



Tax Treatment of Unverifiable Tobacco Losses

This bulletin was revised June 2008 to incorporate formatting changes and changes in ministry name and contact information only.

Highlights

- The Act was amended to provide authority for the Minister to assess a penalty where a person's unverifiable tobacco losses are in excess of a prescribed threshold. The amendments were made December 5, 2001.
- Regulation amendments were introduced to provide the method for calculating a threshold for unverifiable losses as well as a method for calculating unverifiable losses and excess unverifiable losses
- This bulletin provides general information. It is not exhaustive and should not be considered as a substitute for the Tobacco *Tax Act* and its regulations.

Background

Penalty for Unverifiable Losses which Exceed Threshold

While the Ministry acknowledges that there are legitimate unverifiable product losses in the course of manufacturing and distribution of tobacco products, it has been determined that the tax revenue erosion resulting from unverifiable losses which exceed a certain threshold is not acceptable.

The purpose of the amendments described in this bulletin is to provide an incentive to reduce unverifiable product losses while limiting tax revenue erosion.

Subsection 19(3.4) of the Act provides for the assessment of a penalty where a person's unverifiable loss of tobacco is found to be in excess of a prescribed threshold. The penalty is an amount equal to the tax that would have been collectable by the person if the tobacco had been sold to a consumer liable to pay tax.

Regulation 1033, as amended, provides the method for calculating unverifiable losses, excess unverifiable losses, and also provides a threshold for unverifiable losses. The method of calculation of losses and the threshold are detailed below.

These amendments do not apply to losses which may be verified by supporting documentation. For further information on lost, destroyed, stolen, or contaminated tobacco, please refer to [Ontario Tax Bulletin TT 3-2000](#), published October 2000

Elements of Calculation

An **unverifiable loss** exists where an amount of tobacco cannot be accounted for.

Available inventory is the amount of tobacco that must be accounted for. It is the total of opening tobacco inventory plus additions to inventory during a selected period, less closing inventory. A person's unverifiable loss is that portion of the available inventory which cannot be shown, to the satisfaction of the Minister, to have been sold, lost, stolen, destroyed, contaminated, consumed or distributed.

A **threshold** for acceptable losses has been prescribed. Any loss of tobacco which exceeds this threshold is an **excess loss** and it is on any excess loss that a penalty may be assessed.

The threshold is not an allowance. Only where the person has satisfied the Minister that inventory reconciliations show unverifiable losses, will those losses be recognized.

Method of Calculation

Available Inventory A person's **available inventory** of tobacco is calculated over any period of 36 consecutive months using the formula:

$$A + B - C$$

In this formula,

"**A**" is the amount of the person's opening inventory of tobacco at the beginning of the period,

"**B**" is the amount of tobacco produced, received or purchased by the person during the period, and

"**C**" is the amount of the person's closing inventory of tobacco at the end of the period.

Unverifiable Losses **Unverifiable losses** is the amount of a person's available inventory less the amount of tobacco that the person verifies to the satisfaction of the Minister to have been sold, lost, stolen, destroyed, contaminated, consumed or distributed.

Prescribed Threshold The prescribed **threshold** for unverifiable loss is 0.1% (one-tenth of one percent).

Excess Unverifiable Losses **Excess unverifiable losses** exist where the person's unverifiable losses exceed the threshold multiplied by the person's available inventory. That is:

$$\text{excess unverifiable losses} = \text{unverifiable losses} - (0.1\% \times \text{available inventory})$$

If this calculation results in a negative figure, the person does not have excess unverifiable losses.

Penalty

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|---------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Penalty on Excess Unverifiable Losses | A penalty may be assessed on any excess unverifiable losses. The penalty is an amount equal to the tax that would have been collectable by the person if the tobacco had been sold to a consumer liable to pay tax. |
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Additional Information

If this bulletin does not completely address your particular situation, refer to the Act and related regulations, or contact the:

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This bulletin and various other English and French tax materials published by the Ministry of Revenue may be obtained online at ontario.ca/revenue.

The *Tobacco Tax Act* and Ontario's other public statutes and regulations may be obtained online at www.e-laws.gov.on.ca.

Ce bulletin est disponible en français.