

Tobacco Settlement

Revenue Description

Montana receives tobacco settlement revenue per the Master Settlement Agreement (MSA) with 60 tobacco companies which concluded litigation with 46 states, Puerto Rico, American Samoa, the U.S. Virgin Islands, the North Mariana Island, Guam and the District of Columbia (52 total settling entities). The lawsuit and subsequent settlement were regarding tobacco-related health care costs. Montana currently receives an on-going annual payment and a “strategic contribution” payment that will expire after FY 2017.

Statutory Reference

Tax Rate – N/A

Tax Distribution – [Montana Constitution, Article XII, Section 4](#); [17-6-606, MCA](#); [53-4-1011, MCA](#)

Date Due – Annual payments from settling entities due April 15th ([Master Settlement Agreement, Chapter IX\(c\)](#)), General Tobacco annual payments through 2016 due August 30th (General Tobacco Adherence Agreement)

Applicable Tax Rates:

Funds received are subject to adjustments for various reasons including inflation, sales volume, loss of market share due to non-settling companies, operating income, settlements reaches by the non-participating states, offsets for litigation, disputed payments, and others.

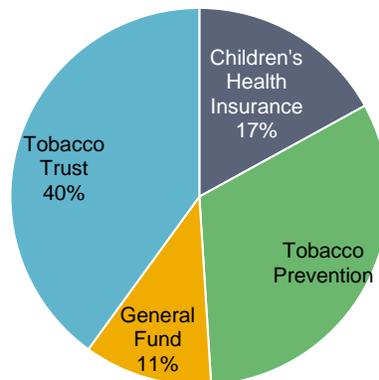
Montana receives 0.4247591% of the total on-going annual payment, and 1.0447501% of the strategic contribution payment.

Collection Frequency

Annual payments are expected each April 15th into perpetuity. General Tobacco, a subsequent participating manufacturer, is required to make annual payments every August 30th through 2016 for obligations incurred from 2000 to 2003.

Distribution

The legislature is required to dedicate no less than 40% of tobacco settlement money to a permanent trust fund. The remaining revenue is distributed between the general fund, the Children’s Health Insurance Program state special revenue fund, and the Tobacco Prevention state special revenue fund. The following chart shows the FY 2014 distribution of the tobacco settlement funds.



Comparison of Legislative and Executive Forecasts

There are no material differences between the legislative and executive branch forecasts.

Tobacco Settlement (\$ Millions)				
	FY 2015	FY 2016	FY 2017	Total
Executive Forecast	\$3.280	\$3.200	\$3.110	\$9.590
Legislative Forecast	3.176	3.145	3.115	9.436
Difference	\$0.104	\$0.055	(\$0.005)	\$0.154
% Difference	3.3%	1.7%	-0.2%	1.6%

Forecast Risks

- Inflation
- Volume
- Changing market share for settling companies
- Payment disputes

Revenue Estimate MethodologyData

PriceWaterhouseCoopers (PWC), the independent auditor to the agreement, gathers all tobacco settlement data and makes all the calculations required by the Master Settlement Agreement for determining the amount owed and the distribution. PWC provides detailed documentation of all calculations that is used to inform the model.

Analysis

The base amount of the settlement is a set value, the analysis and relies on forecasting the adjustments made to that base amount that will result in the final revenue. The adjustments calculated in the model are related to (1) inflation, (2) volume, (3) operating income, (4) states with prior tobacco settlements, (5) non-participating cigarette manufacturers.

1. Inflation – This adjustment cumulatively increases the amount owed by the greater of 3% or the amount of the Consumer Price Index for Urban Consumers. This is forecast using the CPI forecast provided by IHS.
2. Volume – Payments are reduced as the number of cigarettes shipped nationally decreases. The current number of cigarettes is compared to the 1997 base number of 475.7 billion cigarettes. The analysis assumes that the historic trend in number of cigarettes shipped will continue through the biennium. Per the settlement agreement, the calculated adjustment is reduced by 2.0% and then applied.
3. Operating income – Payments increase if the aggregate operating income from the sales of cigarettes exceeds the 1996 base amount of \$7,060.840 million, as adjusted for inflation (see above). This adjustment has not been used since 2000 and therefore is not explained in this document.
4. Previous settling states – Previous to the Master Settlement Agreement, four states had settled lawsuits with certain cigarette manufacturers. The agreement recognized this by allowing reductions to the annual payments (as adjusted for inflation and volume) of 12.45% through FY 2007, 12.24% through FY 2017, and 11.07% thereafter.
5. Non-participating manufacturers (NPM) – If tobacco manufacturers who participate in the Master Settlement Agreement lose market share to those manufacturers who do not, their payments may be reduced, if certain criteria are met.

This adjustment is three times the market share loss of the participating manufacturers. Market share loss is determined by subtracting the current year market share of the participating manufacturers from 97.5835%. If the computed market share loss exceeds 16-2/3%, adjustments are made to account for loss of market share. For this to occur, the change in market share for all PM would have to fall to 80%. It is unlikely that this will occur. While this adjustment is not included as such, the estimate is reduced slightly because the participating manufacturers generally dispute a portion of a payment. FY 2014 was the first year that any disputed payment has completed the cycle of litigation, and the state received the disputed 2003 funds.

These forecast adjustments are applied to the base amount, and the result is the total revenue estimate.

Revenue Estimate Assumptions

FY	Total Settle \$ Millions	GF Settle \$ Millions	Market Share	Volume (Millions)	Annual Inflation (at least 3.0%)
A 2002	\$31.079	\$18.647	0.000	0.384	3.0%
A 2003	31.166	18.700	0.941	0.365	3.0%
A 2004	26.672	2.934	0.938	0.345	3.0%
A 2005	27.071	2.978	0.942	0.339	3.3%
A 2006	24.851	2.734	0.939	0.332	3.4%
A 2007	25.931	2.861	0.941	0.327	3.0%
A 2008	34.614	3.808	0.943	0.312	4.1%
A 2009	37.524	4.128	0.937	0.300	3.0%
A 2010	31.533	3.469	0.936	0.269	3.0%
A 2011	29.625	3.259	0.936	0.258	3.0%
A 2012	30.203	3.322	0.941	0.250	3.0%
A 2013	30.194	3.321	0.939	0.245	3.0%
A 2014	33.142	3.646	0.939	0.235	3.0%
F 2015	28.874	3.176	0.939	0.235	3.0%
F 2016	28.593	3.145	0.939	0.225	3.0%
F 2017	28.317	3.115	0.939	0.216	3.0%

Revenue Projection

