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Tobacco-Settlement: Liggett

MEMORANDUM

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Washington, D.C. 20004-2601
Ph: 202-434-8246; Fx: 202-393-7864

Date/Day: August 27, 1997/Wednesday

To: Paul Weinstein

From: Michael B. Levy

Subject: Various Liggett Documents

Fax: 456-7028

Pages 14

202/434-8375
FAX 202/393-7864

MICHAEL B. LEVY
LEGISLATIVE CONSULTANT

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GEORGETOWN UNIVERSITY

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STATE ATTORNEYS GENERAL
A Communication From the Chief Legal Officers
Of the Following States

August 19, 1997

*via facsimile (202) 456-2983
and U.S. Mail*

Mr. Bruce Lindsey, Deputy Counsel to the President
The White House
1600 Pennsylvania Avenue
Second Floor, West Wing
Washington, D.C. 20502

Re: Attorney General Tobacco Litigation

Dear Bruce:

We are writing with respect to the proposed tobacco resolution.

On March 21, 1997,¹ twenty-one of the Attorneys General signed a settlement agreement with Brooke Group, Ltd., Liggett & Myers and the Liggett Group (collectively referred to as "Liggett").

The linchpin of the agreement was (1) an admission by Liggett that smoking causes health problems, including lung cancer, heart and vascular disease and emphysema, (2) an admission that nicotine is addictive, and (3) an acknowledgment that the industry has targeted children. No tobacco company had publicly admitted any of these important points and all were vigorously contesting each of these facts in litigation and in all other public statements. Indeed, these facts have been bitterly contested by the industry for over forty years. Since the settlement, Liggett's CEO, Bennet LeBow, has testified that nicotine is addictive and that smoking causes cancer and other diseases. All of these statements are unprecedented coming from a member of the tobacco industry.

¹ Subsequently, certain other states also settled with Liggett.

Mr. Bruce Lindsey
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Moreover, since entering into its settlements, Liggett has taken numerous significant actions which have demonstrated its utmost good faith in breaking with past tobacco industry conduct. Those actions involve not only cooperating with the Attorneys General and others in lawsuits against the other tobacco companies, but also assisting public health groups and governmental entities in seeking to resolve smoking and health issues. These actions go well beyond the letter of Liggett's settlement agreements. For example:

- On June 12, 1997, Bennett LeBow testified before the Massachusetts Department of Public Health in favor of a Massachusetts' state law that would compel the tobacco companies to disclose the ingredients in cigarettes on packaging. The other tobacco companies strongly oppose this legislation.
- On July 21, 1997, Bennett LeBow testified, as a plaintiffs' witness in the flight attendants' class action against the tobacco industry in Florida (a case that Liggett has not settled), that smoking causes various diseases and that smoking is addictive. No tobacco company executive had ever testified to these important points. In fact, the tobacco companies continue to contest these facts in pending litigation and elsewhere, notwithstanding their promises in the proposed global resolution.
- Liggett has filed tobacco industry joint-defense privileged documents with various courts around the country, along with memoranda explaining why Liggett believes these select documents should be produced to the Attorneys General over the privilege claims of the other tobacco companies. Certain of these important documents have just been made public in the State of Florida's lawsuit.
- Liggett conducted for the benefit of the Attorneys General and their outside counsel a tour of Liggett's manufacturing plant along with an informative discussion concerning the process of manufacturing cigarettes, and has scheduled the same for representatives from the United States Department of Health and Human Services.
- Liggett has made various currently-employed scientists and researchers available for informational interviews conducted by the Attorneys General and their outside counsel.
- Liggett is working with FDA officials and public health and tobacco experts (including Dr. David Burns) on various critical smoking and health issues and on developing means for their long-term resolution.

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Liggett has assisted, and continues to assist, the Federal Trade Commission, the Department of Justice, Congressional staff members, State agencies and officials and others in their various investigations of the tobacco industry.

Liggett is therefore fulfilling its agreement to turn State's evidence, which includes waiving the attorney-client privilege and providing witnesses to the states.

Liggett's undertakings were significant and are believed by many of us to have been a factor in the willingness of the industry to discuss resolution.

Under the settlement agreement with the Attorneys General, Liggett is required to pay to the settling states as follows:

6.3 Subject to the terms of this Agreement, Liggett shall make the following payments:

6.3.1. An initial payment of \$25 million due 120 days from the date of a Future Affiliate Transaction; and

6.3.2. Subject to the provisions of Sections 6.6 - 6.12, payments, each equivalent to 25% of Liggett's Pretax Income, due 120 days after the end of each fiscal year of Liggett. The first payment shall be made with respect to the first full fiscal year commencing after the date of this Settlement Agreement.

6.4 Liggett shall pay the reasonable and necessary expenses of the administration, allocation, and distribution of the Settlement Fund; provided that Liggett shall not be obligated to pay more than \$1 million in any year for such expenses.

6.5 Since the Settling Defendants are providing historic and valuable cooperation and other considerations under this Agreement and the Mandatory Class Agreement, the amounts payable hereunder to the Settlement Fund shall represent the maximum amounts payable to the Settlement fund under this Agreement and the Mandatory Class Agreement.

In recognition of the valuable contribution of Liggett Section 5.1 of the settlement Agreement provides:

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5.1 Effective upon the execution hereof, the Attorneys General and their respective counsel, each agree (a) to exercise best efforts to ensure that the financial terms, financial obligations or financial conditions of any Global Settlement are no more onerous on, or less favorable to, Brooke Group and Liggett than the financial terms, financial obligations or financial conditions of this Settlement Agreement, and (b) to issue a public statement substantially in the following form and substance:

The historic settlements entered into by Liggett, whereby Liggett has agreed, among other things, to provide full cooperation to twenty-three Attorneys General and to consent to FDA regulation of tobacco marketing, are a major advance in our efforts to prevent smoking by children and adolescents and to ensure that the tobacco industry markets its products lawfully. Accordingly, the undersigned Attorneys General will use their best efforts in Congress and elsewhere to ensure that any such industry-wide resolution provide for financial terms for Liggett that reflect appropriate recognition of Liggett's cooperative efforts.

The terms of the proposed industry wide resolution requires Liggett to make payments far in excess of those required by the Attorneys' General settlement. The Attorneys General who settled with Liggett believe that Liggett deserves special consideration with respect to the financial terms of the proposed resolution. Because of Liggett's valuable role and its willingness to turn State's evidence and with Liggett's permission, we suggest that Liggett's financial obligations be as follows:

Liggett shall have no obligation with respect to the \$10 billion up front payment.

Liggett shall be excused from any of the required per year payments to the extent that its market share is not more than 3%.

To the extent that Liggett's shares ever exceeds 3%, it shall be required to pay its share of the annual payments required by any legislation on the amount over 3%.²


² Liggett has agreed that it will match any mandatory price increase imposed on tobacco companies as part of the legislation. Thus, Liggett would maintain its historic price difference and would not be able to take advantage of other companies as a result of its different financial obligations.


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We were unable to get the industry to agree to this proposal, but feel strongly that Liggett deserves special consideration for turning State's evidence and for making the historic admissions Liggett has made.

We would be glad to discuss this with you further and request the opportunity to do so.

Sincerely,


Grant Woods
Attorney General of Arizona


Daniel E. Lichtig
Attorney General of California


Richard Blumenthal
Attorney General of Connecticut



Robert A. Butterworth
Attorney General of Florida


Margery S. Bronster
Attorney General of Hawaii


Jim Ryan
Attorney General of Illinois


Jeffrey A. Modisett
Attorney General of Indiana


Tom Miller
Attorney General of Iowa

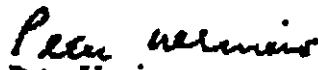

Carla J. Stovall
Attorney General of Kansas

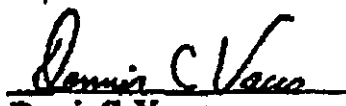

P. Joseph Curran, Jr.
Attorney General of Maryland


Scott Harshbarger
Attorney General of Massachusetts

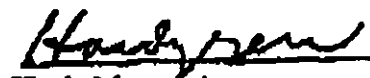

Mike Moore
Attorney General of Mississippi

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Peter Verniero
Attorney General of New Jersey



Dennis C. Vacco
Attorney General of New York



Drew Edmondson
Attorney General of Oklahoma


Hardy Myers
Attorney General of Oregon


Dan Morales
Attorney General of Texas


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Transcript

DATE August 20, 1997
TIME 5:00-6:00 PM (ET)
NETWORK FNC
PROGRAM The Cavuto Business Report

Karen Gibbs, anchor:

In our Business And The Beltway segment, should Liggett be left out of the tobacco settlement? Twenty of the nation's Attorneys General asking President Clinton today to protect the Liggett Group from the financial penalties included in the proposed three hundred and sixty-eight billion dollar tobacco settlement. Liggett the maker of cigarette brands like Lark, Chesterfield and L&M, says the conditions of the deal would virtually bankrupt the company. Liggett chaired by Florida businessman Bennett LeBow broke ranks with the tobacco industry to forge it's own settlement in March of 1996. The Attorneys General say this cooperation should exclude Liggett from paying the ten billion dollar penalty called for in the tobacco agreement.

Joining us now to discuss this issue is Connecticut Attorney General Richard Blumenthal. Mr. Blumenthal thank you very much for joining us...

Richard Blumenthal (Attorney General, Connecticut): Thank you.

Gibbs: Why do you think Liggett should be excluded from this tobacco deal?

Blumenthal: We are asking the President to recognize two facts about Liggett. First of all its market share is really relatively small, less than two percent of the total United States sales. And second, it has turned state's evidence. It provided critical cooperation by admitting that nicotine is addictive, that its products and all tobacco products cause cancer and other deadly diseases. And by testifying actively in court, not only in the Florida case involving stewardesses who are claiming damages from second hand smoke, but in other proceedings around the country, furnishing very, very important documents that are really of explosive impact in many of these litigations.

And we think that kind of action on its part, coming clean with the American people really merits this kind of

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Page: 2

recognition. Not in granting it total exemption because we are asking that that kind of recognition be accorded in financial terms, but that penalty be somewhat lessened.

Gibbs: What about the financial agreement Liggett struck with the Attorneys General in March of '96, twenty-five million dollar fine and then twenty-five percent of pre-tax profits for the next twenty-five years? Some say that Liggett can't even make that.

Blumenthal: I think Liggett will be able to provide for twenty-five percent of its pre-tax profits because after all at some point it will be hopefully more profitable than it is now. Even with the limited market share that it has, I don't think that agreement will bankrupt the company by any means. And Liggett did agree to it. We are asking simply that it be held harmless in effect, for cooperating with the states and with the United States in providing this critical documentary and other evidence in support of our contention that tobacco kills people, that it's addictive, that the tobacco companies have targeted children. That kind of very important cooperation ought to be recognized.

Gibbs: Well why shouldn't they just go bankrupt or out of business?

Blumenthal: Well if they are permitted to go bankrupt or out of business, first of all their cooperation will be imperilled. Their cooperation may not only be important but necessary if the overall global settlement doesn't come through, because we in Connecticut and elsewhere around the country are pursuing our law suits against the industry. Second its market share won't simply disappear, it will be absorbed by other companies. Those people who are addicted to the Liggett products will simply switch to other products and we won't solve the problem simply by permitting or forcing Liggett to go bankrupt.

Gibbs: President Clinton wants to tack on another fifty billion dollars in fines to make up for a tax break in the most recent budget deal. Will that kill this tobacco agreement?

Blumenthal: Definitely not because the fifty billion dollar tax break which the tobacco companies succeeded in achieving, literally at the dead of night in the last moments before congress passed the bill, is in fact a breach of the agreement and we have so written to the industry telling them that they have breached the agreement.

Gibbs: All right Mr. Blumenthal, thank you very much for joining us.

Blumenthal: Thank you.



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Transcript

DATE
TIME
NETWORK
PROGRAM

August 20, 1997
7:00-7:30 PM (ET)
CNN
Moneyline

Jan Hopkins, anchor:

A group of Attorneys General urging the White House to protect Bennett LeBow's Liggett Group from financial penalties in the proposed tobacco settlement. LeBow was instrumental in initiating tobacco talks by becoming the first cigarette executive to admit tobacco is addictive.

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Transcript

DATE
TIME
NETWORK
PROGRAM

August 20, 1997
10:00-11:00 PM (ET)
CNN
The World Today

Leon Harris, co-anchor:

Attorneys General from twenty states want the White House to go a little easier on the Liggett Group, that's the smallest of the tobacco companies involved in that three hundred and eighty-six billion dollar settlement we heard so much about earlier this year. President Clinton reviewed that deal and wants the tobacco companies to pay even more money. The Attorneys General say Liggett deserves a break because unlike the other tobacco companies it was cooperative.

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Transcript

DATE August 20, 1997
TIME 6:30-7:00 PM (ET)
NETWORK PBS
PROGRAM The Nightly Business Report

PAUL Kangas, co-anchor:

Twenty state Attorneys General want the White House to give Liggett Group special consideration in the proposed tobacco settlement. Liggett was the first of the nation's tobacco companies to settle litigation with the states. The Attorneys General say Liggett should not have to pay any money up front and should be excused from making annual payments as long as its market share remains below three percent. Shares of Liggett's parent Brooke Group stock were unchanged at 3 7/16 today.

* * *

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PHILADELPHIA INQUIRER — August 22, 1997

EDITORIALS

Witness protection

Whistle-blowing tobacco company deserves a break.

It was a health breakthrough when the struggling maker of Loraks, L&M's and Chesterfields switched to a new strategy: telling the truth about cigarettes.

In a deal that limited its financial damages, the Liggett Group admitted that its cigarettes are addictive, that they cause cancer and heart disease, and that the industry tries to get teenagers hooked. The company also provided state courts with damning internal documents.

Liggett's whistle-blowing — which began last year and expanded last March — scared the larger tobacco companies toward a more expensive settlement in June. "It was the beginning of the end of this conspiracy of lies," said Arizona Attorney General Grant Woods. His counterpart from Mississippi, Mike Moore, called Liggett's paper trail "the most incriminating documents in the history of tobacco litigation."

That's why 20 state attorneys general, including New Jersey's Peter Verniero, this week wrote to the White House that the industry-wide deal is unfair to this tale's belated

good guy, Liggett. They urged "special consideration" for the company in light of its "valuable role." Amen.

The company says that being included in the industry-wide settlement would cost it billions more than its earlier deal to pay 25 percent of pre-tax profits for 25 years, which cemented its decision to come clean. And that, Liggett says, could drive it out of business.

It would be a grotesque irony if the deal that grew out of Liggett's decision to crack the industry's wall of denial ended up bankrupting the company.

As the attorneys general noted in their letter, the company's whistle-blowing CEO, Bennett LaBow, has gone beyond that deal and become a crusader against his industry's morbidity, smoke and mirrors. He also has echoed the public-health leaders' criticism of the industry-wide deal's weakening of federal regulatory power.

For breaking ranks with Big Tobacco — an act in which his company's interests and the public's were aligned — Mr. LaBow has earned Liggett special treatment.

DJN 11:26 White House Noncommittal On Liggett's Tobacco Exemption

WASHINGTON (Dow Jones)--The Clinton administration was noncommittal towards a proposal by 20 state attorneys general that cigarette-maker Liggett Group Inc. be exempted from the payments envisioned under the tobacco deal.

Twenty attorneys general have signed a letter saying Liggett should be exempted from the \$368 billion in payments on the grounds that Liggett broke ranks with the other major tobacco companies and gave the states the information they needed to wring a deal from the industry.

'We are aware of the letter. That is one of the issues being reviewed by the Reed-Shalala group,' said deputy White House spokesman Barry Toiv, who is accompanying President Clinton on his vacation to Martha's Vineyard.

Domestic Policy Adviser Bruce Reed and Health and Human Services Secretary Donna Shalala are in charge of the White House review of the tobacco settlement negotiated between state attorneys general and the tobacco industry.

White House officials have repeatedly made the point that while the deal negotiated by the state attorneys general is a good starting point, the Clinton administration will make whatever changes it thinks are needed.

Along these lines, Toiv reiterated that the financial terms of the deal are sure to change because of a tax credit the GOP gave to the tobacco industry in the budget deal. The GOP made certain the tobacco industry will be able to offset the new \$0.15 cent a pack tobacco tax against the payments it will make under the tobacco deal.

'The settlement costs have not been established. Nothing has been established until it has all been settled legislatively,' Toiv said. 'But we are going to make sure the costs to the industry are not actually reduced,' he added.

In the past, Reed has said the easiest way to offset the tax credit would be to raise the settlement price by \$50 billion, the expected value of the tax credit.

However, some of Toiv's comments indicated the Clinton administration never intended to allow the tobacco tax credit to benefit the industry even while it was agreeing to do so with the GOP budget negotiators.

'Our negotiators accepted this (tax credit) with the knowledge that it could be dealt with in the future,' Toiv said.

(END) DOW JONES NEWS 08-21-97

11:26 AM

0- 11 26 AM EDT 08-21-

Tob - reT - Liggett

Memo To: Bruce Reed
Elana Kagan
Cynthia Rice
Josh Gotbaum

From: Jon Gruber

Re: Liggett - see attached Jeremy Bulow editorial

Politics is politics, but can't we do something about this? Bulow's suggestion, which strikes me as reasonable on policy grounds, is to simply credit Liggett for their payments to states, and charge them the difference between their share of the national settlement and those state payments. An alternative, to reward their lead role, would be to do something like reward them for 2 times their state payments. But in any case it would be a much smaller loophole.

This might be a bargaining chip to give away as well if we are trying to get industry back on board.

Wall Street Journal, May 13, 1998

A Sweet Deal for a Tobacco Executive

By JEREMY BULOW

Which single person stands to benefit the most from passage of the Senate Commerce Committee's recently approved tobacco legislation? Surprisingly, the answer is not a trial lawyer, though it is a man who's spent plenty of time in court—bankruptcy court, to be exact. Bennett LeBow, controlling shareholder of the Brooke Group Ltd., personally stands to "earn" hundreds of millions of dollars a year if the bill becomes law.

Brooke owns Liggett, which makes L&M, Lark and Chesterfield cigarettes. As this newspaper reported in 1993, Mr. LeBow pulled tens of millions of dollars out of the company and used it to finance a lavish lifestyle, pushing Liggett to the brink of bankruptcy. Under Mr. LeBow's leadership, Liggett's market share has fallen to 1.3% from 8%.

But this time Mr. LeBow has come up with a new way to get money: have Congress give it to him. Under the Commerce Committee's bill, tobacco companies are to pay higher taxes on the sale of cigarettes, increasing to 65 cents a pack in 1999 and \$1.10 a pack beginning in 2003. But Liggett has been made exempt from this tax, so long as it keeps its market share below 3%. Liggett argues that it deserves the break

for turning over secret industry documents to the state attorneys general whose lawsuits against tobacco companies spurred the current legislation.

How much is this exemption worth? Even with the tax increase, the Treasury predicts cigarette sales of slightly over 20 billion packs a year. So if Liggett kept production down to 600 million packs (it sold 322 million last year), it would enjoy a \$1.10 per pack, or \$660 million, cost advantage over its competitors. To keep this in perspective, note that cigarette manufacturing costs are about 20 cents per pack.

If Liggett only adds a dollar to its price when all other manufacturers will be forced to raise prices by \$1.10, Liggett should easily be able to get its 3% share. And the dollar a pack would fall directly to the bottom line, increasing Liggett's pretax profits by \$600 million per year. Liggett has agreed to pay 27% of its future profits in settlement of its health care litigation with the states, and Mr. LeBow owns 51.5% of Brooke, so his share of the bounty will come to \$225 million per year. The state attorneys general, who must not have understood the implications of this provision, agreed to lobby for the Liggett exemption as part of their latest deal with the company, announced March 12.

Perhaps because of the possibility of such a bonanza, Brooke's stock-market value has risen from a low of \$37 million (\$2 a share) a year ago to roughly \$200 million today, despite the company's precipitous operating decline. If Congress comes

to its senses, the deeply indebted company will be worth nothing. But if the bill passes as is, Brooke would be worth at least five times its current price.



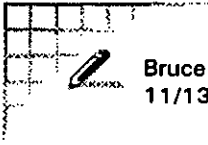
Bennett LeBow

Side by side with the Liggett provision is another, potentially more destructive proposal, encouraging the 100 or so small cigarette manufacturers and importers in the country to increase production. While they are not given as juicy a deal as Liggett, they only have to pay 25% of the \$1.10 on the first 150 million packs they sell and 50% on the next 150 million. So a small manufacturer, currently selling just a few million packs, will be able to crank up production and sell up to 150 million packs for 80 cents a pack less than any of the majors can charge for generic cigarettes.

These firms currently sell only one out of every 1,000 cigarettes in the U.S., but I predict they (and some new entrants) will soon be selling billions of packs per year if the new law is passed, flooding the market with cheaper cigarettes while destroying the businesses of the major companies. As a business school professor, my advice for aspiring young entrepreneurs will be: Start a small cigarette company.

Mr. Bulow is a professor of economics at Stanford Business School.

Tobacco - statement -
Liggett



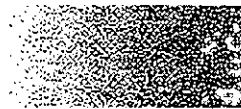
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To: Elena Kagan/OPD/EOP
cc:
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you'll enjoy this...

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To: Bruce N. Reed/OPD/EOP
cc:
Subject: tobacco factoid of the day

I know you have been staying up nights worrying about Liggett's fate. The President has received a letter from concerned AGs. The following fact should then be an enormous relief to you. On 9/17 I invested an imaginary \$1,000 in PM, RJR, Loew's, BAT, Brooke, and UST. As of today, I still have roughly \$1,000 in each company except Brooke, Liggett's parent. At close today, the Brooke stock is worth \$1,870 or roughly a 90% return in less than 2 months. Do you think I should ask Treasury for analysis of why this happened?

cc: Bruce R

Tobacco - settlement - Liggett

STATE ATTORNEYS GENERAL
A Communication From the Chief Legal Officers
Of the Following States

August 19, 1997

via facsimile (202) 456-2983
and U.S. Mail

Mr. Bruce Lindsey, Deputy Counsel to the President
The White House
1600 Pennsylvania Avenue
Second Floor, West Wing
Washington, D.C. 20502

Re: Attorney General Tobacco Litigation

Dear Bruce:

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Mr. Bruce Lindsey
August 19, 1997
Page 2

Moreover, since entering into its settlements, Liggett has taken numerous significant actions which have demonstrated its utmost good faith in breaking with past tobacco industry conduct. Those actions involve not only cooperating with the Attorneys General and others in lawsuits against the other tobacco companies, but also assisting public health groups and governmental entities in seeking to resolve smoking and health issues. These actions go well beyond the letter of Liggett's settlement agreements. For example:

- On June 12, 1997, Bennett LeBow testified before the Massachusetts Department of Public Health in favor of a Massachusetts' state law that would compel the tobacco companies to disclose the ingredients in cigarettes on packaging. The other tobacco companies strongly oppose this legislation.
- On July 21, 1997, Bennett LeBow testified, as a plaintiffs' witness in the flight attendants' class action against the tobacco industry in Florida (a case that Liggett has not settled), that smoking causes various diseases and that smoking is addictive. No tobacco company executive had ever testified to these important points. In fact, the tobacco companies continue to contest these facts in pending litigation and elsewhere, notwithstanding their promises in the proposed global resolution.
- Liggett has filed tobacco industry joint-defense privileged documents with various courts around the country, along with memoranda explaining why Liggett believes these select documents should be produced to the Attorneys General over the privilege claims of the other tobacco companies. Certain of these important documents have just been made public in the State of Florida's lawsuit.
- Liggett conducted for the benefit of the Attorneys General and their outside counsel a tour of Liggett's manufacturing plant along with an informative discussion concerning the process of manufacturing cigarettes, and has scheduled the same for representatives from the United States Department of Health and Human Services.
- Liggett has made various currently-employed scientists and researchers available for informational interviews conducted by the Attorneys General and their outside counsel.
- Liggett is working with FDA officials and public health and tobacco experts (including Dr. David Burns) on various critical smoking and health issues and on developing means for their long-term resolution.

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- Liggett has assisted, and continues to assist, the Federal Trade Commission, the Department of Justice, Congressional staff members, State agencies and officials and others in their various investigations of the tobacco industry.

Liggett is therefore fulfilling its agreement to turn State's evidence, which includes waiving the attorney-client privilege and providing witnesses to the states.

Liggett's undertakings were significant and are believed by many of us to have been a factor in the willingness of the industry to discuss resolution.

Under the settlement agreement with the Attorneys General, Liggett is required to pay to the settling states as follows:

6.3 Subject to the terms of this Agreement, Liggett shall make the following payments:

6.3.1. An initial payment of \$25 million due 120 days from the date of a Future Affiliate Transaction; and

6.3.2. Subject to the provisions of Sections 6.6 - 6.12, payments, each equivalent to 25% of Liggett's Pretax Income, due 120 days after the end of each fiscal year of Liggett. The first payment shall be made with respect to the first full fiscal year commencing after the date of this Settlement Agreement.

6.4 Liggett shall pay the reasonable and necessary expenses of the administration, allocation, and distribution of the Settlement Fund; provided that Liggett shall not be obligated to pay more than \$1 million in any year for such expenses.

6.5 Since the Settling Defendants are providing historic and valuable cooperation and other considerations under this Agreement and the Mandatory Class Agreement, the amounts payable hereunder to the Settlement Fund shall represent the maximum amounts payable to the Settlement fund under this Agreement and the Mandatory Class Agreement.

In recognition of the valuable contribution of Liggett Section 5.1 of the settlement Agreement provides:

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5.1 Effective upon the execution hereof, the Attorneys General and their respective counsel, each agree (a) to exercise best efforts to ensure that the financial terms, financial obligations or financial conditions of any Global Settlement are no more onerous on, or less favorable to, Brooke Group and Liggett than the financial terms, financial obligations or financial conditions of this Settlement Agreement, and (b) to issue a public statement substantially in the following form and substance:

The historic settlements entered into by Liggett, whereby Liggett has agreed, among other things, to provide full cooperation to twenty-three Attorneys General and to consent to FDA regulation of tobacco marketing, are a major advance in our efforts to prevent smoking by children and adolescents and to ensure that the tobacco industry markets its products lawfully. Accordingly, the undersigned Attorneys General will use their best efforts in Congress and elsewhere to ensure that any such industry-wide resolution provide for financial terms for Liggett that reflect appropriate recognition of Liggett's cooperative efforts.

The terms of the proposed industry wide resolution requires Liggett to make payments far in excess of those required by the Attorneys' General settlement. The Attorneys General who settled with Liggett believe that Liggett deserves special consideration with respect to the financial terms of the proposed resolution. Because of Liggett's valuable role and its willingness to turn State's evidence and with Liggett's permission, we suggest that Liggett's financial obligations be as follows:

Liggett shall have no obligation with respect to the \$10 billion up front payment.

Liggett shall be excused from any of the required per year payments to the extent that its market share is not more than 3%.

To the extent that Liggett's shares ever exceeds 3%, it shall be required to pay its share of the annual payments required by any legislation on the amount over 3%².


² Liggett has agreed that it will match any mandatory price increase imposed on tobacco companies as part of the legislation. Thus, Liggett would maintain its historic price difference and would not be able to take advantage of other companies as a result of its different financial obligations.

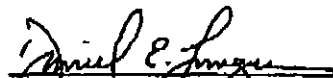
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We were unable to get the industry to agree to this proposal, but feel strongly that Liggett deserves special consideration for turning State's evidence and for making the historic admissions Liggett has made.

We would be glad to discuss this with you further and request the opportunity to do so.

Sincerely,



Grant Woods
Attorney General of Arizona


Daniel E. Lungren
Attorney General of California



Richard Blumenthal
Attorney General of Connecticut



Robert A. Butterworth
Attorney General of Florida



Margery S. Bronster
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Jeffrey A. Modisett
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Carla J. Stovall
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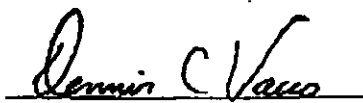

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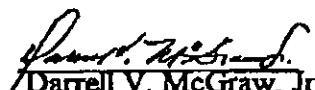

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The Case for Liggett

Tobacco -
LIGGETT

cc: Elena

The Liggett Group is the nation's smallest "major" tobacco company with less than 2 percent of the cigarette market. Liggett has entered legally binding settlement agreements with the Attorneys General of twenty-five states to settle pending suits over tobacco related issues. Now the nation's largest tobacco companies want to void Liggett's settlement agreements, and require Liggett to comply instead with the terms they have negotiated in their recent memorandum of understanding or "global settlement." Liggett did not participate in these latter negotiations, and it would take an act of Congress to preempt Liggett's agreements.

In its settlement agreements with the states, Liggett has agreed to:

- **turn over all documents related to tobacco and public health** and renounce all attorney client and joint defense privileges pertaining to Liggett's documents and work products. To prevent full disclosure to the courts and the Congress, Phillip Morris and R.J. Reynolds are suing Liggett.
- **unfettered regulation by the Food and Drug Administration**, and to compliance with FDA regulations covering the sale, distribution, marketing and advertising of tobacco products to children and adults. Again, this is in sharp contrast to the settlement negotiated by the major tobacco companies.
- **admit to the health risks associated with and addictive nature of smoking**, and include these warnings on its labels. Only four days after the "global settlement" agreement was announced, lawyers for the major tobacco companies attacked Liggett for statements regarding the health risks and addictive nature of tobacco, and shortly after, refused to answer questions relating to tobacco addiction in the first hearings held before Congress.
- **renounce advertising aimed at children and any attempt by firms to expand their underage market share.** Liggett has far less than .02 percent of this market, and has endorsed legislative proposals which would impose severe economic penalties on any firm which does not reduce its share of the youth market. Furthermore, Liggett has agreed to raise its prices to prevent any advantage in the youth market.
- **pay 27½ percent of its annual pretax income to settle its liability.** Liggett would pay its taxes under current law. In contrast, major companies are asking Congress to change current law to allow deductions for punitive damages, thereby enabling companies to claim huge net operating losses on a carryover basis.

Liggett's Treatment Under the Global Settlement:

If Liggett chose not to participate in the global settlement as written, it would go into bankruptcy

immediately. Under the so-called global settlement, a nonparticipating manufacturer would:

- receive no civil liability protection
- pay each year 150% of their would be share into escrow for 35 years. This payment would be in addition to Liggett's obligation to pay 27.5% of pretax profits.
- receive no civil liability protection for the company's distributors, thereby effectively eliminating any distributor willing to carry the company's product

Even if Liggett accepted the agreement as written it would face bankruptcy-- "a certain death sentence (USA TODAY, 6/23/97); "they're going to get killed," (Bloomberg, 6/20)-- because it cannot make the volume based (rather than profit based) payments required by the settlement. Liggett's vulnerability was well understood when Liggett negotiated with the states, and well understood by the major tobacco companies when they negotiated a new agreement without Liggett at the table.

Why Liggett's Agreements with the States Should Be Honored:

In essence the major tobacco companies, through the global settlement, are asking Congress to legislate a "taking" of Liggett's legally binding settlement agreements with the states.

Nearly two years ago, Liggett realized that the cigarette industry needed to break with its past and admit to the health hazards posed by its products. Liggett made its documents available to the courts and accepted its responsibility to protect the public health. **In return, Liggett was given a stiff payment system which nonetheless allowed the firm and its workforce survive.** These agreements were fair, equitable, and legally binding; and they have served the nation well.

Once Liggett led the way, the other major tobacco companies agreed to settle their liability. But they have made far fewer commitments to protect the public health and have taken every opportunity to hide the record from the courts, Congress, and the American people.

All Wall Street analysts agree that the global settlement as written will bring a huge windfall in stock value for major tobacco firms, while Liggett will suffer grievously. It would be an ironic and tragic outcome if the one firm which "blew the whistle" and brought the others to the table-- the one firm which the President has said "told the truth"-- was put out of business while every other major firm prospered.

When whistleblowers testify before Congress, the American people expect them to be protected, and they are. Congress must do no less for Liggett and its workers.

The Proposed Global Deal vs. The Liggett Settlement

The Case for Liggett

Proposed Global Deal	Liggett Agreement and Contract
<p>The Parties:</p> <p><i>The proposed global deal (the "Deal") between the Attorneys General of 36 states and Philip Morris, R.J. Reynolds, Brown & Williamson, Lorillard, and United States Tobacco is not a binding agreement among the parties to terminate formally litigation but is merely an outline for federal legislation. The two largest cigarette companies and one smokeless tobacco company, representing 70 percent of the market of their respective industries, represented the entire tobacco industry.</i></p>	<p>The Parties:</p> <p><i>The Liggett Settlement Agreement/Contract (the "Liggett Settlement") between the Attorneys General of 25 states and Liggett & Myers, Inc., The Liggett Group and Brooke Group Ltd. ("Liggett") is binding on the parties to terminate formally litigation and does not advocate or require federal legislation. Liggett represents 1.6 percent of the United States cigarette market.</i></p>
<p>FDA Regulation:</p> <p><i>The Deal would limit severely the FDA's authority to regulate tobacco and tobacco products. By mandating heightened standards of proof and burdensome regulatory requirements, the Deal effectively prohibits the FDA from restricting hazardous contents of cigarettes, including nicotine, for at least 12 years.</i></p>	<p>FDA Regulation:</p> <p><i>Under the Liggett Settlement, Liggett agreed to unfettered regulation by the FDA and to comply with all of the Administration's currently proposed regulations covering the sale, distribution, marketing and advertising of tobacco products to children and adults. The Liggett Settlement does not affect the standards of proof imposed on the FDA.</i></p>
<p>Payment Requirements:</p> <p><i>The payment provisions of the Deal would bankrupt small non-participating companies such as Liggett. At a minimum, Liggett's first year payment under the Deal would be at least 150 million dollars.</i></p>	<p>Payment Requirements:</p> <p><i>The Liggett Settlement was negotiated to provide the states and others the funds needed to address smoking-related harms while preventing the insolvency and bankruptcy of Liggett. Liggett pays 27-1/2% of its pretax profits to the settlement fund.</i></p>
<p>Tax Subsidies and Loopholes:</p> <p><i>The Deal creates new tax loopholes allowing all payments by tobacco companies to be tax deductible as normal business expenses. Big tobacco companies will be able to carry back large net operating losses and get multi-billion dollar refunds to defray upfront expenses. This allows companies to go back years and reclaim huge tax payments in very profitable years. The total refund in the first year will be billions of dollars.</i></p>	<p>Tax Subsidies and Loopholes:</p> <p><i>The Liggett Settlement does not create any new tax loopholes or subsidies for Liggett. Liggett will continue to pay taxes under current law. Liggett is a small company and has limited or no profit from prior years. No huge refund is available from Net Operating Losses that would be generated by the Deal through new tax loopholes.</i></p>
<p>Public Admissions:</p> <p><i>The Deal does not require any public admissions by the tobacco companies regarding the true nature of tobacco, the causal link to serious health problems, and the fact tobacco companies targeted its marketing to children. Under the Deal tobacco companies would be permitted to state they "do not necessarily agree" with the Deal's provisions.</i></p>	<p>Public Admissions:</p> <p><i>Under the Liggett Settlement, Liggett agreed to admit publicly that smoking is addictive, causes serious health problems, and that tobacco companies used youth-targeted advertising and marketing.</i></p>

Proposed Global Deal	Liggett Agreement and Contract
<p>Document Disclosure:</p> <p><i>Under the Deal, the tobacco companies are <u>not</u> required to make full and complete disclosures. Failure to disclose these documents makes a set of recommendations to forgive past practices and set health care policy into the 21st century impossible.</i></p>	<p>Document Disclosure:</p> <p><i>Under the Liggett Settlement, Liggett has agreed to turn over all documents related to tobacco and public health and renounce all attorney client and joint defense privilege and work product protections pertaining to Liggett's documents and work products. But so far, these documents continue to be concealed from the public, press, regulatory bodies, health officials and Congressional authorities because of Philip Morris and R.J. Reynolds lawsuits.</i></p>
<p>Limitations on Current and Future Legal Actions:</p> <p><i>The Deal provides significant and unprecedented legislative protection from current and future litigation. The Deal would eliminate attorneys general actions, class actions, and "addiction"/dependency lawsuits; would cap compensatory damages; change the rules of evidence; and would restrict third party payor claims and claims by individuals.</i></p>	<p>Limitations on Current and Future Legal Actions:</p> <p><i>Under the Liggett Settlement, Liggett does not receive any legislative protection from litigation. Liggett is still required to settle each action brought by each attorney general in every state. To date, Liggett has settled with 25 states and continues to negotiate with others.</i></p>
<p>Youth Smoking:</p> <p><i>The Deal has meager youth smoking reduction targets and provides the tobacco companies too many loopholes to avoid strict compliance. Under the Deal youth smoking must be quantified to include only daily users of tobacco products, and there are caps on the penalties for failing to meet the look-back targets. And finally, companies cannot be fined if they attempt in good faith to meet the targets but fail — which in effect reduces the economic incentive for the tobacco industry to reduce youth smoking.</i></p>	<p>Youth Smoking:</p> <p><i>Liggett has a minuscule portion of the youth smoking market(.02 percent), is committed to reducing youth smoking, and does not target its advertising to children. Liggett has agreed to support and will not challenge the FDA's regulations concerning the sale of cigarettes to children and adolescents. Additionally, Liggett has endorsed the Waxman bill that would provide a one dollar per pack penalty on any company that does not reduce its youth smoking and has agreed to raise its prices to prevent any advantage in the youth market.</i></p>
<p>Advertising and Marketing:</p> <p><i>The Deal would eliminate traditional forms of tobacco advertising and marketing but would still allow other forms of advertising and marketing.</i></p>	<p>Advertising and Marketing:</p> <p><i>Liggett has agreed to comply with the FDA's advertising restrictions and also instructed its advertising and marketing people to avoid scrupulously any and all advertising or marketing which would appeal to children or adolescents.</i></p>
<p>State Preemption:</p> <p><i>The Deal would place severe limitations on the power of the states to regulate tobacco product ingredients and nicotine.</i></p>	<p>State Preemption:</p> <p><i>The Liggett Settlement does not limit the power of the states to regulate tobacco or tobacco products.</i></p>
<p>Respecting Liggett's Settlement:</p> <p><i>In negotiating the Deal, the big tobacco companies insisted on nullifying the Liggett Settlement.</i></p>	<p>Respecting Liggett's Settlement:</p> <p><i>Under the Liggett Settlement, the Attorneys General committed to ensuring Liggett fair treatment under any global agreement.</i></p>

THE PROPOSED GLOBAL TOBACCO DEAL SHOULD PROTECT THE INTEGRITY OF THE LIGGETT SETTLEMENT

The proposed Global Deal between the Attorneys General of 36 states and Philip Morris, R.J. Reynolds, Brown & Williamson, Lorillard, and United States Tobacco is a proposal for federal legislation to address the societal problems caused by the use of tobacco products. This ground breaking proposal, although laudable for its public health goals, fails to address adequately and fairly, pre-existing tobacco company settlements. The Liggett Settlement is a binding agreement regarding pending tobacco litigation between Liggett and the Attorneys General of 25 states and addresses the very public health goals and related issues in the Global Deal, but the Global Deal as proposed raises serious constitutional and public policy issues.

Any legislation enacting the Global Deal must protect the Liggett Settlement to avoid Fifth Amendment issues. Contractual agreements like the Liggett Settlement have been considered as contract rights by the Supreme Court. The Supreme Court recognized in *Dames & Moore v. Regan* that a suspension of a legal claim under a contract may constitute a compensable taking of private property. If the Global Deal is implemented as proposed, Liggett's contractual rights will not just be suspended but may be abrogated retroactively. In *United States v. Security Industrial Bank* the Supreme Court said that the destruction of property rights by retrospective federal legislation is to be avoided because such legislation can raise "difficult and sensitive questions arising out of guarantees of the Takings Clause." The Liggett Settlement must be protected in any legislation implementing the Global Deal in order to avoid the destruction of its property rights through retroactive legislation.

Legislation enacting the Global Deal that does not protect the Liggett Settlement raises fundamental Due Process issues. Unless the Global Deal legislation protects the Liggett Settlement, it will not meet the fairness and rational legislative purpose requirements of the Due Process Clause. The Due Process clause of the Fifth Amendment to the Constitution includes the requirement of fairness. In *Bolling v. Sharpe*, the Supreme Court recognized that the Due Process clause "stem(s) from our American ideal of fairness. . . ." Due Process also requires that the retrospective aspect of legislation "is itself justified by a rational legislative purpose. *Pension Benefit Guarantee Corp. v. R.A. Gray & Co.* In addition, the Global Deal recognizes that its implementation "may require [the parties] to act (or refrain from acting) in a manner that they might otherwise claim would violate state and federal constitutions" and suggests that the parties be forced to waive their constitutional rights - a proposition of questionable validity that raises serious constitutional and policy concerns.

Fairness requires that the implementation of the Global Deal respect Liggett's Settlement:

- The Liggett Settlement forced the big tobacco companies to negotiate the Global Deal. However, the Global Deal could destroy the Liggett Settlement which in turn would bankrupt Liggett, while doubling the market values of

big tobacco stocks and enriching their officers. It would be fundamentally unfair for Congress to be an unwitting accomplice to the attempts by big tobacco to retaliate against Liggett for its ground breaking agreement.

- Liggett has waived irreversibly its attorney-client privilege and turned over Liggett documents, Liggett-privileged documents and so-called joint defense documents to the courts. So far, these documents continue to be concealed from the public, regulatory bodies, Congress, and health officials because of Philip Morris and R.J. Reynolds lawsuits.
- Under the Liggett Settlement, Liggett agreed (1) to admit publicly that smoking is addictive, causes serious health problems, and the tobacco companies used youth-targeted advertising and marketing, (2) to announce and make adult smokers aware of the health risks and addictive nature of smoking, including the warning label, "Smoking is Addictive" (labels which are already being used), (3) to have Bennett LeBow, CEO of the Brooke Group, make public statements that smoking causes health problems, (4) that marketing toward youth is banned in the Liggett Settlement, including the use of cartoon characters, and (5) that it would be bound fully by the FDA's regulations on the sale, distribution, and advertising of tobacco and tobacco products to children and adults (and unlike the Global Deal, the FDA is not required to use extraordinary or heightened standards of proof or meet burdensome regulatory requirements before it can take action under existing or future law). Liggett has fulfilled these requirements and has continued to rely substantially on the commitments made under the Liggett Settlement.
- Under the Liggett Settlement, Liggett also agreed to (1) pay 27-1/2 percent of its pretax income, (2) pay the reasonable and necessary expenses, up to \$1 million per year, of administering the settlement fund, and (3) adjust payments annually according to changes in market share. No legislation is required to effectuate the Liggett Settlement.

The Global Deal provides for the application of punitive measures for "non-participating" companies like Liggett, which is clearly an unfair attempt to coerce Liggett into abandoning its Settlement.

In a recent case, *U.S. v. Winstar*, the Supreme Court held the U.S. liable when a private party, which had changed its position in reliance on prior government inducements, was bankrupted as a result of a Congressional reversal of the prior government's act. In the present instance, Liggett will be bankrupted if the legislation enacting the Global Deal does not protect its settlement. Liggett settled its lawsuits in good-faith reliance on the ability of the judicial system to enforce its settlement, and it would be fundamentally unfair for Congress to change the rules of the game, especially since the Global Deal would not have occurred without the Liggett Settlement.

The retroactive destruction of the Liggett Settlement by the Global Deal does not have a rational legislative purpose. The Liggett Settlement contracts have been incorporated in state and federal judicial decrees. Unless the legislation which implements the Global Deal protects the Liggett Settlement, it will violate the principle of res judicata. Retrospective legislation that voids settlements is contrary to the public interest in encouraging settlements, and legislation of this type will substantially inhibit future settlements.

Retrospective legislation which impose liability beyond amounts established by a pre-existing settlement or settlements is not a "rational measure to spread the costs" among those who have benefited from past acts (as was the justification for the retroactive application of the Black Lung Benefits Act of 1972. *See Usery v. Turner Elkhorn Mining Co.*), nor is it justified by the need to preclude action during the pendency of the legislative process (as was the case in *PBGC v. Gray*).

Any legislation enacting the Global Deal which obviates settlements by imposing costs over those fixed by the Liggett Settlement would have similarities to the provisions of the Railroad Retirement Act of 1934 that created pensions for employees who had been compensated fully. This requirement was invalidated in *Railroad Retirement Board v. Alton R., Co.*, and the *PBCG v. Gray* decision recognized that this decision may remain applicable.