POLICY REPORT

THE POLITICAL ECONOMY OF TOBACCO CONTROL IN THE PHILIPPINES:

Trade, Foreign Direct Investment and Taxation

Action for Economic Reforms
American Cancer Society

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ACTION FOR ECONOMIC REFORMS

POLICY REPORT

The Political Economy of Tobacco Control in the Philippines: Trade, Foreign Direct Investment and Taxation

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Acknowledgements

This report was supported by a sub-agreement from the Johns Hopkins Bloomberg School of Public Health with funds provided by the Bloomberg Initiative to Reduce Tobacco Use. Its contents are solely the responsibility of the authors and do not necessarily represent the official views of the Bloomberg Philanthropies or the Johns Hopkins Bloomberg School of Public Health. We thank Joanna Cohen and Jacqui Drope for valuable feedback on this report, and Adriana Appau, Carla Mae Badi, Chipo Dendere, Alex Liber, and Veronica Luckow for helpful research assistance. All errors, of course, remain our own.

Suggested Citation

Jenina Joy Chavez, Jeffrey Drope, Raphael Lencucha, and Benn McGrady. "The Political Economy of Tobacco Control in the Philippines: Trade, Foreign Direct Investment and Taxation." Quezon City: Action for Economic Reforms and Atlanta: American Cancer Society. January, 2014.

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List of Acronyms

AER	Action for Economic Reforms
AFTA	ASEAN Free Trade Area
ASEAN	Association of Southeast Asian Nations
BAT	British American Tobacco
BIR	Bureau of Internal Revenue
BIT	bilateral investment treaty
BOI	Board of Investments
DA	Department of Agriculture
DOF	Department of Finance
DOH	Department of Health
DSB	Dispute Settlement Body (World Trade Organization)
DTI	Department of Trade and Industry
ECOZONES	Special Economic Zones
EO	Executive Order
EU	European Union
FCAP	Framework Convention on Tobacco Control Alliance, Philippines
FCTC	Framework Convention on Tobacco Control
FDI	foreign direct investment
FTA	free trade agreement
GATT	General Agreement on Tariffs and Trade 1994
IAC-T	Interagency Committee – Tobacco
IGO	intergovernmental organization
IRR	implementing rules and regulations
ITH	income tax holiday
JTI	Japan Tobacco International
LMIC	low- or middle-income country
MFN	most favored nation
MNC	multinational corporation
NTCS	National Tobacco Control Strategy
NGO	non-governmental organization
NTA	National Tobacco Administration
PCP	Philippines College of Physicians
PEZA	Philippine Economic Zone Authority
PMFTC	Philip Morris Fortune Tobacco Corporation
PMI	Philip Morris International
PMPMI	Philip Morris Philippines Manufacturing Incorporated
PTI	Philippine Tobacco Institute
RA	Regulation Act
RCEP	Regional Comprehensive Economic Partnership
SWAT	Sector-Wide Anti-Tobacco (committee)
TPP	Trans-Pacific Strategic Economic Partnership Agreement (or "Trans-Pacific Partnership")
TRIPS	Trade-Related Aspects of Intellectual Property Rights
WB	World Bank
WHO	World Health Organization
WTO	World Trade Organization

Executive Summary

Governments continue to confront complexities at the intersection of public health and economic policymaking as they seek to develop and improve tobacco control policies. This report seeks to evaluate these dynamics, including risks, opportunities, and threats, utilizing recent developments at this major policy intersection in the Philippines. The themes that emerge in the Philippine case resonate with experiences in many other countries, making it an ideal case study. The report begins with an examination of the potential implications of emerging international trade and investment agreements. We then investigate the political economy of foreign direct investment and its impacts on tobacco control in the Philippines. Next, through the lens of the intersection of tobacco control and trade/investment policies, we evaluate the challenges of intra-governmental cooperation and coordination. Finally, we focus on a major related development, the country's recent restructuring of tobacco excise taxation, which many believe is developing into a Philippine public health success story. We investigate these key lines of inquiry through a thorough survey of official documents, existing literature, and interviews with 37 key informants from every relevant sector. Each line of inquiry provides discrete lessons for those working at the intersection of tobacco control and economic policy, while highlighting key overlapping institutional features that affect the work of tobacco control proponents. The thread that links these discrete features is the persistent challenge facing different actors to navigate divergent policy objectives across sectors.

Implications of Emerging Free Trade Agreements for Tobacco Control

Free trade agreements (FTAs) substantially liberalize all trade between participating countries and thereby go above and beyond commitments made at the World Trade Organization (WTO). FTAs pose two risks for tobacco control that can be analyzed in the context of the Philippines.

First, in some markets lowering tariffs (customs duties) may stimulate tobacco consumption by leading to lower retail prices for imported products and increasing competition among producers. Our analysis suggests that the risk of lower prices is unlikely to occur in the Philippines because it already has very low tariffs on imported tobacco products, imposes zero tariffs on importation from Association of Southeast Asian Nations (ASEAN) Members (with the exception of Vietnam), and has significant low-cost tobacco leaf-growing and domestic cigarette production.

Second, FTAs pose legal risks to tobacco control in that they may place additional legal constraints on the ability of parties to implement tobacco control measures. Ongoing negotiations for a Trans-Pacific Partnership Agreement (in which the Philippines is not currently participating) highlight four important issues for consideration. First, FTAs often include chapters on investment protection, which provide foreign investors, including tobacco companies, with additional legal rights. The Philippines already has many similar agreements in place, such that new commitments are unlikely to increase the country's legal risk. Second, FTAs often include strong obligations with respect to the protection of intellectual property rights. If such obligations provide tobacco companies with a right to use trademarks, they may be problematic for tobacco packaging and labeling measures such as plain packaging. Third, FTAs may include provisions governing regulatory processes that provide the tobacco industry with a forum to challenge tobacco control measures, such as with respect to cost-benefit analysis. Finally, tobacco-specific language in trade agreements may either protect tobacco control measures or endanger them depending on the language used. In summary, policy-makers should evaluate these legal risks in all future FTA negotiations.

Investment

Governments use investment and fiscal incentives, such as tax holidays, to attract foreign investment. In the tobacco context these incentives generate savings that lower the cost of production. The law of supply and demand suggests that tobacco consumption is likely to increase if these savings are passed on to the consumer in the form of lower prices. For this reason, Guidelines to Article 5.3 of the WHO Framework Convention on Tobacco Control (FCTC) recommend that parties should not grant incentives to tobacco companies.

The Philippines has witnessed significant foreign direct investment (FDI) in its tobacco sector, particularly in the form of large investments from Philip Morris. Although Philip Morris established its operations in an industrial zone, Philippine authorities have stated that Philip Morris neither sought nor was granted incentives to enter the Philippine market. This suggests that the decision to do so was based primarily on capturing market share in an emerging market.

Also, British American Tobacco has pledged to increase its investment in the Philippines. In this context, policy-makers and health advocates should be vigilant in ensuring that incentives are not granted to the firm.

Debate continues about the effects of FDI on governments' decisions to regulate. Some observers believe that FDI typically leads to "capture" as governments dismantle regulatory frameworks to attract and maintain investments. Others argue that governments privilege domestic investment either because they believe it is in the public interest or because of entrenched political connections. We use the 2012 tobacco excise tax reform to examine these propositions. In brief, we find that the reality is very complex. Despite substantial investments (hundreds of millions of dollars) over more than a decade, Philip Morris International (PMI) consistently failed to influence tobacco tax policies successfully, even as part of a recent joint venture with the largest domestic tobacco manufacturer. Other variables – including the tobacco tax's link to alcohol tax reform, shifting norms of governance, and specific characteristics of key institutional structures – had serious intervening effects. This does not suggest that foreign investors are not influential – the new PMI-Fortune venture continues to wield enormous resources in order to affect policy, sometimes successfully – but it does suggest that other variables can mitigate or even negate some of these relationships.

The Philippine government is one of the first to mandate an interagency arrangement for the implementation of tobacco control regulations.

IMAGE PROVIDED BY JIMMY DOMINGO

Interagency Coordination and Cooperation

Our work also examined the complex relationships between various actors through the country's mandated Interagency Committee for Tobacco (IAC-T), the Philippine focal point for tobacco control. Interagency arrangements have been touted as a solution for health policy issues that cut across sectors such as tobacco control. The principal rationale for interagency arrangements is to achieve policy coherence within government while facilitating the inclusion of health objectives across sectors. Despite the potential benefits of interagency arrangements, challenges abound, including loss of autonomy for some agencies, stalemate or fragmentation, and resource inefficiencies. It is crucial to understand how such arrangements work in practice in order to preserve the benefits while protecting against the challenges mentioned. The Philippine government is one of the first to mandate an interagency arrangement for the implementation of tobacco control regulations. The IAC-T is the primary agency for the implementation, enforcement, and monitoring of the Tobacco Regulation Act (RA 9211). The agency's mandated structure has generated deep concern among tobacco control proponents. One key objection is to the fact that the Department of Health (DOH) does not lead the IAC-T but is relegated to vice-chair; instead, the Department of Trade and Industry (DTI) chairs the agency. Challenges also stem from the formal inclusion of an industry representative in the IAC-T. Design of the IAC-T also constrains the DOH's legal authority to enforce the RA 9211. In a case brought against the DOH by Philip Morris Manufacturing Incorporated, a court ruled that the IAC-T is the sole body charged with implementing the Act. Tobacco control efforts have suffered, too, because civil society organizations challenging industry representation on the IAC-T have often refused to participate in IAC-T meetings. The composition and authority of the IAC-T provide important evidence that institutional design can result in stalemate, fragmentation, and other process-oriented challenges.

Lessons from the 2012 Tobacco Tax Reform

Last, we examine closely the 2012 "sin tax" reform that changed the structure and rates of government taxes on tobacco and alcohol products. We focus particularly on elements of the reform that provide general lessons for other countries seeking similar measures. First, the government's decision to link the new tax revenues to the emerging universal health program, PhilHealth, was consistently identified by officials and the general public as the main reason to support the reform. Second, the coalition of civil society organizations supporting reform was meaningfully broad, consistently vocalized the same set of compelling messages, and developed strong relationships across government institutions by providing effective technical assistance. On this same note, many observers cited the general importance of technical assistance from both within the country (civil society and government) and externally, including intergovernmental organizations (IGOs) and international non-governmental organizations. Many observers also noted the link between the reform and a

related dispute at the WTO about taxes on distilled spirits. To many – and contrary to much of the conventional wisdom – the sin tax reform would not have happened but for the impetus from a case about taxes on distilled spirits that the Philippines "lost" at the WTO. Finally, a recent WTO dispute between the Philippines and Thailand over cigarette taxes and some major challenges with possible tax evasion after the implementation of the recent Philippine sin tax suggest that, in order to administer ad valorem taxation effectively, governments need to have a strong command of product valuation both domestically and in traded products.

Introduction

In order to develop both public health policies that promote healthier societies and economic policies that engender prosperity, policymakers and proponents of policy reform require a deep understanding of how these two major policy areas intersect and interact. In this report, we examine the nexus of one major public health policy area – tobacco control – and three major economic policy areas – trade, investment, and taxation. Some economic policies can certainly conflict with tobacco control objectives – e.g., tobacco multinational corporations (MNCs) have used trade and investment laws to establish a commercial presence in lower- and middle-income countries (LMICs). In other circumstances economic policies can undermine tobacco control policies directly. Despite this obvious potential for conflict, a more thorough examination of this policy intersection reveals that some threats are misunderstood and that opportunities to promote health exist within the economic policy reform process. Despite the importance of this policy nexus, there is a paucity of rigorous research in this area. Accordingly, this report aims to address this major gap using a country case study, the Philippines, that effectively highlights many of the most pressing issues.

The Philippines offers an ideal case because it permits the examination of the reciprocal effects of trade, investment and taxation policies, and tobacco control efforts using recent concrete examples. In the trade area, the Philippines has greatly liberalized (i.e., removed barriers) its trade regime in the past few decades. Moreover, it has been actively involved in major international trade disputes particularly at the World Trade Organization (WTO), both as complainant and respondent. Additionally, tobacco MNCs have been extremely active in the Philippines. In particular, Philip Morris International's (PMI) investments in the Philippines offer an opportunity to examine how foreign capital inflows might influence key domestic regulatory debates about tobacco. The 2009 joint venture between Philip Morris' Philippines subsidiary and Fortune Tobacco, the historically dominant local firm, further complicates the political economy of PMI's investment. Finally, in late 2012, the Philippines implemented one of the most dramatic tobacco excise tax reforms ever in an LMIC. The political and economic debates around this policy reform illustrate many key features of the broader discussion of the economic-health policy nexus.

Our analysis was conducted using complementary methods and drew from a wide variety of data sources. First, we utilized process-tracing analysis of existing economic policies that affect tobacco control in order to understand how they function and also to predict how different policy options might affect health. Second, we carried out key informant interviews with 37 individuals deeply involved in tobacco control and/or economic policymaking across a range of official governmental institutions (including all relevant ministries and agencies, and the congress), civil society, and the tobacco industry. Third, utilizing pertinent legal, government and public media documents, we performed a rigorous legal analysis of commitments to existing and proposed international trade and investment agreements that could affect the ability of the government to implement tobacco control measures.

The structure of the brief is as follows. We begin in Part I with a consideration of major relevant emerging international economic agreements and how they might affect tobacco control in the Philippines, including through tariff reductions, the elimination of non-tariff barriers, and the inclusion of investor protections. In Part II, we focus on issues around investment. The section begins with a discussion of investment and fiscal incentives in the tobacco sector. It follows with an examination of the broader political economy of investment in the tobacco sector, particularly foreign direct investment (FDI), using the recent tobacco excise tax reform as an illustrative tool. In Part III, we focus on interagency cooperation and coordination, both around the national tobacco control bill and implementation of the Framework Convention on Tobacco Control (FCTC), to which the Philippines is a party. Finally, in Part IV, we examine the experiences around the 2012 tobacco excise tax reform more broadly in order to draw some generalizable lessons for countries seeking to improve tobacco excise tax policies.

Part I – Implications of Emerging Free Trade Agreements for Tobacco Control in the Philippines

This section examines the implications of two free trade agreements (FTAs) under negotiation in the Asia-Pacific region – the Regional Comprehensive Economic Partnership (RCEP) and the Trans-Pacific Strategic Economic Partnership Agreement (TPP) – for tobacco control in the Philippines. We examine the extent to which these negotiations pose risks to public health and how any such risks could be addressed. The RCEP negotiations are an attempt to link the Association of Southeast Asian Nations (ASEAN) (of which the Philippines is a member) with ASEAN's existing FTA partners to create a larger FTA. This FTA would include ASEAN countries as well as Australia, China, India, Japan, South Korea, and New Zealand. The TPP is an existing FTA between Brunei Darussalam, Chile, New Zealand, and Singapore. Australia, Canada, Japan, Malaysia, Mexico, Peru, the United States, and Vietnam are in formal negotiations to join and expand the agreement. For various reasons, the Philippines has not entered the TPP negotiations. Nonetheless, the location of the Philippines in the Pacific Ocean means that, in theory, the Philippines might accede to the agreement at a later date. The TPP may also prove to be a model for future FTAs.

Background

The World Trade Organization (WTO) is the central multilateral regime governing international trade. Under WTO law, WTO Members have placed upper limits on tariffs (customs duties) applied to imported products, including tobacco products. Additionally, the WTO-covered agreements subject Members to various rules concerning non-tariff barriers to trade, such as regulatory measures.

WTO Members are also permitted to enter FTAs, which are usually bilateral or regional in character, and require elimination of practically all restrictive regulations of commerce, such as tariffs, between the territories involved (although some agreements go further than others).[1] FTAs often include rules that go beyond those found in WTO law, such as chapters governing investment protection and "TRIPS-plus" obligations, which require higher levels of intellectual property protection than is required under WTO law and investment protection chapters, often permitting foreign investors to bring claims directly against governments.

In essence, FTAs require deeper trade liberalization, such as through complete elimination of tariffs on the vast majority of products on a preferential basis for goods and services originating in partner countries.

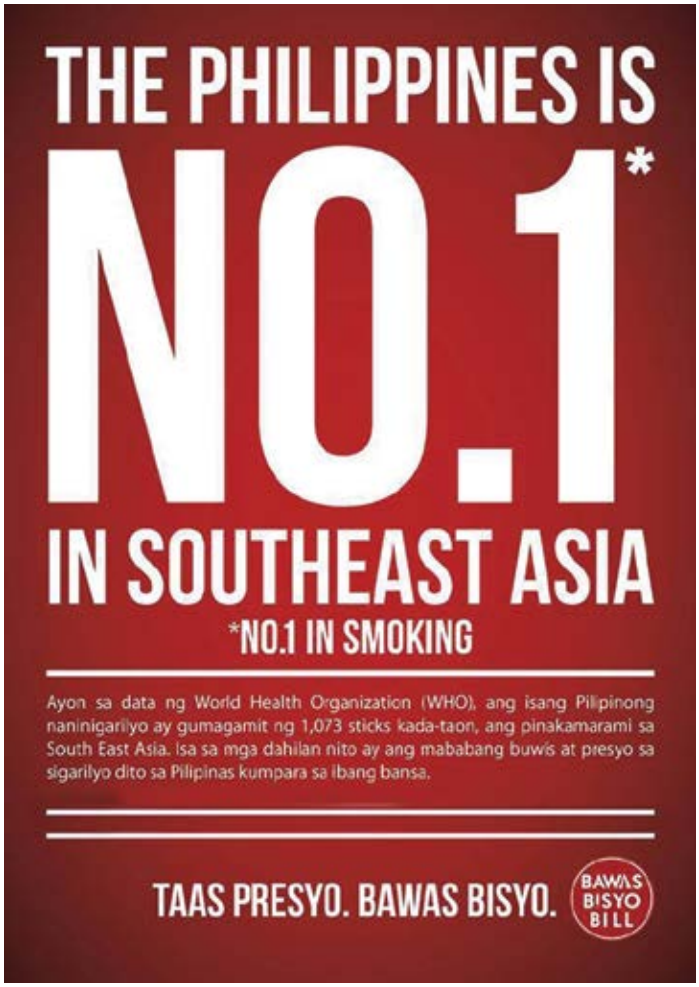
Trade agreements pose two risks for tobacco control. First, lower tariffs may stimulate tobacco consumption by increasing competition among producers, and leading to lower retail prices for imports. The available evidence suggests that the opening of traditionally-closed tobacco markets in LMICs has contributed to increases in prevalence of tobacco use in some of these countries. Reasons for this include lower product prices (when tariff reductions are passed on to consumers), more aggressive marketing by tobacco companies, and the targeting of untapped markets such as women and children.[2]

Second, rules governing non-tariff barriers to trade and investor protection place limits on domestic regulatory autonomy. In other words, domestic tobacco control measures may be subject to legal challenges on the basis of commitments made in FTAs. In this context, there is a risk that expanding those rules could limit regulatory autonomy to a greater degree than is the case under existing agreements.

Tobacco Tariffs and Tobacco Production in the Philippines

In order to examine the risk that new commitments with respect to tariffs might have on demand for tobacco products in the Philippines, it is necessary to examine the existing commitments (bound tariff rates), applied tariff rates, and the composition of the tobacco market. The analysis set out below suggests that there is presently only limited risk to public health associated with the Philippines lowering tobacco tariffs as a part of FTA negotiations. This risk is limited because the Philippines already applies low tariffs to raw tobacco and tobacco products and already provides preferential tariff-free access to raw tobacco and tobacco products from a number of countries, and because a significant proportion of tobacco products consumed in the Philippines are produced at low prices domestically rather than imported. Additionally, the countries with which the Philippines has preferential arrangements are also countries in which tobacco products are produced and sold at low prices.

1. See GATT Article XXIV:8(b) for a more detailed definition.
2. For a summary of the literature see Benn McGrady, Confronting the Tobacco Epidemic in a New Era of Trade and Investment Liberalization, World Health Organization, (2012)



AER / BAWAL BISYO BILL CAMPAIGN

Under its WTO commitments the Philippines has considerable flexibility with respect to tariffs on raw tobacco and tobacco products. On many product lines the Philippines is permitted to charge tariffs in the vicinity of 45 – 50 percent of the value of an imported product. As a matter of practice, however, the Philippines applies much lower rates of 3, 7, and 10 percent (depending on the product line).[3] These rates are applied on a most-favored nation (MFN) basis (to goods from WTO Members, including those without a preferential agreement such as an FTA).

The fact that applied rates are low is important in two respects. First, the lower an applied rate is, the less impact lowering rates further is likely to have on competition between imported and domestic products. Put another way, the Philippine market is already open to competition from imported products, and tariffs play a very minor role in protecting domestic production. Second, the fact that the applied rates are so low suggests that lowering those rates further, such as to zero, is not likely to have a significant impact on the retail price of imported tobacco products.

The Philippines is also party to various FTAs. As an ASEAN Member, the Philippines is a party to the ASEAN Trade in Goods Agreement. As mentioned above, this ASEAN grouping has negotiated FTAs with a number of other countries. The Philippines also has a bilateral FTA with Japan. Under these agreements, the Philippines offers tariff-free entry to raw tobacco and tobacco products from ASEAN Members (except Vietnam), and from other countries with which ASEAN has FTAs.

The preferential access afforded to the Philippine market means that low-priced raw tobacco and tobacco products from many of the countries involved in the TPP and RCEP negotiations already have tariff-free access to the Philippine market. Although some countries involved in the negotiations do not currently have tariff-free access, the landscape of the Philippine market suggests that lowering tariffs for those countries is unlikely to have a significant effect on demand for tobacco products.

As of 2011, less than 1 percent of cigarettes consumed in the Philippines were imported, meaning that the vast majority of cigarettes consumed in the Philippines were not subject to tariffs. From 2010 to the end of 2012, the new Philip Morris-Fortune Tobacco Corporation (PMFTC) had approximately 90 percent share of the Philippine cigarette market. Mighty Corporation had approximately 3.5 percent of the market, and Japan Tobacco International (Philippines) had approximately 3.4 percent. Both PMFTC and Mighty Corporation manufacture tobacco products in the Philippines for sale to the domestic market. These companies source their raw tobacco primarily from within the Philippines, as is illustrated by the fact that in 2011 imported leaf made up less than 1 percent of tobacco leaf used in the Philippines.[4] British American Tobacco (BAT) has also announced that it intends to make a direct investment in manufacturing in the Philippines (discussed below). BAT also sources tobacco leaf in the Philippines.

Accordingly, based on 2011 figures, tariffs in the range of 3 – 10 percent ad valorem are applied to less than 1 percent of cigarettes sold in the Philippines. Based on these figures, it appears unlikely that any new commitments to lower tariffs would have a significant effect on demand for imported cigarettes. Similarly, the fact that less than 1 percent of tobacco leaf used for production in the Philippines is imported suggests that new commitments with respect

3. Information on applied tariffs is available at http://www.tariffcommission.gov.ph/tariff_finder/
4. Tobacco in the Philippines, January 2013, Euromonitor International; See also Philippine Trade Statistics available at http://dti.gov.ph/uploads/DownloadableForms/Phl%20Imports%20from%20the%20World%20FY%202012.pdf

to tariffs on leaf are unlikely to have a significant effect on production costs.

Legal Risks: Non-tariff Barriers and Investor Protection

As noted above, FTAs extend international rules that limit the regulatory autonomy of countries. In this respect, the TPP and RCEP could extend Philippine commitments on investor protection, intellectual property protection, regulatory coherence, and tobacco more specifically. The confidential nature of the negotiations means that it is not possible to examine these issues in detail. Rather, this section highlights the issues, and points to approaches that preserve sufficient regulatory space for sound tobacco control measures.

Investor Protection

States protect the assets of their nationals when invested abroad by agreeing to bilateral investment treaties (BITs) with other States. For example, a BIT between Australia and Hong Kong protects the assets of Australian investors in Hong Kong and Hong Kong investors in Australia. In light of this BIT, Philip Morris (Asia) is bringing a claim against Australia concerning plain packaging of tobacco products based upon the effect that the measure has on its Australian investment (Philip Morris Limited). These types of claims are settled through international arbitration and governed by the terms of the BIT rather than by domestic law. It is common for FTAs to include investment chapters that have similar terms and effects to BITs. Accordingly, an FTA might expand the protections available to foreign investors, such as by extending that protection to nationals of countries with which the Philippines does not have an existing agreement.

At present, the Philippines is a party to approximately 35 BITs.[5] ASEAN FTAs, to which the Philippines is a party, also contain investment chapters modeled on BITs, and the Japan-Philippines FTA contains an investment chapter. Of the countries within the RCEP and TPP negotiations, the Philippines does not have investment agreements with Mexico, Peru, or the United States. Accordingly, in the event that the Philippines accedes to the TPP at some future point, agreeing to an investment chapter in that agreement would extend legal commitments to investors from those countries. It is also conceivable that commitments made in any TPP investment chapter could provide a higher level of investor protection than is provided in existing Philippine agreements.

In this respect, some models in recent treaties clarify the regulatory autonomy of parties to a greater degree than most BITs, and in so doing, provide better protection for tobacco control. The annexes on expropriation and fair and equitable treatment attached to the ASEAN-Australia-New Zealand investment chapter provide a good model for the Philippines to use in protecting policy space for tobacco control.

Equally, it is important not to overstate the risks associated with the Philippines entering new investment agreements. The country already has agreements with Switzerland, where Philip Morris and Japan Tobacco International have corporate headquarters, and the United Kingdom, where British American Tobacco is headquartered. Accordingly, these companies could already bring claims under existing agreements.

Intellectual Property Protection

The Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) is a WTO-covered agreement requiring WTO Members to ensure minimum standards of protection for intellectual property rights. Many FTAs include commitments to protect intellectual property that go above and beyond the minimum standards required by TRIPS. This is relevant to tobacco control because packaging and labeling measures often restrict use of trademarks either directly or indirectly. In fact, claims against the implementation of plain packaging by Australia are based partly on commitments with respect to trademarks under TRIPS.

In the context of the TPP, early leaked US proposals suggest that the agreement could create a positive right to use names that indicate a location, such as Marlboro, as well as colors and figurative elements.[6] Such a clause could limit the ability of parties to implement plain packaging by extending the obligations established under TRIPS. A more recent leak suggests that the right would extend to words, signs, and indications, which may pose a problem for plain packaging.[7]

Regulatory Coherence

In the context of the TPP, the US has proposed to include a chapter on regulatory coherence. The only obligation subject to dispute settlement under this proposal would be an obligation to establish central coordination of new regulatory measures. It is also envisaged in the proposal that TPP countries would conduct regulatory impact assessments and that the TPP would create an international committee open

5. http://unctad.org/Sections/dite_pcbb/docs/bits_philippines.pdf
6. Robert Stumberg, Safeguards for Tobacco Control: Options for the TPPA, 39 Am. J. L. and Med. (2013) 382
7. Secret TPP treaty: Advanced Intellectual Property chapter for all 12 nations with negotiating positions, WikiLeaks release: November 13, 2013, Article QQ.D.14, p. 27; See also http://www.oneillinstitutetradeblog.org/plain-packaging-tobacco-trademarks-geographical-indications-tpp/?utm_source=feedburner&utm_medium=feed&utm_campaign=Feed%3A+oneill-tih+%28Trade%2C+Investment+and+Health%29.

to industry submissions.[8] Although the legal obligations would be minimal, history suggests that tobacco companies would use this chapter to strengthen its position in domestic regulatory debates.

Tobacco-specific Language

In the context of the TPP, the United States has proposed tobacco-specific language to recognize that tobacco consumption poses a risk to health.[9] Malaysia has proposed that tobacco products be excluded completely from the scope of the agreement.[10] Given that Malaysia is also an ASEAN member, it is reasonable to expect that the same proposal will be made in the context of the RCEP negotiations. The Malaysian proposal would exempt tobacco from commitments to lower tariffs (although it would not prevent a country from lowering tariffs unilaterally) and would also eliminate the risk that rules in the TPP could be used to challenge tobacco control measures. The effect of the US proposal is unclear, although it appears to be negligible. The risk associated with each proposal is that it suggests that existing rules, such as those set out in WTO law, do not provide sufficient policy space for tobacco control measures. In future negotiations, this risk should be weighed against the risks to be addressed through tobacco-specific language.

Part I – Implications of New Economic Agreements – Key Findings/Recommendations

In the negotiation of free trade agreements (FTAs), the public health community should evaluate the following:

- Whether lowering tariffs (customs duties) on tobacco or tobacco products is likely to stimulate demand for tobacco products.
- Whether additional rules governing non-tariff barriers to trade will constrain domestic regulatory autonomy in ways that affect tobacco control. These rules include:
  - o Investment commitments that protect foreign investments and give foreign investors new legal rights.
  - o Commitments to protect trademark rights above and beyond those set out in the law of the World Trade Organization ('TRIPS Plus').
  - o Rules governing regulatory decision-making that may provide the tobacco industry with a platform to resist regulation.
  - o Tobacco-specific language, which could carve tobacco out of new commitments, but also affect interpretation of existing commitments.

In the Philippines, it is unlikely that lowering tariffs will stimulate demand, or that new investment chapters in FTAs will extend the rights of tobacco companies much beyond existing rights, but the effect of other rules must be judged at the time an agreement is negotiated.

8. Leaked negotiating texts are available at http://infojustice.org/tpp
9. Details of the proposal are available at http://www.ustr.gov/about-us/press-office/fact-sheets/2013/august/fact-sheet-tobacco-and-tpp
10. See http://www.thesundaily.my/news/826990

Part II – Investment

Investment and Fiscal Incentives in the Philippine Tobacco Sector

Governments use a variety of incentives to attract investment, including tax holidays, subsidies of various types, and privileges associated with manufacturing in free zones where tax and customs laws do not apply. Governments compete with one another for investment and use these incentives to lure investors from other locations or to stimulate investment that may not otherwise occur. Investors seek incentives with a view to lowering their costs of production.

In the tobacco context, lower costs of production may be passed on to the consumer in the form of lower retail prices. The established relationship between the retail price of tobacco products and demand suggests that lower prices may increase the prevalence of tobacco use and total consumption. In turn, this is likely to increase the morbidity and mortality associated with tobacco use. With this in mind, Guidelines to Article 5.3 of the FCTC state that "[b]ecause their products are lethal, the tobacco industry should not be granted incentives to establish or run their businesses."[11]

Granting incentives to the tobacco industry can also create legal risks when it comes to tobacco regulation. For example, commitments made in the context of investment contracts between a government and an investor can constrain a government's regulatory power. The partial sale of a national tobacco monopoly by Laotian authorities offers a prominent example. The investment contract in question provided the investor with a five-year profit tax holiday and fixed the excise tax rate for a 25-year period (2002 – 2026).[12] Under the contract, the investor is entitled to compensation in the event that excise taxes are increased.

Offering investment incentives may also have legal implications under investment treaties. For example, in a dispute between Philip Morris and Uruguay, the arbitral tribunal hearing the claim relied on investment incentives offered by Uruguay to Philip Morris in finding that the tribunal had jurisdiction to hear the claim.[13] Similarly, "umbrella clauses" in investment treaties require governments to respect commitments made to investors. The requirement that a state hosting investment provide fair and equitable treatment to an investor may also be relevant where a state has induced investment by offering an incentive, but has subsequently not honored that inducement.

From a public health perspective, the fact that governments often keep incentives confidential poses a significant challenge in the context of researching investment incentives. Incentives offered for investment are usually viewed as "commercial in confidence" partly because governments compete with one another for investment and do not wish to signal their best offer to other governments, and partly because governments do not want existing investors to feel aggrieved if a better offer is subsequently made to new investors.

In recent years, the Philippines has seen significant FDI in its tobacco sector. Philip Morris made an initial $300 million investment in 2000 in the construction of a factory in Tanauan City in Batangas. Subsequently, Philip Morris entered a joint venture agreement with Fortune Tobacco Corporation, a privately-owned Philippine company. British American Tobacco also pledged a $200 million investment in the Philippines conditional on the reform of tobacco taxes and the tax system. This investment is in the form of expanding the BAT supply chain and purchases of tobacco leaf from within the country. In addition, BAT has indicated that it intends to make an investment in manufacturing in the Philippines.[14]

In addition to both desk and field research (interviews of government officials and others), we made formal requests for information to identify whether investment incentives have been offered to tobacco companies. Our research indicates that investment incentives are offered in the Philippines through the Board of Investments (BOI) and the Philippine Economic Zone Authority (PEZA), which is tasked with managing economic zones.

IMAGE PROVIDED BY JERIK CRUZ

11. Principle 4, page 3
12. Isra Sarntisart, Tax Policies for Tobacco Industry in Lao PDR, Southeast Asia Tobacco Control Alliance, July 2008
13. Philip Morris Brands Sarl, Philip Morris Products S.A. and Abal Hermanos S.A. v. Oriental Republic of Uruguay (ICSID Case No.ARB/10/7) Decision on Jurisdiction, para. 165
14. See http://www.rappler.com/business/industries/30696-cigarette-maker-bat-beefs-up-manufacturing-plans-in-ph

Philip Morris has located its manufacturing facilities in the First Philippine Industrial Park, which is an economic zone administered by PEZA. Under Republic Act No. 7916 (the Special Economic Zone Act of 1995), registered Export or Enterprises operating in ECOZONES or Special Economic Zones enjoy incentives, including these:

- Income tax holiday (ITH) for 4 years to a maximum of 8 years
- After the lapse of ITH, exemption from national and local taxes; in lieu thereof, special 5% tax rate on Gross Income
- Exemption from duties and taxes on imported capital equipment, spare parts, materials and supplies.[15]

PEZA has indicated that although Philip Morris is located within an economic zone, the company is not registered with PEZA and does not receive incentives under the law in question. Similarly, the BOI has indicated that Philip Morris is not registered with the BOI, meaning that the BOI has not provided incentives to the company. Because incentives are often conditional upon exporting a designated percentage of production, the fact that Philip Morris did not seek incentives suggests that the company located in the Philippines largely to capture a share of an emerging domestic market rather than to use the country as a hub for export to the region.

Policy-makers need to be aware of the risks associated with future FDI. At present, BAT has a relatively small share of the Philippine cigarette market, with an approximately 1 percent market share. Nonetheless, BAT was active in legislative debates concerning reform of tobacco tax laws. BAT argued that the tax structure in place prior to reform favored products produced by PMFTC to the disadvantage of BAT products. Taxes were calculated on an ad valorem basis, but brands in the market prior to 1996 had a fixed value for purposes of the calculation. Fortune Tobacco Corporation dominated the lowest price segments of the market, which were the preponderance of cigarettes sold.

In legislative debates around tax reform, BAT held out the prospect of direct investment if reform were to create a level playing field on which the company could compete in the Philippine market. More specifically, BAT indicated that it was willing to invest $200 million over a five-year period, including the possibility of building a manufacturing facility.[16] BAT has also invested in the purchase of tobacco leaf from tobacco-growing areas in the Philippines, possibly to assuage political concerns about the impact of tax reform on tobacco growers.[17] As policy-makers in the Philippines review policies on fiscal incentives more broadly and address the prospect of BAT increasing its investment in the country, the risks associated with offering investment incentives need to be taken into account. In this respect, policy-makers should avoid offering incentives that may lower the costs of production or tie the hands of the government with respect to future tobacco regulation.

The Political Economy of Foreign Direct Investment

Beyond the more technical aspects of investment in the tobacco sector, there is considerable debate about the effects of FDI on tobacco control. Recent events at the intersection of economic and health policymaking in the Philippines can illuminate how FDI might affect countries' efforts to promote public health and regulate the tobacco industry. In this sub-section, we utilize the Philippines' experience with its 2012 tobacco excise tax reform to examine the effects of FDI on the politics of making tobacco-related policy.

The political economic dynamics around and within the Philippines' recent sin tax reform suggest that the relationship between FDI by a tobacco MNC in a large developing country and public health policy is complex. Under certain conditions, FDI might not even be directly detrimental to health policymaking. While it is not possible to isolate definitively the effects of FDI on health policy and other related outcomes, we can evaluate two common narratives in this important case. Some believe that FDI typically leads to "capture" as governments dismantle regulatory frameworks to attract and maintain investments. If this is the case, we would expect to observe large foreign investors successfully influencing policies that privilege their needs over public health policy. Others argue that governments privilege domestic investment either because they believe it is in the public interest or because of entrenched political connections. If this is the case, we would expect powerful domestic economic interests to enjoy more favorable policy conditions.

The recent Philippines sin tax reform scenario permits some insight into these narratives. For much of the late 20th and early 21st century, a large domestic tobacco firm, Fortune Tobacco Corporation, dominated the Philippines manufactured tobacco products (mainly cigarette) sector. In the mid-1990s, it lobbied successfully for a tiered tax structure that not only preserved long-term favorable taxation for most of its products, but also created prohibitive barriers

15. http://www.fpip.com/investor-guide.asp#government
16. http://www.philstar.com/business/2012/12/13/885329/british-american-tobacco-invest-200-million-phl.
17. http://ph.news.yahoo.com/bat-raises-tobacco-buy-commitment-191519545.html.

to other firms seeking to enter the market or improve market share. Considering the size, youth, and economic growth of the market, several tobacco MNCs, including PMI and JTI, fought against these efforts in order to gain a better foothold in the market.

In part of its effort to increase its small market share, PMI lobbied against the tax structure in the 1990s and 2000s, arguing that the tax structure was tilted heavily in favor of incumbent firms. Perhaps because it was gaining limited traction with these arguments, PMI chose another strategy, investing heavily in the Philippines' tobacco manufacturing sector with two major investments, $300 million in 2000 and another $20 million in 2007. Still facing unfavorable market conditions, it sought a joint venture with Fortune Tobacco Corporation, creating a new entity in 2010, Philip Morris Fortune Tobacco Corporation (PMFTC), which has dominated the marketplace (80-90% market share until early 2013, prior to the eventual tax reform).

When tobacco taxation reemerged on the legislative agenda in 2012, the new PMFTC abandoned the previous PMI position of pushing tax reform for a position that preserved the status quo. In effect, as the new "incumbent" firm, the existing conditions suited it better. Not surprisingly, however, as discussed above, BAT actively sought reform in much the same way that PMI had previously. For a variety of reasons, including political will for change, the government reformed the tax structure and dramatically increased rates in 2012. PMFTC was arguably the biggest loser in the reform. So the question remains, why was PMFTC unable to preserve a policy environment that favored its interests? And more importantly, what can we learn about the effects of FDI on legislative and regulatory efforts?

Because the broader sin tax reform included both tobacco and alcohol, it is clear that the complexity of reforming tax structures and rates for both industries within the same legislative package ultimately worked against the tobacco industry. In brief, the alcohol industry, which is primarily domestically-owned, lobbied vigorously to make certain the reform was not too damaging to it. In effect, the alcohol industry lobbied against the tobacco industry. In a complex twist of fate, the former owner of Fortune Tobacco Corporation and now partial owner of PMFTC, Lucio Tan, also owns the second largest brewery and the largest rum manufacturer. Political insiders present conflicting accounts about what role these complexities played. Some suggest that Tan's long-held, out-sized influence has waned from the era when he successfully promoted and preserved the old tobacco tax regime. Others have suggested that, given the choice, he sacrificed the tobacco industry from which he has been aggressively divesting for a better deal for his lucrative alcohol-related ventures.

The tobacco-alcohol dynamic also affected key deliberations and voting in the Ways and Means Committee in the House of Representatives. According to committee members and their staffs, the discussion around the tax reform was vigorous. Ultimately, a core group of supporters for a

AER / BAWAL BISYO BILL CAMPAIGN
The health impact of cigarette smoking was a key focus of the 2012 sin tax advocacy campaign, in which tax reform advocates joined forces with public health activists.

legislative sin tax proposal that placed a greater burden on tobacco emerged. Ten members of this group were from the Nationalist People's Coalition whose founder and chair, Eduardo Cojuangco, Jr., is also the chairman of the country's largest brewer, San Miguel Corporation.

It is possible that PMFTC also miscalculated in its own determination of the political economy of FDI. Several senior government officials involved in early negotiations around the legislation reported that PMFTC chose not to attend meetings with key officials, perhaps believing that it enjoyed levels of influence similar to Fortune Tobacco Corporation's in years past. The alcohol industry, however, actively sought to participate in the discussions with the Department of Finance (DOF) and other major institutions. Most of the tobacco industry, led by PMFTC, instead prepared a legislative proposal favorable to its preferences. Though the then-Senate Finance Committee chair, Ralph Recto, championed a similar proposal, it gained little support among other elected officials or the general public. In fact, as a result of the proposal, Recto was pressured publicly to resign his chair's post shortly thereafter. This turn of events also might reflect what many of our key informants suggested was a fortuitous change towards enhanced government accountability and transparency in relations with private economic interests.

The obvious counterpoint more generally is that the alcohol-tobacco connection could have worked the opposite way: the two industries might have coordinated and/or cooperated in order to influence the legislation for mutual benefit. But in this case, the government strategized clearly that it wanted to reach a certain revenue threshold (the final amount was negotiated) and that it would decide how the burden would fall. This dynamic by design pitted the two industries against each other as they sought to minimize their industry's burden.

It is very difficult to disentangle what role corruption might have played in the reform. On one hand, several key informants both in government and civil society suggested that domestic tobacco industry players continue to play by the "old" rules and had bribed legislative committee members before hearings and votes. There is no direct evidence of these activities, but former and present domestic tobacco firms have a longstanding and consistent reputation of employing similar illegal tactics. On the other hand, some observers speculated that PMFTC was holding itself to new codes of behavior, possibly because of the foreign joint venture partner's (PMI) concern about adhering to the US Foreign Corrupt Practices Act. This possible dynamic casts FDI in a very different light because it suggests the possibility that industries that might have previously played outside the legal rules suddenly pay closer attention to the norms of legal behavior in the interest of global business operations. In the case of corruption, this possibility can only serve to protect government decision-making from pernicious and powerful external actors. Perhaps particularly relevant to this discussion, even if there were such illegal activities and the effects are unknown, we do know that these activities were not sufficient to turn the vote against reform.

The role of BAT in the sin tax reform is predictable: it actively sought the policy that would best serve its interest in gaining a larger foothold in the Philippine tobacco market. Quite simply, a reformed tax structure would take away the incumbent firms' – especially PMFTC – advantages. While it might seem counterintuitive to observe a major tobacco MNC lobbying for a tax structure and rates that would likely have negative long-term effects on consumption (and therefore industry-level sales), the dynamic illustrates how much more money is at stake at the firm level for BAT to be able to compete on a more level playing field in the local market. It is not clear that the BAT's promise of a $200 million investment in the Philippines either played a significant role or that it will come to fruition.

It might seem counter-intuitive that competition in the tobacco industry might generate positive outcomes for public health, but this case demonstrates that increased competition coupled with effective taxation may work in favor of public health under some conditions. If the tobacco taxation structure and rates ensure higher prices, it is possible to mitigate a common effect of increased competition, lower prices. As tobacco sectors open up in some countries, it is important to consider the role that tobacco excise taxation can play in ensuring that the new competition does not affect health outcomes negatively. It is also important to consider how the competing interests of different tobacco firms might serve to nullify their collective impact on health legislation, or even the possibility that this competition can be carefully leveraged in favor of sound legislative and regulatory proposals that promote improved public health. However, it is also important to consider how firms' behaviors change as they establish market presence. While tobacco firms might be open to promoting policies more favorable to health when seeking better market access, once established, the Philippine experience suggests that these firms are likely to return to a strong anti-health stance.

In sum, the tax reform dynamic illustrates a number of key points. Investment by foreign MNCs does not necessarily automatically lead to the worst-case scenario for tobacco control or public health. In fact, in this scenario, even after hundreds of millions of dollars of investment, PMI not only did not get what it sought in terms of key excise tax policy, it experienced a serious policy defeat. It is possible that the government's desire for increased tax revenue was a larger contributing factor in its preference for tax reform than its health goals, but this dynamic will only be tested when the government seeks new health policy reforms that do not have immediate fiscal rewards. The overall political economic impact of the PMI investments, however, is complex and difficult to gauge. While the firm did not achieve its tax-related goals, it continues to challenge other regulatory efforts vigorously, for example, by seeking to use the judiciary to block the DOH's and other governmental entities' efforts to develop smoke-free policies. While it is not clear that this dynamic stems from FDI specifically, it is evident that PMI can leverage its vast global resources to mount concerted challenges to tobacco-related regulatory measures at national and local levels, which is an option not as viable for smaller firms. As we observe in the sin tax scenario, many variables can act as counter-weight to the demands and preferences of strong private economic interest, foreign or domestic. Governments and public health proponents must develop better tools to evaluate the possible threats and opportunities as societies balance the need for capital and the ability to regulate effectively.

Part II – Investment and Tobacco Control – Key Findings/ Recommendations

The Philippine government has used a variety of fiscal incentives, such as tax holidays, to attract foreign investment. Although our research suggests that the major foreign investor in the Philippine tobacco sector, Philip Morris, has not received incentives, the Philippine government should ensure the following:

- Following FCTC Article 5.3, the government must prohibit fiscal and investment incentives to tobacco companies, including to British American Tobacco.

More generally, tobacco control proponents in and out of government should do the following:

- Be aware of the potential challenges associated with new foreign investments in the tobacco sector, but not assume that the status quo is necessarily superior.
- Engender good governance around tobacco by supporting elected and unelected officials who promote pro-public health policies.
- Consider both the risks and rewards of linking tobacco excise tax reform to alcohol tax reform.

Part III – Interagency Relations

While Article 5.2(a) of the FCTC compels parties to "establish or reinforce and finance a national coordinating mechanism or focal points for tobacco control," there has been little investigation into how countries have pursued this obligation and which types of institutional designs and arrangements offer particular utility. The directive in Article 5.2 converges with broad calls for interagency coordination to enhance health policy initiatives.[18] The main rationale provided in the health literature in favor of interagency institutional designs is that many health problems require crosscutting solutions. Other proposed benefits of interagency designs include cost sharing (i.e., pooling of resources)[19], enhanced policy coherence[20], and accountability[21] across sectors. There is also a vast literature that highlights the challenges of interagency designs including conflicting objectives that can lead to stalemate or fragmentation[22], resource inefficiencies, and loss of departmental autonomy[23]. These challenges point out that an interagency institutional design (coordination) does not guarantee alignment among the different agencies in the policy process (cooperation). We examine the interagency mechanism that the Philippine government currently utilizes to govern tobacco control.

The Tobacco Regulation Act (RA 9211) is the principal Act governing tobacco in the Philippines. RA 9211 establishes regulation for tobacco packaging, use (smoke-free public spaces), sale, distribution, and advertisement. RA 9211 also mandates the establishment of the Inter-Agency Committee-Tobacco (IAC-T) to implement the provisions of the act. The IAC-T is the focal point for tobacco control in the Philippines, and is therefore responsible for implementing, enforcing, and monitoring RA 9211. It is specified in RA 9211 that the Department of Trade and Industry (DTI) will serve as chair of the IAC-T and the Secretary of the Department of Health (DOH) will serve as vice-chair. Six other departments[24] are represented on the committee along with a "representative from the tobacco industry to be nominated by the legitimate and recognized associations of the industry"[25] and one representative from civil society nominated by the DOH.

The Philippine Congress adopted the Act in 2003, two years before the Philippines ratified the FCTC. Beginning in the drafting stages of RA 9211, conflicting perspectives on its utility arose. For example, prior to its adoption, a draft of RA 9211 was sent to a high-ranking DOH official with experience in tobacco control, including with the FCTC. He noted that his response was to "have it vetoed because congress made the Department of Trade the chair of the overall committee instead of the Department of Health … (which) was a signal to me that this was obviously … geared towards trade, and health was an afterthought." A prominent tobacco control advocate from civil society, however, had urged this official to support the Act, because, as this individual noted, "no matter how imperfect it is, I think we can start with something rather than have nothing at all." The merit of an incremental approach to tobacco control legislation was echoed by all of the tobacco control advocates that we interviewed. Despite this support, tension persists between actors coming from the health community (e.g., tobacco control NGO representatives, representatives from the DOH) and those from other sectors including agriculture, and trade and industry, pertaining to the content of RA 9211 and its implementation.

The first major tension stems from the purported ambiguity between the RA 9211 and the obligations of the Philippines to implement the provisions of the FCTC. The timing of adoption of RA 9211, its relatively weak provisions (e.g., written rather than graphic warning labels on tobacco product packaging, the absence of a total ban on advertising), the situation of DTI as chair of the IAC-T, and the inclusion of tobacco industry representation on the IAC-T, suggests that the tobacco industry interests intended this

18. Calls for inter-ministerial/inter-sectoral/interagency approaches to health policy can be found as early as 1986 with the Ottawa Charter for Health Promotion.
19. Vangen, S. and Huxham, C. (2003): Enacting Leadership for Collaborative Advantage: Dilemmas of Ideology and Pragmatism in the Activities of Partnership Managers. *British Journal of Management*, Vol. 14.; Lundin, M. (2007): When Does Cooperation Improve Public Policy Implementation? *Policy Studies Journal*, Vol.35(4), pp. 629-652.
20. Kavanagh, D. and Richards, D. (2001): Departmentalism and Joined-Up-Government: Back to the future? *Parliamentary Affairs,* Vol.54, pp. 1-18.
21. Wilkins, P. (2002): Accountability and Joined- Up Government. *Australian Journal of Public Administration,* Vol. 61(1), pp. 114-119.
22. Exworthy, M. and Powell, M. (2004): Big Windows and Little Windows: implementation in the 'Congested State'. Public Administration, Vol. 82 (2), pp. 263-281.
23. Vincent, I. (1999): Collaboration and Integrated Services in the NSW Public Sector. Australian Journal of Public Administration, Vol. 58(3), pp. 50-54.; Ranade, W. and Hudson, B. (2003): Conceptual Issues in Inter-Agency Collaboration. *Local Government Studies,* Vol. 29 (3), pp. 32-50; Lasker, R., Weiss, E. and Miller, R. (2001): Partnership Synergy: A Practical Framework for Studying and Strengthening the Collaborative Advantage. *Milbank Quarterly,* Vol. 79(2), pp. 179-205.
24. Secretaries of the Departments of Agriculture (DA); Justice (DOJ); Environment and Natural Resources (DENR); Department of Science and Technology (DOST); Education (DepEd); the Administrator of the National Tobacco Administration (NTA).
25. Republic Act No. 9211, Tobacco Regulation Act (2003). Republic of the Philippines.

IMAGE PROVIDED BY MADELEINE ALORIA

Act to preempt in many ways the inevitable strengthening of tobacco control in accordance with the provisions of the FCTC. One key informant representing an intergovernmental organization based in the Philippines noted that there is still much confusion on the legal authority of the FCTC. Key informants from DTI confirmed the central role of the RA 9211 in Philippine tobacco control, stating that "policy on cigarettes and tobacco comes from the RA 9211," and that it "is the policy and law with respect to tobacco and cigarettes that we follow." This perspective was enshrined in a Court of Appeals decision in a recent case between PMPMI and the DOH.[26] PMPMI petitioned the court to compel the DOH and the Bureau of Food and Drugs (now the Food and Drug Administration) to grant them the ability to carry out promotional activities, which they argued was lawful according to RA 9211. The DOH had summarily denied PMPMI's application for permission to engage in promotional activities and indicated to PMPMI that tobacco companies were no longer permitted to do so according to RA 9211, but more importantly because of the provisions of the FCTC. The Court of Appeals decided in favor of PMPMI's petition:

> The Framework Convention on Tobacco Control (FCTC) is not self-executing and cannot be the direct legal basis for the respondents to justify its mistaken stance that Tobacco Promotions are now fully prohibited … it provides only for a ***gradual elimination*** of tobacco due to health concerns and takes into account the **"legal environment and technical means available"** to the signatory-Country. Until such time when there is already a new law *totally* eliminating all forms of tobacco use and tobacco-related activities, this Court has no other recourse but to act only in accordance with the prevailing *R.A. No. 9211.* (no emphasis added)

The findings from our interviews indicate that the Philippines Tobacco Institute (PTI) and/or its key members also advanced the authority of RA 9211 in the public discourse on the relationship between the Act and the FCTC, suggesting that the Act indeed has served to preempt stricter tobacco control measures from the FCTC. In one case the PTI sought to set aside the implementing rules and regulations (IRR) of the Food and Drug Administration Act of 2009, arguing that they did not apply to tobacco products because the IRR went beyond RA 9211.[27] The PTI lost this case. In another related case involving a (the) major driver behind the PTI, Fortune Tobacco Company sought to overturn a DOH tobacco regulation suggesting that the DOH had gone beyond the authority of RA 9211. The DOH lost this case.[28]

Agencies and organizations with a public health focus raised concerns that the emphasis within the IAC-T has typically been on business aspects of tobacco regulation and that the strongest actors that are consulted most frequently are the Department of Agriculture (DA) and the National Tobacco Administration (NTA). Participants from DTI noted that RA 9211 represents a "balance" between health and stakeholders from the tobacco sector. This notion of "balance" is enshrined in Section 2 of the Act where it states, "At the same time (the purpose of the Act is to) ensure that the interest of tobacco farmers, growers, workers and stakeholders are not adversely compromised." The fact that the DTI chairs the IAC-T in the Philippines is unusual (though not the only such instance in the world). This institutional design creates an overt tension for tobacco control proponents in that industry interests and participation in tobacco governance are embedded in the same legal document that is meant to serve health objectives. It appears that RA 9211 has ensured that industry interests are preserved and given voice. This situation demonstrates the impact of institutional design on both tobacco control initiatives and collaboration among interested parties.

26. CA-G.R. SP NO. 109493, Philip Morris Philippines v. The Department of Health. September 15th, 2011 and September 4th, 2012.
27. Philippine Tobacco Institute (Petitioner) versus Department of Health and Food and Drug Administration, SCA Case No. 11-0013 in National Capital Judicial Region Regional Trial Court, Branch 255, Las Pi as City. July 4, 2011.
28. Fortune Tobacco Company (petitioner) versus Department of Health, SCA Case No. 2010-796-MK, National Capital Judicial Region Regional Trial Court, Branch 272, Marikina City. June 9, 2010.

Despite the overt challenge of the DTI, an economic agency, chairing the governing body (IAC-T) of what many actors conceive of as health legislation, we found that other subtle challenges arise in the different "theories" promoted by various actors about the role of government. The difference in perspectives is a common challenge of "whole-of-government" approaches to health policy, particularly if the objective is policy coherence. For example, it was a common sentiment by all key informants that each department was guided by different rules both internationally and domestically. DTI noted that they are guided by the rules of the WTO and FTAs; and DTI, the DA, and the NTA all indicated that they are responsible to protect the interests of both industry and tobacco growers. Both the DOH and tobacco control NGOs found this responsibility in conflict with their own responsibility to protect Philippine citizens from the harms of tobacco consumption and to implement the provisions of the FCTC. Put another way, health groups do not see how the DTI mandate can be pursued without compromising tobacco control.

The different theories of government are reflected in three perspectives on the prioritization of issues: 1) health should take precedence over economics, 2) economics should take precedence over health, and 3) there should be a balance between health and economic objectives. RA 9211 seems to reject the first theory by legislating the inclusion of industry representation on the IAC-T, providing the chair position to DTI, and overtly acknowledging that the Act is also meant to protect the interests of the tobacco sector. In this situation, some health advocates have chosen to support weak or imperfect tobacco control measures, while often accepting various decisions to ensure that tobacco control measures do not adversely affect the economic interests of the industry and/or the tobacco agricultural sector (such as through side-payments). Other health advocates, however, choose to abandon the interagency arrangement altogether and find other policy spaces to assert their positions within government decision-making.

It appears that an incremental approach may be a realistic starting point for those seeking to establish systemic solutions to the health consequences of tobacco. The DTI points out that the tobacco industry is legal and therefore one of its legitimate constituents. They have a difficult time reconciling their responsibilities as the chair of the committee and being responsive to a major legal industry. They suggest that they understand the spirit of Article 5.3 of the FCTC, which is meant to protect tobacco control policies from tobacco industry interference, but take the view that it directly contradicts their department's official mandate to serve economic constituents. They do not believe that shifting the responsibility of chairing the committee to DOH would resolve the issue, and alone it likely will not, because the tobacco industry is granted a seat on the IAC-T.

The DOH has taken important steps to establish institutional arrangements that protect against tobacco industry interference. For example, the DOH produced a Memorandum in 2010 on tobacco industry interference and means to protect against such interference.[29] This Memorandum provides guidelines for industry interactions and the de-normalization of industry activities in line with the provisions of Article 5.3 of the FCTC. The DOH reflects a degree of openness to IAC-T governance in such statements: "The Department of Health does **NOT** deal with the tobacco industry or individuals or entities that work to further the interests of the tobacco industry, except to the extent strictly necessary to effectively regulate, supervise, or control the tobacco industry and tobacco products." However, many of the tobacco control advocates from civil society noted that they refused to meet with the IAC-T when the industry representative was present. This adversarial dynamic seems to have created an impasse at times when there is no coordination among health and other sectors. A participant from DTI noted that they found it "strange that NGO health advocates have this policy of not sitting at the table with cigarette companies, but because we are a trade department, it is natural for us to consult all stakeholders … One of the stakeholders is the industry." This divergence in perspectives is an ongoing tension and requires creative solutions. Practitioners and scholars need to learn more and better understand the possible tensions – even contradictions – between Articles 5.2 and 5.3. One interim solution to such impasses, and one that was brought up by a number of tobacco control advocates, is to require mechanisms for transparency including the recording of meetings and making the meeting minutes open to the public. Given the tenuous environment of interagency relations it would be necessary to approach this issue not with reproach but with understanding of the constraints imposed on the different economic agencies to consult with all stakeholders.

29. Department of Health, Office of the Secretary: Protection of the Department of Health, including all of its Agencies, Regional Offices, Bureaus or Specialized/Attached Offices/Unites, against Tobacco Industry Interference. May 6, 2010.

IMAGE PROVIDED BY JERIK CRUZ

It is important to point out that the IAC-T produced a Memorandum in 2008 establishing "Pilot Agencies" for the monitoring and enforcement of RA 9211.[30] This Memorandum delegates responsibility and essentially divides the monitoring and enforcement of RA 9211 between DTI and DOH. DTI is responsible for Access Restrictions including issues such as minimum age sales, proof of age verification, and sale of tobacco products within school perimeters. DOH is responsible for the administration of Healthful Environment (e.g., smoking bans in public places) and Advertising and Promotions (e.g., warnings on cigarette packages, restrictions on advertising and promotions). The establishment of Pilot Agency authority would appear to strengthen the autonomy of DOH to monitor and enforce key facets of the Philippines' tobacco control strategy. However, the above-mentioned case between PMPMI and the DOH resulted in a clarification of DOH authority and ultimately a de-authorization of this authority. PMPMI claimed that the *carte blanche* decision not to accept tobacco industry applications for promotional activities was illegal given that the authority to implement RA 9211 was housed with the IAC-T. Whether the DOH decision pertaining to promotional activities of the tobacco industry was lawful is peripheral to this discussion of how this case resulted in a de-authorization of the role of the DOH in implementing RA 9211. The Court of Appeals decided that "importantly, the DOH, by itself, is without any authority to enforce any provision of *R.A. No. 9211,"* and went further to state that "without a doubt, the DOH arrogated to itself the authority given exclusively to the IAC-Tobacco to administer and implement the provisions of the Tobacco Regulation Act allegedly violated by petitioner."[31] The composition of the IAC-T and its authority within RA 9211 demonstrates how challenging interagency arrangements can be. The Philippines case indicates that preemptive legislation enshrining institutional arrangements that ensure the representation of industry interests can serve to weaken the position of those seeking to strengthen tobacco control regulation in accordance with the commitments to the FCTC.

Our findings suggest that the DOH is frustrated with the IAC-T arrangements, and even refuses to attend meetings on suspicion that the industry representative in the committee uses information from the committee to counter the DOH. In 2011, the DOH led the drafting of the National Tobacco Control Strategy (NTCS) and the Tobacco Control Action Plan 2011-2016. The NTCS "reflects the government's political commitment for the complete implementation of the WHO-FCTC," a buffer to the limitations of RA 9211. Under the strategy, the Sector-Wide Anti-Tobacco (SWAT) committee was formed, with 11 subcommittees meant to address the provisions of the FCTC. Here the DTI is a member, and always attends meetings, but there is no industry representative. SWAT is an attempt at inter-agency relations, minus the tobacco industry as envisioned in the FCTC, but while it has fully operating committees with responsibilities, it does not enjoy legal standing. In fact, one of DOH's targets is for an Executive Order (EO) to mandate the SWAT committee. Aiming for an EO is in recognition of the difficulty of legislation: whether to amend RA 9211 or to replace it with a new act. An EO, however, is insecure and holds only until it is revoked by a new executive.

Riding on the FCTC the DOH is asserting itself, but without legal cover, any dispute brought before the courts will still be resolved using existing laws, including RA 9211. In the meantime the DOH is empowered to roll out programs, at least until they are struck down as illegal. In some respects this may involve brinkmanship that is not good for inter-agency linkages or policy neatness, but perhaps the DOH is trying out an activist tactic that has public opinion in mind.

The interagency arrangement that RA 9211 establishes has clearly created challenges for those attempting to strengthen tobacco control in the Philippines. However, the Act itself represented an improvement in tobacco control legislation from the then-status quo and has resulted in advances in

30. IAC-T Memorandum Circular No. 01: Monitoring and enforcement guidelines of the tobacco regulation act and its implementing rules and regulations.
31. CA-G.R. SP NO. 109493, Philip Morris Philippines v. The Department of Health. September 15th, 2011 and September 4th, 2012.

important measures such as public advertising restrictions and bans on smoking in public spaces. The above case of the IAC-T demonstrates the complex political economy of interagency arrangements. Clear lessons can be drawn from this case including the need to situate health objectives and corresponding arrangements, such as primary leadership by health agencies and the exclusion of industry representatives, from such arrangements. These lessons are overt and uncontroversial.

The nuanced lessons require further examination. First, health advocates must be aware of the institutional constraints imposed on economic agencies to represent all stakeholders. Tobacco control advocates must find creative strategies that protect from industry interference while showing awareness of the possibility that some agencies might be compelled to interact with the tobacco industry. These strategies include forum shifting, providing creative interpretations of DTI mandates and, in some instances, side payments to affected parties such as tobacco growers. (In the latter respect, see the discussion below concerning tobacco tax reform in the Philippines.) Second, the RA 9211 serves to preempt stronger tobacco control legislation in accordance with the FCTC and entrenches industry interests in processes to generate and enforce tobacco control policies. The Philippines is a dualist state meaning that ordinarily international law is not automatically incorporated into domestic law.[32] In domestic cases, national law would be applied, which was highlighted in the case between PMPMI and the DOH wherein the court ruled that RA 9211 applied irrespective of the terms of the FCTC. To become domestic law, Congress must enact the FCTC (in contrast to the provisions of the FCTC becoming law automatically following accession). This fact points to the preemptive power of RA 9211 for tobacco control. The Philippine government as a whole has indeed acceded to the FCTC and as a state it must in good faith implement its provisions. Thus, it should make efforts to pass appropriate enabling legislation for the treaty. This case of the RA 9211 and its corresponding interagency arrangement also serve as a lesson to other countries as they seek to implement stronger tobacco control measures in line with the FCTC. Tobacco control proponents must be vigilant to prevent such hand-tying and must strive to actively hold states accountable to move beyond pre-FCTC tobacco control legislation following accession to the treaty.

Part III – Interagency Cooperation – Key Findings/ Recommendations

- Mandated interagency arrangements can further constrain the work of tobacco control proponents depending on composition (e.g., industry presence and economic agency leadership) and scope of role.
- Interagency arrangements to implement the provisions of the Framework Convention of Tobacco Control must categorically exclude industry representation notwithstanding any mandated responsibility of officials to consult with legal commercial entities.
- Proponents of tobacco control should understand the risks and opportunities of incremental legislation. Some perceived legislative victories may create barriers to even stronger legislation in the future.

32. See Magallona, M.M. 2013. "The Supreme Court and International Law Problems and Approaches in Philippine Practice." *Philippine Law Journal* 85(1,2). Available at http://plj.upd.edu.ph/wp-content/uploads/2013/06/PLJ-volume-85-issue-1-2-THE-SUPREME-COURT-AND-INTERNATIONAL-LAW-PROBLEMS-AND-APPROACHES-IN-PHILIPPINE-PRACTICE-Merlin-M.-Magallona.pdf.

Part IV – Lessons from the 2012 Tobacco Excise Tax Reform

In this section, we discuss the 2012 legislation that dramatically reformed tobacco excise tax structure and rates. In particular, we focus on components of the broader scenario that offer the most utility in terms of possible lessons for other countries seeking tobacco tax reform, including linking the reform to other politically popular policies, the breadth and depth of civil society support for the reform, the importance of technical assistance, and the positive effect of a related international trade dispute. Finally, we discuss the emerging issue of product valuation.

Background on Tobacco Taxes in the Philippines

For much of the latter part of the past century, Section 142 of the Internal Revenue Code assessed an ad valorem excise tax on cigarettes that as a result of low wholesale prices rarely exceeded a few pesos per pack. Cigarette prices in the Philippines, as a result, have been very low by global standards and very affordable even considering significant poverty. Notably, the tax was discriminatory because it assessed lower rates on domestic brands versus domestically-produced foreign brands and imports (imports were assessed the highest rates). In 1997, the Philippines Congress passed a new bill, RA 8424, addressing tobacco excise taxes. The final legislation – similar to a proposal backed vigorously by the largest domestic cigarette producer at the time, Fortune Tobacco Corporation – included four cigarette price tiers, with an increasing specific excise tax rate.[33] Importantly, the legislation locked the prices that the Bureau of Internal Revenue (BIR) considered for tax tier placement at 1996 prices. The price-tier freeze had the effect of ensuring the lowest tax rate for the vast preponderance of Fortune's product line for as long as the legislation was in effect, even if actual product values increased. In 2004-05, there was another reform, this time of both alcohol and tobacco taxation. PMI vigorously sought the elimination of both the price tiers and the price-freeze designations.[34] Ultimately, there were very modest increases in the specific excise tax rates, but the tiered structure and the price freeze element endured. In 2012, after vigorous public and legislative debate, Congress passed a new sin tax bill, RA 10351, which dramatically reformed the earlier excise tax laws. The bill immediately reduced the number of price tiers from four to two, which would then decrease to just one after two years. The rates in the new bill were significantly higher than previous rates.[35] The bill removed the price freeze component and includes a provision to index the rates each year to address inflation and income growth, which should directly affect the affordability and thereby consumption of cigarettes.[36]

The PhilHealth Link

Every key informant argued that the excise tax reform's direct link to PhilHealth, the country's emerging universal health program, was vital to its success. PhilHealth administers the country's National Health Insurance Program, which provides facilities-based health care insurance coverage to members. Membership is compulsory for workers in the formal sector, from whose salaries monthly premiums are deducted. Membership by the informal sector is voluntary, but the national and local governments fully subsidize insurance costs for the poor.

Proponents of sin tax reform chose to link increased tobacco taxes to funding for universal health coverage in part to elicit support for the tax reform from both government officials and the general public. In previous attempts to reform tobacco taxes in the Philippines, former and current DOF officials noted that a larger emphasis was placed on broader revenue generation (i.e., not linked to health or other social services). In the 2012 effort, however, the emphasis shifted to using the revenues for the provision of healthcare to the most vulnerable segments of society. Specifically, roughly 68% of tobacco tax revenues are now earmarked toward provision of PhilHealth benefits to the lowest socioeconomic quintile. Leftover funds from this main allocation are directed to the next quintile. In addition, approximately 17% of the tobacco tax revenues are to be spent on health infrastructure investments including updating older health facilities and building new ones throughout the country.

33. The four retail price (per pack in pesos) tiers with per pack tax rates: P5 (tax P2.72); P5-P6.50 (P7.56); P6.50-P10 (P12); and >P10 (P28.30).
34. Philip Morris. 2003. "Letter to President Arroyo" (made public by PMI). February 3, 2003.
35. The new tax rates are: Php12.00 for cigarettes priced at less than Php11.50/pack, and Php25.00 for those priced at Php11.50 and up. These are expected to increase from 2014-2017 to: for 1st tier Php17 -> 21 -> 25 -> 30; for 2nd tier Php27 -> 28 -> 29 -> 30 (effectively, merging into one tier by 2017).
36. For a discussion of affordability's effects on consumption, see E. Blecher and CP van Walbeek. An international analysis of cigarette affordability. *Tobacco Control.* 2004 Dec;13(4):339–46.

The PhilHealth link has a structural component in terms of a much broader allocation of resources across political districts. Before 2012, tobacco tax revenues were mostly directed back to the tobacco-growing provinces. Twenty-one provinces officially grow tobacco, but production is mostly concentrated in five provinces in northern Luzon, so as a result, most resources went to very small number of districts. Many informants noted, too, that the money typically "disappeared" into these regions and there was little transparency about who was receiving the money and for what purposes. Several legislators and members of their staffs suggested that both the new formula and greater resources provided tangible public goods to many more legislative districts. The proposal to earmark taxes for PhilHealth offered a tremendous opportunity for politicians to demonstrate to their constituents how the government was providing much needed and vital public services, particularly in the House, in which 80% of the legislators are elected by district.

The proposal also prudently allocated the remaining 15% back to the tobacco-growing districts. This aspect of the formula provided political cover to supporters who were concerned about the protection of tobacco growers. With the increased rates, the projected size of the allocation was still substantial and would make it difficult for growers to gain significant public sympathy. This policy linkage relied on arguments to generate revenue for a salient social issue, garnering public support, while recognizing and utilizing the political interests of elected representatives.

Civil Society

Key informants from different government sectors and civil society suggested that civil society played a key role in the successful reform. Most interviewees suggested that civil society support was a necessary but not sufficient factor in the reform. The key challenge is identifying the specific components of civil society's participation that were central to its critical role. First, in comparison with previous efforts, there was consensus among interview subjects that the 2012 coalition was composed of a broader collection of organizations. For example, the core group of supporting organizations included the nationally well-reputed Philippine College of Physicians, a strong economically-focused research and advocacy organization (Action for Economic Reforms) with extensive experience in tax reform and the main tobacco control coalition, the Framework Convention on Tobacco Control Alliance, Philippines (FCAP). This composition, with a mixture of both health- and economic-based organizations, seemed to contribute to more nuanced arguments that could be directed across government sectors.

The second component that observers noted consistently was civil society's strong relationship with government. The Philippine government was mostly new to major tax reform of this nature and needed support from other societal actors with the requisite experience and knowledge. As a result, supporting organizations provided material support to key official institutions as they made the empirical case for the reform. For example, the DOF worked closely and openly with the economics-focused civil society organization, Action for Economic Reforms (AER), to provide assistance to House and Senate champions of the reform, specifically on technical and economic matters, while the DOH worked with FCAP and PCP on the health aspects.

Third, several government officials commented that the broader pro-tax reform coalition was well coordinated and remained consistently "on message." According to observers, the key actors and organizations met often, developed ideas together, and presented a coherent and consistent message.

Finally, the coalition had material support, both from within the country and from external sources. The large domestic coalition described above worked with several international collaborators, including the World Health Organization, the World Bank, and the Bloomberg Initiative to Reduce Tobacco Use.

Technical Assistance

Many key informants, particularly those in more technical roles, argued that strong and appropriate technical assistance played a very important role in the successful reform. Domestically, the DOF played a key role in providing technical assistance to proponents in both congressional houses, particularly through modeling different tax reform scenarios. High-ranking officials in the DOF also noted specifically that AER played an important role in developing appropriate and useful empirical models for considering price elasticity, and changes in revenues and consumption. Several government officials suggested that having domestic capacity to work through these issues was important for making the case for reform convincingly because the core arguments and evidence came largely from within Philippine society. This domestic dynamic helped to address complaints that the concept of higher tobacco excise taxes was imported from developed countries.

Internationally, among other actors, the World Bank (WB), the World Health Organization, and several independent consultants played vital roles in providing some of the templates for models and helping authorities at the DOF and the BIR to develop Philippine-specific models. One of the issues that the WB representative worked on with the DOF was the "real" economic impact on farmers, which was thought to be necessary because of the argument that the tax reform was being developed "on the backs of farmers." Many observers noted that, though domestic capacity was strong, the experience and assistance from the IGOs and other international actors was important and meaningful in the policy reform.

The assistance was vital at different parts in the process. Members of both the Senate Finance Committee and the House Ways and Means Committee noted that tobacco excise tax experts came well prepared to committee meetings with models of different scenarios and were able to make compelling, empirically-supported arguments in support of reform.

The only consistent complaint that we noted from interviewees was an occasional lack of follow-up from some of the external technical experts immediately prior to some of the major legislative hearings. In one scenario, prior to a Senate hearing, the team preparing testimony in support of the tax reform was seeking information on other countries' experiences after a large excise tax rate increase and had difficulty obtaining these data from their external counterparts. Perhaps most during the near-daily grind of a legislative session, it is imperative to make certain that the appropriate support team remains in place.

Pleasant Side Effects? DS403 – *Philippines Distilled Spirits*

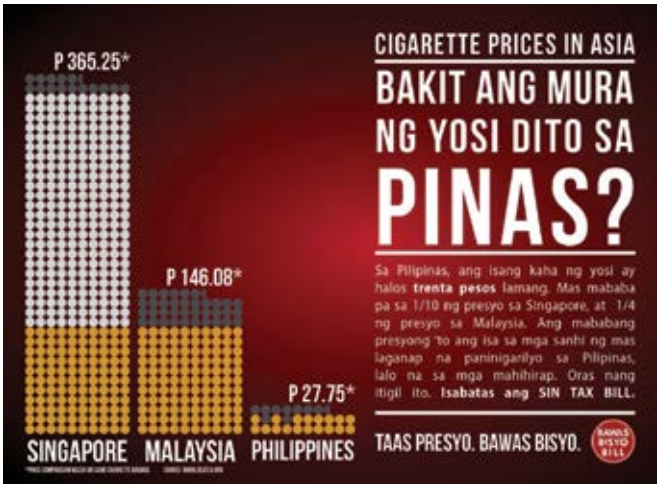
Perhaps counter-intuitively to many in the global health field, the main impetus behind the sin tax reform was arguably the outcome of a WTO complaint brought by the European Union (EU) against the Philippines. This conclusion is significant because it runs counter to much of the global health narrative suggesting that aspects of the increasingly open world trading system, particularly rules governing non-tariff barriers to trade and the formal dispute settlement process, undermine efforts to promote public health. In fact, this conclusion is consistent with arguments made by proponents of trade agreements, who suggest that the rules-based system can insulate governments from the private interests of domestic firms, thereby leading to better policy decisions.

In this dispute, the EU argued that the Philippine tax system governing distilled spirits discriminated against imported products. The law taxed distilled spirits made from inputs common in the Philippines – e.g., sugar cane – at a considerably lower rate than other grain-based spirits not typically manufactured in the Philippines. The WTO panel ruled that this feature of the Philippines' tax structure was discriminatory in that it treated imported products less favorably than like domestic products. The direct public health effect of this decision is probably minimal, but the indirect effect has been highly consequential.

The Philippines was ordered to bring its law into compliance with WTO law, which required reform of taxes governing distilled spirits. Facing possible retaliation from the powerful complainant (the EU), the Philippine government used the obligation as an opportunity to reform the tax system for both alcohol and tobacco products, a so-called "sin tax." In the tobacco context, the reform simplified the excise tax structure to remove several features – price tiers and freezes on the tier-identification – that were helping to keep taxes and prices of established tobacco products low and affecting market entry. Moreover, the legislation ultimately placed a larger burden on tobacco than alcohol, and one that was much larger than any previous tax obligation. In sum, the outcome has the potential to be one of the most significant public health victories in recent memory in the Philippines, and it was propelled initially by the results of a WTO dispute. This experience suggests that certain economic policy-related events can alter political conditions in favor of reform in the interests of health. Such events include a finding that a tobacco or alcohol tax measure does not comply with WTO law, thus permitting the government to generate one that produces superior health outcomes. Of course, the government could have reformed the polices in a manner that did not generate positive public health outcomes, but in future, the public health community might consider more carefully under what conditions economic agreements might actually present opportunities to push regulatory efforts in the public health arena.

Political Will

All of the key informants that we interviewed remarked on how the confluence of support from key high-level government officials helped to make the reform possible. These high-level officials included President Benigno Aquino III; Secretary of Finance, Cesar Purisima; BIR Commissioner, Kim Henares; Senate Finance Committee Chair, Franklin Drilon; and House Ways and Means Committee Chair,



AER / BAWAL BISYO BILL CAMPAIGN
The affordability of cigarettes in the Philippines is a major reason for the high prevalence of smoking.

Isidro Ungab. Of course, it is challenging in other contexts to replicate this kind of cross-institutional support in other countries, but it is crucial to be aware of scenarios where this kind of wide support might be brought to fruition. The key variable, by most accounts, was President Aquino's strong and unwavering support. The public support at the highest level was the cue to other high-level officials that they should and could champion the reform. Thus, the lesson learned is that if a country's chief executive is indicating genuine support for such a reform, the public health community must rally around the cause – as they did in the Philippines – to encourage and engender the initiative among other key decision-makers in different sectors of government.

The WTO, the Sin Tax, and Valuation

In 2008, the Philippines filed a complaint against Thailand at the WTO concerning Thailand's tobacco tax regime. The Philippines argued that Thailand's tax regime violated rules concerning customs valuation because the regime valued Philip Morris cigarettes imported from the Philippines at a level higher than the value declared by Philip Morris. The effect was to require Philip Morris to pay a higher tax on imported cigarettes than would be due if the declared value were accepted for purposes of customs valuation. Thailand countered that Philip Morris was under-valuing its exported cigarettes in a concerted effort to pay less tax to Thailand. After mandatory preliminary bilateral negotiations failed, the case went to adjudication at the Dispute Settlement Body (DSB). The panel ruled in 2010, and the Appellate Body in 2011. Both decisions favored the Philippines, and Thailand was compelled to accept the Philippines' valuation.

While the merits of the case arguably have little to do with public health directly and more to do with technical valuation issues, several broader concerns merit consideration. First, because WTO disputes between two LMICs are rare and the Philippines is not a frequent user of the dispute settlement system, the Philippines' decision to pursue this particular complaint has attracted scrutiny. In particular, many in the Philippines public health community have demonstrated concern that the tobacco industry received special treatment from the government. International trade disputes are complex and pursuing them is expensive, and therefore governments do not enter into them lightly. In interviews with former and current high-level officials in DTI and the Department of Foreign Affairs, however, informants defended the decision on the merits of the case – the valuation issue – and were transparent about the significant role played by PMI providing background materials in order to build the legal case. It is important to make distinctions between a case like this one about technical financial issues and other WTO cases such as the current tobacco plain packaging complaints against Australia that clearly target domestic public health regulations.

However, a broader issue about valuation does deserve attention in the broader context of this report. Specifically, officials at the DOH noted in interviews that they believed there was indeed a deeper valuation issue: they claimed that some Philippine manufacturers were under-reporting value in order to minimize taxes within the Philippines. Notably, however, DOF, BIR, and DTI all supported the WTO claim, which provided tacit approval of the valuation, even though it might not have been accurate.

Second, in an important addendum to the earlier valuation issues, this process surfaced again soon after implementation of the tax increase in 2013 as a possible concern. In the face of huge losses in market share, tobacco MNCs are loudly accusing a small, long-established domestic manufacturer, Mighty Tobacco Corporation, of under-valuing its products in order to undercut the competition. For example, in terms of input costs, Mighty is reporting a cost of $0.68 per kilogram of tobacco, while other companies report between $3 and $5, to establish that it is not taking huge losses on its suddenly brisk sales (market share has jumped from around 4% in 2012 to between 20 and 30% according to some media reports). As of late 2013, BIR and DOF have publicly demonstrated concern about the valuation specifically for the tax implications – i.e., the possibility that this is a form of evading taxes – and are examining the issue. While these institutions found PMI and PMFTC's possibly suspect valuations acceptable in the WTO case, it remains to be seen whether they will find Mighty's calculations also reasonable.

Here is an important larger lesson: valuation is crucial to the implementation of ad valorem taxes. Over the long term, key actors in the process need to agree upon what is fair valuation, particularly because of the enormous implications for taxation and exporting. All governments need to have systems in place to resolve such issues fairly; in the Philippines, BIR, DOF, and possibly DTI need to coordinate effectively on this important task. In addition, a broader solution might reasonably include a much higher specific tax to ensure that an undervaluation will have less or no impact on both tax revenues and price.

Part IV – Tobacco Excise Tax Reform – Key Findings/ Recommendations

- Linking tobacco excise tax reform to funding for a popular and useful public good such as universal health coverage may be an effective way to generate support from both elected officials and the general public.
- Engendering domestic technical capacity to support tobacco tax reform can increase the probability of successful policy change.
- International organizations – governmental and non-governmental – can provide vital technical support for tax policy reform; these organizations must remain engaged throughout the process.
- International economic disputes may provide political opportunities for improved domestic and international public health policies.
- For tax and trade reasons, governments must develop and maintain strong, effective, and transparent systems to determine and monitor valuation of products in the context of ad valorem taxes, or perhaps better in many cases, replace ad valorem taxes with specific taxes altogether.

Conclusion

This report has sought to illuminate the complex intersection of tobacco control and economic policymaking. Unfortunately, in both policy realms, there is considerable misinformation as public health policies interact with major economic policies, particularly concerning trade, investment, and taxation. Having better information will surely help decision-makers to develop policies that work best for both improved public health and economic prosperity. In brief, policymakers in the Philippines must be thoroughly aware of the possible implications of entering into new economic agreements – simply agreeing, for example, to partner countries' demands for increased intellectual property rights protection or greater rights for investors could in certain circumstances undermine public health efforts. On the other hand, channeling resources to block tariff reductions will likely not result in the desired health outcomes in most scenarios. Similarly, with FDI more broadly, governments need to consider the broader economic and policy contexts to identify if and how new investment might affect public health. As the Philippines case suggests, the relationships are complex and do not always generate obvious outcomes. For both of these tasks, improved coordination, or even better, actual cooperation, among the appropriate economic and health authorities is paramount to resolving difficult issues at this policy nexus. An adversarial approach is likely to be mostly counter-productive. The challenge is how officials can understand their counterparts' policies and obligations – perhaps even demonstrate empathy – towards reconciling difficult positions. We noted consistently that most health officials were not well informed about trade, investment, or tax policies and goals, and that most economic officials lacked a sufficient understanding of health policies and goals, including tobacco control. Finally, the recent sin tax reform experience actually demonstrates how better coordination and cooperation can lead to the positive policy outcomes that most governments and the general public are seeking: superior public health and improved economic prosperity.

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