



PHILIP MORRIS

ASIA LIMITED

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Honorable Andrew Cheng Kar-foo

Chairman

Bills Committee on Smoking (Public Health) (Amendment) Bill 2005

Room 303, Oi Wo House

Tai Wo Estate

Tai Po

New Territories

Dear Mr. Cheng:

Further to our letter to you dated August 5, in which we request our participation in the Bills Committee's public consultation on the Smoking (Public Health) (Amendment) Bill 2005, we respectfully submit this letter to provide a summary of our views on the key regulatory issues which are under consideration in the Amendment Bill or which we believe could further advance the objectives of the Amendment Bill.

During our recent meetings with the various members of the Bills Committee, we discussed a range of issues on which we were invited to submit our views (please see the attached position paper which was submitted to the Health Welfare & Food Bureau in November 2004). This letter reiterates our support for comprehensive regulation and focuses on three points where we wish to further discuss with the Bills Committee during the public consultation session on October 6, 2005. These points are: (1) health warnings, (2) descriptors, and (3) youth smoking prevention.

1. Health Warnings: We believe that all cigarette packages should contain a clear and conspicuous health warning and we defer to the Government on the content of the warnings, whether text and/or graphic health warnings. Warnings should make clear the health effects of smoking, while allowing us sufficient space to continue to communicate to the adult smokers who choose to continue to smoke. If the Bills Committee is considering graphic health warnings, we suggest considering overseas experience, including Brazil and Australia. Both countries have strict tobacco control laws, including graphic health warnings, but also allow manufacturers sufficient space to communicate our brands.
2. Descriptors: Rather than banning the use of certain words on packs, such as "lights", "mild", or "ultra light" which adult smokers use to differentiate taste and flavour of cigarette brands, we would support regulations requiring all manufacturers to provide consumers with additional information about the health risks of smoking, emphasizing that there is no safe cigarette, and tell consumers they should not assume that lower tar cigarettes are safer or less harmful for them. Since 2003, we have voluntarily provided this type of additional health information on product packaging and/or in advertisements in a number of countries in Europe, Latin America and Asia. This initiative was launched in Hong Kong in November 2004. We also suggest the Bills Committee to consider overseas experience on this issue, including Japan and Mexico, both countries require cigarette manufacturers to print additional information on packs reminding adult smokers

that there is no safe cigarettes or that they should not assume that “lights” or “mild” cigarettes are safer.

3. Youth Smoking Prevention: We do not want children to smoke, and we support regulations and strict enforcement thereof aimed at preventing youth from smoking. We support clear designation of a specific government entity such as the Tobacco Control Office to carry out enforcement of the minimum age regulation. We would also support the introduction of a licensing system for retailers so as to address the issue of youth having access to cigarettes.

As stated in our recent discussions with the various parties and our previous submissions, we support the decision of the Hong Kong SAR Government to supplement the Smoking (Public Health) Ordinance and, in fact, we support many of the provisions of the Amendment Bill. We only ask that the Government do so in a way that allows us to exercise our fundamental rights to do business in Hong Kong.

Very truly yours,

Tammy Chan
General Manager

c.c. Miss Maggie Chiu, Clerk to Bills Committee, Legislative Council Secretariat

Philip Morris Asia Limited's Views on the Amendment of the Smoking (Public Health) Ordinance (Cap 371)

The purpose of this document is to provide the views of Philip Morris Asia Limited ("PMAL"), an affiliate of Philip Morris International, on the amendment of the Smoking (Public Health) Ordinance (Cap 371) ("Smoking Ordinance"). Since we last expressed our views on the Smoking Ordinance in 2001, Member States of the World Health Organisation have since adopted the Framework Convention on Tobacco Control ("FCTC"), which calls on Member States to adopt broad national tobacco regulation. We are aware, as well, that there is a strong demand for tighter tobacco control legislation in Hong Kong. We therefore would also like to take this opportunity to provide suggestions for further regulation of tobacco products in Hong Kong.

Introduction

Before we present our views on the amendment of the Smoking Ordinance and detailed recommendations for comprehensive tobacco regulation, it is important to make clear our position on smoking and health and why we support strong and effective regulation of the tobacco industry and its products.

Comprehensive tobacco regulation coupled with effective enforcement can achieve important public health goals. Smoking is addictive and causes serious diseases, including lung cancer, heart disease and emphysema. Further, smokers are far more likely to develop serious diseases, like lung cancer, than non-smokers and there is no "safe" cigarette. Regulation can ensure that consumers continue to be informed about these health effects. It can also help prevent minors from having access to tobacco products. Regulation can also help reduce the prevalence of tobacco use which we agree is an appropriate public health objective.

The World Health Organization (WHO) has acknowledged that, even if it is extremely successful in all that it is doing to stop people from smoking, there will be as many adult smokers in 50 years as there are today. There is thus an obvious and legitimate need for tobacco companies, governments and tobacco-control advocates to work together to find solutions to the harm caused by smoking. Comprehensive product regulations can and should play an important role in reducing the harm of smoking for those adults who continue to smoke, and for society as a whole.

In considering a comprehensive legislative framework for tobacco regulation, a number of important points should be considered.

First, regulations must establish clear rules which are applied consistently to all participants in the tobacco business. The regulatory framework we propose could be facilitated through the adoption of a comprehensive licensing program covering each participant in the industry, including manufacturers, importers, exporters, wholesalers, distributors and retailers. Each participant would be required to register with the

Government in order to obtain a license, which would be withdrawn if they do not comply with specific rules regarding their category of business. By creating a limited and controlled network the Government will be able to better prevent the sale of tobacco products to minors, more effectively combat illicit trade in counterfeit and smuggled cigarettes and verify that only legitimate operators are involved in the tobacco business. A nominal licensing fee could also provide additional funding to cover the costs of regulation and enforcement.

Second, any tobacco regulation being enacted today should be able to take into account possible future developments. Philip Morris International is devoting a substantial amount of effort and resources to develop tobacco products which may have the potential to reduce the risks associated with smoking. We firmly believe that if such products can be developed, they should be made available to adult smokers. We also believe that governments have an important role to play both in regulating these products and determining what claims can be made about them.

Finally, achieving comprehensive regulation of tobacco will require the work of many branches of the Government. PMAL is committed to working with the Department of Health, Food and Welfare Bureau, the Department of Financial Services and the Treasury, the Customs and Excise Department and other governmental departments, the Executive Council and the Legislative Council in order to achieve tobacco regulation. We would also be pleased to meet with all appropriate stakeholders – other manufacturers, retailers, vendors and non-governmental organizations - to discuss our recommendations and to provide further information regarding tobacco regulation.

Detailed Comments

1. Amendment of the Smoking Ordinance

A. Health Warnings

We believe all smoking related decisions should be based on a consistent public health message. Everyone must be informed of the risks of smoking. We believe therefore that all cigarette packages should contain a clear and conspicuous health warning in the principle language or languages of each country. Warnings should be rotating, clear and visible.

We defer to the Government on the content of the warnings. Some public health authorities believe that graphic health warnings more effectively communicate the health effects of smoking than textual warnings. Our views on graphic health warnings are the same as our views on text-only warnings: warnings should make clear the health effects of smoking, and in order to do so, it is not necessary for those warnings to dominate the package. Consumers should be able to easily distinguish one brand from another, and we should be able to clearly display our valuable trademarks and logos.

We believe that the current requirement in Hong Kong of a 28% front and back health warning (black text on a white background with a black border) provides a clear and

legible warning for consumers and permits us sufficient space to display our trademarks.

Any new legislation on health warnings should provide manufacturers with sufficient time to re-design packaging to accommodate new warnings. For example, any new legislation should require that packaging with the new warnings be introduced at least 12 months after the legislation has been published. In order to clear existing stocks, any packaging which is not compliant with the new legislation should be allowed to remain on sale at retail establishments for a further 6 months.

B. Advertising Restrictions

As in 2001, we understand that the Government is considering revocation of the current exemption for the display of tobacco advertisements at licensed hawker stalls and retail outlets that employ not more than two employees.

Tobacco products should be marketed in a responsible way and we therefore support restrictions on tobacco marketing and advertising, including bans on certain types of advertising, to decrease the chances that children will see them.

We do not oppose further restrictions on the display of point of sale advertisements at small licensed hawker stalls and retail outlets. For example, the amended Smoking Ordinance could establish limits on the size and location of such advertisements.

We believe that *some* communication with adult smokers should continue to be permitted, though. Specifically, we believe the following proposals should be implemented either to expand on or amend the existing Smoking Ordinance, or introduce new requirements as follows:

1. Tobacco advertising and promotional activities should be permitted at venues restricted to adults 18 years or older provided that access to such venues is controlled through checks on proof of age.
2. One-to-one communications to adult consumers should be permitted, including information mailed and emailed directly to an adult smoker, with appropriate age verification protocols and measures to limit access to adult smokers.
3. The sponsorship of any social, charitable or cultural event in the name of a company which manufactures tobacco products should be permitted, as long as the company name is used in a manner clearly distinct from any names used for tobacco products, and does not include any logos or other distinguishing marks used for tobacco products.

Of course, tobacco advertising should carry a health warning.

In summary, some basic communication with adult smokers should be permitted so that adult smokers can still have basic information about tobacco products. In this way, competition and product innovation in the industry can be preserved and fostered. This

is especially true in Hong Kong where most other means of advertising are prohibited and where one of the basic principles of the Hong Kong legal system is that consumers have a right to receive accurate information about products so that they can make informed choices.

We are, of course, not the only stakeholder in this issue; we urge the Government to seek input from all others, including the operators of the small retail outlets that are currently allowed to advertise tobacco products.

C. Public Smoking Restrictions

Public health officials have concluded that secondhand smoke from cigarettes causes disease, including heart disease and lung cancer, in non-smoking adults, as well as conditions in children such as asthma, respiratory infections, cough and wheeze. We believe the public should be guided by the conclusions of public health officials regarding the health effects of secondhand smoke and that based on these conclusions, governments should regulate smoking in public places.

Consideration of public smoking restrictions should include many factors, including: (1) the conclusions of public health officials that exposure to secondhand smoke causes disease, (2) the principle that the public should be able to choose whether or not to be in places where smoking is permitted, (3) the type of venue (office, restaurant, bar, public transportation), (4) the ability of business owners – particularly in the hospitality sector – to retain some flexibility to determine the smoking policy for their establishment, and (5) the fact that a sizable proportion of adults in virtually every country in the world are smokers.

In general, people should be able to avoid being around secondhand smoke in places where they must go, such as public transportation, educational facilities and health care facilities. Accordingly, we support regulation on public smoking provided in the Smoking Ordinance which bans smoking on public transportation, health care facilities, cinemas, indoor areas in shopping malls, supermarkets or banks. We also support the proposal to extend this prohibition to include all indoor and outdoor areas of primary and secondary educational institutions, and all *indoor* areas of post-secondary / tertiary educational institutions.

At the same time, we believe that the Government should recognize that some business owners and their patrons wish to permit smoking in certain locations. Regulation should provide business owners with the choice to permit or prohibit smoking, and to decide how best to address the preferences of non-smokers and smokers. We suggest that all stakeholders be consulted and that the best way going forward is to ensure the power to choose is maintained for all parties, be they business owners, patrons, smokers and non-smokers. For example, we believe that many bar and nightclub owners and their employees and customers (both smokers and non-smokers) expect to find comfortable public places to smoke in those venues. We would suggest that before acting on this topic, the Government consider surveying bar and nightclub owners, their employees and their patrons, and to consider their suggestions for workable public smoking policies.

Public smoking regulation should also clearly define and distinguish each type of venue (i.e. office, workplace, bar, restaurant) where smoking is banned or permitted. The Government may even consider restricting smoking to facilities that receive a government licence permitting smoking only where certain criteria are met.

Where smoking is permitted, we support regulation that requires business owners to clearly mark those areas where smoking is permitted and to post a warning sign stating the public health community's conclusion that secondhand smoke causes diseases in non-smokers.

D. Descriptors

There has been increasing focus of discussion recently in Hong Kong on the use of "descriptors" such as "light", "mild", or "ultra light" on cigarette packaging. We use those terms to describe the strength of taste and flavour of cigarette brands. Given the questions that have arisen about the machine test methodology and "light" cigarettes, there is concern that consumers perceive "light" cigarettes as being less harmful or as an alternative to quit smoking. That concern can be addressed in ways other than banning the use of certain words on packs.

Simply banning words that adult smokers have been familiar with for many years, with no explanation about the underlying facts, is not likely to help consumers better understand the meaning of those terms. Rather, we would support regulations requiring all manufacturers to provide consumers with additional information about the health risks of smoking, emphasizing that there is no safe cigarette, and tell consumers they should not assume that lower tar cigarettes are safer or less harmful for them.

For example, manufacturers could be required to develop a comprehensive communication campaign, providing a series of additional statements or information on product packaging or in advertisements, these statements could advise smokers that: (1) no cigarette (including low tar cigarettes) has been scientifically established to be safer than any other, (2) low tar cigarettes are not a suitable alternative to quitting, (3) smokers may change the way they smoke when switching to a low tar cigarette and, as a result, may take in as much tar and nicotine as they would with a full flavoured cigarette, and (4) any tar and nicotine measurement does not measure how much tar and nicotine is actually inhaled by the smoker. Starting in 2003, Philip Morris International has begun to provide additional health information on product packaging and/or in advertisements in a number of countries in Europe, Latin America and Asia Pacific, and will soon be implementing this communication initiative in Hong Kong. We would support regulations requiring further communications, in the media or on packs, to address concerns about consumer perceptions of lower tar and nicotine cigarettes. We would be happy to provide the Government with specific recommendations in this regard.

2. Comprehensive Product Regulation

Cigarette smoking causes fatal diseases and is addictive. Governments and the public health community should continue to take measures to discourage adults from smoking and to seek ways to help make cigarettes less harmful, and most certainly should do everything possible to prevent kids from gaining access to cigarettes. We support further legislative or regulatory requirements to continue progress on these objectives. Given that a number of adults will continue to smoke for the foreseeable future, though, we believe that comprehensive product regulations should also play a part in the Government's harm reduction strategies. Regulations should identify areas for further scientific inquiry and understanding. Regulations should encourage manufacturers to develop and responsibly market products that reduce individuals' exposure to harmful smoke constituents and that may ultimately reduce societal harm. And regulations should allow adults who choose *not* to quit to receive information about the availability and attributes of products that have the potential to reduce exposure to harmful smoke compounds, ideally with prior regulatory approval of both the products and the communications about them.

A. Ingredients Information

The World Health Organization's Scientific Advisory Committee on Tobacco Product Regulation suggested that ingredient disclosure requirements are "[t]he first logical step" in developing a coherent regulatory framework for tobacco products.¹ Philip Morris International supports regulations that would require manufacturers to provide the Government with comprehensive information about the ingredients used to make cigarettes, including the maximum quantities at which these ingredients would be used. At the same time, precise brand recipes are valuable trade secrets, and the format for providing the information should protect these trade secrets.

Philip Morris International uses a three-list format to provide EU Member States and several governments in the Asia Pacific region with the information about all the ingredients used in our products available on their markets, including the maximum quantity of each ingredient used. The three-list format provides regulators with the information they need to assess our use of ingredients while protecting our brand recipes. Ingredient information in that format can be made public without jeopardizing proprietary information. We would recommend the same approach be taken in Hong Kong. In addition, we support sharing ingredient information with the public, so long as proprietary information is adequately protected. The information Philip Morris International provides to governments using the three-list format is published on its website.²

¹ World Health Organization, Scientific Advisory Committee on Tobacco Product Regulation, *Statement of Principles Guiding the Evaluation of New or Modified Tobacco Products*, November 2002 at 6.

² http://www.philipmorrisinternational.com/pages/eng/smoking/Cig_ingredients.asp (English)
http://www.philipmorrisinternational.com/pages/zho/smoking/Cig_ingredients.asp (Chinese)

B. Ingredient Toxicology Data

In addition to knowing the identity of the ingredients used to make cigarettes sold in Hong Kong, the Government should be able to verify that the ingredients used in making cigarettes do not increase the harmful effects or addictive nature of smoking. We would support regulation in Hong Kong requiring manufacturers or importers to disclose available toxicological data on the ingredients used to make their cigarettes, so that the Government could assess the appropriateness of the ingredients' use. Philip Morris International has already provided such information to the Member States of the European Union, pursuant to the European Union Product Directive.

Of course, any assessment of ingredients must take into account two facts. First, cigarettes themselves – without ingredients added, including those containing only tobacco and paper – are inherently unsafe. Second, there is no international scientific consensus on how to assess the risk of cigarette ingredients. But neither fact should prevent the Government from acting so long as regulations are based on appropriate scientific principles.

C. Tar, Nicotine and Carbon Monoxide

Although ingredient use is an appropriate topic for regulatory consideration, “[t]he preferred focus for regulation is the emission from the product when it is used as intended...”³ Tobacco smoke, not cigarette ingredients, causes harm. Understanding tobacco smoke and the constituents it comprises is the key to harm reduction. We support regulations requiring manufacturers to provide information on tobacco product emissions to the Government and, as the Government deems appropriate, to consumers.

Tar, nicotine, and carbon monoxide are three commonly-known smoke constituents.⁴ Over the last thirty years, ISO has developed methods for machine-measuring tar, nicotine, and carbon monoxide yields, and many governments, including Hong Kong, specify ISO methods for obtaining quantitative information about cigarette smoke. Those machine-measured numbers may be useful for comparing one cigarette to another, for research purposes, or (as in Hong Kong) for complying with regulatory requirements, and we do not oppose a requirement to disclose ISO-measured tar, nicotine, and carbon monoxide yields with the Government.

But machine-measured numbers have limitations, particularly as a means of communicating with consumers. From the beginning, it was recognised that people do not smoke cigarettes in the same way as machines. ISO methods specify that each machine smokes every cigarette under the exact same conditions and in the exact same way. Different people smoke differently; an individual may smoke different products differently; and an individual may smoke the same cigarette brand differently at one

³ World Health Organization Scientific Advisory Committee on Tobacco Product Regulation, *Recommendation on Tobacco Product Ingredients and Emissions*, November 2002, at 1.

⁴ “Tar” is actually a group of chemicals – the total cigarette smoke particulate residue (minus nicotine and water) as captured on a smoking machine filter pad.

time than at another. A person who smokes more intensely will inhale more tar and nicotine than a person who smokes less intensely. Machine-generated yield numbers therefore do not indicate with precision the amount of tar, nicotine, or carbon monoxide a smoker will actually inhale. As a result, many public health groups have suggested that tar, nicotine and carbon monoxide yields measured using the ISO method should not be communicated with consumers.

The ISO methods can continue to play a role in the regulation of tobacco products, even though they have limitations. Today, ISO machine-based methodologies represent the most widely used standardised measurement system for smoke constituents. They are important tools for researchers and can provide a basis for maintaining a historical perspective that allows one product to be compared to another and for pursuing ways to reduce the harm caused by smoking. For example, one possible way to develop less harmful products is through the removal of certain toxic smoke compounds. The success of this strategy can only be achieved if the “quality” of the tar is changed; that is, if the new product produces less of these toxic components at equal tar delivery compared to a conventional product. This determination has to be based on fully standardised machine smoking methods, such as ISO, to ensure the measurements reflect equal tar deliveries.

The WHO has also called for the continuing use of ISO methodology, at least until new methodology has been developed:

“Although the existing machine-smoking methods employed/adopted by ISO and the Federal Trade Commission do not accurately reflect human smoking behaviour, and consequently do not accurately reflect the delivered dosages of toxic and carcinogenic constituents of smoke, it is recommended that such testing be continued to the extent that it provides a basis for a comparison of the results with new testing protocols until protocols that reflect variations in human smoking behaviour according to different cigarette designs are developed.”⁵

D. Other Smoke Compounds

As with any organic material, thousands of chemicals are formed when tobacco is burned. Nearly 5,000 constituents have been identified in tobacco smoke to date, and public health authorities have classified between 45 and 70 of those as particularly harmful to health.

Brazil, Canada, Australia and the Commonwealth of Massachusetts have required manufacturers to measure and report on about 45 of these smoke constituents, commonly referred to as “the Hoffmann analytes.” Continuing research may demonstrate that certain of the Hoffmann analytes are not linked to smoking-related

⁵ WHO Study Group on Tobacco Product Regulation, Recommendation 6: Guiding Principles for the Development of Tobacco Product Research and Testing Capacity and Proposed Protocols for the Initiation of Tobacco Product Testing, (2003), at 13
http://www.ensp.org/files/SACTob_Rec_6_for_PDF.pdf

diseases and certain compounds not on the list may be identified as quite relevant. Consequently, the list of compounds to be tested should be periodically reviewed.

The testing methodologies should be developed over time as well. Although Health Canada has published methods for measuring 44 Hoffmann analytes, those methods have not been validated and cannot be considered as internationally recognised standards. It will take time to develop such standards. ISO is currently working on standard methods for measuring benzo[a]pyrene and tobacco specific nitrosamines. On average, it takes at least two years to carry out the necessary inter-laboratory testing to develop an ISO standard. If Hong Kong believes it is desirable to develop standardised measurement methods for some or all of the Hoffmann analytes, a coordinated programme should be put in place to expedite that process. We would welcome the opportunity to participate and assist in any such programme.

As a first step, we believe regulations could require manufacturers to submit by-brand data on the levels of some or all Hoffmann analytes, together with information on how the data were generated. (The data each manufacturer submits to the government would not necessarily be comparable because of different measurement methods or other differences.) Unlike the information on tar, nicotine and carbon monoxide yields, it would be very difficult to independently verify these data until standardised methods are developed. We would therefore suggest that the information be submitted once for all brands on the market and only up-dated when new brands are introduced or when there is a significant change to any existing brand. A significant change could be defined as any alteration which results in a change in the reported tar, nicotine or carbon monoxide yields.

E. Other Product Regulation

We would support regulation on a wide variety of other aspects as well – including science-based product performance standards and, ultimately, regulations concerning the development and marketing of products that have the potential to reduce the risk and harm of tobacco use. Developing products that could potentially reduce individual risk and societal harm of smoking is one of Philip Morris International's top priorities. Ideally, regulations should establish whether a product has the potential to offer reduced harm and what manufacturers can tell consumers about it. As there are currently no internationally agreed standards for conducting such an assessment, we would support establishing a scientific review process (comprising scientists from the public health community, the industry and other relevant stakeholders) to begin investigating appropriate, internationally accepted review methods.

Our scientists and regulatory experts have significant expertise in these areas, and have shared that expertise with the Commission of the European Union, the UK Department of Health and the WHO. We would welcome the opportunity to share information and experience with the Health, Welfare and Food Bureau, the Department of Health and the rest of the Government as well.

F. Youth Smoking Prevention

We do not want children to smoke, and we support regulations aimed at preventing youth from smoking.

The FCTC requires the adoption of effective legislative, administrative and other measures to prohibit sales of tobacco products to persons under the age of 18. Hong Kong already has very strong regulations that prevent tobacco product sales to persons under 18, including the requirement of a sign at the point of sale to indicate that no tobacco product may be sold to any person under the age of 18 years, the ban on packs less than 20 cigarettes, free samples and the vending machine sales. The minimum age law is also supported by heavy penalties for violation (e.g., HK\$10,001 - \$25,000), making youth access restriction a potentially meaningful measure in efforts to combat youth smoking.

As you may know, PMHK has been active in implementing youth smoking prevention programs since 1994. For example, in cooperation with the retail business in Hong Kong, we recently launched our annual YSP Access Prevention Program "Under 18, No Tobacco" campaign to remind our retailers not to sell tobacco products to minors. The campaign involves distribution by our employees of publicity materials including Government warning stickers, cashier tent cards, staff badges, caps, paper weights and parasols carrying the warning message to some 10,000 retailers all over the territory. Participating retailers included Circle K, 7-Eleven, the Daily Stop, Caltex Oil, ExxonMobil, Park n' Shop Express and the newspaper vendors throughout Hong Kong.

We believe that more can and should be done to prevent youth smoking. For example, we are undertaking research studies on several fronts with the objectives to measure the effectiveness of our youth smoking prevention programs, to understand cigarette retailers' compliance level with the law, and to understand retailer's reactions/behaviour towards selling cigarettes to those aged below 18. Ultimately, we would want to provide more concrete data to the Government to on stricter law enforcement of the minimum age law.

In addition, we would support measures to strengthen the enforcement of the minimum age regulation under the Smoking Ordinance. For example, we support clear designation of a specific government entity such as the Tobacco Control Office to carry out enforcement of the minimum age regulation. Unlike cigarette packaging regulation (e.g. health warning and tar and nicotine labelling on pack) where Customs and Excise is designated as the enforcement authority, there appears to be no designate authority to enforce the minimum age regulation. Once an enforcement entity has been designated, we would also support such entity to establish a mechanism for the inspection of the retail outlets to determine compliance. Finally, we support strict imposition of the penalties for violation of the minimum age regulation as mandated in the Smoking Ordinance.

Another measure which we would support to ensure that the minimum age law is enforced is the enactment of a retail license system. Similar to the licensing system described in section H below to help address the illicit trade of tobacco products, this

licensing system should be backed by deterrent penalties, ranging from revocation of the license, monetary fines, and/or criminal prosecution.

G. Other Measures to Reduce Tobacco Product Consumption

Article 20, section 2 of the FCTC states that “The Parties shall establish, as appropriate, programmes for national, regional and global surveillance of the magnitude, patterns, determinants and consequences of tobacco consumption and exposure to tobacco smoke.” In this respect, we would support extensive monitoring of smoking incidence and tobacco consumption trends, including analyses by age, gender and income groups. We would, of course, be happy to continue sharing our data on sales volumes and consumption with you. We would also support regulation requiring members of the tobacco industry to invest in the regulatory infrastructure of measuring cigarette consumption trends – for example, by funding market surveillance based on their market share.

Philip Morris International has taken a number of steps to support the consistent dissemination of information on the health effects of smoking, including its web site (www.pmintl.com), public service announcements, point-of-sale brochures, and on-pack communications. We would support further education and information programs designed to remind both smokers and non-smokers of the serious health effects of smoking. We support government programs to remind the public of the health effects of smoking and would support requirements for tobacco product manufacturers or importers to participate in such programs.

H. Combating Illicit Trade in Tobacco Products

We and our affiliates around the world support efforts to stop illicit trade in cigarettes whether they are counterfeit or genuine products. Contraband cigarettes, which may be either genuine or counterfeit product that is smuggled and sold in violation of required taxes and other tobacco specific regulations, disrupt the market and unfairly compete with our products. As a result, they have an adverse impact on our brands’ market shares.

We agree and support Article 15 of the FCTC which states that “the elimination of all forms of illicit trade in tobacco products, including smuggling, illicit manufacturing and counterfeiting, and the development and implementation of related national law, in addition to sub-regional, regional and global agreements, are essential components of tobacco control.”

We encourage all governments to enact and enforce legislation to achieve these goals. For Hong Kong, where legislation and strict enforcement of law are already in place, additional legislative measures may include, among others:

(i) Licensing

We believe that comprehensive licensing could help create a secure distribution network through which cigarettes are manufactured, transported, and sold to consumers in

accordance with all applicable fiscal and other requirements. All legitimate traders in the tobacco business should be subject to regulation designed to stop the illicit trade in tobacco products. An important aspect of this regulatory structure includes the licensing of all participants in the distribution network such as manufacturers, importers, distributors, wholesalers and retailers

In Hong Kong, the licensing of cigarette retailers would assist law enforcement agencies to identify parties authorized to sell tobacco products, ensuring that only legitimate tobacco products are sold by retailers, and that all applicable taxes are paid. Such a licensing system would prove a useful tool for law enforcement authorities in their fight against the increasing number of illegal street hawkers in Hong Kong who are selling contraband cigarettes, the majority of which are likely to be counterfeit.

The licensing system should be backed by meaningful deterrent penalties. Licensed retailers should be subjected to heavy penalties for knowingly or negligently engaging in the sale of contraband products (or in the sale to minors), including revocation of their license (for a fixed period initially and permanently for serious offences and repeat offenders), significant monetary fines which act as a deterrent, and/or criminal prosecution.

In short, the introduction of a simple retail licensing system for cigarette retailers would prove beneficial to both law enforcement and the retailers. Such a licensing system would serve as an additional tool for law enforcement authorities in their fight against the illegal vendors who are selling contraband products (both counterfeit and genuine product) as well as those who are selling to minors in violation of the minimum age law. Contraband cigarettes sold by illegal street hawkers unfairly "compete" with products sold by legitimate retailers, as these products do not pay the appropriate taxes and thus are sold at much lower price. When consumers purchase a counterfeit product from illegal street hawkers, rather than from legitimate retailers, the legitimate retailers lose revenue, which in turn, cause manufacturers and distributors to lose revenue as well.

Lastly, to ensure that consumers are purchasing cigarettes from retailers in accordance with applicable fiscal requirements, the legitimate channel must be protected and policed so that it is the only channel by which consumers can purchase cigarettes. Simply put, if consumers can only buy cigarettes through the legitimate channel, then there will be no real incentive and no practical mechanism for illegal sales.

We recognize and appreciate the efforts of the Hong Kong Customs and Excise Department, and will continue to work with the Department and other law enforcement agencies, to put a stop to the illicit trade in cigarettes in Hong Kong. We recognize, however, that combating contraband cigarettes is an enormous task for any government, and any effective solutions will require integrated action by industry, government, and consumers. We are willing and ready to discuss our views on possible solutions to address the issue of contraband cigarettes in Hong Kong in more detail with you.

(ii) Tax

Governments should take into account the unintended and often unforeseen consequences of increasing taxation levels on illicit trade in tobacco products. Although a number of studies state that it is possible to maintain high tax rates without a correspondingly higher level of smuggling provided that there are effective enforcement measures, tax is an important factor for illicit trade. The World Bank has stated "Differences in price between countries or states will clearly increase the incentives to smuggle cigarettes. However, the determinants of smuggling appear to be more than price alone."⁶ In other words, governments need to consider the impact of taxation levels on the incentive to illicit trade.

In determining its tax policy on tobacco, we submit the Government should also consider earmarking a percentage of tobacco tax revenues to fund anti-counterfeiting initiatives such as the seizure and destruction of illicit products, prosecution of the counterfeiters, as well communications programs with retailers and consumers to increase awareness of and to provide solutions to the problems.

Please see Section 3 below for more details on tax and price measures on tobacco products.

(iii) Duty-Free Sales

Hong Kong currently allows duty-free sales of tobacco products and should continue to do so. Duty-free sales are expected and accepted by Hong Kong visitors and international travellers, and duty free businesses make significant contributions to the Hong Kong economy.

The FCTC does *not* require a ban on duty free sales, and the Government should regulate but not ban them. Duty free sales likely do not increase consumption in Hong Kong, and banning such sales is unlikely to decrease consumption or reduce youth smoking. Banning well-regulated duty free sales will not contribute to the elimination of illicit trade in tobacco products. Finally, banning duty-free sales may contravene tax exempt privileges granted to foreign diplomats, consular officers, and their family members by international treaties.

Duty-free cigarette sales, like all other sales of tobacco products, should be subject to meaningful and effective regulation. We and our parent company, Philip Morris International, would support regulation requiring duty-free products to bear prominent, visible health warnings, with the appropriate content determined by the Government. We would support a requirement that all duty-free product be clearly marked as such. We also support recommendations from leaders in the customs enforcement community who have called for the computerization of government systems controlling the movement of duty-suspended goods to help such authorities monitor and track

⁶ World Bank (1999), "Measures to Reduce the Supply of Tobacco", in Curbing the Epidemic: Governments and the Economics of Tobacco Control, ch. 5.

shipments, thus reducing the opportunities for the diversion of duty-suspended product into domestic commerce.

A carefully regulated, monitored and enforced duty-free system should effectively prevent the diversion of duty-free products into free circulation in domestic commerce. We believe that the Hong Kong Government is putting in place such a system, for example, the limitation of the amount of duty free cigarettes which can be brought into Hong Kong which is supported by a computerized system to ensure compliance.

We and the Philip Morris International affiliate responsible for duty-free trade would welcome the opportunity to work with the Government on this subject.

3. Tax and Price Measures

Article 6 of the FCTC states that “price and tax measures are an effective and important means of reducing tobacco consumption by various segments of the population, in particular young persons” and recommends that Parties should consider “implementing tax policies and, where appropriate, price policies, on tobacco products so as to contribute to the health objectives aimed at reducing tobacco consumption.” We believe that tax and price can be appropriate measures to promote important government objectives, such as generating government revenue and discouraging consumption of tobacco products, especially by young people.

At the same time, it is important that tax policies do not result in products which are too expensive for adult smokers to buy, or result in an increase in the illicit trade in tobacco products. This can happen when the tax level is high, as is the case in Hong Kong. Based on economic theory (i.e. the Laffer Curve), Hong Kong’s current revenue maximising rate for tobacco duty is estimated to be approximately HK\$690-740 per thousand cigarettes. Therefore, the current rate of HK\$804 per thousand cigarettes is already beyond the point at which tobacco duty is expected to be maximised.

In many countries, tax-driven increases in cigarette prices have led to the introduction and proliferation of low-priced cigarette brands and/or increased purchases of untaxed or contraband products (both counterfeit and genuine product). The consequences are lower than anticipated revenue streams for government and a failure to reduce consumption because demand is driven to alternative available low price brands – and even to untaxed or contraband products. That has been the recent experience in Singapore and several countries in the European Union such as the United Kingdom, Germany and France.

A similar problem is emerging in Hong Kong. The low priced segment has been increasing, from 10% in 1998 to 23% of the industry volume in 2004 (July), while the premium segment has been decreasing, from 81% to 70% during the same period. Moreover, it is clear from available Government data that the Government loses tobacco duty revenue due to illicit cigarette sales.

In considering the tax policy on tobacco products, the Government should consider whether the current structure of taxation is achieving the Government's objectives of generating revenues and reducing tobacco consumption, or whether such structure simply facilitates a shift in demand from higher priced products to lower priced products or even untaxed or contraband products. According to Government data, the rate of smoking incidence in Hong Kong actually increased from 12.4% in 2000 to 14.4% in 2003.

We believe that a tax policy of moderate and regular tax increases would likely maintain Government revenue both in the short and long term and help the Government to further reduce tobacco consumption. As mentioned above, the level of tax increase must take into account the consumer purchasing power to ensure that tobacco products do not become so costly that consumers are encouraged to purchase alternative products including those from outside the legitimate channel.

The FCTC also suggests that price measures may be an appropriate method of discouraging smoking. Some governments have found that increasing tax levels merely encourages consumers to shift to cheaper cigarette brands or other types of tobacco products. To address that phenomenon, France recently adopted a regulation which prohibits manufacturers from selling below 95% of the average price of all brands in the market. We understand that the Italian government is considering adopting similar regulation. Ireland has had similar regulation in place since 1978, and defines sale below a three-tiered reference minimum price as prohibited promotional activity.

We would not oppose to such a regulation in Hong Kong. The adoption of a benchmark minimum price for tobacco products could help prevent down-trading as an alternative to quitting and could advance public health goals. If the objective of the tax policy is to reduce consumption, as suggested by the FCTC, a minimum price could advance that objective.

Of course, any tax increase will likely increase the prices of cigarettes sold in the market, thereby increasing the reference price determined by the Government and subsequently the minimum price below which the sale of cigarettes would be prohibited.

We look forward to discussing with you our view on this important issue in more detail.

Conclusion

We appreciate this opportunity to present our views on the amendment of the Smoking Ordinance and other key regulatory areas that could advance the goal of reducing the harm caused by smoking. Our intention is to work cooperatively and constructively with the Government to achieve effective and practical tobacco control legislation and to address issues that are of legitimate concern to the Government, public health authorities, consumers and the industry. We respect the Government's goal of reducing tobacco consumption and harm of tobacco products. Our view and approach may be met with some scepticism. Many assume that a tobacco company would oppose regulation,

especially regulations that seek to reduce the use of tobacco products. But declining consumption is a fact worldwide. Regulations – whether aimed at reducing consumption or regulating tobacco products - can both meet public health objectives and provide us with the rules by which we – and other tobacco companies – must conduct our business.

We look forward to the opportunity to meet with you to present in more detail our positions on these important issues.