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# **Explanatory Notes Relating to Regulatory and Legislative Proposals Relating to the Taxation of Cannabis**

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Published by  
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Minister of Finance

September 2018



## **Preface**

These explanatory notes describe the proposed *Excise Duties on Cannabis Regulations* and amendments to related regulations and legislation. These explanatory notes describe these proposed amendments, clause by clause, for the assistance of Members of Parliament, taxpayers and their professional advisors.

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These notes are intended for information purposes only and should not be construed as an official interpretation of the provisions they describe.

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## PART 1

### DRAFT EXCISE DUTIES ON CANNABIS REGULATIONS

#### Clauses 1 to 5

#### Excise Duties on Cannabis Regulations

The *Excise Duties on Cannabis Regulations* (the Regulations) are proposed to be made. The sections of the Regulations are described in the following commentary.

#### Section 1 – Definitions

Section 1 of the Regulations defines terms used in the Regulations.

Section 1 is deemed to have come into force on Announcement Date.

#### “Act”

The definition “Act” in section 1 of the Regulations means the *Excise Act, 2001*.

#### “base amount”

If a cannabis product is delivered or made available to a person that obtains it otherwise than by means of a purchase, the definition “base amount” in section 1 of the Regulations means, in respect of the cannabis product and a listed specified province (see commentary for the definition “listed specified province”), the fair market value of the cannabis product.

In any other case, it means the amount upon which a portion of the amount of the additional cannabis duty in respect of the listed specified province may be calculated, where the additional cannabis duty is imposed under subsection 158.2(1) or 158.27(1) of the Act on cannabis products produced in Canada (see commentary for subsection 5(2) of the Regulations and the commentary for Schedules 1 to 12 to the Regulations).

The base amount in respect of a cannabis product and a listed specified province, as specified by the formula in the definition, is determined by multiplying a particular amount by a percentage.

The particular amount is determined by subtracting two amounts from an amount that is generally equal to the amount of consideration for a sale of the cannabis product on which the Goods and Services Tax (GST) or the Harmonized Sales Tax (HST) is applied in respect of that sale, and may also include additional amounts in certain circumstances such as when an additional consideration, as determined for the purposes of the GST/HST, for a container in which the cannabis product is contained is charged to the purchaser. The first amount that is subtracted from the amount of consideration to determine the particular amount is the amount determined in respect of the cannabis product under section 1 of Schedule 7 to the Act, which is the amount of duty imposed on the cannabis product under subsection 158.19(1) of the Act. The second amount that is subtracted from the amount of consideration to determine the particular

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amount is the amount determined in respect of the cannabis product under section 1 of the corresponding schedule for the listed specified province.

The percentage represents the percentage that is obtained by dividing 100% by the total of (1) 100%, and (2) the additional cannabis duty adjustment rate percentage (see commentary for the definition “listed specified province”), which is set out in section 5 of the corresponding schedule for the listed specified province.

*“listed specified province”*

The new definition “listed specified province” lists provinces and territories that have entered into an agreement with Canada in respect of the coordination of cannabis taxation and that have requested an adjustment to the additional cannabis duty to reflect in whole or in part differences between the general sales tax rate applied to cannabis in the province and the highest prevailing general provincial sales tax rate, or rate of the provincial component of the HST, in Canada. The listed specified provinces are Ontario, New Brunswick, Prince Edward Island, Alberta, Saskatchewan, Newfoundland and Labrador, and Nunavut.

#### Section 2 – Cannabis product – exclusions

Section 2 of the Regulations provide that, for the purposes of the definition “cannabis product” in section 2 of the Act, the following substances, materials or things are not included in that definition:

- a test kit, as defined in subsection 2(1) of the *Narcotic Control Regulations*, that contains cannabis and for which a registration number has been issued, but not cancelled, under these regulations; and
- a reference standard – a highly purified and standardized form of a given substance used as a measurement base to confirm the identity, strength, quality or purity of a substance – that contains a known quantity or concentration of a chemical component of cannabis, such as cannabidiol, cannabidiolic acid, delta-9-tetrahydrocannabinolic acid or THC (as defined in section 2 of the Act), that is designed to be used during the course of a chemical or analytical procedure for a medical, laboratory, industrial, educational, law administration or enforcement, or research purpose, and the contents of which are not intended to be consumed or administered.

Section 2 is deemed to have come into force on June 21, 2018.

As of October 17, 2018, however, the above description of a test kit will be replaced. From that date, a test kit will only be excluded from the definition “cannabis product” in section 2 of the Act if it is a test kit as defined in subsection 1(2) of the *Cannabis Regulations* for which a registration number has been issued, but not cancelled, under these regulations. It should be noted that paragraph 159(6)(a) of the *Cannabis Act* has the effect of deeming a registration number issued under the *Narcotic Control Regulations* that applies to a test kit that contains cannabis to be, as of October 17, 2018, a registration number issued under the *Cannabis Regulations* until the registration number is cancelled.

### Section 3 – Dutiable amount

Subsection 3(1) of the Regulations sets out the prescribed percentages in respect of the specified provinces (see commentary for section 4 of the Regulations) for the purposes of subparagraph (i) of the description of C in paragraph (a) of the definition “dutiable amount” in section 2 of the Act. That subparagraph states that the dutiable amount in respect of a cannabis product is to be adjusted by a prescribed percentage in respect of a specified province if additional cannabis duty in respect of the specified province is imposed on the cannabis product.

The prescribed percentage in respect of a listed specified province is equal to the total of the percentage set out in section 2 of the corresponding schedule for the listed specified province, and the percentage set out in section 5 of the corresponding schedule for the listed specified province.

The prescribed percentage in respect of a specified province that is not a listed specified province is equal to the percentage set out in section 2 of the corresponding schedule for the specified province.

Subsection 3(2) sets out prescribed circumstances and a prescribed amount for the purposes of paragraph (b) of the definition “dutiable amount” in section 2 of the Act. If a cannabis product is delivered or made available in a specified province to a person that obtains it otherwise than by means of a purchase and if an amount in respect of the cannabis product is to be determined under any of sections 2 and 6 of Schedules 1, 4, 6 to 9 and 12 and section 2 of Schedules 2, 3, 5, 10 and 11, the dutiable amount of the cannabis product is equal to the fair market value of the cannabis product

Section 3 is deemed to have come into force on Announcement Date.

### Section 4 – Specified province

Section 2 of the Act defines a “specified province” as a province prescribed by regulations. Provinces that have entered into an agreement with Canada in respect of the coordination of cannabis taxation would be prescribed for the purposes of this definition.

Section 4 of the Regulations prescribes the following provinces and territories for the purposes of that definition: Ontario, Quebec, Nova Scotia, New Brunswick, British Columbia, Prince Edward Island, Alberta, Saskatchewan, Newfoundland and Labrador, Yukon, the Northwest Territories and Nunavut.

Section 4 is deemed to have come into force on Announcement Date.

### Section 5 – Prescribed circumstances and amount – subsections 158.2(1) and 158.27(3) of Act

Section 5 of the Regulations prescribes certain rules for the purposes of subsections 158.2(1) and 158.27(3) of the Act.

Subsection 158.2(1) imposes a duty in respect of a specified province on cannabis products produced in Canada in circumstances prescribed by regulations in the amount determined in a

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manner prescribed by regulations. This duty is payable by the cannabis licensee that packaged the cannabis product at the time it is delivered to a purchaser.

Subsection 158.27(3) imposes a duty in respect of a specified province on cannabis products that are produced in Canada and delivered to a purchaser before commencement day for sale or distribution on or after that day. This duty is imposed in circumstances prescribed by regulations in the amount determined in a manner prescribed by regulations, and is payable on commencement day by the cannabis licensee that packaged the cannabis products. Commencement day means October 17, 2018, the day on which subsection 204(1) of the *Cannabis Act* comes into force, and it represents the day on which adults will start to be able to legally purchase and possess cannabis subject to conditions under the *Cannabis Act*.

Subsection 5(1) prescribes the circumstances in which a duty under subsection 158.2(1) or 158.27(1) is imposed. For the purposes of subsections 158.2(1) and 158.27(3), a duty in respect of a specified province is imposed under those subsections on cannabis products produced in Canada if the cannabis products are for consumption in the specified province, use in the specified province or sale to consumers in the specified province.

Subsection 5(2) prescribes the amount of duty imposed under subsection 158.2(1) or 158.27(3). For the purposes of subsections 158.2(1) and 158.27(3), the amount of duty imposed under those subsections in respect of cannabis products produced in Canada and in respect of a specified province is, where the specified province is a listed specified province, an amount that is equal to the total of:

- the greater of the amount determined in respect of the cannabis products under sections 1 and 2 of the corresponding schedule for the specified province; and
- whichever of the following amounts is applicable:
  - the amount determined in respect of the cannabis products under section 5 of the corresponding schedule for the specified province if the amount determined in respect of the cannabis products under section 1 of that schedule is greater than the amount determined in respect of the cannabis products under section 2 of that schedule; and
  - the amount determined in respect of the cannabis products under section 6 of the corresponding schedule for the specified province, in any other case.

Where the specified province is not a listed specified province, the amount of duty imposed under those subsections of the Act is equal to the greater of the amounts determined in respect of the cannabis products under sections 1 and 2 of the corresponding schedule for the specified province.

Section 5 is deemed to have come into force on Announcement Date.

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### Section 6 – Prescribed circumstances and amount – subsection 158.22(1) of Act

Section 6 of the Regulations prescribes certain rules for the purposes of subsection 158.22(1) of the Act.

Section 158.22 imposes a duty in respect of a specified province on imported cannabis products in circumstances prescribed by regulations in the amount determined in a manner prescribed by regulations. This additional duty on imported cannabis products is payable by the importer or owner or another person that is liable under the *Customs Act* to pay duty levied under section 20 of the *Customs Tariff* on the cannabis product or that would be liable to pay that duty if they were subject to that duty.

Subsection 6(1) prescribes the circumstances in which a duty under subsection 158.22(1) is imposed. For the purposes of subsection 158.22(1), a duty in respect of a specified province is imposed under that subsection on imported cannabis products if the person that is liable under subsection 158.22(2) to pay the duty is resident in the specified province.

Subsection 6(2) provides that for the purposes of determining residency as per subsection 6(1), a person is deemed to be resident in a province if the person is deemed under section 132.1 of the *Excise Tax Act* to be resident in that province for the purposes of Part IX of that Act.

Subsection 6(3) prescribes the amount of duty imposed under subsection 158.22(1). For the purposes of subsection 158.22(1), the amount of duty imposed under that subsection in respect of imported cannabis products and in respect of a specified province is, where the specified province is a listed specified province, an amount that is equal to the total of:

- the greater of the amounts determined in respect of the cannabis products under sections 1 and 3 of the corresponding schedule for the specified province; and
- the amount determined in respect of the cannabis products under section 7 of the corresponding schedule for the specified province.

Where the specified province is not a listed specified province, the amount of duty imposed under that subsection of the Act is equal to the greater of the amounts determined in respect of the cannabis products under sections 1 and 3 of the corresponding schedule for the specified province.

Section 6 is deemed to have come into force on Announcement Date.

### Section 7 – Prescribed circumstances and amount – subsections 158.25(2) and 158.26(2) of Act

Section 7 of the Regulations prescribes certain rules for the purposes of subsections 158.25(2) and 158.26(2) of the Act.

Subsection 158.25(2) provides that if cannabis products are taken for use, then a duty in respect of a specified province is imposed on the cannabis products in circumstances prescribed by regulations in the amount determined in a manner prescribed by regulations. This duty is payable

at the time the cannabis products are taken for use by the person responsible for the cannabis products at that time.

Subsection 158.26(2) provides that if the person that is responsible at a particular time for cannabis products cannot account for the cannabis products as being, at the particular time, in the possession of a cannabis licensee or in the possession of another person in accordance with subsection 158.11(3) or paragraph 158.11(5)(a) of the Act, then a duty in respect of a specified province is imposed on the cannabis products in circumstances prescribed by regulations in the amount determined in a manner prescribed by regulations. This duty is payable by the person responsible for the cannabis products at the time the cannabis products cannot be accounted for.

Subsection 7(1) prescribes the circumstances in which a duty under subsection 158.25(2) is imposed. For the purposes of subsection 158.25(2), a duty in respect of a specified province is imposed under that subsection on cannabis products if the location of the cannabis products at the time at which the cannabis products are taken for use is in the specified province.

Subsection 7(2) prescribes the circumstances in which a duty under subsection 158.26(2) is imposed. For the purposes of subsection 158.26(2), a duty in respect of a specified province is imposed under that subsection on cannabis products that cannot be accounted for if the last known location of the cannabis products before the time at which the cannabis products cannot be accounted for is in the specified province.

Subsection 7(3) prescribes the amount of duty imposed under subsection 158.25(2) or 158.26(2). For the purposes of subsections 158.25(2) and 158.26(2), the amount of duty imposed under those subsections in respect of cannabis products and a specified province is, where the specified province is a listed specified province, an amount that is equal to the total of:

- the greater of the amounts determined in respect of the cannabis products under sections 1 and 4 of the corresponding schedule for the specified province; and
- the amount determined in respect of the cannabis products under section 8 of the corresponding schedule for the specified province.

Where the specified province is not a listed specified province, the amount of duty imposed under those subsections is equal to the greater of the amounts determined in respect of the cannabis products under sections 1 and 4 of the corresponding schedule for the specified province.

Section 7 is deemed to have come into force on Announcement Date.

#### Section 8 – Prescribed specified provinces – offences

Section 8 of the Regulations prescribes the specified provinces for the purposes of section 218.1 of the Act. Section 218.1 provides that any person that contravenes section 158.11 of the Act (selling unstamped cannabis) or 158.12 of the Act (sale or distribution by a licensee) is guilty of an offence and is liable to a fine or imprisonment or both.

Section 218.1 provides for particular methods for determining the minimum amount and maximum amount of this fine in the case where the offence occurs in a specified province that is prescribed by regulation. Section 8 provides that the listed specified provinces are prescribed for this purpose.

Section 8 comes into force on the day on which the Regulations are published in the *Canada Gazette*.

#### Section 9 – Prescribed specified provinces – penalties

Section 9 of the Regulations sets out which specified provinces are prescribed for the purposes of sections 233.1, 234.1 and 238.1 of the Act. Section 233.1 provides that a cannabis licensee that contravenes section 158.13 of the Act (packaging and stamping of cannabis) is liable to a penalty. Section 234.1 provides that any person that contravenes section 158.02 (production of cannabis products without a license), section 158.1 (prohibition regarding cannabis products for sale, etc.) or that sells or offers to sell cannabis products in contravention of sections 158.11 (selling unstamped cannabis) or 158.12 (sale or distribution by a licensee) of the Act is liable to a penalty. Section 238.1 provides that a person to whom excise stamps are issued is liable to a penalty if the person cannot account for the stamps as being in their possession.

Each of these sections of the Act provides for particular methods for determining the amount of the penalty in the case where the contravention occurs in a specified province that is prescribed by regulations. Section 9 provides that the listed specified provinces are prescribed for these purposes.

Section 9 is deemed to have come into force on Announcement Date except that, before October 17, 2018, section 9 is to be read without reference to “paragraph (a) of the description of C in section 234.1 of the Act”.

#### Schedules 1-12 – Rates of additional cannabis duty

Schedules 1 to 12 to the Regulations provide rules that are used in determining the amount that is prescribed for the purposes of the duty imposed on cannabis products in respect of the specified provinces under various sections of the Act. There is one schedule for each of the specified provinces.

Section 1 of each of the Schedules calculates an amount in respect of a cannabis product produced in Canada or imported that is equal to the total of:

- a dollar amount (\$0.75 as of October 17, 2018) multiplied by the quantity of flowering material, in grams, included in the cannabis product,
- a dollar amount (\$0.225 as of October 17, 2018) multiplied by the quantity of non-flowering material, in grams, included in the cannabis product,
- a dollar amount (\$0.75 as of October 17, 2018) multiplied by the number of viable seeds included in the cannabis product, and

- a dollar amount (\$0.75 as of October 17, 2018) multiplied by the number of vegetative cannabis plants included in the cannabis product.

The amounts calculated under section 1 are used in the determination of amounts under subsections 4(2), 5(3) and 6(3) of the Regulations for the purposes of subsections 158.2(1), 158.22(1), 158.25(2), 158.26(2) and 158.27(3) of the Act.

Section 2 of each of the Schedules calculates an amount in respect of a cannabis product produced in Canada that is equal to the dutiable amount of the cannabis product multiplied by a percentage (7.5% as of October 17, 2018). The amounts calculated under section 2 are used in the determination of amounts under subsection 4(2) of the Regulations for the purposes of subsections 158.2(1) and 158.27(3) of the Act.

Section 3 of each of the Schedules calculates an amount in respect of an imported cannabis product that is equal to the value of the cannabis product multiplied by a percentage (7.5% as of October 17, 2018). The amounts calculated under section 3 are used in the determination of amounts under subsection 5(3) of the Regulations for the purposes of subsection 158.22(1) of the Act.

Section 4 of each of the Schedules calculates an amount in respect of a cannabis product taken for use or unaccounted for that is equal to the fair market value of the cannabis product multiplied by a percentage (7.5% as of October 17, 2018). The amounts calculated under section 4 are used in the determination of amounts under subsection 6(3) of the Regulations for the purposes of subsections 158.25(2) and 158.26(2) of the Act.

The schedules for specified provinces that are not listed specified provinces contain only the four sections described above. The schedules for specified provinces that are listed specified provinces contain the four sections described above as well as sections 5 to 8 as described below. The schedules for listed specified provinces indicating amounts to be multiplied by 0% for sections 5 to 8 signify provinces that currently have the highest prevailing general sales tax rate, or rate of the provincial component of the HST, in Canada. Nonetheless, these provinces have requested an adjustment to the additional cannabis duty should a difference occur in the future between the general provincial sales tax rate, or rate of the provincial component of the HST, in the province and the highest prevailing general provincial sales tax rate, or rate of the provincial component of the HST, in Canada.

Section 5 of each of the Schedules for a listed specified province calculates an amount in respect of a cannabis product produced in Canada that is equal to the base amount for the cannabis product multiplied by a percentage. Section 6 of each of the Schedules for a listed specified province calculates an amount in respect of a cannabis product produced in Canada that is equal to the dutiable amount for the cannabis product multiplied by a percentage. The amounts calculated under sections 5 and 6 are used in the determination of amounts under subsection 4(2) of the Regulations for the purposes of subsections 158.2(1) and 158.27(3) of the Act.

Section 7 of each of the Schedules for a listed specified province calculates an amount in respect of an imported cannabis product that is equal to the value of the cannabis product multiplied by a

percentage. The amounts calculated under section 7 are used in the determination of amounts under subsection 5(3) of the Regulations for the purposes of subsection 158.22(1) of the Act.

Section 8 of each of the Schedules for a listed specified province calculates an amount in respect of a cannabis product taken for use or unaccounted for that is equal to the fair market value of the cannabis product multiplied by a percentage. The amounts calculated under section 8 are used in the determination of amounts under subsection 6(3) of the Regulations for the purposes of subsections 158.25(2) and 158.26(2) of the Act.

## **PART 2**

### **DRAFT AMENDMENTS TO THE REGULATIONS RESPECTING THE POSSESSION OF TOBACCO PRODUCTS OR CANNABIS PRODUCTS THAT ARE NOT STAMPED**

#### **Clauses 6 and 7**

#### **Prescribed persons and conditions**

Regulations Respecting the Possession of Tobacco Products or Cannabis Products That Are Not Stamped

1.3

The *Regulations Respecting the Possession of Tobacco Products or Cannabis Products That Are Not Stamped* identify the classes of persons that may possess unstamped tobacco products and cannabis products and the conditions under which the possession of unstamped tobacco products or cannabis products by those persons may occur.

New section 1.3 of these regulations provides that, for the purposes of paragraph 158.11(6)(a) of the *Excise Act, 2001*, a person may possess cannabis products in a particular specified province that are not stamped to indicate that additional cannabis duty in respect of the particular specified province has been paid if

- the person holds a licence for sale for medical purposes issued under section 62 of the *Cannabis Act*; or
- the following conditions are met:
  - the person is authorized by another province to sell cannabis products in the other province; and
  - if the other province is a specified province, the cannabis products are stamped to indicate that additional cannabis duty in respect of the other province has been paid.

These amendments come into force, or are deemed to have come into force, on October 17, 2018.

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### PART 3

#### DRAFT AMENDMENTS TO THE STAMPING AND MARKING OF TOBACCO AND CANNABIS PRODUCTS REGULATIONS

##### Clauses 8 and 9

##### Prescribed persons

Stamping and Marking of Tobacco and Cannabis Products Regulations

4

Subsection 4(3) of the *Stamping and Marking of Tobacco and Cannabis Products Regulations* provides rules for determining who is a prescribed person for the purposes of paragraph 158.05(2)(c) of the *Excise Act, 2001* (the Act). That paragraph of the Act provides an exception to the general prohibition for a person to possess a cannabis excise stamp that has not been affixed to a cannabis product or its container. Under subsection 4(3), a prescribed person is a person that transports a cannabis excise stamp on behalf of the person that lawfully produced the cannabis excise stamp or the person to which the cannabis excise stamp is issued.

Subsection 4(3) is amended to add a person that has in their possession a cannabis excise stamp only for the purpose of applying adhesive to the stamp on behalf of the cannabis licensee to which the cannabis excise stamp is issued as another exception for the purposes of paragraph 158.05(2)(c).

This amendment is deemed to have come into force on June 21, 2018.

### PART 4

#### DRAFT AMENDMENTS TO THE CREDIT FOR PROVINCIAL RELIEF (HST) REGULATIONS

##### Clauses 10 and 11

##### Definition “Ontario regulation”

Credit for Provincial Relief (HST) Regulations

1

Section 1 of the *Credit for Provincial Relief (HST) Regulations* defines terms used in these regulations. The existing definition “Ontario regulation” in section 1 refers to Ontario provincial regulation 317/10 entitled *Rebates for First Nations in Ontario*.

That definition is amended consequential to Ontario’s decision, as announced by the province on March 28, 2018, to exclude off-reserve purchases of recreational cannabis, once legalized, from the relief offered by Ontario for the provincial component of the Harmonized Sales Tax. Such relief is generally available in respect of a supply of qualifying property or services made in

Ontario to an Indian, a band or a council of a band (as defined in the *Indian Act*, R.S.C. 1985, c. I-5). Following Ontario's announcement, Ontario made corresponding changes to the provincial regulation. As a consequence of those changes, this amendment amends the definition "Ontario regulation" to update the date as of which the provincial regulation is to be read (in order that the definition refers to the newly modified provincial regulation).

This amendment comes into force, or is deemed to have come into force, on the day that is the later of October 17, 2018 and the day on which section 2 of Ontario Regulation 382/18, made under the *Retail Sales Tax Act*, R.S.O. 1990, c. R.31, comes into force.

## PART 5

### DRAFT AMENDMENTS TO THE EXCISE ACT, 2001

#### Clause 12

#### Dutiable amount

EA, 2001

2.1

New section 2.1 of the *Excise Act, 2001* sets out rules that apply in determining an amount of consideration for the purposes of the definition "dutiable amount" in section 2 of that Act. The concept of consideration as determined for the purposes of Part IX of the *Excise Tax Act*, which relates to the goods and services tax/harmonized sales tax, is relevant for the determination of the dutiable amount in respect of a cannabis product. The dutiable amount is itself used to determine the amount of an *ad valorem* duty on the cannabis product.

New paragraph 2.1(a) provides that if a provision of Part IX of the *Excise Tax Act* deems the consideration, or part of the consideration, for a supply not to be consideration for the supply, a supply to be made for no consideration or a supply not to have been made by a person, then that deeming does not apply for the determination of an amount of consideration for the purposes of the definition "dutiable amount".

New paragraph 2.1(b) provides that, in determining an amount of consideration for the purposes of the definition "dutiable amount", subsection 155(1) of the *Excise Tax Act* is to be read without reference to the words "and the recipient of the supply is not a registrant who is acquiring the property or service for consumption, use or supply exclusively in the course of commercial activities of the recipient,".

New section 2.1 is deemed to have come into force on Announcement Date.