

The following file contains two documents:

- A memorandum to the Joint Budget Committee members dated March 15, 2013, concerning a FY 2012-13 supplemental request and a FY 2013-14 budget amendment submitted by the Department of Law on March 8 concerning tobacco litigation funding.
- A packet dated January 9, 2013, including staff recommendations related to the Department of Law's supplemental requests for FY 2012-13 that were submitted in January 2013.

**COLORADO GENERAL ASSEMBLY
JOINT BUDGET COMMITTEE**



**SUPPLEMENTAL REQUEST FOR FY 2012-13 AND
BUDGET AMENDMENT FOR FY 2013-14
CONCERNING TOBACCO LITIGATION FUNDING**

DEPARTMENT OF LAW

**JBC Working Document - Subject to Change
Staff Recommendation Does Not Represent Committee Decision**

**Prepared By:
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March 15, 2013**

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Prioritized Supplemental and Budget Amendment

SUPPLEMENTAL REQUEST #1, TOBACCO LITIGATION FUNDING

	FY 2012-13		FY 2013-14	
	Request	Recomm.	Request	Recomm.
Total	<u>715,630</u>	<u>715,630</u>	<u>750,000</u>	<u>\$750,000</u>
FTE	0.0	0.0	0.0	0.0
General Fund	515,630	515,630	0	750,000
Cash Funds – Tobacco Settlement Defense Account	0	0	750,000	0
Cash Funds – Attorney Fees and Costs Account	200,000	200,000	0	0

Does JBC staff believe the request meets the Joint Budget Committee's supplemental criteria? [An emergency or act of God; a technical error in calculating the original appropriation; data that was not available when the original appropriation was made; or an unforeseen contingency.]	YES
JBC staff and the Department agree that this request is the result of <i>an unforeseen contingency</i> .	

This request was submitted to JBC Staff on Friday, March 8, 2013, at 2:39 pm.

Department Request: The Department of Law requests additional funding in both FY 2012-13 and FY 2013-14 to support its tobacco litigation efforts. The Department originally anticipated that the work of its outside counsel (Hale Westfall) would decrease for several months following Colorado's December 2012 arbitration hearing related to the non-participating manufacturers (NPM) adjustment. However, Hale Westfall has worked with the Department to analyze and assess the possible settlement of the 2003 NPM adjustment and several future adjustments. While two previous settlement attempts failed, the participating manufacturers and the 19 states that signed on to the most recent settlement proposal ("Signatory States") have agreed to move forward. The current settlement structure, with less than unanimous support from the tobacco Master Settlement Agreement (MSA) states, was not foreseen.

The 29 states that have not signed on to the most recent settlement proposal ("Majority States") believe that the proposed settlement is an impermissible amendment to the tobacco MSA, and have challenged the implementation of the settlement before the NPM adjustment Arbitration Panel. At the request of the Department, Hale Westfall has taken the lead role for the Majority States in opposing the settlement. This has resulted in an increased workload that was not anticipated. Hale Westfall has represented the Majority States in two hearings, met with several Majority States for arbitration preparation, and coordinated drafting among Majority States of group briefs and pleadings.

The Department cannot determine how long this increased workload will continue for Hale Westfall. The challenge to the settlement may require action in Denver District Court, Colorado's court of continuing jurisdiction under the tobacco MSA. It is also possible for multiple state court actions by the Signatory States, the participating manufacturers, and the Majority States. There is the possibility of consolidation of these state court actions in federal court, or original actions in federal court. This uncertainty could last for some time and at least through the April 15, 2013, annual MSA payment (this payment is directly affected by the ongoing hearings). The Department indicates that it hopes that in the near future this dispute will shift to the political arena and the Attorneys General will be engaged in creating a new settlement structure.

The Department's FY 2012-13 supplemental request assumes that the increased workload for Hale Westfall will continue through June 2013, requiring \$150,000 per month. For FY 2013-14, the Committee previously approved the Department's initial request for \$500,000 for outside counsel, which provides about \$42,000 per month. The Department's budget amendment would provide an additional \$75,000 per month from July through December 2013, and an additional \$50,000 per month from January through June 2014. These estimates are based on significant workload through FY 2013-14 and the potential for state to state disputes on diligent enforcement, assuming the Signatory States are successful.

For FY 2012-13, the Department requests a mix of General Fund (\$515,630) and cash funds from the Attorney Fees and Costs Account (\$200,000). For FY 2013-14, the Department has requested the full amount (\$750,000) from the Tobacco Settlement Defense Account within the Tobacco Litigation Settlement Cash Fund (Defense Account), based on the assumed passage of H.B. 13-1180.

Staff Recommendation: Staff recommends approving the request, with one modification and one addition:

- Staff recommends including an additional section in the 2013 Long Bill to appropriate a total of \$715,630 (including \$515,630 General Fund and \$200,000 cash funds from the Attorney Fees and Costs Account) for FY 2012-13.
- **Staff recommends appropriating through the 2013 Long Bill \$750,000 General Fund** (rather than cash funds from the Defense Account) **for FY 2013-14.**
- **Staff recommends adding an appropriation clause to H.B. 13-1180** (in the Senate Appropriations Committee) **to refinance the \$750,000 General Fund appropriation for FY 2013-14 with cash funds from the Defense Account.** [This bill will also require an appropriation of approximately \$676,952 cash funds from the Defense Account for FY 2013-14 to substitute for General Fund appropriations that have already been approved by the Committee.]
- **Staff recommends amending H.B. 13-1180 to extend for one additional year the annual transfer of \$1,000,000 from the Tobacco Litigation Settlement Cash Fund to the Defense Account.**

Staff has provided an analysis of the request below, as well as background information concerning the following topics:

- Payment Dispute Concerning Non-Participating Manufacturers
- Tobacco Settlement Defense Account
- Attorney Fees and Costs Account

Analysis: On February 13, 2013, the Committee took action on the Department of Law's FY 2013-14 budget request. The Committee approved the Department's request for \$676,952 General Fund in FY 2013-14 to support its tobacco litigation efforts because moneys are no longer anticipated to be available in the Defense Account. The Committee has also introduced a bill (H.B. 13-1180) that would transfer a total of \$3,792,244 of tobacco settlement moneys to the Defense Account over the next two years (including \$1,792,244 prior to July 1, 2013, and \$1,000,000 in each of the next two fiscal years). Passage of this bill would allow the General Assembly to continue to appropriate cash funds from the Defense Account rather than General Fund.

The Department's tobacco litigation efforts include two components:

- The Department's Antitrust, Tobacco, and Consumer Protection Unit includes an attorney (1.0 FTE) who is responsible for enforcing the tobacco MSA and related tobacco laws. This individual monitors compliance with the numerous injunctive terms, ensures that Colorado's interests are protected under the payment calculation provisions, and works with the Department of Revenue to enforce escrow payment obligations of NPMs.
- The Department contracts with outside counsel to represent Colorado in the NPM adjustment arbitration proceedings. This involves representing Colorado at all multi-state meetings and arbitration hearings, negotiating with counsel for the participating manufacturers on behalf of Colorado and other states, and monitoring all contested state arbitrations. Due to the above-described Department attorney's involvement in developing and monitoring the Department of Revenue's NPM enforcement program, he can be called to testify during the arbitration proceeding. Thus, the Department is required to utilize outside counsel.

To date, the above litigation efforts have been funded from the Defense Account (this account is described more fully below). This account is projected to be exhausted by the end of FY 2012-13, so the Department requested General Fund to continue litigation efforts on behalf of the State. The following table details the existing appropriation for FY 2012-13, the amounts already approved by the Committee for FY 2013-14, and the recently submitted requests for both fiscal years.

*JBC Staff Supplemental Recommendations: FY 2012-13
Staff Working Document – Does Not Represent Committee Decision*

Department of Law: Tobacco Litigation Funding Request			
Description	FY 2012-13	FY 2013-14	Two Year Total
<i>Existing FY 2012-13 Appropriation and Amounts Approved by JBC for FY 2013-14:</i>			
Antitrust, Tobacco, and Consumer Protection Unit (1.0 FTE attorney and associated central appropriations)	\$178,603	\$176,952	\$355,555
Tobacco Litigation (funding for outside counsel to represent Colorado in arbitration proceedings)	<u>880,000</u>	<u>500,000</u>	<u>1,380,000</u>
Approved	1,058,603	676,952	1,735,555
General Fund	0	676,952	676,952
Cash Funds - Defense Account	1,058,603	0	1,058,603
<i>March 2013 Supplemental Request and Budget Amendment:</i>			
Subtotal: Supplemental Request/ Budget Amendment (for Tobacco Litigation)	715,630	750,000	1,465,630
General Fund	515,630	0	515,630
Cash Funds - Defense Account	0	750,000	750,000
Cash Funds - Attorney Fees and Costs Account	200,000	0	200,000
<i>Total Appropriations Requested:</i>			
Antitrust, Tobacco, and Consumer Protection Unit	178,603	176,952	355,555
Tobacco Litigation	<u>1,595,630</u>	<u>1,250,000</u>	<u>2,845,630</u>
Total Funds	1,774,233	1,426,952	3,201,185
General Fund	515,630	676,952	1,192,582
Cash Funds - Defense Account	1,058,603	750,000	1,808,603
Cash Funds - Attorney Fees and Costs Account	200,000	0	200,000

Staff recommends approving the request, with one modification and one addition. As reflected in the Defense Account statute, the General Assembly has always anticipated a need for ongoing legal work related to the MSA. The current NPM legal dispute has high financial stakes for the State, and ceasing or substantially limiting financial support for litigation efforts (including the settlement proposed by 19 states) at this point appears unwise. The Defense Account of the Tobacco Litigation Settlement Cash Fund was established out of tobacco MSA moneys received in compensation for attorney fees, and other costs that Colorado incurred in its legal action against tobacco manufacturers. Due to the increased workload required to represent Colorado's interests in response to the settlement proposed by 19 states, the balance in the Defense Account will not be sufficient to cover litigation costs through the end of FY 2012-13.

For FY 2012-13, staff recommends approving the request for \$515,630 General Fund and \$200,000 cash funds from the Attorney Fees and Costs Account. The Department has limited the amount of General Fund required by requesting a portion from this account, which consists of any moneys received by the Attorney General as an award of attorney fees or costs that are not considered custodial moneys. Moneys in this account are subject to annual appropriation by the General Assembly for legal services provided by the Department. If the Committee approves the Department's supplemental request, the Account's fiscal year-end balance is projected to be reduced to \$632,687. The Department relies on this account to cover unanticipated legal

expenses that arise over the course of the fiscal year, especially when the General Assembly is not in session. Staff agrees that it is prudent to leave a reasonable balance available in this account to cover these types of expenses in future fiscal years.

For FY 2013-14, staff recommends approving the request but appropriating the \$750,000 through the 2013 Long Bill from the General Fund (rather than cash funds from the Defense Account). Given that H.B. 13-1180 only recently passed the House, staff recommends that the Committee include appropriations in the 2013 Long Bill based on current law. At this point appropriations from the Defense Account should only be included through an appropriation clause in H.B. 13-1180. Thus, staff recommends adding an appropriation clause to H.B. 13-1180 (in the Senate Appropriations Committee) to refinance the \$750,000 General Fund appropriation for FY 2013-14 with cash funds from the Defense Account. [This bill will also require an appropriation of approximately \$676,952 cash funds from the Defense Account for FY 2013-14 to substitute for General Fund appropriations that have already been approved by the Committee.]

Finally, given the increased expenses associated with the settlement proposed by 19 states, staff recommends transferring an additional \$1,000,000 from the Tobacco Litigation Settlement Cash Fund to the Defense Account. Specifically, staff recommends extending the annual transfer of \$1,000,000 for one additional year (FY 2015-16). This action would reduce the amount of additional moneys made available for the Nurse Home Visitor Program in FY 2015-16 (an increase of \$802,274 in FY 2015-16 rather than \$1,802,274), as detailed in the following table.

Impact of H.B. 13-1180 On Allocations from the Tobacco Litigation Settlement Cash Fund									
Fiscal Year	Current Law			With HB 13-1180 (With Recommended Modification)			Difference		
	Nurse Home Visitor Program	Defense Account	General Fund	Nurse Home Visitor Program	Defense Account	General Fund	Nurse Home Visitor Program	Defense Account	General Fund
2012-13	\$12,737,350	\$0	\$1,792,244	\$12,737,350	\$1,792,244	\$0	\$0	\$1,792,244	(\$1,792,244)
2013-14	13,524,950	0	1,803,330	14,328,280	1,000,000	0	803,330	1,000,000	(1,803,330)
2014-15	14,560,570	0	1,820,072	15,380,642	1,000,000	0	820,072	1,000,000	(1,820,072)
2015-16	15,319,330	0	1,802,274	16,121,604	1,000,000	0	802,274	1,000,000	(1,802,274)
2016-17	16,365,985	0	909,221	17,275,207	0	0	909,221	0	(909,221)
2017-18	14,425,207	0	0	14,425,207	0	0	0	0	0

Background Information – Payment Dispute Concerning Non-Participating Manufacturers.

When the tobacco MSA was signed in 1998, participants recognized that the extra costs that the settlement imposed on participating manufacturers would place them at a competitive disadvantage when compared with manufacturers that had not joined the agreement. In an effort to level the playing field, the MSA required states to enact "qualifying statutes" that force non-participating manufacturers (NPM) to make payments into escrow accounts that are comparable to what they would have paid had they participated in the agreement. House Bill 99-1208 added the qualifying statute to Colorado law. The MSA requires states to "diligently enforce" their qualifying statutes. If certain preconditions are met, settlement payments to states that do not diligently enforce are reduced.

Since 2006, Colorado and the other states have been involved in a legal dispute with the participating manufacturers, who allege that the states are not diligently enforcing their NPM laws. Due to this dispute, some tobacco companies have withheld a portion of their settlement payments, placing them in escrow. When a diligent enforcement question arises, it is settled by a panel of arbitrators who must decide the issue in a unified national proceeding in which a separate decision will be made on the diligent enforcement efforts of each participating state. Thus the arbitrators might decide that one state should receive a reduced payment because it failed to diligently enforce, while another state diligently enforced and is entitled to its full payment.

This lengthy multi-state arbitration process currently concerns tobacco settlement payments in 2003. Colorado's state-specific hearing occurred in December 2012, and final resolution of the 2003 arbitration is likely to be in late 2013 or early 2014. Following a decision for the 2003 adjustment, the arbitration process will be repeated for 2004 and subsequent years. Depending upon the results of this legal dispute for Colorado, the outcome related to 2003 disputed payments could range from:

- Receipt of an additional \$10.9 million (payout of amounts withheld); to
- Loss of the entire 2003 tobacco allocation for the State (\$86.1 million).

The State faces similar potential additional payouts and financial risks related to 2004 and subsequent years. Pursuant to S.B. 12-114, if the dispute is resolved in the State's favor, the additional revenue would be deposited to the General Fund. If the State is penalized as a result of the dispute, staff anticipates negotiations on *when* the penalty would be applied. Fiscal impacts could be spread across multiple years.

Background Information – Tobacco Litigation Settlement Cash Fund Defense Account

The Tobacco Settlement Defense Account of the Tobacco Litigation Settlement Cash Fund¹ (Defense Account) is to be used by the Department of Law “to defend the state in lawsuits arising out of challenges or arising under the provisions of the master settlement agreement...to enforce and defend all rights and obligations of the state under said settlement agreements...and to resolve any dispute with any participating manufacturer...or nonparticipating manufacturer...”. The statute specifies that any moneys received to compensate the state for attorney fees, court costs, or other expenses incurred by the State in obtaining the settlement, and all interest earned on these funds, is deposited in this account.

The Account initially received \$4.0 million in FY 2000-01 (including \$3.83 million from the Agreement for attorney fees, plus interest earned). The General Assembly began appropriating moneys from the Defense Account to the Department of Law in FY 2001-02. From FY 2001-02 through FY 2011-12, the Department spent a total of \$4,066,330 from the Defense Account, with annual expenditures ranging from a low of \$66,096 in FY 2006-07 to a high of \$1,139,303 in FY 2010-11. A balance of \$1,025,710 remained in the Defense Account at the beginning of the current fiscal year. The fund balance is anticipated to be exhausted by the end of FY 2012-13.

¹ See Section 24-22-115 (2) (a), C.R.S.

JBC Staff Supplemental Recommendations: FY 2012-13
Staff Working Document – Does Not Represent Committee Decision

Background Information –Attorney Fees and Costs Account

Various court awards are deposited into the Attorneys Fees and Costs Account, which is established in Section 24-31-108 (2), C.R.S. This account consists of any moneys received by the Attorney General as an award of attorney fees or costs that are not considered custodial moneys. Moneys in the Account are subject to annual appropriation by the General Assembly for legal services provided by the Department. The following table details revenues and expenditures for this account. If the Committee approves the Department's supplemental request, the Account's fiscal year-end balance is projected to be reduced to \$632,687.

Attorney Fees and Costs Account				
Fiscal Year	Beginning Fund Balance	Revenues	Expenditures	Ending Fund Balance
2005-06	\$208,794	\$23,276	(\$100,477)	\$131,593
2006-07	131,593	244,420	(71,333)	304,680
2007-08	304,680	267,118	(142,251)	429,547
2008-09	429,547	105,671	(94,595)	440,623
2009-10	440,623	202,185	(54,021)	588,787
2010-11	588,787	123,861	(22,417)	690,231
2011-12	690,231	442,207	(7,426)	1,125,012
2012-13	1,125,012	143,556	(435,881)	832,687

**COLORADO GENERAL ASSEMBLY
JOINT BUDGET COMMITTEE**



**SUPPLEMENTAL REQUESTS FOR FY 2012-13
DEPARTMENT OF LAW**

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Staff Recommendation Does Not Represent Committee Decision**

**Prepared By:
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January 9, 2013**

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Non-Prioritized Supplementals

PREVIOUSLY APPROVED DORA INTERIM SUPPLEMENTAL REQUEST REGULATION OF APPRAISAL MANAGEMENT COMPANIES

	Previously Approved
Total	<u>\$62,839</u>
FTE	0.5
Reappropriated Funds	62,839

Summary: The Committee approved this supplemental request submitted by the Department of Regulatory Agencies (DORA) in September 2012. DORA requested appropriations to three departments for FY 2012-13 for the implementation of H.B. 12-1110, which concerns the regulation of appraisal management companies. The request was necessary due to a technical issue with the effective date clause included in the act. The request included an appropriation to the Department of Law for the provision of 830 hours of legal services to DORA (based on an hourly rate of \$75.71).

The rules governing interim supplementals in Section 24-75-109 (5), C.R.S., require the Committee to introduce all interim supplementals that it approves. Staff will include this portion of the supplemental previously approved by the Committee in the Department of Law's supplemental bill.

NON-PRIORITIZED SUPPLEMENTAL DEPARTMENT OF PUBLIC SAFETY SUPPLEMENTAL REQUEST #S-2: LEGAL SERVICES

	Request	Recommendation
Total	<u>\$188,645</u>	Pending JBC Action on DPS Request
FTE	1.4	
Reappropriated Funds	188,645	

Summary: The Department of Public Safety has submitted a supplemental request (priority #2) to increase its appropriation for the purchase of legal services from the Department of Law by \$188,645 General Fund. The Department of Law would need corresponding spending authority to receive the additional funds from the Department of Public Safety. The staff recommendation for this request is pending Committee action on the Department of Public Safety's supplemental request. Staff asks permission to include in the Department of Law's supplemental bill the spending authority and FTE that correspond with the Committee's action.

Statewide Common Policy Supplemental Requests

This request is not prioritized and is not analyzed in this packet. The JBC will act on this item later when it makes decisions regarding common policies.

Department's Portion of Statewide Supplemental Request	Total	General Fund	Cash Funds	Reapprop. Funds	Federal Funds	FTE
Liability Premiums Technical True-up	\$40,207	\$40,207	\$0	\$0	\$0	0.0
Department's Total Statewide Supplemental Requests	\$40,207	\$40,207	\$0	\$0	\$0	0.0

Staff Recommendation: The staff recommendation for this request is pending Committee approval of common policy supplementals. Staff asks permission to include the corresponding appropriation in the Department's supplemental bill when the Committee approves this common policy supplemental. If staff believes there is reason to deviate from the common policy, staff will appear before the Committee later to present the relevant analysis.

JBC Staff Supplemental Recommendations - FY 2012-13
Staff Working Document - Does Not Represent Committee Decision

Appendix A: Number Pages

	FY 2011-12 Actual	FY 2012-13 Appropriation	FY 2012-13 Requested Change	FY 2012-13 Rec'd Change	FY 2012-13 Total W/ Rec'd Change
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DEPARTMENT OF LAW

Previously Approved DORA Interim Supplemental

LEGAL SERVICES TO STATE AGENCIES

Personal Services	<u>19,247,465</u>	<u>20,550,841</u>	<u>56,555</u>	<u>56,555</u>	<u>20,607,396</u>
FTE	226.3	238.0	0.5	0.5	238.5
Cash Funds	1,560,550	253,320	0	0	253,320
Reappropriated Funds	17,686,915	20,297,521	56,555	56,555	20,354,076
Operating and Litigation	<u>1,533,916</u>	<u>1,675,225</u>	<u>6,284</u>	<u>6,284</u>	<u>1,681,509</u>
Cash Funds	0	27,256	0	0	27,256
Reappropriated Funds	1,533,916	1,647,969	6,284	6,284	1,654,253

Total for Previously Approved DORA Interim

Supplemental	20,781,381	22,226,066	62,839	62,839	22,288,905
FTE	<u>226.3</u>	<u>238.0</u>	<u>0.5</u>	<u>0.5</u>	<u>238.5</u>
Cash Funds	1,560,550	280,576	0	0	280,576
Reappropriated Funds	19,220,831	21,945,490	62,839	62,839	22,008,329

Totals Excluding Pending Items

LAW					
TOTALS for ALL Departmental line items	51,592,093	57,251,130	62,839	62,839	57,313,969
FTE	399.4	429.2	0.5	0.5	429.7
General Fund	9,326,453	9,896,185	0	0	9,896,185
Cash Funds	9,481,375	10,779,963	0	0	10,779,963
Reappropriated Funds	31,330,489	34,998,817	62,839	62,839	35,061,656
Federal Funds	1,453,776	1,576,165	0	0	1,576,165