U.S. DEPARTMENT OF HEALTH & HUMAN SERVICES
OFFICE OF THE GENERAL COUNSEL

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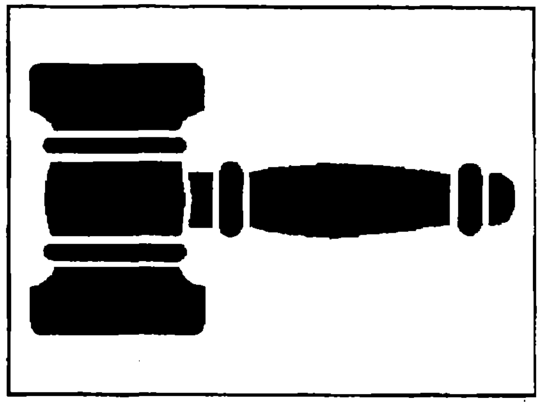
DATE: March 31, 1997



TO: **ELIZABETH DRYE**
fax: 456-5581

FROM: ANDREW D. HYMAN
Special Assistant to the General Counsel
Office of the General Counsel, Room 707F
U.S. Department of Health and Human Services
200 Independence Ave., SW
Washington, D.C. 20201

COMMENTS: Call me about the attachment.

No. of Pages (including cover): 3

DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of the Secretary

Washington, D.C. 20201

March 26, 1997

NOTE TO: The Deputy Secretary
Through: ES_____
DES_____

FROM: Jerry Walters
Policy Coordinator, ES

SUBJECT: **Tobacco Litigation and Liggett Settlement--BRIEFING**
Friday, March 28, 1997, 9:00 - 10:00 a.m.
The Deputy Secretary's Conference Room

Participants:

Bruce Vladeck
John Monahan
Andy Hyman
Rich Tarplin
LaVarne Burton
Gary Claxton
Claudia Cooley
Jackie White

Background:

Liggett Group entered into settlement agreements with five States for tobacco-related illnesses. HCFA requested that all settling States treat the settlement as a recovery of third party liability for Medicaid expenditures, and that States credit the federal government with its share. Two States complied with HCFA's request. HCFA would like to take those actions necessary to bring all the States into compliance with its request.

Attached is a note from HCFA that explains its recommendation. ES believes that this meeting will provide HCFA an opportunity to explain more fully, and provide Department principals with an occasion to discuss the issues.

Attachment

DEPARTMENT OF HEALTH & HUMAN SERVICES

Health Care Financing Administration

The Administrator
Washington, D.C. 20201

— Next weekly —

MAR 11 1997

— a/4 —

TO: Kevin Thurm

FROM: Bruce C. Vladeck

SUBJECT: Tobacco Litigation and Liggett Settlement

I would like to update you on the status of Medicaid's collections from the Liggett tobacco settlements, and suggest that the Department move ahead with enforcement actions against States that have refused to yield the federal share of these recoveries.

As you know, the Liggett Group entered into a settlement agreement with Massachusetts, Florida, West Virginia, Mississippi, and Louisiana based on litigation concerning health care expenditures for tobacco-related illnesses. The settlement provided for initial payments of $200,000 for each State, and continuing payments over succeeding years.

HCFA has requested that all 5 settling States treat the settlement as a recovery of third party liability for Medicaid expenditures, and credit the federal government with its share (by offsetting the recovery against State Medicaid expenditures before claiming federal financial participation). The request was in the form of instructions for crediting the federal share on the quarterly expenditure report. Massachusetts and Florida did so. West Virginia and Mississippi refused. Louisiana did not respond to HCFA's request (and did not credit any payment to the Medicaid program).

The Office of General Counsel has reviewed the complaints in the underlying litigation and the settlement agreement, and advised that the recovery was based primarily on Medicaid expenditures by the States. As such, any settlement received must be credited, in full or in part, to the Medicaid program. As a Medicaid recovery, HCFA cannot "forgive" a State's obligation to credit the federal government with its share, and there is no clear basis to compromise the federal claim. Compromise of this position would jeopardize the effectiveness of all third party liability requirements of statute and regulation which give the Medicaid program a primary claim on all recoveries. While there may be some flexibility to negotiate a reasonable allocation of settlement funds among the parties (if, for example, the States can show that some of the recoveries relate to State-only health program expenditures), denial of any Medicaid recovery would threaten the credibility of the federal government to require Medicaid recoveries in other actions.

Thus far, HCFA has taken no enforcement. The next annual Liggett payment is apparently due soon, and should be reported on States' next quarterly expenditure report due. We believe that, unless some enforcement action is taken, the two States currently complying with the requirement will cease to do so. I therefore recommend that we begin enforcement action against West Virginia, Mississippi, and Louisiana to collect the federal share of this recovery.

Leo Intergovernmental Lumn.

97-0180

APPROPRIATIONS
BUDGET
ENVIRONMENT AND PUBLIC WORKS
SMALL BUSINESS
HELSINKI COMMISSION

United States Senate

WASHINGTON, DC 20510-3002

March 13, 1996

The Honorable Janet Reno
Attorney General
U.S. Department of Justice
10th and Constitution Avenue
Washington, D.C. 20530

The Honorable Donna Shalala
Secretary
U.S. Department of Health and Human Services
200 Independence Avenue, S.W.
Washington, D.C. 20201

Dear General Reno and Secretary Shalala:

In a historic announcement today, the Liggett Group Inc., one of this country's largest tobacco companies, stated that it would settle a class action lawsuit in New Orleans, Louisiana. Under the reported terms of the agreement, the Liggett Group has agreed to pay the states of Florida, Massachusetts, Mississippi and West Virginia approximately $4 million over the next ten years to help cover Medicaid costs associated with treating tobacco-related illnesses.

I strongly urge you to file a similar suit to recoup the Federal health care costs associated with tobacco related illnesses. As you know, the taxpayers pay approximately $20 billion a year in Medicare and Medicaid costs to treat persons with tobacco-related illnesses. These costs alone made up about 12 percent of the entire Federal deficit last year.

If the tobacco companies are going to reimburse these states for their Medicaid costs associated with tobacco-related illnesses, it is only fair that taxpayers throughout the country get reimbursed for the same expenditures.

This is a historic opportunity to reduce the deficit and make the tobacco companies pay for the costs that their products inflict on our society. I strongly urge you to seize it.

Thank you for your consideration of this request.

Sincerely,

Frank R. Lautenberg

Y TO:

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The New York Times
MONDAY, MARCH 24, 1997

LIGGETT PROPOSAL WOULD LIMIT FUNDS TO HELP SMOKERS

FEW DOLLARS TO AID MANY

Company Would Gain the Most Financially, Along With the Lawyers Who Filed Suit

A1

By BARRY MEIER

The public's applause over the calculated capitulation last week by the Liggett Group, one of the nation's largest cigarette makers, has overshadowed a sobering fact: thousands of smokers who have pursued the company in court for years stand to receive little under a proposed legal settlement also announced last week.

Liggett received wide publicity last week when it struck a deal to resolve claims by 22 state attorneys general. But less widely noticed was that the company and a group of plaintiffs' lawyers also won preliminary approval from a state court judge in Mobile, Ala., for a companion plan to settle all current and future suits by smokers, their survivors, cities, counties and insurers.

The terms of that plan, which caught other lawyers with cases involving Liggett by surprise, are both financially lean and legally harsh. Smokers, their survivors and others would share with the attorneys general in 25 percent of Liggett's pretax income, which the company would put into a settlement fund over every year for the next 25 years.

Based on Liggett's 1995 income, its payment that year would have been some $575,000, papers filed with the Alabama court indicate. There are potentially thousands or perhaps tens of thousands of claimants.

In an unusual legal move, the plan would not allow those who oppose the terms to opt out and pursue their own lawsuits. In contrast, most class-action lawsuits allow plaintiffs to drop out of a settlement. In addition, plan participants would not receive any details about the allocation of settlement money until after the pact is approved, court papers indicate.

The documents filed in Alabama

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suggest that the plan's immediate financial winners would be Liggett itself and participating plaintiffs' lawyers, whose fees and expenses would be paid by the tobacco company. Last year alone, Liggett spent $9.6 million defending itself against smokers' lawsuits with an undisclosed portion of that money coming from other tobacco producers, court documents state.

For their part, state attorneys general have said the real value of any settlement with Liggett to the public would not be financial. Rather, they point to the company's unprecedented acknowledgment in the settlement of the state cases that tobacco is addictive. They also noted that the company agreed to make potentially damaging documents available for use in lawsuits against other cigarette makers.

Smoking opponents have also applauded Liggett's agreement not to fight Government efforts to regulate cigarette marketing.

The plaintiffs' lawyers involved in the proposal filed in Alabama said it was the best they could get given Liggett's weak financial position. The company's market share has declined steadily in recent years, and it says it has a negative net worth.

Both plaintiffs' lawyers and Liggett acknowledged in court papers that the settlement plan provided

A plan that largely aids Liggett and plaintiffs' lawyers.

"uniquely favorable terms" to the tobacco company based on factors like its finances and its decision to step forward. The company sells brands that include Chesterfield, L&M and Lark.

"This is a compromise, and we hope that there is adequate funding for this class," said Norwood S. Wilner, a lawyer from Jacksonville, Fla., who represents smokers in that state and helped negotiate the plan. "But given Liggett's financial condition, you probably couldn't collect a major court judgment."

Still, the proposal is expected to come under fire from other plaintiffs' lawyers. Minnesota, which took part in the settlement involving the attorneys general, and Blue Cross Blue Shield in that state expect to oppose the Alabama plan, said Michael Ciresi, a lawyer for the state and the insurer.

Stanley Rosenblatt, a lawyer in Miami who is heading two class-action lawsuits filed in that state against Liggett and other cigarette producers, said: "This is a phony gimmick designed to enrich a bunch of plaintiffs' lawyers. It doesn't put a dime in the pocket of any individual who was damaged by smoking."

Some legal experts also questioned the constitutionality of an Alabama state court's issuing a ruling that would bind officials, insurers and individuals around the country to a plan with no opt-out provision. And they said they were concerned that more state attorneys general had not spoken out against the proposal.

"It is disgraceful that attorneys general would allow a plan that doesn't allow their own citizens to opt out," said Susan Koniak, a professor of law at Boston University. Marc E. Kasowitz, a lawyer for Liggett, acknowledged in an interview that the proposal was likely to provide little, if any, direct financial benefit to those who claim they developed lung cancer or emphysema from smoking the company's cigarettes.

"The alternative to this deal is that Liggett goes bankrupt, and in that case the cooperation to the class and the injunctive relief would not be available," Mr. Kasowitz said.

Technically, the type of "non-opt" class-action pact being proposed in the Liggett case is known as a limited fund settlement plan, and is used when defendants do not have sufficient assets to satisfy all claims.

Last year, when Liggett was unsuccessfully trying to conclude agreements to settle claims brought by five state attorneys general and a class-action lawsuit on behalf of smokers nationwide, the company was offering to pay $5 million, contribute up to 7.5 percent of its annual pretax income to a settlement fund and pay out $50 million for stop-smoking courses.

The latest round of settlement talks started soon after the early pact unraveled. One central figure was Mr. Wilner, the lawyer from Jacksonville, who won a $750,000 jury verdict last year against the Brown & Williamson Tobacco Corporation. That verdict is being appealed.

Mr. Wilner said he was asked last year by Liggett to get involved in settlement talks involving the company, other plaintiffs' lawyers and state attorneys general. But there has been grumbling by some other plaintiffs' lawyers involved in those talks that Mr. Wilner and his associates stole the march on them last week by filing the settlement plan and seeking the prominent role of class counsel. If approved by the court as class counsel, Mr. Wilner and his colleagues would both receive compensation and be put in a position to vie for leadership roles in other tobacco-related litigation.

"They went down and filed this complaint without telling anybody," said one lawyer in a group representing plaintiffs who was involved in the Liggett settlement proposal that failed last year.

Currently, the Liggett plan provides only a structure for how the company's annual payment to the settlement fund would be allocated.

Under the plan, the state attorneys general and the class counsel representing all other plaintiffs would first have to agree on how to apportion the money among themselves. If they were unable to do so, an arbitrator would be selected to make that decision, court papers indicate.

Then a nine-member panel that would include representatives of public health groups would determine the distribution of the money allocated to the class, including smokers, cities and insurers. Both Liggett and plaintiffs' lawyers have asked the Alabama court to approve the plan without regard to the specifics of its final distribution or allocation to "avoid distracting the parties and the court" from other issues involving the fairness of the settlement. The plan would allow smokers and others to make recommendations once it is approved. The next step for the plan is a fairness hearing, in which members of the class can present supporting and opposing arguments, on July 11 in Mobile.

If the settlement plan involving smokers and others is not approved, the deal with the state attorneys general will still go forward, said Mr. Kasowitz, the Liggett lawyer. In that case, Liggett would make a maximum of 20 percent of its pretax income available for a settlement fund. That payment would then be reduced based on the portion of the nation's Medicaid patients represented by the states participating in the plan.

A1

Drug Trade Feeds on Payoffs at Mexico Line

By DAVID JOHNSTON and SAM HOWE VERHOVEK

CALEXICO, Calif. — At this dusty border crossroads east of San Diego, two Federal inspectors helped a Mexican drug ring move hundreds of pounds of cocaine across the border, simply by waving the smugglers through the checkpoint without even glancing inside their cars.

In El Paso, two Federal Customs inspectors tried to shake down an informer posing as a drug smuggler, one of them demanding more than $1 million to look the other way when cocaine-laden vehicles crossed from the Mexican border city of Juárez into the United States.

And in Zapata County, Tex., a remote stretch of the Texas-Mexico border, drug traffickers turned to local law-enforcement officials for protection in a big way: most of the county's leaders, including the county judge, the sheriff and the clerk, were convicted of or pleaded guilty in Federal court to charges of aiding the international drug trade.

Narcotics-related corruption does not stop at the Rio Grande or at a line in the desert separating the United States and Mexico, which has been rocked in recent weeks by reports that leading officials helped big-time drug traffickers. Nothing on that scale has occurred on this side of the

BRIBERY ON THE BORDER

A special report.

border, but corruption of law-enforcement officials — at the local and now Federal level — has become a corrosive byproduct of the vast river of cocaine, marijuana and heroin that pours into the United States across the 2,012-mile border that reaches from Brownsville, Tex., to Imperial Beach, Calif.

The Federal authorities have long thought that a few law-enforcement officials in remote border counties have been lured by the promise of easy money into leaving Mexican drug gangs alone. Now, the same Federal authorities say they have mounting evidence of systemic corruption in some of those counties. They include Zapata, where the county's leaders were convicted and forced out of office three years ago, and Starr County, Tex., where 79 people, including a deputy sheriff, were indicted a few months ago for taking part in a long-running marijuana smuggling operation.

There are signs of growing corruption in the Federal ranks as well, including of Customs and immigration inspectors, who had long been viewed as more stalwart lines of defense against the drug invasion.

Internal documents shared with The New York Times by current and former officials at the United States Drug Enforcement Administration highlight the drug-corruption issue: one 1995 memorandum, from the Government's El Paso-based clearinghouse for drug intelligence to top drug officials in Washington, warns of "increased and constant receipt" of reports from informers, Government employees and ordinary citizens about "the use of corrupt and

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compromised U.S. Customs and immigration inspectors" to insure that drug shipments cross the border.

Indeed, other documents show that scores of these reports have been passed on to drug agency administrators or Federal prosecutors over the last few years.

"The sorry truth is that people in law enforcement do not make a lot of money, and that's especially true for local officers," said Fred C. Ball, the former head of the Drug Enforcement Administration in McAllen, Tex., who leads a Federal interagency drug intelligence task force covering the entire Rio Grande Valley of Texas. "In some of these counties, somebody will walk up to an officer with $50,000, $60,000 or more and say, 'All you have to do is just turn your head the other way tonight.'"

Mr. Ball added: "That's an explanation for why it happens. It's not an excuse."

Growth Industry

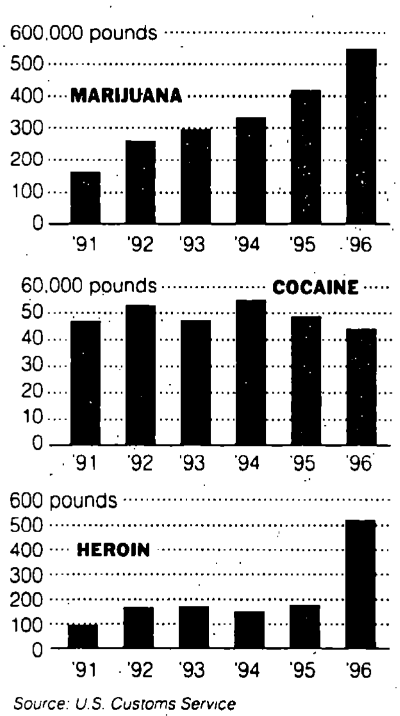
Traffickers' Choice Is Often Bribery

The problem here is limited compared with the scale of the accusations that have been shaking Mexico. But by all accounts, narcotics-related corruption in the United States is serious and growing, and it fuels

FOR EXAMPLE

Against the Tide

Drugs seized by United States Customs at border crossings between Mexico and the U.S. in each fiscal year.



Source: U.S. Customs Service

The New York Times

critics in Mexico and elsewhere who say the United States should grapple with the effects of its own drug problems before it attacks other countries. A review of court records and interviews with state and Federal prosecutors indicate that beyond the informer accounts described in the internal Federal reports, at least 46 Federal, state and local law-enforcement officials have been indicted on or convicted of drug-related corruption charges in the last three years in the border states of California, Arizona, New Mexico and Texas. And that includes only cases in which drugs were transported across the border by land.

That number is unprecedented, Federal law-enforcement officials say, and yet it represents only a small part of the problem: When corruption often involves nothing more than passively allowing smugglers to go about their business, it is extremely difficult to detect and even tougher to prosecute.

As drug dealers have become more brazen and the volume and value of drugs moving across the United States-Mexico border have skyrocketed, many Federal officials openly concede that they fear the problem will grow worse.

"These organizations are no longer mom-and-pop organizations paying people to carry drugs across the border in a knapsack," said Stanley Serwatka, the chief prosecutor in the United States Attorney's office in El Paso. "They are General Motors. To maintain your profit structure, you simply have to import in large quantities," which places a premium on paying off a border official.

Large-scale drug trafficking continues, experts say, despite vows by successive Administrations in Washington to stop it. Traffickers, responding to America's interdiction efforts in the mid-1980's, shifted routes from Florida to Mexico, increasing their reliance on the Southwest border as a transit point. The Customs Service reported that at five border crossings on the California-Mexico border, marijuana seizures increased to 3,518 in 1996 from 2,490 in 1995; that is more than 272,000 pounds of marijuana seized last year.

The heavy flow of drugs across the border has brought an increased law-enforcement presence, which has ratcheted up the pressure on traffickers. In the border area of San Ysidro, south of San Diego, the construction of a 10-foot-high, 14-mile-long steel fence between border crossings to deter illegal immigrants has forced narcotics smugglers to change tactics. Instead of trying to bring drugs across at remote border areas, they are trying to get through at the legal ports of entry, a switch that has created a further incentive to bribe border officials.

Rudy M. Camacho, who manages the San Ysidro crossing, reports 10 to 20 multikilogram seizures a day from traffic there that reaches 45,000 vehicles a day.

"If you have a corrupt inspector, he can make $35,000 to $40,000 with a flick of the hand," said one investigator who asked not to be identified, referring to the motion used by border officials to wave vehicles through checkpoints. "They do it hundreds of times a day. Who can say they knew any car had a compartment with drugs inside?"

Court records from border towns offer a glimpse of just how seductive the lure of money can be, and of the ease with which border patrols and other Government agents can satisfy drug traffickers' needs. The records show, for example, how Border Patrol agents and other Federal employees are offered tens of thousands of dollars simply to "take a break" for a few moments at prearranged times.

Jose de Jesus Ramos, a former El Paso Customs inspector who pleaded guilty to cooperating with traffickers, matter-of-factly described how a few years ago he became corrupted after a fellow inspector appealed to his dissatisfaction with the Customs Service and the job's low pay.

"The situation was that if I was willing, there was always ways to make a little more money," Mr. de Jesus Ramos testified at the inspector's trial last year.

Soon, he said, he was meeting with traffickers in places like the parking lot of the Home Depot store in El Paso, collecting $5,000, then $10,000, then $20,000. With cellular phones and coded beeper messages, he said, it was easy to let drug couriers know which inspection booth was his. Eventually, the two inspectors hatched plans to allow at least 1,000 kilograms of cocaine into the United States over a period of several months, charging informers posing as drug traffickers $1,000 per kilogram — or $1 million in all. The inspectors were arrested before putting the plan into effect.

The New York Times

MONDAY, MARCH 24, 1997

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