

June 29, 2021

Mr. Phil King
Director General
Department of Finance Canada
14th floor
90 Elgin Street
Ottawa, Ontario K1A 0G5
Email: fin.vaping-taxation-vapotage.fin@canada.ca

Re: Vaping Tax Consultation, Budget 2021 Tax Measures

Dear Mr. King,

Juul Labs Canada Ltd. respectfully submits written comments in response to the Department of Finance intentions to introduce a new taxation framework for the imposition of excise duties on vaping products in 2022, as described in Budget 2021.

Introduction

Juul Labs Canada Ltd. ('JLC') supports Health Canada in its goal to reduce tobacco use to less than 5% prevalence by 2035 and supports Canada's Tobacco Strategy goal to "protect the health of young people and non-smokers from the dangers of tobacco use." We believe that Canada can accelerate the end of smoking by continuing the tradition of embracing tobacco harm reduction and maintaining adult access to non-combustible alternatives, such as vaping products, for those who will not quit nicotine use entirely.

As JLC strives to reset our company and category in Canada, we are focused on listening and building constructive relationships with regulators, policymakers, and other stakeholders to advance the harm reduction potential for adults who smoke. One of the key tenets of these efforts is our commitment to combat underage use of our products through evidence-based interventions.

In the fight to reduce the harm from combustible cigarettes, we must all be clear in our message: We do not want any non-nicotine users, especially those underage, to try our products as they exist only to transition Canadian adults who smoke away from combustible cigarettes. We believe people who smoke should first and foremost quit. Those who have not successfully quit should completely switch to potentially less harmful alternative nicotine products.

We support risk-proportionate regulation for vaping products and other reduced-risk, noncombustible options. Such a policy framework, at its core, applies the most stringent regulations to the riskiest products (e.g., combustible cigarettes) and encourages adults who smoke to migrate to potentially less harmful alternatives (e.g., vaping products). To be clear, risk-proportionate regulation does not mean a “lenient” approach to noncombustible alternatives. Rather, it means a robust, informed regulation of tobacco and nicotine products, which also applies to fiscal policy and excise tax frameworks.

A well thought out, balanced tax structure can only contribute to the massive decreases Canada has already seen in the prevalence of current smoking, which recent Statistics Canada surveys have indicated are at the lowest estimates ever recorded.¹ We are encouraged by the direction and intent of this newest ‘Vaping Tax Consultation’ proposal from the Department of Finance Canada (‘Finance Canada’), and appreciate the opportunity to provide feedback to further protect against underage vaping and support adult smokers looking to access noncombustible alternatives.

Detailed below we highlight minor, evidence-based amendments that we believe will help achieve the balanced intent of the Tobacco and Vaping Products Act (TVPA). We believe a clear ‘per mL’ tax, a considerable implementation timeline and a Federal-Provincial-Territorial (FPT) Agreement would achieve all the balanced objectives of the TVPA: discourage persons who do not already use nicotine products to start, while encouraging adult combustible cigarette consumers to switch to less harmful options.

Risk-Proportionate Taxation

“To incentivise and signal the importance of substituting tobacco with less harmful forms of nicotine, the level of taxation applied to non-tobacco nicotine products should be proportionate to their harm relative to tobacco.

*To this end, tax on medicinal nicotine should be abolished and tax on electronic cigarettes reduced.” **Royal***

College of Physicians²

The tax system can be an important lever to support harm reduction by encouraging smokers to quit, or to switch to potentially less harmful alternatives. Research generally supports a substitution effect between vaping products and combustible cigarettes, which has been examined under several different contexts in North America. In Canada, Ian Irvine of Concordia University has written extensively about the significant and

¹ StatsCan 2020. CTNS <https://www150.statcan.gc.ca/n1/daily-quotidien/210317/dq210317b-eng.htm>

² <https://www.rcplondon.ac.uk/projects/outputs/smoking-and-health-2021-coming-age-tobacco-control>

unprecedented decline observed in cigarette stick sales following the federal legalization of vaping products.³ Additionally, in an examination of the impact of the launch of the JUUL system on the Canadian market, research showed a city-wide decrease of combustible tobacco sales of 1.5%, on average, following the JUUL system becoming available in each city.⁴

Research examining vaping products in the U.S. generally illustrate a substitution effect due to changes in tax. Vaping products in these studies also appear to be more price elastic than combustibles.⁵ A study funded by the National Institutes of Health using retail data from 35,000 retailers across the U.S. estimates that for every vaping pod not purchased due to a vaping tax, 5.5 additional packs of combustible cigarettes are purchased.⁶ Three other studies utilized U.S. survey and sales data from the Nielsen Scanner, Behavioral Risk Factor Surveillance System, National Health Interview Survey, and Current Population Survey Tobacco Use Supplements, reporting a general consumption shift towards cigarettes after an increase in ENDS taxes.⁷⁸⁹

All this indicates vaping product taxation needs to be carefully considered, and must be informed by an overall tobacco strategy taking into account the taxation of other nicotine products; especially combustible tobacco.

Risks of an Uneven Approach

We are encouraged by the direction of Finance Canada's fiscal policies and their intention to create price differentials - powerful tools that can help push adults who smoke away from cigarettes and pull them to noncombustible products. However, the heterogeneity of the Canadian vaping market, combined with the proposed tax base, undermines those price differentials. The excise duty structure should support Finance Canada's overall objective of increasing the price of vaping products while also providing a framework to encourage users of nicotine to switch to less harmful forms.

However, we note that the proposal is likely to have the significant and unintended consequence of providing a competitive advantage to some vaping products and dramatically distorting the competitive environment. Specifically, the "tax cliff" created by the per 10 mL tax base "or any fraction thereof" puts products with smaller container sizes (of around 1 mL that cannot be easily changed) at a significant disadvantage. **We urge Finance Canada to simply strike the "any fraction thereof" language to create a pure 'per mL' duty, which would effectively correct this unprecedented "tax cliff" structure.**

³ <https://www.cdhowe.org/public-policy-research/taxation-nicotine-canada-harm-reduction-approach-profusion-new-products>;

<https://www.cdhowe.org/intelligence-memos/ian-irvine-%E2%80%93-smart-youth-drive-enormous-smoking-declines>;

<https://www.cdhowe.org/intelligence-memos/ian-irvine-%E2%80%93-vilification-vaping>

⁴ <https://thelogic.co/news/juul-seeks-role-in-reducing-smoking-as-it-pursues-vaping-category-reset/>

⁵ <https://www.rcplondon.ac.uk/projects/outputs/smoking-and-health-2021-coming-age-tobacco-control>




⁶ https://www.nber.org/system/files/working_papers/w26724/w26724.pdf

⁷ https://www.nber.org/system/files/working_papers/w27000/w27000.pdf

⁸ <https://rd.springer.com/article/10.1007%2Fs11166-020-09330-9>

⁹ https://www.nber.org/system/files/working_papers/w26589/w26589.pdf

In Canada, the market for vaping products is extremely heterogeneous and diverse; there are pod-based systems, open tank systems requiring e-liquid refill bottles and disposable systems (Displayed in Figure 1). There is heterogeneity in how the devices work and heterogeneity of the amount of liquid each product contains.

		
Open tank system	Pod-based system	Disposable system
<p>Figure 1. Representative images of three types of vaping products on the market. Open tank systems are user-filled, from a large bottle of e-liquid, the tank and heating element are reusable and interchangeable. Pod-based systems are comprised of a battery and a closed pod containing the liquid and the heating element, the pod is disposed of after use. Disposable systems are closed, however both the container and battery are disposed of after use.</p>		

The proposed tax cliff privileges some products over others, and even differentiates between individual brands in the same product category which is distortionary and will grant unfair commercial advantage to certain manufacturers or brands over others. Table 1 illustrates the amount of liquid in each immediate container. **The proposed excise tax framework leads to some vaping products being taxed over ten times more on a 'per mL' basis than others.** This also creates incentives to build larger tanks or devices and penalizes pod-based systems over open tank systems. Unlike combustible cigarettes, where changing the size of a pack is a matter of adjusting packaging, changing the volume of e-liquid in a pod such as JUULpods requires re-engineering the entire device itself.

The closed-system products most privileged by this proposed excise tax structure are disposable products, which generally have larger volumes of vaping liquid than pod-based systems. JLC has contracted with Euromonitor International regarding a research study of the disposable vaping market in Canada. In a

preliminary report, they found a wide range of devices and vaping liquid volumes, with Euromonitor estimating disposable product sales almost doubling between 2019 and 2020 (\$151mn-\$264mn). In the most recent U.S. National Youth Tobacco Survey, disposable product use increased significantly: “disposable e-cigarettes are being used by 26.5% of high school e-cigarette users (up from 2.4% in 2019) and 15.2% of middle school e-cigarette users (up from 3% in 2019)”.¹⁰ Finally, research on the disposable products available in the U.S. showed they had unreliable labelling, low quality of construction and poor temperature control, all which lead to greater potential harm.¹¹ A pure ‘per mL’ tax on vaping products would not incentivise disposable products over other closed systems.

Table 1. Excise paid per immediate container	
Immediate container	Excise paid per mL
30 mL bottle of e-liquid (for open tank system)	\$0.10
JUULpod (0.7mL)	\$1.42
Vuse epod (1.9mL)	\$0.52
Ghost XL (3.2mL)	\$0.31
ENVI Boost (5mL)	\$0.20
Allo Ultra 1500 (6.0mL)	\$0.16
Puff Bar Max (8.0mL)	\$0.13

This approach is also inconsistent with a growing number of international precedents.

Vaping Tax Outside of Canada

- **In the United States**, there is no excise tax required at the Federal level. Twenty-two States have not imposed an excise tax on vaping products. Thirteen states have chosen to levy a vaping excise tax on a per-milliliter basis (on either closed systems or on the entire vaping category). For example, the state of North Carolina which imposes a \$0.05 tax on each milliliter of vaping liquid, and the state of Ohio imposes a similar tax at the rate of \$0.10/mL.
- **In the EU**, vaping products are not currently covered by the Excise Duty Directive (2011). Around half of Member States choose to apply a vaping tax (Portugal, Romania, Slovenia, Latvia, Estonia, Sweden,

¹⁰<https://www.fda.gov/news-events/press-announcements/national-survey-shows-encouraging-decline-overall-youth-e-cigarette-use-concerning-uptick-use>

¹¹ <https://tobaccocontrol.bmj.com/content/early/2021/05/11/tobaccocontrol-2020-056362>

Lithuania, Poland, Hungary, Finland, Greece, Italy and Croatia) - all of whom levy the tax on a 'per mL' basis.

The European Commission is also currently consulting on tobacco excise taxation, and the options proposed for comment are setting a minimum excise tax on a per mL basis at: none, €0.1/mL, or €0.3/mL.

- In Poland, the excise tax on vaping products is calculated per milliliter at €0.12 EUR per 1mL (compared to €59.44 EUR per KG of tobacco used in HnB).
- In Italy, the excise tax on liquid for vaping products is capped at 15% of the rate used for combustible cigarettes.
- Globally, no country that imposes a vaping product excise tax on a per milliliter basis employs the fractional cliff structure as seen in the Finance Canada proposal.¹²

A Harmonized Framework

The reduction in price differential between cigarettes and vaping products varies across provinces and territories. Appendix 1 illustrates the mean prices of cigarettes and two of the major vaping product brands in Canada, as of May 2021. Cigarette prices vary across the provinces, due to differences in tobacco control policy. As a result, the price of vaping liquid as a percentage of a pack of cigarettes varies widely. For example, in Ontario, the mean cost of a pack of 20 cigarettes (including excise and all provincial taxes) is \$13.80; a single JUULpod is currently 43% of this price, while a Vuse ePod is 57% of this price. Adding the proposed excise tax increase, a JUULpod becomes 51% of the price and a Vuse ePod increases to 65% of the price. The most stark example, however, is in Quebec, where the average price of a pack of 20 cigarettes (including excise and all provincial taxes) is \$10.72, the proposed regulations lead to a JUULpod increasing from 56% of this price to 67% and a Vuse ePod increasing from 75% to 86%. Due to own-price elasticity for vaping products being higher than that of combustible cigarettes¹³, any decrease in the gap between cigarette and vaping product prices will push vaping product users back to cigarettes.

Finance Canada should consider a Federal-Provincial-Territorial (FPT) Agreement, similar to the existing agreement used for the cannabis excise stamp system.¹⁴ An FPT Agreement could maintain vaping products tax rates within a specified range of cigarette taxation rates in each province; e.g., 5% and 10%. This is similar to the approach taken in Italy, where the excise tax on liquid for vaping products is capped at 15% of the rate used for combustible cigarettes. An FPT Agreement for vaping products would help avoid a highly complicated, patchwork system of ever changing prices for vaping products across provinces, ensure harm

¹² <http://www.smoke-free.ca/SUAP/2020/e-cigarette-tax.pdf>

¹³ <https://pubmed.ncbi.nlm.nih.gov/29363611/>

¹⁴ https://www.canada.ca/en/department-finance/news/2017/12/background_federal-provincial-territorial-agreement-on-cannabista.html

reduction and avoid pushing people back to cigarettes. A harmonized system is key to avoiding illicit trade, including cross border illicit trade.

Excise Stamp Implementation and Other Excise Duty Regime Matters

Excise stamps have served as a means of evidencing that duty has been paid on packaged cigarettes and cannabis products in Canada with the intention to hinder illicit trade, streamline compliance checks and promote consumer trust. Finance Canada should be mindful of the ability to administer and enforce any excise stamp regime as well as take into account the additional cost and time imposed on vaping manufacturers and distributors.

There are areas of excise stamp implementation that we hope are closely considered to ensure a smooth transition for vaping products in Canada. An ample implementation timeline and exact specifications about the size, placement and material of the new stamps is critical to allow manufacturers to redesign packaging to accommodate new requirements. Both commercial and government stakeholders will need to commit to various new investments and procedures to implement new excise duty stamps. If there is to be a FPT Agreement, the potential of which was indicated by the Finance Canada proposal, additional time should be provided as this will significantly split logistical requirements for compliance. JLC respectfully submits that, in light of the design, manufacturing and logistical reality it will face in order to affix the excise stamps, an official transition period of at least 180 days should be provided, from the time draft legislation detailing the rules is introduced.

An additional consideration in regards to implementation of excise stamps is that closed-system vaping products are typically imported, unlike most cannabis products in Canada. This reality, which resembles the import of tobacco products, should be taken into consideration when designing implementation timelines, application and enforcement. There are four areas to highlight: 1) the excise duty regime should provide for the delivery, transport and affixing of the excise stamps outside of Canada; 2) the licensee should be allowed to possess unstamped vaping products; 3) the excise duty regime should allow for an unlicensed third party, including licensee's affiliates or third parties contractors, to be in possession of excise stamps for the purposes of affixing the excise stamps on vaping products on behalf of the licensee; and 4) the excise duty regime should allow a licensee that imports unstamped packaged vaping products into Canada not to be required to stamp the product until it leaves the licensee's premises for sale into the duty-paid market.

Furthermore, we respectfully submit that the legislation governing the excise duty regime should make it clear that 1) a licensee is permitted to purchase vaping products from foreign unlicensed suppliers for import into Canada, and 2) the payment of excise duty in respect of imported vaping products that are not fully packaged

for retail sale to a final adult consumer should be deferred until such time that the fully packaged vaping products are delivered by the licensee who fully packaged the vaping products to a purchaser.

An FPT Agreement, a considered implementation guidance and a clear 'per mL' duty would achieve all the balanced objectives of the TVPA: discourage persons who do not already use nicotine products to start, while encouraging adult combustible cigarette consumers to switch to less harmful options.

Harmonizing Tobacco Control Strategies

The proposed excise tax should not be considered in a vacuum of other impending tobacco control regulations; in 2021 Health Canada will decrease the nicotine concentration available in vaping products, and limit the flavours available for sale in vaping liquids, two attributes sought by adult smokers looking to transition. Additionally, the nicotine concentration decrease may contribute to increased consumption of e-liquid by adults who use vaping products and the regulations limiting the flavours allowed for sale in vaping products may increase the desire for non-compliant flavoured products. Additionally, the significant price change for pod-based and small tank disposable products may further encourage non-compliance and an illicit market. All of these changes make: 1) combustible cigarettes the most efficient and appealing nicotine delivery source, 2) the price differential between combustible cigarettes and vaping products significantly narrowed, 3) illicit or non-compliant products the cheapest and most appealing vaping products. Increased liquid consumption and use of illicit products are both factors that increase the potential harm of using vaping products, thus a risk-proportionate tax structure should steer adults away from increasing their liquid consumption as well as from the illicit market.¹⁵

Conclusion

As we move forward towards resetting our company and the vaping products category, we remain committed to a positive, collaborative approach with Finance Canada. We will share ideas and address concerns, and we will continue to offer solutions to fully realize the historic harm reduction opportunity before us. We hope Finance Canada considers a pure 'per mL' tax, a considerable implementation timeline and an FPT Agreement in order to achieve all the balanced objectives of the TVPA. JLC supports Health Canada's goal to reduce tobacco use to less than 5% by 2035 and shares Canada's Tobacco Strategy goal to "protect the health of young people and nonsmokers from the dangers of tobacco use." We support a risk-proportionate regulatory framework in Canada that guards against appeal of and access to all tobacco and nicotine products for underage users, while facilitating adults who smoke to transition to less harmful products. We are committed to working with governments, regulators, and other stakeholders in Canada to create a responsibly regulated and adequately safeguarded vaping product category and thank the Finance Department for its consideration.

¹⁵ <https://academic.oup.com/ntr/article/20/8/998/4004823>

APPENDIX

PROVINCE/ TERRITORY	CURRENT MEAN PRICE OF 20 CIGARETTES	CURRENT PRICE PER JUULPOD	PROPOSED PRICE PER JUULPOD	CURRENT PRICE PER VUSE EPOD	PROPOSED PRICE PER VUSE EPOD	CURRENT PRICE 30ML BOTTLE OF E-LIQUID	PROPOSED PRICE 30 ML BOTTLE OF E- LIQUID
ALBERTA	\$14.46	\$5.51	\$6.56	\$7.34	\$8.39	\$20.99	\$24.14
BRITISH COLUMBIA	\$15.31	\$6.61	\$7.87	\$8.81	\$10.07	\$25.19	\$28.97
MANITOBA	\$15.62	\$5.88	\$7.00	\$7.83	\$8.95	\$22.39	\$25.75
NEW BRUNSWICK	\$15.54	\$6.03	\$7.18	\$8.04	\$9.19	\$22.99	\$26.44
NEWFOUNDLAND & LABRADOR*	\$15.54	\$7.24	\$8.62	\$9.65	\$11.03	\$27.59	\$31.73
NORTHWEST TERRITORIES*	\$13.48	\$5.51	\$6.56	\$7.34	\$8.39	\$20.99	\$24.14
NOVA SCOTIA**	\$15.54	\$6.15	\$7.30	\$8.73	\$9.88	\$40.24	\$43.69
NUNAVUT*	\$13.40	\$5.51	\$6.56	\$7.34	\$8.39	\$20.99	\$24.14
ONTARIO	\$13.80	\$5.93	\$7.06	\$7.90	\$9.03	\$22.59	\$25.98
PRINCE EDWARD ISLAND	\$15.54	\$5.51	\$6.56	\$7.34	\$8.39	\$20.99	\$24.14
QUEBEC	\$10.72	\$6.03	\$7.18	\$8.04	\$9.19	\$22.98	\$26.43
SASKATCHEWAN	\$15.48	\$6.61	\$7.87	\$8.81	\$10.07	\$25.19	\$28.97
YUKON*	\$13.61	\$5.51	\$6.56	\$7.34	\$8.39	\$20.99	\$24.14

Cigarette prices were based on the mean sale price of a package of 20 cigarettes in each province covered by Nielsen reporting for the period April 2021-May 2021. Where unavailable, values were taken from Physicians for a Smoke-Free Canada's best estimates*. Presented mean cigarette prices are inclusive of Federal and Provincial Tobacco and Sales Taxes. JUULPod prices were based on the current MSRP of \$20.99 per 4-pack. Vuse ePod prices were based on the current MSRP of \$13.99 per 2-pack. It was assumed the MSRP of a 30mL bottle of e-liquid was \$19.99. Vaping product prices include Federal and Provincial Sales and Vaping Taxes, where administered.

** Nova Scotia currently has a \$0.50/mL tax, this was added to the MSRP pre-sales tax