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Epidemic on trial
Blue Cross tobacco case quantified smoking's costs

by Richard Niemiec and Nancy Nelson

The costs of tobacco use are staggering. In Minnesota alone, it is estimated that one in six deaths is attributable to smoking, and the cost for medical care and lost worker productivity is estimated at $1.3 billion every year, according to estimates by the Minnesota Health Department. That doesn't take into account personal losses to smokers, their families, and their friends.

In a new attack on the tobacco epidemic, Blue Cross and Blue Shield of Minnesota joined the State of Minnesota in 1994 to test a new legal approach: sue the tobacco companies for consumer fraud and antitrust violations. Instead of a lawsuit by an individual smoker, the tobacco companies would face the resolve and resources of a multimillion-dollar corporation in partnership with a state's attorney general.

Blue Cross remains the only health plan from the private sector in the nation to have sued and settled with the tobacco industry. Actuaries at Blue Cross played a key role in several aspects of the lawsuit and settlement. The lawsuit was groundbreaking in setting legal precedents and opening to the public long-hidden secrets of the tobacco industry's inner workings.

More important, the settlement holds great potential to set a new standard in the health care industry. Blue Cross is proposing to invest in tobacco reduction and other health improvement programs that should return $3 for each $1 spent and deliver to Minnesotans better health and quality of life.

1994: the lawsuit begins

Blue Cross and the state of Minnesota filed a joint lawsuit against the tobacco industry in August 1994. They charged that cigarette manufacturers had violated consumer fraud and antitrust laws by deceiving consumers. The resulting damage was higher medical costs for the state and Blue Cross to cover care for smoking-related illnesses. In other words, it was the actions of the cigarette makers, not the product of cigarettes, that were the target of the lawsuit. The damages were directly to Blue Cross and the state, not to individual smokers.

In filing the lawsuit, Blue Cross forged a strategic partnership with the State of Minnesota. Blue Cross is Minnesota's oldest and largest private-sector health plan. It was founded in 1933 with a charter to serve the public's health. On the state side, Hubert Humphrey III, Minnesota's attorney general when the lawsuit was filed, had built a reputation over the prior decade for strengthening and enforcing consumer fraud laws.

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Another key partnership in the lawsuit was with the Minneapolis-based law firm of Robins, Kaplan, Miller, and Ciresi, which had agreed to take the case on a modified contingency basis.

The case posed a significant risk. The tobacco industry was undefeated in the courts. Big Tobacco was also known for its tactics of overtly attacking its opponents. But in 1994, Blue Cross CEO Andy Czajkowski inspired the Blue Cross board to take on the lawsuit as an important means to attack the tobacco epidemic. The lawsuit's goals were to unveil the truth about the tobacco industry's manipulation of consumers, to stop cigarette makers from marketing to children, and to hold the industry financially accountable for the harm it has caused. The ultimate goal is to change the way the tobacco industry operates in Minnesota, reduce tobacco use, lower the rates of illness and deaths caused by tobacco, and cut health care costs for treating smoking-related illness.

The combination of the state, Blue Cross, and the Robins Kaplan legal team presented a strong front to withstand the legal onslaught of the tobacco industry's legion of attorneys.

Managed care
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MCO, an open access requirement affects the ability of the MCO to coordinate and manage care.

It seems that if consumers want comprehensive and affordable care such as that associated with managed care, they must be willing to accept the controls and constraints on service associated with managed care — or be prepared to accept the high premium increases that accompany indemnity insurance.

Building the case against Big Tobacco

The lawsuit was filed against the six largest cigarette manufacturers in the United States: Philip Morris, RJ Reynolds, Lorillard, Liggett, and Brown and Williamson and its parent company, British American Tobacco, as well as the industry's trade group (the Tobacco Institute) and the industry's research arm (the Council for Tobacco Research).

There were two tracks to developing the legal arguments for the lawsuit: documents and damages.

For the first time, tobacco companies were required to turn over millions of internal documents to be examined for consumer fraud and antitrust activities. The legal team succeeded in obtaining through court order the index of tobacco industry documents to guide the discovery process. More than 26 million pages of memos, marketing and research plans, and other internal information were compiled at a document depository in north Minneapolis. Another 7 million pages of internal documents were compiled in England from the British American Tobacco Company. The documents represent the largest collection of information from a single industry and perhaps the most important collection on a public health issue of this century.

The documents revealed how tobacco companies manipulated nicotine to keep smokers addicted, how they marketed to children, and how they collaborated in a massive public relations campaign to counter mounting information on the hazards of smoking.

As one legal team poured over the details of the documents, another was formed to create a damages model. That team consisted of epidemiologists and biomedical statisticians.

Their first step was to identify smoking-related diseases to be built into the damages model. Smoking-related illnesses include heart disease, hardening of the arteries, emphysema, peptic ulcers, and cancers of the lung, mouth, larynx, esophagus, kidney, pancreas, and bladder. There is also a category of diminished health status — illnesses made worse because the person smokes. For example, research has shown smokers take longer than nonsmokers to recover from injury, illness, or surgery.

Blue Cross' damages model was based on 60 million medical claims from Blue Cross for these diseases for 20 years, from 1978 through 1997. This included claims from only fully insured groups and excluded self-insured members, members in Blue Cross' HMO, and fully insured individuals. The Blue Cross actuarial department was responsible for extracting and preparing the data for use by the expert teams of biomedical statisticians.

Each of the smoking-related diseases was identified in medical claims by their ICD-9 diagnosis codes. But because the claims did not record whether the person was a smoker, the damages model needed to extrapolate the percent of claims directly attributable to smoking. The percent of smokers was drawn from the Minnesota Behavioral Risk Factor Surveillance System, a telephone survey of a sample of adults conducted by the Minnesota Health Department each year for the past decade. The damages model was also adjusted for confounding factors, such as the percent of persons who were obese or had other complicating health problems.

The result was a damages claim by Blue Cross of $460 million, which we considered a conservative estimate. The state claimed $1.7 billion in damages over the same period of time.

Blue Cross as plaintiff

Blue Cross sued for damages from only fully insured group claims because they presented the strongest case that Blue

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Cross had suffered higher medical costs as a result of the tobacco industry's actions.

In fact, one of the first actions the tobacco industry attorneys took in the first year of the lawsuit was to file a motion challenging Blue Cross' standing as a plaintiff. The motion was appealed all the way to the Minnesota Supreme Court. The court's ruling, issued in July 1996, confirmed Blue Cross' right to sue on its own behalf.

The tobacco companies had argued that Blue Cross did not suffer any damages and that it was the smokers themselves or the individuals and organizations that paid premiums to Blue Cross that should be suing. But the court rejected this "pass-through defense." In presenting the majority opinion, Justice Sandra Gardebring wrote:

> Here, the tobacco companies argue that because Blue Cross is a nonprofit corporation, any increased costs associated with increased medical care needed by its nicotine-addicted consumers will simply be passed on to employer subscribers. … The argument that no injury has been suffered because costs were passed through one entity to customers, consumers, or other entities usually arises in antitrust cases. It has been uniformly rejected in the courts, primarily on the theory that the injury is sustained as soon as the price, artificially raised for whatever reason, has been paid.

The ruling set a precedent for private-sector corporations in Minnesota to sue the tobacco companies. But no other health plan in the country filed a lawsuit against the tobacco industry until 1998, four years after Blue Cross filed its lawsuit.

The Blue Cross-State of Minnesota lawsuit set another precedent when the trial began on Jan. 20, 1998. Similar cases involving Mississippi, Texas, and Florida had been settled before any trial could begin.

Two actuaries at Blue Cross were deposed prior to the trial and were on the witness list for the plaintiffs and even for the tobacco industry's defense. They were involved in extensive preparation to take the stand, but neither ended up as witnesses.

Tobacco companies agreed to pay Blue Cross $9 million more than the original damages claim.

The Minnesota trial lasted four months, until May 8, the day the jury was to begin deliberations on the case, when the tobacco industry agreed to an out-of-court settlement.

In the settlement, the tobacco companies met all the demands Blue Cross and the state had laid out before the trial. Nearly all of the documents collected for the trial are open to the public for the next 10 years. Tobacco companies agreed to stop advertising on billboards or transit boards in Minnesota, to stop selling cigarette brand promotional items, and to meet numerous other restrictions on marketing. They also agreed to pay Blue Cross $469 million over the next five years to cover past and future claims for smoking-related illness, $9 million more than the original damages claim from Blue Cross.

Blue Cross received its first payment of $160 million in September 1998. The final payment will be received on Jan. 1, 2003. Blue Cross estimates the present value of the lawsuit settlement at $434 million. As a taxable nonprofit corporation, Blue Cross must pay federal and state income taxes. It has already paid $75 million in taxes and may have future tax liabilities. Another $21 million was transferred to the Blue Cross and Blue Shield of Minnesota Foundation to provide grants to communities around Minnesota for health improvement.

Under state law, the Minnesota Department of Commerce has authority to regulate what Blue Cross does with its settlement proceeds. Over the past year, Blue Cross has developed a plan for investing the proceeds in health improvements for Blue Cross' fully insured business. The goals are to reduce tobacco use among Blue Cross members by 30% and reduce other health-risk behaviors. Blue Cross estimates that its savings from improving health will be nearly $2 billion over 20 years, about a 3-to-1 return on investment. We also expect the health improvement programs to offer significant residual effect for our self-insured business.

Actuaries from Blue Cross were responsible for modeling financial aspects of the 20-year plan and responding to Commerce Department requests for further financial information. The Commerce Department is expected to issue a ruling on the Blue Cross tobacco proceeds plan in the next few months.

The health improvement programs will be based on scientific research and evaluated for their effectiveness, and the results will be published and shared with the medical community. This will provide a new model for health plans. More importantly, prevention programs will improve the health of future generations. This historic lawsuit and landmark settlement are the beginning of the end of the tobacco epidemic.

Richard Niemiec is senior vice president, corporate affairs and subsidiary operations, and Nancy Nelson is vice president and chief actuary, Blue Cross and Blue Shield of Minnesota. More information on the tobacco trial or the settlement can be found at *www.mnbluecrosstobacco.com*.