **95 percent** of the cases in which outside counsel is retained, the State or one of its agencies or employees is the defendant. After State employees are served with process (the formal delivery of a lawsuit), they may make a written request for representation to the Attorney General pursuant to K.S.A. 75-6108 (e). If the written request is received by the Attorney General within 15 days of the date of service, the State is generally obligated to represent that person.

A lawsuit normally must be responded to within 20 days of service of process. This often leaves me with only a few days to respond to the suit or hire outside counsel. If the suit includes a prayer for injunctive relief, the response time can be reduced to less than 24 hours. In the defense of State employees, there is simply no way a complicated and lengthy bidding process can provide the services needed.

As to those cases in which the Attorney General's Office has used outside counsel to bring suit, the attorneys retained either brought the idea to the Attorney General or were selected after discussions with numerous firms. For example, in *Kansas v. Colorado,* a Kansas Bar Association statewide water law seminar was used to invite Kansas lawyers to apply for the position of Special Water Counsel to head the litigation. In the Oil Overcharge Cases, in which the State has collected over $50 million in the past two decades, Attorney General Stephan selected the Washington D.C. law firm that approached him with the idea for the suit.

In cases in which outside counsel must be retained, with the advice of staff I select a law firm which I can professionally recommend. This recommendation is based not only on location, expertise and office infrastructure, but is also based on the requests of the client and on trust and confidence. Civil litigation is a very personal and traumatic experience for the person being sued. Defendants face possible dire financial, political and social consequences. In any case before the court, the State faces not only the possible financial impact of an adverse judgment, but limitations on the legislative and executive branches' authority by Federal and State courts.

Under the current system, I consistently have selected law firms of the highest Martindale-Hubbell ratings at hourly costs below those found by Kansas and Federal courts to be market value. The Kansas law firms hired, such as Wright-Henson, Polsinelli-White, Berger & Carmody, Depew & Gillen, Morris-Laing, Morrison & Hecker, Foulston & Siefkin, Bennett-Lytle, Martin-Pringle, and Entz & Chanay are excellent firms. The national firms selected, such as Ness-Motley; Mayer, Brown & Platt; Dickstein, Shapiro & Morin; and Montgomery & Andrews enjoy national and even international reputations. The selection of high quality firms gives the State its best chance to prevail in litigation.

It is currently the public policy of Kansas, as expressed by the Governor and the State Finance Council, to vigorously defend any and all legal actions brought against the State. Unlike an insurance company, Kansas never settles suits brought against it unless its leadership believes that a reasonable jury could find that the State or its employees did wrong. The settlement of lawsuits is seen as an important policy decision and not solely a financial decision.

So long as the State maintains this policy, it will need to continue to hire the best attorneys it can get. The decision as to whom those attorneys are should be left with the State's elected Attorney General who has been selected by the people as the State's Chief Attorney. Post Audit in its draft report states: "Selecting attorneys to handle lawsuits for the State is clearly a professional judgment call." The selection of outside attorneys has been and should remain a professional legal decision, not a bureaucratic process.

COST OF OUTSIDE ATTORNEYS

As with all too many things, the cost of outside attorneys has been increasing. When I took office I wanted to reduce the cost of outside counsel without compromising the quality of legal services. This is not easy to do. I cannot usually pick the cases we will defend, and I cannot retain a case in-house if the Supreme Court Rules dictate that I not be involved due to a conflict or the client's need for specialized counsel.

Since taking office the State has been faced with some extraordinary litigation. The *KUMC Heart Transplant Program* cases, *The Pedicle Screw* cases, *Phelps v. Hamilton, Zipper v. Todd, et al.*, and *Tonkovich v. Board of Regents, et al.*, are all examples of extraordinary cases which are expensive to defend. Because of such cases, the Office has not yet met my goal of reducing outside attorney costs. However, I have instituted two new programs which I believe, given time, will reduce costs.

In my first year as Attorney General I secured permission from the Legislature to hire two full-time staff attorneys, and at the suggestion of the Legislature used Tort Claims Fund money to

pay their salaries. The idea is that a staff attorney can be used full time, reducing the hourly cost to less than a third of an $85-an-hour outside attorney. That program has worked. No new case in my administration has been referred to outside counsel because the attorneys on staff did not have time to take the case as had happened in prior administrations. In addition, the hiring of experienced in-house lawyers has helped the State prevail in cases in which the plaintiffs were asking for very large sums of money.

In my second year as Attorney General I initiated planning, and have now implemented, a new legal services billing review using a company known as Examen, Inc. This national company specializes in auditing legal bills. To date, most of its clients are large insurance companies and other corporations. While it is too early to tell if Examen will save the State money, it has allowed us to develop and apply consistent standards for the independent review of all of our legal billings. Both Post Audit and I are hopeful that Examen will produce favorable results.

I DON'T PLAY FAVORITES

When selecting outside legal counsel for a person or agency I think only of one thing, **THE CLIENT.** I served on the Kansas Parole Board for four years. During that time I was sued on a regular basis by inmates. I know the feeling of being unjustly sued, and I know the comfort of being defended by the Attorney General's Office. I would never jeopardize a client by selecting any attorney who was not, in my judgment, the right lawyer for the job.

I do not have an interest in any private law firm. Legislative Post Audit did not find a hint of any violation of any of the State's conflict of interest laws. The record shows that most of the money spent on outside lawyers hired by my Office went to attorneys who did not contribute to my political campaign.

The attorneys I retained are winning *Kansas v. Colorado.* I believe the attorneys I hired for the *Tobacco Litigation* will prevail over the big tobacco companies and win that case. The lawyers I hired or retained who happened to have made campaign contributions to me have won *Rice v. Garrison*, won *Jestes v. Hannigan*, won *Kansas v. Hendricks*, won *Geis v. Kansas Parole Board,* won *Schbley v. Fort Hays State University, et al.*, won *Torrence v. Kansas Parole Board*, won *Karr v. Adjutant General*, won *Marsh v. Koenig*, won *Kaul v. Stephan*, and won *Hayes v. Kansas Department of Human Resources*. Combined, the plaintiffs in these cases were seeking millions of dollars against the State -- and these lawyers successfully defended the State's interests and, consequently, the State paid nothing in money judgments.

I cannot promise that we will win every case. I do promise that I will always do my best to select those attorneys who will provide the best defense possible.

COST VERSUS APPEARANCE

The draft report's conclusions and recommendations are based on the belief that the people are suspicious of any State contracts which have even the appearance of favoritism. Post Audit acknowledges that "[s]electing attorneys to handle lawsuits for the State is clearly a professional judgment call." The Post Audit acknowledges that it would be difficult for an Attorney General never to have known the attorneys with whom he or she contracts; yet, it suggests that the solution to this suspicion is a bureaucratic procedure.

How much will Kansans have to pay for this bureaucratic procedure? I am afraid that the amount will surprise people. The cost will be increased attorneys' fees, a larger bureaucracy, increased litigation and greater money judgments against the State.

The draft report suggests that it should be a goal of the Office to hire as many different attorneys and law firms as possible. This will increase the cost of attorneys' fees and possibly lead to greater money judgments against the State. The State has special immunity defenses not available to the private clients. The defenses contained in the 11th Amendment, the Kansas Tort Claims Act, the Kansas Act for Judicial Review and Civil Enforcement of Agency Actions, the Kansas Administrative Procedures Act, Judicial Immunity, Legislative Immunity, and Qualified Immunity are defenses which are unique to government. If we pay attorneys $85 an hour to learn these defenses and then refrain from hiring them again, at best we will see increased costs in educating lawyers and unnecessary discovery; at worst we will see them fail to properly use these defenses leading the State to pay more in money judgments.

A larger bureaucracy would result from the draft report's plan. Additional professional and clerical staff time and other operating expenditures would be required. Publishing notices, investigation and evaluation of applicant qualifications, maintaining lists of applicants by numerous legal categories, and developing, maintaining and defending detailed rationale regarding the selection and non-selection of attorneys all would add to the costs of contracting with outside counsel. The draft report's plan would not be inexpensive.

As attorney for the State I must warn the committee that any and all information collected at State expense most likely will be used against the State in lawsuits. All hiring decisions will be subject to State and Federal court review, both by the attorneys not hired as well as by defendants who are provided coverage under the Tort Claims Act and allege they were not provided with adequate legal counsel.

In addition to the above, it should be noted the draft report's recommendations are based on models from the Board of Indigent Defense Services and Insurance Department, where it says cases are rotated in alphabetical order by region among interested and qualified attorneys whose names are kept on lists. These models for handling large numbers of similar, generally less

complex cases simply are not appropriate for use in defending the State against the relatively few highly complex and varied claims that I have contracted out.

There simply is no comparison between Second Injury Fund administrative actions and litigation such as that filed by members of the Phelps family against District Attorney Joan Hamilton or by former KU law professor Tonkovich against 32 other KU faculty and administrators. Nor is there any comparison between the cases my Office handles and indigent criminal defense, which is the bread and butter of many recent law school graduates, and which is work performed largely as a public service by more experienced attorneys who otherwise would command much higher hourly rates.

The State, its taxpayers and officials who are sued deserve and should expect the best defense possible, if for no other reasons than to limit the payment of unnecessary judgments and to discourage the filing of otherwise frivolous litigation.

For the reasons stated above, it is both my policy and legal advice to the Legislature that the draft report's recommendations not be adopted.

ATTORNEYS CONTRIBUTED MORE TO THE INSURANCE COMMISSIONER

The real concern of the draft report centers around campaign contributions to elected officials. It cites the Insurance Department as an example of a bureaucratic model that could be of benefit. This made us curious to see if the Insurance Department had developed a system to prevent lawyers who had contributed to the Commissioner's campaign from contracting with the Department.

Attorneys and their firms who have received payments for legal work by the Insurance Department contributed at least $33,750 to the current Insurance Commissioner's 1994 campaign. This is **more** than the amount reported by Post Audit as contributed to my 1994 campaign from lawyers who received contracts from the Attorney General's Office.

Has the Insurance Department's process, which was recommended by the draft report, made a difference regarding the reality that some attorneys who do business with the State also have made contributions to the campaigns of statewide elected officials? The answer clearly is "NO."

WHO SHOULD BENEFIT – ATTORNEYS OR THE PUBLIC

Another question raised by the draft report's recommendations is who should benefit from the selection of outside counsel by the Attorney General. The draft report maintains that the bureaucratic procedure suggested would "help ensure that all interested and qualified attorneys are considered for work to be contracted out," and that "rotating the work among the interested and qualified firms appears to be desirable because it can give more firms an opportunity to participate in State business."

I do not issue contracts for legal representation required by the State or its employees in order to benefit attorneys. My sole duty is to the State and our clients. The idea that I would not continue to use an attorney or law firm that had been successful in the past makes no sense to me. The best indication of future performance is past performance. I know of no reasonable person or business that would abandon a proven winner in order to conduct an ongoing experiment with new lawyers for each case.

STATEMENTS OF SUBSTANTIAL INTERESTS

The draft report implies that an insufficient number of my staff file statements of substantial interests. My Office has followed the requirements of State law, specifically K.S.A. 46-247, -282, -283 and -285, in determining who among my employees should file statements of substantial interests. Under the law, defined "designees" are required to file statements of substantial interests with the Secretary of State. "Designees" include "major policy making" positions (also defined to include department or division heads), persons responsible for contracting and procurement, persons responsible for drafting agency contract specifications, persons responsible for awarding grants and persons responsible for licensing and regulating businesses and individuals.

Eighteen officers and employees within the Office of Attorney General file statements of substantial interests. These persons are carefully selected under the criteria set out in K.S.A. 46-282. The list includes myself, board members, administrative staff, Deputy Attorneys General who head Office divisions and Assistant Attorneys General where their duties arguably meet the criteria to be a designee. The Commission on Governmental Standards and Conduct is authorized to request that we ask additional staff to file if it believes they should be added. No such request has ever been received.

I believe it is clear that my staff is in compliance with this law. Since those who do not file are not responsible for the duties set out in K.S.A. 46-282, I see no benefit in naming them as designees. In addition, there are Assistant Attorneys General who regularly prosecute murderers and drug dealers. I believe it would be dangerous to require them to publicly list their addresses and identity of family members. I would oppose any such listing for those reasons.

CONCLUSION

I have throughly reviewed the draft report, including its conclusions and recommendations. I have set out the many sections of the draft report with which I am in agreement. The scope of the audit became quite broad, and it really is only the recommendations which deal with the narrow area of procedures used to select outside counsel where I am in substantive disagreement with the draft report. I believe my reasons for disagreement are sound and well documented above.

I have been elected by the citizens of Kansas to exercise my professional legal judgment in defense and prosecution of legal actions on behalf of the State, its officers, employees, citizens and taxpayers. I will continue to exercise that judgment to the best of my ability and will decline to implement the suggestion that I adopt a bureaucratic process for selection of those who will defend and prosecute in the name of the Attorney General and the State of Kansas.

I am pleased that the report has set straight misinformation with regard to the *Kansas v. Colorado* litigation and the growth in programs and duties the Office of Attorney General has experienced in the past three years. I am pleased the report has substantiated the tremendous job I believe the Attorney General's Office has done for many years. I appreciate the hard work and professionalism of Post Audit staff, and I thank the Committee for this opportunity to respond to the draft report.

Very respectfully yours,

Carla J. Stovall

Carla J. Stovall
Attorney General

DRAFT 6/4/96
APPROVED BY CJS

STATE OF KANSAS
OFFICE OF THE ATTORNEY GENERAL
CARLA J. STOVALL

ENGAGEMENT AND CONTINGENCY AGREEMENT

AGREEMENT as of this 5th day of June, 1996 by and between the State of Kansas by Carla J. Stovall, Attorney General, "Attorney General" and the law firm of Hutton & Hutton, "Hutton & Hutton".

Whereas, cigarette smoking kills approximately 400,000 individuals each year in the United States more than the number of deaths caused by guns, drug use and automobile accidents combined;

Whereas, the cost to the State of Kansas and its citizens of health care and related expenditures for smoking related diseases exceeds tens of millions of dollars per year;

Whereas, any litigation involving tobacco-related industries is likely to entail numerous complex factual and legal issues;

Whereas, any such litigation will require the expenditure of substantial resources and attorney time;

Whereas, the Attorney General seeks to avoid the expenditure of state resources of direct costs and attorney time in any such litigation; and

Whereas, the Attorney General plans to bring an action against cigarette companies and related entities pursuant to her authority under the Common Law and Kansas Statutes Annotated

NOW THEREFORE, IT IS AGREED BY AND BETWEEN THE ATTORNEY GENERAL AND HUTTON & HUTTON AS FOLLOWS:

1. Hutton & Hutton is retained to provide legal services to the State of Kansas for the purpose of seeking injunctive relief, monetary relief (including, without limitation, damages and civil penalties) and other relief against tobacco industry companies and related entities ("defendants") in litigation arising from the advertising, marketing, manufacturing promotion, sale and/or distribution of cigarettes (hereinafter "the Litigation").

2. The Attorney General, as the chief legal officer of the State of Kansas, retains final authority over all aspects of the Litigation. As provided herein, Hutton & Hutton is authorized to take appropriate legal steps to prosecute the Litigation and participate in all settlement

negotiations and the State of Kansas and the Attorney General hereby further agrees not to settle this action without prior consultation with Hutton & Hutton.

3. The Attorney General may appoint members of her staff to monitor the prosecution of the Litigation. Hutton & Hutton shall consult in advance with and obtain the prior approval of the Attorney General, or her designee, concerning all significant matters related to the Litigation. Regular status meetings shall be held as requested by either the Attorney General or Hutton & Hutton.

4. It is specifically agreed by the parties that neither Hutton & Hutton or any third party employed whose services or products are used by either the State of Kansas or Hutton & Hutton in furtherance of this agreement or its goals, is not considered, or paid as a state employee, but is an independent contractor.

5. It is specifically agreed by the parties that any documents or any other tangible objects produced by Hutton & Hutton, or any third party employed pursuant to this agreement, which were produced or procured in the performance of this agreement, shall be the property of the State of Kansas.

6. Hutton & Hutton shall communicate with state agencies through the Attorney General, unless alternative arrangements are made in advance with the Attorney General. Where written communications from Hutton & Hutton to state agencies are authorized, the Attorney General shall be provided with copies of those communications.

7. Hutton & Hutton shall provide sufficient resources, including attorney time, to prosecute the Litigation faithfully and with due diligence. Hutton & Hutton may, with the prior expressed approval of the Attorney General, bring in additional counsel. Said counsel, will be obligated to observe all of the provisions of this agreement unless explicitly excused by the Attorney General.

8. The Attorney General, by this agreement designates Hutton & Hutton as lead national counsel, lead local counsel and lead trial counsel in the Litigation. The Attorney General retains the right, after a showing of just and good cause to revoke such designations and make new designations at any time.

9. The compensation, if any, paid to third parities pursuant to this agreement shall be the responsibility of Hutton & Hutton.

10. It is anticipated that additional private legal firms shall be needed in the representation of the State of Kansas in the Litigation. The Attorney General, after consultation and agreement by Hutton & Hutton, retains the right to add firms to the group of firms participating in the Litigation. Hutton & Hutton agrees that any firms added to the group conducting the Litigation shall share in such compensation, if any, as agreed upon by Hutton & Hutton and the new firm, subject to the approval of the Attorney General.

11. Hutton & Hutton agree to maintain contemporaneous time and expense records. Hutton & Hutton shall submit quarterly statements to the Attorney General setting forth for that period the hours and services devoted to the Litigation, and all disbursements.

12. Expense records and related documents maintained by Hutton & Hutton in connection with the Litigation shall be subject to audit by the Attorney General.

13. (a) The State of Kansas is not liable to pay any attorney fees in the event the litigation is unsuccessful. Hutton & Hutton's attorney fees, if recovered, are contingent upon a successful settlement and or judgement.

(b) Hutton & Hutton shall advance all expenses of the litigation, except for those funds appropriated by the Legislature for that purpose.

(c) If any recovery is obtained, all reasonable expenses advanced by Hutton & Hutton will be paid to the firm before the computation of attorneys' fees. During the pendency of the Litigation, the Attorney General agrees to petition the Kansas Legislature the funds needed for expenses in the Litigation. If the event no recovery is made by the State of Kansas, Hutton & Hutton agree to waive any legal claims that it might have against the State of Kansas, or any of its officers or employees for reimbursement of costs, reasonable expenses and attorney fees and submit the same to the Joint Committee on Special Claims Against the State for determination by the Legislature. The Attorney General agrees to support Hutton & Hutton's claims.

if waive, no right to make claim

14. The sole contingency upon which compensation is to be paid is the recovery and collection by Hutton & Hutton, on behalf of the State of Kansas, of monies in the Litigation, whether by settlement or judgment.

15. Compensation on the foregoing contingency shall be made in accordance with 1995 Kan. Ct. R. Annot. 226, MRPC 1.5 and shall not exceed 25% of the amount of money recovered by the State of Kansas in the Litigation. In accordance with 1995 Kan. Ct. R. Annot. 226, MRPC 1.5 (d) litigation and other expenses shall be deducted from the recovery before the contingency fee is calculated.

16. As used in this Agreement, the term "disbursement" shall include travel expenses, telephone charges, copying charges, fax charges, deposition costs, investigator costs, messenger service costs, mediation expenses, computer research fees, medical or nursing consultation fees, expert fees, other consultation fees and all other reasonable out-of-pocket costs incurred in the Litigation.

17. (a) Hutton & Hutton shall, to the extent allowed under the laws of the State of Kansas and subject to the approval of the Attorney General, attempt to recoup all expenses, costs and fees due them or the State of Kansas from the defendants in the Litigation.

(b) As to the court awarded or ordered expenses and costs, moneys actually recovered from the defendants for expenses and costs advanced by Hutton & Hutton shall be the property of Hutton & Hutton. It is the intent of the parties that such moneys recovered from the defendants be used to offset the expenses and costs due to Hutton & Hutton and that only such reasonable expenses and costs not recovered as such from the defendants be deducted by Hutton & Hutton from the recovery prior to the calculation of the contingency fee.

(c) As to attorneys fees awarded or ordered by the court to Hutton & Hutton for their services in the Litigation shall be considered in the evaluation of the reasonableness of Hutton & Hutton's continency fee. In addition, as to evaluation of the fee, both parties concur and agree that the Litigation is novel and extremely difficult; the skills requisite to perform the legal service in the Litigation are extraordinary; the 25% fee is customarily charged in similar litigation in other states; the experience, reputation and ability of Hutton & Hutton is extraordinary.

(d) If for any reason the parties are unable to agree to the reasonableness of the contingency fee, the matter shall be referred to the appropriate court having jurisdiction of the matter for determination pursuant to 1995 Kan. Ct. R. Annot. 226, MRPC 1.5 (e). In no event, however, will the total attorneys' fees exceed 25% of the recovery.

18. In the event the Litigation is resolved, by settlement or judgment, under terms involving the provision of goods, services or any other "in-kind" payment, the parties hereto agree to seek, as part of any such settlement, compensation for Hutton & Hutton equivalent to the 25% contingency fee and expenses to which Hutton & Hutton would be entitled under this Agreement. In the event the Attorney General is unable to secure such compensation. For Hutton & Hutton as part of any "in-kind" settlement, the Attorney General agrees to petition the Legislature to appropriate funds to reasonable compensate Hutton & Hutton.

19. Provided, further, that the provisions found in the Contractual Provisions Attachment (form DA-146a) attached hereto, are hereby incorporated in this contract and made a part hereof. In addition, Second Party shall incorporated the provisions of Form DA-146a into any contract with any third party.

20. Second Party agrees to abide by the provisions of K.S.A. 46-239(c) which states:

> Any individual within one year after the expiration of a term as a legislator, who contracts to perform any service for a state agency other than the legislature, shall not later than 10 days after the acceptance of such contract, file a disclosure statement as provided in this section. Any agency of the state of Kansas which enters into a contract with any legislator, or any member of a firm of which such legislator is a member, under which the legislator or the member of such firm is to perform services for such agency for compensation shall make a report on a form prescribed and provided by the commission giving the name of the state agency, the purpose of the employment and the method of determining and computing the compensation for such employment. All such forms shall be filed quarterly in the office of the secretary of state.

Further, Second Party agrees to notify First Party in the event K.S.A. 46-239(c) is applicable and assist First Party in fulfilling his/her reporting requirements.

IN WITNESS WHEREOF, the parties have hereunto set their hands the day and year first above written.

CARLA J. STOVALL
Attorney General of Kansas
Kansas Judicial Center, 2d Floor
Topeka, Kansas 66612
913/296-2215
913/296-6296 - Fax Number

First Party

Hutton & Hutton
8100 East 22nd Street North, Building 1200
P.O. Box 638
Wichita, Kansas 67226-2321
316/668-1166
316/686-1077 - Fax Number
Federal I.D. Number: _____

Second Party

APPROVED:

John W. Campbell
Sr. Deputy Attorney General

Neil A. Woerman
Director of Budget and Special Projects
Office of the Attorney General

June 5, 1996

SENT VIA FACSIMILE
TO (913) 296-6296
AND VIA REGULAR MAIL

Mr. John Campbell
Assistant Attorney General
2nd Floor, Judicial Center
Topeka, KS 66612-1567

Re: Cigarette Litigation

Dear John:

Thank you for your latest fee contract draft of June 4, 1996. Admittedly, we would rather work on the case than work on drafting the language of a contingent fee contract, but nevertheless please find enclosed our latest draft. The way the contract is being proposed by your office could lead to an open issue as to whether the contract is a contingent fee contract or a contract where a ceiling has been placed with no certainty as to what the fee may be. In other words, the proposed contract is one where the fee is uncertain and we would run the risk of not knowing what the percentage fee might be.

Due to the complexity, the high risk, and the necessity of getting other attorneys involved in this litigation, it may be difficult to encourage other stellar risk-takers to get involved without some certainty as to what the contingent fee really is. The total man- hours to be expended, the total cost to be expended, and the forbearance of other high risk opportunities in the successful prosecution of this matter really necessitates some certainty as to what the contingent fee would be. We are result-oriented and will make the sacrifices necessary to assemble the appropriate team to ensure that we give the tobacco cartel a hell of a fight. As Arlen Specter, the fine U.S. Senator from Pennsylvania and born and raised in Russell, Kansas, once said, "Hell hath no fury like a lawyer with a contingent fee contract."

We agree that MRPC 1.5(e) permits all fee contracts to be reviewed by the appropriate court and expect the same to apply in this instance. We would, however, like to start our relationship having the client agree that the proposed 25% fee is fair and reasonable.

We understand that the potential recovery in this litigation could be enormous. The risks, however, are likewise as enormous. We are willing to bear that risk whether this case takes a few years or a few decades. We are duty-bound to maximize the State's recovery of taxpayer dollars expended for smoking-related diseases and recognize the fee, like the recovery for the State, could be quite large. The more we recover for the State, the more we get paid as fee. That's the value of a contingent fee contract. The contingent fee is balanced against the attorney bearing the entire risk and, in our particular case, potentially spending millions and millions of dollars of time and money to maximize the client's recovery.

With that said, we would like some certainty that the State agrees that a contingent fee of 25% is fair and reasonable. We have made some changes to your latest draft, which I would encourage you to review and to discuss with us.

Very truly yours,

Mark B. Hutton

MBH/sm

12-2

Mark W. Hutton · †
Andrew W. Hutton

Derek S. Casey ·
Anne H. Pankratz
Christopher P. Christian
Chan P. Townsley ··

· Also Admitted in Oklahoma
·· Also Admitted in Missouri
† Certified Trial Advocate
National Board of Trial Advocacy

HUTTON & HUTTON

FAXED

Law Offices
8100 East Twenty-Second Street North, Building 1200
Wichita, Kansas 67226-2321
Mail: P.O. Box 638
Wichita, Kansas 67201-0638

General
(316) 688-1166
Facsimile
(316) 686-1077

Products Liability
(316) 686-1242
Facsimile
(316) 686-2049

Tax I.D.# 48-0966751

August 7, 1996

SENT VIA FACSIMILE
TO (913) 296-6296
AND VIA REGULAR MAIL

Ms. Carla Stovall
Attorney General
2nd Floor, Judicial Center
Topeka, KS 66612-1567

Re: Cigarette Litigation

Dear Attorney General Stovall:

I had a nice talk with John Campbell this morning and understand you have selected someone else to represent the State of Kansas in the Cigarette Litigation. Of course we are disappointed, but we will be working on other cigarette litigation as well. We wholeheartedly support your cause in this matter and if we can ever be of any help in the future please feel free to give us a call.

Incidently, we will also be involved in a Smokeless Tobacco class action out of state which seems to be very promising litigation. Unfortunately, the children seem to be the primary targets of the smokeless tobacco advertisements.

Best regards, I am

Very truly yours,

A. W. Hutton

Andrew W. Hutton

AWH/jjb

House Taxation
Date 2/15/00
Attachment # 13

ENTZ & CHANAY, P.A.
ATTORNEYS AT LAW

STEWART L. ENTZ
JEFFREY A. CHANAY
J. PHILLIP GRAGSON*

3300 SW VAN BUREN STREET
TOPEKA, KANSAS 66611
(913) 267-5004
FAX: (913) 267-7106

*ADMITTED IN KANSAS AND MISSOURI

July 31, 1996

Mr. John W. Campbell
Senior Deputy Attorney General
Office of the Attorney General
301 S.W. 10th Avenue
Topeka, Kansas 66612-1597

Re: *Tobacco Litigation*

Dear John:

Per our telephone conference, July 31, 1996, enclosed please find:

1. The draft Engagement Letter with Mr. Scruggs' amendments.
2. General information on the issue of naming Shook, Hardy & Bacon.
3. Rough draft of Petition prepared by Ness, Motley.

I again requested Steve Bozeman to have Jay Smith call you or Mary Horst.

Very truly yours,

Stewart L. Entz

sle/sja
cc: Mr. Scruggs
Mr. Bozeman
Mr. Baker

House Taxation
Date 2/15/00
Attachment # 14

LEGISLATURE OF KANSAS
LEGISLATIVE DIVISION OF POST AUDIT

MERCANTILE BANK TOWER
800 SOUTHWEST JACKSON STREET, SUITE 1200
TOPEKA, KANSAS 66612-2212
TELEPHONE (785) 296-3792
FAX (785) 296-4482
E-MAIL: LPA@postaudit.ksleg.state.ks.us

February 3, 2000

John Campbell, Senior Deputy Attorney General
Memorial Building
Topeka, Kansas 66612

Dear Mr. Campbell:

I'm providing you with all the materials from our working papers related to the Attorney General's selection of Entz & Chanay as the local counsel for the tobacco settlement litigation. These materials include the following:

- a page from our working papers that summarizes the legal arrangements for firms paid on contingency
- the engagement and contingency agreement between the Attorney General's Office, Entz & Chanay, and other law firms involved in the tobacco lawsuit
- the Attorney General's guidelines for contracts for legal services
- our interview notes and materials related to the process of selecting attorneys for the tobacco lawsuit

Please let me know if you have any questions about these materials, or if we can be of any more help.

Sincerely,

Barbara J. Hinton

Barbara J. Hinton
Legislative Post Auditor

enclosures

House Taxation
Date 2/15/00
Attachment # 15

Interview notes re: tobacco

C. Lash

John Campbell, Senior Deputy Attorney General, 8/27

Mr. Campbell said the reason they didn't go with Hutton and Hutton was twofold: first, Hutton and Hutton wanted the State to agree that a 25% fee was per se fair and reasonable; second, Hutton and Hutton are part of the Castano group, which filed a class action case in the 5th Circuit. Their emphasis is medical malpractice, and they normally represent plaintiffs.

The Attorney General first met with Scruggs, et.al. in late Spring, 1996. Per John's calendar, she was scheduled to meet with Mike Moore, the Mississippi Attorney General, on 4/28 to discuss Scruggs. The meeting didn't occur because bad weather prevented Mr. Moore's plane from landing. She initially met Mr. Scruggs in Chicago on 5/3 at a conference. They talked again in St. Louis on 6/8.

Morrison and Hecker and Don Barry were interested in pursuing the case, but didn't want to front the expenses.

If the current national settlement happens, the State won't pay anything to attorneys. There will probably be a national arbitration board, and every firm that thinks they have had a role in achieving the settlement can apply for compensation. A national settlement would take the place of the State contract. (In Florida, attorneys had $20 million in expenses. They spent 17,000 hours just to pick a jury).

Mary Barrier, Morrison & Hecker, 816-691-2600 (KCMO)

Ms. Barrier could not remember if the Atty. General's Office approached them, or if her office initiated the interaction. However, they put together a presentation in early spring for the AG's Office. They eventually decided they didn't want to be responsible for expenses that could potentially run so high. Several months later, the AG's Office contacted them about serving as local counsel, with Scruggs and Ness/Motley as national counsel, and with expenses to be worked out between local and national counsel. Members of Morrison & Hecker considered the offer, but decided they had a possible appearance of a conflict of interest and declined.

Don Barry, 273-3153 (Topeka)

Mr. Barry said he wasn't interested in being part of the audit. He said he wasn't contacted by the AG's Office about serving as local counsel.

Mark and Andy Hutton, Hutton & Hutton, 316-688-1166 (Wichita)

The Huttons said that through their involvement with the Castano Group they became interested in seeing Kansas enter into tobacco litigation. They sent Carla Stovall a letter on March 14, 1996 introducing themselves and expressing their interest. Within a few days, they got a call from John Campbell, and came up for an interview with John and the AG. They said they felt they were well-received, and told the AG they could finance the up-front expenses. They used Stu Entz as a reference, because Mark clerked for him while in law school. They said John Campbell called after the meeting and asked them to send him a proposed contract.

The Huttons were trying in the contracts to convince the AG that a 25% contingency fee was fair, although they said they indicated to the AG or John verbally that they would take less

House Taxation
Date 2/15/00
Attachment # 16-1

than 25%. The Huttons felt that having the phrase "up to.." in the contract was akin to not having a contract, that there was no guarantee of what you would be paid.

The Huttons said they had been talking with John Campbell a couple times each week when things suddenly dried up. John said the AG's Office had to do due diligence to see if there was anyone else out there who was qualified and interested. This went on all summer, with the Hutton's leaving messages and getting no response. Finally John Campbell called and said the Office was going to use Scruggs and Motley, with Entz & Chanay as local counsel. That surprised them, but they sent the AG a letter on August 7th saying they were glad she was going ahead with the litigation.

In the Huttons' opinion, whether or not local counsel for the case was in Topeka wasn't relevant--it might be convenient, but not necessary. They said you only go for court on pre-trial matters about once every three months, and noted that they travel all around the country for cases they represent.

Jeff Chanay, Entz & Chanay, 267-5004 (Topeka) 9/9/97

Mr. Chanay said that on 5/2/96 he attended a meeting of the Attorney General's Committee for Crime and Violence Prevention in Salina. He rode with Nancy Lindberg of the AG's Office. She mentioned that the Office was looking for counsel, and he said he would be interested in serving as local counsel. Mr. Chanay didn't know if Ms. Lindberg passed the information on to the AG, but about a month later General Stovall called to see if his firm would be interested in serving as local counsel. In late June or early July, they met with the AG briefly. She said she was considering Scruggs, et. al. and wanted Entz & Chanay to meet with him to discuss the theory of the litigation (that the State can be damaged, not just individuals, by the use of tobacco because the State provides health care to employees, Medicare recipients, prisoners, etc.)

Mr. Chanay said when they met with Scruggs he was trying to get more states to file lawsuits against the tobacco companies, and particularly states with Republican leadership (at that time, no "Republican" states had filed lawsuits, and he wanted to make it a bipartisan issue). Also, he wanted to get to a "critical mass" of states filing (15-20) in order to put more pressure on the tobacco companies. Entz & Chanay met with Scruggs again during July to discuss the mechanics of getting Kansas into tobacco litigation.

Mr. Chanay said they actually started work before the contract was signed, based on the Attorney General's representations to them. They hadn't talked about expenses, other than the fact that the State would not pay expenses on an ongoing basis. He said they didn't discuss expenses because in their excitement at taking on a case of this importance they weren't thinking about what expenses might run, and because they weren't aware of what their role would turn out to be. He said normally local counsel simply makes sure out-of-State lead counsel comply with Kansas law, gives the judge a chance to see familiar faces, and files all pleadings. As they worked with Scruggs on details of the agreement in early August, they began to realize how much expenses might be and told Scruggs they had some trepidation about the costs. Scruggs said between him and others there was plenty of money in the pot to cover expenses. Entz & Chanay asked that the contract state the lead counsel would pay expenses, and Scruggs agreed. The Attorney General was not involved in these negotiations. (Mr. Chanay said they have absorbed some expenses, such as traveling to meeting with other lawyers, but that they have been reimbursed other expenses such as filing fees and mailing charges.

Scruggs proposed the fee split contained in the contract, as well as the "up to 25%" figure. At that time, it was typical of what was in other states' contracts. The first 20 states took a big risk, because at that time there was no notion of a settlement. Since the Liggett settlement the whole situation has been perceived differently, and lawyers are accepting 10% contracts.

As the suit has evolved, Entz & Chanay has seen its role expand far beyond that of traditional local counsel. They have been responsible for drafting petitions, doing research, writing responses, and turning them into pleadings (all with consultation from Scruggs). They also took an active role in evaluating and filing the lawsuit against the Liggett Tobacco Co. (this is separate from the suit against the other tobacco companies). In addition, they serve as the repository for the documents gained from Liggett, and are responsible for reviewing and cataloging them.

Mr. Chanay cited several reasons he thought they were chosen as local counsel:
1. Trust. The lawsuit is a risky proposition, and the AG know the suit would be criticized on its theory and politics. Because she was casting her lot with out-of-State attorneys, she needed local counsel that wouldn't steer her wrong. In addition, the AG is in the suit to win, and she wouldn't have chosen them if she had concerns about their handling of it.
2. Medicaid experience. Mr. Chanay frequently works with nursing homes, representing them to the State and federal government on regulatory issues and reimbursement issues. He knows what types of documentation nursing homes and government agencies have available.
3. Legal research abilities. The AG and Mr. Chanay worked together on a casino gaming case. She is very comfortable with their research abilities.
4. Knowledge of the State system. Entz & Chanay have the background to work with State agencies to gather information. Mr. Chanay gave several examples of how this might be necessary, for example, in Mississippi, the tobacco companies made the State pull the archives of the universities to look for studies on tobacco, looked at corrections records to see if the state ever gave free cigarettes to inmates, and looked at state revenue records to see if the companies had been taxed more than the damages that might be due.

Finally, Mr. Chanay said if the litigation lasted over a number of years, his firm could receive 12.5% of whatever the State is awarded, subject to the judge's assessment of reasonableness. He thinks it is unlikely they would get that much. He said if the national settlement falls through, the tobacco companies would likely file for bankruptcy. Kansas's claims are unliquidated (they have never been tried in court), so they could simply be discharged by a judge. In addition, several large states are in line ahead of us for damages, including Texas and Minnesota. He said he is concerned Kansas won't get anything if a national settlement isn't approved.

From: CARLA STOVALL
To: campbelj
Date: 6/28/96 3:35pm
Subject: smoking

Jeff is very interested in getting involved with us. He understands the contract would say "whatever court awards." I wasn't sure what Skruggs wanted to do about expenses, but I think Jeff can live with either asorbing them initially or getting them paid thruough Skruggs. I told him that you'd tell Skruggs they were on board and Skruggs can get ahold of him. 913-267-5004.

Also told him we had to crawdad out of arrangment/discussions with Hutton&Hutton. I'll let you communicate with Huttons and Skruggs about the above. Thjanks.

Have a GREAT trip -- and be very, very careful. (I know, I sound like your mom. Your mom doesn't want to lose her son and I don't want to lose my Senior VITAL deputy.)

PS (You are wearing a helment aren't you???)

Richard Scruggs

601-762-6068 - off

601-990-0965 -

Get Alderson OK truck briefs for 10th Amendment for Michigan speech

16-4

SCOPE STATEMENT

Reviewing the Attorney General's Expenditures for Water Rights Litigation and Procedures for Selecting Attorneys

Since the beginning of the century, there as been an ongoing controversy between Kansas and Colorado with regard to the use of water from the Arkansas River. In 1949 the Arkansas River Compact was formed to deal with each state's rights. The Arkansas River Compact Administration was formed to administer the Compact.

In 1985, then Attorney General Stephan filed suit alleging Colorado had violated the Compact by increased post-compact well pumping. The original lawsuit sought only a decree commanding that the waters of the Arkansas River be delivered in accordance with the provisions of the Compact. However, in 1987, the U.S. Supreme Court ruled that money damages could be recovered in water compact enforcement cases. Kansas filed a motion to amend its complaint and was allowed to include money damages.

In 1995, the Supreme Court upheld the finding that Kansas should prevail in the lawsuit. The lawsuit currently is in the phase where the amount of damages will be determined.

Recently legislators have raised questions about the amount of money being spent on the lawsuit, who is being paid to perform work for the litigation, and how that work is being funded. Specifically, legislators are concerned that the Attorney General is using operating moneys to fund the lawsuit and thereby creating the need to come back to the Legislature with supplemental requests for operating moneys. There also is a concern that the law firms representing the State may be trying to claim part of the settlement, even though they've been paid in full for their costs to date. A performance audit of this topic would address the following questions:

1. **How much money has the Attorney General's Office spent to date on water rights litigation with the State of Colorado, and have those payments covered the full cost of the litigation?** We would interview appropriate officials in the Attorney General's Office, and review accounting records since the start of the water rights litigation to determine how much money has been paid to individuals or firms for work related to that litigation. As necessary, we would interview previous Attorneys General. We also would determine generally what services those individuals or firms provided, and the source of the moneys (special appropriations for the litigation, or operating moneys for the Attorney General's Office). Through reviews of timesheets or other documentation at the agency, or through interviews with employees as necessary, we would attempt to determine the cost of time spent by the Attorney General's own staff on the project during the past two years. Finally, we'd review any estimates the General has made regarding likely future costs of the litigation.

2. **What contractual agreements has the Attorney General's Office made with private attorneys?** By reviewing a sample of contracts with private law firms who have been hired

(over)

by the Attorney General's Office, we would determine what provisions have been made for their compensation and employment. As needed, we would interview the current and former Attorneys General, or principals of the contracting firms, to obtain clarification about the contractual provisions.

3. **Does the Attorney General's Office follow adequate procedures to prevent potential conflicts of interest when it hires private attorneys and law firms?** Through discussions with appropriate officials in the Attorney General's Office we'd determine what procedures are supposed to be followed in selecting law firms that do work on behalf of the State. We would review those procedures to ensure that they are adequate to prevent unwarranted bias in the selection of attorneys or firms. We also would review a sample of contracts with private attorneys or law firms to determine whether the Attorney General's Office followed its procedures for selecting those firms. As part of the audit, we'd review campaign finance reports filed by the Attorney General and identify any individuals or firms performing work for the Office that were campaign contributors. We also would review statements of substantial interest, employment records, or other records as needed to determine whether there were any beneficial relationships or previous employment relationships between the Attorney General and any of the firms doing work for that office.

Estimated completion time: 8-10 weeks

Staff Note: Actual time will depend upon how much of the cost information has already been pulled together, how many contractors are involved in the litigation, and the number of relationships that need to be checked out.

Sebelius & Griffiths (Karen Griffiths) p 13	$250/case $30/hour-paralegal $20/hour-law clerk	Kansas Parole Board

Firms paid on contingency

Entz & Chanay; Scruggs, Millette, Lawson, Bozeman & Dent; Ness, Motley, Loadholt, Richardson & Poole	If the State receives nothing, no fees are due from the State to Counsel. If the State receives funds by reason of settlement, legislation, judgment, litigation or by any other form or process for resolution of the litigation, Counsel shall be paid a fee. Counsel Fees shall be determined in accordance with this Agreement, 1995 Kan. Ct. R. p 227 Annot 226, MRPC 1.5, by the terms of any settlement agreement or as provided in any other resolution process. Counsel Fees to Lead Local Counsel (Entz and Chanay) shall not exceed Twelve and One-Half Percent (12.5%) and Counsel Fees to Lead Local Counsel shall not exceed Twelve and One-Half Percent (12.5%) of funds received by the Sate as a result of claims asserted in the Litigation.	Tobacco litigation
Dale M Sprague and Thomas H. Brill	Counsel shall be reimbursed for fees and expenses in the event of a successful resolution. The State shall reimburse advanced costs including but not limited to service fees, filing fees, deposition p. expenses, reproduction costs, Notice and Publication expenses, fees of experts and similar expenses. If counsel is terminated before full resolution the Attorney General will petition the legislature on their behalf for fees x 2.5. (Senior counsel rates presently range $250-$275/hour and junior counsel rates range from $150-$200/hour.) At time of termination all outstanding expenses will be paid.	NASDAQ Market-Makers Antitrust Litigation
Berger and Carmody	33% of net recovery. Client will pay expenses of litigation. (depositions, expert witnesses, document printing, copying, collating, and travel) p. 14	Estate of Lester L. Copely, Deceased

House Taxation
Date 2/15/00
Attachment # 18-1

STATE OF KANSAS
OFFICE OF THE ATTORNEY GENERAL
CARLA J. STOVALL

ENGAGEMENT AND CONTINGENCY AGREEMENT

THE AGREEMENT, effective the _____ day of August, 1996 between the **STATE OF KANSAS BY CARLA J. STOVALL, ATTORNEY GENERAL,** (herein the "Attorney General"), and the law firms of **ENTZ & CHANAY, P.A.; SCRUGGS, MILLETTE, LAWSON, BOZEMAN & DENT, P.A.;** and **NESS, MOTLEY, LOADHOLT, RICHARDSON & POOLE, P.A.,** (herein "Counsel"), is as follows:

WHEREAS, cigarette smoking kills approximately 400,000 individuals each year in the United States; more than the number of deaths caused by guns, drug use and automobile accidents combined; and,

WHEREAS, the cost to the State of Kansas and its citizens for health care and related expenditures for smoking related diseases exceeds tens of millions of dollars each year; and,

WHEREAS, any litigation involving tobacco-related industries is likely to entail numerous complex factual and legal issues; and,

WHEREAS, any such litigation will require the expenditure of substantial resources and attorney time; and,

WHEREAS, the Attorney General seeks to avoid the expenditure of state resources for direct costs and attorney time in any such litigation; and

WHEREAS, the Attorney General plans to bring an action against tobacco companies and related entities pursuant to her authority the Common Law and Kansas Statutes Annotated;

1.5 It is specifically agreed by the parties that any documents or any other tangible objects produced by Counsel, or any third party employed pursuant to this Agreement, which were produced or procured solely in the performance of this agreement, shall be the property of the State of Kansas.

1.6 Counsel shall communicate with state agencies through the Attorney General, unless alternative arrangements are made in advance with the Attorney General. Where written communications from Counsel to state agencies are authorized, the Attorney General shall be provided copies of those communications.

Section 2. Designation of Counsel

2.1 The Attorney General, by this agreement designates Scruggs, Millette, Lawson, Bozeman & Dent, P.A., and Ness, Motley, Loadholt, Richardson & Poole, P.A., as "Lead National Counsel" and Entz & Chanay, P.A. as "Lead Local Counsel" in the Litigation. The Attorney General retains the right, after a showing of just and good cause to revoke such designations and make new designations at any time.

2.2 It is anticipated that additional private law firms may be needed in the representation of the State of Kansas in the Litigation. The Attorney General, after consultation with and agreement by Counsel, retains the right to engage additional counsel to participate in the Litigation. All such added Counsel shall be bound by the terms of this Agreement.

Section 3. Contingent Fee

3.1 Counsels' fees are contingent upon the State receiving funds as a result of claims asserted in the Litigation. If the State receives nothing, no fees are due from the State to Counsel. If the State receives funds by reason of settlement, legislation, judgment in litigation or by any other form or process for resolution of the litigation, Counsel shall be

Section 4. Expenses of Litigation

4.1 Lead National Counsel shall advance all expenses of the Litigation except those expenses paid by funds appropriated by the legislature of the State of Kansas for said purpose.

4.2 If recovery is obtained, all expenses advanced by Counsel will be paid to said firms advancing the same before the computation of attorney's fees. During the pendency of the litigation the Attorney General retains the right to petition the Kansas legislature for funds needed for expenses in the litigation. In the event no recovery is made by the State of Kansas, Counsel agree to waive any legal claim that they may have against the State of Kansas or any of its officers or employees for reimbursement of costs, expenses and attorney's fees, but may submit the same to the Joint Committee on Special Claims against the state for determination by the legislature. The Attorney General agrees to support Counsel's claims. As to the Court ordered expenses and costs, monies actually recovered from the Defendants for expenses and costs advanced by Counsel shall be the property of Counsel. It is the intent of the parties that such money as is recovered from the Defendants be used to offset the expenses and costs due to Counsel and that only such reasonable expenses and costs not recovered as such from the Defendants be deducted by Counsel from the recovery prior to the calculation of the Contingency Fee.

4.3 Counsel shall, to the extent allowed under the laws of the State of Kansas and subject to approval of the Attorney General, attempt to recoup all expenses, costs and fees due them or the State of Kansas from the Defendants in the Litigation.

4.4 As used in this Agreement the term "expenses" shall include travel, lodging, telephone charges, copying charges, fax charges, deposition costs, investigator costs, messenger service costs, mailing costs, mediation expenses, computer research fees, medical or nursing consultation fees, expert witness fees, consultant's fees, printing costs and all other costs incurred in relation to or as a result of the pendency and prosecution of the Litigation.

IN WITNESS WHEREOF, the parties have hereunto set their hands the day and year first above written.

THE STATE OF KANSAS

CARLA J. STOVALL
Attorney General of Kansas
Kansas Judicial Center, 2nd Floor
Topeka, Kansas 66612
(913) 296-2215
(913) 296-6296 (fax)

By _____

LEAD NATIONAL COUNSEL

SCRUGGS, MILLETTE, LAWSON
BOZEMAN & DENT, P.A.
734 Delmas Avenue
P.O. Box 1425
Pascagoula, Mississippi 39568-1425
(601) 762-6068
(601) 762-1207 (fax)

By _____

LEAD LOCAL COUNSEL

ENTZ & CHANAY, P.A.
3300 S.W. Van Buren
Topeka, Kansas 66611
(913) 267-5004
(913) 267-7106 (fax)

By _____

LEAD NATIONAL COUNSEL

NESS, MOTLEY, LOADHOLT,
RICHARDSON & POOLE, P.A.
151 Meeting Street, Suite 600
P.O. Box 1137
Charleston, South Carolina 29402
(803) 577-6747

By _____

18-5

Department of Administration
Division of Accounts and Reports
DA-146a (Rev. 7-97)

Agency No. _____ Contract No. _____

CONTRACTUAL PROVISIONS ATTACHMENT

Important: This form contains mandatory contract provisions and must be attached to or incorporated in all copies of any contractual agreement. If it is attached to the vendor/contractor's standard contract form, then that form must be altered to contain the following provision:

"The provisions found in Contractual Provisions Attachment (form DA-146a), which is attached hereto, are hereby incorporated in this contract and made a part hereof".

The parties agree that the following provisions are hereby incorporated into the contract to which it is attached and made a part thereof, said contract being the _____ day of _____, 19____.

1. TERMS HEREIN CONTROLLING PROVISIONS
It is expressly agreed that the terms of each and every provision in this attachment shall prevail and control over the terms of any other conflicting provision in any other document relating to and a part of the contract in which this attachment is incorporated.

2. AGREEMENT WITH KANSAS LAW
All contractual agreements shall be subject to, governed by, and construed according to the laws of the State of Kansas.

3. TERMINATION DUE TO LACK OF FUNDING APPROPRIATION
If, in the judgment of the Director of Accounts and Reports, Department of Administration, sufficient funds are not appropriated to continue the function performed in this agreement and for the payment of the charges hereunder, State may terminate this agreement at the end of its current fiscal year. State agrees to give written notice of termination to contractor at least 30 days prior to the end of its current fiscal year, and shall give such notice for a greater period prior to the end of such fiscal year as may be provided in this contract, except that such notice shall not be required prior to 90 days before the end of such fiscal year. Contractor shall have the right, at the end of such fiscal year, to take possession of any equipment provided State under the contract. State will pay to the contractor all regular contractual payments incurred through the end of such fiscal year, plus contractual charges incidental to the return of any such equipment. Upon termination of the agreement by State, title to any such equipment shall revert to contractor at the end of State's current fiscal year. The termination of the contract pursuant to this paragraph shall not cause any penalty to be charged to the agency or the contractor.

4. DISCLAIMER OF LIABILITY
Neither the State of Kansas nor any agency thereof shall hold harmless or indemnify any contractor beyond that liability incurred under the Kansas Tort Claims Act (K.S.A. 75-6101 et seq.).

5. ANTI-DISCRIMINATION CLAUSE
The contractor agrees: (a) to comply with the Kansas Act Against Discrimination (K.S.A. 44-1001 et seq.) and the Kansas Age Discrimination in Employment Act (K.S.A. 44-1111 et seq.) and the applicable provisions of the Americans With Disabilities Act (42 U.S.C. 12101 et seq.) (ADA) and to not discriminate against any person because of race, religion, color, sex, disability, national origin or ancestry, or age in the admission or access to, or treatment or employment in, its programs or activities; (b) to include in all solicitations or advertisements for employees, the phrase "equal opportunity employer"; (c) to comply with the reporting requirements set out at K.S.A. 44-1031 and K.S.A. 44-1116; (d) to include those provisions in every subcontract or purchase order so that they are binding upon such subcontractor or vendor; (e) that a failure to comply with the reporting requirements of (c) above or if the contractor is found guilty of any violation of such acts by the Kansas Human Rights Commission, such violation shall constitute a breach of contract; (f) if the contracting agency determines that the contractor has violated applicable provisions of ADA, that violation shall constitute a breach of contract; (g) if (e) or (f) occurs, the contract may be cancelled, terminated or suspended in whole or in part by the State Department of Administration.

Parties to this contract understand that subsections (b) through (e) of this paragraph number 5 are not applicable to a contractor who employs fewer than four employees or whose contracts with this agency of the Kansas state government total $5,000 or less during this fiscal year.

6. ACCEPTANCE OF CONTRACT
This contract shall not be considered accepted, approved or otherwise effective until the statutorily required approvals and certifications have been given.

7. ARBITRATION, DAMAGES, WARRANTIES
Notwithstanding any language to the contrary, no interpretation shall be allowed to find the State or any agency thereof has agreed to binding arbitration, or the payment of damages or penalties upon the occurrence of a contingency. Further, the State of Kansas shall not agree to pay attorney fees and late payment charges beyond those available under the Kansas Prompt Payment Act (K.S.A. 75-6403), and no provision will be given effect which attempts to exclude, modify, disclaim or otherwise attempt to limit implied warranties of merchantability and fitness for a particular purpose.

8. REPRESENTATIVE'S AUTHORITY TO CONTRACT
By signing this document, the representative of the contractor thereby represents that such person is duly authorized by the contractor to execute this document on behalf of the contractor and that the contractor agrees to be bound by the provisions thereof.

9. RESPONSIBILITY FOR TAXES
The State of Kansas shall not be responsible for, nor indemnify a contractor for, any federal, state or local taxes which may be imposed or levied upon the subject matter of this contract.

10. INSURANCE
The State of Kansas shall not be required to purchase, any insurance against loss or damage to any personal property to which this contract relates, nor shall this contract require the State to establish a "self-insurance" fund to protect against any such loss or damage. Subject to the provisions of the Kansas Tort Claims Act (K.S.A. 75-6101 et seq.), the vendor or lessor shall bear the risk of any loss or damage to any personal property in which vendor or lessor holds title.

18-6

HUTTON & HUTTON
Attorneys at Law

MARK B. HUTTON
Attorney at Law

Street Address: 8100 E. 22nd Street North,
Building 1200 • Wichita, KS 67226-2312
Mail: P.O. Box 638 • Wichita, KS 67201-0638
Phone: (316) 688-1166 • Fax: (316) 686-1077
Products Liability Phone: (316) 686-1242 • Fax: (316) 686-2049

House Taxation
Date 2/15/00
Attachment # 19-1

Andy Dutton —

Front expenses —
Minimum years —
#1/2 - 2 million

Certain Price Control - #30 m/yr in Kansas
#40-50 m./year

$500,000.00

Contingency — 25%

1-2 firms in Kansas —

→ Unjust enrichment
Conspiracy — CTR...
Fraud

Substitutes —

No research on Kansas law —
No mention of C.P.

RTS
Stn Entg] reference!

MARY L. BARRIER

MORRISON & HECKER L.L.P.
ATTORNEYS AT LAW

Telefax
816-474-4208

2600 Grand Avenue
Kansas City
Missouri 64108-4606

Telephone
816-691-2600

House Taxation
Date 2/15/00
Attachment # 20-1

April 8th

[Andy Hutton
Mark Hutton

Anyone who's addicted
Addiction cost - smoking abatement
spent on cigarettes

65 law firms joined -

Andy chairs Committee on Science of Addiction.

6 member firm - they "finance" Tulsa firm.
They'd front all expenses
Contract w/ other & write / research

2y - 5 firms to get involved.

Fla, W Va, Ms, Mn. → Motley

Castano

LeBow - head of Liggett
RJR - settlement if LeBow buys RJR.
Documents of Liggett + RJR point finger
@ Phillip Morris.

NJS
Md
Ma
Tx
WVa –
Fla

Fla – abrogated CL negligence.

Indivd ~~Ks~~ < Assumption of Risk
Comparative / contributory

~~Medicaid~~ ⓐ *medical assistance
ⓑ legal obligation – Sec. SRS re to recover from 3rd parties

ⓒ purpose → spouses / family members

State Actions:
Fraud
Deceit
Deception
Conspiracy
Strict liability –

20-3

Cons. Prot. – deceptive practice if consumer not [illegible] / Penalties / fees / damages

B+W –
Ligett –

Some of states using C.P.

FDA – lotsa info there
Much public info: deceptive info
Joint Agmnt – Tobacco Institute Research = TRC . .
suppressed negative studies.
1950's.
Abandoned efforts to get "safer" cigarette bc
dont want to acknowledge any problems.

Ligett – maybe can still sue/recover from them.

GP –
Medicaid payments –
medicare – states don't pursing.

MN – BC/BS has joined state suit.

Fla – HG – + Cur –
MS –

Premption —
NJ — Fed'l labeling laws prompted "failure to warn"
fraud / deceit / etc. USSct.

Failure to warn — ~~duty to~~ notify Congress + public . . .

'53 scientist — mice painted w/ ~~tobacco~~ nicotine residue

~~Smoke~~ Cigarette companies —

TN class action in Louisiana
nicotine addiction
certified a class — appeal

assumption of risk —
comparative negl.

Exec. Comm.

- Formally evaluate case (free games)

✓ Discounted rate / straight time . . .
✓ An hourly rate – small contingency rate.

⊗ Not straight contingency . . . (pro bono approach.

New Atty / client law in Kansas. *
law firms as members of conspiracy.

2-3 partners
5-6 associates
7-8 full time attys . . .

Expenses → client will absorb!
Mn – document repository.

#1 million / per year – 5 years.
expenses and atty fees.

Senate

Kim

Bank Moran

Van C

Alicia

B Lawrence

S Morris

Roch

Platy

Brady

Kerr

(✓) Medicaid fraud —

(✓) C.P.

House App

Robyn J.

Carmody

Bradley ✓

Cornfeld

Edinson ✓

Farmer

Guthrie

Gresson

Kyser

Old Irvine

Lowther

McChesney ✓

Penfield ✓

Walk

Ken Wilson

Helga

Rehm

Edland (blind)

Cross

Hochhauser

Minor

Nichols

Rhinehart

Anti trust?
Add RICO.

SRS - Medicaid recovery
Dept Rev - Every sale of cigarettes / tobacco...

Ligett settlement -

~~Restitution~~ →
Common Deposit -

[10%: contingency plus discounted hourly rate...

Statute limitations - ~~Stat~~. (1 year)

CP - recovery atty fees -

STATE OF KANSAS
OFFICE OF ATTORNEY GENERAL
CARLA J. STOVALL

GUIDELINES FOR CONTRACTS FOR LEGAL SERVICES
JULY 1, 1997

Introduction

The following guidelines are intended to help both the law firm and the Office of the Attorney General in providing effective and efficient legal representation to the State of Kansas, its agents and employees. We welcome any suggestions regarding these guidelines and if you have any questions concerning the policies presented in them, please do not hesitate to contact the Senior Deputy Attorney General.

These Guidelines are concerned with the financial aspects of our contractual relationship. An attorney's professional responsibilities are prescribed in the Model Rules of Professional Conduct, as well as substantive and procedural law. The Attorney General has chosen your law firm for this contract because she believes that the attorneys in the firm not only follow the Model Rules but that personal conscience and the approbation of professional peers guide them. She trusts that your firm will continue to strive to attain the highest level of skill, to improve the law and the legal profession and to exemplify the legal profession's ideals of public service.

Communication with the Office of the Attorney General

The Office of the Attorney General respects the independence of our retained counsel. However, to assist us in our administrative functions, we require a quarterly status report for all cases you are handling for us. The report will generally require no more than one page for each case, and once instituted, should only be updated to reflect significant developments over the preceding quarter and action items for the immediate future. Do not repeat information you have previously reported to us. Your reports should be brief if you are keeping us routinely informed of all significant developments. Preparation of this concise report is considered an administrative cost and part of your firm's overhead. Should you find it necessary to contact us with respect to your retention, please direct your questions or comments to the Senior Deputy Attorney General.

Use of Resources

In conducting legal research, the law firm is expected to utilize all appropriate sources reasonably available, including previously prepared briefs and memoranda. While value-added premiums will not be paid, the Office of the Attorney General will pay for actual time spent in updating and tailoring such previously prepared briefs and memoranda to address assigned matters.

Computerized Research

The actual time of the attorney or paralegal who performs computerized legal research will be compensated. However, we consider the subscription and on-line charges for computerized legal research services to be an overhead cost of the law firm, augmenting the firm's legal library. As with other overhead costs, on-line charges for computerized research services will not be paid.

Settlement

In order to promote uniformity and efficiency in the settlement or compromise of actions falling within the purview of the Kansas Tort Claims Act, all such settlements or compromises must conform to the provisions of K.S.A. 75-6101, *et seq.* and the current version of the Attorney General's policy statement on settlement procedures.

Staffing

Approved Billers

Each law firm professional assigned to a matter should make a clear contribution to the efficient handling of the legal matter. Generally, the Office of the Attorney General will pay for a team of up to two attorneys and one paralegal to perform services on any case. Any deviation from this staffing model must be considered and approved on a case by case basis. You must advise us about who will be assigned to work on each case, and we will pay fees only for the attorneys and paralegal you have designated.

The Office of the Attorney General will not pay for work performed by firm personnel who have not been identified as assigned to a matter. We will not pay for the learning curve of replacement personnel substituted for original team members or training for inexperienced

21-2

Compensable Legal Services

Only services requiring specialized legal knowledge will be paid. Fees billed for professional services should reflect only the time actually devoted to such services during a given day. Matters that are capable of being handled by a secretary, case clerk or courier should not be billed. Charges for law clerk and paralegal time should be billed only for services that would otherwise be performed by an attorney.

Appropriate Billing

In approving billings, the engagement partner should focus attention particularly on time devoted to such items as internal conferences, legal research on basic or general legal principles, training and supervision of inexperienced attorneys and paralegals, drafting standard form documents, and duplicative attendance at meetings, depositions and hearings. We expect that attorneys will handle attorney-level work, paralegals will handle paralegal-level work and secretaries will perform the secretarial work. In this regard, the engagement partner should consider the appropriate ratio of attorney hours to paralegal hours for various tasks.

Avoiding Duplication of Effort

We do not pay for more than one attorney to attend a hearing or deposition, conduct a field investigation or interview, or otherwise handle casework requiring an appearance other than trial. We also ask you to avoid the involvement of more than one attorney in telephone and office conferences with us and within your own firm.

We will not pay for administrative or supervisory conferences among firm personnel. Should strategic conferences involve more than one individual from your firm, whether they are internal conferences or those that involve other parties, we will pay for the time billed by the senior attorney only.

Maintaining Competence

The Office of the Attorney General should not be charged for outside counsel to maintain general professional competence, including lawyer training time, time spent in legal education seminars, or reading advance sheets or periodicals.

Administrative Matters

Your firm should not charge for time spent preparing billing statements or reviewing retention issues, including budgeting.

21-3

Fiscal Year Requirements

Our accounting year ends on June 30th of each year. On or before July 5 of each year, your firm must submit your final billing for the prior fiscal year. If you fail to submit the final billing for the current fiscal year on or before July 5th, you will forfeit payment for all charges incurred during the fiscal year but not billed by the deadline.

Bill Format

Your monthly invoices should be submitted via e-mail or other electronic means to abr@examen.com, referencing the Office of the Attorney General for the State of Kansas. If you do not have electronic transmission capability, please submit invoices on diskette in ASCII format to the Office of the Attorney General for the State of Kansas, c/o Examen, Inc., PO Box 340850, Sacramento 95834-0850, unless other arrangements have been made. Your Examen Account Manager can assist you in resolving formatting and transmission problems. Distinct matters must be invoiced separately. Each invoice should include the following information:

1. The case caption;
2. The court case number;
3. The date of each service performed and a full description of each service rendered. A full description should include the activity performed, the names of the individuals involved, and the subject or purpose of the charges. For example, bills should reference the purpose of conferences and the names of participants, the subject matter and recipient of all correspondence prepared or reviewed by the firm, the titles of documents, proceedings and motions, and the specific issues involved in any legal research billed;
4. The name of each partner, associate and paralegal performing each service and the number of hours worked on each task, billed in .10 hour increments (tasks charged as "block" or multiple item entries are not acceptable);
5. The hourly rate for each person and the resulting total charge for each service;
6. Total fees for all professional services rendered during the billing period;
7. An itemized list of all disbursements (include the per page charge for photocopies). Receipts may be requested from time to time; and

21-4

Itemization of Travel Expenses

All travel expenses require an itemized accounting submitted with your bill. This accounting must include detailed information about car rental, hotel, air and train fare, regardless of amount.

Specific Expense Items

Internal Photocopying

Copying will be reimbursed at a maximum of 10 cents per page, or your actual cost if lower. The actual number of copies must be reflected on the bill.

Fax Charges

The Office of the Attorney General will pay for telephone line charges incurred to send faxes. However, charges for receipt of facsimiles and for other overhead expenses of the firm, such as machine maintenance, paper or operator costs, will not be paid. There should be no charges for local faxing.

Hotel Accommodations

The Attorney General will pay for hotel accommodations for attorneys and paralegals necessarily required to travel out of town regarding a matter, but such accommodations shall not exceed the lowest single occupancy rate available to the firm in economy or moderately priced hotels.

Personal Expenses

The Attorney General will not pay additional charges for room service, in-room movies, garment cleaning or similar items charged to the room. Non-reimbursable expenses include charges for unused guaranteed hotel reservations, airline headsets, recreation and health club facilities and personal trip insurance.

Meals

Meal charges for attorneys and paralegals generally will not be paid whether or not out of town. Exceptions may be made for clearly justified hospitality provided to witnesses or others where the names and the reason for the hospitality is stated on the bill. Any such hospitality shall be reasonably priced and liquor charges will not be paid.

21-5

Computerized Legal Research and Data Services

The Attorney General considers subscription data services to be a part of your firm's overhead.

Auditing

The Office of the Attorney General has the right to audit all bills, using either in-house auditors or the services of an independent auditor. Retained counsel will maintain all necessary bills, pre-bills, receipts and records and will make them available to us or our representatives for this purpose. The Attorney General will give retained counsel advance notice of any such audit.

21-6

STATE OF KANSAS
OFFICE OF THE ATTORNEY GENERAL
CARLA J. STOVALL

ENGAGEMENT AND CONTINGENCY AGREEMENT

THE AGREEMENT, effective the _____ day of August, 1996 between the **STATE OF KANSAS BY CARLA J. STOVALL, ATTORNEY GENERAL**, (herein the "Attorney General"), and the law firms of **ENTZ & CHANAY, P.A.; SCRUGGS, MILLETTE, LAWSON, BOZEMAN & DENT, P.A.;** and **NESS, MOTLEY, LOADHOLT, RICHARDSON & POOLE, P.A.**, (herein "Counsel"), is as follows:

WHEREAS, cigarette smoking kills approximately 400,000 individuals each year in the United States; more than the number of deaths caused by guns, drug use and automobile accidents combined; and,

WHEREAS, the cost to the State of Kansas and its citizens for health care and related expenditures for smoking related diseases exceeds tens of millions of dollars each year; and,

WHEREAS, any litigation involving tobacco-related industries is likely to entail numerous complex factual and legal issues; and,

WHEREAS, any such litigation will require the expenditure of substantial resources and attorney time; and,

WHEREAS, the Attorney General seeks to avoid the expenditure of state resources for direct costs and attorney time in any such litigation; and

WHEREAS, the Attorney General plans to bring an action against tobacco companies and related entities pursuant to her authority the Common Law and Kansas Statutes Annotated;

NOW, THEREFORE, IT IS AGREED BY AND BETWEEN THE ATTORNEY GENERAL AND COUNSEL AS FOLLOWS:

Section 1 - Engagement of Counsel

1.1 Counsel is retained to provide legal services to the State of Kansas for the purpose of seeking injunctive relief, monetary relief (including, without limitation, damages and civil penalties) and other relief against tobacco industry companies and related entities ("Defendants") in litigation arising from the advertising, marketing, manufacturing, promotion, sale and/or distribution of cigarettes and other tobacco products (hereinafter "the Litigation"). Counsel shall provide sufficient resources, including attorney time, to prosecute the Litigation faithfully and with due diligence.

1.2 The Attorney General, as the Chief Legal Officer of the State of Kansas shall retain final authority over all aspects of the Litigation. As provided herein, Counsel is authorized to take appropriate legal steps to prosecute the Litigation and participate in all settlement negotiations and the State of Kansas and the Attorney General hereby further agrees not to settle this action without prior consultation with Counsel. However, the Attorney General specifically reserves the right to settle the Litigation without the approval of Counsel.

1.3 The Attorney General may appoint members of her staff to monitor the prosecution of the Litigation. Counsel shall consult in advance with and obtain the prior approval of the Attorney General, or her designee, concerning all significant matters related to the Litigation. Regular status meetings shall be held as requested by either the Attorney General or Counsel.

1.4 It is specifically agreed by the parties that neither Counsel nor any third party employed whose services or products are used by either the State of Kansas or Counsel in furtherance of this agreement or its goals, is considered, or paid as a State employee, but is an independent contractor.

1.5 It is specifically agreed by the parties that any documents or any other tangible objects produced by Counsel, or any third party employed pursuant to this Agreement, which

were produced or procured solely in the performance of this agreement, shall be the property of the State of Kansas.

1.6 Counsel shall communicate with state agencies through the Attorney General, unless alternative arrangements are made in advance with the Attorney General. Where written communications from Counsel to state agencies are authorized, the Attorney General shall be provided copies of those communications.

Section 2. Designation of Counsel

2.1 The Attorney General, by this agreement designates Scruggs, Millette, Lawson, Bozeman & Dent, P.A., and Ness, Motley, Loadholt, Richardson & Poole, P.A., as "Lead National Counsel" and Entz & Chanay, P.A. as "Lead Local Counsel" in the Litigation. The Attorney General retains the right, after a showing of just and good cause to revoke such designations and make new designations at any time.

2.2 It is anticipated that additional private law firms may be needed in the representation of the State of Kansas in the Litigation. The Attorney General, after consultation with and agreement by Counsel, retains the right to engage additional counsel to participate in the Litigation. All such added Counsel shall be bound by the terms of this Agreement.

Section 3. Contingent Fee

3.1 The State of Kansas is not liable to pay any attorney fees in the event the Litigation is unsuccessful. Counsel's attorney's fees are contingent upon a successful settlement and/or judgment in the Litigation, the amount of which shall be determined in accordance with 1995 Kan. Ct. R. Annot. 226. MRPC 1.5. In the event of a judgement it is the intent of the Attorney General to request that a court set the amount of attorney's fees. In the event of settlement it is the intent of the Attorney General to include attorney's fees within the settlement agreement.

3.2 The sole contingency upon which compensation is to be paid to Counsel is the recovery and collection by Counsel, on behalf of the State of Kansas, of monies in the Litigation, whether by settlement or judgment.

3.3 Compensation on the foregoing contingency as set forth in Paragraph 3.2, above, shall be made in accordance with 1995 Kan. Ct. R. Annot. 226, MRPC 1.5 and shall not exceed 12.5% to Lead National Counsel and 12.5% to Lead Local Counsel of the amount of money recovered by the State of Kansas in the Litigation.

3.4 In accordance with 1995 Kan. Ct. R. Annot. 226, MRPC 1.5(d), Litigation and other expenses shall be deducted from any recovery before the Contingency Fee is calculated.

3.5 Settlement, for purposes of this Agreement, may include any structure, type or form of settlement of issues raised in the Litigation, including state or federal legislation, state or federal Court multi-party settlement structures or any other structure, means of device to settle and resolve the claims of a nature as alleged in original Petition and any amendments thereto for damages asserted therein or which could have been asserted therein.

3.6 In the event the Litigation is resolved, by settlement or judgment, under terms involving the provision of goods, services or other "in-kind" payment, the parties hereto agree to seek, as part of any such settlement, compensation for Counsel equivalent to the said Contingency Fee and expenses to which Counsel would be entitled under this Agreement. In the event the Attorney General is unable to secure such compensation for Counsel as part of any "in-kind" settlement, the Attorney General agrees to petition the legislature to appropriate funds to reasonably compensate Counsel in accordance with the terms and provisions of this Agreement for both fees and expenses.

Section 4. Expenses of Litigation

4.1 Lead National Counsel shall advance all expenses of the Litigation except those expenses paid by funds appropriated by the legislature of the State of Kansas for said purpose.

4.2 If recovery is obtained, all expenses advanced by Counsel will be paid to said firms advancing the same before the computation of attorney's fees. During the pendency of

the litigation the Attorney General retains the right to petition the Kansas legislature for funds needed for expenses in the litigation. In the event no recovery is made by the State of Kansas, Counsel agree to waive any legal claim that they may have against the State of Kansas or any of its officers or employees for reimbursement of costs, expenses and attorney's fees, but may submit the same to the Joint Committee on Special Claims against the state for determination by the legislature. The Attorney General agrees to support Counsel's claims. As to the Court ordered expenses and costs, monies actually recovered from the Defendants for expenses and costs advanced by Counsel shall be the property of Counsel. It is the intent of the parties that such money as is recovered from the Defendants be used to offset the expenses and costs due to Counsel and that only such reasonable expenses and costs not recovered as such from the Defendants be deducted by Counsel from the recovery prior to the calculation of the Contingency Fee.

4.3 Counsel shall, to the extent allowed under the laws of the State of Kansas and subject to approval of the Attorney General, attempt to recoup all expenses, costs and fees due them or the State of Kansas from the Defendants in the Litigation.

4.4 As used in this Agreement the term "expenses" shall include travel, lodging, telephone charges, copying charges, fax charges, deposition costs, investigator costs, messenger service costs, mailing costs, mediation expenses, computer research fees, medical or nursing consultation fees, expert witness fees, consultant's fees, printing costs and all other costs incurred in relation to or as a result of the pendency and prosecution of the Litigation.

4.5 Counsel are not required to maintain time records, but shall maintain expense records. It is understood and agreed by the Attorney General that Lead National Counsel bring to the Litigation thousands of hours of legal work and research regarding tobacco litigation in other states, and the State of Kansas will benefit from such legal work, which Lead National Counsel agree to share with the State of Kansas.

Section 5. Miscellaneous

5.1 Counsel agrees to abide by the provisions of Kansas Statute Annotated 46-239(c). Counsel agrees to notify the Attorney General in the event K.S.A. 46-239(c) is applicable and to assist the Attorney General in filing her reporting requirements.

5.2 The provisions found in the contractual provisions (Form DA-146a) attached hereto, are hereby incorporated in this contract and made a part hereof. In addition, Counsel shall incorporate the provisions of Form DA-146a into any contract with any third party.

IN WITNESS WHEREOF, the parties have hereunto set their hands the day and year first above written.

THE STATE OF KANSAS

CARLA J. STOVALL
Attorney General of Kansas
Kansas Judicial Center, 2nd Floor
Topeka, Kansas 66612
(913) 296-2215
(913) 296-6296 (fax)

By_____

LEAD NATIONAL COUNSEL

SCRUGGS, MILLETTE, LAWSON
BOZEMAN & DENT, P.A.
734 Delmas Avenue
P.O. Box 1425
Pascagoula, Mississippi 39568-1425
(601) 762-6068
(601) 762-1207 (fax)

By_____

LEAD LOCAL COUNSEL

ENTZ & CHANAY, P.A.
3300 S.W. Van Buren
Topeka, Kansas 66611
(913) 267-5004
(913) 267-7106 (fax)

By_____

LEAD NATIONAL COUNSEL

NESS, MOTLEY, LOADHOLT,
RICHARDSON & POOLE, P.A.
151 Meeting Street, Suite 600
P.O. Box 1137
Charleston, South Carolina 29402
(803) 577-6747

By_____

APPROVED:

22-7

John W. Campbell
Sr. Deputy Attorney General

Neil A. Woerman
Director of Budget and Special Projects
Office of the Attorney General

22-S

ENTZ & CHANAY, P.A.
ATTORNEYS AT LAW

STEWART L. ENTZ
JEFFREY A. CHANAY
J. PHILLIP GRAGSON*

3300 SW VAN BUREN STREET
TOPEKA, KANSAS 66611
(913) 267-5004
FAX: (913) 267-7106

*ADMITTED IN KANSAS AND MISSOURI

August 14, 1996

Mr. John W. Campbell
Senior Deputy Attorney General
Office of the Attorney General
301 S.W. 10th Avenue
Topeka, Kansas 66612-1597

Re: *Tobacco Litigation*

Dear John:

Enclosed is a proposed revision to Section 3 of the Engagement and Contingent Agreement. It replaces paragraph 3.1, 3.2 and 3.3. I tried to bring together all of the ideas of the earlier draft. As far as the State of Kansas is concerned, I believe this language provides that

1. If the State receives nothing, there is no fee.

2. If any judgment is entered, the Court can determine the fee pursuant to Rule 1.5.

3. If there is a settlement, the fee shall be a part of the settlement and the State must approve any settlement.

4. There is an absolute "cap" on Counsel's fee at less than the normal contingent fee.

Quite simply, the state pays a fee only if it "wins and (1) if the "win" is by judgment the Court can set the fee and (2) if the State "wins" by settlement the fee will be set out in the very Settlement Agreement that the States approves. Our concern is that litigation of this size and nature may be resolved in an "other-than-ordinary" fashion. All we want to do is to insure that, if the State does benefit greatly because of the expertise, time and expenses advanced by Counsel, Counsel is compensated in the fashion contemplated by this Agreement at the time of the engagement.

House Taxation
Date 2/15/00
Attachment # 23-1

Please give me a call so we can get this matter concluded and can focus on the "filing".

Very truly yours,

Stewart L. Entz

sle/sja

ENTZ & CHANAY, P.A.
ATTORNEYS AT LAW

STEWART L. ENTZ
JEFFREY A. CHANAY
J. PHILLIP GRAGSON*

3300 SW VAN BUREN STREET
TOPEKA, KANSAS 66611
(913) 267-5004
FAX: (913) 267-7108

*ADMITTED IN KANSAS AND MISSOURI

July 25, 1996

Mr. Richard F. Scruggs
SCRUGGS, MILLETTE, LAWSON,
BOZEMAN & DENT, P.A.
734 Delmas Avenue
P.O. Drawer 1425
Pascagoula, Mississippi 39568-1425

VIA FACSIMILE
(601) 762-1207

Mr. Ronald L. Motley
NESS, MOTLEY, LOADHOLT,
RICHARDSON & POOLE, P.A.
151 Meeting Street, Suite 600
P.O. Box 1137
Charleston, South Carolina 29402

VIA FACSIMILE
(803) 577-7513

Re: Kansas Tobacco Litigation

Gentlemen:

I have enclosed a draft proposed agreement between counsel and the State of Kansas for your review and consideration. It is, for the most part, the document originally provided by Mr. Campbell with some topical reorganization. As soon as you approve the same, we will deliver the document to Mr. Campbell for his review, approval and execution.

Very truly yours,

Stewart L. Entz

cc: Mr. John Campbell
Enclosure

House Taxation
Date 2/15/00
Attachment # 24-1

STATE OF KANSAS
OFFICE OF THE ATTORNEY GENERAL
CARLA J. STOVALL

ENGAGEMENT AND CONTINGENCY AGREEMENT

THE AGREEMENT, effective the day of July, 1996 between the **STATE OF KANSAS BY CARLA J. STOVALL, ATTORNEY GENERAL**, (herein the "Attorney General"), and the law firms of **ENTZ & CHANAY, P.A.; SCRUGGS, MILLETTE, LAWSON, BOZEMAN & DENT, P.A.;** and **NESS, MOTLEY, LOADHOLT, RICHARDSON & POOLE, P.A.**, (herein "Counsel"), is as follows:

WHEREAS, cigarette smoking kills approximately 400,000 individuals each year in the United States; more than the number of deaths caused by guns, drug use and automobile accidents combined; and,

WHEREAS, the cost to the State of Kansas and its citizens for health care and related expenditures for smoking related diseases exceeds tens of millions of dollars each year; and,

WHEREAS, any litigation involving tobacco-related industries is likely to entail numerous complex factual and legal issues; and,

WHEREAS, any such litigation will require the expenditure of substantial resources and attorney time; and,

WHEREAS, the Attorney General seeks to avoid the expenditure of state resources for direct costs and attorney time in any such litigation; and

WHEREAS, the Attorney General plans to bring an action against tobacco companies and related entities pursuant to her authority the Common Law and Kansas Statutes Annotated;

NOW, THEREFORE, IT IS AGREED BY AND BETWEEN THE ATTORNEY GENERAL AND COUNSEL AS FOLLOWS:

Section 1 - Engagement of Counsel

1.1 Counsel is retained to provide legal services to the State of Kansas for the purpose of seeking injunctive relief, monetary relief (including, without limitation, damages and civil penalties) and other relief against tobacco industry companies and related entities ("Defendants") in litigation arising from the advertising, marketing, manufacturing, promotion, sale and/or distribution of cigarettes and other tobacco products (hereinafter "the Litigation"). Counsel shall provide sufficient resources, including attorney time, to prosecute the Litigation faithfully and with due diligence.

1.2 The Attorney General, as the Chief Legal Officer of the State of Kansas shall retain final authority over all aspects of the Litigation. As provided herein, Counsel is authorized to take appropriate legal steps to prosecute the Litigation and participate in all settlement negotiations and the State of Kansas and the Attorney General hereby further agrees not to settle this action without prior consultation with Counsel.

1.3 The Attorney General may appoint members of her staff to monitor the prosecution of the Litigation. Counsel shall consult in advance with and obtain the prior approval of the Attorney General, or her designee, concerning all significant matters related to the Litigation. Regular status meetings shall be held as requested by either the Attorney General or Counsel.

1.4 It is specifically agreed by the parties that neither Counsel nor any third party employed whose services or products are used by either the State of Kansas or Counsel in furtherance of this agreement or its goals, is considered, or paid as a State employee, but is an independent contractor.

1.5 It is specifically agreed by the parties that any documents or any other tangible objects produced by Counsel, or any third party employed pursuant to this Agreement, which were produced or procured in the performance of this agreement, shall be the property of the State of Kansas.

1.6 Counsel shall communicate with state agencies through the Attorney General, unless alternative arrangements are made in advance with the Attorney General. Where written communications from Counsel to state agencies are authorized, the Attorney General shall be provided copies of those communications.

Section 2. Designation of Counsel

2.1 The Attorney General, by this agreement designates Scruggs, Millette, Lawson, Bozeman & Dent, P.A., and Ness, Motley, Loadholt, Richardson & Poole, P.A., as "Lead National Counsel" and Entz & Chanay, P.A. as "Lead Local Counsel" in the Litigation. The Attorney General retains the right, after a showing of just and good cause to revoke such designations and make new designations at any time.

2.2 It is anticipated that additional private law firms may be needed in the representation of the State of Kansas in the Litigation. The Attorney General, after consultation with and agreement by Counsel, retains the right to engage additional counsel to participate in the Litigation. All such added Counsel shall be bound by the terms of this Agreement.

Section 3. Contingent Fee

3.1 The State of Kansas is not liable to pay any attorney fees in the event the Litigation is unsuccessful. Counsel's attorney's fees are contingent upon a successful settlement and/or judgment in the Litigation.

3.2 The sole contingency upon which compensation is to be paid to Counsel is the recovery and collection by Counsel, on behalf of the State of Kansas, of monies in the Litigation, whether by settlement or judgment.

3.3 Compensation on the foregoing contingency as set forth in Paragraph 3.2, above, shall be made in accordance with 1995 Kan. Ct. R. Annot. 226, MRPC 1.5 and shall not exceed 12.5% to Lead National Counsel and 12.5% to Lead Local Counsel of the amount of money recovered by the State of Kansas in the Litigation.

3.4 In accordance with 1995 Kan. Ct. R. Annot. 226, MRPC 1.5(d), Litigation and other expenses shall be deducted from any recovery before the Contingency Fee is calculated.

3.5 Settlement, for purposes of this Agreement, may include any structure, type or form of settlement of issues raised in the Litigation, including state or federal legislation, state or federal Court multi-party settlement structures or any other structure, means of device to settle and resolve the claims of a nature as alleged in

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original Petition and any amendments thereto for damages asserted therein or which could have been asserted therein.

3.6 In the event the Litigation is resolved, by settlement or judgment, under terms involving the provision of goods, services or other "in-kind" payment, the parties hereto agree to seek, as part of any such settlement, compensation for Counsel equivalent to the said Contingency Fee and expenses to which Counsel would be entitled under this Agreement. In the event the Attorney General is unable to secure such compensation for Counsel as part of any "in-kind" settlement, the Attorney General agrees to petition the legislature to appropriate funds to recently compensate Counsel in accordance with the terms and provisions of this Agreement for both fees and expenses.

Section 4. Expenses of Litigation

4.1 Lead National Counsel shall advance all expenses of the Litigation except those expenses paid by funds appropriated by the legislature of the State of Kansas for said purpose.

4.2 If recovery is obtained, all expenses advanced by Counsel will be paid to said firms advancing the same before the computation of attorney's fees. During the pendency of the litigation the Attorney General agrees to petition the Kansas legislature for funds needed for expenses in the litigation. In the event no recovery is made by the State of Kansas, Counsel agree to waive any legal claim that they may have against the State of Kansas or any of its officers or employees for reimbursement of costs, expenses and attorney's fees, but may submit the same to the Joint Committee on Special Claims against the state for determination by the legislature. The Attorney General agrees to support Counsel's claims. As to the Court ordered expenses and costs, monies actually recovered from the Defendants for expenses and costs advanced by Counsel shall be the property of Counsel. It is the intent of the parties that such money is recovered from the Defendants be used to offset the expenses and costs due to Counsel and that only such reasonable expenses and costs not recovered as such from the Defendants be deducted by Counsel from the recovery prior to the calculation of the Contingency Fee.

4.3 Counsel shall, to the extent allowed under the laws of the State of Kansas and subject to approval of the Attorney General, attempt to recoup all expenses, costs and fees due them or the State of Kansas from the Defendants in the Litigation.

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4.4 As used in this Agreement the term "expenses" shall include travel, lodging, telephone charges, copying charges, fax charges, deposition costs, investigator costs, messenger service costs, mailing costs, mediation expenses, computer research fees, medical or nursing consultation fees, expert witness fees, consultant's fees, printing costs and all other costs incurred in relation to or as a result of the pendency and prosecution of the Litigation.

4.5 Counsel are not required to maintain time records, but shall maintain expense records. It is understood and agreed by the Attorney General that Lead National Counsel bring to the Litigation thousands of hours of legal work and research regarding tobacco litigation in other states, and the State of Kansas will benefit from such legal work, which Lead National Counsel agree to share with the State of Kansas.

Section 5. Miscellaneous

5.1 Counsel agrees to abide by the provisions of Kansas Statute Annotated 46-239(c). Counsel agrees to notify the Attorney General in the event K.S.A. 46-239(c) is applicable and to assist the Attorney General in filing her reporting requirements.

5.2 The provisions found in the contractual provisions (Form DA-146a) attached hereto, are hereby incorporated in this contract and made a part hereof. In addition, Counsel shall incorporate the provisions of Form DA-146a into any contract with any third party.

IN WITNESS WHEREOF, the parties have hereunto set their hands the day and year first above written.

24-6

THE STATE OF KANSAS

CARLA J. STOVALL
Attorney General of Kansas
Kansas Judicial Center, 2nd Floor
Topeka, Kansas 66612
(913) 296-2215
(913) 296-6296 (fax)

By_____

LEAD NATIONAL COUNSEL

SCRUGGS, MILLETTE, LAWSON
BOZEMAN & DENT, P.A.
734 Delmas Avenue
P.O. Box 1425
Pascagoula, Mississippi 39568-1425
(601) 762-6068
(601) 762-1207 (fax)

By_____

LEAD LOCAL COUNSEL

ENTZ & CHANAY, P.A.
3300 S.W. Van Buren
Topeka, Kansas 66611
(913) 267-5004
(913) 267-7106 (fax)

By_____

LEAD NATIONAL COUNSEL

NESS, MOTLEY, LOADHOLT,
RICHARDSON & POOLE, P.A.
151 Meeting Street, Suite 600
P.O. Box 1137
Charleston, South Carolina 29402
(803) 577-6747

By_____

APPROVED:

_____
John W. Campbell
Sr. Deputy Attorney General

_____
Neil A. Woerman
Director of Budget and Special Projects
Office of the Attorney General

24-7

Mark B. Hutton · †
Andrew W. Hutton

Derek S. Casey ·
Anne H. Pankratz
Christopher P. Christian
Chan P. Townsley ··

· Also Admitted in Oklahoma
·· Also Admitted in Missouri
† Certified Trial Advocate
National Board of Trial Advocacy

HUTTON & HUTTON

Law Offices
8100 East Twenty-Second Street North, Building 1200
Wichita, Kansas 67226-2321
Mail: P.O. Box 638
Wichita, Kansas 67201-0638

General Office
(316) 688-1166
Facsimile
(316) 686-1077

Products Liability
(316) 686-1242
Facsimile
(316) 686-2049

Tax I.D.# 48-0966751

June 10, 1996

SENT VIA FACSIMILE
TO (913) 296-6296
AND VIA REGULAR MAIL

Mr. John Campbell
Assistant Attorney General
2nd Floor, Judicial Center
Topeka, KS 66612-1567

Re: Cigarette Litigation
John Campbell

Dear John:

Just for your information, when a private attorney in Kansas is responsible for recoveries of money in an action where Medicaid is reimbursed, there is statutory authority that the attorneys' fees be one-third for cases settled prior to trial or 40 percent when the trial is convened. See K.S.A. 39-719a and b. We encounter this section quite frequently in our medical malpractice actions in which we are successful in recovering money on behalf of the State of Kansas against a negligent tort-feasor. I thought you might find this interesting.

Very truly yours,

Andrew W. Hutton

AWH/sm

AWH/sm

House Taxation
Date 2/15/00
Attachment # 25-1

CASE ANNOTATIONS

1. Parent released by court order from contributing to support could not be sued for reimbursement for aid to dependent children. Harder v. Towns, 1 K.A.2d 667, 669, 573 P.2d 625.

2. Absent parent defined; statute constitutional since defenses may be asserted before judgment. State ex rel. Secretary of SRS v. Castro, 235 K. 704, 714, 715, 684 P.2d 379 (1984).

39-718b. Liability of parent or guardian for assistance provided child, exceptions. (a) Except as provided in subsection (b), a child's parent, parents or guardian shall be liable to repay to the secretary of social and rehabilitation services any assistance expended on the child's behalf, regardless of the specific program under which the assistance is or has been provided. When more than one person is legally obligated to support the child, liability to the secretary shall be joint and several. The secretary shall have the power and authority to file a civil action in the name of the secretary for repayment of the assistance, regardless of the existence of any other action involving the support of the child.

(b) With respect to an individual parent or guardian, the provisions of subsection (a) shall not apply to:

(1) Assistance provided on behalf of any person other than the child of the parent or guardian;

(2) assistance provided during a month in which the needs of the parent or guardian were included in the assistance provided to the child; or

(3) assistance provided during a month in which the parent or guardian has fully complied with the terms of an order of support for the child, if a court of competent jurisdiction has considered the issue of support. For the purposes of this subsection, if an order is silent on the issue of support, it shall not be presumed that the court has considered the issue of support. Amounts paid for a particular month pursuant to a judgment under this act shall be credited against the amount accruing for the same month under any other order of support for the child, up to the amount of the current support obligation for that month.

(c) When the assistance provided during a month is on behalf of more than one person, the amount of assistance provided on behalf of one person for that month shall be determined by dividing the total assistance by the number of people on whose behalf assistance was provided.

(d) Except as provided in subsection (b), a child's parent, parents or guardian shall be liable to repay to an agency or subdivision of another state any assistance substantially similar to that defined in subsection (d) of K.S.A. 39-702 and amendments thereto which has been expended in the other state on the child's behalf, regardless of the specific program under which the assistance is or has been provided. When more than one person is legally obligated to support the child, liability to the agency or subdivision shall be joint and several.

(e) Actions authorized herein are in addition to and not in substitution for any other remedies.

History: L. 1988, ch. 218, § 5; July 1.

CASE ANNOTATIONS

1. Parent's obligation to repay SRS for assistance noted; obligation held ended when parental rights voluntarily terminated (38-125 et seq.). State ex rel. Secretary of SRS v. Clear, 248 K. 109, 116, 804 P.2d 961 (1991).

2. Fact that conception results from violation of 21-3503 does not relieve victim of duty of support. State ex rel. Hermesmann v. Seyer, 252 K. 646, 648, 655, 847 P.2d 1273 (1993).

39-719.

History: L. 1937, ch. 327, § 17; Repealed, L. 1939, ch. 203, § 1; April 4.

Revisor's Note:

L. 1939, ch. 203, § 2 reads as follows: "All liens heretofore taken under the provision of section 39-719 of the General Statutes Supplement of 1937 are hereby discharged and canceled: Provided, The repealing of this section shall not affect any judgment rendered at the time this act becomes effective."

CASE ANNOTATIONS

1. Lien provision held constitutional. Hawkins v. Social Welfare Board, 148 K. 760, 761, 762, 764, 84 P.2d 930.

2. History of section and similar sections discussed in construing 39-713. In re Estate of Butler, 159 K. 144, 147, 152 P.2d 815.

39-719a. Recovery of medical assistance paid; obligation of third party; payment by secretary secondary costs paid proportionately by parties as determined by court. (a) Where medical assistance has been paid by the secretary and a third party has a legal obligation to pay such medical expenses to or on behalf of the recipient, the secretary may recover the same from the recipient or from the third party and shall be in all respects subrogated to the rights of the recipient in such cases except as provided under K.S.A. 39-786 and 39-787, and amendments thereto, or under section 303 and amendments thereto of the federal medicare catastrophic coverage act of 1988, whichever is applicable. Payment of medical assistance by

25-2

the secretary shall be secondary to any other insurance coverage or third party with a legal obligation to pay such medical expenses to or on behalf of the recipient.

(b) Pursuant to this section unless otherwise agreed, the court shall fix attorney fees, which shall be paid proportionately by the secretary and the injured person, such person's dependents or personal representatives, in the amounts determined by the court. Attorney fees to be paid by the secretary shall be fixed by the court in an amount not to exceed 1/4 of the medical assistance recovered pursuant to subsection (a) for cases settled prior to trial, or in an amount not to exceed 2/5 of the medical assistance recovered pursuant to subsection (a) in cases when a trial is convened.

(c) In the event of a recovery pursuant to K.S.A. 60-258a, and amendments thereto, the secretary's right of subrogation shall be reduced by the percentage of negligence attributable to the injured person.

History: L. 1953, ch. 224, § 1; L. 1967, ch. 245, § 7; L. 1969, ch. 226, § 6; L. 1970, ch. 168, § 1; L. 1973, ch. 186, § 12; L. 1988, ch. 143, § 9; L. 1989, ch. 124, § 3; L. 1991, ch. 119, § 1; July 1.

Cross References to Related Sections:
Duty to support certain patients, see 59-2006, 76-1936.

Research and Practice Aids:
Social welfare assistance as demands, Kansas Probate Law and Practice § 801.

Law Review and Bar Journal References:
Nature, determination and effect upon homestead law of claim considered, opinion of attorney general, 2 K.L.R. 212, 213 (1953).

Retrospective operation of statute considered, opinion of attorney general, 2 K.L.R. 215 (1953).

"More Goo for Our Tort Stew: Implementing the Kansas Collateral Source Rule," James Concannon and Ron Smith, 58 J.K.B.A. No. 2, 19, 23, 28 (1989).

"Medicaid Eligibility For Nursing Home Care: Understanding The New Eligibility Rules," Patrick H. Donahue, 59 J.K.B.A. No. 4, 26, 27 (1990).

CASE ANNOTATIONS

1. Claim for assistance supplied previously deceased spouse is a demand against estate of surviving spouse; not barred by nonclaim statute. In re Estate of Schwarz, 197 K. 267, 268, 269, 270, 271, 272, 273, 416 P.2d 760.

2. Section construed; amount recoverable hereunder limited to the assistance furnished to either or both of a married couple during the marriage relationship. State Department of Social Welfare v. Dye, 204 K. 760, 761, 762, 763, 764, 466 P.2d 354.

3. Mentioned in case holding that probate court may charge the cost of administering a no-asset estate to the creditor who petitioned for administration of the estate. State Department of Social Welfare v. Emert, 205 K. 393, 394, 469 P.2d 435.

39-719b. Duty of recipient to report changes which affect eligibility; actions by secretary; recovery of assistance obtained by ineligible recipient. If at any time during the continuance of assistance to any person, the recipient thereof becomes possessed of any property or income in excess of the amount ascertained at the time of granting assistance, or if any of the recipient's circumstances which affect eligibility to receive assistance change from the time of determination of eligibility, it shall be the duty of the recipient to notify the secretary immediately of the receipt or possession of such property, income, or of such change in circumstances affecting eligibility and said secretary may, after investigation, cancel or modify the assistance payment in accordance with the circumstances.

Any assistance paid shall be recoverable by the secretary as a debt due to the state. If during the life or on the death of any person receiving assistance, it is found that the recipient was possessed of income or property in excess of the amount reported or ascertained at the time of granting assistance, and if it be shown that such assistance was obtained by an ineligible recipient, the total amount of the assistance may be recovered by the secretary as a fourth class claim from the estate of the recipient or in an action brought against the recipient while living.

History: L. 1953, ch. 224, § 2; L. 1973, ch. 186, § 13; L. 1977, ch. 151, § 1; July 1.

CASE ANNOTATIONS

1. Cited; in absence of specific statutory authority the S.R.S. cannot maintain action for punitive damages. State ex rel. Secretary of S.R.S. v. Fomby, 11 K.A.2d 138, 144, 715 P.2d 1045 (1986).

2. Funds from discretionary trust for nongrantor beneficiary not a resource for purpose of eligibility. State ex rel. Secretary of SRS v. Jackson, 15 K.A.2d 126, 128, 130, 803 P.2d 1045 (1991).

3. Action for recovery of public assistance benefits; net income from trust was an available resource. State ex rel. Secretary of SRS v. Jackson, 249 K. 635, 636, 822 P.2d 1033 (1991).

39-719c. Proof deemed prima facie evidence assistance unlawfully received. In any action or proceeding for the recovery of assistance paid to an alleged ineligible recipient of assistance, proof that the recipient of assistance possesses or did possess property or income which does or would have rendered him ineligible to reeeive such assistance shall be deemed prima facie evidence that such assistance was unlawfully received.

History: L. 1953, ch. 224, § 3; June 30.

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STATE OF MISSISSIPPI

OFFICE OF THE ATTORNEY GENERAL

MIKE MOORE
ATTORNEY GENERAL

FAX TRANSMITTAL

JUNE 7, 1996

TO: **Attorney General Carla J. Stovall and Tobacco Contact**

FAX: **913/296-6296**

FROM: **MISSISSIPPI ATTORNEY GENERAL MIKE MOORE**

In addition to the tobacco meeting open to all states from 3:30 p.m. to 5:00 p.m. on Tuesday, June 11th, several states already committed to the litigation have suggested that an opportunity be provided for those states to meet to discuss issues related to ongoing cooperation and information sharing among filed states. To accommodate this interest, the Hawthorne II Room has been reserved for Sunday morning, June 9th, from 9:00 a.m. to 11:00 a.m. This time does not conflict with the formal NAAG meeting program.

The Sunday meeting is for those states who have filed, publicly announced their intention to file, or who are preparing to file, tobacco medical expenses reimbursement cases. I know that representatives from Minnesota, Mississippi, Florida and Massachusetts are planning to attend this session and hope that other litigating state attorneys general or their staff can join us as well. See you in St. Louis!

cc: Attorney General Harshbarger
Attorney General Humphrey
Chris Milliken

For problems receiving documents, contact: Nancy East 601/359-3692

House Taxation
Date 2/15/00
Attachment # 26-1

STATE OF MISSISSIPPI

OFFICE OF THE ATTORNEY GENERAL

MIKE MOORE
ATTORNEY GENERAL

MEMORANDUM

TO: ATTORNEY GENERAL

FROM: ATTORNEY GENERAL MIKE MOORE

DATE: APRIL 25, 1996

RE: TOBACCO LITIGATION UPDATE

We have scheduled a one-day tobacco litigation update and conference for Friday, May 3, 1996, in Chicago, Illinois. (Agenda attached)

PLACE: O'Hare Hilton
Chicago, Illinois

TIME: 8:00 a.m. to 5:00 p.m.

A block of rooms have been reserved for Thursday, May 2, 1996 under the name *"Attorneys General Conference."* Reservations can be made by calling the hotel at 301/686-8000. The cost of each room is $145.00. The hotel and conference room are located within O'Hare Airport.

Reservations must be made prior to Tuesday, April 30, 1996.

CARROLL GARTIN JUSTICE BUILDING • POST OFFICE BOX 220 • JACKSON, MISSISSIPPI 39205-0220 • TELEPHONE (601) 359-3680 • FAX (601) 359-3441

26-2

Mark B. Hutton · †
Andrew W. Hutton

Derek S. Casey ·
Anne H. Pankratz
Christopher P. Christian
Chan P. Townsley --

· Also Admitted in Oklahoma
-- Also Admitted in Missouri
† Certified Trial Advocate
National Board of Trial Advocacy

HUTTON & HUTTON

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Products Liability
(316) 686-1242
Facsimile
(316) 686-2049

Tax I.D.# 48-0966751

April 10, 1996

SENT VIA FACSIMILE
TO (913) 296-6296
AND VIA REGULAR MAIL

Ms. Carla Stovall
Attorney General
2nd Floor, Judicial Center
Topeka, KS 66612-1567

Re: Cigarette Litigation

Dear Attorney General Stovall:

Mark and I would like to thank you for allowing us to meet with you on April 8, 1996. Consistent with our oral representation, we would like to head up a litigation team against the tobacco cartel in a state action for Medicaid reimbursement, similar to that which is being done in West Virginia, Minnesota, Florida, Mississippi, Massachusetts, Texas and Louisiana. We would bear all the litigation costs and expenses, and be paid on a 25 percent contingent fee basis. John Campbell mentioned possibly having Morrison & Hecker involved and we would welcome their assistance. Further, we would welcome your input in the selection of other lawyers to assist us in this major undertaking.

We are doing research on Kansas law to determine what particular cause of action exists, including any special violation of consumer protection statutes. We have found out that West Virginia seeks to hold cigarette manufacturers, cigarette distributors, public relation firms, cigarette component manufacturers, the Council for Tobacco Research, and the Tobacco Institute, Inc. liable for smoking-related diseases.

West Virginia seeks recovery under 10 theories: restitution/unjust enrichment; common-law public nuisance; negligent performance of a voluntary undertaking; fraud (intentional misrepresentation); conspiracy and concert of action; aiding and abetting liability; consumer protection violations; antitrust violations; injunctive relief; and declaratory judgment.

House Taxation
Date 2/15/00
Attachment # 27-1

Mississippi states four theories for recovery: restitution/unjust enrichment; indemnity; public nuisance; and injunctive relief.

Minnesota claims 10 theories for recovery: undertaking a special duty; antitrust law (conspiracy to unreasonably restrain trade and commerce); antitrust law (monopoly); consumer fraud; unlawful trade practices; deceptive trade practices; false advertising; restitution (performance of another's duty to the public); restitution (unjust enrichment); and conspiracy.

Florida also claims 10 theories for recovery: restitution/unjust enrichment; indemnity; negligence; strict liability; breach of express and implied warranties; negligent performance of a voluntary undertaking; fraud and intentional misrepresentation; conspiracy and concert of action; aiding and abetting liability; and injunctive relief.

We are excited about working with you and the State of Kansas in an effort to provide reimbursement for tax monies spent due to the manufacture of a drug intentionally designed to cause addiction, disease and death. We are equally enthusiastic of the opportunity assist in the prevention of the targeting, marketing and sale of cigarettes to the children of Kansas.

Very truly yours,

Andrew W. Hutton

AWH/sm

Mark B. Hutton · †
Andrew W. Hutton

Derek S. Casey ·
Anne H. Pankratz
Christopher P. Christian
Chan P. Townsley ··

· Also Admitted in Oklahoma
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April 10, 1996

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TO (913) 296-6296
AND VIA REGULAR MAIL

Ms. Carla Stovall
Attorney General
2nd Floor, Judicial Center
Topeka, KS 66612-1567

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West Virginia seeks recovery under 10 theories: restitution/unjust enrichment; common-law public nuisance; negligent performance of a voluntary undertaking; fraud (intentional misrepresentation); conspiracy and concert of action; aiding and abetting liability; consumer protection violations; antitrust violations; injunctive relief; and declaratory judgment.

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Very truly yours,

Andrew W. Hutton

AWH/sm

28.2

MORRISON & HECKER L.L.P.
ATTORNEYS AT LAW

2600 Grand Avenue
Kansas City, Missouri 64108-4606
Telephone 816-691-2600
Telefax 816-474-4208

Mary L. Barrier

April 10, 1996

VIA FEDERAL EXPRESS

Carla Stovall, Esq.
Attorney General
Judicial Center
301 S.W. 10th Avenue
Topeka, Kansas 66612

Re: Proposed State Suit Against Tobacco Companies

Dear Carla:

Thank you for taking the time to meet with Bob Vancrum and me.

Enclosed is a copy of the Liggett settlement which we discussed. The Agreement provides for an "Attorney General Settlement Fund" to be administered by an "Attorney General Board." The initial settling defendants share the initial five million dollar settlement payment. One million dollars was to be paid immediately; the remaining four million is to be paid in equal annual installments over nine years. In addition, annual payments, the greater of 2.5% of Liggett's pretax income or $30 million per year, are to be paid over a 25 year period.

States which were not parties at the time of the March 15, 1996 settlement may join. A fund will be established for states filing after the settlement who wish to participate. Initially, $25 million will be paid to this fund. The share of subsequent settling defendant states is to be determined by the ratio of that state's Medicaid population to the total Medicaid population of 10,000,000 (reduced by the population of the initial settling states) multiplied by 5% of Liggett's pretax income, or $50 million, whichever is greater. Additional formulas are provided in the event other defendants settle. These settlement funds might be available to help defray the costs of any action brought on behalf of Kansas should the state opt in to the Settlement Agreement.

House Taxation
Date 2/15/00
Attachment # 29-1

As John noted during our meeting, the Agreement also provides settling defendants can terminate the Agreement if nonsettling defendants win on the merits, or "too many" states file attorney general actions and do not join the settlement. What is "too many" is within the sole discretion of settling defendants.

Again, it was a pleasure to meet with you and John Campbell. If there is anything further I can do to assist you in your evaluation of the proposed suit, or your selection of a firm, please let me know.

Sincerely,

MORRISON & HECKER, L.L.P.

Mary Barrier

Mary L. Barrier

MLB/sm

Enclosure

cc: Robert J. Vancrum, Esq. (w/o encl.)

MLBØWM.KCM

29-2

ATTORNEYS GENERAL SETTLEMENT AGREEMENT

This SETTLEMENT AGREEMENT is entered into this 15th day of March, 1996 by and among the State of West Virginia, State of Florida, State of Mississippi, Commonwealth of Massachusetts, and State of Louisiana (collectively, "Plaintiffs") and Brooke Group Ltd., a Delaware corporation ("Brooke Group"), Liggett & Myers, Inc., a Delaware corporation ("Myers"), and Liggett Group, Inc., a Delaware corporation (which, with Myers, is hereinafter referred to as "Liggett").

R E C I T A L S

WHEREAS,

A. On or about May 23, 1994, the State of Mississippi, by and through its Attorney General, Mike Moore, brought an action entitled Moore v. The American Tobacco Co., et al., CN 94-1429, Chancery Court of Jackson County, Mississippi, against, among others, the American Tobacco Company, Inc., R.J. Reynolds Tobacco Company, Brown & Williamson Tobacco Corporation, Philip Morris, Inc., Liggett & Myers, Inc., Lorillard Tobacco Company, Inc., and United States Tobacco Company and their various parent and related companies ("Defendants"), asserting claims for, among other things, expenses allegedly arising from tobacco-related matters and injunctive relief concerning sales of cigarettes to minors (the "Mississippi Action").

B. On or about September __, 1994, the State of West Virginia, by and through its Attorney General Darrell V. McGraw, Jr., brought an action entitled McGraw v. The American Tobacco Co., et al., 94-C-1707, Circuit Court of Kanawha County, West

Virginia, against, among others, the Defendants asserting similar claims (the "West Virginia Action").

C. On or about February 21, 1995, the State of Florida, by and through its Attorney General Robert Butterworth, brought an action entitled The State of Florida, Lawton M. Chiles, Jr., Individually and as Governor of the State of Florida, Department of Business and Professional Regulation, and the Agency for Health Care Administration v. The American Tobacco Co., et al., CN 95-1466, Fifteenth Judicial Circuit, Palm Beach County, Florida, against, among others, the Defendants asserting similar claims (the "Florida Action").

D. On or about December 19, 1995, the Commonwealth of Massachusetts, by and through its Attorney General Scott Harshbarger, brought an action entitled Commonwealth of Massachusetts v. Philip Morris Inc., et al., Civil No. 95-7378, Massachusetts Superior Court, against, among others, the Defendants asserting similar claims (the "Massachusetts Action").

E. On or about March 13, 1995, the State of Louisiana, by and through its Attorney General Richard P. Ieyoub, brought an action entitled Richard P. Ieyoub, Attorney General ex rel, State of Louisiana v. The American Tobacco Company, et al., Civil No. 96-1209, 14th Judicial District Court, Parish of Calcasieu, State of Louisiana, against, among others, the Defendants asserting similar claims (the "Louisiana Action").

F. Other States are reportedly planning to bring or are considering bringing actions similar to the above-mentioned actions.

G. On or about March 12, 1996, Brooke Group, Liggett and the plaintiffs in an action entitled Dianne Castano, et al. v. The American Tobacco Company, Inc., Civil No. 94-1044, United States District Court for the Eastern District of Louisiana ("Castano"), entered into a national class settlement, subject to, among other things, court approval, with respect to a putative class of allegedly nicotine-dependent smokers and their families.

H. Brooke Group and Liggett have denied, and continue to deny, each and all of the claims and contentions alleged by the plaintiffs in each and all of the above-mentioned actions, and have denied, and continue to deny, any wrongdoing or any legal liability of any kind.

I. Plaintiffs and Brooke Group and Liggett recognize and support the public interest in preventing smoking by, or promotion of smoking to, children and adolescents.

J. The Food and Drug Administration ("FDA") has proposed certain new regulations purportedly concerning the sale and distribution of nicotine-containing cigarettes and smokeless tobacco products to children and adolescents.

K. Brooke Group and Liggett recognize and acknowledge that defending the continued prosecution of the Attorney General Actions against them through trial and appeals would require considerable resources and expense and would entail uncertainty and risk. Brooke Group and Liggett have determined that the settlement, in accordance with this Agreement, of the claims in the Attorney General Actions against them will be beneficial to Brooke Group and Liggett.

L. The Settling States and the Attorneys General recognize and acknowledge that the continued prosecution of the Attorney General Actions against Brooke Group and Liggett through trial and appeals would require considerable time and expense and would entail uncertainty, risk and delay. The Settling States and the Attorneys General have determined that the settlement, in accordance with this Agreement, of the claims in the Attorney General Actions against Brooke Group and Liggett will be beneficial to their respective States.

NOW, THEREFORE, in consideration of the foregoing and of the promises and covenants set forth in this Agreement, the undersigned Attorneys General, on their own behalf and on behalf of their respective States, and Brooke Group and Liggett hereby stipulate

and agree that the Attorney General Actions shall be settled as against Brooke Group, Liggett, and upon such Future Affiliate becoming bound by this Agreement, a Future Affiliate (as defined hereinbelow) of Liggett or Brooke Group and that all claims asserted in the Attorney General Actions against Brooke Group, Liggett and such Future Affiliate shall be dismissed, all on the terms contained herein, as follows:

1. Definitions

As used in and solely for the purpose of this Agreement, the following terms shall have the following respective meanings:

"Affiliate" means a Present Affiliate or a Future Affiliate.

"Agreement" means this Settlement Agreement.

"Attorney General Actions" means the Mississippi Action, the West Virginia Action, the Florida Action, the Massachusetts Action, and the Louisiana Action or any similar action commenced by or on behalf of the other States against the Defendants.

"Attorney General Settlement Fund" means the fund established as provided in Section 5 of this Agreement.

"Attorney General Settlement Fund Board" or "Attorney General Board" and "Attorney General Board Document" mean, respectively, the entity to be established as provided in Section 5 of this Agreement and the document or documents that the Attorneys General of the Settling States shall enter into by which the Attorneys General of the Settling States, or their respective designees shall administer, among other things, the Attorney General Settlement Fund provided for under the terms of this Agreement.

"Brooke Group" means Brooke Group, Ltd. and its Present Affiliates other than Liggett.

"Castano Settlement Agreement" means the settlement entered into as of March 12, 1996 by the plaintiffs in Castano and Brooke Group and Liggett.

"Defendants" means the American Tobacco Company, Inc., R.J. Reynolds Tobacco Company, Brown & Williamson Tobacco Corporation, Philip Morris, Inc., Liggett & Myers, Inc., Lorillard Tobacco Company, Inc., and United States Tobacco Company and their various parent and related companies.

"Domestic Tobacco Operations" means the manufacture and/or sale of cigarettes in the United States and its possessions.

"Future Affiliate" means any one entity, other than an entity with a Market Share greater than 30% as of the date of this Agreement, which is a defendant in the Attorney General Actions and which, with the prior written approval of Brooke Group, subsequent to the date, and during the term, of this Agreement but prior to the fifth anniversary (subject to the $5 million payment required by Section 5.10) of the date of this Settlement Agreement: (i) directly or indirectly acquires or is acquired by Liggett or Brooke Group; (ii) which directly or indirectly acquires all or substantially all of the stock or assets of Liggett or Brooke Group; (iii) all or substantially all of whose stock or assets are directly or indirectly acquired by Brooke Group or Liggett; or (iv) directly or indirectly merges with Brooke Group or Liggett or otherwise combines on any basis with Liggett or Brooke Group.

"Inflation" means the percentage by which the national Consumer Price Index for all urban consumers issued by the Bureau of Labor Statistics of the U.S. Department of Labor increases or decreases for the relevant period. The beginning index figure shall be the consumer price index for March 1996.

"Initial Settling States" means the States of Mississippi, West Virginia, Florida, the Commonwealth of Massachusetts, Louisiana, and the respective Attorneys General thereof.

"Liggett" means Liggett Group, Inc. and Liggett & Myers, Inc.

"Market Share" means, with respect to a Defendant and a specified year, the domestic market share in that year of all of such Defendant's tobacco products, as determined by The Maxwell Consumer Report published by Wheat First Butcher Singer or a comparable successor report.

"Medicaid Population" means, with respect to a Settling State and a specified date, the Medicaid population of such Settling State as reported by the most recent United States Census.

"Non-settling Defendant" means each of the American Tobacco Co., Lorillard Tobacco Co., Philip Morris Inc., R.J. Reynolds Tobacco Co., Brown & Williamson Tobacco Corp., and United States Tobacco Co., unless and until it becomes a Settling Defendant, as hereinafter defined.

"Parties" means the Plaintiffs, Brooke Group, Liggett and any other Settling Defendant, as hereinafter defined, if, as and when such Settling Defendant becomes bound by this Agreement.

"Present Affiliate" means, with respect to a specified corporation or entity, another corporation, partnership or other entity which as of the date of this Agreement, directly or indirectly, controls, is controlled by, or is under common control with, such specified corporation.

"Present Value" means, with respect to a specified amount or amounts, the present value of such amount or amounts as calculated using a discount rate equal to the yield on 10-year Treasury Notes as reported in the Wall Street Journal at the time of such calculation.

"Pretax Income," with respect to a specified Settling Defendant other than Liggett for a specified year, means the operating income (or equivalent designation) from Domestic

Tobacco Operations of the Settling Defendant and its affiliates, on a consolidated basis, as determined in accordance with generally accepted accounting principles ("GAAP") for the Settling Defendant's most recent fiscal year, as reported in filings to the United States Securities and Exchange Commission or, if there is no such filing, as reported by the Settling Defendant's independent outside auditors. For purposes of the consolidation intended hereby, interest expenses on parent company debt and parent company corporate and other expenses, less amortization of parent company acquisition goodwill, shall be allocated pro rata to all operating units according to operating income. If GAAP changes in any material respect during the term of this Agreement so that the benefits anticipated by the parties (in light of GAAP applicable on the date of this Agreement), an appropriate adjustment shall be made to the formulas and calculations hereunder to achieve the parties' expectations as of the date hereof.

"Pretax Income," with respect to Liggett, means for a specified year, the "Income before Income Taxes" as determined in accordance with generally accepted accounting principles ("GAAP") of Liggett for its most recent fiscal year, as reported in filings to the United States Securities and Exchange Commission or, if there is no such filing, as reported by Liggett's independent outside auditors. If GAAP changes in any material respect during the term of this Agreement so that the benefits anticipated by the parties (in light of GAAP applicable on the date of this Agreement), an appropriate adjustment shall be made to the formulas and calculations hereunder to achieve the parties' expectations as of the date hereof.

"Proposed Rule" means the regulations proposed by the FDA concerning the sale and distribution of cigarettes and other products, dated August 9, 1995, published at 21 C.F.R. Parts 801, 803, 804, and 897, and bearing document number 95N-0253.

"Settling Defendants" means Brooke Group, Liggett and, if, as, and when it joins in this Agreement, one Future Affiliate; provided that in the event of any corporate restructuring, reorganization or spinoff involving any Settling Defendant, only the entity or entities which, affect such reorganization or spinoff, retain the Domestic Tobacco Operations of such Settling Defendant shall thereafter be treated as the Settling Defendant for purposes of the payment obligations of Section 6 of this Agreement.

"Settling Defendants' Counsel" means the law firm of Kasowitz, Benson, Torres & Friedman L.L.P.

"Settling States" means the Initial Settling States and Subsequent Settling States, if any.

"Smoking Claims Expense" means, with respect to a specified year, the aggregate amount of the out-of-pocket expenses paid during that year by a Settling Defendant for the payment of legal fees and costs, including attorney's fees, and any settlements (other than payments made pursuant to the Castano settlement) or judgments, in connection with litigation arising from smoking-related claims other than the Attorney General Actions (or other civil cases pending on January 1, 1996).

"Subsequent Settling States" means States other than the Initial Settling States which commence an Attorney General Action and which become bound by this Agreement pursuant to Section 3.1 hereof prior to six months from the date of this Agreement (unless such six-month period is extended or reopened at the option of the Settling Defendants).

2. Settlement Purposes Only.

2.1. This Agreement is for settlement purposes only, and neither the fact of, or any provision contained in, this Agreement nor any action taken hereunder shall constitute, be construed as, or be admissible in evidence as, any admission of the validity of any claim, any

argument or any fact alleged or which could have been alleged by Plaintiffs as to their standing or as to any jurisdictional, constitutional or any other legal or factual issue in any Attorney General Action or alleged or which could have been alleged in any other action or proceeding of any kind or of any wrongdoing, fault, violation of law, or liability of any kind on the part of any of the Settling Defendants or any admission by any of them of any claim or allegation made or which could have been made in any Attorney General Action or in any other action or proceeding of any kind, or as an admission by any of the Plaintiffs of the validity of any fact or defense asserted against them in any Attorney General Action or in any other action or proceeding of any kind.

2.2. Nothing contained in this Agreement shall constitute or be construed as any admission of the validity of the FDA's assertion of jurisdiction over cigarettes or any other product.

3. Parties.

3.1. This Agreement shall be binding, in accordance with the terms hereof, upon Brooke Group, Liggett and the Future Affiliate and the Initial Settling States and each Subsequent Settling State upon its execution of a copy of this Agreement; provided that the payment obligations of this Agreement shall be binding only upon the Affiliates of such Settling Defendants which are engaged in the Domestic Tobacco Operations.

3.2. The Settling States shall not seek to enjoin a spinoff or like disposition of the stock of Nabisco Holdings Inc. by RJR Nabisco Holdings Corp. in the event that a slate of nominees proposed by Brooke Group for election to the RJR Nabisco Holdings Corp. Board of Directors is elected.

4. Advertising Limitations.

4.1. Each Settling Defendant, promptly after the later of the Settlement Date and the date said Settling Defendant becomes bound by this Agreement, shall (i) withdraw its objections and opposition to the Proposed Rule and to the assertion of jurisdiction by the FDA for the sole purpose of promulgating the Proposed Rule with respect to all Defendants; (ii) file pleadings or other documents necessary to effectuate such withdrawal; and (iii) withdraw as a party from litigation against state officials in the Settling States related to the tobacco litigation. By withdrawing said opposition and objections, Settling Defendants do not and shall not be deemed to consent to or acknowledge such jurisdiction and do not and shall not be deemed to waive or abandon said opposition and objections in the event this Agreement is terminated. Each Settling Defendant, notwithstanding the foregoing, may object to or oppose the Proposed Rule to the extent that compliance is impractical or excessively expensive. If, prior to the Proposed Rule taking final nonappealable effect as to the tobacco industry generally, the FDA asserts that it has acquired or can or should acquire jurisdiction to promulgate or enforce the Proposed Rule as to a Settling Defendant by virtue of its entry into or compliance with this Agreement, then, in such event, this Section 4 and its subparts shall be null and void ab initio in their entirety.

4.2. Each Settling Defendant shall follow and abide by the provisions of the Proposed Rule, insofar as they pertain solely to such Settling Defendant's Domestic Tobacco Operations, as set forth in, and modified by, paragraphs 4.2.1 to 4.2.9 hereof until a final determination is reached respecting the Proposed Rule, at which time the Settling Defendants will be bound by the Rule only insofar as, and to the extent that the Rule becomes an enforceable obligation binding upon all of the Settling Defendants and Non-Settling Defendants.

4.2.1. Proposed Rule ss. 897.16(a), but only to the extent that such section applies to a trade or brand name of a non-tobacco product which is in use in the United States and has a demonstrated or likely appeal to minors; provided that in any dispute hereunder, the Settling Defendant shall have the burden to show compliance with this Subsection in binding arbitration.

4.2.2. Proposed Rule ss. 897.16 (b), as proposed.

4.2.3. Proposed Rule ss. 897.16 (d), except to the extent free samples are distributed under circumstances where no minors are present or likely to be present.

4.2.4. Proposed Rule ss. 897.30 (a), as proposed.

4.2.5. Proposed Rule ss. 897.30 (b), but only to the extent that such section applies to billboards within 1,000 feet of a clearly marked and state-licensed elementary or secondary school or a clearly marked, outdoor, municipal or other government-operated public playground for children.

4.2.6. Proposed Rule ss. 897.32(a), except that the requirements of such section will be applicable only to a publication whose regular readers aged less than eighteen years constitute 15% or more of the publication's total regular readership; provided that for those publications in which the Settling Defendants currently advertise which exceed the 15% rotation, Settling Defendants will, through incremental reduction, meet the requirements of this rule within a period of five (5) years.

4.2.7. Proposed Rule ss. 897.34(a), to the extent such section applies to clothing or outerwear or to any items or services, other than clothing or outerwear, which have not prior to the date of this Agreement been marketed, licensed, distributed or sold, and which are more likely to appeal to minors than to adults; provided that such section does not apply to

any clothing, outerwear, items or services customarily marketed, licensed, distributed or sold at the site and at the time of events permissible under Section 4.2.9 of this Agreement.

4.2.8. Proposed Rule ss. 897.34(b), to the extent that gifts or items distributable or redeemable pursuant to this rule are more likely to appeal to minors than to adults.

4.2.9. Proposed Rule ss. 897.34(c), except that such section will be applicable only to an athletic, musical, artistic or other social or cultural event whose past patrons or attendees aged less than eighteen years constitute 15% or more of the event's total past patronage or attendance; provided that this section does not apply to any events that Settling Defendants have sponsored, conducted, engaged or participated in within the last ten years.

4.3. Notwithstanding anything to the contrary in the Proposed Rule or in this Agreement, each such Settling Defendant will commence compliance with Section 4.2 of this Agreement, according priority as to compliance to the Initial Settling States and then to Subsequently Settling States as soon as reasonably practicable; provided that such Settling Defendant may limit its compliance to the extent, if any, necessary to ensure that the net annual out-of-pocket cost to the Settling Defendant of such compliance not exceed $1 million; and provided further that such Settling Defendant shall not be obligated pursuant hereto to breach pre-existing legal obligations, if any, it may have with respect to the matters covered by Section 4.2 (and shall use its reasonable best efforts to minimize the degree to which any such obligations would impede its full compliance therewith). For purposes of this paragraph, the phrase "net annual out-of-pocket costs" means the excess of (a) the additional out-of-pocket expenditures incurred during a particular year by a particular Settling Defendant in complying with the matters specified in Section 4.2, over (b) savings, if any, in out-of-pocket expenditures realized during such year by such Settlement Defendant directly from the implementation of the matters covered by Section 4.2.

4.4. If, when and to the extent that the Proposed Rule, in whole or in part, becomes an enforceable legal obligation binding upon all of the Defendants, each Settling Defendant will comply therewith.

4.5. As promptly as reasonably practicable after becoming bound by this Agreement, each Settling Defendant shall eliminate cartoon characters, such as "Joe Camel," from all of its advertising and promotional materials and activities with respect to tobacco products.

4.6. Each Settling Defendant other than Brooke Group and Liggett shall contribute to a fund to be administered by the Attorneys General of the Settling States, the amount of $250,000 per year, per Initial Settling State, for a period of three years from the date such Settling Defendant becomes bound by this Agreement for the purposes of monitoring the point-of-sale advertising amounts, types, locations, and proximity to schools, in the Initial Settling States.

5. Attorney General Settlement Fund.

5.1. All amounts due and owing by Settling Defendants under this Agreement shall be paid when due into the Attorney General Settlement Fund to be administered, allocated and distributed by the Attorney General Board to Settling States in accordance with this Agreement and the Attorney General Board Document; it being understood that payments shall be first applied by each Settling State to compensate state health care programs bearing the greatest percentage of state taxpayer contribution.

5.2. Settling Defendants shall have no interest in or responsibility for allocations or distributions from the Attorney General Settlement Fund and do not guarantee any earnings or insure against any losses from any portion of the Attorney General Settlement Fund assets that may be maintained or administered as provided in Section 5.1 above.

5.3. Liggett shall pay into the Attorney General Settlement Fund (a) for the benefit of the Initial Settling States, an initial amount equal to five million dollars ($5,000,000), of which one million dollars ($1,000,000) shall be payable within five business days of the date of this Agreement and the remaining four million dollars ($4,000,000) shall be paid in equal annual installments, indexed and adjusted for Inflation, over the following nine years during the term of this Agreement (except that any then remaining unpaid amount under this Section 5.3(a) shall be due and payable within sixty (60) days of the date (i) a Future Affiliate becomes bound by this Agreement or (ii) Liggett defaults on any of its payment obligations under this Agreement) and (b) in each year beginning in the second year during the term of this Agreement (i) for the benefit of the Initial Settling States, an annual amount equal to 2.5% of Liggett's Pretax Income and (ii) for the benefit of each Subsequent Settling State, if any, an annual amount equal to the product of (A) the ratio that the Medicaid Population of such Subsequent Settling State then bears to a total Medicaid Population of ten million (10,000,000) reduced by the Medicaid Population of the Initial Settling States and (B) 5% of Liggett's Pretax Income; provided, however, that in no event shall the aggregate amount to be paid under clause (b)(ii) of this Section 5.3 ever exceed 5% of Liggett's Pretax Income. The Attorney General Board shall make all decisions regarding payments to the Settling States hereunder.

5.4. The Future Affiliate shall, within sixty (60) days of the date such Settling Defendant becomes bound by this Agreement, (a) pay into the Attorney General Settlement Fund, for the benefit of the Initial Settling States, an aggregate amount equal to one hundred thirty-five million dollars ($135,000,000), and (b) make available an amount up to twenty-five million dollars ($25,000,000) to be paid at the direction of the Attorneys General Board to Subsequent Settling States in connection with their joining this Agreement.

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5.5. The Future Affiliate shall, commencing one year after the date such Settling Defendant becomes bound by this Agreement and on each anniversary of such date during the term of this Agreement, pay into the Attorney General Settlement Fund (a) for the benefit of the Initial Settling States, an amount equal to 2.5% of such Settling Defendant's Pretax Income, provided that the amounts payable under this Section 5.5(a) shall not be less than thirty million dollars ($30,000,000) per year (except as otherwise provided herein), indexed and adjusted for Inflation, and (b) for the benefit of each Subsequent Settling State, if any, an annual amount equal to the product of (i) the ratio that the Medicaid Population of such Subsequent Settling State then bears to a total Medicaid Population of ten million (10,000,000) reduced by the Medicaid Population of the Initial Settling States and (ii) 5% of the Settling Defendant's Pretax Income; provided, however, that in no event shall the aggregate amount to be paid under clause (b)(ii) of this Section 5.5 ever exceed 5% of Liggett's Pretax Income in the aggregate.

5.6. With respect to each Settling State, in the event of the entry of any final non-appealable monetary judgment in such Settling State's Attorney General Action (other than by way of settlement) against any one or more of the Non-Settling Defendants, then each Settling Defendant shall have the right to reduce the payments it is obligated to make pursuant to this Agreement to the extent necessary to make (i) the then Present Value of all amounts theretofore paid and thereafter payable to that Settling State pursuant to this Agreement by any Settling Defendant per percentage point of the then Market Share of such Settling Defendant no more than seventy-five percent (75%) of (ii) the then Present Value of the dollar amount of such judgment per percentage point of the then Market Share of each such Non-Settling Defendant; provided that such Settling Defendant give written notice of such reduction and the method of calculating such reduction to the Settling State's Attorney

General as soon as practicable after the entry of judgment; and provided further that to the extent any such reduction would reduce the Settling Defendant's annual payment to less than $30 million, indexed and increased for Inflation such Settling Defendant shall have the right to reduce payments it is obligated to make under this Agreement only to the extent necessary to make the quotients in Sections 5.6(i) and (ii) equal.

For purposes of this Section 5.6, computations based on future payments due any of the Initial Settling States shall be based on the minimum payments in Sections 5.3 and 5.5, indexed and increased for inflation at 5% per annum (computations based on future payments due any Subsequent Settling States shall assume, solely for this purpose, that each such state would be entitled to a payment proportionate to the total minimum payments due the Initial States (as so indexed and increased above), adjusted solely for relative size of Medicaid Population.

5.7. Each Settling Defendant shall, during the term of this Agreement, have the right to a credit against amounts due in each year pursuant to this Agreement in an amount equal to fifty percent (50%) of the difference between (a) such Settling Defendant's Smoking Claims Expense in the prior year and (b) such Settling Defendant's Smoking Claims Expense for the twelve months prior to the date of this Agreement; provided that the amount of such credit shall not be greater than ten percent of the amounts that would otherwise be due from such Settling Defendant in such year; provided further that each Settling Defendant shall have the right to terminate this Agreement with respect to that Settling Defendant in the event that the amount of such difference is greater than twenty-five percent (25%) of the amount so due from such Settling Defendant in such year; and provided further that such credit shall not apply to the extent that it would render the amounts payable under Section 5.5 less than thirty million dollars ($30,000,000) per year.

5.8. With respect to each Settling Defendant, in each year beginning with the second year such Settling Defendant becomes bound by this Agreement, the annual payment amount due under Sections 5.3 and 5.5 of this Agreement from such Settling Defendant shall be decreased in proportion to any decrease and (only if there shall have been a prior such decrease) increased in proportion to any increase, in such Settling Defendant's Market Share from the prior year; provided, however, that (a) such annual payment amount shall not be so decreased to the extent, if any, that such annual payment amount in such year is decreased as a result of a decrease in such Settling Defendant's Pretax Income and (b) such annual payment amount shall never be increased such that the aggregate amount of any such increases exceeds the aggregate amount of any such decreases (and in no event more than the maximum amount set forth in Sections 5.3, 5.4 and 5.5 hereof).

5.9. Insofar as the Castano Settlement Agreement is terminated (and no settlement contemplated by Section 11.2 thereof is entered into in any putative class action subsequent to Castano), the Castano CTCIR research fund contemplated by Section 6.4(b) of the Castano Settlement Agreement shall be administered by the Attorney General Board. At the time a Future Affiliate or other entity becomes bound by this Agreement and the Castano Settlement Agreement to the extent the CTCIR Research Fund is not funded under the Castano Settlement Agreement, that $10 million shall be paid into the Attorney General Settlement Fund and used for the same or similar purposes set forth in the Castano Settlement Agreement. If at any time under the terms of the Castano Settlement Agreement the funds with regard to the CTCIR Research Fund are due and payable, all future funds shall be paid under the Castano Settlement Agreement. But if a lapse in the obligation occurs under Castano, the funds shall be paid under this Agreement.

5.10. If the Brooke Group or Liggett fails to consummate a merger or other transaction with a Non-Settling Defendant which results in the creation or acquisition of a Future Affiliate within three years of the date of the execution of this Agreement, Liggett shall pay into the Attorney General Settlement Fund $5 million for distribution to each of the Initial Settling States on an equal share basis.

5.11. No Non-Settling Defendant may become a Future Affiliate if after the date of this Agreement that Non-Settling Defendant has by spin off, sale or other transaction substantially changed its Domestic Tobacco Operations so as to result in a material reduction in Market Share caused by such voluntary corporate action. No Settling Defendant shall sell, dispose or transfer any of its cigarette brands or business without first causing the acquiror, on behalf of itself and its successors, to be bound by all of the obligations of a Settling Defendant hereunder as to such transferred brand or business.

6. Release.

6.1. Upon the effective date of this Agreement, or, in the case of a Future Affiliate, the date such Future Affiliate becomes bound by this Agreement, for good and sufficient consideration as described herein, each such Settling State and each Attorney General thereof shall for the duration or term of this Agreement (whichever is shorter) be deemed to and hereby does release, dismiss and discharge each and every civil claim, right, and cause of action (including, without limitation, all claims for damages, restitution, medical monitoring, or any other legal or equitable relief) known or unknown, asserted or unasserted, which they had, now have or may hereafter have against each such Settling Defendant (including its past and present parents, subsidiaries, affiliates, employees, directors and shareholders, but only in such capacities, vis-a-vis, each such Settling Defendant, and downstream distribution entities of Liggett or other Settling Defendant to the extent of their distribution on behalf of Liggett

or other Settling Defendant, but not including any individual Non-Settling Defendants or other defendants in the Attorney General Actions to the extent they would otherwise be part of the foregoing), (i) which was asserted in that State's Attorney General Action, and/or (ii) which was not asserted in said Action but which is smoking-related or otherwise arises out of, or concerns, the acts, facts, transactions, occurrences, representations, or omissions set forth, alleged, referred to or otherwise embraced in the complaint of that Settling State's Attorney General Action.

Upon the later of the date of each Settling Defendant becoming bound by this Agreement and the date of each Settling State becoming bound by this Agreement, for good and sufficient consideration as described herein, each such Settling Defendant shall for the duration or term of this Agreement (whichever is shorter) be deemed to and hereby does release, dismiss and discharge each and every claim, right, and cause of action (including, without limitation, all claims for damages, restitution, fees, expenses, or any other legal or equitable relief), whether known or unknown, asserted or unasserted, which they had, now have or may hereafter have as of the effective date of this Agreement against each such Settling State, its public officials and employees in connection with, arising out of or related to the acts, facts, transactions, occurrences, representations, or omissions set forth, alleged or referred to or otherwise embraced in the complaints of the settling Attorney General Actions.

Provided, however, as follows:

1) If this Agreement expires upon completion of its full term, this release shall continue in full force and effect with respect to all released claims through and including the date of such expiration, but only as to such claims through and including such date; if this Agreement terminates for any reason prior to its full term, this release shall be of no further force and effect and Settling Defendants shall be entitled to a credit to the extent otherwise

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provided in this Agreement against all claims covered by the release for the full amount paid by such Settling Defendants hereunder.

2) This release does not pertain or apply to any other existing or potential defendant in any present or future Attorney General Action, except the "Future Affiliate" which joins in and complies with the provisions of this Agreement, including but not limited to Sections 4 and 5.

6.2. Nothing in this Agreement shall prejudice or in any way interfere with the rights of Settling States or Settling Defendants to pursue any or all of their rights and remedies against Non-Settling Defendants or other parties not released hereunder.

7. Exclusive Remedy; Dismissal of Action; Jurisdiction of Court.

7.1. Except as otherwise provided in this Agreement, this Agreement shall be the sole and exclusive remedy for any and all claims of Settling States released hereby against the Settling Defendants, and upon the later of the date a Settling State becomes bound by this Agreement and the date a Settling Defendant becomes bound by this Agreement, each such Settling State shall be barred from initiating, asserting, or prosecuting any claims released hereby against each such Settling Defendant.

7.2. On the later of the date each Settling State becomes bound by this Agreement and the date a Settling Defendant becomes bound by this Agreement, each such Settling State shall dismiss without prejudice its corresponding Attorney General Action as against such Settling Defendant.

7.3. On the later of the date each Settling State becomes bound by this Agreement and the date a Settling Defendant becomes bound by this Agreement, each such Settling Defendant shall withdraw without prejudice from any action brought against any Settling State with respect to claims released hereby.

8. Term.

8.1. Unless earlier terminated in accordance with the provisions of this Agreement, the duration of this Agreement shall be twenty-five (25) years from the date of this Agreement.

8.2. Each Settling Defendant shall have the right to terminate this Agreement with respect to that Settling Defendant and with respect to the Settling State in which there is a full and final dismissal on the merits as to any of the Defendants in that Settling State's Attorney General Action; provided that in the event of any such termination, the payments due from such Settling Defendant pursuant to this Agreement shall be reduced by the amount payable to that Settling State; provided further that any and all payments made pursuant to this Agreement prior to any such termination by such Settling Defendant shall be retained by the Attorney General Settlement Fund. The Attorney General Board shall provide the Settling Defendant with the information necessary to determine the amount of such reduction.

8.3. Each Settling Defendant shall have the right at any time during the term of this Agreement to terminate this Agreement with respect to such Settling Defendant in the event that, in its sole and exclusive discretion, it determines that too many states have filed Attorney General Actions and have not resolved such cases with respect to the Settling Defendant by becoming bound by this Agreement in accordance with the terms hereof; provided that such Settling Defendant give written notice of such termination to the Attorneys General of the Settling States and provided further that any and all payments due up to the date of such termination shall be paid and all payments made pursuant this Agreement prior to the giving of such notice by such Settling Defendant shall be retained by the Attorney General Settlement Fund.

8.4. In the event of a termination of this Agreement with respect to any Settling State by any Settling Defendant, such Settling Defendant shall be entitled to offset any payments made to such Settling State prior thereto against any judgments thereafter obtained by such Settling State against such Settling Defendant in an Attorney General Action.

8.5. If any Settling Defendant subsequently withdraws from this Agreement, or this Agreement, for whatever reason, is terminated other than by reason of the expiration of its term, then the applicable statute of limitations or any similar time requirement for a Settling State or a terminating Settling Defendant to file a claim that would otherwise be released hereunder against or by any Settling Defendant shall be tolled from the date such Settling State became bound by this Agreement until the later of the time permitted by applicable law or for one year from the date of such termination with the effect that the parties shall be in the same position as they were at the time the Settling State filed its original Attorney General Action with respect to the statute of limitations.

8.6. Except as may be otherwise specifically provided in this Agreement, a termination by a Settling Defendant hereunder shall have the effect of rendering this Agreement as having no force or effect whatsoever, null and void ab initio, and not admissible as evidence for any purpose in any pending or future litigation in any jurisdiction.

9. Continuing Enforceability.

Unless earlier terminated, as to the Settling States, this Agreement and each provision of or obligation arising from this Agreement shall continue and remain fully executory and enforceable if a Settling Defendant institutes or is subject to the institution against it of any proceeding or voluntary case under title 11, United States Code, or other proceeding seeking to adjudicate it insolvent or seeking liquidation, winding up, reorganization, arrangement, adjustment, protection, relief or composition of it or its debts under any law relating to

bankruptcy, insolvency or reorganization or relief or protection of debtors or other proceeding seeking the entry of an order for relief or the appointment of a receiver, trustee, custodian or other similar official for it or for any part of its property (each, a "Bankruptcy Proceedings"). The Settling States acknowledge and agree that Brooke Group has the right but not the obligation to cure and to perform any and all obligations of Liggett under this Agreement notwithstanding the occurrence and continuation of any Bankruptcy Proceeding with respect to Liggett; provided, however, that until such time as Liggett decides whether to reject or assume this Agreement, Brooke Group shall have the obligation to pay the annual installments as provided in Section 5.3(a) hereof and so long as the Brooke Group is paying all amounts due hereunder and no such payments are voidable, then the Settling States waive any and all rights they may have not to accept such cure or performance in any Bankruptcy Proceeding.

10. Entry of Good Faith Bar Order on Contribution and Indemnity Claims.

10.1. The Parties shall request that the respective courts in the Attorney General Actions enter orders barring and prohibiting the commencement and prosecution of any claim or action by any Non-Settling Defendant against any Settling Defendant, including but not limited to any contribution, indemnity and/or subrogation claim seeking reimbursement for payments made or to be made to any Settling State for claims settled under this Agreement. Settling Defendants shall be entitled to dismissal with prejudice of any Non-Settling Defendants' claims against them which violate or are inconsistent with this bar, if granted.

10.2. Upon entering into this Agreement, each Settling State shall seek to amend its pleadings, or take such other appropriate steps (including, but not limited to, moving to dismiss third-party claims asserted against a Settling Defendant), such that each Settling State is seeking only recovery of amounts from Non-Settling Defendants as to which said Non-Settling Defendants have no claim or right to contribution or indemnification from Settling

Defendants. The Settling States shall not seek to collect any amount on any judgment against a Non-Settling Defendant to the extent that such Non-Settling Defendant has a right of contribution or indemnification against any of the Settling Defendants. Brooke Group and Liggett represent and warrant to the Settling States that none of them are subject to any agreement or understanding, written or otherwise, with any Non-Settling Defendants or any other party that entitles any Non-Settling Defendant to indemnity or contribution from the Brooke Group or Liggett.

10.3 Should a Settling State receive a final non-appealable monetary judgment against a Non-Settling Defendant which then results in the Non-Settling Defendant being legally entitled to require a Settling Defendant to make payment toward that judgment, the Settling States shall to seek Court approval to reduce the judgment by an amount sufficient to result in the Settling Defendant having no obligation toward the judgment.

10.4. In the event that a Settling Defendant has entered into any contract or series of contracts, the effect of which is to render the Settling Defendant liable for all or any portion of a tobacco liability judgment entered against a Non-Settling Defendant, and to render a Non-Settling Defendant liable for all or any portion of a tobacco liability judgment entered against such Settling Defendant (a "Reciprocal Payment Arrangement"), the Settling Defendant shall endeavor to terminate such Reciprocal Payment Arrangement or have same judicially declared to be null and void. In the event that a Settling State obtains a judgment in its Attorney General Action against a Non-Settling Defendant (the "NSD Obligee") which, pursuant to a Reciprocal Payment Arrangement, would have to be paid in whole or in part by a Settling Defendant, such Settling Defendant shall permit the Settling State to enter judgment against it in the same or other Attorney General Action in an amount sufficient to require a Non-Settling Defendant (the "NSD Obligor") to pay, pursuant to a Reciprocal Payment

Obligation, a sum equal to the amount of the judgment against the NSD Obligee which the NSD Obligee claims must be paid by such Settling Defendant, and such Settling State shall accept an assignment from the Settling Defendant of its right to payment by the NSD Obligor as full satisfaction of said judgment. The NSD Obligee and the NSD Obligor may, but need not, be the same entity.

10.5. In the event that any potential Future Affiliate shall have entered into any contract the effect of which is to render the potential Future Affiliate liable for all or any portion of a tobacco liability judgment entered against another Non-Settling Defendant and which is not part of a Reciprocal Payment Arrangement (a "Unilateral Payment Obligation"), then at the time the potential Future Affiliate seeks to join this Agreement, it will advise the Settling States of the existence of any such contract, and the Settling States and the potential Future Affiliate shall thereupon cooperate in seeking a judicial determination that the Unilateral Payment Obligation is null and void and, until resolution of said request for judicial declaration, all payment obligations of the Settling Defendant under this Agreement will be suspended. In the event that such determination is judicially denied, or there is no resolution within a period of one year, the potential Future Affiliate may either terminate within thirty (30) days thereafter its election to join this Agreement, or if the potential Future Affiliate fails to so terminate, then it shall join in this Agreement and honor all of its obligations hereunder notwithstanding such Unilateral Payments Obligation.

11. Tax Status of Attorney General Settlement Fund.

11.1 The Attorney General Settlement Fund created under this Agreement will be established and maintained as a Qualified Settlement Fund ("QSF") in accordance with Section 468B of the Internal Revenue Code of 1986, as amended, and the regulations promulgated thereunder. Any Settling Defendant shall be permitted, in its discretion, and at

its own cost, to seek a private letter ruling from the Internal Revenue Service ("IRS") regarding the tax status of the Attorney General Settlement Fund. The parties agree to negotiate in good faith any changes to the Agreement which may be necessary to obtain IRS approval of the Attorney General Settlement Fund as a QSF.

11.2. The Attorney General Board is appointed to act as administrator of the Attorney General Settlement fund. As administrator, such board will undertake the following actions in accordance with the regulations under IRC section 468B: (a) the Board shall apply for the tax identification number required for the Attorney General Settlement Fund; (b) the Board shall file, or cause to be filed, all tax returns the Attorney General Settlement Fund is required to file under federal or state laws; (c) the Board shall pay from the Attorney General Settlement Fund all taxes that are imposed upon the Attorney General Settlement Fund by federal or state laws; and (d) the Board shall file, or cause to be filed, tax elections available to the Attorney General Settlement Fund, including a request for a prompt assessment under IRC section 6501(d) if and when the board deems it appropriate to do so.

11.3. The Settling Defendants, as transferors of the Attorney General Settlement Fund, shall prepare and file the information statements concerning their settlement payments to the Attorney General Settlement Fund as required to be provided to the IRS pursuant to the regulations under IRC section 468B.

12. Effect of Default of Any Settling Defendant.

In the event any Settling Defendant fails to make a payment due and owing under the terms of this Agreement, or is in default of this Agreement in any other respect, Plaintiffs' Counsel shall so notify the defaulting Settling Defendant, which shall then be given 60 calendar days to "cure" the default. If the defaulting Settling Defendant does not "cure" the

default in the time provided in this Section 12, the Settling State may apply to the court for relief in addition to any other remedies it may have hereunder.

13. Representations and Warranties.

13.1. Each Settling Defendant represents and warrants that (i) it has all requisite corporate power and authority to execute, deliver and perform this Agreement and to consummate the transactions contemplated hereby; (ii) the execution, delivery and performance by such Settling Defendant of this Agreement and the consummation by it of the actions contemplated herein have been duly authorized by all necessary corporate action on the part of such Settling Defendant; (iii) the Agreement has been duly and validly executed and delivered by such Settling Defendant and constitutes its legal, valid and binding obligation; and (iv) this Agreement does not violate the charter or bylaws of such Settling Defendant or any agreement to which the Settling Defendant (other than the Future Affiliate) is a party.

13.2. Each Settling State represents and warrants that pursuant to its statutory and/or common law authority (i) it has all requisite power and authority to execute, deliver and perform this Agreement and to consummate the transactions contemplated hereby; (ii) the execution, delivery and performance by such Settling State of this Agreement and the consummation by it of the actions contemplated herein have been duly authorized by all necessary action on the part of such Settling State; and (iii) the Agreement has been duly executed and authorized by such Settling State and constitutes its legal, valid and binding obligation.

14. Arbitration.

In the event that the Parties are unable to agree, after good faith efforts, as to the determination or calculation for any applicable year of Market Share or Pretax Income

hereunder, such determination or calculation shall be submitted to binding arbitration in accordance with the rules of the American Arbitration Association.

15. Most Favored Nation.

15.1. It is the intent of the parties hereto that the Settling Defendants enjoy a preferred position with respect to Non-Settling Defendants, in recognition of the Settling Defendants' willingness to enter into this Agreement. Accordingly, it is generally contemplated that settlements which involve all Settling States, and a Non-Settling Defendant (a "Group Other Settlement") or involving one Settling State and a Non-Settling Defendant (a "Single State Other Settlement") shall meet certain requirements in terms of the initial, periodic or lump sum payments to be made by the Non-Settling Defendant (each a "Benchmark Figure"). For purposes of this Section, a settlement involving a Non-Settling Defendant and some, but not all, Settling States shall be deemed a Single State Other Settlement, and the preferred position of the Settling Defendant shall be governed by subsections 15.1.4, 15.1.5 and 15.1.6 hereof, and determined on a state-by-state basis.

15.1.1. In the case of a Group Other Settlement which includes an Initial Payment such as that provided for in Section 5.3 hereof, the Benchmark Figure shall be that figure which represents three times the Present Value of the Initial Payment made hereunder, adjusted for Market Share at the time of such payment. Thus, if at the time of the Initial Payment hereunder, the Future Affiliate had a market share of 20 percent, and made a payment the Present Value of which is $150 million, and the Settling States subsequently enter into a Group Other Settlement with a Non-Settling Defendant which has a market share of 10 percent, the Benchmark Figure for the Initial Payment shall be $225 million. To the extent that the Initial Payment actually provided for in such Group Other Settlement is less than the Benchmark Figure, the Settling Defendant shall receive a credit in like amount, up to

the amount of the present value of the Initial Payment made hereunder, against all future payment obligations hereunder.

15.1.2. In the case of (i) a Group Other Settlement which includes only a lump sum or periodic payments, and (ii) with respect to the periodic payments included in a Group Other Settlement which also includes an Initial Payment, if the percentage of Pretax Income payable by a Settling Defendant hereunder is between 2.0 and 5.0 percent, the Benchmark Figure shall be that amount which constitutes three times the Present Value of all amounts paid or payable by the Settling Defendant hereunder (excluding, if the Group Other Settlement contains an Initial Payment, the Initial Payment hereunder), assuming, in the case of future payments, no increase or decrease in Market Share but assuming Inflation in revenues, all adjusted for Market Share. Thus, if the Present Value of a Settling Defendant's payments made or to be made hereunder is $600 million and such Settling Defendant enjoys a Market Share of 20%, the Benchmark Figure for a Non-Settling Defendant which at the time of a Group Other Settlement enjoys a Market Share of 15% would be $1,350 million. Similarly, the Benchmark Figure for a Non-Settling Defendant which at the time of a Group Other Settlement enjoys a Market Share of 5% would be $450 million. To the extent that the Present Value of the lump sum or periodic payments to be made under a Group Other Settlement is less than the Benchmark Figure, the Settling Defendant shall receive a credit in like amount, up to the amount of any remaining payment obligations hereunder.

15.1.3. In the case of a Group Other Settlement such as described in 15.1.2, if the percentage of Pretax Income payable by a Settling Defendant hereunder is in excess of 5.0 percent, the Benchmark Figure computed as in 15.1.2 above, except that the multiplier shall be the quotient yielded by dividing the percentage of Pretax Income payable by the Settling Defendant plus 10 by the percentage of Pretax Income payable by the Settling Defendant.

Thus, if the Settling Defendant is paying 6.0 percent Pretax Income, the multiplier is 6 ÷ 10 divided by 6 = 2-2/3; if the Settling Defendant is paying 7.5 percent of Pretax Income, the multiplier is 7.5 ÷ 10 divided by 7.5 = 2-1/3.

15.1.4. In the case of a Single State Other Payment which includes an Initial Payment such as that provided for in Section 5.3 hereof, the Benchmark Figure shall be that figure which represents three times the present value of the Initial Payment made hereunder to such Settling State, adjusted for Market Share at the time of such payment, computed in accordance with Section 15.1.1. To the extent that the Initial Payment actually provided for in such Single State Other Settlement is less than the Benchmark Figure, the Settling Defendant shall receive a credit in like amount, up to the amount of the present value of the Initial Payment made to the Settling State hereunder, against all future payment obligations to the Settling State hereunder.

15.1.5. In the case of a Single State Other Settlement which includes only a lump sum or periodic payments, and with respect to the periodic payments included in a Single State Other Settlement which also includes an Initial Payment, if the percentage of Pretax Income payable by a Settling Defendant to all Settling States hereunder is between 2.5 and 5.0 percent, the Benchmark Figure shall be that amount which constitutes three times the Present Value of all amounts paid or payable by the Settling Defendant to the Settling State hereunder (excluding, if the Single State Other Settlement contains an Initial Payment, the Initial Payment hereunder), assuming, in the case of future payments, no increase or decrease in Market Share but assuming Inflation in revenues, all adjusted for Market Share, computed as set forth in Section 15.1.2. To the extent that the Present Value of the lump sum or periodic payments to be made under a Single State Other Settlement is less than the Benchmark

Figure, the Settling Defendant shall receive a credit in like amount, up to the amount of any remaining payment obligations to the Settling State hereunder.

15.1.6. In the case of a Single State Other Settlement such as described in 15.1.5, if the percentage of Pretax Income payable by a Settling Defendant to all Settling States hereunder is in excess of 5.0 percent, the Benchmark Figure shall be computed as in 15.1.2 above, except that the multiplier shall be the quotient yielded by dividing the percentage of Pretax Income payable by the Settling Defendant to all Settling States plus 10 by the percentage of Pretax Income payable by the Settling Defendant to all Settling States.

15.1.7. Solely for the purposes of Sections 15.1.5 and 15.1.6, the payments due to each of the Initial Settling States shall be deemed to be equivalent to 0.5% of the Settling Defendant's Pretax Income. In cases of determining Present Value of future payments, each Initial Settling State's share shall be one-fifth of the amount computed in accordance with the second paragraph of Section 5.6 hereof.

15.2. Except as provided in Section 15.1 hereof, in the event that, subsequent to the date of this Agreement, any settlement of any Settling State's Attorney General Action is reached with any Non-Settling Defendant which is not a Party hereto and such settlement is on any terms more favorable to such Non-Settling Defendant than are the terms of this Agreement to a Settling Defendant, such Settling Defendant shall have the right to replace or modify any or all of the terms of this Agreement with, or add to this Agreement, any or all of such more favorable terms.

15.3. In the event that, subsequent to the date of this Agreement, any of the Settling Defendants enters into a settlement agreement with any State other than a Settling State on terms relating to the then Present Value of amounts payable under such settlement agreement, compliance with the Proposed Rule or cooperation that are more favorable to the State than

those contained herein (as adjusted for relative Medicaid Population), the Settling States shall have the right with respect to such Settling Defendant to replace or modify any or all of the terms of this Agreement with, or add to this Agreement, any or all such more favorable terms (adjusted for relative Medicaid Populations).

16. Miscellaneous.

16.1. All terms of this Agreement and/or obligations created thereby shall be deemed to include a covenant of good faith and fair dealing on behalf of all parties.

16.2. Brooke shall provide to the Settling States at the time of execution of this Agreement and at the time the Future Affiliate joins this Agreement, an opinion in form satisfactory to the Settling States from legal counsel for the Brooke Group (or Future Affiliate, as the case may be) as to the due execution of the Settlement Agreement by the Brooke Group and Liggett (or Future Affiliate, as the case may be) and its enforceability against the Brooke Group, Liggett (or Future Affiliate, as the case may be) and such other matters contemplated by Section 13.1 (other than the "agreements" referenced in clause (iv)).

16.3. In the event that a termination occurs pursuant to any sections of this Agreement, no Settling State shall be required to return any payment.

16.4. This Agreement, including all Exhibits attached hereto, if any, shall constitute the entire Agreement among the Parties with regard to the subject of this Agreement and shall supersede any previous agreements and understandings between the Parties with respect to the subject matter of this Agreement. This Agreement may not be changed, modified, or amended except in writing signed by all Parties.

16.5. With respect to each Settling State, this Agreement shall be construed under and governed by the laws of such State applied without regard to its laws applicable to choice of law.

16.6. This Agreement may be executed by the Parties in one or more counterparts and by facsimile, each of which shall be deemed an original but all of which together shall constitute one and the same instrument.

16.7. This Agreement shall be binding upon and inure to the benefit of the Settling States, the Settling Defendants, and their representatives, heirs, successors, and assigns.

16.8. Nothing in this Agreement shall be construed to subject any Settling Defendant's parent or affiliated company to the obligations or liabilities of that Settling Defendant except as otherwise provided herein.

16.9. The headings of the Sections of this Agreement are included for convenience only and shall not be deemed to constitute part of this Agreement or to affect its construction.

16.10. Any notice, request, instruction, application for Court orders sought in connection with this Agreement or other document to be given by any Party to any other Party shall be in writing and delivered personally or sent by registered or certified mail, postage prepaid, if to the Settling Defendants to the attention of each Settling Defendant's respective representative and to Plaintiffs' Counsel on behalf of the Settling States. As of the date of this Agreement, the respective representatives are as follows:

Mike Moore, Attorney General of the State of Mississippi
Office of the Attorney General
Jackson, Mississippi

Darrell V. McGraw, Jr., Attorney General of the State of West Virginia
Office of the Attorney General
Charleston, West Virginia

Robert Butterworth, Attorney General of the State of Florida
Office of the Attorney General
The Capitol, Suite PL01
Tallahassee, Florida 32399-0150

Scott Harshbarger, Attorney General of the Commonwealth of Massachusetts
Office of the Attorney General
One Ashburton Place
Boston, Massachusetts

Richard P. Ieyoub, Attorney General of the State of Louisiana
Office of the Attorney General
Baton Rouge, Louisiana

Marc Kasowitz, Settling Defendants Counsel
Kasowitz, Benson, Torres & Friedman LLP
875 3rd Avenue
New York, New York 10022
212 407-3800
Fax 212 319-6756

Bennett S. LeBow, for Settling Defendants
Brooke Group Ltd.
International Place
100 SE 2nd Street
Miami, Florida 33131

Michael L. Hirschfeld, for Settling Defendants
Milbank Tweed Hadley & McCloy
One Chase Manhattan Plaza
New York, New York 10005-1413

The above designated representatives may be changed from time to time by any Party upon giving notice to all other Parties in conformance with this Section 16.7.

16.11. References to or use of a singular noun or pronoun in this Agreement shall include the plural, unless the context implies otherwise.

16.12. Brooke Group and Liggett shall:

(1) cooperate with the Attorneys General in that they will take no steps to impede or frustrate the Attorneys General's investigations into, or prosecutions of, any of the Non-Settling Defendants, so as to secure the just, speedy and inexpensive determination of the Attorney General Actions against the Non-Settling Defendants;

(2) cooperate in and facilitate reasonable non-party discovery from the Brooke Group or Liggett in connection with any pending Attorney General Action, provided that such information is not disclosed to any third parties except as required by law, including non-settling Attorneys General, without the written consent of the Brooke Group or Liggett, and provided that such cooperation shall not be deemed a waiver of applicable privileges;

(3) review the issues relating to discovery propounded by the Attorneys General against Brooke Group or Liggett, confer with such Attorneys General and, if appropriate, take reasonable steps to facilitate judicial determinations of the privileged nature of any documents or other information within the possession, custody or control of Brooke Group or Liggett which have been sought in discovery by the Attorneys General;

(4) insofar as Brooke Group or Liggett have or obtain any material information concerning any fraudulent or illegal conduct on the part of any parties, including Non-Settling Defendants or their agents, designed to frustrate or defeat the Attorney General Actions against the Non-Settling Defendants, or which have the effect of unlawfully suppressing evidence relevant to the Attorney General Actions, such information will be disclosed to the appropriate judicial, regulatory agencies, and such Attorneys General.

IN WITNESS WHEREOF the parties have executed this Agreement under seal as of the day and date first written above.

STATE OF MISSISSIPPI

/s/ MIKE MOORE

Mike Moore, Attorney General

STATE OF LOUISIANA

/s/ RICHARD P. IEYOUB

Richard P. Ieyoub, Attorney General

STATE OF WEST VIRGINIA

/s/ DARRELL V. MCGRAW, JR.

Darrell V. McGraw, Jr.,
Attorney General

BROOKE GROUP Ltd.

By: /s/ BENNETT S. LEBOW

STATE OF FLORIDA

/s/ ROBERT BUTTERWORTH

Robert Butterworth,
Attorney General

LIGGETT GROUP, INC.

By: /s/ BENNETT S. LEBOW

COMMONWEALTH OF MASSACHUSETTS

/s/ SCOTT HARSHBARGER

Scott Harshbarger,
Attorney General

LIGGETT & MYERS, INC.

By: /s/ BENNETT S. LEBOW

tobacco litigation

Mark B. Hutton · †
Andrew W. Hutton

Derek S. Casey ·
Anne H. Pankratz
Christopher P. Christian
Chan P. Townsley ··

· Also Admitted in Oklahoma
·· Also Admitted in Missouri
† Certified Trial Advocate
National Board of Trial Advocacy

HUTTON & HUTTON

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8100 East Twenty-Second Street North, Building 1200
Wichita, Kansas 67226-2321
Mail: P.O. Box 638
Wichita, Kansas 67201-0638

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Facsimile
(316) 686-1077

Products Liability
(316) 686-1242
Facsimile
(316) 686-2049

Tax I.D.# 48-0966751

FACSIMILE COVER SHEET

DATE: 04/19/96 TIME: _____

TO: JOHN W. CAMPBELL FAX NUMBER: (913) 296-6296

FROM: ANDREW W. HUTTON # OF PAGES TO FOLLOW: 2

RE: ATTORNEY-CLIENT AGREEMENT

SPECIAL MESSAGE AND/OR INSTRUCTIONS: _____

FAX COVER NOTICE OF CONFIDENTIALITY:

House Taxation
Date 2/15/00
Attachment # 30-1

Mark B. Hutton · †
Andrew W. Hutton

Derek S. Casey ·
Anne H. Pankratz
Christopher P. Christian
Chan P. Townsley ··

· Also Admitted in Oklahoma
·· Also Admitted in Missouri
† Certified Trial Advocate
National Board of Trial Advocacy

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Tax I.D.# 48-0966751

April 19, 1996

John W. Campbell
ATTORNEY GENERAL'S OFFICE
DEPARTMENT OF LITIGATION &
ANTITRUST
2nd Floor, 301 S.W. 10th Avenue
Topeka, KS 66612

Re: Litigation Against Cigarette Manufacturers

Dear John:

Please find enclosed a working rough draft of an Attorney-Client Agreement. Once you have reviewed same please give me a call.

Very truly yours,

Andrew W. Hutton

AWH/jjb
Enclosure

30-2

DRAFT

ATTORNEY - CLIENT AGREEMENT

STATE OF KANSAS -vs- CIGARETTE MANUFACTURERS

THIS AGREEMENT, by and between THE STATE OF KANSAS, and HUTTON & HUTTON, is made and entered into on this _____ day of _____, 1996. THE STATE OF KANSAS employs HUTTON & HUTTON to represent THE STATE OF KANSAS in its claims for reimbursement and costs expended by the State secondary to tobacco related health problems.

HUTTON & HUTTON will be designated as lead counsel. Lead counsel, HUTTON & HUTTON has the right to bring in additional counsel and said additional counsel will be paid under the terms of this contract. Even with additional counsel HUTTON & HUTTON will have control over the course and direction of the litigation with the consultation and advice of THE STATE OF KANSAS. Additional counsel has no right to any additional fees beyond the terms of this contract.

HUTTON & HUTTON is to make no settlement without THE STATE OF KANSAS' consent. HUTTON & HUTTON is to receive no fee if nothing is recovered.

HUTTON & HUTTON will be employed by THE STATE OF KANSAS on a contingent fee basis. HUTTON & HUTTON will not be paid unless there is a successful recovery by way of settlement and/or judgment. Attorney is to receive a fee of Twenty-Five Percent (25%) of whatever amounts are recovered either by way of settlement and/or judgment in this litigation. HUTTON & HUTTON will bear all the costs of litigation attributed to HUTTON & HUTTON and attorneys under their control and direction. If there is no recovery made by THE STATE OF KANSAS, HUTTON & HUTTON will not seek reimbursement from THE STATE OF KANSAS for expenses incurred. The fee applies to all actual damages, punitive damages and interest recovered in connection with a judgment. HUTTON & HUTTON will advance all expenses of the litigation. If a recovery is obtained, all expenses will be paid before computation of attorney fees.

This agreement is governed by Kansas law.

_____ _____

ATTORNEY CLIENT

30-3

Tobacco Ltg

Mark B. Hutton · †
Andrew W. Hutton

Derek S. Casey ·
Anne H. Pankratz
Christopher P. Christian
Chan P. Townsley ··

· Also Admitted in Oklahoma
·· Also Admitted in Missouri
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Tax I.D.# 48-0966751

March 14, 1996

SENT VIA FACSIMILE
TO (913) 296-6296
AND VIA REGULAR MAIL

Ms. Carla Stovall
Attorney General
2nd Floor, Judicial Center
Topeka, KS 66612-1567

Re: Cigarette Litigation

Dear Attorney General Stovall:

I am a practicing lawyer in Wichita, Kansas, with emphasis in cigarette litigation. Our firm is part of the 65-member Castano Class Action Group that recently created a settlement with the Liggett Group and other states' attorney generals. I am the chairperson of the Science and Causation Subcommittee, as well as the Smokeless Tobacco Subcommittee within the Castano consortium of attorneys.

We would like Kansas to likewise participate in the Medicare reimbursement litigation that is now being done by five other states. I have talked to Attorney General Michael Moore from Mississippi regarding this matter, and he promised me that he was going to contact you regarding our potential involvement in Kansas. We would like to be able to participate in this litigation on behalf of the citizens of Kansas because of our expertise in cigarette litigation.

Please give this consideration and feel free to give me a call at any time.

Very truly yours,

Andrew W. Hutton

Andrew W. Hutton

AWH/sm

House Taxation
Date 2/15/00
Attachment # 31

(Minnesota)

EXHIBIT B

CONTINGENT FEE RETAINER AGREEMENT FOR STATE CLAIMS

WHEREAS, cigarette smoking is the most preventable cause of death in our society;

WHEREAS, cigarette smoking kills approximately 400,000 people each year in the United States (including more than 6,000 Minnesotans each year) -- more than the number of deaths caused by guns, drug use, and automobile accidents combined;

WHEREAS, in addition to the human carnage, the economic costs of cigarette smoking, and, in particular, health care expenditures from smoking-attributable diseases, amount to an onerous burden to society and to the State;

WHEREAS, the tobacco industry had been able to enjoy virtual immunity from its actions due to its economic and political power and its scorched earth tactics in litigation, reaping billions of dollars of profits from unconscionable activities and never to the knowledge of the Attorney General or the Special Attorneys paying any damages despite the decades of litigation;

WHEREAS, the Attorney General and the Special Attorneys believe that, despite the tobacco industry's past successes, the laws of the state of Minnesota were meant to apply to all entities, no matter how powerful;

WHEREAS, the laws of the State are intended to place the consequences of unlawful conduct on the perpetrator, and the contemplated Litigation is the most just and efficient way to accomplish that purpose with respect to the carnage caused by the tobacco industry;

WHEREAS, the State recognizes that RKM&C's undertakings pursuant to the Special Attorney Appointment involve substantial factual and legal issues of first impression, the

resolution of which cannot be fully ascertained at this time;

WHEREAS, the State acknowledges that the successful resolution of the Litigation will require the Special Attorneys to devote substantial resources (both temporal and financial) in furtherance of their undertakings;

THEREFORE, due to all the complex considerations involved in the Special Attorney Appointment, the State and the Special Attorneys have agreed as follows:

1. The State is not liable to pay compensation other wise than from amounts collected for the State by the State Attorneys, unless the State terminates this appointment and the Litigation does not result in a monetary recovery to the State. In the event the State terminates this appointment before the State receives a monetary recovery, the State's responsibility for payment shall be as set forth in paragraphs 7-9 below.

2. The contingency upon which compensation is to be paid is the recovery for the State of monies (at law or in equity), whether by settlement or judgment, from third parties liable for damages arising from the sale and/or distribution of cigarettes.

3. Compensation on the foregoing contingency is to be paid by the State to the Special Attorneys on the following basis: twenty-five percent (25%) of the total recovery to the State, including but not limited to compensatory or punitive damages , restitution, civil penalties, interest, and any amounts which may later be payable to the federal government under the Medicaid program. There is nothing to be subtracted in determining the total recovery, except court-awarded attorneys' fees and costs. In addition to these fees, in the

event of recovery, the State shall reimburse the Special Attorneys for costs and disbursements advanced during the course of the Litigation by the Special Attorneys, in an amount to be approved by the Attorney General.

4. Notwithstanding paragraph 3 above, the State shall pay no higher percentage for compensation of the Special Attorneys than is paid by any other co-plaintiff that the Special Attorneys represent in the Litigation on solely a contingent fee basis. If the Special Attorneys represent any other co-plaintiffs in the Litigation on other than solely a contingent fee basis, the State shall pay no higher comparable rate of compensation to the Special Attorneys considering the totality of circumstances of the different retainer or appointment agreements, including but not limited to the risk factors inherent in the Litigation and the time value of money.

5. The compensation paid hereunder is separate and independent from any compensation which the Special Attorneys may receive from any other party that the Special Attorneys represent in the Litigation.

6. If the court awards, or the adverse parties pay, attorneys' fees and costs, such fees and costs shall be paid to the Special Attorneys to the extent that the award is based on services furnished by the Special Attorneys and to the State to the extent that the award is based on services furnished by the Attorney General staff members. Any such fees awarded by the court or paid by the adverse parties to the Special Attorneys shall be credited to the State and deducted from the fees payable to the Special Attorneys pursuant

to paragraph 3 above.

7. If the Attorney General terminates this appointment before a monetary recovery has been achieved, and the Litigation is dismissed or otherwise does not result in a monetary recovery, then the Attorney General shall apply to the Legislature for the reasonable value of the Special Attorneys' services, as determined by the appropriate court, including fees and costs, and shall use his best efforts to secure a specific appropriation. The Attorney General has no obligation to pay under this paragraph in the absence of such a specific appropriation. IN calculating the value of such services, the court or Legislature may deduct the value of the Special Attorneys' services furnished for the benefit of other parties involved in the joint prosecution of the Litigation.

8. If the Attorney General terminates this appointment before a monetary recovery has been achieved, and the Litigation later results in a monetary recovery ,then the Special Attorneys shall be paid, from the recover, the reasonable value or their services, as determined by the appropriate court, plus fees and costs, but no more than they would have received if this appointment had not been terminated.

9. In determining the reasonable value of the Special Attorneys' services pursuant to paragraphs 7 and 8 above, all factors affecting the value of the Special Attorneys' contributions shall be taken into account, including but not limited to, the length of time spent on the case, the funds invested, the time value of money, the quality of representation, the result of the Special Attorneys' efforts, and the viability of the claim at

the time of termination.

10. During the course of the Litigation, the Special Attorneys shall advance costs and disbursements. If the State is the only plaintiff which the Special Attorneys represent in the Litigation, the State's obligation to reimburse the Special Attorneys' costs is that set forth in paragraphs 1-9 above. If there are other parties plaintiff to the Litigation, and the State enters into a Costs and Disbursements Pro Rata Sharing agreement providing for the sharing of costs and disbursements by the State and such other parties plaintiff, then the State would reimburse the Special Attorneys only for its agreed upon pro rata share of the costs and disbursements and only after the recovery of monies whether by settlement or judgment from third parties liable for damages arising from the sale and/or distribution of cigarettes.

11. In the event there is no recovery, or the recovery is less than enough to cover the State's pro rata share of the Special Attorneys' costs and disbursements, the State shall not be responsible for the deficiency of its pro rata share of costs and disbursements, provided, however, that (1) neither the State nor the Special Attorneys shall be responsible for a court award of costs and disbursements to adverse parties arising out of the conduct of the other, and (2) if the State terminates this appointment in the absence of monetary recovery, paragraphs 7-9 above shall apply.

12. In no event shall the State be obligated to pay to the Special Attorneys more under this agreement than it receives in any monetary recovery, nor to pay any amount until the

Litigation is finally resolved, whether by dismissal, final judgment, or settlement, except as noted in paragraphs 7-9 above.

(Texas)

OUTSIDE COUNSEL AGREEMENT

ON this 22nd day of March, 1996, DAN MORALES, Attorney General of the State of Texas ("Attorney General") and Walter Umphrey; John M. O'Quinn, P.C.; John Eddie Williams, Jr.; Reaud, Morgan & Quinn, and Nix Law Firm ("Counsel") hereby enter into the following agreement for professional services ("Agreement"). Counsel is hereby appointed to provide legal services to the State of Texas ("the State") and the Attorney General, subject to the terms and conditions set forth below:

1. DUTIES. Counsel shall provide legal services to the State and Attorney General relative to seeking recovery and relief from third parties for damages arising from the sale and/or distribution of tobacco (hereafter "the Litigation"). Counsel shall provide legal consultant services as requested by the Attorney General. Such duties are more fully set forth in the attached Exhibit A, which is incorporated herein by reference, as are all exhibits attached hereto.

2. COMPENSATION AND EXPENSES. As compensation for the performance of the duties described, Counsel shall be compensated as set forth in the attached Exhibit B. Counsel shall advance all costs and expenses of the Litigation, including, but not limited to, discovery, pre-trial proceedings, trial, experts, investigators, consultants and other contractors, all personnel, salaries, travel, copying, freight and postage, communications charges, and any other necessary expenses related to the Litigation in an initial amount not to exceed ten million dollars ($10,000,000). In the event expenses exceed ten million dollars ($10,000,000), Counsel, in consultation with the Attorney General, shall consider revision of the terms set forth in Exhibit B.

3. BILLING STATEMENTS. Counsel shall submit a monthly statement to the Attorney General in care of Jorge Vega, First Assistant Attorney General, P.O. Box 12548, Austin, Texas 78711-2548, setting forth in detail the activities and charges with respect to this appointment.

4. AVOIDANCE OF CONFLICTS. Counsel shall not undertake legal work for the Attorney General outside of the scope of this appointment, shall not represent a party involved in a claim, dispute or transaction of any kind which would create a conflict of interests for Counsel or the Attorney General unless and until Counsel have informed the First Assistant Attorney General of the proposed representation and received his written approval to proceed. Counsel also agree to inform their clients of any case involving a potential conflict.

In addition to complying with any applicable professional conduct standards relating to conflicts of interest, Counsel affirms and agrees that he/she has not represented any client

House Taxation
Date 2/15/00
Attachment # 33-1

in any matter pending before the Office of the Attorney General during the 6-month period preceding this Contract, and that he/she will not represent any client in any capacity concerning any matter pending before the Office of the Attorney General during the existence of this Agreement, nor for a 6-month period following the termination of this Agreement.

5. CONFIDENTIALITY. During the term of this appointment, as well as thereafter, Counsel agrees to keep all information, not otherwise open to the public under Chapter 552, Texas Government code, pertaining to the Office of the Attorney General and its personnel, confidential and will not use any such information to the detriment of the Office of the Attorney General or its officers or employers at any time. It is understood and agreed that the Attorney General will serve as the sole public spokesperson for all aspects of the Litigation. It is further understood and agreed that any agreement between Counsel and others providing professional services to Counsel relating to the Litigation shall contain a confidentiality clause that conforms to the requirements of this paragraph.

6. MALPRACTICE INSURANCE. Counsel presently maintains adequate malpractice insurance and agrees to maintain such insurance during the term of the Agreement.

7. TERM. This appointment is effective March 22, 1996.

8. MODIFICATION. This Agreement may be modified at any time, in whole or in part, by consent of the Attorney General and Counsel. Such modifications shall be in writing and signed by all parties to the Agreement.

9. SEVERABILITY. If any part of this Agreement is unenforceable, then that part shall be severed from the Agreement and the remaining provisions shall remain enforceable.

Executed on this the 22nd day of March, 1996, in Port Arthur, Texas.

_____

DAN MORALES
Attorney General

DATE:_____

_____

JORGE VEGA

(Texas)

EXHIBIT A
CASE HANDLING AGREEMENT

Counsel are retained to provide legal service to the Attorney General and the State for the purposes of seeking recovery and relief from third parties for damages arising from the sale and/or distribution of tobacco. This appointment shall be subject to the following guidelines:

1. The Attorney General, as the chief legal officer of the State, retains, at all times, final authority over all aspects of the Litigation.

2. The Attorney General shall appoint delegates from his staff to supervise, monitor and review the conduct of the Litigation. Counsel shall consult with and obtain the prior approval of the Attorney General concerning all substantive issues affecting the Litigation, including, but not limited to the complaint and dispositive motions, selection of consultants and experts, discovery, pre-trial proceedings, trial, settlement negotiations, and participation of additional counsel. Regular status meetings shall be held as requested by the Attorney General.

3. Counsel shall provide the Attorney General with a copy of all substantive correspondence and all pleadings, discovery requests, and other documents served and/or filed in the Litigation.

4. The Attorney General shall designate one or more staff members to act as liaisons with such state agencies as become substantial involved in the Litigation. To the extent feasible, Counsel shall work through such liaisons in communicating with such agencies. A copy of all written communications between Counsel and the state agencies shall be provided to the Attorney General.

5. Subject to the terms of this appointment, it is recognized and agreed that Walter Umphrey shall act as chief litigation counsel for the Litigation.

6. The Attorney General shall provide attorneys and other members of his staff to work on the Litigation with Counsel. The identity and responsibilities of such personnel so assigned shall be determined solely by the Attorney General. Coordination of the Attorney General's staff work on the Litigation will be principally handled by the Attorney General's appointed delegate, in consultation with Counsel.

(Texas)

EXHIBIT B
CONTINGENT FEE RETAINER AGREEMENT

1. Payment for the legal services covered by this contract shall be based on a contingency fee percentage of the dollars recovered as a result of the Litigation. For their services under this Agreement, Counsel is hereby assigned and shall be paid a contingency fee of fifteen percent (15%) of the total recovery.

2. If the State agrees to accept an in-kind settlement of the Litigation, then as part of the settlement the State shall negotiate a mutually agreeable settlement of attorneys fee and expenses and approval by Counsel may not be unreasonably withheld.

3. All costs related to the Litigation advanced by Counsel shall be deducted from any recovery by the State and payable to Counsel in addition to the compensation outlined in Paragraph 1. The repayment of costs is contingent upon a recovery being obtained. If no recovery is made, the State owes nothing for costs.

4. If the court awards attorney's fees and costs, then the State shall be entitled to that portion of the award that is based on services furnished by the Attorney General. Nothing herein shall be construed to limit or prevent an award of attorney's fees and costs to Counsel made in the discretion of the court.

5. All monies recovered by the State under the Litigation shall be made payable jointly to the State and Counsel and placed in the registry of the Court in which the Litigation is filed, from which Counsel shall receive their compensation as outlined in Paragraphs 1-4 of this Agreement.

6. In the event of withdraws of any Counsel pursuant to the contract, Counsel withdrawing shall have not right of recourse against the State for any legal costs incurred or services performed and such withdrawing Counsel's sole recourse shall be against the remaining Counsel.

(Massachusetts)

ENGAGEMENT AND CONTINGENCY AGREEMENT

AGREEMENT as of this _____ day of _____, 1996 by and between the Commonwealth of Massachusetts ("Commonwealth") by Scott Harshbarger, its Attorney General ("Attorney General") and the following law firms, as specified:.....

The foregoing attorneys and law firms are hereafter referred to as the Special Assistant Attorneys General ("SAAGs").

Whereas, cigarette smoking kills approximately 400,000 individuals each year in the United States (including more than 10,000 citizens of Massachusetts each year) -- more than the number of deaths caused by guns, drug use and automobile accidents combined;

Whereas, the cost to the Commonwealth and its citizens of health care and related expenditures for smoking related diseases exceeds hundreds of millions of dollars per year;

Whereas, any litigation involving tobacco-related industries is likely to entail numerous complex factual and legal issues;

Whereas, any such litigation will require the expenditure of substantial resources by any private attorneys retained to assist the Commonwealth;

Whereas, the Attorney General seeks to avoid the expenditure of state resources in any such litigation; and

Whereas, the Attorney General plans to bring an action against cigarette companies and related entities pursuant to his authority under, *inter alia*, Massachusetts common law, M.G.L. c. 12, section 1, *et seq.,* G.L. c. 93A, section 1, *et seq.*, G.L. c. 118E.....; now therefore the

House Taxation
Date 2/15/00
Attachment # 34-1

Commonwealth and the Special Assistant Attorney Generals (SAAGs) AGREE AS FOLLOWS:

I. SCOPE OF SERVICES/CASE HANDLING

A. The SAAGS are retained to provide legal services to the Commonwealth for the purpose of seeking injunctive relief, monetary relief (including, without limitation, damages and civil penalties) and other relief against tobacco industry companies and related entities ("defendants") in litigation arising from the advertising, marketing, promotion, sale and/or distribution of cigarettes (hereinafter "the Litigation").

B. The Attorney General, as the chief legal officer of the Commonwealth, retains final authority over all aspects of the Litigation. As provided herein, the SAAGs are authorized to take appropriate legal steps to prosecute the Litigation and participate in all settlement negotiations and the Commonwealth and the Attorney General hereby further agree not to settle this action without prior consultation with the SAAGs.

C. The Attorney General shall appoint members of his staff to monitor the prosecution of the Litigation. The SAAGs shall consult in advance with and obtain the prior approval of the Attorney General concerning all substantive matters related to the Litigation. Regular status meetings shall be held as requested by either the Attorney General or the SAAGs.

D. The Attorney General shall provide to the SAAGs copies of all correspondence and other documents exchanged between the Attorney General and the defendants not generated by the SAAGs; and the SAAGs shall provide the Attorney General with copies of all correspondence, pleadings, and discovery requests and responses related to the Litigation.

E. The SAAGs shall communicate with state agencies through the Attorney General,

unless alternative arrangements are made in advance among the SAAGs, the Attorney General and the agency. Where written communications from the SAAGs to state agencies are authorized, the Attorney General shall be provided with copies of those communications.

F. Each SAAG shall provide sufficient resources, including attorney time, to prosecute the Litigation faithfully and with due diligence. Each SAAG shall, prior to executing this Agreement, indicate to the Attorney General or his designee in detail the actual attorney resources that the firms will devote to the Litigation. Any change in this commitment shall be made only with the written agreement of the Attorney General.

G. The SAAGs agree that there shall be an Executive Committee that shall oversee the day-to-day conduct of the Litigation. The Executive Committee shall consist of: a designee of the Attorney General, Ronald L. Motley, Esq. (or designee), Michael O. Thorton, Esq. (or designee), Richard M. Heimann, Esq. (or designee), Thomas M. Sobol, Esq. And Robert V. Costello, Esq. (or designee).

H. The Attorney General retains the right to designate lead national counsel, lead local counsel and lead trial counsel in the Litigation. In his sole discretion, the Attorney General may require that any firm designated as a lead counsel shall devote at least two full-time lawyers to the litigation.

I. The compensation, if any, paid to the SAAGs pursuant to this agreement shall be shared among the SAAGs pursuant to an agreement to be entered into by and between the SAAGS.

J. The Attorney General retains the right to add not more than two firms to the group of firms participating in the Litigation as SAAGs. The SAAGs agree that any firms added to the group conducting the Litigation shall share in such compensation, if any, as is earned by the

SAAGs in the manner outlined in this Agreement. In the event that the SAAGs are unable to agree on the terms under which the new firms shall participate in the compensation, the Attorney General or his designee shall decided and such decisions shall be final and binding on all the SAAGs.

K. The SAAGs agree to maintain contemporaneous time and expense records. The SAAGs shall submit quarterly statements to the Attorney General setting forth for that period the hours and services devoted to the Litigation, and all disbursements.

L. Expense records and related documents maintained by the SAAGs in connection with the Litigation shall be subject to audit by the Attorney General.

II. CONTINGENT FEE ARRANGEMENT

A. The Commonwealth is not liability to pay any of the expenses of the Litigation, whether such expenses are attorneys' fees, costs or other amounts, except as provided in paragraphs II(B,C,D,E,F and G), below.

B. The sole contingency upon which compensation is to be paid is the recovery and collection by the SAAGs, on behalf of the Commonwealth, of monies in the Litigation, whether by settlement or judgment.

C. Compensation on the foregoing contingency shall be 25% of any recovery collected by the SAAGs on behalf of the Commonwealth plus the SAAGs' reasonable disbursements in the Litigation; provided, however, that all entities that voluntarily contribute funds to the Attorney General to finance the Litigation shall first be reimbursed in amounts equal to their respective contributions. As used in this paragraph, the term "recovery" shall not include

amounts awarded or ordered to be paid as attorneys' fees and costs. The 25% contingent fee shall be shared and distributed among all SAAGs. If the SAAGs recover monies in the Litigation, but in an amount that does not exceed the disbursements in the Litigation, such monies shall be used to reimburse disbursements.

D. As used in this Agreement, the term "disbursement" shall include travel expenses, telephone charges, copying charges, fax charges, deposition costs, investigator costs, messenger service costs, mediation expenses, computer research fees, medical or nursing consultation fees, expert fees, other consultation fees and all other reasonable out-of-pocket costs incurred in the Litigation. Notwithstanding any other provision of this Agreement, in the event that amounts become payable to the SAAGs for disbursements in accordance with paragraphs II(B) and (C), the SAAGs shall be reimbursed only for those disbursements that are within the limitations set forth in the Attorney General's guidelines on disbursements; to the extent that a category of disbursement is not specifically referred to in these guidelines, it shall be reimbursed only if approved by the Attorney General in his sole discretion.

E. The claims that the Commonwealth intends to assert in the Litigation provide for the payment of Attorneys' fees and costs to the Commonwealth. The Commonwealth intends to seek an order for payment of its attorneys' fees and costs should it prevail, in whole or in part, in the Litigation. If the Court in the Litigation awards attorneys' fees, such fees shall be paid to the SAAGs to the extent the award is based on services furnished by the SAAGs; provided, however, that an amount equal to such attorneys's fees as are awarded by the Court and collected in the Litigation shall be deducted from the fees payable to the SAAGs pursuant to paragraphs II (B and C), above. If the Court awards expenses and costs in the Litigation, such amount shall be applied as directed in this Agreement.

F. In the event the Litigation is resolved, by settlement or judgment, under terms involving the provision of goods, services or any other "in-kind" payment, the parties hereto agree to seek, as part of any such settlement, compensation for the SAAGs equivalent to the 25% contingency fee and expenses to which the SAAGs would be entitled under this Agreement. In the event the Attorney General is unable to secure such compensation. For the SAAGs as part of any "in-kind" settlement, the Attorney General agrees to petition the Legislature to appropriate funds to compensate the SAAGs.

G. The Attorney General shall establish and maintain a separate account for such funds as he receives from third parties for the specific purpose of undertaking the Litigation, as provided in G.L. c. 12, section 4A (hereinafter the "AG Account"). Funds from the AG Account shall be used to pay disbursements in the Litigation; provided, however, that no expenditures shall be made from the AG Account for disbursements by the SAAGs for travel, lodging and meals. The Attorney General shall not be required to pay from the AG Account any disbursement that is incurred by a SAAG that is not (i) consistent with the Attorney General's guidelines on disbursements, or (ii) approved in advance by the Attorney General.

H. All funds contributed by the SAAGs to cover costs and expenses shall be deposited in a separate interest bearing account in a local bank (hereinafter "SAAG Account"). The Executive Committee shall designate a local SAAG to act as "treasurer" who will oversee disbursement from the SAAG Account pursuant to the procedures and guidelines set up by the Executive Committee. Bimonthly reports shall be made by the treasurer unless otherwise requested. Each firm whose attorneys serve as SAAGs agrees that, within ten (10) days of its execution of the Agreement, it shall deposit in the SAAG Account the sum of $50,000.

I. In the first twelve (12) months of the Litigation, funds in the SAAG Account shall be

used to pay disbursements in the Litigation on a dollar-for-dollar matching basis with funds in the AG Account. In succeeding years, disbursements shall first be paid from the AG Account subject to the provisions of paragraph II(G) of this Agreement. In the event that funds in the AG Account are insufficient to pay the disbursement in the Litigation in any succeeding period, the SAAGs shall advance such funds to the SAAG Account as are necessary to prosecute the Litigation faithfully and with due diligence.

J. Pursuant to Massachusetts Supreme Judicial Court Rule 3:05, the Commonwealth is ultimately liable for those reasonable disbursements pursuant to paragraph II (D), subject to appropriation by the Legislature. The SAAGs agree, however, that the Commonwealth shall not be liable for any disbursements in the Litigation in the event that after the date of this Agreement: (i) the Supreme Judicial Court modifies Rule 3:05 to eliminate the requirement making a client ultimately liable for costs of litigation, or (ii) an opinion is issued by the Board of Bar Overseers indicating that Rule 3:05 is inapplicable to the Litigation, to this Agreement or to agreements for legal services arranged by the Attorney General.

K. Throughout the term of the Litigation, the SAAGs shall employ an experienced litigation attorney to undertake the day-to-day administration of the Litigation. This attorney shall be in addition to the attorney resources that the SAAGs agree to commit in Section I of this Agreement. The salary of this attorney may be paid from the SAAG Account, but not the AG Account. To the extent, however, that the funds in the SAAG Account are used to pay for the costs of employing said attorney, such funds will not be reimbursable disbursements for purposes of paragraph II (D) of this Agreement. To meet the requirements of this paragraph, the SAAGs may designate an attorney from one of their firms to spend 100% of his/her time working on the Litigation. In the event that an attorney from one of the firms is selected to meet the

requirements of this paragraph, that attorney's salary shall not be paid from the SAAG Account.

III. GENERAL REQUIREMENTS

A. Each SAAG shall attach to this Agreement a copy of the resumes of all key personnel. The SAAG shall replace or remove key personnel only upon the prior written approval of the Attorney General.

B. Each SAAG agrees to comply with all applicable Federal and State statutes, rules and regulations prohibiting discrimination in employment, and shall attach to this Agreement a copy of the firm's equal employment opportunity policy.

C. Each SAAG shall attach a statement detailing his/her firm's professional liability insurance. Each SAAG certifies that such insurance will be maintained throughout the Litigation and that the services the SAAG will be performing in connection with the Litigation are covered by the SAAG's firm's professional liability insurance policy.

D. During the term of this Agreement, each SAAG shall promptly provide a statement describing any criminal investigation relation to, or material litigation asserted against, the SAAG's firm or members of the firm.

E. Each Massachusetts SAAG shall certify in writing, under the pains and penalties of perjury, that the SAAG's firm has fully complied with the laws of the Commonwealth relating to payment of taxes, including G.L. c. 62C, section 49A.

F. Each SAAG shall list and describe any litigation or representation ever undertaken on behalf of any member of the tobacco industry.

G. All SAAGs are subject to the Conflict of Interest Laws, as outlined in "Guidelines for

SAAGs", attached as exhibit A, and M.G.L. c. 268A.

H. Termination:

1. Without Cause: The Attorney General may terminate this Agreement as to any individual SAAG, without cause and without penalty, by providing a SAAG with written notice of termination delivered to it at least thirty (30) calendar days before the effective date of termination.

2. For Cause: If any SAAG breaches any material term or condition of this Agreement, or fails to perform or fulfill any material obligation required by this Agreement, then the Attorney General may give notice to the SAAG of his intent to terminate or suspend that SAAG by providing at least seven (7) calendar days written notice of an intent to terminate or suspend. If the SAAG does not substantially cure or correct said breach or failure to perform or fulfill said material obligation within seven (7) calendar days after receipt of such written notice from the Attorney General, or within such longer period as the Attorney General might prescribe in writing, then the Attorney General may thereafter terminate the SAAG or suspend the SAAG. In any event, the Attorney General reserves the right to terminate immediately any SAAG who is (a) disbarred or suspended in any jurisdiction, (b) indicted by a grand jury, or (c) convicted of a felony.

3. Force Majeure: Neither the Attorney General nor the SAAG shall be liable to the other not be deemed to be in breach of this Agreement for failure or delay in rendering performance arising out of causes factually beyond their control and without their fault or negligence.

I. If any SAAG is terminated for cause such SAAG shall not be entitled to compensation or reimbursement of any kind under this Agreement. If any SAAG is terminated for cause such SAAG shall not be entitled to compensation or reimbursement of any kind under this Agreement. If any SAAG is terminated for reasons other than "cause", such SAAG shall be entitled (1) to be reimbursed reasonable out-of-pocket costs it incurred, but only if and to the extent and at the time such amounts would otherwise be payable pursuant to Section II, above, and (2) to be paid such compensation as might be payable to it in accordance with any fee sharing arrangement among the SAAGs, but only if, and to the extent and at the time, compensation is payable to the SAAGs from any recovery in the Litigation pursuant to Section II of this Agreement.

J. Hardship: Each of the SAAGs enter into this Agreement with the expectation that each of them can prosecute the Litigation to its conclusion in accordance with the terms of this Agreement. However, in the event that a SAAG becomes insolvent or suffers substantial financial or business hardship such that it would be unduly burdensome for the SAAG to continue to participate in the representation of the Commonwealth in the Litigation, the SAAG may withdraw from this Agreement, effective 60 days after delivery of written notice to the Attorney General. If a SAAG withdraws in accordance with this paragraph, the SAAG shall be entitled to reimbursement and compensation as provided in paragraph II(I) of this Agreement.

K. Confidentiality: In the event any SAAG has access to "personal data" of the Commonwealth, or on behalf of the Commonwealth, and becomes a "holder" of personal data, as defined by M.G.L. c. 66A, the SAAG shall at all times recognize the Commonwealth's ownership of Commonwealth personal data and the exclusive right and jurisdiction of the Commonwealth and "data subject" (as defined in Chapter 66A) to control the use of personal data. The SAAGs shall prevent the misuse and otherwise protect the Commonwealth's rights in

its personal data and ensure the data subject's privacy, and shall take reasonable steps to prevent any unauthorized access, or physical damage, to such data under its control. The Commonwealth shall have full access to any of its personal data held by the SAAGs without the consent of the data subject. Any personal data held by a SAAG after termination of this Agreement shall be delivered to the Commonwealth within 10 days of the completion of the Agreement.

L. Forum and Choice of Law: Any actions arising out of this Agreement shall be governed by the laws of the Commonwealth of Massachusetts, and shall be brought and maintained in a state court within the Commonwealth which shall have exclusive jurisdiction thereof.

M. If any provision of the agreement is found to be illegal, unenforceable, or void, then the parties shall be relieved of all obligations under that provision, provided however, that the remainder of the Agreement shall be enforced to the fullest extent permitted by law. The headings used herein are for reference and convenience only and shall not be a factor in the interpretation of this Litigation.

N. No amendment to this Agreement shall be effective unless it is approved by the Attorney General or his designees and by authorized representatives of all parties to be bound or affected thereby.

O. Copies of all documents required to be produced under this Agreement shall be mailed or delivered to:

George K.Weber, Chief
Consumer Protection and Antitrust Division
Office of the Attorney General
One Ashburton Place
Boston, MA 02108

IN WITNESS WHEREOF, the Attorney General and the SAAGs caused this Agreement to be executed as of the day and year first written above.

34-12

ORIGINAL TRANSCRIPT

BEFORE THE HOUSE TAX COMMITTEE

IN THE MATTER OF

HB 2821 - Imposing a Tax Upon Income Derived From Certain State Controversy Settlement Agreements

TRANSCRIPT

OF

PROCEEDINGS

taken on the 15th day of February, 2000, beginning at 9:00 a.m., at the State Capitol Room 519 South, in the City of Topeka, County of Shawnee, and State Kansas, before the House Tax Committee.

REPRESENTATIVE WAGLE: Today we're going to continue our briefing on tobacco litigation. It appears the attorney general has come back to the committee. When we left yesterday, we were asking questions about the settlement. So today I think we're going to continue with questions about the settlement. General Stovall.

GENERAL STOVALL: Thank you. Actually, I'd like to be sure your committee had several things. As you can see, we've got lots of documents on the table.

REPRESENTATIVE WAGLE: Let me remind you, first of all --

GENERAL STOVALL: I'm still under oath. I'm aware of that.

REPRESENTATIVE WAGLE: You may continue.

GENERAL STOVALL: Thank you very much. As I indicated yesterday, I wasn't sure I could be here. I chair from nine to eleven today the criminal justice coordinating counsel. It was a previously scheduled meeting. The vice-chairman is the governor. Natalie Haag came in from

maternity leave to chair it so I could be with you today. I'm happy, once again, to be back. What we have are some documents. I frankly was stunned yesterday the committee had not been provided copies of the documents we had provided to the chair, so what we have done is to provide for you a complete set of the documents that we gave to the chair so we'll be able to go through those.

REPRESENTATIVE WAGLE: If I could respond to that. I believe we were in the process of Xeroxing the documents yesterday when we had two Xerox machines break on us. We were waiting for a repairman. Edith came in this morning at seven o'clock. I believe -- are the documents in front of every member of the committee?

STAFF: Yes.

REPRESENTATIVE WAGLE: The documents are in a folder in front of you. You may continue, General Stovall.

GENERAL STOVALL: Thank you. What I would like to do is make sure you have a complete set of the documents. That

becomes important to me really only because of correspondence I had yesterday with Representative Jensen, the speaker. The speaker's letter is attached. We're going to distribute that. I'll ask staff to hand out things as we go. The speaker's letter was dated yesterday. He was aware certain documents had allegedly not been provided to the tax committee chair, so he hand-delivered a letter over, in fact, to me. It has four categories of documents that were alleged to him not to have been provided. One of which was the signed, dated copy of the contract with our tobacco counsel. Folks, that was provided to the tax chair on February the 4th of this year. That will be in a cover letter, and the contract that we'll get to as we go through the documents. So I just wanted to be sure the committee has everything. I don't blame the speaker for having been agitated with me at not having provided all the documents because that's what he was apparently led to believe. Perhaps that's why he wanted someone here to be under oath because he had

maybe gotten some wrong information. But I would like to go through all that with you and be sure you know what we have and what we have actually provided to your committee chair.

In addition, before we do that, there's a couple other things that has been requested. As you know, legislators can request material anonymously. That's been done. My travel vouchers for the last four years have been requested anonymously, and our staff -- actually, mine and John Campbell's as well has been requested. We have not gotten all that material together. Staff informed me yesterday some is available. While it will be provided to the legislative staff person who made the request. I thought I would short circuit that and bring it. I'm sure one of two people that requested it are probably in the room today. So let me make that available to the committee chair as well. I guess Representative Powell isn't here today. This was the other copy for him.

To walk through the documents, then, if

we could, we as you might imagine have spent an awful lot of time trying to put this together on short notice. I'm going to ask staff to hand things out as we go. The first is going to be the correspondence with the tax committee chair. That would be the letters then from Susan Wagle to us. The first was a letter January 26th relating to the hiring of private counsel saying she wanted all that information. January 31st was a letter, then, from us to her. That will be provided to you as Mary and Becky hand that around. In that January 31st letter, John Campbell, my senior deputy, wrote back and said the information from the post audit was available and that apparently by phone the tax committee chair had asked to meet with John Campbell private -- well, with the vice chair I understand and perhaps the minority leader. John confirms that meeting will take place. Should you or your staff require additional information or assistance, please contact me. The next letter is from your tax committee chair to me dated February 2nd. First paragraph,

"Thank you for allowing John Campbell to brief the tax leadership yesterday on the tax litigation." The next paragraph then she asks John to come back and brief you yesterday and today. You'll note it wasn't me that was asked to come, and I wasn't asked to come until Wednesday to speak after Representative Powell speaks to you and to talk about the bill he proposed. As I told you yesterday, I don't intend to take a position on that bill. This letter also notes, by the way, the committee would have started at nine o'clock yesterday. The next letter is February 4th. That's from Representative Wagle to us again asking for more documentation, and she's very specific about that. February 4th then from us to Representative Wagle. John is writing to her. He is acknowledging attending the meeting the day before to brief the tax leadership. As I understand it, he says you do not want to take advantage of my offer for either you or your staff to have complete access to the tobacco litigation files. He then goes through four categories

of the documents that were requested by the chair, and he responds to each of those separately. He attaches to this February 4th letter a signed, dated copy of the contract which evidently was not provided to speaker Jenson the other day.

REPRESENTATIVE WAGLE: If I could interrupt you, I think the problem is that we did not receive a dated contract, and that's why the speaker sent you another letter asking for --

GENERAL STOVALL: Well, Representative, it's attached to the letter of February 4th. That's attached to the documents here. It is dated and signed by all the parties. If he didn't see it, that's a different issue. It was provided on February the 4th. Attached to your letter, then, is that contract. You'll see that it's got all the signatures on it. Next -- and I guess I offer that just so you understand maybe what the history of some of this is. The next bit of information then would have to be with the post audit. The post audit report we've provided to you in

full because I understood yesterday from Representative Jenkins question you had not been made aware of the legislative post audit. Attached to some of the post audit will be the actual interview notes. That wouldn't have been available apparently in the actual post audit report. When John requested the information from legislative post audit, they provided the actual interview notes in addition to the published post audit report. So that's being provided, too. You may remember yesterday I quoted from those interview notes speaking both of comments that one of the Hutton brothers made as well as Mary Barrier of Morrison and Hecker. All of that post audit plus those interview notes are being provided to you now. I won't take time going through the legislative post audit report, but you'll see a significant portion of it deals with the tobacco litigation, and you'll see the conclusion legislative post audit drew that there wasn't a violation of the law. The next thing -- are we okay on that? The next will be just simply the

guidelines for contracts provided by the office. I don't know that you'll find this particularly helpful, but it was provided to your tax committee chair. The next document, again, I don't know how helpful you will find it, it is dated June the 7th. It is simply the documentation of the date that John and I met in St. Louis with Attorney General Mike Moore of Mississippi and his counsel, Dick Skruggs. The next series of documents frankly that you will find most interesting I suspect. Those are the correspondence from Hutton and Hutton. There are several letters that were provided to the committee chair and that I want to be sure that you have. Again, I apologize for all the paperwork in the hustle and bustle of this. This is the only way to do it.

REPRESENTATIVE WAGLE: I think what's happening now is each member of the committee has two sets.

GENERAL STOVALL: I wanted them to have my set. My set begins on March the 14th with a letter from Hutton and Hutton. This is before you may remember that I had

even made the decision to file the tobacco lawsuit. It looks like this. This is signed by Andy, and he is introducing himself to me talking about their work in the Castano private class, and asking for some information about that. Then behind that, you will find a document that looks like this. It's just a copy of his business card copied, and behind it are my handwritten notes from that meeting, the first and only meeting that I had with Mark and Andy Hutton. You will see that it's dated April the 8th. In my handwriting which I'm not very proud of, but nonetheless I think you can figure out what I say, we talk about the litigation in general. On the second page, then, in what I've highlighted, it's not going to be highlighted in your copy, but it talks about the contingency fee of 25 percent. Then there's an April 10th letter from Hutton and Hutton provided to your tax committee chair. "Dear Attorney General Stovall: Mark and I would like to thank you for allowing us to meet with you." He goes on to talk about

other state actions and tobacco litigation. Then there is a fax, April the 19th, 1996. It's from Hutton and Hutton. "Dear John: Please find enclosed a working draft of an attorney/client agreement. Once you have reviewed the same, please forward it to me." Behind that, then, is the one-page document, the one-page contract that I mentioned to you yesterday. You will see that there's no provision that counsel keep track of hours, and you will see what they proposed was a 25 percent contingency fee. June the 10th is another letter from Hutton and Hutton. "Dear John: Just for your information, when a private attorney in Kansas is responsible for recoveries of money in an action where Medicaid is reimbursed," remember, folks, this is a Medicaid reimbursement suit, "there is statutory authority that the attorney's fees will be one-third for cases settled prior to trial or 40 percent when the trial is convened." And they were kind enough to send us a copy of the statute and underline on the second page the relevant part. They were still wanting at least a 25

percent contingency fee. That to my knowledge is all the correspondence that was provided from Hutton and Hutton or to them to your tax committee chair. You will find behind the Hutton and Hutton documents an E-mail from me of June the 28th to John Campbell. It was after the phone call that I mentioned yesterday in which Entz and Chanay indicated that they were interested in the contract. You may remember from yesterday that this call came about after we learned that national counsel would be financing, fronting the expenses, and that allowed us to have more flexibility in choosing who to hire. Prior to then, we were going to have to find a law firm that would front the expenses for us, and we were left with only Hutton and Hutton to do that. The June 28th E-mail says -- it's from me, again, to John. "Jeff is very interested in getting involved with us. He understands the contract would say 'whatever court awards.' I told him you would tell Skruggs if they were on board. Skruggs can get ahold of him." Then this is what apparently

has the chair concerned according to what I'm told the Wichita Eagle says. The next sentence is "Also told him," again this is me to John, "Also told him we had to crawdad out of arrangement/discussions with Hutton and Hutton." As we had talked yesterday, John had been continuing to talk with Hutton and Hutton in the hopes of getting them to come off of a guaranteed percent in the contract. We felt like they were our only suitors who were willing to finance the litigation, and if Kansas was going to sue tobacco, it had to be with a firm that would front the expense, because I was sure the $7,000,000 we estimated it would take would not be coming from the legislature. You can see from the rest of the E-mail, John was preparing for a motorcycle trip, and I was concerned about his wearing a helmet and that's on there as well.

There is an article -- we didn't copy newspaper articles, December 13th, 1998. Wichita lawyers say they tried to land tobacco suit. This is an article about Hutton and Hutton. We won't be quoted in it

you'll be able to see. It's based on the Wichita Eagle talking about how they had wanted to do the tobacco litigation, but the contract was not given to them. Anyone who would say Hutton and Hutton had a binding contract with the state would not be truthful and based on other statements of Hutton and Hutton they would not say there was any binding contract with the State of Kansas. Those are the Hutton and Hutton documents.

REPRESENTATIVE WAGLE: General, are those all the documents you have received from Hutton and Hutton?

GENERAL STOVALL: They are all the ones made available to me with the exception of one John showed me last night as he found out he was going through the files as he told you yesterday he was going to do. It is one dated August 2nd.

MR. CAMPBELL: 17th.

THE SPEAKER: That.

GENERAL STOVALL: That in this process did not get brought over. It was a letter from either Mark or Andy enclosing

the copy of an editorial or a column in the Wichita paper that Mernrow (spelled phonetically) wrote about the addictive nature of nicotine. He sent it to me. I did a handwritten note a copy will be provided to you which says something to the effect of thanks for the article. Must be really tough to quit smoking which was the gist of the column, and I said --

REPRESENTATIVE WAGLE: Okay. Did I not ask for all communication which would mean communication from the Huttons to you and communication from your office to the Huttons?

GENERAL STOVALL: Absolutely. It wasn't found until yesterday. I'm telling you it was just neglected to bring over. Someone can bring over 25 copies. I had asked for it to be done and it wasn't.

REPRESENTATIVE WAGLE: Did you on any occasion ever send to Huttons a contract for their services to be involved in tobacco litigation?

GENERAL STOVALL: I don't know.

REPRESENTATIVE WAGLE: John, if

you are going to speak, would you mind going under oath first?

MR. CAMPBELL: No.

JOHN CAMPBELL,

called as a witness on behalf of the Committee, was sworn and testified as follows:

REPRESENTATIVE WAGLE: I just asked about if there was correspondence from the AG's office to Hutton and Hutton as a contract offered to Hutton and Hutton.

MR. CAMPBELL: As I told you yesterday, we're redoing the litigation file in tobacco to make it chronological. I also ran a check on our mail log. Let's see. I've got -- we've got the March 14th letter from Hutton and Hutton. You should have that. There's an April 10th letter. You've got that. I've got an April 15th, '96 fax. I have not found that yet. I've got an April 17th fax. I haven't found that. There's an April 19th fax. You should have that. There's a June 10th fax. You should

have that. I've got an April 24th, May 2nd, May 30 and May 31 which I'm thinking they are probably the same documents. Hutton and Hutton would normally fax something first and then send it in writing. We're looking for that. We got -- there's also a June 3rd and a May 27th, and we've got the August 7th letter which you should have. Let's see, we've got a March 20th we've got and then we had correspondence in November of '98 which you should have. I think the problem is there's twofold. We were shooting drafts back to each other, and I normally wouldn't save a contract draft, but the other and I think what might be in some of these, like I found one letter from Hutton and Hutton about Native Americans. It was about Indian tobacco lawsuits. So that was in the research file with the Indian stuff.

REPRESENTATIVE WAGLE: Do you recall, General Stovall or Deputy Campbell, do you recall ever sending the Huttons a contract for services?

MR. CAMPBELL: I'm sure -- I'm assume we exchanged drafts.

REPRESENTATIVE WAGLE: Would you mind looking at this documents, please? It appears here is a fax from the Kansas Attorney General. Up at the top it says approved by CJS. Who would CJS be?

MR. CAMPBELL: Draft approved by CJS. That would be the attorney general.

REPRESENTATIVE WAGLE: What does that appear to be to you?

MR. CAMPBELL: It's a draft. It's an offering to contract.

REPRESENTATIVE WAGLE: And what's the date on the contract?

MR. CAMPBELL: 6/4/96, June 4th.

REPRESENTATIVE WAGLE: Is it to the Huttons?

MR. CAMPBELL: I'm sure it is.

REPRESENTATIVE WAGLE: Are they required in that draft to keep time logs?

MR. CAMPBELL: Well, let me see.

REPRESENTATIVE WAGLE: Committee, I didn't hand this out to you. This was not in the package the attorney general gave you. We did send a copy out so everybody had a copy of this.

GENERAL STOVALL: I take it it's not a signed contract.

REPRESENTATIVE WAGLE: But wasn't a contract -- would you look at it, General Stovall, and see if you authorized that contract to the Hutton.

GENERAL STOVALL: I don't know if I can say that.

REPRESENTATIVE WAGLE: Does it say approval up in the corner by CJS.

GENERAL STOVALL: Yeah, this would have been a contract draft. Paragraph 15, compensation on the foregoing contingency shall be made in accord with the particular ethical statute 1.5 and not to exceed 25 percent after the amount recovered. We were talking to them about the fees. They wouldn't sign this, though, because they wanted a guarantee.

REPRESENTATIVE WAGLE: So when I asked for all open records regarding your communications with any and all law firms regarding hiring of outside counsel, why was that not included in the documents?

GENERAL STOVALL: John's telling

me we don't have it.

MR. CAMPBELL: You know, if we save every draft, I mean, we'd just -- we had to move. We didn't have enough room for people.

GENERAL STOVALL: There is nothing ominous about it. If it was a signed contract we would have had it. It's consistent with what I told you yesterday.

REPRESENTATIVE WAGLE: Representative Aurand.

REPRESENTATIVE AURAND: I don't know how this works. Is this one of a series of several drafts that was sent to them?

MR. CAMPBELL: Well, I assume it was. I didn't save the drafts, I think. We got a good chronology on pre '96. We're pretty good on '96. I mean we're building a chronological file.

GENERAL STOVALL: Folks. This was four years ago, and we didn't contract with them, so what we may not have kept shouldn't be considered incriminating. We have given you what John has been able to

find. He may not be the most meticulous recordkeeper in the world. He is probably as frustrated by the documents not being in order as I am, but there's nothing ominous about that.

REPRESENTATIVE AURAND: I guess that's my only interest. It seems to me the big point or whatever seems to be the timing and who got the job and when all this happened. This was the beginning of June. I just kind of wondered do you have kind of just a ballpark idea that there was the first draft or several drafts or when the last one might have went to them. You'd say several drafts.

MR. CAMPBELL: Oh, yeah. Oh, yeah.

REPRESENTATIVE AURAND: Do you think this was toward the end of those?

MR. CAMPBELL: I really don't know. It looks like -- you know, with a different type and all that, it looks like we've gone through a couple of things here.

REPRESENTATIVE AURAND: When you sent these at any time on a draft and they

would agree in theory to what the draft said, is sending them a draft is that similar to saying we will go ahead and take you if you accept this.

MR. CAMPBELL: Well, contracts offered, acceptance, consideration. I guess technically the first offer came from them, their letter of engagement. That was not accepted. We countered, I'm sure more than once. To the best of my knowledge -- forgot that. They felt that if you didn't have a fixed percent, you didn't have a contract. And I would say, no, I've got to put a cap on this thing. I don't want to put the cap on money, because I don't know what they are going to make, and I don't know how long it's going to take. And I didn't want to give the tobacco companies an incentive to stall this thing. That's why I never liked the monetary cap.

REPRESENTATIVE AURAND: As you worked through these different draft copies, were there other things you agreed on and this was kind of still out toward the last? Were you gaining ground, I guess.

GENERAL STOVALL: We would have never gained ground Representative on the most important issue which was something other than a guaranteed percent.

REPRESENTATIVE AURAND: I understand. I didn't know if there might have been several other things that maybe -- that's one piece.

GENERAL STOVALL: Fronting expenses we agreed on. They were going to front expenses, and we agreed upon that. The most important component was not having a fixed percent in the contract. There never was an agreement. I'm confident if Hutton and Hutton's come in, they'll tell you that as well. They told post audit in '97 if there wasn't a guaranteed percent in the contract, they felt like it wasn't a contract.

REPRESENTATIVE AURAND: That's where I guess I'm getting at this one, I don't know, E-mail or memo to John about crawdadding out. In the negotiations, when you negotiate with someone, once you learned there was going to be national counsel front

the money, did you then go back to Huttons and say we have an offer now for someone else to front the money, we've got -- basically, we've got a chip. What will you do now in your 25 percent.

MR. CAMPBELL: I should say the General did direct me to tell them the news. I did put that off. Two reasons. One, I didn't want tobacco to know we had Dick Skruggs. I'm in no way implying the Huttons would have gone out and told them. There is a community and word gets out pretty quick. I didn't want tobacco to know, and also I wanted to see what kind of draft they came up with.

REPRESENTATIVE AURAND: What kind of what, what kind of draft?

MR. CAMPBELL: Ness Motley and Chanay, Entz and Chanay were working on a draft. I was, too. We were there. I wanted to see what they came up with. I had a pretty good idea from the Chicago meeting in May what they tried -- were going to try to do. I wanted to see it first. And I did put off till the 7th calling Andy.

REPRESENTATIVE AURAND: The 7th of August.

REPRESENTATIVE AURAND: Of August.

MR. CAMPBELL: I did put off in July calling them. I don't want to say I never talked to them in that time frame. Tell them we're out.

REPRESENTATIVE AURAND: Was it yesterday you said August 1st was kind of when you hired.

GENERAL STOVALL: They started working in July. Once we had national counsel that was willing to front expenses and we had Dick Skruggs who was the premiere states Medicaid recoupment tobacco lawyer, we didn't need Hutton and Hutton. That was at tracks in the beginning of Hutton and Hutton, they were the only one prior to Skruggs to front expenses. Once we had national counsel to do that, we didn't need Hutton and Hutton to front the local expenses.

REPRESENTATIVE AURAND: I guess that's the part I don't understand. If they

fronted that and for whatever reason you've been working with Hutton and Hutton exchanging drafts and trying to get something with them. Now you have basically a bargaining chip to go back to Hutton and Hutton who I presume -- I don't know anything about lawyers, have a good reputation to go back to them and say, look, now we have another offer fronting legal expenses, what will you do for us now.

GENERAL STOVALL: You know why? I was tired of messing around with them. They weren't coming off of that guaranteed percent in the contract. Every meeting we'd had with them, every conversation John had had with them indicated they were stuck on that percent. I had no reason to believe they weren't going to come off of it. We didn't have time to waste. The tobacco companies were suing attorneys general around the country in a preemptive strike to get to court before attorneys general did. I did not want that to happen. We wanted to get to court. We had the No. 1 national counsel in the country. That's who I wanted

all along. They were fronting expenses. They wouldn't take a guaranteed expense. I had the sweetheart deal I wanted for the State of Kansas.

REPRESENTATIVE AURAND: With that national counsel that you had and then how that ties back into choosing your state counsel, I guess I miss how getting them on the national level throws out Hutton and Hutton on the state level and brings Entz and Chanay on the state level.

GENERAL STOVALL: Hutton and Hutton wanted to take the leadership roll in litigation. They wanted to be the national counsel for Kansas. They wanted to put together a consortium of law firms to put their money together to pool to cover the expenses. That's what they wanted to do and to be the lead counsel. They didn't want to be second dog, if you will, to Dick Skruggs. Additionally, Skruggs and that group of folks were not interested in working with Castano lawyers that had done that class action. And so because our national counsel wasn't interested in working with that

particular firm, it was an easy call in my mind. I simply made the judgment that I wanted to go with somebody who was going to give us the best deal possible and whom I trusted. I make these decision about who to hire law firms all the time.

REPRESENTATIVE AURAND: So with the relationship from the national counsel back to the state, they played a large part in deciding who --

GENERAL STOVALL: Absolutely.

REPRESENTATIVE AURAND: Who you hired. They wouldn't work with Castano group lawyers.

GENERAL STOVALL: They didn't want to work with the particular firm in Wichita. There's a particular division in the bar of various kinds of lawyers. Skruggs and Ness Motley -- Ron Motley tends to be quite a plaintiff's lawyer. He and Skruggs had come to an understanding over this. You would ordinarily put, I think, Motley, and I know this is far afield from what you guys want. There is particular intricacies involved in all litigation but

certainly tobacco litigation. It just wasn't going to work to have the Wichita firm we've spoken of contracting with us and have Dick Skruggs as well.

REPRESENTATIVE AURAND: So the Wichita firm wasn't interested. They said we're not going to work as an underling to federal counsel.

GENERAL STOVALL: I didn't ask them that. They had always made -- in the one conversation I had with them, they made it obvious to me they wanted to be the lead attorneys, and they wanted to put the other law firms together. I think their one-page contract suggests that as well, that they would be lead counsel.

REPRESENTATIVE AURAND: Thank you.

REPRESENTATIVE WAGLE: General Stovall, can you explain why you were in contract negotiations with Hutton and Hutton and in those contracts you offered them you required them to keep time records and then in the contract that you settled with Entz and Chanay, there was a specific clause to

not keep time records.

GENERAL STOVALL: I think I described that yesterday. The national law firms of Ness Motley out of North Carolina or South Carolina and the one out of Mississippi are traditional plaintiff firms, and they do not keep hours. They insisted that there not be a provision in the contract that required that. Because they were getting paid on contingency, it didn't matter to us whether or not they kept hours. Our standard is to require lawyers to keep hours because we tend to bill -- or they tend to bill us on an hourly rate. It's important. I suspect it was a standard provision in the contract. John can perhaps address if it came from some other purpose.

REPRESENTATIVE WAGLE: Is it standard most law firms keep track of hours on any case no matter what it is.

GENERAL STOVALL: No, it's not. Ness Motley and Dick Skruggs' firms do not keep track of any hours. They have no mechanism to keep track of hours. The number of hours doesn't matter when you get

paid not by the hours worked but by the results achieved.

REPRESENTATIVE WAGLE: Okay. And so it appears from what we have sitting here this morning, you offered Hutton and Hutton a contract where they fronted the expenses, and they had to keep track of hours.

GENERAL STOVALL: And they would.

REPRESENTATIVE WAGLE: You were in negotiations. Then it appears within a matter of days you turned around and offered a contract to your old law firm where they don't have to keep track of hours and where they don't have to front expenses. Is that not a sweetheart deal?

GENERAL STOVALL: The sweetheart deal for the State of Kansas is we are paying not one dime for having the privilege of collecting $1.6 billion. The lawyers are being paid out of big tobacco one and a half percent. If I would have signed the contract you seem to think is the deal of the century, it would have committed us to 25 percent of the tobacco recovery to Hutton and Hutton. That would be

approximately $400,000,000. I don't think they would be willing or probably any law firm willing to walk away from $400,000,000 for 1 and a half percent or 27 million dollars. I did the sweetheart deal I believed was in the best interest of the State of Kansas. I did in August of 1996, and I still believe that.

REPRESENTATIVE WAGLE: Did you ever offer Hutton and Hutton a contract for the same amount of up to 25 percent?

GENERAL STOVALL: Yeah, you just showed it to us.

REPRESENTATIVE WAGLE: That says up to?

GENERAL STOVALL: Yes, I just read it to you.

REPRESENTATIVE WAGLE: You just offered that to Hutton and Hutton.

GENERAL STOVALL: You gave it to me.

REPRESENTATIVE AURAND: Just out of curiosity, Entz and Chanay was not required to keep track of hours, and this whole thing is leading up to a tax bill

which I think people I've talked to have different reasons for wanting to support the tax bill. There is various reasons out there where people want to support this tax bill. Did you ever ask them if they did keep track, not that they had to, did you ever ask them if they just kept track in passing?

GENERAL STOVALL: I did not, no.

REPRESENTATIVE AURAND: Do you know if they might have?

GENERAL STOVALL: They have said that they didn't.

REPRESENTATIVE AURAND: I guess the other thing I was kind of wondering if you figure this out, the 10,000 hours is what everybody is kind of --

GENERAL STOVALL: It was in the arbitration decision the tobacco companies estimated local counsel put in 10,000 hours on that case. It works out to about 2,700 hours it's one and a half percent of the billion and a half the stated will receive. The state is not paying a dime of it.

REPRESENTATIVE AURAND: I

understand the percentage is low. The $2,700 an hour, did you say the attorney general's office billed out.

REPRESENTATIVE WAGLE: 200--233-some thousand.

GENERAL STOVALL: John was 150. I was 165. That's what you get for being the boss.

REPRESENTATIVE AURAND: The extra 15 bucks an hour.

GENERAL STOVALL: Not that any of it comes to us, obviously.

REPRESENTATIVE AURAND: The 2,700 an hour as compared to that 150 an hour, can you see why some people as far as tacking on a tax making whatever 16, 17 times as much per hour might bother a lot of people.

GENERAL STOVALL: I understand -- I don't understand about the tax at all. I think if you're going to tax these guys, tax the people that defended big tobacco. They are the bad guys in my mind. I don't understand that. Those lawyers made plenty of money. They made it every single month in regular checks from the tobacco

companies. They didn't put anything up front. They didn't risk anything. They knew they were going to get paid every single months and dozens got paid on just the Kansas case. Clearly, 27,000,000 is a lot of money. I wouldn't tell you any differently. It's more money than I'm ever going to see in my lifetime I'm sure. The issue is not that they got 27,000,000 in my mind. It's the fairness of all of it. They did a lot of work. The arbitration panel is the one that made that determination. If Hutton and Hutton would have gotten the contract, what would they have gotten? They wanted a guaranteed percent. They would not have taken from the arbitration money, the tobacco pot money. They would have been able to as attorneys in Maryland, Illinois and I think Iowa have sued or filed liens against the state, oh, no, we had a guaranteed percent whatever it was, guaranteed 15 percent, let's say, for purposes of discussion contract with the state. We don't want to take from the arbitration panel. Those numbers are really

low, one percent, two percent. We want our guaranteed percent. The attorney general in that state guaranteed us 20 percent of what the state got. We want that. The state hasn't gotten the 38,000,000 Kansas has gotten from tobacco. They put liens on it. We're not facing that at all, folks. No question. Entz and Chanay is who I used to work for part time in the 1990's. Did they do a good job for us. Yes, they did. Did they front expenses along with national counsel. Yes. Did they risk it all. Yes. Did they take it on a contingency, yes. Are they now being financially compensated. Absolutely. That was the nature of this agreement. Nobody in August of 1996 had any idea that any money was involved in this contract.

REPRESENTATIVE WAGLE: General Stovall, could we address that question. I have here another document from Hutton and Hutton dated June 5th that I'd like you to look at. It's a letter from John Campbell. I'm wondering if you ever saw it. On the second page, "We understand the potential

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recovery in this litigation could be enormous."

GENERAL STOVALL: Sure. It could be.

REPRESENTATIVE WAGLE: Wasn't that the word on the streets.

GENERAL STOVALL: Well, I don't know what the word --

REPRESENTATIVE WAGLE: The word among people that were involved in litigation, and you said yesterday yourself that we were talking at the beginning of your testimony a potential --

GENERAL STOVALL: Potential, yeah, big tobacco had never paid a dime to any plaintiff ever.

REPRESENTATIVE WAGLE: Did you ever receive a document stating the potential recovery was enormous? Did you go into this knowing if we did recover we were talking about massive amounts of money?

GENERAL STOVALL: And that is why we didn't want a guaranteed percent in the contract that Hutton and Hutton wanted. I would not guarantee the percent because we

did not know. It could have been because big tobacco had never paid anybody any dime anytime. But on the other hand, there was money involved. That's why we sued because the state's Medicaid reimbursement for smoking related illnesses was substantial. But I could not have told you nor would I have bet money, yes, we were going to get it.

REPRESENTATIVE WAGLE: But you entered the lawsuit believing there was a potential there to settle.

GENERAL STOVALL: Of course there was. We wouldn't have sued if there wasn't a potential for litigation. There's always a settlement. We could settle with Nebraska in water, but I don't think that's very likely.

REPRESENTATIVE WAGLE: And the new national strategy involving the attorneys general across the nation could result in massive amounts of money. I mean --

GENERAL STOVALL: I was the 11th state to sue. Not the 49th. When I sued in

August of 1996, there was not the mass swelling or the grand swell of support of attorneys general for this litigation. One of the documents quoted in the lengthy book I call it that John and I gave you yesterday talks about two attorneys general, one from Alabama and one from Ohio that in 1997 both were saying don't be getting in that tobacco litigation. The theories are weak, not very strong, weak at best I think prior said and bizarre at worst. There was not a grand swell of support in August of 1996. I am guilty of not having a crystal ball to have known that. For that I apologize to this committee. I did not know this would result in $206,000,000,000 in a national settlement that was historic in the history of the world.

REPRESENTATIVE WAGLE: John, just so you could show that document to the attorney general.

GENERAL STOVALL: I don't doubt that we got it.

REPRESENTATIVE WAGLE: So that was just --

MR. CAMPBELL: But the risks, however, are likewise enormous.

REPRESENTATIVE WAGLE: Right.

MR. CAMPBELL: With that said, we'd like some certainty that the state agrees a contingency of 25 percent is fair and reasonable. We have made some changes to your latest draft. Rejection, counter offer which I would encourage you to review and discuss with us. Yeah.

REPRESENTATIVE WAGLE: That was provided to me by the Hutton law firm.

GENERAL STOVALL: John doesn't have it apparently. We have given what we have.

REPRESENTATIVE WAGLE: Representative Wilk.

REPRESENTATIVE WILK: Just an observation. The legal fees that are going to be paid, are they not -- is that scheduled over 25 years.

GENERAL STOVALL: It is.

REPRESENTATIVE WILK: 27,000,000 and dividing it by 25 years.

GENERAL STOVALL: However long it

takes to be paid up to 25 years, no interest.

REPRESENTATIVE WILK: Just an observation. We are focusing on the money here. I don't know that that ought to be the focus. Let's go back to 1996. Look at how many people actually ever won a lawsuit and then let's ask -- I look at this putting it back in business terms. Basically, if you use the 10,000 hours, you've got a law firm that invested close to a quarter of a million dollars. And they didn't know if they were going to win. Up to 1996, nobody had won anything. If they took that quarter of a million dollars and look at some rate of return over that, you're basically looking at a ten-fold return over 25 years. I suggested to the committee, if you've got a quarter of a million dollars to invest in 1996, that probably wouldn't have been the top spot to put it in the tobacco lawsuit because there are countless other investments you could have got a ten-fold return on in much less than 25 years. So I think we ought to put it in perspective.

Let's move beyond the money. We can come back and talk about it.

REPRESENTATIVE WAGLE: Is there a possibility the monies could be paid out earlier than 25 years?

GENERAL STOVALL: I indicated it was to be paid at the end of 25 years. The lawyers are looking at 15 to 20. If I could go on with the documents that we provided this morning, this set is from the Morrison and Hecker law firm. It is another firm as you know that we talked with. The first thing you'll be given hopefully is a Xeroxed copy of the business carried of Mary Barrier, B A R R I E R. She came along with Bob Vancrum who was formerly a colleague of yours who now works with Morrison and Hecker. Behind that business card will be my handwritten notes as to that discussion. And on one of the pages it will enumerate what the financial arrangements are that that firm was tentatively talking about. They certainly hadn't made a decision to take the case, but they talked about we would have to front expenses as well as pay

some discounted rate of hourly fees. They estimated at the bottom of one of the pages you'll see $1,000,000 a year for five years. As I told you, that was unacceptable to us. They sent a follow-up letter that is the April 10th letter that should be in your possession as well. That confirms the discussion in the meeting. You may remember yesterday legislative post audit -- from my comments about post audit anyway that Mary Barrier called back after this meeting and told John that the firm was unwilling to front expenses. Then when we found that Skruggs was willing to front expenses, John talked to Morrison and Hecker, called Morrison and Hecker to see if they would be local counsel. They at that time told us they had a conflict of interest discovered, some partner of theirs had, I don't know, some tangential relationship, and they didn't want to be involved. So that was the Morrison and Hecker conversations. The next things we provide to the tax chair are documents regarding the Entz and Chanay consultations. Things aren't necessarily in

chronological order. I grouped them by subject matter, perhaps that would be easier. The first thing is a July 25th letter with a proposed draft of the contract in it. Behind that is a July 31st letter. That's the one you may remember from yesterday that I handed to the committee chair yesterday, not to you committee members because John had uncovered it Sunday night and it had not been originally provided. It says attached is the draft engagement letter, information about naming some other party defendants and then a rough draft of the petition. That was provided. Then on August the 14th is a letter from Entz and Chanay actually signed by Stu Entz to John saying enclosed is the proposed revision to the contract. They set out four things that is their interpretation of the payment clauses in the contract. No. 1, if the state receives nothing, there is no fee. No. 2, if any judgment is entered, the court can determine the fee pursuant to rule 1.5. That you've heard us talk about is the requirement ethically for lawyers to have

fees determined as reasonable. No. 3, if there is a settlement, the fee shall be a part of the settlement and the state must approve settlement. That made sure the lawyers couldn't settle without my approval. No. 4, there is an absolute cap on counsel's fees at less than the normal contingent fee. Normally, contingent fees are one-third, 33 percent. Then attached to that was the draft contract, not the signed dated one. I've given you that before, but a draft contract.

Let me provide to you, too, what's called Q and A. This is something I mentioned yesterday in my testimony to you that is the Q and A that we provided the day of the press conference announcing the lawsuit. It was handed out attached to every statement that I made as well as to the press release. Question No. 13 on the back page: How did you choose counsel for the State of Kansas. Answer: We have sought the assistance of both local and national counsel in this lawsuit. Entz and Chanay, P.A., Attorney General Stovall's

former law firm, was chosen because it's a leading expert on Medicaid reimbursement and holds Attorney General Stovall's utmost trust in protecting the interest of taxpayers. We never ever hid who it was that we had hired.

The last thing that I would like you to be sure to have then is a copy of the arbitration decision. That, too, was made available to your tax committee chair. I have copies of the bio's of the three members that served on that arbitration panel. I didn't copy those thinking that was going a little too far. If you have desire for that, I absolutely will make that available. But it's the arbitration decision, then, that is how the attorney fees were decided. Every law firm in the country that chose the route of arbitration goes through this kind of process. They present their side. The tobacco company presents their side. In this case, it took several months, a decision was made. They go through, you'll see, and evaluate what the contract said which was up to 25

percent. They talk about the nature of the lawsuit. I would even boast for a moment because I'm sure no one else will and say this opinion says "given the political atmosphere in the State of Kansas, it appears that the Kansas Attorney General took a courageous step in commencing litigation against the settling companies." You can say that again. Nonetheless, it talks about the work of local counsel in evaluating those 2,500 documents that I mentioned to you yesterday that we broke the joint defense privilege on and that stood to be opened up to the rest of the country. The decision as you know concludes that totally. 54 million is what will be paid to the three law firms that represents Kansas. This panel doesn't know how the split will be made. That was done in the original contract. Nonetheless, that, I believe, is all the documents that we have provided to the tax committee chair, and I wanted to be sure you had those as well.

REPRESENTATIVE WAGLE: General Stovall, on the arbitrator's decision which

was faxed to the press on the day that they determined --

GENERAL STOVALL: Right. And then I made available to them as well.

REPRESENTATIVE WAGLE: And you made available to everyone. There is three signatures here. Who is John Calhoun Wells?

GENERAL STOVALL: I believe he's the one who was chosen mutually --

REPRESENTATIVE WAGLE: By tobacco.

GENERAL STOVALL: And the state's lawyers.

REPRESENTATIVE WAGLE: A neutral party?

GENERAL STOVALL: Chosen by those two parties.

REPRESENTATIVE WAGLE: And the Honorable Charles Renfro?

GENERAL STOVALL: Chosen by tobacco.

REPRESENTATIVE WAGLE: Chosen by tobacco. He was a judge?

GENERAL STOVALL: Yes, I maybe should have made this available. Used to

work for Standard Oil Company. A partner in Pillsbury, Madison and Sutro (spelled phonetically). He was a deputy attorney general of the United States. U.S. District Judge for the Northern District of California, had been with Pillsbury before that. Was a part-time instructor at a law school at Berkley, very good resume. I can make that available. That's who the tobacco company's choose.

REPRESENTATIVE WAGLE: Harry.

GENERAL STOVALL: Hugey (spelled phonetically). That's who the state's lawyers chose.

REPRESENTATIVE WAGLE: A neutral panel to determine fees.

GENERAL STOVALL: I didn't say it was neutral. The tobacco companies choose one person. He's there to look out for the financial interests for the tobacco companies, one person that the state's lawyers chose who they thought would be sympathetic to their concerns, and a third person chose and it was mutually agreed upon or else there wouldn't have been consensus

on that person.

REPRESENTATIVE WAGLE: Did you appear before this counsel?

GENERAL STOVALL: I did not except by telephone.

REPRESENTATIVE WAGLE: You called in, and you gave them facts about the Kansas case?

GENERAL STOVALL: I talked to them about what had happened in Kansas, yes.

REPRESENTATIVE WAGLE: Okay. Is there written testimony about what you said to this panel?

GENERAL STOVALL: No. I was in Pasadena for the Colorado water lawsuit. Called in from my hotel room on a Saturday morning. Made comments. I have rough drafts of notes I would have spoken from.

REPRESENTATIVE WAGLE: Would you care to deliver those notes to the committee?

GENERAL STOVALL: Well, I'd be happy to if you think that's important. It wasn't anything you had requested earlier.

REPRESENTATIVE WAGLE: No, it

wasn't anything I requested earlier. I think this was the basis -- your communications was a basis by which they arrived at a $54 million settlement.

GENERAL STOVALL: Mine as well as a lot of other information they received. What I refused to do in that telephone call was to name any amount of money. I said that from the outset. I had no idea how much Kansas counsel was asking for. I assumed they asked for an amount. They provided information about the work they had done. This panel, based on the prior decisions and their knowledge, came up with what amount was appropriate. I told them at the beginning and despite the harsh questioning by this Mr. Renfro demanding basically that I name an amount, I refused to do so. I explained this very issue to them. Because I had worked with Stu and Jeff, I simply was not going to name a number. It put me in a very uncomfortable position, and I would not do that. So I told them about the work, about what it was like when I filed, how I chose them and how

pleased I was with the work we did. We were the only state in the country to break the joint defense privilege which was crucial. We talked about that.

REPRESENTATIVE WAGLE: Is there a document of this conversation between you and the arbitration panel? Is it documented anywhere?

GENERAL STOVALL: I don't know if they did a transcript or not.

REPRESENTATIVE WAGLE: I was wondering if there was anyway for you to look at it, if there is anyway to provide to the committee whatever your testimony was to the arbitration panel. Would that be possible?

GENERAL STOVALL: I can sure call them and see. I wasn't there. I don't know if they had a court reporter or not. They might have.

REPRESENTATIVE WAGLE: Could you have stated to this panel that on page 6 it says Entz and Chanay, they were a small -- they were a small four to five person law firm selected by the Kansas AG Stovall after

several Kansas counsel refused to take the case.

GENERAL STOVALL: Well, I -- I don't remember what I said. I don't know if I would have explained how we came to them, that Hutton and Hutton didn't want it for the contract terms. I don't know if I talked about Morrison and Hecker not wanting it because of the financial arrangements and their later conflict of interest, and I don't remember if I talked about Don Barry not wanting it because of the expenses be fronted. I don't remember that.

REPRESENTATIVE WAGLE: So you don't know if you stated to this panel that several Kansas counsel refused to take the case.

GENERAL STOVALL: I don't know. That's exactly right.

REPRESENTATIVE WAGLE: I think it's very important that the committee is able to look at those documents.

GENERAL STOVALL: Why?

REPRESENTATIVE WAGLE: I think it's very important. This was a decision --

okay. We are the client. We are the State of Kansas. You were representing the State of Kansas --

GENERAL STOVALL: Those law firms were --

REPRESENTATIVE WAGLE: -- and securing a law firm on behalf of the State of Kansas to represent Kansas in the matters, and I believe that that testimony is very important.

GENERAL STOVALL: I'd be happy to make it available. I will call and see if there is a transcript available. You sound like maybe you know there is one. Maybe you could make the request as well. Do you know if there is one? It looks like you do.

REPRESENTATIVE WAGLE: I honestly don't know if there is one. I'm very concerned here the Kansas Attorney General Stovall says after several Kansas counsel refused to take the case. We are not seeing that that is the case.

GENERAL STOVALL: What do you recall Morrison and Hecker? Did they refuse to take the case?

REPRESENTATIVE WAGLE: It appeared they did.

GENERAL STOVALL: Did Don Barry refuse take the case?

REPRESENTATIVE WAGLE: It's my understanding he refused.

GENERAL STOVALL: That's two. Hutton and Hutton wouldn't take it for the contract terms we insisted upon.

REPRESENTATIVE WAGLE: Okay. That's your statement today.

GENERAL STOVALL: That's exactly my statement today. It was yesterday, and it has been every day.

REPRESENTATIVE WAGLE: Thank you. Representative Johnston and then Representative Campbell.

REPRESENTATIVE JOHNSTON: Thank you, Madam Chair. First-- I've got two things. First, I want to ask you one of those whispering questions that goes around the capital that nobody has asked.

GENERAL STOVALL: There aren't any whispering questions in this place.

REPRESENTATIVE JOHNSTON: Lots of

them. It's very simple. Why did you choose to contract out for these legal services rather than doing the services in-house like, say, Colorado did?

GENERAL STOVALL: We talked about that yesterday. When Colorado signed on, they would have sued on June the 5th of 1997. That was June the 23rd-- just two weeks probably, three weeks before the June 23rd settlement was announced. Everybody knew at that point there was going to be a settlement. You may remember all the media hype about the settlement. Secret negotiations, and they weren't. Colorado sued banking on the fact there would be settlement, and Gail Norton, the Colorado attorney general, gambled she would never have to try that lawsuit. The first 20 states that sued contracted out of house to do it because as I indicated yesterday, nobody could manage it in-house. I was pretty comfortable in believing that the $7,000,000 we estimated it would take over three years would not be forthcoming from the legislature. And if I wanted to sue

tobacco, this was the only way to make it happen.

REPRESENTATIVE JOHNSTON: I appreciate your response to that. I think it's important that you are fully heard on that question. The second thing I guess I want to say, and since I didn't read anything about this in the newspaper this morning, again, I want to state that the whole reason, I'm not sure what the purpose of this hearing is, but what I have learned from it is that this whole situation is a stellar example of why we should require a process for competitive bidding in professional contracts. That having been said, I do not believe that you've done anything illegal, but I have to admit to you, General Stovall, that I was very disappointed when I read on page 10 of your testimony yesterday that you ruled out hundreds of attorneys and presumably law firms just because they weren't registered Republicans. That is appalling to me. I'd like you to respond to that.

GENERAL STOVALL: Thank you. We

didn't rule out them. We considered everybody who came to us. Hutton and Hutton -- I don't know what their political affiliation is. They are trial attorneys. The stereotype is that makes them Democrats. I don't know. Morrison and Hecker, there is so many lawyers, Bob Vancrum I happen to know is a Republican. A member of this body. He was in the legislature. It didn't mean every firm with Democrats in the state I wouldn't have talked to if they had come in. But a concern was how this lawsuit was viewed statewide. I took-- as I shared with you in the book yesterday we put together, that after the decision to file the many, many, many editorials that were very, very critical of my decision to file the lawsuit, people believing that tobacco was a lawful product which it is, that the state should not be suing, so for me to go with the traditional plaintiff's lawyers, trial lawyers would be furthering that, giving more fuel to people that I expected to be critical of the lawsuit decision, and that very much was part of my decision. And

every year, every few years the legislature has a bill to require some other kind of legislative process to go through attorneys, we will comply with it with whatever law it is that you pass. We ask for flexibility only because when we are sued, we have to respond within 20 days. It needs to be fast. But we'll do whatever it is that you tell us to do.

REPRESENTATIVE JOHNSTON: And I appreciated that. I appreciate your response. As I said yesterday, it's the fault of the legislature that we haven't done that, but, you know, the testimony yesterday still gave me serious pause. The next question was I had a representative mention to me yesterday that your office during the budget process and the appropriations process had been asked last year and may have even been in the budget as a line item to develop the process for making these decisions for, you know, establishing, I guess, a regulatory process or process of rules by which you hire outside counsel. Has that happened?

GENERAL STOVALL: Guidelines. Yes. That was distributed. It's this. It's the July 1, 1997 guidelines for hiring counsel. In addition to that, what post audit talked about was we have an accounting firm, a specialty accounting firm I think in California called Examine. They look at all the bills of counsel that we contract with to go through them to be sure they are reasonable, they are accurate. That's on the contracts that are the standard. This one clearly was not a standard contract. We don't engage in this kind of litigation on a regular basis. That's in place as well.

REPRESENTATIVE JOHNSTON: Thank you very much. Thank you, Madam Chairman.

REPRESENTATIVE WAGLE: Representative Campbell.

REPRESENTATIVE CAMPBELL: Forgive me, the arbitration panel, was it part of their process you would interface with them, or did you make the overture to call in to them?

GENERAL STOVALL: They very much expected attorneys general to participate in

that process. My understanding is most did it in person with the exception of Attorney General Jim Ryan of Illinois. It was their feeling if the person who did the contracting, the person responsible for the litigation could talk about how it went, that helped them decide, helped them look at evaluating the whole case.

REPRESENTATIVE CAMPBELL: An invited process and standard, normal with what they were doing?

GENERAL STOVALL: Yes, sir.

REPRESENTATIVE CAMPBELL: Thank you.

REPRESENTATIVE WAGLE: Are there further questions of the committee? Representative Gregory.

REPRESENTATIVE GREGORY: Thank you. As contingency fees go, what is the largest ever awarded within the state?

GENERAL STOVALL: The percent or the amount?

REPRESENTATIVE GREGORY: The amount.

GENERAL STOVALL: To my knowledge,

the percent certainly is not. The settlement totally was the largest settlement in the history of the world. So I would guess -- I know bringing in a billion six for the state is the largest settlement. Whether or not 27 million is the biggest fee. John has been with the office 20 some years and has a better history than I do.

MR. CAMPBELL: The biggest one in Kansas paid so far was 12,000,000 to Frieden when he did the military thing. KPERS, I don't think this has been paid yet.

GENERAL STOVALL: 30 to 40 percent.

MR. CAMPBELL: It's 40 percent. I think it's about 18 million. I think this is the biggest one, but I don't really know.

GENERAL STOVALL: The percent is by far tiny compared to those other percent. KPERS right now is paying 40 percent for its attorney fees. I think we've recouped about 60 million. 30 to 40 percent is going out in fees. That's not what I wanted to see happen here.

REPRESENTATIVE WAGLE: Further questions? Representative Gatewood.

REPRESENTATIVE GATEWOOD: Madam Chairman, will these other attorney fees be affected by this tax bill?

REPRESENTATIVE WAGLE: What other attorney fees?

REPRESENTATIVE GATEWOOD: Such as the KPERS fund? Will these other attorneys --

REPRESENTATIVE WAGLE: We're going to focus on the bill tomorrow if that's okay and answer the questions and try and get staff --

REPRESENTATIVE GATEWOOD: Will they be affected?

REPRESENTATIVE WAGLE: I really don't know.

GENERAL STOVALL: That might be interesting to the lawyers that represent KPERS and lots of other lawyers in the state. I would offer if you're going to do it --

REPRESENTATIVE WAGLE: We'll get into the details of the bill tomorrow. It's

not open for discussion. My plans are Representative Powell will appear before the committee tomorrow to discuss the bill specifically and what it does and what impact it has and on who the impact-- you know, who is impacted. Representative Tomlinson.

REPRESENTATIVE TOMLINSON: Comment first. My mother always wanted me to be a lawyer.

GENERAL STOVALL: I bet she's happy, isn't she, Representative?

REPRESENTATIVE TOMLINSON: If she's not, I am. I'm sure you said this yesterday. I was.

GENERAL STOVALL: We missed you.

REPRESENTATIVE TOMLINSON: I'm in graduate school.

GENERAL STOVALL: I am sorry for that.

REPRESENTATIVE TOMLINSON: Believe me, it's much better than this. My question is, the settlement amount the arbitrator set for Kansas is within -- it's within -- well, education would say within

one standard deviation. It is close to the other figures or the other percentages that were set for other states.

GENERAL STOVALL: At this point in time, it is the second smallest award that's been made. Illinois counsel's received 1.29 percent. That is after their attorney general did not show up. Then there was a 4.4 percent for Iowa. 12.37 percent for Louisiana, 6.52 percent for Hawaii. The other four states, Mississippi, Florida, Texas, Massachusetts -- Massachusetts got 9 percent. The other three states were tremendously large, 34 percent, 26 percent and 19 percent. They were the first three that settled. I think the vast criticism from those attorney fees made the panels think maybe we overdid on those. Everything since those is much, much less.

REPRESENTATIVE TOMLINSON: It has something to do with the order of the entrance in the suit?

GENERAL STOVALL: And level of risk.

REPRESENTATIVE TOMLINSON: And level of risk. Since we were 11, there was some significant risk and so on and so on. Does it have anything to do with what-- has some to do with your testimony in Pasadena, from Pasadena as well you would think. We would hope you had some influence.

GENERAL STOVALL: I don't know that they weighed factors. I don't know how much impact that had. Had I not participated, that might have been negative than my testifying did have positive.

REPRESENTATIVE TOMLINSON: They solicited information from the firm themselves in terms of the work?

GENERAL STOVALL: The three law firms my understanding were present as well as the tobacco lawyers.

REPRESENTATIVE TOMLINSON: The tobacco lawyers had the opportunity to present and argue their point in terms of how much work.

GENERAL STOVALL: It was quite an adversarial process, I understand.

REPRESENTATIVE TOMLINSON: Okay.

Thank you.

REPRESENTATIVE WAGLE: Representative Ray.

REPRESENTATIVE RAY: Thank you. If the Kansas law firm would have received half of what they did, what would have happened to the other money, the 13 million?

GENERAL STOVALL: I'm sorry, say that again?

REPRESENTATIVE RAY: If they would have awarded our law firm half of the percentage, one-half of a percent.

GENERAL STOVALL: Of 54 million -- 54 million is what all the Kansas three law firms get.

REPRESENTATIVE RAY: I'm trying to find out if we didn't bring it in paying this law firm from this arbitration fund, where does it go.

GENERAL STOVALL: No, we wouldn't get anything else. If they had awarded less -- if they awarded anything less than they did, the state doesn't get anymore money. The law firms would get whatever they awarded, and this big pot of lawyer money

that big tobacco committed to pay would just have that money.

REPRESENTATIVE RAY: The tobacco company.

GENERAL STOVALL: Right.

REPRESENTATIVE RAY: So any lesser is a savings for the tobacco company.

GENERAL STOVALL: Absolutely. Big tobacco is paying all this. The strategic contribution fund set up by this agreement that awards states based on what they did decided for Kansas $159,000,000, that comes from 2008 and 2017 in terms of when it's paid to the State of Kansas over the period of time. I think it's wonderful recognition of the role we played in it. Again, I'm proud the role Kansas did in this litigation and being No. 11 and not waiting until the handwriting was on the wall. That's not my style.

REPRESENTATIVE WAGLE: Further questions? General Stovall, I think it would be real important for us to have copies of the documents that you gave and maybe tobacco gave to the arbitration panel.

GENERAL STOVALL: I gave nothing to the tobacco panel.

REPRESENTATIVE WAGLE: You didn't speak with them over the phone? You did speak with them? You did have notes?

GENERAL STOVALL: Right.

REPRESENTATIVE WAGLE: If there was a recording, I'd like a reporting.

GENERAL STOVALL: I would ask if there was.

REPRESENTATIVE WAGLE: It does say, clarify, national counsel provided most of the personnel power and resources for the Kansas case.

GENERAL STOVALL: When I looked at that, I highlighted it. That is not at all what happened. I questioned counsel about that, and I personally know Joe Rice. He's with the Ness Motley firm. What in the heck are you talking about? It was not an accurate statement at all of what happened, and anybody who looks at that who was at the conference will say it was a misstatement. Joe Rice could not under oath say that, and he would have been misquoted.

REPRESENTATIVE WAGLE: Maybe it's very important this committee sees those documents if there are documents that may exist.

GENERAL STOVALL: I'll make the phone call when I get back to the office and see.

REPRESENTATIVE WAGLE: Is there one more question? Representative Vickery.

REPRESENTATIVE VICKERY: At the point of this arbitration, does this affect what the State of Kansas would receive at all?

GENERAL STOVALL: Absolutely not.

REPRESENTATIVE VICKERY: So this is just what their fees will be.

GENERAL STOVALL: That's right. Had they not chosen to go the arbitration route, their fees would be subtracted out of the Kansas settlement, and we would be writing a check to the firms. The way the arbitration was set up, the state wouldn't have any expense for the litigation and tobacco pays for all of it. States filed very, very late in the game, and they did

not hire outside counsel. Those states are getting the same allocations that were set out on the chart on November the 23rd of 1998 as we are getting. The states that aren't paying lawyers or didn't have lawyers that tobacco has to pay, they are not getting any incentive, any boost, any subsidy, nothing as compared to those that got in early and the companies are having to pay attorney fees for those states. We are suffering not a dime for this. In fact, it's a huge benefit that we are not paying attorney fees.

REPRESENTATIVE WAGLE: Okay. Committee, you have a ton of information to digest. We're going to adjourn. Tomorrow we will look into the specifics of the bill that Representative Powell has proposed. Thank you.

GENERAL STOVALL: Thank you for courtesies committee members.

C E R T I F I C A T E

STATE OF KANSAS

ss.

COUNTY OF SHAWNEE

I, Sandra S. Biggs, a Certified Shorthand Reporter, commissioned as such by the Supreme Court of the State of Kansas, and authorized to take depositions and administer oaths within said State pursuant to K.S.A. 60-228, certify that the foregoing was reported by stenographic means, which matter was held on the date, and the time and place set out on the title page hereof and that the foregoing constitutes a true and accurate transcript of the same.

I further certify that I am not related to any of the parties, nor am I an employee of or related to any of the attorneys representing the parties, and I have no financial interest in the outcome of this matter.

Given under my hand and seal this 22nd day of February, 2000.

Sandra S. Biggs, C.S.R.

COSTS: _____

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