

**PHILIP MORRIS U.S.A.
CORPORATE AFFAIRS DEPARTMENT
ISSUES HANDBOOK**

FEBRUARY 1995

CONFIDENTIAL

20820805609

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SMOKING AND HEALTH

Executive Summary:

It is commonly acknowledged that smoking is a risk factor for certain human diseases. Consumers are aware of these potential risks, however, and adults are entitled to make their own decisions about smoking, just as they are entitled to make other lifestyle choices that may present potential health risks. Almost 50 million American adults make the informed decision to smoke.

Philip Morris U.S.A. position:

1. Each year since 1964, the Surgeon General has issued a report on some aspect of cigarette smoking and its potential health effects. While we disagree with many of the statements and conclusions of the reports, we do recognize cigarette smoking as a risk factor for certain diseases.
2. Consumers are aware of the potential health risks associated with tobacco use. Warning labels have appeared on every cigarette pack since 1966 and in every advertisement since 1971.
3. Adults are entitled to choose whether or not to smoke just as they are entitled to make other lifestyle choices that may present potential health risks. Almost 50 million American adults make the informed decision to smoke, and they do so because they enjoy smoking.

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CONSUMER EXCISE TAXES

Executive summary:

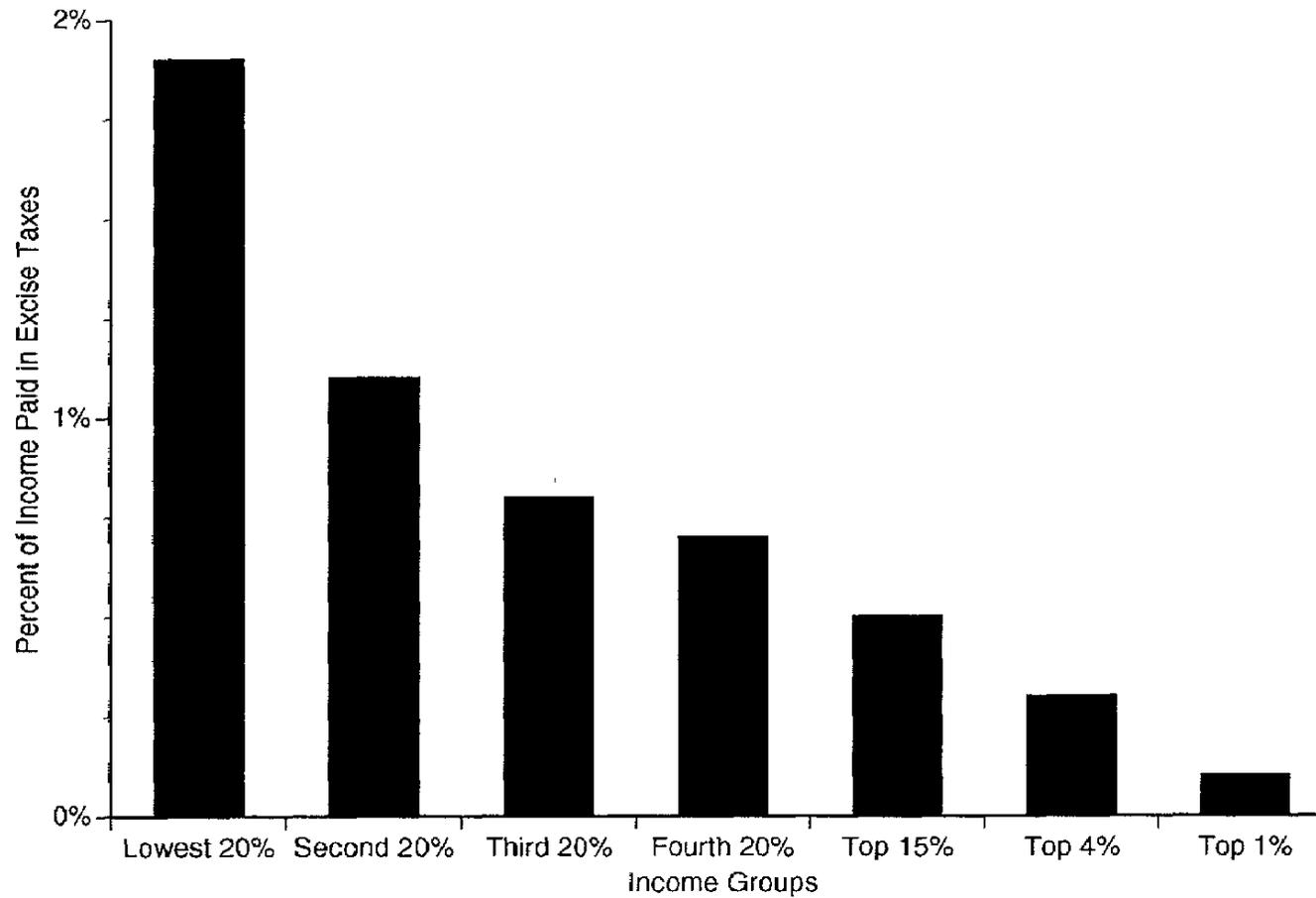
Smokers currently pay more than \$14 billion annually in federal, state and local taxes on cigarettes. Despite this, efforts are made each year to impose even higher excise taxes on cigarettes.

Philip Morris U.S.A. strongly opposes cigarette excise taxes for several reasons. Excise taxes unfairly single out one group of consumers to pay for government services that benefit everyone. Excise taxes take a much larger percentage of income from working people than from the rich. Excise taxes cost jobs, as higher prices drive down sales.

Philip Morris U.S.A. position:

1. Excise taxes cost jobs. As excise taxes drive up the price of the product being taxed, sales of that product decrease. This in turn results in job loss. For example, according to a study by Price Waterhouse, a 75-cent per pack increase in the federal excise tax on cigarettes would result in the loss of almost 275,000 jobs nationwide in core tobacco and related industries.
2. Excise taxes single out one group of consumers to pay government costs that are everyone's responsibility. Smokers pay more than \$14 billion in federal, state and local cigarette taxes each year, taxes that non-smokers do not pay, but which fund government services that presumably benefit everyone.
3. Excise taxes hurt lower-income people hardest. A 1993 study by the Peat Marwick accounting firm found that 53 percent of all American families earn less than \$30,000 annually. The study also found that while these families account for only 19 percent of all family income earned in the U.S., they pay 43 percent of all excise taxes.
4. High cigarette excise taxes could encourage violent crime. Canada is a perfect example. In 1990, the Canadian government imposed cigarette taxes that were so steep that the price of a pack of premium cigarettes rose to roughly \$4.70 [Canadian]. The result was a surge in violent crime related to cigarette smuggling, theft and black market sales. The problem became so extreme, that during 1993 Canada's federal and provincial governments lost a combined C\$2 billion, due to smuggling. Finally, the government was forced to respond to the growing crime problem and in 1994, lowered the federal excise tax by as much as C\$10.00 per carton.
5. Cigarette taxes are an unreliable source of revenue. Excise tax revenue fluctuates from year to year because it is tied directly to sales of the taxed product. Since higher taxes tend to reduce sales, the revenue from cigarette excise taxes is rarely as high as proponents project it will be.

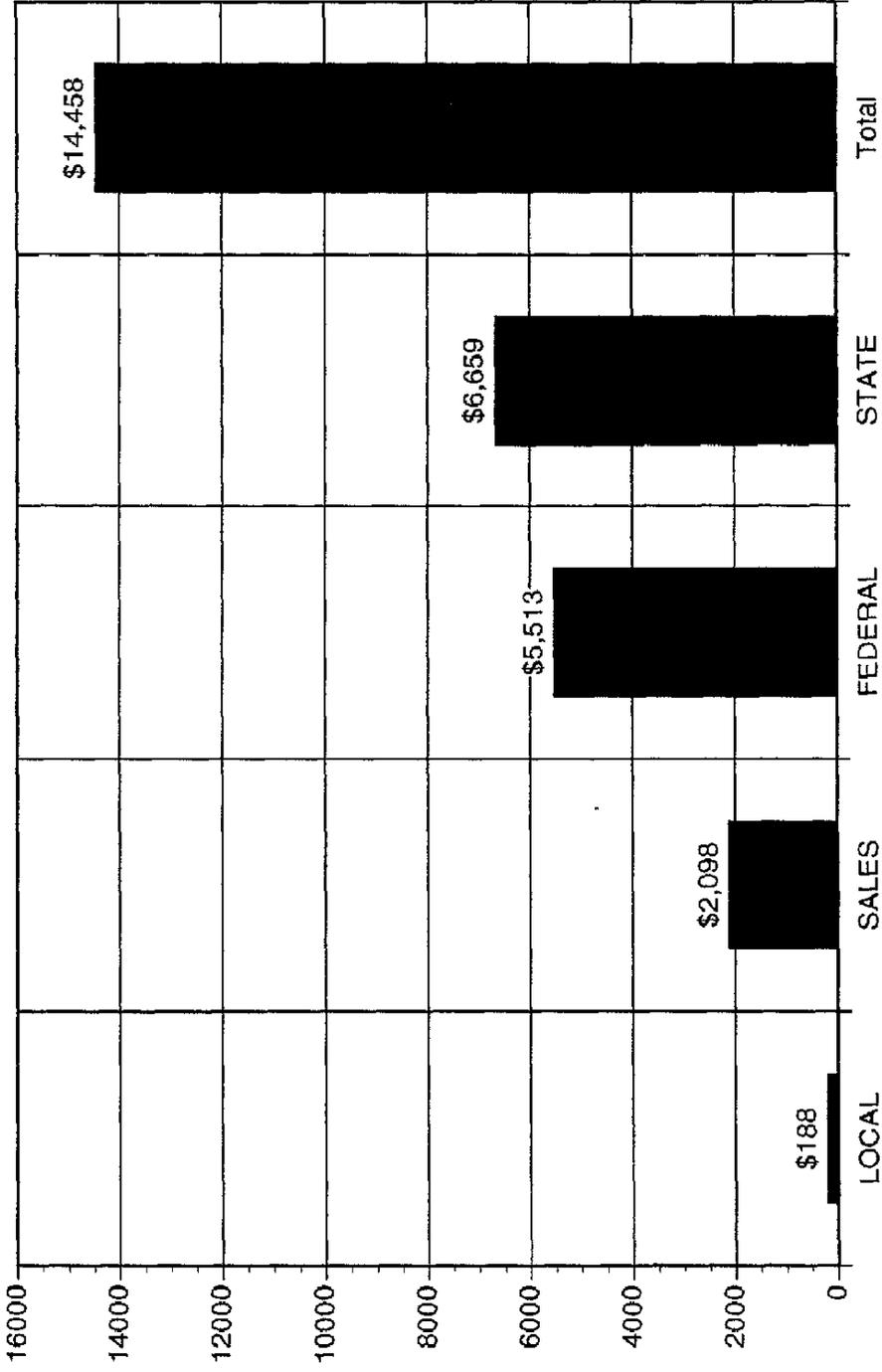
Lower Income Consumers Pay a Disproportionate Percentage of Income in Excise Taxes



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Source: Citizens for Tax Justice

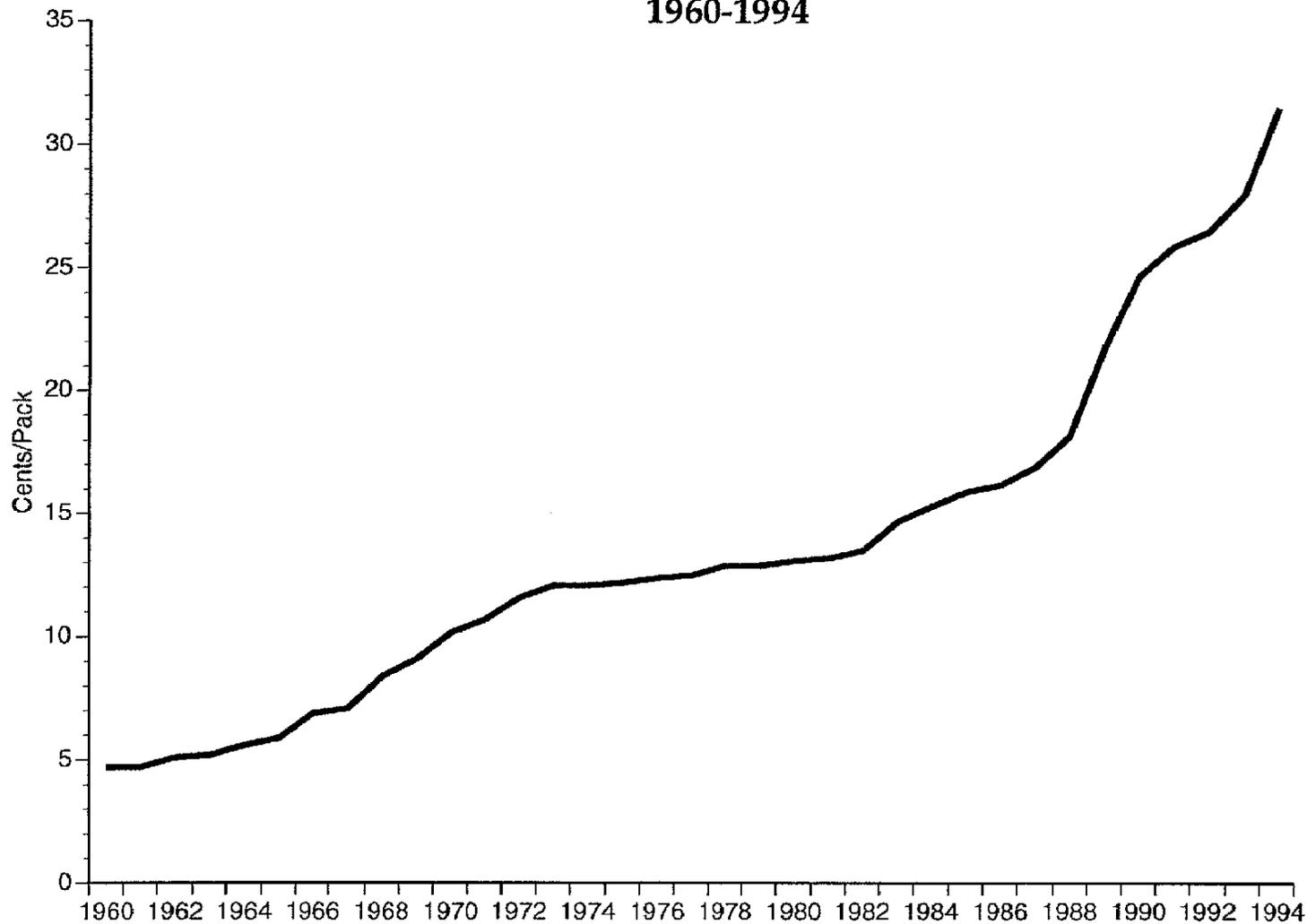
Cigarette Excise Taxes Paid by Smokers
(\$Millions)



Source: Tobacco Institute

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**Total Weighted Average
Cigarette Excise Tax
1960-1994**



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Note: For fiscal year ending June 30th.

Source Tobacco Institute, 1995

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EARMARKING EXCISE TAXES

Executive Summary:

In some instances, elected officials and special interest groups try to increase cigarette excise taxes to pay for specially "earmarked," or pet projects. For example, smokers in Cleveland helped fund construction of a new baseball stadium for the Cleveland Indians. Smokers in Massachusetts and California are now funding multi-million dollar anti-smoking campaigns. And at a national level, during 1994 President Clinton called on smokers to help fund an overhaul of the nation's health care system through a 75-cent per pack increase in the federal excise tax on cigarettes.

Anti-smokers try to justify cigarette tax increases as a way to prevent minors from smoking, force people to stop smoking, or inflict economic punishment on people who continue to smoke. This is a blatant misuse of our nation's tax system. The tax code is designed to raise revenue, not to engineer social change.

Earmarked taxes of any kind are unfair because they force one group of consumers to pay for government programs that may serve all citizens. In addition, earmarked taxes are an unreliable source of revenue, and make government less flexible and less able to respond to changing budgetary needs.

Philip Morris U.S.A. Position:

1. Excise taxes are an unreliable source of revenue. This is because as taxes increase, sales of the product being taxed decrease. Fewer sales mean less tax revenue is generated. As a result, states that rely on excise tax income may find that actual revenue generated falls short of projected tax income. The result? Legislatures may resort to additional excise tax increases, and the cycle begins again.
2. Government services such as health care and public education should not depend on the number of cigarettes sold in a given year.
3. Earmarking prevents comprehensive budgeting. It reduces fiscal flexibility, making it more difficult for the government to adapt a budget to changing economic conditions.
4. Earmarking, by removing expenditures from review, makes the budgetary process arbitrary. Inefficient or obsolete programs may be continued simply because they are financed by earmarked revenues. Responsible fiscal policy requires that programs should be evaluated periodically and funded on the basis of their necessity, efficiency and success.
5. It is unfair to force smokers to pay for government services that benefit the entire community. Services such as education, highway maintenance and health

care are everyone's responsibility. These programs should be funded with fair, progressive, broadly-based taxes.

6. Taxes should be used to raise revenue, not to impose moral standards. Taxing people to force them to change their legal behavior amounts to social engineering -- an inappropriate and inefficient use of the tax code. Many everyday pleasures, such as high-fat foods and motorcycle driving, present potential health risks to the people who choose to enjoy them. Obesity allegedly "costs" \$39 billion a year (*Journal of the American Medical Association*, October 19, 1994), and softball sliding injuries produce an annual "cost" of \$2 billion in medical expenses alone (*The American Journal of Sports Medicine*, November 1990). It is as wrong to put a punitive tax on cigarettes as it would be for the government to levy special taxes on high fat foods or bats and balls.

DIVESTMENT

Executive Summary:

Some investment funds and other holders of Philip Morris stock have decided to sell their holdings as a way of protesting the company's tobacco operations. Other firms have threatened to "divest" their holdings if Philip Morris does not adequately address their political or social concerns.

We believe that Philip Morris stock is an excellent investment, and that any investment manager who makes a decision not to invest in a company based on a sense of moral righteousness or political correctness, is not serving the interests of his or her investors. The job of investment managers is to make decisions based on financial considerations. Indeed, it is their responsibility to make decisions for financial reasons only.

Philip Morris USA position:

1. Investment managers must maintain a clear distinction between political and financial considerations. If some activist group's protests were allowed to affect investment decisions, virtually no industry or organization would be safe from attack. Even U.S. government bonds would be vulnerable, as the government is criticized by some for being in the weapons and nuclear energy businesses, and by others for deriving substantial revenue from taxes on controversial products like tobacco, alcoholic beverages and gasoline.

2. Investment managers must maintain a long-term perspective. It would be wrong to hold the financial security of thousands of people hostage to political or social passions of the moment.

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SOCIAL COSTS

Executive Summary:

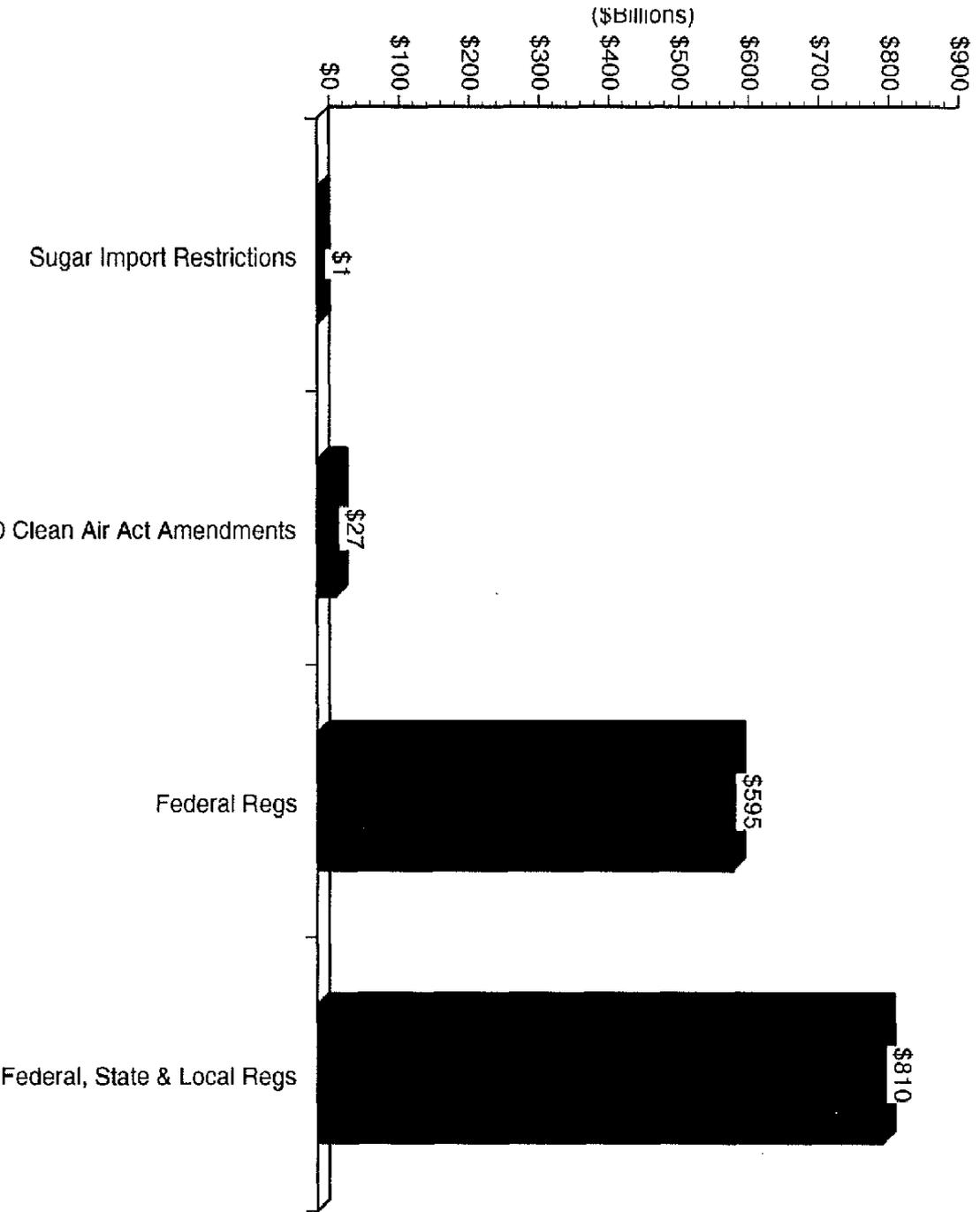
Some anti-smoking critics claim that cigarette smoking imposes an alleged "social cost" on society. According to the New York Times, in testimony before a Congressional committee in March 1994, former Johnson and Carter Administration official Joseph Califano claimed that in-patient treatment for smoking related diseases accounted for \$16 billion of Medicare's \$87 billion budget.

But the very idea of an alleged "social cost" of human activity is spurious. Shall we assign a "social cost" to time "wasted" eating, sleeping or relaxing when productive work could be done?

Philip Morris U.S.A. position:

1. Almost any activity can be said to impose "social costs." Obesity allegedly "costs" \$39 billion a year (*Journal of the American Medical Association*, October 19, 1994), and softball sliding injuries produce an annual "cost" of \$2 billion in medical expenses alone (*The American Journal of Sports Medicine*, November 1990). It is as wrong to put a punitive tax on cigarettes as it would be for the government to levy special taxes on high fat foods or bats and balls.
2. Smokers often pay extra for health and life insurance. In addition, smokers pay federal, state and local governments more than \$14 billion a year in taxes that non-smokers do not pay.
3. Proponents of social cost theory assume smokers are less productive or miss work more often than other workers. In fact, a number of studies have concluded that just the opposite is true. The Bureau of National Affairs, for example, conducted a study which found that only five percent of the companies that banned smoking reported any financial savings. A U.S. Chamber of Commerce study found no significant effect of smoking on employee absenteeism.
4. Social cost theory implies that citizens are the property of the state. Their loss to the workforce thereby becomes equivalent to the loss of a steer on a ranch or the breakdown of a piece of machinery. This reasoning may be appropriate for machines and animals, but not for human beings.
5. There have also been charges made about the alleged "social costs" of environmental tobacco smoke on non-smokers' health care costs. However, in testimony before a U.S. Congressional committee, Congressional Research Service Senior Specialist Jane Gravelle stated: "Our assessment of the existing evidence on passive smoking was made as a basis for drawing conclusions about the efficiency justifications for an increase in the cigarette tax. Based on that evidence...our evaluation was that the statistical evidence does not appear to support a conclusion that there are substantial health effects of passive smoking."

Societal Costs of Government Regulations



Source: GAO, Heritage Foundation,

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TOBACCO REGULATION

Executive Summary:

Critics claim that federal, state and local regulation of tobacco products is insufficient. The fact is, few other consumer products are as regulated, in so many ways, or by so many agencies, as tobacco products. No additional regulation is warranted.

Philip Morris U.S.A. position:

I. Cigarettes are already among the most highly regulated consumer products. From seed-bed to sales-counter, from how the product is produced to where and when it may be used, tobacco products are subject to extensive government regulation. Following are just a few of the agencies that have regulatory control over tobacco:

Agriculture:

- United States Department of Agriculture: Inspects all tobacco imported into the U.S.
 - Agricultural Stabilization and Conservation Service: Sets production quotas and price levels for tobacco leaf.
 - Commodity Credit Corporation: Sets production quotas and price levels for tobacco leaf.
 - Agricultural Marketing Service: Categorizes individual lots of tobacco for auction purposes.

Production:

- Bureau of Alcohol, Tobacco and Firearms: Regulates disclosure of certain information on every tobacco pack or carton. Prohibits certain promotional practices.
- Department of Health and Human Services
 - Office on Smoking or Health: Cigarette manufacturers have been required since 1986 to submit annually to HHS a complete list of all ingredients added to tobacco in the manufacture of cigarettes.
- Federal Trade Commission: Regulates proper reporting by tobacco companies of cigarette "tar" and nicotine levels. Ensures compliance with health warning requirements.

Sale:

- Bureau of Alcohol, Tobacco and Firearms: Collects excise tax revenue.
- State revenue departments: All 50 states collect excise taxes, ranging from a high of 75 cents per pack in Michigan to Virginia's 2.5 cents per pack. Each state has in place a regulatory office to oversee the collection of these tax revenues.
- All 50 states have in place legislation to restrict the sale of cigarettes to minors.

Restrictions on Usage:

- Department of Health and Human Services: In 1990 HHS launched a seven-year, \$165 million anti-smoking program known as ASSIST, to fund anti-smoking campaigns in 17 states.
- Department of Labor
 - Occupational Safety and Health Administration: In 1994 OSHA proposed sweeping new restrictions that would virtually ban smoking from the nation's workplaces. OSHA's proposed regulation is currently under administrative review.
- Department of Transportation
 - Federal Aviation Administration: Enforces Congressional ban on smoking during most domestic flights.
 - General Services Administration: Regulates smoking in most federal buildings.
 - All 50 states have in place legislation to dictate where public smoking is permissible. In addition, hundreds of localities have similar laws in place.

Marketing Practices:

- Federal Trade Commission: Through the Federal Cigarette Labeling and Advertising Act, Congress has banned cigarette advertising on television and radio. This law also requires all cigarette packs, cartons and advertisements to carry specified health warnings. The FTC has the authority to enforce this law.

2. The U.S. Congress, over the past 30 years, has established a comprehensive regulatory scheme, reserving to itself major decisions concerning tobacco, including delegation of authority to agencies.

3. The government agencies that currently regulate cigarettes are best suited to do so. Anti-smoking advocates sometimes complain that cigarettes are not subject to regulation under the Federal Hazardous Substances Act, the Toxic Substances Control Act or the Controlled Substances Act. Cigarettes do not fall into the classes of products addressed by these statutes, and the agencies responsible for administering them lack the expertise and resources to regulate cigarettes.

4. Claims of under-regulation are political. The true aim of anti-tobacco activists is not to ensure that tobacco products are regulated, but to put the tobacco industry out of business and eliminate a product that nearly 50 million Americans use and enjoy. Any system of regulation that fails to guarantee these results will be decried by anti-tobacco activists as "under-regulation."

5. FDA Commissioner David Kessler has indicated his desire to assert regulatory control over tobacco products. Although Commissioner Kessler has not outlined the specifics of his plan, there is speculation that his true motivation is to impose regulations that would severely restrict, if not prohibit, the marketing and sale of tobacco products. Philip Morris believes that FDA jurisdiction over tobacco products is unjustifiable and unwarranted. Most simply, tobacco is neither a food or a drug. The FDA itself has repeatedly stated in the past that the agency does not have the legal authority to regulate cigarettes as ordinarily marketed. Further, the FDA is already unable to meet its current responsibilities. To extend the FDA's jurisdiction to include another huge industry would be foolish.

ADDICTION

Executive Summary:

Over the years, anti-smokers have claimed that nicotine is addictive and that cigarettes should therefore be more rigorously regulated. In recent months, these claims have been revived, most notably by Food and Drug Administration Commissioner David Kessler and Representative Henry Waxman (D-CA).

Philip Morris believes that nicotine is not addictive. More than 40 million Americans have quit smoking, 90 percent have done so on their own without any outside help. Furthermore, smoking is not intoxicating nor does it impair judgment as truly addictive drugs do. Current efforts to label nicotine as "addictive" trivialize the very real social crises of addiction to drugs like heroin and cocaine.

Philip Morris U.S.A. position:

1. A reasonable definition of "addiction" looks to three objective phenomena: intoxication, tolerance and withdrawal (or physical dependence). For many years, the scientific community, including the 1964 Surgeon General's Report, considered smoking to be a habit, rather than an "addiction." When examined in light of the preceding criteria, only through the adoption of ever looser and less verifiable criteria did some authorities, as in the 1988 Surgeon General's Report, describe cigarettes as "drugs of addiction."
2. In the past 40 years, overall nicotine yields of our cigarettes have declined by 50 percent, in response to consumer preferences. Consumers' desires for lower-yield products does not fit the profile of addictive behavior.
3. Nicotine is not addictive. Many people tend to loosely use the word "addiction" to refer to their enjoyment of a particular product, and this usage has been finding its way into official pronouncements and the scientific literature. Currently, there is scientific literature that argues that everything from caffeine to shopping to heroin is addictive.
4. Nicotine occurs naturally in tobacco. The presence of nicotine, however, does not make cigarettes a drug or smoking an addiction. Caffeine occurs naturally in coffee but few would consider coffee a drug or coffee drinkers to be "drug addicts."
5. People can and do quit smoking. According to the 1988 Surgeon General's Report, there are more than 40 million former smokers in the United States and 90 percent of those who quit did so on their own, without any outside help. These facts are at odds with the view that cigarette smokers are "addicted" to nicotine.

6. Smoking is not intoxicating nor does it impair judgment. No one has claimed that smokers cannot function normally nor is anyone likely to be arrested for "driving under the influence of cigarettes."

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CHARGES OF NICOTINE "SPIKING"

Executive Summary:

On February 24, 1994, and in subsequent broadcasts, ABC-TV's "Day One" program charged that Philip Morris "spikes" and "fortifies" its cigarettes with nicotine. Food and Drug Administration Commissioner David Kessler thereafter made similar charges beginning with the public release of a letter he sent to a national anti-smoking organization. The letter suggested that tobacco companies add nicotine to cigarettes and intentionally manipulate the level of nicotine in cigarettes.

These allegations are totally false. Philip Morris U.S.A. does not "spike" cigarettes with nicotine or "manipulate" nicotine levels. In fact, the cigarette manufacturing process produces cigarettes that contain less nicotine than was in the raw materials from which they were made. Filtration further results in lower yields of all smoke components, including "tar" and nicotine. Nicotine (and "tar") yields appear in every advertisement for cigarettes. Overall nicotine yields of our cigarettes have been falling continually for decades.

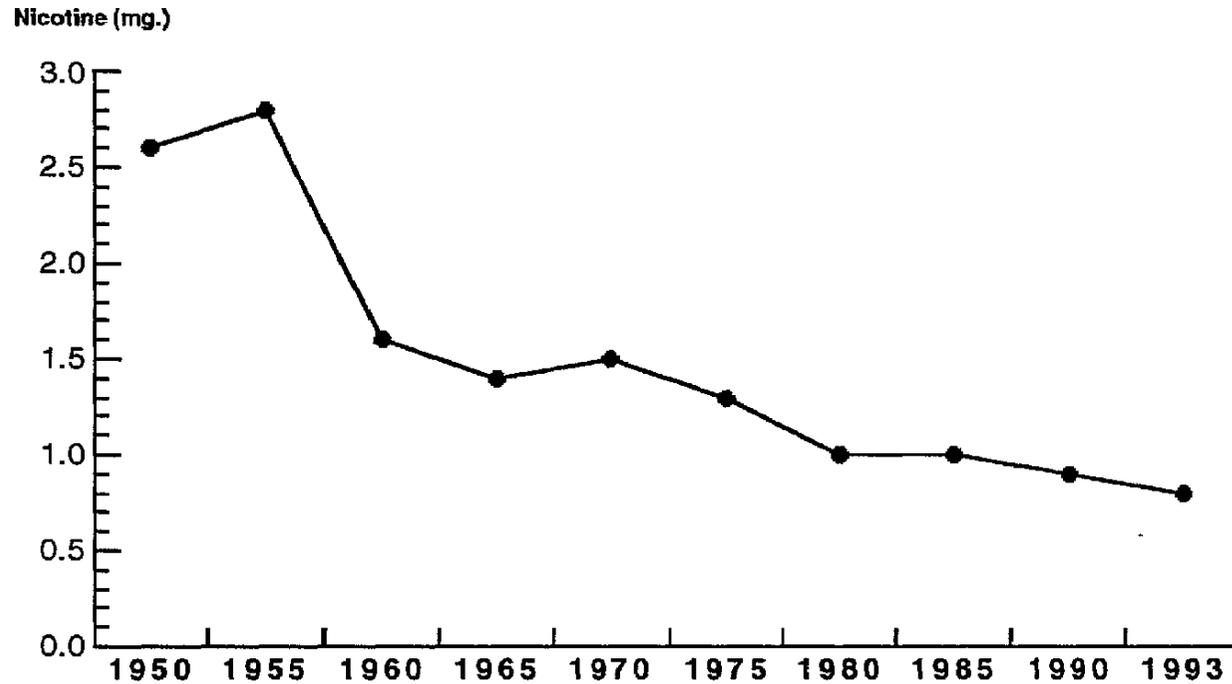
Philip Morris U.S.A. position:

1. Philip Morris U.S.A. does not "spike" its cigarettes with nicotine. Nicotine occurs naturally in tobacco. There is nothing in the processing of tobacco or the manufacture of cigarettes by Philip Morris that increases the nicotine in our products above what is naturally found in tobacco. In fact, nicotine levels in raw, unprocessed tobacco are higher than those found in the finished cigarette.
2. The overall nicotine yield of our cigarettes has declined by more than 50 percent over the last 40 years.
3. We manufacture products covering a range of "tar" and nicotine yields. These yields are published in all of our advertisements.
4. Philip Morris has spent hundreds of millions of dollars attempting to develop a cigarette made with denicotinized tobacco that would have acceptable flavor characteristics. So far, we have been unsuccessful.
5. In March 1994, Philip Morris initiated a \$10 billion libel suit against ABC. In the complaint Philip Morris charges that ABC knowingly made a number of false allegations against Philip Morris and that both Philip Morris Companies Inc. and Philip Morris U.S.A. have been severely damaged by the false and defamatory statements made by ABC. A trial date of June 5, 1995 has been set.

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The Reduction of Nicotine in Cigarette Smoke

Sales Weighted Industry Average Nicotine



Sources: "Nicotine, Smoking, and the Low Tar Programme," Wald and Froggatt (1989)

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The Maxwell Consumer Report; Management Science Associates.

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ENVIRONMENTAL TOBACCO SMOKE (ETS)

Executive Summary:

In January 1993 the U.S. Environmental Protection Agency (EPA) issued a "risk assessment" categorizing environmental tobacco smoke (ETS) as a Group A (known human) carcinogen. The EPA report was based upon a review and statistical analysis of selected research studies. The EPA report continues to receive considerable media attention, and has been the basis for lawsuits against the tobacco industry, legislative and regulatory efforts to restrict smoking, and private employers' decisions to ban smoking.

Philip Morris U.S.A. believes the EPA's risk assessment is riddled with inconsistencies and inaccuracies. We believe that even before the EPA set out to compile this report, the researchers involved had already decided that the report would conclude that secondhand smoke is a carcinogen. Philip Morris has joined other industry groups in a federal lawsuit to have the entire report declared null and void.

Philip Morris U.S.A. position:

1. The individuals who conducted this investigation did no original research but instead selectively sorted through existing research.
2. For example, the EPA chose to omit from its report one of the largest studies ever conducted on this issue. Funded in part by the National Cancer Institute, this study reported no overall statistically significant increased risk of lung cancer among spouses of smokers.
3. Of the 30 studies that were included in the EPA report, 24 showed no statistically significant relationship between ETS and lung cancer among non-smokers. But the EPA took these studies, and simply manipulated the data to support its pre-conceived notions. The six that did show a statistical association did not take into consideration confounding factors including cultural and environmental influences.
4. Of the 30 studies included in the report, only 11 were conducted in the United States. None of the 11 U.S. studies originally reported an overall statistically significant increased risk of lung cancer for the non-smoking spouses of smokers.
5. None of the studies included in the EPA report focused on exposure to ETS in the workplace.
6. The EPA claims a relative risk for lung cancer in the non-smoking spouses of smokers of 1.19 (a relative risk of 1.0 means there is no statistical risk.) The scientific community considers a relative risks of less than 2.0 to be "weak." To put the EPA's claimed relative risk of 1.2 into perspective, one study has reported a relative risk of developing lung cancer associated with drinking green tea to be 2.7.

7. According to a National Cancer Institute press release, dated October 26, 1994: "In epidemiologic research, relative risks of less than 2 are considered small and are usually difficult to interpret. Such increases may be due to chance, statistical bias, or effect of confounding factors that are sometimes not evident."

8. In June 1993 we joined with other industry groups, including R.J. Reynolds Tobacco Company, in filing a lawsuit in federal court to have the entire EPA report declared null and void. In July 1994 the federal district court rejected the EPA's motion to dismiss the industry action. This ruling by the court permits the case to proceed toward trial for a full review of the merits of our claims.

9. Some people are bothered or annoyed by cigarette smoke in the air, and Philip Morris believes their rights and preferences should be respected. We support the principle of accommodation, whereby the preferences of both non-smokers and smokers can be met through properly established and maintained designated areas. With this in mind, we created The Accommodation Program, which now has more than 14,000 member businesses across the country. Through The Accommodation Program, businesses including restaurants, bars, hotels, motels, bowling centers and shopping malls are provided with materials about how to establish and maintain properly designated seating areas for non-smokers and smokers.

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SMOKING RESTRICTIONS -- WORKPLACE

Executive Summary:

The Occupational Safety and Health Administration (OSHA), a division of the U.S. Department of Labor, has proposed a regulation that could effectively ban smoking in all public buildings and indoor workplaces, including restaurants and bars. The proposal is so broad, it could include home offices and homes if there is a hired individual such as a plumber or electrician present. Philip Morris U.S.A. believes the OSHA proposal is unnecessary and overly broad, and that business owners, employees and customers should be permitted to develop workplace smoking policies that suit their own particular preferences, without government interference.

Philip Morris U.S.A. position:

1. Philip Morris U.S.A. favors accommodation of both smokers and non-smokers in the workplace through designated smoking areas. We believe a smoking policy that provides for well-maintained and easily accessible smoking areas is the fairest and most efficient way to settle smoking conflicts.
2. A large majority of Americans agree with us. A March, 1994, *USA Today/CNN* poll found that two-thirds of respondents favor workplace smoking policies that provide smoking accommodation.
3. Philip Morris U.S.A. acknowledges that smoking may be bothersome or annoying to some people, and that is why designated smoking and non-smoking sections work best.
4. Workplace smoking policies often fail to address the real source of employee discomfort -- inadequate ventilation. Building ventilation systems can become choked with fungus, mold and other allergenic substances. Tobacco smoke in the air is the symptom -- not the cause -- of some indoor air problems. In fact, tobacco smoke has been found to be the cause of indoor air quality complaints in only two to five percent of the buildings studied, according to The National Institute of Occupational Safety and Health.
5. OSHA conducted a public comment period, during which more than 200,000 letters were received from consumers and business owners in opposition to the agency's proposed smoking regulations. In September 1994 OSHA initiated hearings to consider the proposed regulations. Following the hearings, a revised regulation may be issued. Whatever national smoking policy OSHA decides to implement will, in all likelihood, not take effect until late 1995 or early 1996.

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SMOKING RESTRICTIONS -- RESTAURANTS and PUBLIC PLACES

Executive Summary:

Some cities, and even the states of Vermont, Utah and California, have passed laws banning smoking in restaurants, hotels, outdoor sports stadiums and even shopping centers. Philip Morris U.S.A. opposes such restrictions in favor of accommodation. Philip Morris believes that business owners should be permitted to determine their own smoking policies.

Philip Morris U.S.A. position:

1. A March, 1994 *USA Today/CNN* poll found that 61 percent of respondents favored smoking sections in restaurants and 78 percent favored accommodation in hotels and motels.
2. The owners and managers of individual restaurants, hotels and other businesses serving the public are best qualified to determine the needs and preferences of their customers. Indeed, business owners already have the option of banning smoking.
3. Restaurant smoking bans can impose severe hardships on restaurant owners and employees, who lose business to surrounding communities. For example, the Charlton Research Company conducted a survey of Los Angeles restaurants shortly after that city's smoking ban went into effect. More than half of the restaurants surveyed say the smoking ordinance has impacted the amount of business they do. In these restaurants receipts were down (on average) over 24%, or over \$11,000 per month. Further, 16% of all restaurants surveyed have had to lay off workers. According to the Los Angeles Times, businesses in the city of Los Angeles lost almost \$10 million when the National Association of Convenience Stores decided to hold their annual convention someplace else.
4. Philip Morris U.S.A. believes that non-smokers and smokers can be accommodated in public places. So, we created The Accommodation Program as a tool for restaurant owners and other businesses in the hospitality industry. The program provides welcome signs, employee training materials, technical bulletins on ventilation, and a comprehensive "Source Book" with details on how to create separate areas to accommodate the preferences of all customers, non-smokers as well as smokers. To date, more than 14,000 businesses nationwide are participating in The Accommodation Program. Business owners can find out more about the program by calling 1-800-800-5197.

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LAWSUIT ACTIVITY AGAINST PHILIP MORRIS

Executive Summary:

In recent months Philip Morris has been sued, along with all other tobacco companies, in lawsuits seeking new types of relief. Several of these lawsuits are brought as "class actions" by individuals who seek to represent millions of other present and former smokers who have allegedly suffered harm from smoking. A few additional lawsuits are brought by states seeking to recoup Medicaid and other related health care costs supposedly associated with smoking. These cases claim members of the tobacco industry were aware that smoking was a health hazard or "addictive."

Philip Morris believes each of these cases to be without merit. As we have done successfully in other smoking and health litigation, we will vigorously defend Philip Morris against these false and legally invalid allegations.

Class Action Lawsuits

Philip Morris U.S.A. position:

1. Class actions are inappropriate in situations where the lawsuit cannot be decided on facts that are common to all class members and where a determination has to be made on an individual-by-individual basis whether a given person is a "class member." Whether a smoker is "addicted" or has a disease "caused" by cigarette smoking are examples of exactly the type of individualized inquiries not suitable for a class action.
2. If cases are allowed to proceed as class actions, tens of millions of individual trials will have to be held just to resolve whether a particular person is a "class member," for instance, and whether the person is "addicted" to cigarette smoking. These cases will burden the courts for years and years without any savings in time or money for the parties or the judiciary.
3. Lawyers who represent plaintiffs in so-called class actions stand to profit the most from the lawsuits -- as much as 25 percent of any award.
4. Juries have consistently rejected smokers' attempts to recover money in past lawsuits because jurors understand that individuals make an informed choice whether to smoke. The same common sense result will be reached in any class action.
5. Except for the number of plaintiffs, class action lawsuits are not significantly different from the individual product liability cases that Philip Morris and others in the tobacco industry have been successfully defending for 40 years. No tobacco industry defendant has ever paid a penny in damages in any of these suits. The new class action strategy will not change the ultimate outcome.

State Medicaid Recovery Lawsuits

1. The few suits by states to recover Medicaid and other health-related costs allegedly associated with tobacco are an improper effort to change the rules of litigation in the states' favor -- at the expense of tobacco companies' constitutional rights and settled principles of law.
2. States are attempting in the Medicaid recovery suits to eliminate the tobacco industry's traditional defenses, like freedom of choice, that have been so successful in defeating individual suits brought by smokers. These defenses are applicable, despite the states' endeavor to avoid them, because the states are subject to the same requirements which would exist if each Medicaid recipient had brought suit.
3. States cannot rely on statistics to escape their responsibility to prove that each Medicaid recipient's illness was caused by smoking. Individualized proof of liability, causation, and damage is required.
4. States that sue to recover Medicaid costs may -- even if they "win" -- end up losing money because of the expense of the litigation, the tremendous bonanza in attorneys' fees the plaintiffs' attorneys will reap and the states' obligations to reimburse the federal government for its share of Medicaid costs.
5. State revenues from cigarette excise taxes, cigarette sales permits and vending machine licensing fees are enormous. It would be inequitable for the states to recover the costs of treating illnesses allegedly associated with smoking without offsetting the income received by the states from cigarettes.

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ADVERTISING RESTRICTIONS

Executive Summary:

Anti-smokers claim that tobacco advertising is a primary reason why minors smoke, and use this false claim as justification for supporting severe restrictions on cigarette advertising and sales practices.

Philip Morris U.S.A. opposes all attempts to restrict the right to advertise. Tobacco is a legal product, and all truthful speech, including advertising, is protected by the First Amendment to the U.S. Constitution.

Philip Morris U.S.A. Position:

1. Free speech, which includes truthful commercial speech, is a foundation of American society and one of the great strengths of our form of government.
2. Restricting or banning truthful speech about legal products would set a dangerous precedent. Further restrictions or bans on tobacco ads would encourage some people to seek further restrictions or bans on advertising for other controversial products, such as alcohol beverages, meat, sugar, sports cars, fur, and so on.
3. People do not start smoking because of cigarette advertising. In recent polls, the Gallup Organization asked smokers -- both adults and youth -- to identify the factors that influenced them to start smoking. In the reported data, cigarette advertising or cigarette promotion were not listed as factors that influenced them to start smoking. In fact, Gallup reported that for adult smokers, "The number-one reason smokers said they started smoking was because other friends smoked." (Thomas, R.M.; Larsen, M.D.; Smoking Prevalence, Beliefs and Activities by Gender and Other Demographic Indicators. Princeton, NJ/The Gallup Organization, Inc., 1993.)
4. For youth smokers, Gallup reported, "The most common reason adolescents start to smoke is because they have friends who smoke." (Larsen, M.D.; Colsher, P.; Smoking Prevalence and Attitudes Towards Smoking Among Adolescents. Princeton, NJ/ The Gallup Organization, Inc., 1994.)
5. Many published research studies conclude that aggregate cigarette advertising expenditures in the United States have little or no effect on aggregate consumption, but that advertising is one source of competition between brands for marketshare. (See, e.g., Wilcox, Gary B. (1991) Cigarette Brand Advertising and Consumption in the U.S.: 1949-1985, Journal of Advertising Research, August/September (1991), pp. 61, 64).
6. One way to affect brand equity is advertising. The probability that a smoker may buy another brand is directly related to the equity of their own brand. On any given purchase occasion, 23% of the 50 million adult smokers -- or as many as

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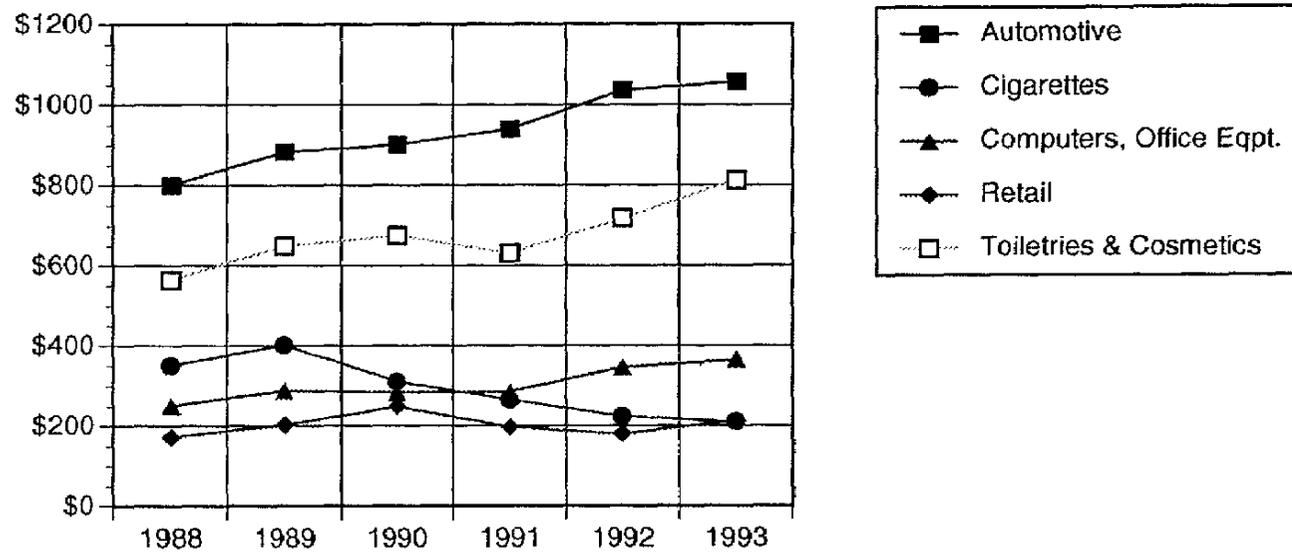
30,000 every day -- in the United States may be willing to purchase a brand other than their own. Given that the U.S. market has annual sales of \$45.2 billion, the total buying power of those smokers could be as much as \$10.3 billion. (Roper Reports 90-2, Question 58, P. 39)

7. Proposals are routinely made in the U.S. Congress to repeal the deductibility of the tobacco industry's advertising expenses. Advertising deductibility is a tax exemption claimed by virtually every business that advertises in this country. Philip Morris U.S.A. believes that attempts to eliminate the deductibility of tobacco advertising are "back-door censorship." Using the tax code to limit the freedom of speech would violate the most basic American values. Truthful commercial speech is protected by the First Amendment to the U.S. Constitution.

8. Advertising costs are a legitimate business expense, as essential to industry as salaries, plants and equipment. If tobacco advertising expenses can be singled out for punitive tax treatment, what other business expenses will become non-deductible? Using the tax code to enforce political correctness could open new avenues for tyranny and *de facto* censorship.

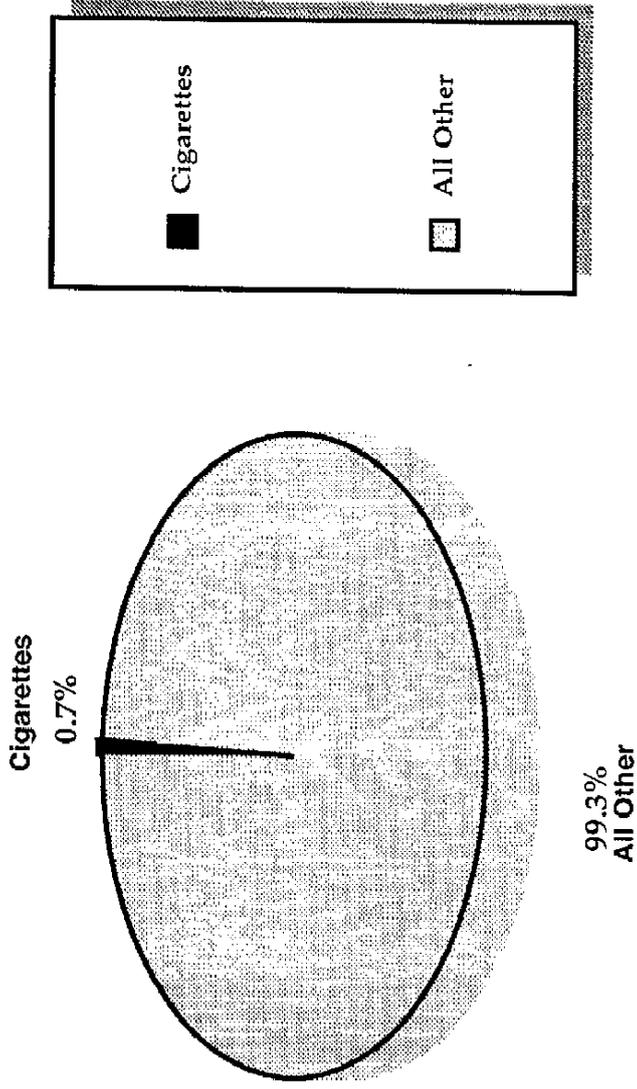
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U.S. Magazine Ad Spending 1988-1993
(Millions of Dollars)



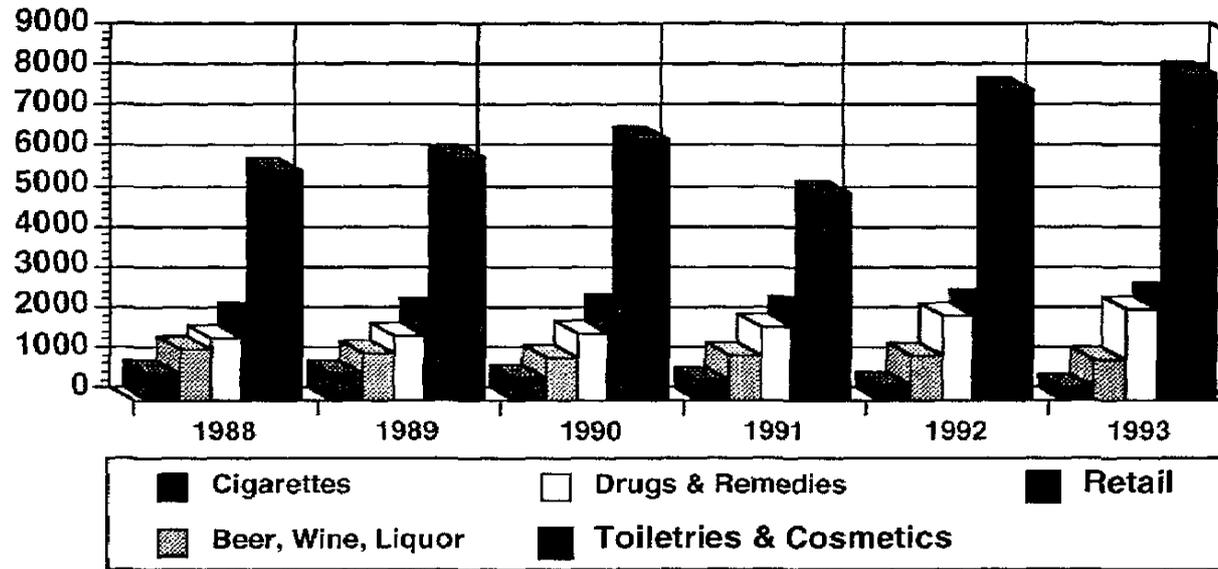
Data Source: Advertising Age

1993 Cigarette Ad Spending vs. All Other U.S. Ad Spending



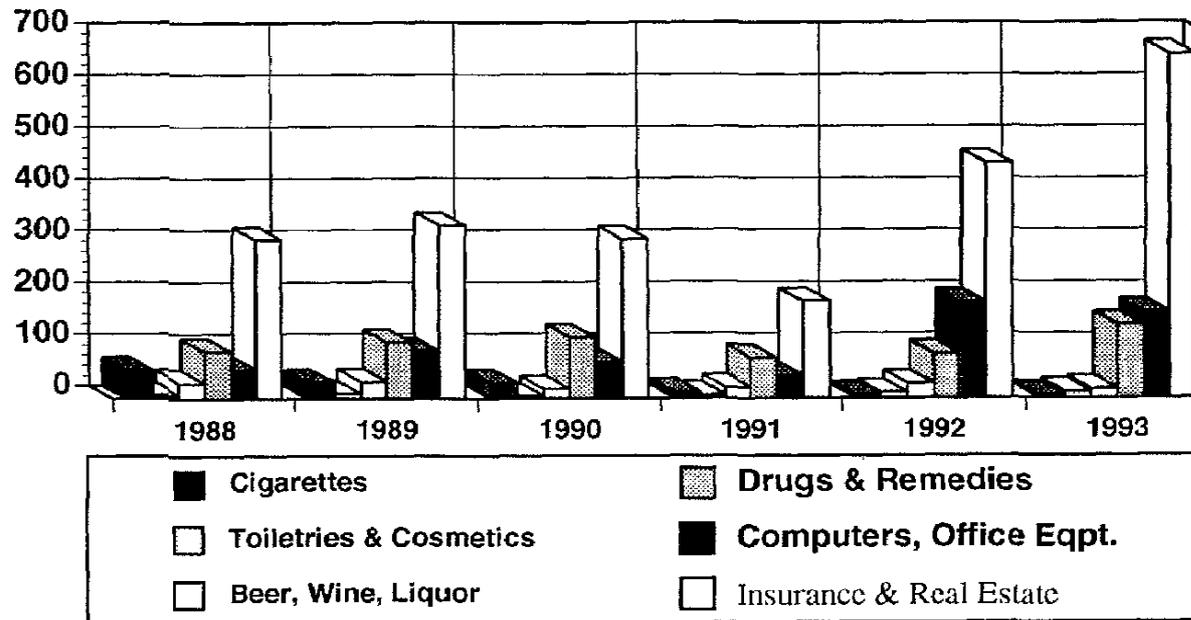
Data Source: Advertising Age

Total U.S. Ad Spending 1988-1993
 (Millions of Dollars)



Data Source: Advertising Age

U.S. Newspaper Ad Spending 1988-1993
 (Millions of Dollars)



Data Source: Advertising Age

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POINT-OF-PURCHASE DISPLAYS AND SELF-SERVICE SALES

Executive Summary:

Legislative proposals have been introduced, primarily at the local level, to ban all point-of-purchase displays and to eliminate "self service sales," which include cigarette vending machines. Supporters of this legislation claim that self service sales make it easier for minors to steal cigarettes, and that point of purchase advertising is an enticement for children to smoke.

Philip Morris U.S.A. believes that these allegations are unfounded and would create unnecessary hardships for retailers, would unfairly infringe on our right to advertise, and create an unnecessary inconvenience for adult consumers.

Philip Morris U.S.A. position:

1. It is illegal in all 50 states to sell cigarettes to minors. Before additional laws aimed at retailers are imposed, the laws already on the books should be enforced.
2. If minors steal cigarettes from a self-service display, the store manager, not the government, is in the best position to deal with the problem.
3. Eliminating self-service displays places a greater burden on store personnel. Either more employees would have to be hired, or those already employed would be forced to spend a greater proportion of their time with customers who want to buy only cigarettes.
4. Eliminating point-of-sale materials would also impact a retailer's ability to participate in programs offered by manufacturers.
5. In addition, once the precedent is set for eliminating point-of-sale advertising for one controversial product, it is only a matter of time before other items, such as beer, liquor and snack-food products, are also attacked.
6. Eliminating self-service displays creates an inconvenience for adult smokers.

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Move to Advertising

MARKETING PRACTICES

Sporting and Cultural Event Sponsorships

Executive Summary:

A part of Philip Morris U.S.A.'s marketing strategy is to sponsor events, including sporting events, concerts and cultural events, that are attended by adult smokers. Over the years we have sponsored soccer, bowling, women's tennis, IndyCar racing, country music, rock and roll, jazz and rhythm and blues, just to name a few.

Anti-smokers, including some members of Congress, believe that we should not be allowed to participate in these events. Despite having no credible supporting evidence, opponents claim that our participation is inappropriate and causes children to smoke.

We believe that sponsorship of sporting and cultural events should remain a business, not a government decision, and we will continue to pursue sponsorships that fit our marketing objectives.

Philip Morris U.S.A. position:

1. Philip Morris U.S.A. directs its marketing efforts at smokers 21 years of age and older. We sponsor activities where we believe a large number of smokers are in attendance, and thus through sponsorship of sporting and cultural events we gain an opportunity to communicate directly with those consumers.
2. Who should or should not sponsor sporting or cultural events should remain a business decision -- not a government decision. Our sponsorship will continue to be based on whether the event or program fits our marketing needs -- that is, whether adult smokers attend the events -- as well as whether we believe we are getting good value for our sponsorship dollars. We will continue to make these decisions based on business criteria.
3. Athletes and artists do not endorse our products.
4. Philip Morris U.S.A. has been accused of paying movie producers, actors and other people in the film industry to place PM products on screen. These accusations are false. We neither solicit nor accept any offers to have our products, signage or other advertising and promotions placed in any film, television show or theater production. We turn down every offer and request that comes our way.

MARKETING PRACTICES
Marketing to Women, Minorities, Special Groups

Executive Summary:

Philip Morris U.S.A. markets cigarettes to all adults who choose to smoke, regardless of their race, color, gender, creed or sexual orientation. All adults should be free to make lifestyle decisions.

Philip Morris U.S.A. position:

1. Underlying the charge that women and minorities make easy targets for marketing is the chauvinistic belief that they are incapable of making informed personal decisions for themselves. Dr. Benjamin Hooks, former executive director of the National Association for the Advancement of Colored People, said "critics of tobacco marketing efforts believe women and blacks are not capable of making their own free choice and need guardian angels to protect their best interests."
2. Philip Morris believes that American adults have the intelligence and discretion to make their own choices about whether to smoke. As former Congressman Alex McMillan (R-NC) pointed out: "The fact is that the complaints do not come from those people who are allegedly targeted but from anti-smoking zealots who use them to achieve their own agenda."
3. The diverse array of media in which we advertise reflects the diverse group of adult consumers who smoke. Smokers come from all walks of life and represent diverse interests and backgrounds. Our advertising and promotions are designed to reach all adults who choose to smoke.

MARKETING PRACTICES

Allegations Concerning Marketing to Youth

Executive Summary:

Critics claim that Philip Morris U.S.A. intentionally markets cigarettes to minors. These unfounded allegations are used to support calls for increased restrictions on tobacco marketing and advertising practices.

Philip Morris U.S.A. does not market cigarettes to minors. In fact, we have committed considerable time and resources to preventing minors from smoking. We abide by the tobacco industry's strict, detailed, voluntary Cigarette Advertising and Promotion Code and support laws, now on the books in all 50 states, that make it illegal to sell tobacco products to minors.

Philip Morris U.S.A. position:

1. Philip Morris does not want minors to smoke. Philip Morris supports laws, now on the books in all 50 states, that make it illegal to sell tobacco products to minors. To help retailers comply with these laws, we support the "It's the Law" program, which helps educate retailers and their employees about minimum age laws, and how to better comply with them.

2. The tobacco industry's voluntary Cigarette Advertising and Promotion Code includes strict rules for almost every element of advertising. All of the models appearing in our ads must be -- and look -- at least 25 years old, for example. All of our promotional items are available in adult sizes only, and none may have any special appeal to children. Philip Morris does not place advertising in college publications, even though most college students are 18 years of age or older and thus legally old enough to smoke.

3. According to the 1994 Surgeon General's Report: "A misguided debate has arisen about whether tobacco promotion "causes" young people to smoke -- misguided because single-source causation is probably too simple an explanation for any social phenomenon." (Surgeon General's Report, page iii)

4. Philip Morris' advertising is directed at individuals who have already made the decision to smoke. As a practical matter, however, despite our best efforts, it is impossible for us to advertise cigarettes to smokers while at the same time shielding all non-smokers, including minors, from passive exposure to our ads. In addition, however, there is no serious scientific evidence which supports allegations that if children can remember certain slogans or imagery for cigarettes, they are more likely to start smoking. Are children more likely to buy life insurance, for example, if they remember that the cartoon character Snoopy appears in ads for Metropolitan Life Insurance?

5. As of 1993, total advertising expenditures by all U.S. tobacco companies accounted for less than one percent of the total U.S. media expenditures for all advertisers. (Advertising Age, September 28, 1994.)

6. Data show that cigarette advertising expenditures routinely fall well below advertising expenditures for other industries. According to data in Advertising Age, for the period 1988 to 1993, all cigarette advertising expenditures continue to decline. Currently, in terms of total advertising expenditures, cigarette advertising ranks fifth behind advertising expenditures for beer, wine and liquor, drugs and remedies, toiletries and cosmetics and retail. In terms of magazine advertising, Advertising Age data show that cigarette advertising currently ranks fourth along with retail advertising, behind advertising expenditures for computers and office equipment, toiletries and cosmetics and automotive. In terms of newspaper advertising, cigarette advertising expenditures currently rank sixth behind advertising expenditures for toiletries and cosmetics, beer, wine and liquor, drugs and remedies, computers and office equipment and insurance and real estate. (Advertising Age, September 28, 1994.)

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*Beavis
New Section*

MARKETING PRACTICES

Youth Smoking Initiatives

Executive Summary:

Philip Morris U.S.A. strongly opposes tobacco use by minors. Smoking is an adult choice and it is illegal to sell cigarettes to minors in all 50 states. We have backed up that conviction by supporting programs and legislation to prevent retailers from selling cigarettes to minors.

- 1. Legislative.** Philip Morris U.S.A. supports laws to restrict the sale of cigarettes to minors, and we have worked with states to pass and enforce these laws. Philip Morris believes that retailers who sell cigarettes to minors should be fined. In those states where retailers are licensed, we believe that retailers who repeatedly sell cigarettes to minors should have their licenses revoked.
- 2. Advertising.** We do not place cigarette advertising in publications directed primarily to those under 21 years of age, including school, college, or university media, comic books or comic supplements. PM requires all outdoor advertising suppliers to restrict billboard advertising to at least 500 feet away from any elementary school, junior high school, high school or playground.
- 3. Continuity Programs (Marlboro Adventure Team, Marlboro Country Store, V-Wear Catalogs).** In addition to bearing the federally required Surgeon General's warning, all Philip Morris promotional offers clearly state that they are limited to smokers 21 years of age or older and that respondents must certify their age by including a signature and a date of birth when participating.
- 4. Sales.** Philip Morris U.S.A. supports the "It's the Law" (ITL) program. This program is designed to educate retailers about their state's minimum age law so that they can work with their employees to prevent cigarette sales to minors. More than 50,000 retailers, chains and other interested parties have received ITL materials. ITL materials are available free of charge simply by calling Philip Morris at 1-800-343-0975.
- 5. Trademark Infringement.** We have taken legal action more than 1,800 times in instances where our tobacco brand logos were used illegally; often on products intended for use by minors. We work continuously, on our own and with the United States Customs Service, to prevent the importation and sale of such products and to trace them back to the manufacturer even if the products are never sold in the United States.

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TOBACCO PROHIBITION

Executive Summary:

Some anti-smokers advocate a complete ban on tobacco. This, despite the fact that prohibition has already been tried in this country and didn't work. Philip Morris U.S.A. opposes any attempt to return to prohibition on alcohol or cigarettes, whether it be by an outright ban or excessive taxation.

Philip Morris U.S.A. position:

1. A ban on tobacco would serve no useful purpose. The Volstead Act, which banned beverage alcohol in the 1920's, made criminals out of millions of otherwise law-abiding Americans. A ban on tobacco could have the same effect: it could create an enormous black market and provide lucrative new opportunities for violent criminals.
2. We should learn from the mistakes of other countries. We have seen the severe negative effects of Canada's tobacco taxes, which were so high that they verged on outright prohibition. According to some economists, during the early 1990's one in four cigarettes consumed in Canada was contraband. Cigarettes were being sold from car trunks, without regard for the purchaser's age. The illegal trade became increasingly violent. Finally, in order to stem the tide of smuggling, the Canadian federal government and several provinces rolled back cigarette taxes in February, 1994.
3. If tobacco were banned, local, state and federal agencies would lose more than \$14 billion in excise and sales tax revenues every year. That money would have to be made up with painful new spending cuts or higher taxes.
4. In addition, devastating job loss nationwide could occur if cigarettes were suddenly to become illegal. According to Price Waterhouse, the tobacco industry affects, directly and indirectly, about 2.3 million jobs in the United States. Those jobs generate more than \$66 billion annually in compensation, and the tobacco industry generates more than \$38 billion in taxes when you add up tobacco taxes, personal and corporate income taxes, social security and sales taxes.

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Lanced
David

JOB DISCRIMINATION AND PRIVACY

Executive Summary:

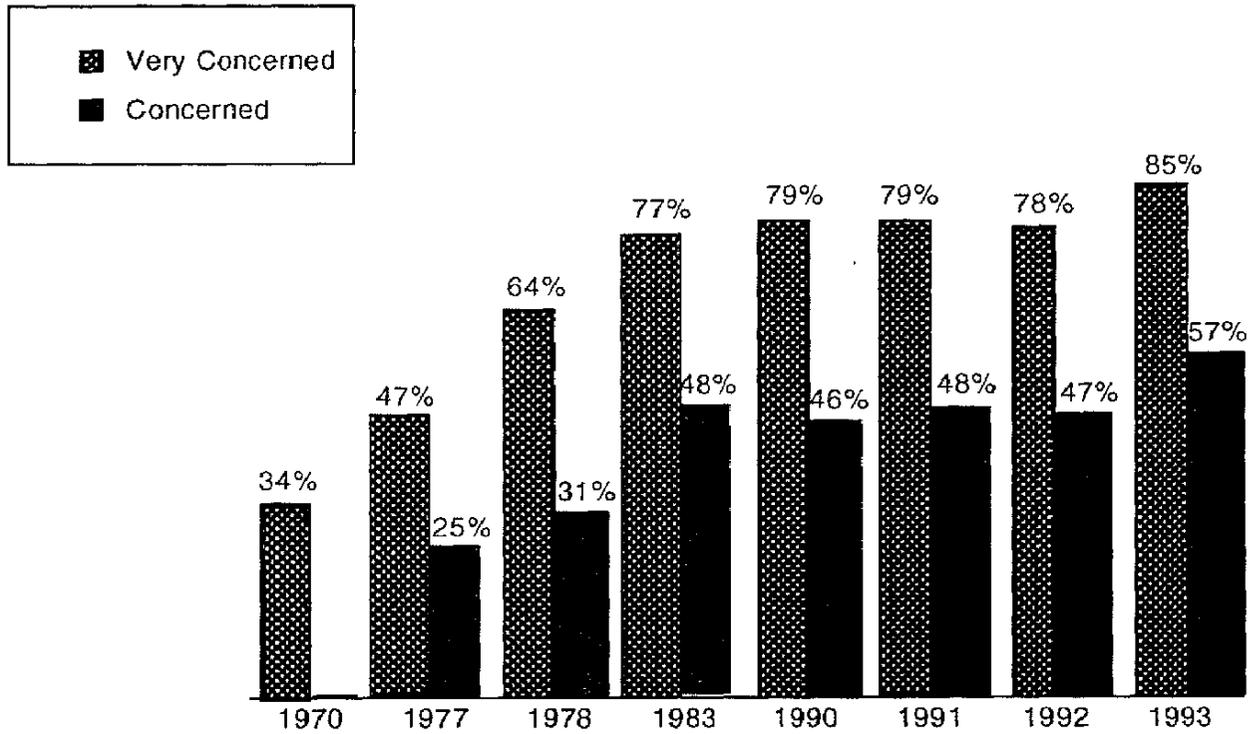
Some employers believe they have a right to dismiss, or refuse to hire individuals who smoke during non-working hours. Employers allege that smokers are less productive, miss work more often and incur greater health care costs than non-smokers.

We believe that such practices are unwarranted intrusions into employees' personal lives. We actively support legislation, now on the books in 29 states and the District of Columbia, to prohibit hiring or firing decisions based on legal off-the-job activities.

Philip Morris U.S.A. position:

1. An employer's right to control the legal behavior of employees ends at the factory gate or office exit. Our society values the distinction between company time and private time, and we should work to preserve that distinction. We support legislation -- already enacted in 29 states and the District of Columbia -- that forbids an employer from penalizing current or prospective employees for smoking off the job.
2. Americans increasingly agree that employers have no right to interfere with employees' off-the-job behavior. The 1993 Harris-Equifax Health Information Privacy Survey reported that 80 percent of respondents are very or somewhat concerned about threats to their personal privacy. Discriminating against employees or job applicants because they choose to smoke when they are away from work paves the way for greater intrusion by employers.
3. Allowing employers to discriminate against employees who may choose to smoke during non-working hours sets a precedent for discrimination against employees who may engage in other lawful activities of which an employer may also disapprove. People who drink alcoholic beverages, consume red meat or snack food, or who engage in activities such as motorcycle riding could all be at risk for on-the-job repercussions.

Public's Privacy Concerns Still Rising, 1970-1993



• Source: Louis Harris and Associates 1970-1993



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TOBACCO PRICE SUPPORT PROGRAM

Jay Poole

Executive Summary:

Tobacco farmers do not receive any federal "subsidy." The Tobacco Price Support Program is a cooperative effort among farmers and manufacturers to avoid sudden catastrophic changes in the supply and price of tobacco.

Philip Morris U.S.A. position:

1. The Tobacco Price Support Program does not cost taxpayers a cent. It relies on government-backed loans, not gifts to farmers. These loans are repaid in full by the farmers -- with interest.
2. The Tobacco Price Support Program is a cooperative effort that guarantees farmers fair prices for their crops, and helps prevent wild swings in tobacco prices that could ruin family farms. Because of agreed upon quotas, the end result of the program is a smaller supply and higher prices for domestic tobacco.
3. Cooperative efforts by farmers have nothing to do with public health policy. Even former Surgeon General C. Everett Koop, an outspoken anti-smoker, has said that the Tobacco Price Support Program is an agricultural and economic matter, not a health issue.

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SOLID WASTE AND PACKAGING

Executive Summary:

Philip Morris U.S.A. strives to be an environmentally-conscious manufacturer of consumer products. As such, Philip Morris U.S.A. conducts its operations in accordance with all applicable environmental laws and regulations. As appropriate, we will anticipate solid waste and other environmental issues and take voluntary initiatives to address them.

Philip Morris U.S.A. position:

1. Philip Morris U.S.A. supports the development of an integrated, comprehensive municipal solid waste management system that takes into account all of the tools of solid waste management including source reduction, recycling, composting, waste-to-energy incineration and landfill. All of these tools need to be used together to help provide effective management of solid waste.
2. Philip Morris U.S.A. also recognizes the value of recycling among the many approaches to municipal solid waste management. For example, our Richmond Manufacturing and Operations Center sends its office and manufacturing waste to the local Municipal Recycling Facility. Our three manufacturing facilities jointly develop strategies for recycling by identifying viable end markets for our manufacturing waste.
3. Although packaging is one of the most visible components of the municipal solid waste stream, it is only one of many such components. Moreover, packaging provides several important benefits including maximizing product quality and consumer satisfaction. Packaging represents only a small fraction of solid waste management issues.

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