

# **Tobacco Tax Act Review – Consultation Paper #1**

**June 2024**



Ministry of  
Finance

# TOBACCO TAX ACT REVIEW – CONSULTATION PAPER #1

## INTRODUCTION

The Ministry of Finance (the Ministry) is undertaking a project to review the *Tobacco Tax Act* and make recommendations for proposed amendments to better reflect current practices in the tobacco industry, support improved administration including the ability to combat illicit tobacco, and streamline requirements. As part of the review, the Ministry is engaging in consultations and making recommendations for improvement.

Several key topics are being considered as part of the project. These topics are discussed in two consultation papers. This is Consultation Paper #1, which discusses improving administration, strengthening compliance and enforcement, and reducing complexity. For discussion of the exempt sale retail dealer program and the band tobacco tax, see Consultation Paper #2.

The project does not include changes to the tax base or that impact provincial revenue. For example, the project does not consider changing tobacco tax rates or imposing any new tax.

## GOAL – IMPROVE ADMINISTRATION

### PERMITS

Persons selling or offering to sell tobacco at wholesale or at retail in British Columbia must hold a dealer's permit or retail authorization. The *Tobacco Tax Act* and the *Tobacco Tax Act Regulation* (the regulation) set out different requirements, limits and conditions for each class of permit and authorization. Over time, the terminology under the *Tobacco Tax Act* and regulation that is used by government and tobacco businesses has ceased to accurately reflect industry practice and, as a result, has added complexity and created confusion.

To address these issues, the Ministry proposes the following permits be created or continued for the purpose of authorizing tobacco sales:

- **Retail Dealer Permit** – the retail dealer permit is proposed to replace the term “retail authorization” and would not affect businesses’ operations. Similar to current requirements, a retailer dealer permit would be required to be held by persons that sell taxable tobacco at retail. A separate permit would be required for each retail location in British Columbia from which the person sells taxable tobacco, including vending machines.
- **Wholesale Dealer Permit** – a wholesale dealer permit would continue to be the type of permit required by all those dealers that sell tobacco at wholesale and is proposed to include those that only sell cigars at wholesale, no longer necessitating a separate wholesale dealer permit for cigars. Those businesses

that currently hold a cigar wholesale dealer permit would be transitioned to a generic wholesale dealer permit with no effect on businesses' operations.

- **Exempt Sale Retail Dealer Permit** – an exempt sale retail dealer permit would continue to be the type of permit required to be held by all those dealers that sell tax-exempt tobacco (e.g., black stock) at retail. Exempt sale retail dealer permit holders are located on First Nations land or are a duty-free shop or ship's chandler.
- **Special Retail Dealer Permit** – a special retail dealer permit would continue to be the type of permit required by dealers that sell tobacco at retail on reserve land where a band tobacco tax agreement relates applies. See Band Tobacco Tax in Consultation Paper #2.

### *Authority to Issue, Suspend and Cancel*

The Ministry proposes to recommend expanding the director's authorities under the *Tobacco Tax Act* regarding issuing, suspending and canceling each of the above types of dealers' permits. (The director is the person authorized by the Minister of Finance to administer the *Tobacco Tax Act*.) The purpose of this proposal is to strengthen the powers of the director and to improve administration across the consumption tax acts.

The first recommendation is to provide authority to the director to cancel a dealer's permit on receiving a copy of a prohibition order to that dealer issued under the *Tobacco and Vapour Products Control Act* (TVPCA). The director would have discretion to cancel the dealer's permit subsequent to (or as an alternative to) the existing mandatory suspension set under the *Tobacco Tax Act*. Notice would be provided to the dealer of a proposed cancellation, as well as an opportunity to respond. Under the current rules, the director must suspend a dealer's permit on receiving a copy of a prohibition order issued under the TVPCA, but the rules are silent on cancelling the permit. This proposal gives the director the option to cancel the permit in appropriate situations.

The second recommendation is to add authorities like those under the other British Columbia consumption tax acts (*Provincial Sales Tax Act, Motor Fuel Tax Act, Carbon Tax Act*). Those Acts contain circumstances not included in the current *Tobacco Tax Act* in which the director may suspend or cancel a registration, certificate or appointment. Adding similar circumstances in relation to permits under tobacco tax legislation would create consistent administration across the consumption tax acts.

Proposed circumstances under which the director could refuse to issue, suspend or cancel a dealer permit would expressly include:

- Person does not hold the registrations, licenses, permits or other authorizations the person is required by law to hold to carry on business;
- Person fails to deposit a bond as required by the director;

- Director reasonably believes the person is or will be committing an offence under the *Tobacco Tax Act* or any other enactment, or under a law of Canada or another province, in selling tobacco; and
- Director is satisfied a person knowingly submitted an application or information that contains false or misleading information or fails to disclose a material fact.

## **CLARIFYING COLLECTOR APPOINTMENTS**

The Ministry proposes to create specific authority for the director to appoint persons as collectors. A collector is proposed to be a person who sells tobacco for the first time after import or manufacture in British Columbia (i.e., the person at the top of the supply chain in British Columbia). In addition to being a collector, these persons would also be required to hold the appropriate dealer's permit to sell tobacco at wholesale or retail.

The authority to appoint these persons as collectors would replace the existing system. Currently, all persons holding a wholesale dealer permit are deemed to be a collector even if they are not importing tobacco. Additionally, there is a lack of clear authority for retailers that import tobacco themselves to be appointed collectors.

As a result of this proposal, those business that do not import or manufacture tobacco to sell for the first time in British Columbia but instead purchase all their tobacco within British Columbia will not be a collector. While the change to or from collector status may affect some businesses, the impact is anticipated to be limited and transitory. The change will remove an unnecessary legal requirement that currently exists under the *Tobacco Tax Act* for these businesses to remit tax (or security) or file tax returns to government. This requirement is unnecessary as the businesses that are importing tobacco for sale are already required to remit the tax (or security) to government and file tax returns in respect of the tobacco. Retail dealers who only purchase tobacco within British Columbia are not impacted by this proposal.

## **GOAL – STRENGTHEN COMPLIANCE AND ENFORCEMENT**

### **ILLICIT TOBACCO**

Tobacco in British Columbia is strictly regulated to keep illicit tobacco from getting to young people, from eroding tax revenue, and from contributing to other criminal activities. Selling and possessing illicit tobacco in British Columbia is an offence under the *Tobacco Tax Act* and is a crime under the *Criminal Code* (Canada).

To further combat illicit tobacco in the province, the Ministry proposes to recommend several changes to strengthen compliance and enforcement powers to bring British Columbia in line with current practices in other Canadian jurisdictions.

Specifically, the Ministry proposes to strengthen enforcement provisions to improve its ability to combat illicit tobacco sales by:

- Clarifying and expanding the director's authorities to suspend and cancel dealer's permits and increasing the maximum length of suspensions from 30 days to 60 days;
- Expanding inspection powers by authorizing inspectors to inspect anything at a business premise and requiring an occupant of the business to promptly produce tobacco at the premise. This measure will help government inspectors where businesses try to hide illicit tobacco;
- Creating new authorities for the Ministry to issue administrative monetary penalties for non-compliance. Other than a costly court prosecution, the current *Tobacco Tax Act* lacks timely and effective penalties for certain types of non-compliance, such as selling tobacco without a permit or selling tobacco that is not properly marked. See Administrative Monetary Penalties below;
- Reviewing fine amounts. Some existing fines are significantly less than in other provinces and no longer provide an adequate deterrent. See Fine Amounts below;
- Creating a new class of permit and compliance rules for manufacturing and transporting tobacco in British Columbia. See Manufacturing and Distribution below;
- Modernizing the legislation by adding a general anti-avoidance rule (GAAR) like in the *Provincial Sales Tax Act*. A GAAR serves as a deterrent against tax avoidance schemes and a practical means of recovering revenue that would otherwise be lost to such schemes.

## **ADMINISTRATIVE MONETARY PENALTIES**

The Ministry proposes to recommend creating new administrative monetary penalties (AMPs) for contravening certain rules under the tobacco tax legislation. An AMP is a monetary penalty imposed by the Ministry against a person for not complying with rules under the *Tobacco Tax Act* or the regulation. They differ from offences which proceed as convictions and may result in imprisonment.

Specifically, the Ministry proposes to add AMPs for the following types of non-compliance:

- (a) Selling or offering to sell tobacco without a valid permit;
- (b) Selling or offering to sell tobacco for resale to a person who does not have a valid permit;
- (c) Selling or offering to sell tobacco from a location where a permit is suspended or cancelled;
- (d) Acquiring tobacco in British Columbia for resale from a person who does not hold a valid wholesale dealer permit;
- (e) Participating or acquiescing in any of the above contraventions ((a)-(d));
- (f) Not producing records or answering questions as required, or hindering or interfering with an inspection or audit, or preventing a person from carrying out an inspection or audit;

(g) Selling tobacco that does not bear the required tobacco stamp or mark.

These new AMPs would provide the Ministry with a wider range of enforcement tools to ensure compliance. The proposed AMPs will be particularly useful for minor situations of non-compliance or situations of non-compliance not directly related to failing to pay, collect or remit tax (which are already covered by existing penalties).

Generally, the penalty amount of a proposed AMP will depend on the type of contravention. AMP amounts are proposed to be similar to those available to the administrator under the TVPCA for purposes of that legislation. For example, depending on the rule, an AMP could be up to \$1,000 or \$3,000 for a first contravention. Penalty amounts imposed may be increased on a second or subsequent contravention in accordance with a schedule of penalties.

As is the case currently, in the event of a contravention of a more significant or wilful nature or manner (for example, involving counterfeit tobacco or potential criminal activity), the non-compliance could be pursued under an offence proceeding.

## **COURT FINES**

Fines are enforcement tools to punish persons for not complying with tobacco tax rules and deter non-compliance. Fines are imposed through the court system and, depending on the offence, are an alternative to or in addition to imprisonment. The Ministry proposes to review fine amounts and make recommendations for increasing certain fines. Currently, there is a substantial difference in some fine amounts between British Columbia and other provinces' tobacco tax acts. Alberta, Saskatchewan and Ontario provide for certain fines of up to \$1,000,000 (for example, for unauthorized marking of tobacco). Recommended changes would bring fine amounts in line with other Canadian jurisdictions.

## **MANUFACTURING AND DISTRIBUTION**

The Ministry proposes to recommend creating two new permit classes and related requirements for manufacturing tobacco and transporting unmanufactured tobacco (including raw leaf tobacco) in British Columbia.

The proposed manufacturing permit would allow a dealer to manufacture tobacco in British Columbia and provide for the related activity of importing or purchasing unmanufactured tobacco for use in a manufacturing operation in the province, subject to holding all other required permits or authorizations (e.g., a tobacco licence issued under the federal *Excise Act, 2001* to manufacture tobacco products in Canada). Generally, tobacco manufacturing includes any step in the preparation of unmanufactured tobacco into a tobacco product, including packing, stemming, reconstituting, converting or packaging the raw leaf tobacco or tobacco product. Any person who does not hold the proposed permit would be prohibited from manufacturing tobacco in British Columbia. In addition, it is proposed that those holding tobacco manufacturing permits be required

to report imports, distribution (movement within the province) and export of their unmanufactured and manufactured tobacco. Reporting frequency is proposed to be monthly or other frequency determined by the director.

The proposed transporting permit would allow a person to transport unmanufactured tobacco in British Columbia with specific responsibilities and obligations attached. For example, it is proposed that transportation permit holders be required to keep, in each vehicle used to transport tobacco, a manifest or waybill for each load transported. Each manifest or waybill will be required to contain specified information and be made available to enforcement authorities for inspection.

Manufacturing tobacco and the related activity of importing or receiving unmanufactured tobacco (including raw leaf) into the province to manufacture tobacco products has not been a traditional business activity in British Columbia and, as such, has not been regulated by the province to date. However, it is becoming necessary to include an appropriate framework for regulating manufacturing within the provincial legislation.

Unlike manufacturing of tobacco, the *Tobacco Tax Act* does currently provide some regulation of the transportation of tobacco. Under the current rules, persons are prohibited from transporting in British Columbia tobacco in bulk in excess of 10 kilograms or cigarettes in quantities in excess of 50 cartons. However, the prohibition does not apply to dealers permitted to sell tobacco or a person in the business of transporting goods and contracted to a permitted dealer to transport tobacco for that dealer, nor does it apply to unmanufactured tobacco. Therefore, it is also necessary to establish a more comprehensive regulatory framework for the transportation of tobacco, including unmanufactured tobacco.

The proposed changes to enable the authorization of manufacturing and better regulate transportation of tobacco will help to align British Columbia with other provinces. Other provinces have registration and regulatory requirements for manufacturers and transporters of raw leaf tobacco. For example, Ontario requires a registration to import or export tobacco in bulk. Québec requires a manufacturer's permit to possess or bring into the province tobacco manufacturing equipment. Both provinces require a carrier permit for the transport of raw leaf or other specified tobacco in the province. Fines and other penalties, including impoundment or seizure of the transporting vehicle, may be imposed for non-compliance. Such rules are important tools to respond to illicit tobacco problems including the production and distribution of unlawful tobacco.

## **PROHIBITIONS**

Numerous prohibitions are already included under the *Tobacco Tax Act*. The purpose of these prohibitions is to prevent activity that leads to or may lead to undermining of the tax on tobacco through unlawful selling, possession and distribution of tobacco in British Columbia.

In addition to these existing prohibitions, the Ministry proposes to recommend adding new prohibitions. Specifically, the Ministry intends to recommend adding new prohibitions regarding the proposed obligations specific to the manufacture and transportation of unmanufactured tobacco in British Columbia. See Manufacturing and Distribution above. Also, the Ministry proposes to (a) prohibit the sale of tobacco specific to a suspended or cancelled permit at that location (i.e., tobacco specific to another permit at the location, that is not suspended or cancelled, may continue to be sold), and (b) prohibit a person from acquiring tobacco while their permit is suspended.

These last two new prohibitions will help address two specific issues. First, in certain circumstances the director may suspend or cancel a person's dealer's permit or suspend or cancel a person's permit for a specific location. An issue arises where a person holds more than one permit for a single location. For example, in a situation where a person holds both a retail dealer permit and an exempt sales retail dealer permit for the same location, there may be an issue with the way the person is selling taxable tobacco at the location but is otherwise compliant for selling exempt tobacco at the same location. However, when the director suspends or cancels the retail dealer permit and not the other, the current prohibition applies to any tobacco being sold from the location, including any tobacco sold under authority of the permit that is not suspended or cancelled. The proposed change will provide the director more flexibility to target enforcement actions.

Second, the *Tobacco Tax Act* prohibits a person from selling tobacco to a dealer whose permit is suspended to limit the ability of that person to make further sales. However, the *Tobacco Tax Act* does not expressly prohibit the dealer whose permit is suspended from purchasing tobacco for resale. Currently, the Ministry sends a letter to dealers whose permit is suspended advising that, in addition to being prohibited from selling tobacco, they cannot purchase tobacco for resale. The Ministry proposes to add an express prohibition against purchasing tobacco for resale while a person's permit is suspended to support the administrative practice and help deter unlawful distribution of tobacco.

## **GOAL – REDUCE COMPLEXITY**

The current scheme in the *Tobacco Tax Act* under which government receives tax revenue is complex with multiple interlinked obligations. To reduce this complexity and simplify the scheme, the Ministry proposes to recommend changing how the tax is levied (charged) and collected.

Note: The proposal to how the tax is levied and collected would not apply in respect of tax-exempt tobacco (e.g., black stock) authorized to be purchased and sold in British Columbia.

First, the Ministry proposes to recommend changing the point in time at which the obligation for collectors to pay tax to government arises. The Ministry proposes to change the required time to pay from the time of import to the time of the first sale in



British Columbia after import or manufacture. This proposed change has the advantage of ensuring there is clarity for persons who manufacture tobacco in British Columbia and aligning the timing of the tax payment obligation with the approach in tobacco tax legislation in Alberta, Manitoba, Ontario and Québec. It also aligns with the approach to tax collection in British Columbia's *Motor Fuel Tax Act* and *Carbon Tax Act*, enabling simplified administration for the Ministry.

Second, the Ministry proposes to recommend changing the overall tax collection system from a security scheme to a tax reimbursement scheme (for a visual comparison of the two schemes see Appendix A and B). Although opaque to dealers, the current legislation imposes both tax collection and security payment obligations on retail and wholesale dealers. Wholesale dealers' obligations to collect tax are relieved if security (an amount equal to the tax) is paid on the tobacco.

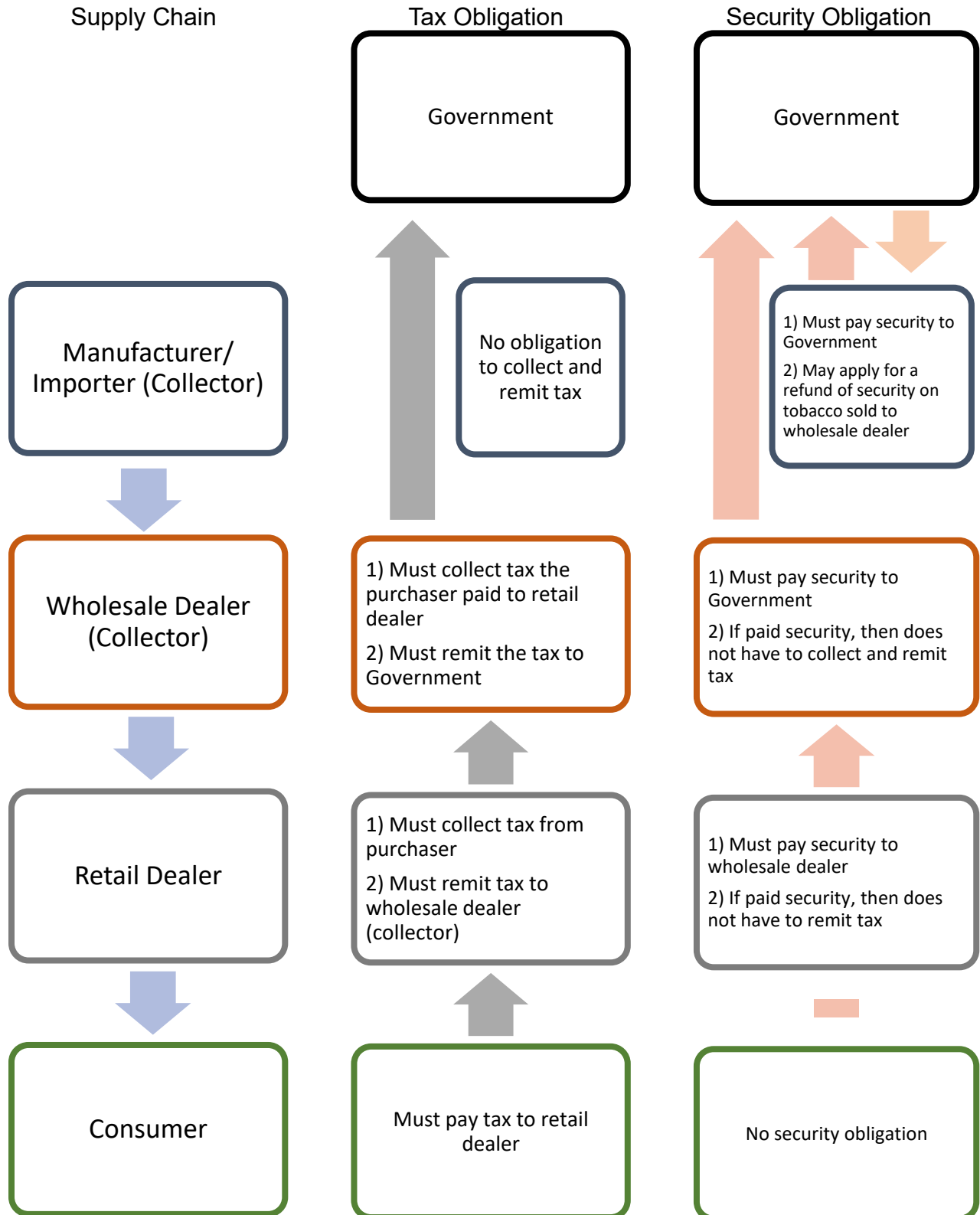
A tax reimbursement scheme eliminates this legislative complexity by removing the parallel obligations on dealers to both collect tax and pay security. Under the proposed model, the first dealer to import or manufacture taxable tobacco for sale in British Columbia (the collector) must pay tax to government on that tobacco when they sell it for the first time after the tobacco is imported into or manufactured in British Columbia. The amount of tax paid to government is the same amount eventually required to be paid by end consumers on their purchase of the tobacco. The next dealer (wholesale or retail) in the supply chain would, in turn, be required to pay tax to their supplier on any tobacco purchased in British Columbia and collect tax on their subsequent sale of the tobacco. In this manner, each dealer is reimbursed for the tax they paid on tobacco by being able to retain the tax they collect from the next dealer in the chain or, in the case of retail dealers, the tax they collect from the consumer of the tobacco. Ultimately, the consumer will bear the burden of the tax, just as they do currently.

Under this scheme, collectors are only required to pay tax to government on the tobacco they import into or manufacture in and sell in British Columbia. Collectors and other wholesale and retail dealers that purchase tobacco for resale in British Columbia would not be required to pay tax or security to government on that tobacco and government would no longer require an administrative process to eliminate the duplicate payments of security to government by wholesale dealers currently required by the *Tobacco Tax Act*. The duplicate payment obligation arises from the fact that both wholesale dealers that import tobacco and wholesale dealers that purchase tobacco in British Columbia must pay security to government on the same tobacco.

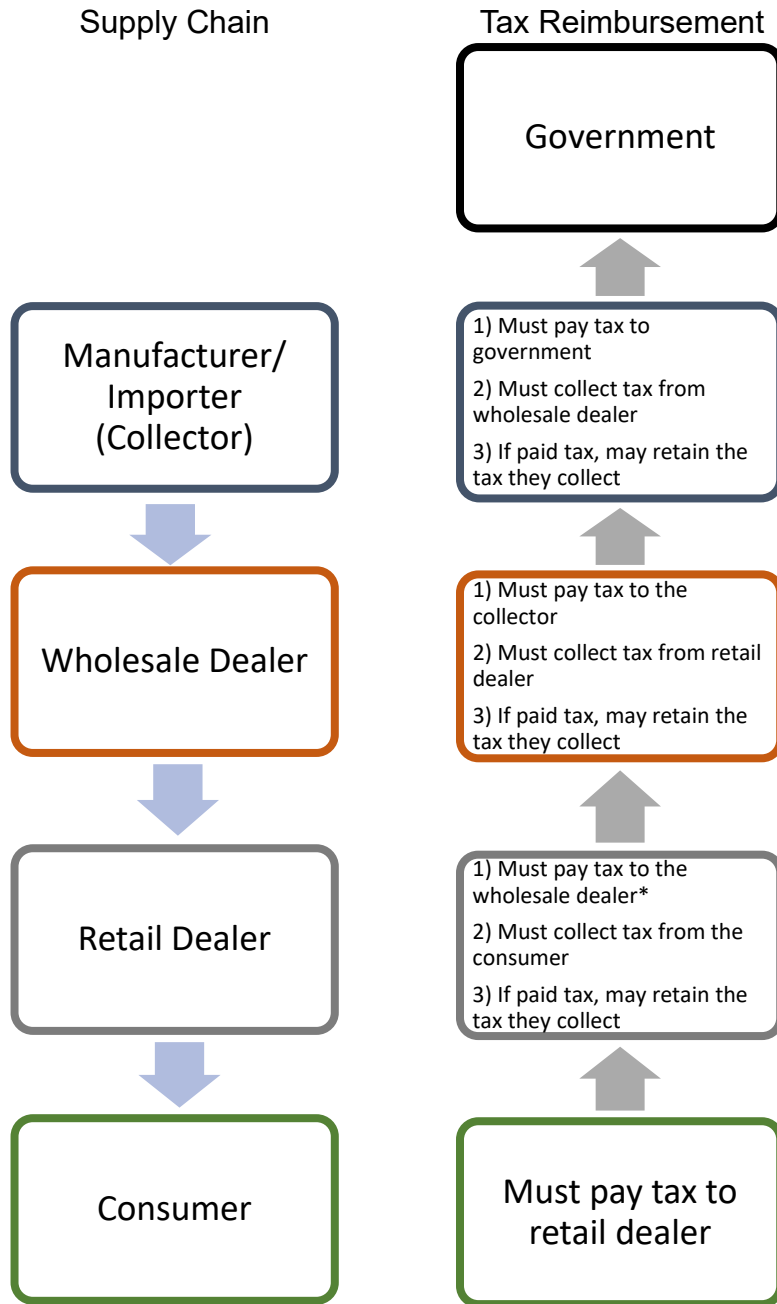
A tax reimbursement scheme does not change the ability of government to protect tax revenue by having tax paid at the top of the supply chain. However, it significantly simplifies the administrative and legal scheme and therefore better enables the Ministry to assess compliance with the requirements. Under this proposed change, the Ministry estimates that 25% fewer businesses (those wholesale dealers that only purchase their tobacco inventory in British Columbia) would be required to pay tax directly to government and file tax returns while not impacting the net tax revenue received by

government. All other tobacco dealers (wholesale or retail) would see their obligations remain effectively the same.

## Appendix A: Current Tobacco Tax Security Scheme



## Appendix B: Proposed Tobacco Tax Reimbursement Scheme



\* Where a collector sells direct to the retail dealer, the retail dealer pays tax to the collector. Where the collector also acts as the retail dealer (i.e., direct to consumer sales), the collector still pays tax to government but also collects tax from the consumer.