

THE WHITE HOUSE

WASHINGTON

May 11, 1995

MEMORANDUM TO ABNER MIKVA
JAMES CASTELLO

FROM: CHRIS CERF *Cse*

RE: Florida Tobacco Litigation

I was asked to evaluate whether the United States could intervene in the tobacco litigation referenced in the attached article.

In the Florida suit, the state is seeking to recoup health care dollars it has spent as the result of tobacco induced diseases. A necessary predicate of the suit is a state statute that, among other things, overrides traditional causation rules and permits the allocation of liability on the basis of market share. That statute has since been repealed, and Governor Chiles has announced his intent to veto the repealing legislation. It is unclear whether there will be enough votes to override the veto.

The Civil Division of the Department of Justice has considered the advisability of participating in the suit and strongly advises against it. The basis for DOJ's recommendation is as follows:

1. The viability of the underlying action is unclear at best in light of the recent repeal of the Florida statute

described above.

2. As a defendant in other actions (e.g., Agent Orange litigation) the U.S. should be very reluctant to endorse a market share theory of liability.

3. Bringing the suit would be very resource intensive.

4. The U.S.'s interests are protected in any event since it would have subrogation rights to any state recovery.

I am further informed that Seth Waxman has already briefed someone at the White House about this. I believe he is seeking approval for the AG to send a letter to Governor Chiles turning down his request for the U.S. to participate in the suit.

Please let me know if anything further is needed on this.



U.S. Department of Justice
Office of the Associate Attorney General

Deputy Associate Attorney General

Washington, D.C. 20530

*file
tobacco*

FACSIMILE TRANSMITTAL COVER SHEET

DATE: May 17, 1995

TO: Jennifer O'Connor

FACSIMILE NO. 456-7929

TELEPHONE NO. _____

FROM: Nancy E. McFadden

Principal Deputy Associate Attorney General

FACSIMILE NO. 202--514-0238

TELEPHONE NO. 202--514-9700

NUMBER OF PAGES (INCLUDING COVER SHEET): 2

COMMENTS:

Jennifer --

Nancy said this should be considered close hold.

Sherry



Office of the Attorney General
Washington, D. C. 20530

The Honorable Lawton Chiles
Governor of the State of Florida
The Capitol
Tallahassee, Florida 32399-0001

Dear Governor Chiles:

Thank you for your letter concerning the possibility of the Department of Justice participating in the State of Florida's lawsuit against cigarette manufacturers. As you know, similar suits have been filed by the States of Mississippi, Minnesota, and West Virginia.

At my request, the Department's Civil Division has been monitoring the tobacco litigation. Thus far we have not been persuaded that participation would be advisable. We will continue to actively monitor these cases, however, and will reconsider this decision should circumstances persuade us otherwise. In this regard, I note your suggestion that representatives meet with the coalition chief counsels. If these attorneys wish to meet with Department representatives, the office of the Associate Attorney General would be pleased to arrange a meeting.

It was a pleasure to be with you during President Clinton's address to the legislature. As always, I was delighted to see you again.

Sincerely,

Janet Reno

To: Marcia Hale cc: Lawton
Fr: Emo
Dt: 4/12/95
Re: Tobacco Lawsuit

5016
To: HAROLD - Do you
know about this? If Chiles
is misrepresenting POTUS' position,
we should let him know

Someone from Kentucky sent me the attached letter from Gov.
Chiles to Janet Reno, which states that POTUS has expressed
interest in having Justice join in the Florida lawsuit against
tobacco companies. Have you seen this? It will undoubtedly
provoke a strong response from Gov. Hunt and Gov. Jones.

emo
x 87953

States
litigation

not
We should find out
how POTUS feels about this.

Did we
intervene
& what are
we doing?

4/18-

HAROLD -

Tina also
called about
this -- see
attached

TO: Harold Ickes
FROM: Tina Flourney
RE: Chiles request to DOJ

Per your request the following is some brief background on the matter that we discussed this morning.

1. During the waning hours of last year's legislative session, the Florida leg. passed leg. (referred to as Senate Bill 2110) which specifically permits the State to sue third parties to recover funds paid out in the form of Medicaid payments to treat illnesses allegedly related to the actions of those third parties or the use of products that they make.
2. The bill is not tobacco specific, i.e. can be applied to any industry (though the Governor has indicated it will only be applied to tobacco); it provides for market share liability; and it takes away affirmative defenses such as assumption of the risk and comparative fault.
3. The response in the press in Fla. has been almost uniformly negative, based, in large part, on the fact that the leg. was passed without discussion and from all reports with most members of the leg. not knowing what they were approving. Two bills have recently been passed in committee to repeal the leg.
4. In late February, acting under 2110, the state of Florida filed suit against the tobacco industry.
5. Three other states have filed suit, though none of them has passed enabling legislation similar to 2110: West Virginia (Governor Caperton opposes the action -- brought by the AG); Mississippi; and Minnesota. These states have joined together to form something called the National Coalition of States for Tobacco Liability.
6. Press reports indicate that Gov. Chiles discussed the suit with the Pres. during his recent trip to Tallahassee. And in a letter to Attorney General Reno, Gov. Chiles has asked the Justice Department to join the National Coalition in its efforts.
7. Obviously, we believe - for several reasons --that DOJ should stay out of this matter, among them being that this is a state matter and should stay with the states. Additionally, from a purely political stand point, it would seem to make little sense for the administration to proactively take on a battle that it does not need to join and, in fact, can legitimately avoid.

I really appreciate your looking into this, and I will gladly provide whatever additional information you need.

cc: Janice Enright



THE GOVERNOR OF THE STATE OF FLORIDA

LAWTON CHILES

April 8, 1996

Honorable Janet Reno
United States Attorney General
Main Justice Building, Room 5111
10th & Constitution Avenues
Washington, D.C. 20530

Dear Janet:

The President brought us an outstanding week and your presence was a major part of the success.

This letter, in addition to conveying our great appreciation to you for being here, is to carry forward the discussion which was initiated with the President regarding Florida's lawsuit against "Big Tobacco" brought by us to recover Medicaid outlays due to cigarette smoking.

As I mentioned to you, the President expressed interest in having the Justice Department participate in the State's actions that have been initiated. We informed him that we had formed a coalition with Mississippi, Minnesota and West Virginia and other states to join soon. We expect Maryland and Massachusetts to join very soon and we have been informed that the British Commonwealth, or some agencies thereof, is considering suit.

As we discussed, there are significant federal funds involved in the Medicaid payments we are seeking to recover. Also, the presence of the Justice Department would enhance the cooperation of Federal Agencies, assist us in obtaining witnesses and give us greater strength in fighting off the powerful tobacco lobby.

Professor Laurence H. Tribe's staff (he is assisting Florida in the suit pro bono) believes the appearance of counsel from the Justice Department rather than the United States formerly becoming a party would have no impact causing removal from the present venue of Palm Beach county Circuit Court. Such appearance could be for evidence and key motions.

A RECYCLED PAPER PRODUCT PRINTED WITH SOY INK

10-Apr-96 4122

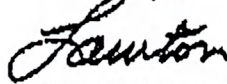
Honorable Janet Reno
April 8, 1995
Page 2.

If, after appropriate review, you believe the participation by the Justice Department would be advisable we could schedule a meeting of the coalition including all coalition chief counsels, as well as participants from Health Care Financing Administration, Health and Human Services, the Medicaid program and other federal agencies which might lend assistance.

We enlist the aid of the Justice Department in our effort to collect the taxpayers funds and would be most honored to work with you and your Department.

With kind regards, I am

Sincerely,



LAWTON CHILES

LC/gdd

10-Apr-95 10:47:22

TO: Janice Enright
 DATE: April 8, 1995
 RE: Convention and one other thing

1. PM owns both Kraft and Miller Brewing Company
2. Kraft is headquarter in Illinois and Chicago is one of Miller's largest markets. Consequently, they are each interested in having a significant presence around the convention. Primarily, this will be in terms of hosting events -- which we will work out directly with interested constituents or the City of Chicago.
3. However, to the extent that there are official events/ DNC events, etc., at which beer is provided, we would like Miller to have a presence (product will be donated).
4. This request may be somewhat of an issue because I believe that the WH has a relationship with Augie Busch, although I do not believe that Anheiser has come through on its dollar commitment to the DNC (I'll double check on that, so please don't report this as fact. Also, remember the Terry McAullife connection to Busch through Gephardt)
5. In any event, I hope next week to have a discussion with Truman Arnold and Debra DeLee re: our interest. Would appreciate your checking it out on your end to see if there are other traps to go through.
6. We gave 50k this calendar year.

ONE OTHER THING

I'd like to talk to Harold re: reported conversation that POTUS had with Gov. Chiles re: suits that Fla., West Va. Miss., Minn. have filed against the tobacco industry.

AS ALWAYS. THANK YOU VERY MUCH!!!!

4/16/95 - J - I don't understand what we need to check out, especially if she is going to meet w/ Truman & Debra - ?

↑
 Your support because of relationship(s) with Anheiser - Busch.

May 20, 1995

5 fates
1.1 gahr

MEMORANDUM FOR HAROLD ICKES

FROM: JENNIFER O'CONNOR

SUBJECT: TOBACCO

John Emerson recommends we not get involved in the tobacco lawsuit that Chile is filing because it would put us on the other side of other Governors. For instance Governor **Hunt** of NC and **Jones** of KY are both opposed to lawsuit against tobacco companies to win medicaid and medicare cost reimbursement. In addition, although West Virginia is also suing tobacco companies on this theory, Governor **Caperton** is opposed to his own Attorney General for doing so.

THE WHITE HOUSE
WASHINGTON

Jerry O'Connor
Litigation

August 18, 1995

TO: Harold Ickes
Erskine Bowles

From: Chris *CR*

Re: Tobacco Litigation

I met this morning with the DOJ litigators who are handling the three tobacco cases that have been filed (two in Greensboro, N.C. and one in Tennessee). They report the following:

1. Since none of the plaintiffs filed a motion for a TRO or preliminary injunction, our first responsive pleading is not due until October 10th.

2. If someone does file a preliminary injunction motion, we would have 20 days to respond.

3. Our first filing would be a motion to dismiss on grounds of ripeness, i.e., that their suit is premature until the final rule has been issued.

4. Although the ripeness argument should prevail, there are no guarantees considering the judge we drew in North Carolina.

5. Given the risks, DOJ is not inclined to file the motion to dismiss until the end of the filing period (early October).

I agree with this recommendation.

DEPARTMENT OF HEALTH & HUMAN SERVICES
OFFICE OF THE GENERAL COUNSEL

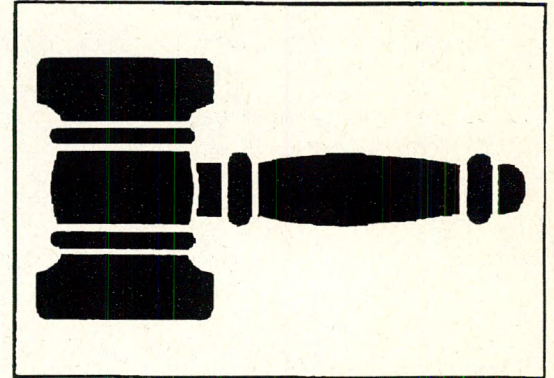
*tabacco
litigation*

PHONE: (202) 690-6318

FAX: (202) 690-7998

DATE: May 6, 1996

TO: JEN O'CONNOR



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

COMMENTS: Just wanted to make sure you were aware of this latest filing.

No. of Pages (including cover): 4

IN THE UNITED STATES DISTRICT COURT FOR THE
MIDDLE DISTRICT OF NORTH CAROLINA
GREENSBORO DIVISION

CIVIL ACTION NO. 2:95CV00593

AMERICAN ADVERTISING FEDERATION;)
AMERICAN ASSOCIATION OF)
ADVERTISING AGENCIES, INC.;)
ASSOCIATION OF NATIONAL)
ADVERTISERS, INC.; MAGAZINE)
PUBLISHERS OF AMERICA;)
OUTDOOR ADVERTISING ASSOCIATION)
OF AMERICA; POINT OF PURCHASE)
ADVERTISING INSTITUTE;)

Plaintiffs,)

v.)

DAVID A. KESSLER,)
Commissioner, Food and Drug)
Administration; UNITED STATES FOOD)
AND DRUG ADMINISTRATION; AND)
DONNA SHALALA, Secretary,)
U.S. Dept. of Health and)
Human Services;)

Defendants.)

**NOTICE OF ADDITIONAL FACTS RELATING TO THE FDA RULEMAKING TO
REGULATE ADVERTISING OF TOBACCO PRODUCTS**

In light of the Notice filed by the Defendants concerning the FDA's rulemaking proceeding, Plaintiff advertisers hereby notify the Court of recent remarks by the President of the United States relating to the administration's commitment to FDA jurisdiction over tobacco advertising, and of recent actions by several state attorneys general demonstrating that the FDA's assertion of jurisdiction has already had a substantial regulatory impact. Plaintiff advertisers also call the Court's attention to a recent decision of the D.C. Circuit, permitting immediate judicial

review of plaintiff's challenge to the absence of any authority to issue an executive order that was to be implemented by agency regulations.

On March 25, 1996, President Clinton underscored the finality of the Administration's decision that the FDA regulate cigarette advertising. The President, addressing a meeting of the state attorneys general, stated:

[W]e believe we must act much more strongly to make cigarettes less accessible and to make children less subject to the lures of the advertising. And in that connection, I know that 27 of you wrote to the FDA in support of those objectives. I want to thank you for that. It seems to me that all the evidence clearly indicates that we have to continue to move on this front.

See Attachment A. On March 20, 1996, the President, made a similar commitment in comments to Advocates Against Youth Smoking. See Attachment B.

Other recent events further demonstrate the regulatory impact of the FDA's assertion of jurisdiction. As shown in Attachment C, several state attorneys general, relying on the FDA's purported authority to regulate cigarette advertising, have compelled a major cigarette manufacturer to comply with a number of the FDA's proposed advertising restrictions in the settlement of product liability claims. This effect is similar to the regulatory impact relied upon by this Court in its finding of finality in *Flue-Cured Tobacco Co-op. v. U.S. E.P.A.*, 857 F. Supp. 1137 (M.D.N.C. 1974), where the U.S. Postmaster, without direct regulatory compulsion, relied on the EPA report to ban smoking in postal facilities.

Plaintiff advertisers also reference for the Court's attention a recent decision of the D.C. Circuit that followed *Leedom v. Kyne*, 385 U.S. 184 (1958), and precluded judicial review of a claim that the President lacked statutory authority to issue an Executive Order barring federal contracts with firms hiring replacement workers. *Chamber of Commerce of U.S. v. Reich*, 74

F.3d 1322, 1327-1328 (D.C. Cir. 1996). The suit had been filed prior to the promulgation of implementing regulations by the Department of Labor. The court relied on its inherent right to determine the limits of executive authority and not on any statutory review provision. *Id.* In an earlier decision in the same case, the D.C. Circuit had held that the suit was ripe, finding "no institutional interest in deferring review" of the claim that the executive action was *ultra vires*. *Chamber of Commerce v. Reich*, 57 F.3d 1099, 1100 (D.C. Cir. 1995).

Respectfully submitted,

Eric C. Rowe

C. Allen Foster (NC State Bar No. 1499)
Eric C. Rowe (NC State Bar No. 10713)
PATTON BOGGS, L.L.P.
P.O. Drawer 20004
Greensboro, N.C. 27420
(910) 273-1733

Garrett G. Rasmussen by Eric C. Rowe
Garrett G. Rasmussen
PATTON BOGGS, L.L.P.
2550 M St. N.W.
Washington, D.C. 20037
(202) 457-6347

Ernest Gellhorn by Eric C. Rowe
Ernest Gellhorn
2907 Normansstone Lane, N.W., Suite 100
Washington, D.C. 20008-2725
(202) 319-7104

ATTORNEYS FOR PLAINTIFFS

April 30, 1996



U.S. Department of Justice

Office of the Assistant Attorney General
Civil Division

Litigation

George J. Phillips
Counselor to the Assistant Attorney General

10th & Constitution Ave., N.W., Room 3143
Washington, D.C. 20530
(202) 514-5713
Fax (202) 514-8071

November 20, 1995

VIA FACSIMILE
(202) 456-2146

Christopher Cerf
Associate Counsel to the President
OFFICE OF COUNSEL TO THE PRESIDENT
Room 136
Old Executive Office Building
Washington D.C. 20500

VIA FACSIMILE
(202) 690-7998

Harriet S. Rabb, General Counsel
DEPARTMENT OF HEALTH AND HUMAN SERVICES
Room 722A Humphrey Building
200 Independence Ave., S.W.
Washington, D.C. 20201

VIA FACSIMILE
(301) 443-0739

Margaret Porter
Chief Counsel
FOOD AND DRUG ADMIN.
5600 Fishers Lane
Rockville, Maryland 20857

VIA FACSIMILE
(301) 443-0739

Eric M. Blumberg
Deputy Chief Counsel
FOOD AND DRUG ADMIN.
5600 Fishers Lane
Rockville, Maryland 20857

RE: Am. Advertising Federation, et. al. v. FDA, et. al.
M.D. N.C. (Osteen), Case No. 2:95CV00593

Dear Mr. Cerf, Ms. Raab, Ms. Porter and Mr. Blumberg:

At the end of last week we got a phone call from Garret Rasmussen of Patton Boggs who represents the Advertisers. He requested that the government consent to adding the following North Carolina Congressmen as plaintiffs: Charlie Rose, Howard Coble, Charles Taylor, David Funderburk, Walter Jones and Cass Ballenger.

We intend to tell them that we would not consent to the addition of these plaintiffs and that we would likely oppose their motion to do so on the grounds that these Congressmen do not have the requisite standing to be added as plaintiffs. The Justice Department routinely opposes parties being added which do not have standing whether they are Congressmen or otherwise. We are waiting to hear from FDA whether they agree with this proposed response.

Sincerely,

George J. Phillips



Office of the Attorney General
State of Texas

DAN MORALES
ATTORNEY GENERAL

FOR IMMEDIATE RELEASE
THURSDAY, MARCH 28, 1996
512-463-2050

CONTACT: RON DUSEK(rdusek@oag.state.tx.us)
WARD TISDALE(wtisdale@oag.state.tx.us)
SONYA SANCHEZ(ssanchez@oag.state.tx.us)

**TEXAS CHARGES TOBACCO INDUSTRY WITH VIOLATIONS
OF FEDERAL RACKETEERING LAWS**
State Aims To Recoup Billions

Texas Attorney General Dan Morales on Thursday filed a multi-count federal lawsuit in United States District Court against the nation's largest tobacco companies, alleging, among other grounds, violations of the federal Racketeer Influenced and Corrupt Organizations (RICO) Act.

The Texas suit marks the first official governmental allegation that the industry has engaged in illegal conduct, including, but not limited to, violations of federal mail fraud statutes, wire fraud statutes, federal racketeering laws and federal conspiracy laws. The Texas suit also alleges violations of state and federal antitrust laws and public nuisance laws.

The suit alleges that for decades the tobacco industry deliberately, maliciously and deceitfully caused the addiction of millions of persons to tobacco products through the manipulation of nicotine impact levels. The tobacco industry also shamelessly targeted advertising at children to create new users of cigarettes and smokeless tobacco products to replace those adult users dying from various tobacco-related diseases.

The result of the tobacco industry's lawless and immoral activities has been millions of deaths and debilitating diseases. The lawsuit seeks an end to advertising targeted at children, plus billions of dollars in restitution from the tobacco industry for health care costs for Texans who received treatment under Medicaid.

"The tobacco industry has violated the law for so long and in so many ways, it has become standard operating procedure," Morales said. "History will record the modern-day tobacco industry alongside the worst of civilization's evil empires."

-more-

MORALES 2-2-2

"This lawsuit is not an effort to ban smoking by adults. Adults can make mature choices when presented with the truth. We want the tobacco industry to leave our impressionable children alone. We also want them to stop secretly manipulating the nicotine impact levels in cigarettes and smokeless tobacco products; and, we want them to pay for the damaged lives they leave behind on the way to the bank."

The lawsuit was filed in U.S. District Court in Texarkana against The American Tobacco Company, Inc.; R.J. Reynolds Tobacco Company; Brown & Williamson Tobacco Corporation; B.A.T. Industries P.L.C.; Philip Morris, Inc.; Liggett Group, Inc.; Lorillard Tobacco Company, Inc.; United States Tobacco Company; Hill & Knowlton, Inc.; the Council for Tobacco Research-USA, Inc. (successor to Tobacco Institute Research Committee); and Tobacco Institute, Inc.

Morales has contracted with five highly successful law firms with extensive experience in complex litigation to assist with the lawsuit on a contingency fee basis. The private law firms will receive 15 percent of the jury award against the tobacco industry. That is half of what the other states are paying their lawyers in similar litigation. The State of Texas should receive 100 percent of its share of Medicaid costs because the federal government will pay the state a 15 percent incentive payment for collecting its share of Medicaid costs.

Attorneys participating in the litigation include two of the preeminent legal scholars in the country, law professors Laurence Tribe and Arthur Miller of Harvard Law School. The legal team also includes Walter Umphrey of Beaumont; John O'Quinn of Houston; John Eddie Williams Jr. of Houston; Wayne A. Reaud of Beaumont; Harold W. Nix of Daingerfield; and Hugh E. McNeely of Port Arthur.

Morales alleges multiple causes of action in the lawsuit, including violations of the federal Racketeer Influenced and Corrupt Organizations Act (RICO), state and federal antitrust laws, conspiracy, fraud, liability for a defective and dangerous product, breach of warranty and public nuisance.

The Attorney General said the evidence against the tobacco industry comes primarily from the industry's own documents, research and former employees. He said the evidence shows that the industry has known for decades that nicotine causes addiction and that combined with the more than 40 other carcinogenic compounds in tobacco smoke, causes cancer and other respiratory diseases.

-more-

MORALES 3-3-3

Morales said the evidence also shows that the tobacco industry conspired to suppress the development of a safer cigarette.

The evidence reveals that the industry hired a public relations firm (Hill & Knowlton) to organize a propaganda campaign against the growing body of evidence that tobacco was harmful; that it created a so-called "health research" arm (Council for Tobacco Research) for propaganda purposes, but stifled and even hid research in foreign countries that showed the harmful effects of smoking.

The tobacco industry's own documents indicate that it created high-potency tobacco plants and calculated precisely how much nicotine was necessary to addict an average smoker.

Morales also alleges that the tobacco industry has targeted young America, teenagers, with its advertising campaign. Statistics show that most smokers begin smoking as children. Statistics also show that once a person reaches adulthood, he or she is less likely to begin smoking, and those who do start smoking as adults, do not remain smokers as long.

The Attorney General provided statistics showing that:

- * nationally, healthcare costs associated with smoking was \$97 billion in 1994;
- * the number of preventable deaths in Texas in 1993 attributed to smoking is 25,900 compared to the next highest preventable death rate of 3,184 from auto accidents;
- * nationally, children purchase \$1.26 billion in tobacco products each year;
- * the success rate for children who try to buy cigarettes from vending machines is more than 90 percent in Texas;
- * 43 percent of Texas high school students who have tried smoking, started at age 12 or younger;
- * the tobacco industry addicts 3,000 children each day.
- * Joe Camel is as familiar to six-year-olds as is Mickey Mouse.

"It is time to fight back. It is time for the tobacco industry to face a jury armed with the facts. We have no doubts that a jury will find the tobacco industry guilty of deliberately targeting children and causing the addiction and subsequent deaths or debilitating disease of thousands of Texans, and costing taxpayers billions of dollars in Medicaid expenses.



Statement by Attorney General Dan Morales

This morning my office filed a 10-count federal lawsuit in United States District Court against the nation's largest tobacco companies.

For decades, the tobacco industry has denied responsibility for the harm its products cause. They argue that their customers freely choose to use tobacco. But freedom of choice is not at issue. The real issue is that no individual, no company, and no industry is above the law.

If you are an adult and you choose to smoke, that's your business. But when the tobacco industry blatantly violates Texas law, that's our business.

We intend to prove to a Texas jury, that the tobacco industry knowingly and deliberately engaged in illegal conduct, including violations of federal mail fraud and wire fraud laws, federal racketeering and conspiracy laws, state and federal antitrust laws, consumer protection laws, and other state and federal laws.

The people of Texas are seeking to recover more than \$4 billion dollars in Medicaid costs incurred due to cigarettes and other tobacco products. We will show that executives of these corporations conspired to amass profits from a product designed to cause mass addiction, an addiction they know results in disease and death.

We will prove that these companies deliberately suppressed data proving nicotine is addictive. We will prove that while they publicly denied the addictive properties of nicotine, their own internal documents show they were lying.

We will prove that the tobacco industry's own research groups served as fronts, whose sole purpose was to distort medical and scientific facts, and discredit respected scientific researchers and public health officials. And we will prove that the cigarette companies suppressed research to make a safer cigarette.

For 40 years the tobacco industry has spent billions of dollars and employed armies of lawyers and public relations firms, in their increasingly desperate efforts to shirk their responsibility.

In Texas, the cigarette companies filed a frivolous lawsuit which claims that any effort on our part to hold them responsible for the billions of dollars they have cost our state would violate their constitutional rights.

This type of nonsense may have been successful for the tobacco industry elsewhere, but it will not work here. No one has the constitutional right to violate our laws or shirk responsibility for one's behavior. The cigarette companies like to brag that they've never lost a lawsuit. But they're suing Texas now, and we don't like to lose either.

We want every business in Texas to understand that we're not suing the tobacco industry because we're anti-business. We're suing the tobacco industry because they repeatedly and flagrantly broke state and federal laws. Any business that conducts itself in a similar fashion should expect to suffer the same consequences.

When all the evidence is presented to a Texas jury, it will become clear that the tobacco industry has violated every standard of ethical business practice, betrayed every public promise, and sold out their customers and their country.

We will show that the tobacco industry systematically targets kids, to addict them to cigarettes, before they are old enough to make mature, responsible, adult decisions. It is no accident that Joe Camel is as widely known to elementary school students as Mickey Mouse. It is no accident that 82% of adult smokers began as children.

The truth is that the tobacco industry's marketing campaign to children is no Mickey Mouse operation. They saturate stores near public schools with cigarette promotions, and continue to resist all efforts to ban vending machine cigarette sales because they know that's how most kids purchase cigarettes.

Each year, the tobacco industry must find 25,000 new Texans to replace those who died from using their products. And the overwhelming majority of those new customers are our children. Let me be clear: more than anything else, what we want from the tobacco industry is to LEAVE OUR CHILDREN ALONE.

As recently as 1994, the chief executive officers of the nation's largest tobacco companies testified under oath in Congress that cigarettes don't cause cancer, that nicotine is not addictive, and that the tobacco companies do not manipulate nicotine levels to ensure the addiction of their customers. Their own internal documents prove they were lying.

Although the tobacco industry continues to deny that they conspired to break our laws, we now have a smoking gun. Literally thousands of pages of previously-concealed industry information and internal memos have been made public. Those documents trace this conspiracy back to 1953, when Big Tobacco

first learned that cigarette smoke causes cancer. For 40 years, the industry has employed code names, clandestine operations and secret files to hide the truth from their customers.

We anticipate that the tobacco industry will wage a very public disinformation campaign about this case. Just remember, no medical group, no health group, no citizens group, and no business group in Texas will oppose our lawsuit unless they are being paid by the tobacco companies.

The day of reckoning is at hand. It is time for the tobacco industry to face a jury armed with the facts. We are confident that the jury will see through the tobacco industry's smoke screen and decide the time has finally come for these dealers in death to pay for the pain and suffering they have caused us all.



U.S. Department of Justice

Office of the Assistant Attorney General
Civil Division

to: J.O. Conrad

George J. Phillips
Counselor to the Assistant Attorney General

10th & Constitution Ave., N.W., Room 3143
Washington, D.C. 20530
(202) 514-5713
Fax (202) 514-8071

April 12, 1996

State
lawsuits

HAND DELIVERY

Mr. Christopher Cerf
Associate Counsel to the President
Office of Counsel to the President
Old Executive Office Building, Room 136
Washington, D.C. 20500

Dear Chris,

Enclosed are two preliminary and draft memorandums. One is a review of the Liggett settlement and the other summarizes the status of the state lawsuits. HHS (HCFA) is still assessing the Liggett settlement in terms of whether the federal government has any claim to any portion of the money being paid to the states pursuant to existing recoupment agreements that Medicare/Medicaid has with the states.

Sincerely,

George J. Phillips

Enclosures

DRAFT~~CONFIDENTIAL~~**DRAFT**

SUMMARY OF THE STATES' LAWSUITS AGAINST THE TOBACCO INDUSTRY
(4/12/96)

DETERMINED TO BE AN ADMINISTRATIVE

General

MARKING INITIALS: *N* DATE: *3/2/21* *2021-0267 S*

To date, seven states have filed lawsuits against the major tobacco companies in an effort to recover health care costs stemming from smoking-related illnesses. The states that have brought lawsuits are: Mississippi, Minnesota, West Virginia, Louisiana, Massachusetts, Florida, and Texas. Five states (Mississippi, West Virginia, Florida, Louisiana, and Massachusetts) have settled their lawsuits with one of the tobacco companies, Liggett Group, Inc. None of the other tobacco companies have settled with any of the states.

Mississippi

On May 23, 1994, Mississippi became the first state to sue the tobacco industry. Discovery is now underway. However, Governor Kirk Fordice has publicly denounced the litigation against the industry, and has taken legal action to prevent Attorney General Mike Moore from continuing with the lawsuits. Apparently in reliance on the governor's position, the tobacco companies have filed a motion to dismiss the action, which is currently pending before the trial court.

Minnesota

Minnesota sued the tobacco companies on August 17, 1994. An early attempt by the industry to dismiss several of the state's claims was rejected by the trial court. Discovery is currently ongoing. Although Minnesota participated in the negotiations for the Liggett settlement, the state ultimately chose not join the settlement. The attorney general stated that the terms were too favorable for Liggett.

West Virginia

West Virginia filed its lawsuit against the tobacco industry on September 20, 1994. In May 1995, the trial court dismissed most of the state's causes of action on the basis that the attorney general lacked the authority to sue under the common law unless the governor authorizes it. Governor W. Gaston Caperton has opposed the litigation. In October 1995, the trial court also ruled that the state cannot pay private attorneys on a contingency fee basis for their assistance in litigating the tobacco case. The state is seeking appellate review of these results.

DRAFT

~~CONFIDENTIAL~~

DRAFT

Florida

Prior to filing suit, the Florida legislature enacted a law which would facilitate an attempt by the state to recover its health care costs from the tobacco industry. The law removed several of the tobacco industry's key defenses (e.g. comparative negligence), allowed the state to file a class action, and sanctioned the use of a market share theory of liability and statistical evidence. Thereafter, the state filed its lawsuit on February 21, 1995. The tobacco companies quickly challenged the constitutionality of the legislation. Consequently, the lawsuit had been stayed by the trial court pending a ruling on the constitutional issues from the Florida Supreme Court. Briefing and oral arguments are complete and a ruling is expected soon. Last month, the trial court partially lifted the stay to set a scheduling order for some pretrial activities. Lawyers for the various tobacco companies have stated that they will move to dismiss the action.

Apart from the legal challenges to the Florida legislation, the tobacco companies also attempted to have the law repealed. Their efforts have failed for now because in March, the Florida Senate declined to repeal the law.

Massachusetts

The Massachusetts lawsuit was filed on December 19, 1995. Prior to the attorney general filing suit in state court, the tobacco companies attempted to block the litigation by filing a declaratory judgment action in federal court in November 1995. The companies argued that the (then anticipated) state lawsuit would violate various provisions of the United States Constitution. As with Florida, the Massachusetts legislature had enacted a special law allowing the attorney general to sue to recover health care costs. The state has moved to dismiss the action filed by the tobacco companies. Earlier this year, the tobacco companies removed the state court action to federal court. Massachusetts then moved to remand the case to state court and this motion is still pending.

Louisiana

Near the time that several of the states were settling their claims with the Liggett Group, Inc., Louisiana filed its lawsuit on March 13, 1996. As with the governors of Mississippi and West Virginia, Governor Mike Foster of Louisiana opposes the lawsuit. Governor Foster has convened a special session of the state legislature, partially in an attempt to preclude his attorney general from pursuing the litigation. There will probably not be much progress with Louisiana's lawsuit until after the legislature has completed its special session.

DRAFT~~CONFIDENTIAL~~**DRAFT***Texas*

The most recent state to file a lawsuit was Texas, whose lawsuit was commenced on March 28, 1996. Governor George W. Bush has indicated his support for the attorney general's decision to sue the tobacco companies. As with the Massachusetts litigation, the tobacco industry attempted to stop the lawsuit before it began by first filing a declaratory judgment action in state court on November 28, 1995. The companies allege that the attorney general lacks authority under state law to proceed with the suit to recover health care costs. The state court action by the industry has not yet been resolved.

A tabular summary of the seven lawsuits is provided below.

TABLE 1: SUMMARY OF CURRENT STATE LAWSUITS AGAINST THE TOBACCO INDUSTRY

STATE	FILING DATE	GUBERNATORIAL POSITION	CURRENT STATUS	PARTY TO LIGGETT SETTLEMENT
Mississippi	2/23/94	Opposes lawsuit	Pending motion to dismiss; discovery underway	Yes
Minnesota	8/17/94	Favors lawsuit	Discovery underway	No
West Virginia	9/20/94	Opposes lawsuit	Case on hold after successful motions by tobacco industry; pending appeal by state of dismissal of claims	Yes
Florida	2/21/95	Favors lawsuit	Challenge to statute pending before state supreme court; case partially stayed.	Yes
Massachusetts	12/19/95	Unknown	Pending decl. judg. action by industry	Yes
Louisiana	3/13/96	Opposes lawsuit	Recently filed	Yes
Texas	3/28/96	Favors lawsuit	Pending decl. judg. action by industry	No



U. S. Department of Justice

Civil Division

DRAFT

~~CONFIDENTIAL~~

DRAFT

Office of the Assistant Attorney General

Washington, D.C. 20530

April 12, 1996

DETERMINED TO BE AN ADMINISTRATIVE

MARKING INITIALS: M DATE: 3/2/96

7024-0267-5

MEMORANDUM

TO:

[REDACTED]

FROM:

George J. Phillips
Counselor to the Assistant
Attorney General

[REDACTED]

SUBJECT: Analysis of Liggett Corporation's Settlement of Tobacco Lawsuits

The Federal Tort Claims Act Staff of the Torts Branch has prepared the following summary and analysis of the settlement agreement that the Liggett Group, Inc. ("Liggett"), has entered into with the various state attorneys general. (Attachment 1) We have also included some preliminary comments regarding certain aspects of the agreement.

General Features of the Settlement

To date, seven states have filed lawsuits against the major tobacco companies in an effort to recover health care costs stemming from smoking-related illnesses.¹ On March 15, 1996, one the tobacco companies, Liggett Group, Inc. (and its related companies) entered into a settlement with the following states: Mississippi, West Virginia, Florida, Massachusetts, and

¹ They are Mississippi, Minnesota, West Virginia, Louisiana, Massachusetts, Florida, and Texas.

DRAFT**DRAFT**

Louisiana. *See* Attorneys General Settlement Agreement at 1 ("Setl. Agmt.").² The settlement anticipates that other states and tobacco companies may subsequently choose to join the agreement, but if they do so, they will be governed by somewhat different terms than the initially settling parties. *See infra*. Although Liggett's decision to settle these cases is unprecedented for a tobacco company, Liggett expressly does not admit any wrongdoing or legal liability based on the states' contentions, nor does it concede that the FDA has jurisdiction to regulate cigarettes. (Setl. Agmt. at 3, ¶ 2.2.)

There are two main features of the settlement agreement: first, Liggett agrees to abide by selected provisions of the FDA's proposed rules regarding the sale and advertising of cigarettes; and second, the agreement creates and funds an "Attorney General Settlement Fund" for use by the states to defray their health care costs caused by smoking-related illnesses.

At the time of the settlement, it was reported that the majority shareholder of Liggett, Bennett LeBow, was hoping that the settlement would improve his chances for a corporate take-over of R.J. Nabisco. The settlement agreement addresses this scenario. If Liggett fails to merge with another company within three years, Liggett must pay an additional \$5 million. (Setl. Agmt., ¶ 5.10.) Moreover, if another company merges with Liggett, the "future affiliate" will need to pay additional sums under the agreement, but will be accorded the more favorable status that Liggett has vis-a-vis the other non-settling tobacco companies. (Setl. Agmt. at 8, ¶ 16.)

Advertising Limitations

On August 11, 1995, the FDA published for comment proposed regulations concerning the sale and distribution of tobacco products to children and adolescents. *See* 60 Fed. Reg. 41314 (1995) (to be codified at 21 C.F.R. pt. 801). Liggett has agreed to withdraw its objections to FDA's jurisdiction to issue the proposed rules. (Setl. Agmt., ¶ 4.1.) However, Liggett may object to the proposed rules insofar as their compliance is "impractical or excessively expensive." (Setl. Agmt., ¶ 4.1.) In addition, Liggett will ultimately be bound by the rules only to the extent that they become enforceable obligations. (Setl. Agmt., ¶ 4.2.)

Liggett's compliance with the FDA's proposed rules is qualified in many respects. *See* Setl. Agmt., ¶ 4.2.1 - 4.2.9 and Attachment 2. For example, Liggett has not agreed to establish a national public educational program to discourage minors from smoking. *Compare* 60 Fed. Register 41374, § 897.29 *with* Setl. Agmt., ¶ 4.2. Liggett must commence compliance with the rules "as soon as reasonably practicable" but its efforts are limited because Liggett need not incur a loss of more than \$1 million in net annual out-of-pocket costs as a result of the rules. (Setl. Agmt., ¶ 4.3.) Liggett will eliminate from its advertising cartoon characters such as "Joe

² Liggett also settled a class action suit brought by private individuals. *See* Attachment 3, Summary of Settlement Agreement in *Castano, et al. v. American Tobacco Co., et al.*, Civ. No. 94-1044 (E.D. La.).

DRAFT~~CONFIDENTIAL~~**DRAFT**

Kool" which target younger audiences. (Setl. Agmt., ¶ 4.5.) Finally, as opposed to Liggett, other companies that later settle must pay \$250,000 per year, per state, for a period of three years, to fund efforts to monitor compliance with the advertising rules. (Setl. Agmt., ¶ 4.6.)

Comment: The Office of Consumer Litigation has prepared a summary of the provisions of the FDA's rules that will be binding on Liggett. See *Attachment 2*. Liggett will ultimately only need to comply with the rules if they are enacted. Thus, if the rules are never finalized, withdrawn, or deemed beyond the scope of FDA's jurisdiction, Liggett need not comply with them. Resolution of the proposed rules may take some time; the states have secured at least a temporary compliance by Liggett. Yet because Liggett's market share is only 2.5%, the practical effect may be minimal. As explained above, Liggett's monetary risk for non-compliance is limited to \$1 million. Finally, Liggett retains the right to object to rules to the extent that it determines they are "impractical or excessively expensive." By these terms, Liggett has negotiated discretion for how it will comply with the proposed rules and has left open its option to challenge the rules through administrative or legal action.

Attorneys General Settlement Fund

Apart from the adherence to the FDA rules, the second major component of the settlement is the establishment of a general fund to repay the states a portion of their health care costs. The agreement creates an "Attorney General Settlement Fund", to be administered by an "Attorney General Board." (Setl. Agmt., ¶ 5.1, 5.2.)³

The monetary contribution of Liggett to the fund comprises a lump sum and an annual payment for 25 years. Liggett shall pay into the fund \$5 million over nine years. (Setl. Agmt., ¶ 5.3.) In addition, Liggett will pay a sum that is apparently derived from its share of the tobacco market. Specifically, Liggett will contribute to the fund 2.5% of its pretax income per year beginning in the second year for the duration of the agreement (for the benefit of the

³ On March 12, 1996, Liggett settled the class action in *Castano*. Apart from administering the states' settlement, the board will also oversee a research fund contemplated by the *Castano* settlement if that settlement is terminated. (Setl. Agmt., ¶ 5.9)

DRAFT

~~CONFIDENTIAL~~

DRAFT

initially settling states).⁴ (*Id.*) For subsequently settling states that join the agreement, Liggett will pay an amount based on a specified formula.⁵

If Liggett eventually merges with another company, there will be additional payments. The future affiliate of Liggett shall pay \$135 million into the fund for use by the initially settling states, and "make available" an amount up to \$25 million to be paid at the direction of the Attorneys General Board for the benefit of any subsequently settling states. (Set. Agmt., ¶ 5.4.) The future affiliate will contribute 2.5% of its pretax income to the fund (for initially settling states) and for the benefit of subsequent settling states pay an amount based on a specified formula. *See* Footnote 5. (Setl. Agmt., ¶ 5.5.)

In consideration of amounts to be paid by Liggett, the states will dismiss all of their present claims against Liggett. (Setl. Agmt., ¶ 6.1.)

Comment: It is unclear how the amount that Liggett has agreed to pay compares with the smoking-related health care costs that the five states attribute to Liggett's products (in other words, is Liggett going to pay its "fair share"?). The fund is to be administered by a board of the attorney generals of the settling states. The settlement agreement is silent as to the board's organization, the method of apportionment of the funds among the states, and the general operating procedures (e.g. how often funds will be disbursed, dispute resolution among the states, etc.). The settlement alludes to future agreements between the states that may address these issues. In addition, the creation of the board raises a question concerning the federal government's right to the fund's proceeds. To the extent that the United States may bring a claim for any of the funds paid by Liggett, the United States seemingly may seek recovery from the board, the individual states, or, where authorized, by administrative action on the part of HHS. While the creation of the fund with an overseeing board resembles the well-established legal mechanism of a revocable trust (with the board acting as the trustee and the states' citizens as the indirect

⁴ The Wall Street Journal reported that this amounts to approximately \$250,000/yr., and the total deal is worth \$41 million from Liggett alone. Milo Geyelin, Liggett, Five States Set Pact Covering Treatment of Smoking-Related Illnesses, Wall Street Journal, March 18, 1996, at A3. This percentage (2.5) may change if Liggett's market share increases or decreases. (Setl. Agmt., ¶ 5.8.)

⁵ The amount equals the product of (i) the ratio of Medicaid population of the state to a Medicaid population of 10 million reduced by the Medicaid population of the initial settling states and (ii) 5% of Liggett's pretax income. This amount cannot exceed 5% of Liggett's pretax income. (Setl. Agmt., ¶ 5.3)

DRAFT~~CONFIDENTIAL~~**DRAFT**

beneficiaries), the parties clearly did not intend to set up a trust estate or a trust relationship.

Termination and Other Rights

The agreement provides for a right of offset. If a settling state obtains a monetary judgment against a non-settling defendant (e.g. another tobacco company), then each settling defendant can reduce its payments according to a prescribed formula.⁶ (Setl. Agmt., ¶ 5.6.) Liggett also would be able to credit against the amount it must pay each year a percentage of its expenses incurred in defending other smoking-related litigation. (Setl. Agmt., ¶ 5.7.) Liggett can terminate the agreement if the difference in what it paid before and after the agreement for smoking-litigation expenses exceeds twenty-five (25) per cent of the amount it has to pay under the agreement. (Setl. Agmt., ¶ 5.7.)

The time period for the settlement is twenty-five (25) years. However, Liggett can terminate the agreement, with respect to a particular state, if a full and final dismissal as to any of the tobacco companies is entered in that state. (Setl. Agmt., ¶ 8.2.) In addition, Liggett can terminate the entire agreement if it determines, "in its sole and exclusive discretion," that "too many states" have filed actions and have not agreed to be bound by the settlement agreement. (Setl. Agmt., ¶ 8.3.) To allow the states to resurrect their lawsuits, the statute of limitations would be tolled in the event that Liggett chose to terminate the agreement. (Setl. Agmt., ¶ 8.5.)

With regard to dispute resolution, the parties have agreed that each state's respective law will apply to the agreement as it affects that state and that certain terms will be submitted to binding arbitration (e.g. calculation of market share or pretax income). (Setl. Agmt., ¶¶ 14, 16.5.) Liggett has also agreed to cooperate with the states in their discovery efforts and to provide any information it has concerning efforts by the other tobacco companies efforts to mislead or defraud the attorneys general in pursuing their actions. (Setl. Agmt., ¶ 16.12.)

Finally, in recognition of Liggett being the first tobacco company to enter a settlement such as this one, the states have included a "most favored nation" clause. (Setl. Agmt., ¶ 15.) By this clause, the states agree to apply a multiplier to other settlements they may reach with other tobacco companies so that Liggett's payments are relatively less. If a state agrees to more favorable terms with another tobacco company, Liggett can modify or replace the relevant terms in its agreement. (Setl. Agmt., ¶ 15.2.) The parties also agreed that Liggett's settlement should bar other tobacco companies from seeking contribution or indemnity from Liggett. (Setl. Agmt., ¶ 10.1.)

⁶ Liggett would have the right to reduce its payments to make the present value of the amounts it has paid, per percentage point of its then market share, no more than 75% of the present value of the judgment amount, per percentage point of the market share of the non-settling defendant. (Setl. Agmt., ¶ 5.6.)

DRAFT

~~CONFIDENTIAL~~

DRAFT

Comment: Liggett has retained several escape hatches to allow it to rescind the agreement --- most notably if it determines in its own discretion that too many other states who have sued do not join the agreement. Of the initial states that sued the tobacco companies, Minnesota is the only one that has rejected the settlement. Although Minnesota participated in the negotiations, the state attorney general for Minnesota viewed the settlement as too lenient for Liggett. Liggett has capped its liabilities with the initially settling states and can later take advantage of any legal victories by the other tobacco companies by terminating the agreement. While Liggett does receive many benefits, it is the smallest of the big six tobacco companies (in terms of market share). Thus, the lion's share of the potential recovery against the industry would not be diminished by these favorable terms. Regardless of the states' and Liggett's intention, the right of other tobacco companies to seek contribution or indemnity accordingly will be governed by the applicable state law. Strategically, the states have accomplished a quick, and unprecedented, settlement that may damage the aura of invincibility of the tobacco industry. Practically, the amount of money recouped in comparison to the health care costs for smoking-related illnesses paid (and to be paid) by these states seems relatively small, unless Liggett is bought by a larger cigarette manufacturer.

Conclusion

The settlement agreement has many special features, perhaps most notably the creation of the Attorneys General Fund (and Board). In exchange for securing Liggett to break ranks with the other tobacco companies, the states have provided Liggett with favorable settlement terms. Since the settlement, Texas has filed suit and Maryland may soon follow. Because the other tobacco companies will probably not be able to obtain similar terms and have much more at stake in terms of market share, the states will probably face very expensive litigation that will continue for the foreseeable future.

[REDACTED]

DRAFT

~~CONFIDENTIAL~~

DRAFT

ATTACHMENT 2

LIGGETT COMPLIANCE WITH FDA'S PROPOSED REGULATIONS

Pending FDA's final action on its proposed regulations, Liggett has agreed in its Settlement Agreement with five states to abide by the proposed regulations listed below to the extent indicated⁷:

Section 897.16(a)

FDA Proposal--No use of trade or brand name of non-tobacco product as trade or brand name of tobacco product (i.e., no Gucci cigarettes).

Liggett Compliance--Limited to non-tobacco trade or brand names in use in the United States and having a "demonstrated likelihood to appeal to minors" (disputes to be submitted to binding arbitration with Liggett having the burden to show compliance).

Section 897.16(b)

FDA Proposal--No sale or distribution of cigarettes in packages containing fewer than 20 cigarettes.

Liggett Compliance--Full compliance.

Section 897.16(d)

FDA Proposal--No distribution of free samples of cigarettes or smokeless tobacco products.

Liggett Compliance--May distribute free samples "under circumstances where no minors are present or likely to be present."

⁷ The settlement is further limited as follows: Liggett apparently has not agreed to abide by any of FDA's proposed regulations except those specifically listed in the Settlement Agreement. The compliance to which Liggett has agreed is expressly limited to "net annual out-of-pocket cost" to Liggett of \$1 million. Liggett is to accord priority in its compliance efforts to the states which are parties to the Settlement Agreement. If FDA asserts, prior to publication of final rules, that it has jurisdiction to enforce its proposals against Liggett by reason of the Settlement Agreement, the agreement, with respect to FDA's proposals, "shall be null and void ab initio."

DRAFT

~~CONFIDENTIAL~~

DRAFT

Section 897.30(a)(1)

FDA Proposal--Allows advertising bearing cigarette or smokeless tobacco brand name only in newspapers, magazines, periodicals, on billboards, posters and placards only in accordance with section 897.30(b).

Liggett Compliance--Full compliance (but see section 897.30(b) limitation below).

Section 897.30(a)(1)

FDA Proposal--Allows labeling which bears cigarette or smokeless tobacco brand name only in point of sale promotional material, audio and video formats delivered at point of sale, and on entries and teams in sponsored events.

Liggett Compliance--Full compliance.

Section 897.30(b)

FDA Proposal--No outdoor advertising for cigarettes or smokeless tobacco allowed within 1000 feet of any playground, elementary or secondary school.

Liggett Compliance--Limited to billboards within 1000 feet of "clearly marked and state-licensed elementary or secondary school or a clearly marked, outdoor, municipal or other government-operated public playground for children."

Section 897.32(a)

FDA Proposal--Advertising and labeling permitted under section 897.30 limited to black text on white background except in publications whose readership consists of 85 percent or more persons 18 years old or older and whose readership consists of fewer than 2 million persons under 18 years old.

Liggett Compliance--Limited to advertising in publications "whose regular readers aged less than eighteen years constitute 15% or more of the publication's total regular readership," and, where Liggett currently advertises in publications whose readership exceeds the 15 percent limit, Liggett "will, through incremental reduction, meet the requirements of this rule within a period of five years."

Section 897.34(a)

FDA Proposal--No marketing, licensing, distribution or sale of any item or service (other than cigarettes and smokeless tobacco products) bearing brand name, logo, etc. of any cigarette or smokeless tobacco product.

Liggett Compliance--Limited to "clothing or outerwear or to any items or services, other than clothing or outerwear, which have not [previously] been marketed, licensed, distributed or sold,

DRAFT

~~CONFIDENTIAL~~

DRAFT

and which are more likely to appeal to minors than to adults," and not applicable to "items or services customarily marketed, licensed, distributed or sold at the site and at the time of events permissible under [section 897.34(c) as modified below]."

Section 897.34(b)

FDA Proposal--No offering of any gift or item, or right to participate in any contest to any person purchasing cigarettes or smokeless tobacco products.

Liggett Compliance--Limited to gifts or other items which are "more likely to appeal to minors than to adults."

Section 897.34(c)

FDA Proposal--No sponsorship of any athletic, musical, artistic, social or cultural event in the brand name, logo, etc. of any cigarette or smokeless tobacco product. (Sponsorship in the corporate name allowed.)

Liggett Compliance--Limited to events "whose past patrons or attendees aged less than eighteen years constitute 15% or more of the event's total past patronage," and no compliance required for events that Liggett has "sponsored, conducted, engaged or participated in within the last ten years."

DRAFT

~~CONFIDENTIAL~~

DRAFT

There are also many substantive provisions of FDA's proposed regulations by which Liggett has not agreed to abide to any extent. These are:

Section 897.10

FDA Proposal--Each manufacturer, distributor, and retailer is responsible for ensuring that its tobacco products comply with the FDA regulations. (This provision in FDA's proposed regulations seems to attempt to make cigarette manufacturers and the like responsible for the actions of third parties.)

Section 897.12(a)

FDA Proposal--Each manufacturer is to remove from each point of sale, all self-service displays, advertising, labeling and other manufacturer-supplied or manufacturer-owned items that do not comply with FDA's proposed regulations.

Section 897.12(b)

FDA Proposal--When tobacco manufacturers' representatives visit points of sale, they are to visually inspect and insure that the products are labeled, advertised, and distributed in accordance with FDA's proposed regulations.

Section 897.14

FDA Proposal--Retailers are responsible for: checking photo i.d. for all sales; not using vending machines or any other electronic or mechanical device to supply the product; and not selling cigarettes or tobacco in any quantity less than the quantity in an unopened package.

Section 897.16(c)

FDA Proposal--No vending machines, self-service displays, mail-order sales, and other impersonal modes of sale.

Sections 897.24

FDA Proposal--Established name (e.g., "Cigarette," "Loose Leaf Chewing Tobacco") required on each cigarette or smokeless tobacco product package, carton, box, or container.

Section 897.29

FDA Proposal--Each manufacturer shall establish and maintain an effective national public educational program (mostly on television) to discourage minors from using tobacco. (All manufacturers together are supposed to spend \$150 million per year on these programs.)

DRAFT

~~CONFIDENTIAL~~

DRAFT

Section 897.32(b)

FDA Proposal--All advertising shall include the product's established name and a statement of its intended use (e.g., "Cigarettes--A Nicotine-Delivery Device").

Sections 897.32(c) and (d)

FDA Proposal--All advertising shall include a brief conspicuous prominent statement contiguous to the Surgeon General's warning and printed in black text on a white background, such as "About one of three kids who become smokers will die from their smoking."

Section 897.36

FDA Proposal--Labeling or advertising of any cigarette or smokeless tobacco product is false or misleading if the labeling or advertising contains any express or implied false, deceptive, or misleading statement, omits important information, lacks fair balance, or lacks substantial evidence to support any claims made for the product.

Sections 897.40(a) and (b)

FDA Proposal--Each manufacturer shall submit annually to FDA copies of all labels and labeling and a representative sampling of advertising.

Section 897.40(c)

FDA Proposal--Certain records and other information collected under or related to FDA's proposed regulations are to be made available to FDA representatives for inspection, review, copying, and other uses related to enforcement of the FD&C Act and the proposed regulations.

DRAFT~~CONFIDENTIAL~~**DRAFT****ATTACHMENT 3****Summary of the *Castano* Settlement Agreement**

On March 12, 1996, Liggett settled a class action lawsuit brought against it on behalf of all addicted smokers in *Dianne Castano, et al. v. The American Tobacco Company, Inc., et al.*, Civil No. 94-1044 (E.D. La.). See *Castano Settlement Agreement* at 1 ("*Castano Agmt.*"). As with the attorneys' general settlement, the *Castano* settlement has two main features. First, Liggett again agreed to abide by selected provisions of the FDA's proposed rules. The extent of its compliance tracks the terms of the states' settlement agreement. (*Castano Agmt.*, ¶ 5.) Second, the *Castano* agreement creates a fund to be managed by a newly created board. In many important aspects (e.g. the effect of Liggett finding a future affiliate, the term of agreement, Liggett's ability to terminate the agreement, etc.), the two agreements are identical. However, the agreements are significantly different in the purposes of the funds that are created.

As opposed to defraying state health care costs (as in the states' lawsuits), the monetary damages to be paid in *Castano* will be used in other ways. The *Castano* settlement contemplates the creation of the "*Castano Center for Tobacco Control Innovation and Research*" ("*CCTCIR*") and a "*Castano Settlement Fund*." The CCTCIR will be an entity whose purpose is to conduct research concerning tobacco cessation programs and the prevention of smoking by minors. (*Castano Agmt.*, ¶ 6.4.) The settlement fund will provide the necessary money for settling class members to attend smoking cessation programs. (*Castano Agmt.*, ¶ 6.4.)

Liggett's payment responsibilities differ between the *Castano* case and the states' actions. In *Castano*, Liggett has agreed to provide "periodic payments sufficient on an ongoing basis to reimburse one-half of the cost of Approved Smoking Cessation Programs" for eligible class members. (*Castano Agmt.*, ¶ 6.4.) Liggett shall not have to pay in any single year more than 5% of its pretax income or more than \$50 million. (*Castano Agmt.*, ¶ 6.4.) The agreement anticipates that other companies may join the settlement. Subsequently settling companies will have the following responsibilities: each must pay \$5 million in the first year, and up to \$10 million in each subsequent year (up to the fifteenth year) to fund research by the CCTCIR. (*Castano Agmt.*, ¶ 6.4.) In addition, each tobacco company besides Liggett also must advance \$25 million to the settlement fund to defray the initial start-up costs. The only monetary award available to an eligible class member apparently is the cost of reimbursement of an approved smoking cessation program. (*Castano Agmt.*, ¶ 6.2.3.)

Because the plaintiffs comprise a class action, the settlement requires approval of the district court before it becomes final. None of the other defendants have indicated a desire to settle, and, to the contrary, they have stated their intention to proceed with their appeal of the class certification before the Fifth Circuit Court of Appeals.

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").

RECITALS

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 Daniel V. McGraw, Jr., brought an action entitled McGraw v. The American Tobacco Co., et al., 94-C-1797, 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., et al., 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, after such reorganization or spinoff, retains 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 Brown's 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 § 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 § 897.16 (b), as proposed.

4.2.3. Proposed Rule § 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 § 897.30 (a), as proposed.

4.2.5. Proposed Rule § 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 § 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% limitation, Settling Defendants will, through incremental reduction, meet the requirements of this rule within a period of five (5) years.

4.2.7. Proposed Rule § 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 § 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 § 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)(i) 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.

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 proportional 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 punitive 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 anytime 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 acquirer, 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 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 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

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 to 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 Proceeding"). 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 one 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 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 Obligor") 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 Obligor which the NSD Obligor 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 Obligor 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 a (i) 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 $6 = 2\frac{2}{3}$; if the Settling Defendant is paying 7.5 percent of Pretax Income, the multiplier is $7.5 + 10$ divided by $7.5 = 2\frac{1}{3}$.

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 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

Danrell 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 1002
212 4073800
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 Attorney General

(5) insofar as Brooke Group or Liggett have or obtain any material information concerning any scandalous or illegal conduct on the part of any person, including New-Seeling Defendants or their agents, designed to frustrate or defeat the Attorney General Actions against the New-Seeling 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

Mike Moore
Mike Moore, Attorney General

STATE OF LOUISIANA

Richard P. Lynch
Richard P. Lynch, Attorney General

STATE OF WEST VIRGINIA

Samuel V. McGraw, Jr.
Samuel V. McGraw, Jr., Attorney General

By: [Signature]
BROOKE GROUP Ltd.

STATE OF FLORIDA

Robert Butterworth
Robert Butterworth, Attorney General

By: [Signature]
LIGGETT GROUP, INC.

COMMONWEALTH OF MASSACHUSETTS

[Signature]
Scott Harshbarger, Attorney General

By: [Signature]
LIGGETT & MYERS, INC.