WORKING HAND IN HAND FOR TAX POLICY REFORMS

Southeast Asia Initiative on Tobacco Tax (SITT) Year 3 Annual Report

March 2013
MESSAGE FROM THE CHAIR OF THE SITT STEERING COMMITTEE

Dr. Somsak Chunharas

Last year’s World Health Assembly in May adopted a global voluntary target of 25% reduction in premature deaths from non-communicable diseases (NCDs) by 2025. Such an ambitious target is only achievable through the accelerated implementation of effective tobacco control measures as contained in the WHO Framework Convention on Tobacco Control. More recently, at its 132nd meeting last 21-29 January 2013, the WHO Executive Board (EB) endorsed a Global Monitoring Framework for NCDs, including 9 targets and 25 indicators, for adoption by all WHO Member States at the 66th World Health Assembly in May 2013. For tobacco, the proposed target is a reduction of 30% by 2025 in smoking prevalence among persons aged 15 and older.

In the light of ongoing global consultations on the post-2015 development agenda, EB Members also discussed the achievement of the health-related Millennium Development Goals (MDGs) and the role of health in the post-2015 development agenda. During the discussions, Member States emphasized that health should be the cornerstone for the post-2015 development framework and widely agreed on the importance of universal health coverage (UHC) within this framework. While access to health services and coverage by health programs are essential, reducing health risks such as tobacco requires more than effective health services. Strong political will to take bold actions, balancing economic gains and health benefits, are at the core of better health for our people in the increasingly complex and inter-related world.

The tobacco control achievements in the region, particular those linked to SITT’s focus on raising tobacco taxes to reduce tobacco consumption and the use of tobacco tax revenues for health are, therefore, most notable in showing such political commitment to health as a cornerstone in the overall development framework. They are undoubtedly key steps bringing us closer to achieving the ambitious global targets of not only saving lives and improving health but well being for all.

On behalf of the SITT Steering Committee, I commend all our partners for their hard work over the past year and their relentless efforts to work together in good partnership among key stakeholders – policymakers, academicians and civil societies generating useful knowledge and evidences as well as joint learning among them. I hope our experiences in SITT add to the learning of wider local as well as global players. I wish us all continued success in the year ahead resulting in concrete health benefits of our people in the region and also valuable contribution to our global partners.

MESSAGE FROM THE SITT PROJECT DIRECTOR

Dr. Ulysses Dorotheo

This past year has seen several important tobacco control milestones in our region: the establishment of a Tobacco Control Fund in Lao PDR, the approval of Vietnam’s comprehensive Tobacco Control Law (including a Tobacco Control Fund), the institution of major tobacco tax reforms in the amended Sin Tax Law of the Philippines, and the passage of the long awaited government regulations to implement pictorial health warnings in Indonesia, in addition to the growing commitment for tobacco tax reforms in Cambodia and Indonesia, all of which SEATCA and our SITT partners have been privileged to contribute to. We are, therefore, happy to share some of these case studies in this Year 3 report and hope they will be useful to our readers, even as we invite the international public health community to join in our celebration and congratulate all the many government and civil society partners for their hard work.

Also in 2012, at its fifth session, the Conference of Parties to the WHO FCTC adopted a set of Guiding Principles and Recommendations for the implementation of Article 6 (tax and price measures), providing governments with an important tool for raising tobacco taxes and prices, making tobacco less affordable, and reducing tobacco consumption to improve health and save lives.

Thus, as always, it remains an exciting time to be implementing tobacco control in the region, and we continue to be fortunate to work alongside friends, partners and funders, who are similarly committed to public health as a cornerstone of human development.
In this Year 3 Annual Report, the SITT regional team and our country partners give special focus to Indonesia and the Philippines to provide a glimpse of the unique contexts and dynamic forces with which our partners work to champion policy reforms in tobacco taxation and pictorial health warnings.

In this edition, significant policy changes and processes are documented in case studies to highlight the challenges and lessons learned in the achievement of the following milestones:

• Passing the Sin Tax Reform Law in the Philippines
• Moving policy in tobacco taxation using research-based evidence in Indonesia
• Passing and implementing the pictorial health warning regulation in Indonesia

A general overview of policy developments in other SITT countries is also captured in this report, recognizing the hard work of all country partners, both government and civil society, in changing the landscape for effective tobacco control in the region.

Policy is a bargained outcome, the environment is conflictual and the process is characterized by diversity and constraint.
To create or change policy, negotiation, participatory design and implementation, and situation specificity are required.

(Gordon, Lewis and Young, 1997)
Tobacco Taxes in ASEAN

The importance and effectiveness of tax and price measures to reduce tobacco consumption, particularly among the young, is clearly emphasized in Article 6 of the WHO FCTC, and all Parties to the Convention are obligated to establish effective policies for its implementation. To this end, the World Bank has recommended a tobacco tax burden of 66 to 80% of the retail price, while WHO recommends a tobacco excise tax burden of 70% of the retail price to effectively reduce consumption. However, within Southeast Asia, only Brunei Darussalam, Singapore and Thailand have attained these tax benchmarks (Figure 1).

Although government revenues from tobacco taxes have slowly increased (nominally) over the years, the increases in their real values have generally not been significant, and without any real impact in reducing tobacco consumption. The fast growth of national economies and household incomes in Southeast Asia is a significant, and without any real impact in reducing tobacco consumption. The (nominally) over the years, the increases in their real values have generally not been

Cigarette prices vary across the region but prices relative to income (expressed as Relative Income Prices in Figure 2) have been steadily and seriously declining, indicating increasing affordability and providing little incentive to reduce consumption. It is therefore crucial to increase tobacco tax at much higher rates than at present, not only to save lives and reduce health care costs, but also to contribute to more government revenues to fund health promotion activities and social development programs.

Research studies produced under SITT have demonstrated the positive impact of tobacco tax increases and suggest prospective actions to decrease affordability for achieving these positive outcomes. Some of these potential impacts on government revenue, smoking prevalence and the number of lives saved are shown in Table 1.

Over the course of three tax increases in Indonesia, the revenue from tobacco tax increased from IDR 32.6 trillion in 2005 to IDR 69 trillion in 2010, while the smoking prevalence was estimated to have dropped by 1.6% points, saving 890,000 lives (over a 5-year period). In Lao PDR, after the imposition of an additional specific excise tax at LAK 1,500 per pack in 2010, it was increased to LAK 5,000 per pack in 2011, the revenue from tobacco excise tax was estimated to have increased from LAK 31.8 billion in 2009 to LAK 162.9 billion in 2011; the smoking prevalence was also estimated to have dropped by 0.72% points, saving 8,708 lives. While both these countries experiences clearly demonstrate the large fiscal benefits from small tax increases, the reductions in prevalence and lives saved have been relatively small.

More recent policy developments in increasing tobacco taxes and dedicating tax revenues to health promotion have taken place in four SITT countries. In Indonesia, the government had increased the tobacco tax rate to 62% of the retail price in 2011; however, due to a legal case filed by tobacco companies (Indonesian law sets a maximum excise tax rate of 57%), the government reverted to the current rate of 46%. In the Philippines, the passage of the Sin Tax Reform Law (effective 1 January 2013) removed a 16-year price classification freeze, shifted the four-tiered tax rates to a unitary rate (2 tiers in 2013, single tier by 2017), and increased the tax rate by 4% annually beginning in 2018. Finally, in both Lao PDR and Vietnam, a Tobacco Control Fund has been established from earmarked tobacco taxes for tobacco control activities.

Challenges in achieving SITT’s tax objectives:

- Simplifying the multi-tier tax systems, particularly in Indonesia
- Increasing taxes to a level that counters the increase of per capita GDP and economic growth, in order to make cigarettes increasingly less affordable
- Countering the tobacco industry’s expected opposition to tax increases and its consistent actions to defeat tax initiatives that could effectively reduce consumption
- Developing country-specific sustainable funding mechanisms, based on tobacco taxes, for tobacco control and health promotion
- Overcoming regional economic and trade agreements which treat tobacco as a regular commodity in terms of tariff exemption and free flow of business

Table 1: Tobacco excise tax increase scenarios and impact on smoking prevalence, lives saved, and tax revenues

<table>
<thead>
<tr>
<th>Countries</th>
<th>Excise Tax Increase Scenarios</th>
<th>Reduction in Smoking Prevalence (% points)</th>
<th>Lives Saved (persons)</th>
<th>Current Tax Revenue</th>
<th>Total Tax Revenue After Increase</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cambodia</td>
<td>From 10% to 20%</td>
<td>0.85 (from 23% to 22.15%)</td>
<td>None</td>
<td>KHR 65.8 billion</td>
<td>KHR 86.40 billion (31.4% more revenue)</td>
</tr>
<tr>
<td>Indonesia</td>
<td>From 50% to 57%</td>
<td>0.9 (from 32.4% to 31.5%)</td>
<td>500,000</td>
<td>IDR 73.3 billion</td>
<td>IDR 98.74 billion (34.7% more revenue)</td>
</tr>
<tr>
<td>Lao PDR</td>
<td>Additional specific tax of LAK 1,500 (on top of 15% ad valorem tax)</td>
<td>0.47 (from 38.7% to 38.24%)</td>
<td>5.838</td>
<td>LAK 201.3 billion</td>
<td>LAK 29% 60 billion (41% more revenue)</td>
</tr>
<tr>
<td>Philippines</td>
<td>From 41% to 66%</td>
<td>5.3 (from 28.3% to 23%)</td>
<td>1,130,000</td>
<td>PHP 26 billion</td>
<td>PHP 72.20 billion (37.7% more revenue)</td>
</tr>
<tr>
<td>Vietnam</td>
<td>From 65% to 75%</td>
<td>6.6 (from 23.6% to 17.2%)</td>
<td>1,000,000</td>
<td>VND 14 billion</td>
<td>VND 18.30 billion (24.6% more revenue)</td>
</tr>
</tbody>
</table>

*Note: Cambodia excise tax base is only 65% of invoice price. Vietnam excise rate is % of ex-factory price. Indonesia and Philippines use a specific excise tax system.

*RIP = percentage of per capita GDP required to purchase 100 packs of cigarettes

Figure 1: Tobacco Tax Burden as a Percentage of Retail Prices in ASEAN, 2013

Figure 2: Relative Income Prices (RIP)* in six ASEAN countries, 1999-2010

*Note: Cambodia excise tax base is only 65% of invoice price. Vietnam excise rate is % of ex-factory price. Indonesia and Philippines use a specific excise tax system.
Highlights of 2012 Achievements

The past year marks a significant period in the implementation of the SITT project. Developments in achieving policy objectives in both country and regional levels took place following the previous years’ work to position the initiative as an urgent policy agenda in each of the five SITT countries.

National governments, particularly policymakers, have benefitted from numerous research-based materials developed with support from this project. In addition, the opportunities created for officials from the Ministry of Finance, Ministry of Health, Parliament/National Assembly, and civil society members, among others, to collaborate with one another and learn from other colleagues in the region have paved the way for stakeholders to adopt a common position to advance tobacco tax reforms and institute sustainable mechanisms for health, in light with the emerging global focus on non-communicable diseases.

The availability of resources and technical assistance to establish the positive impact of increasing tobacco taxes and pictorial health warnings for Indonesia, as both fiscal and health measures, has catalyzed the policy process leading to the passage of the following in 2012:

- Tobacco Control Law in Vietnam
- Sin Tax Reform Law in the Philippines
- Government Regulation (including Pictorial Health Warning provisions) in Indonesia

In addition, strong commitment for tobacco tax reform has been achieved with Cambodia’s Tobacco Tax Working Group, as well as significant progress towards the passage of the Decree creating the Tobacco Control Fund in Lao PDR and the recent increase in the tobacco excise tax in Indonesia.

### 2009-2012 Achievements

<table>
<thead>
<tr>
<th>Year</th>
<th>Event</th>
</tr>
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<tbody>
<tr>
<td>2009</td>
<td>Start of SITT</td>
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<tr>
<td>2010</td>
<td>Publication of SITT Tax Report Cards describing each country’s tobacco tax system and identifying and recommending specific reforms for each</td>
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<tr>
<td>2011</td>
<td>Country partners implemented research on cigarette affordability and impact of increasing taxes and other policy-relevant studies</td>
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<td>Fourth Conference of Parties to the WHO FCTC decided to establish a working group to develop Article 6 Guidelines, which is joined by Thailand as Key Facilitator, and Cambodia, Philippines and Vietnam as members</td>
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<td></td>
<td>Lao PDR increased its specific excise tax on cigarettes from LAK 100/pack to LAK 500/pack (on top of ad valorem taxes)</td>
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<td></td>
<td>Prakas formally creating the Tobacco Tax Working Group is signed by the Deputy Prime Minister of Cambodia</td>
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<td></td>
<td>Completion of National Adult Tobacco Survey – Cambodia</td>
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<td>2012</td>
<td>Technical Working Group on Health Promotion Funding created by the Philippine Department of Health</td>
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<td></td>
<td>Shared SITT case studies on experiences and lessons learned in building alliances across sectors to change policy and on evidence-informed policymaking</td>
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<td></td>
<td>The National Assembly ratified the Tobacco Control Law in Vietnam, including establishment of a Tobacco Control Fund based on tobacco tax revenues</td>
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<td></td>
<td>The fifth Conference of Parties to the WHO FCTC adopted a set of Guiding Principles and Recommendations for implementation of FCTC Article 6</td>
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<td>President Benigno Aquino III signed the Sin Tax Reform Law in the Philippines</td>
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<td></td>
<td>President Susilo Bambang Yudhoyono signed the Peraturan Pemerintah (PP) or Government Regulation mandating the implementation of pictorial health warnings in cigarette packs in Indonesia</td>
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</tbody>
</table>
Southeast Asia's largest economy, not yet having signed the WHO FCTC, and allowing very lenient regulations of the tobacco industry, Indonesia is a haven for local and multi-national tobacco companies. While the number of cigarette firms has decreased over the years, (1,555 in 2009 to 1,132 in 2011), recent Ministry of Industry (MOI) data indicates that cigarette production is continuously increasing -- from 220 billion sticks in 2005 to 258 billion sticks in 2011.

Among thousands of cigarette manufacturers in the country, three companies dominated the local market in 2011: Gudang Garam (28.2%), Sampoerna (18.8%), and Djarum (12.7%). There are three types of cigarette in Indonesia: machine-made kretek cigarette (sigaret kretek mesin or SKM), hand-rolled kretek cigarette (sigaret kretek tangan or SKT) and white-machined cigarette (sigaret putih mesin or SPM). Between 2005-2010, the yearly average production of SKM reached 58% of the total national cigarette production, followed by SKT with 35%, and SPM with 7%.

A Complicated Taxation System

Favoring the tobacco industry even further, the current Indonesian tax system is one of the most complicated systems in the world. Excise rates imposed on tobacco products are determined by the tobacco type, production scale of the firms and the range of reference prices or harga jual eceran (HJE). The HJE per stick or per gram is determined by Ministry of Finance (MOF), which includes in its calculation the production cost, excise burden (specific excise tax and VAT) and distributor profit. Cigarette firms propose the amount/value of the reference price for each of their tobacco products, and since the reference price is different for every brand, there are thousands of reference prices and excise rates that must be determined by the MOF for application.

The difference in the excise rates is causing a wide range of HJE between the cheapest and the most expensive tobacco products. Furthermore, different excise rates based on the production scale of firms create loopholes for cigarette firms. By producing in the lower production scale, cigarette firms can avoid paying higher excise rates.

Between December 2006-2009, Indonesia used a mixed (ad valorem and specific) excise system with 19 tiers (reduced to 15 tiers in 2012). Being easier to administer, the specific excise system was considered more efficient than the ad valorem system; however, the multiple tiers for calculating the HJE keep the excise tax administration complicated.

Table 1. Average excise tax burden in Indonesia, 2008-2013

<table>
<thead>
<tr>
<th>Year</th>
<th>Percentage (%)</th>
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</thead>
<tbody>
<tr>
<td>2008</td>
<td>33</td>
</tr>
<tr>
<td>2009</td>
<td>38</td>
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<tr>
<td>2010</td>
<td>44</td>
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<tr>
<td>2011</td>
<td>46</td>
</tr>
<tr>
<td>2012</td>
<td>51</td>
</tr>
<tr>
<td>2013</td>
<td>46</td>
</tr>
</tbody>
</table>

Rationale for Reforms

There have been efforts from the government to gradually simplify the excise system by removing the production category, determining specific excise and raising the excise rates for all cigarette types; however, the average increase in the excise rate is still relatively slow and not automatically adjusted to inflation. By 2013, the average excise rate will decrease to 46% (51% in 2012) due to MOF’s increase in both the excise rate and price range of the HJE, whereas between 2008-2012, the MOF increased only the excise rates.

Furthermore, previous policy changes have barely considered increasing tax rates as a public health or tobacco control tool, and thus, have minimal health impact by reducing consumption. If this remains unchecked, Indonesia is set to face a future with a high burden of disease with its increasing youth smoking prevalence, which is already at 19%.

Changing the Policy Landscape through Evidence and Advocacy

This scenario provided the perfect platform for SEATCA to intervene by partnering with the Demographic Institute (DI), a local think-tank under the Faculty of Economics, University of Indonesia as its Southeast Asia Initiative on Tobacco Tax (SITT) country partner. By capitalizing on DI’s strength and credibility in conducting research, the SITT project hopes to encourage the national government to adopt progressive tobacco tax systems that achieve both the health and fiscal objectives of the country.

The research established that despite nominal cigarette price increases in the average retail price per pack (16 cigarette sticks) in the last decade (IDR 2,955 in 2000 to IDR 6,023 by 2010), Indonesia still has among the world’s cheapest and most affordable cigarettes, but due to the addictive nature of tobacco and the inelasticity of demand for cigarettes, increasing the excise tax has the potential to not only reduce consumption but also generate significant additional revenues for the government. In addition, simulation results showed that in spite of the reduced smoking prevalence and cigarette consumption, none of the simulated tax increases had any significant impact on industry revenues.

2. Optimal Utilization of the 2% Earmarked Tobacco Tax

Based on Law 39/2007, revenues generated from cigarette excise must be distributed to tobacco-producing provinces. This revenue sharing must be used for five purposes: improving the quality of raw materials, developing the industry, improving social welfare, disseminating Customs regulations, and law enforcement on illegal cigarettes, to achieve the three main priorities of public interest under the law, i.e. employment, health, and government revenue. However, evidence showed that the 2% earmarked tobacco tax has not been used properly. Local governments and NGOs who are entitled to use the fund, did not know how to access this specific resource or had not been using the fund for its specific purpose. Stemming from this study, DI has helped the Ministry of Health develop guidelines, providing a list of options and best practices for local government units and NGOs, on how to use the fund for social, specifically health, programs and local development.
3. Exit Strategy for Small-scale Industry

This study found that the MOF and Ministry of Small-scale Industry (MOSSI) had different definitions for a small-scale cigarette industry. The MOF categorized those that produce less than 400 million sticks per year as small-scale, while MOSSI categorized those that earn IDR 3 million -- IDR 2.5 billion per year as small-scale. Based on MOF calculations, sales of small-scale industry producers -- whose minimum price is IDR 234 per cigarette stick-- could reach IDR 93 billion per year. Thus, there were producers categorized as small-scale industry paying very low excise rates, when they could in fact pay more and were actually too big to be considered small-scale.

Based on a recommendation from the study to revisit the government’s definition of small-scale industry -- so that producers pay the appropriate excise based on their capacity -- the MOF Fiscal Policy Board has reclassified cigarette manufacturers that produce at least 300 million cigarette sticks as no longer small entrepreneurs because their production is tantamount to IDR 60 billion in sales. Based on this reclassification, such manufacturers must now pay higher excise taxes, such that, because cigarette excise is considered the next highest component in cigarette taxation system and the increasing affordability of cigarettes with the MOF using the results from the affordability study and exit strategy for small-scale industry in February 2011. Several briefings attended by the media, academics and government officials were also organized to disseminate the results of the 2% earmarked tobacco tax study and the affordability study, in December 2010 through March 2011. And in January 2012, a research briefing was also organized for MOF officials to discuss the findings from the price and retailer survey.

The SITT team also had the opportunity to brief President Susilo Bambang Yudhoyono on the advantages of introducing tobacco tax policies that will benefit public health and government revenues, for which he expressed support. Government agencies that participated in these activities, particularly the MOF and MOH, have benefitted from the research findings generated in the form of policy briefs, factsheets and other information materials. This evidence has been used as basis in introducing new policies and instituting reforms to existing legislation (e.g. challenging the 57% maximum cap in the Tax Law), as well as for countering tobacco industry arguments aimed at protecting the existing system that heavily favors the industry.

Other tobacco control groups within the Indonesia Tobacco Control Network (ITCN) have also often quoted from the SITT findings, which proves the credibility and usefulness of these studies to further advance tobacco control policies in Indonesia. In addition, the wide media coverage that has often followed every dissemination activity of the SITT studies, shows their effectiveness in framing the issues not just in the macroeconomic perspective but in putting a human face to economic disparity, diseases and lingering poverty associated with the tobacco industry.

While there is still much ground to be covered before other tobacco control policies can be put in place, policymakers and other stakeholders have taken the initial steps in this direction by heeding to the policy issues presented by SITT. The SITT country partners composed of leading researchers and academics will continue to advance these issues by producing and presenting compelling evidence towards further reforms in Indonesia’s tobacco control landscape.

4. Price and Retailer Survey

The study found that the banderol price is lower than the retail price for most cigarette products. Assuming that the retailer’s profit margin for cigarette was unchanged between 2007 and 2011, the whole excise tax is therefore paid by the consumer or no longer subsidized by the tobacco company. This finding also indicates that the government tax calculation of the reference price is underestimated, especially for the brands of Gudang Garam International and Gudang Garam Surya that have already surpassed their HJE range.

Armed with solid evidence from the researches listed above, the SITT country team initiated a series of high-level meetings with key decision makers from the Ministries of Finance and Health. Backed by leading economic experts, the team was able to discuss and map the existing problems in the tobacco excise taxation system and the increasing affordability of cigarettes with the MOF using the results from the affordability study and exit strategy for small-scale industry in February 2011. Several briefings attended by the media, academics and government officials were also organized to disseminate the results of the 2% earmarked tobacco tax study and the affordability study, in December 2010 through March 2011. And in January 2012, a research briefing was also organized for MOF officials to discuss the findings from the price and retailer survey.

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Lessons Learned:

• Utilizing local evidence and researchers who understand the socio-political environment is needed for convincing policymakers.
• Research institutions / university think-tanks are perceived as academics and offer credibility in presenting research evidence.
• Framing tax policies as health policies puts a human dimension to fiscal issues, and thus, broadens support from different stakeholders.
• The media play an important role in building public awareness and framing public opinion on the benefits of tax reforms for health and social welfare.
Previous Efforts to Pass a Sin Tax Reform Bill

Tobacco products sold in the Philippines are imposed value-added tax (VAT), import tariff and excise tax. The current reform is on excise tax, or the tax imposed on goods manufactured or produced in the Philippines for domestic sale or consumption.

Since 1984, the country’s National Internal Revenue Code has been amended only four times; prior to 2012, these amendatory laws in 1986, 1997 and 2004 reflected changes mainly in the type of tobacco tax regime, mandating minimal increases following a fixed tax schedule.

Of particular interest is the 1997 tax reform initiative by then President Ramos’ administration, including excise tax on tobacco products. At that time, the Department of Finance (DOF) was the main mover of the reform as involving the Department of Health (DOH) in fiscal matters was then unheard of.

The resulting law, Republic Act 8240, was disappointing. It stipulated a four-tiered tax structure on machine-packed cigarettes, based on each brand’s 1996 net retail price (NRP). The structure was similar to an ad valorem system with higher tax rates for brands with higher NRPs and lower taxes for brands with lower NRPs. Because this classification of brands would remain in force unless revised by Congress, it is also referred to as the “price classification freeze” as it effectively protected existing brands from being passed up to higher tax tiers even when their actual NRPs went up. This reflected a typical struggle between the DOF and the Congress that was evident during the proceedings that led to the passage in 2004 of RA 9334, which prescribed insignificant tax increases every two years until 2011 and perpetuated the four-tiered price classification freeze. By this time, Philip Morris Philippines Manufacturing Inc. (PMPMI) had established its foothold in the Philippine cigarette market, having set up a USD 300 million manufacturing plant in Tanauan, Batangas, following its observation of the “liberalization of the investment climate” in the country.

Public health was obviously not considered in past tobacco tax law reforms, resulting in laws that tended to protect the tobacco industry’s interests and providing them stability to exist and thrive, to the detriment of public health. Previous lack of tobacco control advocates, poor public information about tobacco harms, and insufficient tobacco control knowledge were exploited by the tobacco industry to their advantage. While the industry bleeds from increasingly tight regulations in developed countries, the Philippines has been targeted as a gold mine for tobacco profits.

Reform Initiatives in Light of the WHO FCTC

With the WHO FCTC’s entry into force, tobacco taxes have become widely accepted public health tools to reduce the demand for cigarettes and prevent young people from taking up smoking. The Philippines sells the cheapest cigarettes in the world and has one of the highest smoking prevalence rates and, therefore, will greatly benefit from raising taxes on tobacco products.

The Philippines became a Party to the WHO FCTC in 2005, while the DOF proposals to institute tobacco tax reforms began in 2008. At that time, it was not their intention to comply with the WHO FCTC, but to help reduce the government budget deficit.

Part of what spurred the tobacco tax reform movement was the Southeast Asia Initiative on Tobacco Tax (SITT) Project, under which HealthJustice formed an informal technical working group from among civil society organizations and government agencies, including DOF and DOH.

Prior to SITT, there was no unified position among stakeholders on the changes needed for the tobacco excise tax system. After consultations with the technical working group and collaborative activities, there was an obvious shift in perspective. This effort was effective in building pressure to reform the tobacco tax system. In 2011, several proposals restructuring tobacco taxes were filed before the Lower House, which were consistent with Taxing Health Risks, A Policy Paper on Tobacco Excise Tax and Health Promotion by HealthJustice and University of the Philippines College of Law. This was further supported by SITT research demonstrating increasing affordability of cigarettes and the potential health and fiscal benefits of tax reforms as illustrated in scientific modeling of tax increases.

Development in the Current Congress

President Aquino did not openly support the sin tax reform measure in his first year in office, and only a few legislators from the Lower House championed the reform of the tobacco tax system. These were Henedina Abad, Pryde Henry Teves, Jocelyn Limkaichong, George Arnaiz and Niel Tupas, Jr. By 2011, more champions were identified such as Isidro Ungab and Emilio Abaya. And in August 2011, sin tax reforms were listed among the administration’s priority measures during the Legislative-Executive Development Advisory Council (LEDAC) meeting. With this impetus, tobacco control advocates began working even more closely with the DOF and DOH, as they were requested by the President to ensure the passage of the reform bill.

Obstacles in Passing RA 10351

There were major obstacles at the Lower House during the law development process. At the start of Pres. Aquino’s term, there was a “no new taxes policy”, but the Finance Secretary convinced him that a restructuring of tobacco tax can be potential sources of funds for his programs, such as the kalusuganang pangkalahatan (universal health care). At that time, the former chairman of the Committee on Ways and Means, Herminio Mandanas, was not supportive of tax reforms, so pro-sin tax groups were able to replace him with Isidro Ungab of Davao, who was able to rally for tax reforms. And since the sin tax reform measure did not have the majority support for its approval at that time, the DOF conceded to the amendments proposed by legislators aligned to the alcohol industry. There were also delays and threats to water-down the tobacco tax bill especially when pro-tobacco legislators expressed opposition. The process was shortened because the Lower House used its political clout and rejected outright the amendments sought to be introduced by pro-tobacco legislators.

Another common tobacco industry tactic was to use tobacco farmers as their front group. With the creation of the Philippine Tobacco Growers’ Association (PTGA), tobacco companies had a new group to represent its interests and providing them stability to exist and thrive, to the detriment of public health. It is also worth noting that Sen. Drilon’s first wife was a smoker, who died of lung cancer. Immediately after the SONA in 2012, more important, several political opportunities opened up for reforming the tobacco tax system at the Lower House. First, a majority of the elected members of the Lower House were new or first-termers, who have not yet interacted with the tobacco industry and are receptive to reforms that can impress and win their constituents’ support and votes in the next elections; second, the change of leadership in the Ways and Means Committee of the Lower House towards the end of 2011 provided a friendly approach; third, the champions of sin tax reform were senior members of the Lower House and very influential because they belonged to the same political party as the President who had leadership in strategic committees in Congress.

After the tobacco tax bill’s approval by the Lower House Ways and Means Committee, the President certified it as urgent to dispense with the requirement of having the bill read three times on separate days at the Plenary session. After its passage by the Lower House plenary by a 210-21 vote, the President asked the Senate to act on the bill immediately in his 2012 State of the Nation Address (SONA) and again certified it as urgent to fast track its approval at the Senate plenary.

At the Senate, the champions were Senators Miriam Defensor-Santiago, Pia Cayetano and Franklin Drilon. Two of these champions held strategic positions: Sen. Defensor-Santiago as Chairwoman of the Foreign Relations Committee is handling all matters relating to international agreements and obligations, among others; and Sen. Cayetano as Chair of the Health and Demography Committee is concerned with all public health matters. It is also worth noting that Sen. Drilon’s first wife was a smoker, who died of lung cancer. Immediately after the SONA in 2012, the Senator favors the tobacco industry and has been instrumental in promoting and advancing its interests in the Senate. The Senate, however, passed the law on October 30, 2012, despite the tobacco industry’s efforts to delay its passage. The law was signed by President Aquino on November 1, 2012, and was known as Republic Act 10351 or the Sin Tax Reform Act of 2012.
the Senate started deliberating on the tobacco tax bill approved by the House of Representatives. Other senators supportive of the measure were Panfilo Lacson, who unsuccessfully pushed for major reforms in 2004, and Sergio Osmeña III.

Senate President Juan Ponce Enrile, a known industry supporter, warned that the Senate’s discussion of the bill was expected to be “bloody”. Tobacco control advocates, civil society organizations, professional medical societies, academe, the World Health Organization, and the World Bank rallied their forces in securing support for the passage of the bill. In particular, HealthJustice conducted several briefings with and supplied various technical briefers to the Senators, whether identified allies or not. In addition, Dr. Prakit Wathesatongkij, a former Thai senator and internationally renowned tobacco control expert, flew in to meet with the Senators, as well as with key officials from the DOH, DOF and PhilHealth. Dr. Prakit relayed Thailand’s experience in increasing excise taxes, and noted that arguments about tax increases leading to lower tobacco sales would cause revenue declines and job losses.

Several opportunities at the Senate made it possible for the law to be passed within 2012. The sin tax bill’s certification as urgent compelled the Senate to prioritize its discussion, the resignation several weeks later of Sen. Ralph Recto as chairman of the Senate’s Ways and Means Committee following vilification in mass and social media for rendering a committee report resembling Philip Morris’ proposal paved the way for Sen. Drilon, an ally, to replace him; and lastly, champions of the bill were senior members of the Senate, while some were politically aligned with the President.

Achievement of Tax Reforms for Public Health

Republic Act 10351

After the two houses of Congress approved their respective versions: House Bill 5727 and Senate Bill 3299, a Bicameral Conference Committee meeting was convened to agree on the final version of the bill to be presented to the President.

There was a risk that differences between HB 5727 and SB 3299 were not the only changes that could have been effected in the Bicameral Conference Committee’s version; fortunately, the following features were retained in RA 10351 (see also the inset on strengths and weaknesses of the final version of the law):

• Removal of the price classification freeze
• Two-tiered structure for the first four years and unitary on the fifth year onwards
• Subsequent yearly increase in tax rates after the fifth year of implementation
• Earmarking of revenues for tobacco farmers’ alternative livelihoods
• Earmarking of revenues for health: universal health care, attainment of millennium development goals (MDGs), health awareness programs, medical assistance and health facilities enhancement

The Implementing Rules and Regulations for tax administration under RA 10351 were issued on 21 December 2012. The tax law took effect on 1 January 2013. As the country is beginning to implement RA 10351, several measures must be taken to ensure that the health and revenue objectives are attained and the tobacco industry’s subversive tactics are countered.

Tobacco industry actions to undermine the revenue and health objectives as a response to the tax increase should be monitored to effectively counter them. The Bureau of Customs (BOC) should strengthen and more strictly implement policies on cigarette smuggling, noting with interest the clear evidence of smuggling being fuelled by tobacco companies. In line with this, the Bureau of Internal Revenue (BIR) has taken the first steps into adopting a tax stamp technology that can help prevent tax evasion and enable both BIR and BOC to track and trace tobacco products.

Even with the passage of RA 10351, the tobacco industry through PTGA came up with a campaign to vote against the Senators who approved the law. A dedicated website: http://senator1000.com/ was put up for this purpose, and a Facebook page called “Boycott the 100% Tax Hike Club” was created. There is, therefore, a need to continually counter tobacco industry front groups and expose their relationship with the tobacco industry.

Civil society participation and support was instrumental in the tobacco tax reform by utilizing media advocacy and simplifying the technical points, and ensuring that the public understood the issues. This led to the building of a critical mass base for supporting the efforts of tobacco control advocates and pushing for the passage of the tobacco tax law.

Strengths

1. The unitary system of taxation will help in reducing the number of smokers as it removes the incentive to downshift to cheaper, lower-taxed products, while at the same time increasing the government revenues.
2. The four percent (4%) annual increase beginning on the sixth year may be inflexible but ensures that there will be subsequent increases that will help reduce affordability by reducing the effects of inflation and income growth.
3. The law also allocates 15% of the incremental revenues on programs for tobacco farmers’ alternative livelihoods, which is consistent with Articles 17 and 18 of the WHO FCTC.
4. While the law allows cigarette packs to contain less than 20 sticks (“kiddie packs” intended to increase accessibility and affordability), a pack of 5s or 10s will have the same tax rate as a pack of 20s, thereby discouraging the tobacco industry from manufacturing such kiddie packs.

Weaknesses

1. The requirement that manufacturers and sellers must procure 15% of their raw tobacco leaves from locally grown sources encourages tobacco planting. This undermines the recommendations under the WHO FCTC and the objective of earmarking tax revenues for alternative livelihood programs for tobacco farmers.
2. Although some revenues are earmarked for health, there are no funds specifically dedicated for health promotion, which represents a lost opportunity to secure sustainable funding for tobacco control and other health promotion programs that empower the Filipino people to improve their own health.
3. The allocation of an unspecified amount of financial support for displaced tobacco manufacturing workers acknowledges the unproven assumption that tax increases result in massive unemployment, particularly when the entire tobacco industry’s employee population represents less than one percent (1%) of the country’s employed workforce, including farmers. This provision also requires the government to give special treatment to the tobacco industry and subsidizes its expenses for its displaced workers, a privilege not given to other industries.
Tobacco Package Health Warnings in ASEAN

Health warnings on tobacco packages are among the most effective and cost-effective tobacco control measures for communicating and increasing awareness among smokers and the public of the harmful effects of smoking and exposure to secondhand smoke. Committed to implement strong tobacco control policies, Parties to the WHO FCTC are obliged to adopt effective health warnings and to prohibit the use of misleading terms, descriptors or trademarks (such as “light” and “mild”) within three years of their ratification of the treaty (Article 11).

In November 2008, at its third session, the Conference of Parties (COP3) adopted the FCTC Article 11 Guidelines, based on international best practices and scientific evidence, to assist Parties meet this obligation to develop effective packaging and labeling requirements, recommending they implement large and prominent pictorial health warnings (PHWs) on tobacco packages.

As part of a growing worldwide trend, at least 63 countries/jurisdictions, including six in ASEAN, currently mandate PHWs. To further enhance the effectiveness of PHWs and eliminate all product advertising including brand colors, logos and design elements on packages, Australia became the first country to successfully implement plain packaging that requires tobacco packages to come in a standardized shape, color and format, effective by 1 December 2012. New Zealand has also recently announced that it will pursue plain packaging, and several other countries (e.g. UK, Canada, Turkey and India) are also considering it. In addition, at least 73 countries including Brunei Darussalam, Malaysia, Singapore, Thailand and Vietnam have banned the use of false, deceptive, and misleading terms such as “light” and “mild” on cigarette packages.

Singapore was the first ASEAN country (2004) to implement six rotating PHWs covering 50% of the upper front and back of tobacco packages with accompanying English language health messages and a Quitline number. A second set of six rotating PHWs was introduced in 2006, and a third set of PHWs will be implemented in 2013. The amendments to the Tobacco (Control of Advertisements and Sale) Act (effective 1 March 2013) ban the use of false and misleading terms, and applies to all trademarks, including prohibiting these terms as part of tobacco brand names.

In 2005, Thailand also began requiring six rotating PHWs covering 50% of the upper front and back of the cigarette pack with Thai language text health messages. A second set of nine rotating PHWs was introduced in 2006, and a third set of PHWs will be implemented in 2013. The amendments to the Tobacco Harms (June 2012) requires six rotating PHWs covering the upper 50% of the front and back of the pack in 2008. The health messages are printed in both Malay and English language on the package. The amendments to the Tobacco (Labeling) Regulations (effective 1 September 2012) introduced the second set of seven rotating PHWs and increased their size to 75%, the current largest in the region.

Malaysia also mandated six PHWs beginning January 2009 under the Control of Tobacco Products Regulations (Amendment 2008). It requires PHWs covering the upper 40% of the front and back of the packs with accompanying English language health messages. A Quitline number is also printed on the pack. Additionally, a ban on the sale of kiddie packs (less than 20 cigarette sticks per pack) became effective in 2010.

Vietnam’s new Law on Prevention and Control of Tobacco Harms (June 2012) requires six rotating PHWs occupying 50% of the upper front and back of tobacco packages with accompanying Vietnamese language health messages. This will come into force by 1 May 2013 with full implementation by 1 November 2013.

Indonesia is the most recent ASEAN member state to require PHWs, having recently passed a new Government Regulation No. 109/2012 (Restraining Addictive Substance of Tobacco Product for Health) to replace the existing small and ineffective textual warning. Five rotating PHWs covering the upper 40% of the front and back of cigarette packages will be implemented by 1 July 2014.

The remaining ASEAN member states (Cambodia, Lao PDR, Myanmar and Philippines) carry text-only warnings, although legislation has been proposed in some countries to also implement PHWs.
Indonesia Takes Steps in Tobacco Control: An Account of Introducing Pictorial Health Warnings

By Dr. Widyastuti Soerojo, SITT Indonesia Packs Coordinator, and Ms. Tan Yen Lian, SEATCA Knowledge and Information Manager

Close to 65 million Indonesian smokers will finally be informed about the health risks of smoking. The Indonesian Government will implement pictorial health warnings (PHWs) in 2014 after enacting on 24 December 2012 a landmark Government Regulation (Peraturan Pemerintah or PP) No. 109/2012 “Restraining Addictive Substance of Tobacco Product for Health”. With the fourth highest tobacco consumption rate in the world (over 250 billion sticks in 2010), this step is timely for protecting the well-being of all Indonesians, despite the country not yet having acceded to the WHO FCTC.

While the government has shown leadership in the implementation of the PP, part of the success can be attributed to a supportive relationship between the Ministry of Health (MOH) and civil society, including a regional partner, SEATCA. The relationship between civil society and SEATCA began over six years ago when SEATCA held its first training workshop to build tobacco control capacity in local NGOs. A cross-sectoral working team on pack warnings (called ‘Pack’ team) was established after another SEATCA regional workshop on “Advancing Pictorial Health Warnings” in Hanoi, Vietnam in 2006.

In 2007, the Indonesian Tobacco Control Network (ITCN) was formed as an extension of the Tobacco Control Working Group with the support of the Bloomberg Initiative to Reduce Tobacco Use. At this time SEATCA assisted in the production of local policy-driven research: a health warnings study conducted between 2005 and 2007, which showed that the majority of the public preferred pictorial warnings and supported 50%-size health warnings on cigarette packages. The research provided important local evidence that was used to propose an amendment of the previous Government Regulation (PP No. 19/2003) on textual health warnings.

In October 2009, the new Health Law No. 36/2009 was passed and required not only PHWs but also the expansion of smoke-free areas and the listing of tobacco as an addictive substance. Soon after, under its new BMGF-funded Southeast Asia Initiative on Tobacco Tax (SITT), SEATCA began its partnership with the University of Indonesia (UI) to focus on two issues: tobacco tax reform and PHWs on packs. The SITT pack component, implemented in partnership with the UI Faculty of Public Health, and MOH’s compliance with Health Law No. 36/2009 commenced simultaneously.

A Collaborative Approach to Implementation

Early 2010 to June 2011

Health Law No. 36/2009 as stipulated in Article 116, set the legal basis for drafting of the Government Regulation on “Restraining Addictive Substance of Tobacco Product for Health”. An inter-ministerial taskforce comprising of representatives from 18 ministries was formed at government level under coordination of MOH to discuss the technical aspects of the draft Government Regulation (RPP). At the same time, a technical working group (TWG) focusing on the pack component was set up with 15 members from the UI Public Health Faculty, relevant units at MOH, NGOs (e.g. Tobacco Control Support Center (TCSC), Indonesian Consumers Organization (YLKI), Jakarta Residents Forum (FAKTA), Center for Research and Information Services (P3DI)), WHO, along with the SITT Indonesia Pack and Tax Coordinators. The TWG was responsible for providing information and advice to the inter-ministerial taskforce through the MOH representatives.

The SITT Indonesia Pack team collaborated with MOH technical staff by providing relevant local, regional and international evidence that would assist MOH’s policy development. Ongoing technical assistance to the MOH was also provided during a series of RPP-specific public consultation and inter-ministerial meetings coordinated by the MOH through 2010 and 2011 to finalize the technical contents of the RPP before its submission to the Ministry of Law and Human Rights for legal harmonization to ensure consistency of law, regulations and best practices.

The government conducted meetings with various stakeholders, including tobacco control advocates and the tobacco industry (TI), and enabled the SITT Indonesia team to provide: 1) answers to technical questions raised during the discussions and in impromptu meetings of the government with the TI and its allies (e.g. Indonesian Tobacco Alliance (Aliansi Masyarakat Tembakau Indonesia-AMTI), Smokers Club, Tobacco Farmers Association, Kretek Industry Business Association and White Cigarettes Business Association); 2) samples of cigarette packages with pictorial health warnings exported from Indonesia to other countries; and 3) informal responses to issues raised by representatives of Economic Ministries (Ministry of Finance, Ministry of Industry and Ministry of Trade) during the technical inter-ministerial meetings.

Implementation Challenges

June 2010 to September 2011

The RPP faced a number of obstacles to its introduction. Significant challenges came from the Ministry of Trade (MOT), which objected to any implementation of PHWs, and the Ministry of Industry (MOI), which requested that the size of PHWs be decreased from 50% to 30%.

The objections were addressed by two counter-arguments: 1. It was highlighted that tobacco companies were already exporting cigarette packages with PHW sizes of 50% and 75%, in compliance with the PHW regulations of Singapore, Malaysia and Brunei Darussalam, respectively. SEATCA’s PHW image bank provided samples of cigarette packs from these countries to illustrate the point. 2. It was further suggested that the Indonesian government’s position would be perceived as not only setting double standards but also hiding the real reason for downsizing the PHWs, which was to dilute their effect on smokers and others.

September 2011 to June 2012

On 26 September 2011, the SITT Pack and Tax Coordinators joined an audience with Indonesia’s President Susilo Bambang Yudhoyono along with the National Commission on Tobacco Control (NCTC) to discuss tobacco control issues in general. The President indicated his awareness of the FCTC and WHO policy on tobacco control measures and stressed a step-wise implementation approach for Indonesia. The inter-ministerial disagreement on PHW size between 50% and 30% was also discussed and resulted in the President’s decision of 40% size of PHWs, which was also accepted by the MOT.

Five weeks after the audience with the President (1 November 2011), in response to a judicial review filed by the Alliance on Protection of the Guarantee and Protection of Every Person’s Right to Obtain Information as stipulated in Article 28F Law 1945 (page 122),” the Constitutional Court issued its verdict on Health Warning and Elucidation, which further strengthened the tobacco control advocates position, stating that:

“Article 114 of Law 36/2009 and its Elucidation must be of the meaning that it is the duty of cigarette manufacturers and importers to insert warnings in the form of clear text and pictures [emphasis added]. This is related to the guarantee and protection of every person’s right to obtain information as stipulated in Article 28F Law 1945 (page 122).”

While waiting for an opportunity for the MOT to present the draft RPP to the Limited Cabinet Meeting (an additional pre-requisite to the normal legislative process), the RPP was further delayed by another request by the Coordinating Minister of People’s Welfare for approval from two Coordinating Ministries – Economics and Social Welfare; however, between January and April 2012, all nine appointments made with the two Coordinating Ministries were canceled at the last minute.

On 19 April 2012 the draft RPP was finally approved by all required parties and proposed the following: 1) 40% PHW coverage on cigarette packages with an
On 24 December 2012, the Indonesian Government Regulation (PP) No. 109/2012 on Restraining Addictive Substance of Tobacco Product for Health, which was officially announced on 8 January 2013. The PP requires the inclusion of five proven PHWs to be printed on the upper 40% of the front and back or the principal surfaces of all cigarette packages. It will replace existing tobacco warnings regulated under PP No. 19/2003.

Challenges Ahead

While the passing of PP No. 109/2012 signified a triumph for tobacco control advocates in Indonesia, the region, and the world, an end to the interference from the tobacco industry is not in sight. Already, the industry is stating that the transition period of 18 months is too short and requesting that MOH set a longer period for the full implementation of PHWs, which is a common delaying tactic that has been used by the industry in other countries that have implemented PHWs. Small-scale tobacco companies also expressed concerns on higher production costs for printing colored images of PHWs.

Currently, the SITT Indonesia Pack team, with technical assistance from SEATCA, is seeking copyright-free use of five images from Thailand to facilitate implementation. In addition, technical guidelines on PHW implementation from neighboring countries (Malaysia and Vietnam) provide a good reference for developing the Indonesian Ministerial Decree on PHWs implementation.

The case study shows the time and persistence required for achieving policy changes and the full implementation of new tobacco control regulations. An effective working relationship between government and civil society was a crucial element for progress in developing PHW regulations for Indonesia. The full implementation of PHWs by July 2014 is also likely to benefit from continued regional and national collaboration.
Tobacco Taxes in ASEAN


Southeast Asia Tobacco Control Alliance. ASEM Tobacco Tax Report

Reforming Tobacco Tax Policy through Research in Indonesia

Earnings and Affordability of Tobacco Taxation in Indonesia. (2010)

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Reforming Tobacco Tax Policy through Research in Indonesia


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Since its formation in 2001, SEATCA has nurtured partnerships and worked collectively with various government organizations (GOs), non-governmental organizations (NGOs), universities and the World Health Organization in ASEAN countries to curb the tobacco epidemic in Southeast Asia.

Our SITT country partners are:

**Cambodia:** World Health Organization and General Department of Taxation, Ministry of Finance. SITT Country team: Dr. Yel, Daravuth as SITT Cambodia Coordinator, and Ms. Yoeu Phallin, SITT Project Officer

**Indonesia:** Faculty of Public Health and Demographic Institute, University of Indonesia. SITT Country teams: Dr. Widyastuti Soerojo, SITT Indonesia Coordinator and Ms. Sri Mufti, SITT Indonesia Assistant Coordinator, for Packs; and Mr. Abdillah Ahsan, SITT Indonesia Coordinator, Ms. Ayke Soraya Kiting, SITT Indonesia Assistant Coordinator, Ms. Flora Aninditya, SITT Indonesia Project Staff, for Tax

**Lao PDR:** Tobacco Control Taskforce, Ministry of Health and Department of Tax, Ministry of Finance. SITT Country team: Dr. Maniphanh Vongphosy, SITT Lao Coordinator, and Dr. Bounlhorn Ketsouvannasane, SITT Technical Adviser

**Philippines:** HealthJustice. SITT Country team: Atty. Irene Patricia Reyes, SITT Philippine Coordinator, Atty. Dianne Lim, SITT Research Manager, and Mr. Ralph Emerson Degollacion, SITT Project Coordinator

**Vietnam:** HealthBridge, Department of Tax Policy, Ministry of Finance, and VINACOSH. SITT Country team: Dr. Pham Thi Hoang Anh, SITT Vietnam Coordinator, Ms. Le Thi Thu, SITT Project Manager, and Dr. Nguyen Tuan Lam, SITT Technical Adviser

Working closely with country partners, the SITT regional team takes the lead in the overall project management and provides continuing capacity building and technical assistance to in-country activities. These include support for policy-relevant studies and framing evidence for policy development and advocacy. The regional team is also at the forefront to promote the project’s visibility and has continuously explored opportunities for institutional linkages with potentials partners, keeping in mind the needs of country partners and emerging issues that are expected to impact the initiative.
VISION
Towards a healthy, tobacco-free ASEAN

MISSION
Working together to save lives by accelerating effective implementation of the FCTC in ASEAN

SEATCA
Southeast Asia Tobacco Control Alliance
Thakolsuk Place, Room 2B, 115 Thoddamri Road, Dusit, Bangkok 10300 Thailand
Telefax: +66 2 241 0082 | Email: info@seatca.org
www.seatca.org

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