

13.

SERVICE NOVA SCOTIA AND MUNICIPAL RELATIONS - FUEL AND TOBACCO TAX

BACKGROUND

13.1 The Department of Service Nova Scotia and Municipal Relations (SNSMR) is responsible for administering the Revenue Act. Under the Act, the Department administers taxes on tobacco products, gasoline and diesel oil (fuel), and the private purchase of designated tangible personal property (e.g., motor vehicles, boats and aircraft). Total revenue received under these three taxes for the year ended March 31, 2002 was \$327.4 million (see Exhibit 13.2 on page 217).

13.2 Tobacco wholesalers (including manufacturers) are designated under the Act as collectors and remitters of tobacco tax. These taxes are paid to the Province by the wholesalers based on sales of tobacco products to retailers. The taxes are factored into the price of tobacco products and are ultimately passed on to the consumer. In 2001-02, tobacco tax revenue totaled \$105.7 million, of which \$92.2 million (87%) was remitted by the six largest wholesalers.

13.3 In accordance with Federal legislation, sales of tobacco on native reserves to status Indians are exempt from tax. The government requires special marking of packaging to distinguish tax-free from taxable tobacco.

13.4 Similarly, fuel oil companies are designated under the Act as collectors and remitters of fuel taxes. These taxes are paid by the companies based on sales of taxable gasoline or diesel oil products to retailers and consumers. The taxes are factored into the price of fuel and are ultimately passed on to the consumer. In 2001-02, gasoline and diesel fuel tax totaled \$207.9 million, \$198.4 million (96%) of which was remitted by the six largest fuel oil companies.

13.5 Gasoline and diesel fuel used in certain circumstances is not taxed. Tax-exempt fuel can be used to operate qualified machinery in designated activities such as lumbering, farming, fishing and aquaculture. Tax-exempt fuel can also be used by the Department of Transportation and Public Works, fire departments, municipal governments, as well as in certain marine applications. To distinguish it from taxable fuel, tax-exempt fuel is dyed (marked). Companies or individuals must obtain a consumer exemption permit to be allowed to purchase marked fuel.

13.6 The government's partnership with the Federal government in the collection of Harmonized Sales Taxes (HST) is not addressed by the Revenue Act. Except for HST owing on vehicles purchased outside of a province participating in the harmonized sales tax program, Canada Customs and Revenue Agency administers HST and remits Nova Scotia's share to the Province. Service Nova Scotia and Municipal Relations and the Nova Scotia Department of Finance liaise with the Federal government on this matter.

RESULTS IN BRIEF

13.7 The following are our principal observations from this audit.

- The Department has a broad mandate under the Revenue Act and Regulations. We did not observe any unmet legislative requirements.

- Control over the processing of tax payments needs strengthening. We observed deficiencies relating to segregation of duties, recording and security of money received, and reconciliations of deposits to accounting records.
- We noted tax returns with incomplete or missing supporting schedules and insufficient details on the calculation of taxes owing, and returns regularly being received after due dates.
- As a result of a 1991 Provincial Court decision, gasoline purchased on a reserve by a status Indian is exempt from Provincial taxes. The government established a process to refund the fuel tax previously paid by band members who purchased fuel from on-reserve gasoline retailers. In July 2002 government reached a tentative agreement with the Eskasoni band to refund band members \$16 million for fuel taxes paid (including interest). The government is negotiating agreements with the remaining 12 bands. The total cost of this rebate program is estimated to be \$19.6 million.
- There are serious deficiencies in the planning, monitoring and documentation of tax audits and inspections, and insufficient auditing of oil company head offices, gasoline retailers and tobacco wholesalers.
- There are reasonable systems and good documentation to support measures taken to pursue infractions of law discovered by the Department.

AUDIT SCOPE

13.8 In November 2002 we completed a broad scope audit at Service Nova Scotia and Municipal Relations. It was conducted in accordance with Section 8 of the Auditor General Act and auditing standards established by the Canadian Institute of Chartered Accountants, and included all tests and other procedures we considered necessary in the circumstances.

13.9 The objective of this assignment was to assess the Department's processing, monitoring, inspection and auditing activities as they relate to the requirements of legislation, regulations and/or policy for tobacco and gasoline and diesel oil taxes. Audit criteria were developed to assist in our assessment of the systems and practices of the Department. The audit criteria were discussed with and accepted as appropriate by senior management of the Department, and are outlined in Exhibit 13.1.

PRINCIPAL FINDINGS

Compliance with Legislation

13.10 The Department has a broad mandate under the Revenue Act and Regulations. Staff and clients of the Department are made aware of changes to the Act and Regulations through distribution of the Act, Regulations, tax bulletins and other communications. This information is also available on the Department's website. Tax bulletins provide the Department's interpretation of the Act and Regulations and announce significant changes.

13.11 We did not observe any unmet legislative requirements.

Processing Tax Returns

13.12 Tobacco wholesalers and fuel oil companies are required to submit monthly returns and remit all taxes collected. Department staff process payments and record them in the Department's online licensing and collection system. A review is performed on returns to analyse and assess the reasonableness of information reported.

13.13 We reviewed the system used to process tax payments received. In our opinion, the system of internal control to process payments needs strengthening. We observed deficiencies relating to segregation of duties, recording and security of money received, and reconciliations of deposits to accounting records.

Recommendation 13.1

We recommend the Department implement an appropriate system of internal control over cash receipts.

13.14 We also noted that the processing of tax payments involves many manual procedures. We encourage the Department to determine the feasibility of computerizing the cash receipts system and integrating it with its licensing and collection system.

13.15 We examined how monthly returns received from tobacco wholesalers and fuel oil companies are processed and checked. We found inadequate documentation of the reviews performed on returns. For example, there are no standard procedures to be performed and minimal records of the actual procedures performed. Review findings and adjustments and related disposition are poorly documented, if at all. There is minimal reconciliation or verification of sales and product transfers between organizations reported in the returns. Also, there is limited, if any, supervision of the work performed by staff conducting the reviews.

Recommendation 13.2

We recommend that the examination of monthly returns be appropriately documented and reviewed, and standards be developed to specify the frequency and nature of the procedures to be performed.

13.16 We examined a sample of monthly tobacco tax returns and fuel tax returns. We noted returns with incomplete or missing supporting schedules and details on the calculation of taxes owing, and returns regularly being received after due dates. We also observed inappropriate delays in recording and depositing tax payments.

Recommendation 13.3

We recommend that the Department ensure returns and tax payments are processed on a timely basis and that all information required on a return is received.

13.17 The Department issues permits to authorize the use of tax-exempt fuel in certain circumstances (see paragraph 13.5). Fuel oil companies submit monthly statements of tax-exempt sales which are examined during the review of monthly tax returns. Certain fish processing plants have been issued a restricted retailer license to sell tax-exempt fuel, and they too submit a monthly statement of tax-exempt sales. However, the statements received from restricted gasoline retailers are reviewed and verified only as time permits.

Recommendation 13.4

We recommend tax-exempt sales statements be reviewed monthly, at least on a sample basis. This process should include checking to see that tax-exempt fuel is only being sold to companies and individuals who have consumer exemption permits.

13.18 Currently, the Department is unable to track and report on tax-exempt sales by individual permit holder. This would be useful in highlighting problems warranting closer attention (e.g., a formal inspection). Current information on the total dollar value of fuel tax exemptions is not available either. The Department has begun to compile a database to record this information, but this data is only being entered as time permits.

13.19 A report on taxes levied under the Revenue Act is prepared monthly to monitor actual and forecasted tax revenue. The report is reviewed by senior staff of SNSMR and the Department of Finance. It includes detailed financial and statistical information. Revenue forecasts are based upon various economic models. Commentary is provided on variances between taxes received and forecasted when the Department is aware of the reasons for the variances.

Sales of Tobacco and Fuel on Native Reserves

13.20 Under Section 87 of the Federal Indian Act, status Indians have the right to purchase tax-exempt tobacco and fuel products for their own use.

13.21 The thirteen First Nation bands in Nova Scotia are allowed a monthly quota of three cartons of tax-exempt cigarettes, identified by peach-coloured tear-tape, and 200 grams of tobacco in any other form for each band member, regardless of age. Only tobacco retailers designated by a band council and operating on a reserve are allowed to sell tax-exempt tobacco products. Tax-exempt tobacco products can only be sold to reserve residents possessing a status Indian card. The courts have determined that this process is a valid means of providing the exemption stipulated under Section 87 of the Indian Act. The annual dollar value of this exemption, as estimated in July 2002, is \$12 million.

13.22 We noted that 19 retail outlets selling tobacco products on two reserves have not been designated by their respective band councils. Management indicated that the Department is actively working with the band councils to establish these designations.

13.23 Band councils designate the tobacco wholesalers from which on-reserve retailers must purchase tax-exempt tobacco products. Tobacco wholesalers so designated are required to submit monthly sales reports to the Department. Staff review monthly sales reports for reasonableness. Reports are generated to help monitor the sale of tax-exempt tobacco products on each reserve. We believe there could be more formal reporting of this information to senior management of the Department.

13.24 As a result of a 1991 Provincial Court decision, gasoline purchased on a reserve by a status Indian is exempt from Provincial taxes. The government is currently collecting fuel tax on such purchases, but is developing a system that will allow band members to purchase tax-exempt gasoline at the point-of-sale on reserves. This system is scheduled to be operational by December 2002. Each band member who possesses a valid Nova Scotia driver's license will be able to purchase up to 400 litres of tax-exempt fuel each month. The total cost of this exemption is estimated to be \$400,000 to \$500,000 per year.

13.25 The Court decision is to be applied retroactively. The government established an interdepartmental committee to develop a process to refund the fuel tax previously paid by band members who purchased fuel from on-reserve gasoline retailers. In July 2002 government reached a tentative agreement with the Eskasoni band to refund band members \$16 million for fuel taxes paid (including interest). The government is negotiating agreements with the remaining 12 bands. The total cost of this rebate program is estimated to be \$19.6 million.

Inspections and Audits

13.26 The Department is authorized by legislation to ensure compliance with the Revenue Act through inspections and audits of tobacco manufacturers, wholesalers and retailers, oil refineries, fuel oil companies, gasoline retailers, users of tax-exempt fuel, as well as interprovincial carriers registered under the International Fuel Tax Agreement (IFTA).

13.27 The Department does not have current policy and procedure manuals for performing audits and inspections (except for those pertaining to IFTA), processing cash receipts, or for guiding tax collection and enforcement practices. Some of the policies and procedures currently being followed are from the sales tax and fuel and diesel oil tax audit manuals of the former Provincial Sales Tax Commission. These manuals have not been updated for several years.

13.28 We also concluded that there are serious deficiencies in the planning and monitoring of inspection and audit assignments. There is no master list of vendors indicating which have been audited or inspected. There is no formal risk-based assessment process to determine audit and inspection frequencies. There is little information available on which projects have been assigned to which staff members, and new permits issued and permits cancelled are not factored into the assignment of projects on a timely basis. We observed instances where establishments have been inspected more than once in a short period of time with no stated rationale, while other establishments go years between visits. We observed that sometimes two officers will perform inspections of small establishments together, and we received no reasonable explanation for this apparent duplication considering the large number of inspections to be done.

13.29 There is no review of past audit or inspection history prior to performing an assignment. There are no due dates set for the completion of assignments and minimal progress reporting on assignments in process. We noted numerous instances of inspection reports not being submitted until long after an assignment commenced. Management was generally unaware of the inordinate length of time taken to finalize some inspections.

13.30 We also observed that time reporting by auditors and compliance officers is inconsistent and lacking in detail. Such reporting is not a formal requirement of the Department and appears to be a voluntary continuation of practices employed by the former Provincial Tax Commission. As a result, management do not regularly review time reports and are often not aware of the exact nature of the work being done by inspection and audit staff. There are no standards on the amount of work (e.g., number of inspections or audits) that would be reasonable for a set period of time. Such standards would help management monitor the productivity of staff.

13.31 When an inspection or audit report has been completed, it receives only a cursory review by management. In our view, the review of inspection and audit reports needs to be more stringent to ensure reports are complete and contain sufficient information to support the conclusions derived. Also, there is no system to ensure that a follow-up inspection occurs when significant irregularities are noted or an officer recommends one for another reason.

Recommendation 13.5

We recommend that the Department implement a formal, comprehensive system for audit/inspection planning, management and quality control.

13.32 Due to lack of technical training or expertise within the audit and inspection staff, oil company head offices and gasoline retailers have not been audited or inspected in several years. Also, only one small tobacco wholesaler has been audited within the last year. Staff efforts have been directed primarily to ensuring that tax revenue owing to the Province from recent tobacco tax increases has been accurately remitted. It is expected that audits of tobacco wholesalers will recommence when the focus on collecting tax-increase revenue is completed.

Recommendation 13.6

We recommend that audits of oil company head offices, gasoline retailers and tobacco wholesalers be performed. Staff should be provided with the training necessary to audit oil company head offices and gasoline retailers, and/or the expertise should be obtained from outside the Department.

13.33 We believe there are benefits to be achieved from a greater use of technology by audit and inspection field staff. Although staff have notebook computers, while out of the office they cannot access information on the establishments they plan to visit, nor can they record the results of their assignments in the systems.

Recommendation 13.7

We recommend that information system improvements be implemented to facilitate a more effective and efficient inspection and audit process.

13.34 We also noted a significant change in the amount of resources dedicated to inspections and audits over the last several years. In 1993, there were 39 individuals dedicated to inspections and audits relating to tobacco and fuel tax. Staff numbers were subsequently reduced when tax and other changes reduced the smuggling of tobacco products and the enforcement activities required to control the problem. At the time of our audit there were 20 individuals, some of whom were on extended sick leave or seconded to another area of the Department. It was unclear to us whether the number of staff performing audits and inspections is adequate and, if not, whether staff available were focusing on the highest priority work.

Recommendation 13.8

We recommend a comprehensive review of the staffing, organization and work responsibilities of the Department as they relate to tobacco and fuel taxes, concurrent with the above-recommended information system improvements, to ensure all tax-related responsibilities are fulfilled in the most efficient and effective manner.

13.35 We examined a sample of inspection reports pertaining to tobacco retailers, gasoline retailers and users of tax-exempt fuel. We noted problems relating to ratios calculated by inspectors to indicate whether there may be problems which need further investigation. We found errors in the

calculation of ratios and ratios outside of acceptable ranges without comment on action taken. In some situations, there were differences between gasoline retailers' records and compliance officer calculations of the amount of gasoline sold, but no comments recorded on the acceptability of the differences. We also observed that compliance officers regularly do not document a conclusion on the result of their work (i.e., whether there was sufficient compliance with legislation and regulations).

Recommendation 13.9

We recommend that better documentation be prepared to support the procedures performed and conclusions drawn from audits and inspections.

13.36 The Province is a participant under the International Fuel Tax Agreement. The agreement applies to all Canadian provinces and territories and certain American states, and governs the uniform collection and distribution of fuel taxes paid by interprovincial and interstate carriers to the members of the agreement. There are 62 jurisdictions participating in the agreement. Each carrier is required to pay a certain amount of fuel tax in each jurisdiction, based on the distance traveled in each jurisdiction. Registered carriers must file a quarterly fuel tax return which covers the distance traveled in all IFTA member provinces, territories or states.

13.37 The Department is responsible for administering IFTA in Nova Scotia. The Department collects or refunds net fuel tax from/to Nova Scotia registered carriers on behalf of all members in accordance with the agreement. Under the terms of the agreement, the Province is required to audit a minimum of 3% of registered carriers in Nova Scotia each year to ensure the proper amount of fuel tax has been paid by carriers. The agreement also subjects the Province to an audit every four years by the governing body of IFTA to ensure the Province is complying with the agreement. The most recent audit was completed in January 2002 and covered the period January 1, 1997 to December 31, 2000. The audit report concluded that the Province was in compliance with all terms of the agreement.

Collections and Enforcement

13.38 Monthly tax returns and payments are to be sent to the Department by the 20th of the following month. After a grace period, collection staff will telephone a delinquent vendor and request the return and payment. A maximum of three requests are made before additional action is taken. This may involve revoking a permit, cancelling an agreement or initiating legal action.

13.39 When an audit has been conducted of a vendor responsible for collecting fuel or tobacco taxes, it may result in an assessment of additional taxes and a formal notice to the vendor. We found that some unpaid assessments were not being followed up due to a deficiency in the computer system. A manual system is being used while the Department tries to fix the problem, but staff are unsure whether all overdue assessments are being identified. We also noted that certain assessments are not recorded in the system at all, and that collection is handled manually for these assessments. We encouraged the Department to address these information system deficiencies as soon as possible to ensure all assessments can be recorded in the system and all overdue accounts followed up.

13.40 A penalty of 5% of the outstanding amount, plus interest, is automatically applied to the vendor's account once delinquent. When an application is made for a licence/permit renewal, outstanding balances have to be paid before a renewal is granted. In addition, the Department can take legal action to recoup outstanding amounts. Various avenues of appeal exist if a vendor believes it is being treated unfairly.

13.41 When it is suspected that tax-exempt (marked) fuel is being used contrary to the Act, a compliance officer will take a sample of the fuel and have it analysed. The analysis will determine if the fuel contains dye used to identify the fuel as tax-exempt. Additional information will be collected to assist in deciding the nature of enforcement action to take. Enforcement action can vary from a disciplinary letter to legal action. In certain circumstances it may be necessary to issue an assessment to recover taxes avoided by using tax-exempt fuel. For the year ending March 31, 2002, there were 15 (2001 - 25) instances where either disciplinary or legal action occurred relating to gasoline and diesel oil taxes.

13.42 If legal action is successful, a fine is imposed and authorization to use tax-exempt fuel is suspended. If applicable, Registry of Motor Vehicle permits are suspended (30 days for a first offense) and/or a suspension from handling tax-exempt fuel for 60 days is imposed. Notification of the length of suspension is sent to both the offender and the fuel company which supplied the marked fuel. Department staff monitor the tax-exempt sales statements received from fuel companies to ensure no tax-exempt sales are made to the offender during the suspension period.

13.43 If a tobacco product vendor is convicted of illegal actions (e.g. selling to an unlicensed retail establishment, possession of illegal products), a fine is imposed and the vendor's permit to sell tobacco products may be suspended. In less severe cases, a disciplinary letter may be sent. If a permit is suspended, a letter is sent to the offender outlining the reason for the suspension and explaining the right to appeal. Suspension periods can range from one week to five years, depending on the number of times an offense has occurred and the quantity involved. Companies which sell tobacco products to the vendor are notified and asked to not sell to them during the suspension period. Compliance officers are required to ensure that the terms of suspension are followed. For the year ending March 31, 2002, there were 11 (2001 - 4) instances where either disciplinary or legal action occurred relating to tobacco taxes.

13.44 We examined a sample of situations where enforcement action was taken. We found that files were complete and well documented. However, we noted that there is no system to ensure suspensions of permits and licences are recorded in Department computer systems, and we suggested that notices of suspensions be routinely submitted for entering into the systems.

13.45 The Revenue Act stipulates specific actions to be taken when a vendor is suspended or convicted. We reviewed the enforcement practices that the Department uses when there is a violation of the Act and found they are consistent with the Act.

Licensing

13.46 Under the Revenue Act, operators of certain businesses are subject to Provincial licensing requirements. Licences, permits and agreements are used extensively to regulate the sale of taxable and tax-exempt tobacco and fuel in the Province. To ensure fuel oil companies only sell fuel to registered gasoline retailers, they are provided with a listing of bulk plant and gasoline retailer licences issued. Fuel oil companies are provided with a listing of consumer exemption permits that have been issued. To ensure tobacco wholesalers only sell tobacco products to registered tobacco retailers, a monthly listing of tobacco retailer licences issued is provided to wholesalers.

13.47 The Department administers the licensing process, which includes collecting any required fees, reviewing and verifying application information, and issuing the permits and licences (see Exhibit 13.3 on page 218). We reviewed the systems used by the Department to ensure it receives complete and accurate information to process and issue permits and licences.

13.48 Standard application forms are completed by applicants. Verification of the applications includes ensuring all required information is provided, companies are registered with the Registry

of Joint Stocks and/or Canada Customs and Revenue Agency, and no outstanding amounts are payable to the Department. For some permits, staff must ensure security bonds in the correct amounts have been received, the correct application fees have been paid, and agreements between the applicant and the Department have been signed.

13.49 The Department has established time lines for the completion of the various registration processes. We were informed staff are aware of the time lines and try to achieve the targets. However, there is no formal system to ensure the time lines are met. We encouraged the Department to more formally monitor the time involved in processing licences and permits and compare it to targets.

13.50 We examined a sample of licence applications and identified three issues of concern.

- Tobacco wholesalers are required to provide security, in the form of surety bonds, based upon the volume of tobacco products they sell. However, this commenced in 1996 and tobacco wholesalers who were licensed prior to that time are not required to provide a surety bond. Since there is a cost to tobacco wholesalers to provide surety bonds, we believe it is not reasonable to use an implementation date as the only criteria to decide which wholesalers should provide security.
- Applicants requesting a bulk fuel vendor permit are required to have a motive fuel wholesaler licence from the Department of Environment and Labour. However, there is no procedure to ensure this licence is in place.
- Under the Revenue Act, certain fuel oil companies are considered fuel agents and must sign an agreement with the Department. Surety bonds are submitted to the Department as part of the licensing process. The Department does not review the surety bonds on a periodic basis to identify bonds that have expired and should be renewed.

Recommendation 13.10

We recommend that the Department establish risk-based criteria for determining which companies should provide surety bonds, and ensure it has up-to-date surety bonds from companies required to provide them. The Department should also ensure that licences or permits required by a client from another Department are in place.

CONCLUDING REMARKS

13.51 Based on our audit, Service Nova Scotia and Municipal Relations has systems to ensure it complies with the Revenue Act and Regulations as they relate to tobacco and gasoline and diesel oil taxes.

13.52 Systems for issuing and monitoring licences and permits are adequate. However the Department has inadequate systems for processing fuel and tobacco tax returns, and for conducting taxation-related audits and inspections. Also, improvements should be made to strengthen the collection of past due taxes.

*Exhibit 13.1***AUDIT CRITERIA**

Audit criteria are reasonable and attainable standards of performance and control, against which the adequacy of systems and practices can be assessed. They relate to the audit objectives developed for an assignment and are used to design the detailed audit tests and procedures.

The following criteria were used in our audit of Service Nova Scotia and Municipal Relations.

- The Department should comply, and have systems to ensure compliance, with applicable provisions of Provincial legislation and regulations.
- The Department's policies should be consistent with Provincial legislation and regulations.
- There should be systems and controls to ensure the correct amounts of gasoline and diesel oil and tobacco taxes are being remitted.
- There should be a system to ensure that inspections and audits are carried out in a reasonable manner and on a regular and timely basis.
- There should be reasonable follow-up of recommendations and warnings resulting from inspections and audits.

Exhibit 13.2

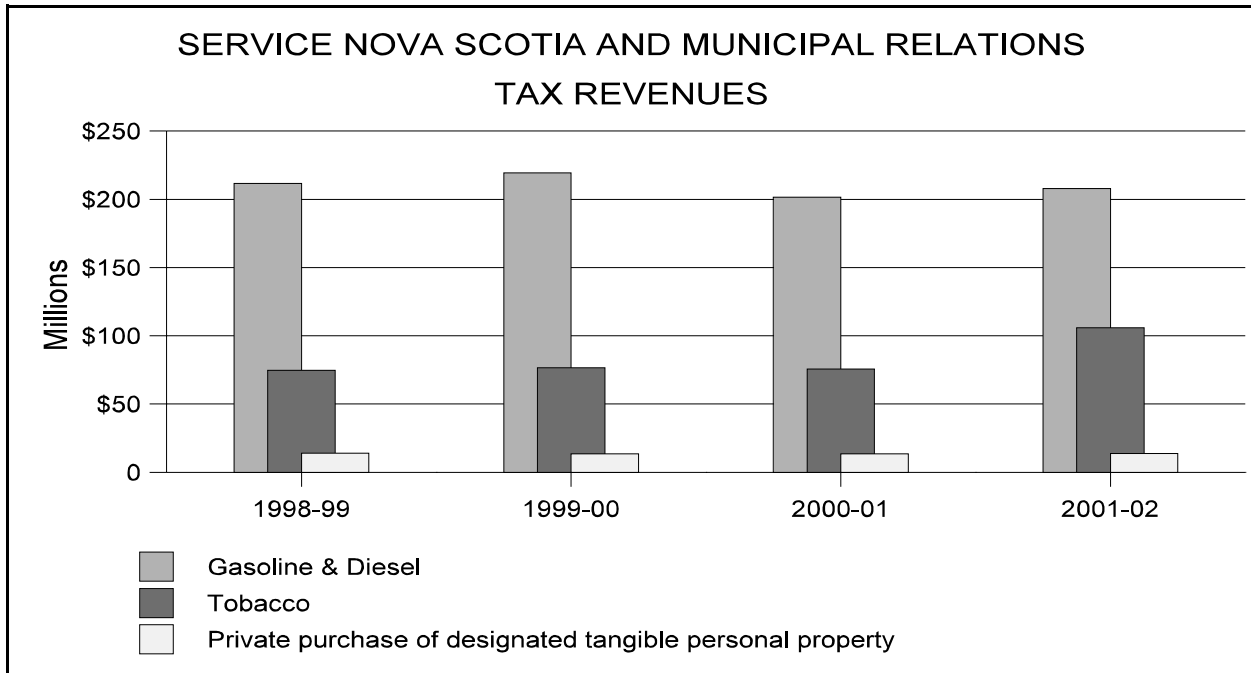


Exhibit 13.3

**SERVICE NOVA SCOTIA AND MUNICIPAL RELATIONS
LICENCES AND PERMITS ISSUED
AS AT MARCH 31, 2002**

TOBACCO

Type of Permit	Number Issued
Tobacco Manufacturer	12
Tobacco Wholesaler	37
Purchase and Sell Unmarked Tobacco	32
Stamp Imported Tobacco	2
Tobacco Retail Vendor	2,210
Designated Retail Vendor	<u>44</u>
Total	<u><u>2,337</u></u>

FUEL

Type of Permit	Number Issued
Fuel Agent	33
Bulk Plant	59
Fuel Retail Vendor	546
Fuel Retail Vendor - Fish Plant	74
Marine Tax Rate	54
Exempt Consumer	<u>4,428</u>
Total	<u><u>5,194</u></u>

*Exhibit 13.4***SERVICE NOVA SCOTIA AND MUNICIPAL RELATIONS
TYPES OF LICENCES AND PERMITS****TOBACCO**

Tobacco Manufacturer's Permit - anyone who wants to manufacturer and mark tobacco products for resale in Nova Scotia.

Tobacco Wholesaler's Permit - anyone who wants to sell wholesale tobacco products in Nova Scotia.

Permit to Purchase and Sell Unmarked Tobacco - anyone in Nova Scotia who wants to sell tobacco products into another jurisdiction, into another country, to designated retail vendors, or with imported tobacco stamping.

Tobacco Retail Vendor (Seller) Permit - any retail store owner who wants to sell tobacco products in Nova Scotia.

Permit to Stamp Imported Tobacco - any tobacco retail vendor who wants to import tobacco products into Canada for resale in Nova Scotia.

Designated Vendor (Retail) Permit - any tobacco retail vendor designated by the Provincial Tax Commissioner who sells tobacco in Nova Scotia to a consumer at a retail store on a reserve (as defined in the Indian Act).

FUEL

Bulk Vendor Permit - any wholesaler of petroleum products who operates a bulk plant, bulk station and/or terminal and who stores gasoline and/or diesel oil in storage tanks.

Gasoline, Propane and Diesel Oil Retail Vendor (Seller) Permit - anyone wishing to sell gasoline, propane or diesel fuel at the retail level in Nova Scotia.

Consumer's Exemption Permit - anyone in Nova Scotia who qualifies for an exemption from the gasoline or diesel oil tax on purchases of marked gasoline and/or diesel oil used to operate qualified machinery and apparatus in any of the defined activities.

Marine Tax Rate Letter of Authority - anyone who wants to buy gasoline or diesel oil at a reduced rate of tax for use in a ship, boat or vessel operated solely for commercial purposes.

Application for International Fuel Tax License - any individual or firm who wants to operate a commercial vehicle weighing 26,000 pounds or more, and who resides in a province or state which has implemented the International Fuel Tax Agreement.

Single Trip Permit - any carriers (trucking companies) who want to enter Nova Scotia and are not members of the International Fuel Tax Agreement.

**DEPARTMENT OF SERVICE NOVA SCOTIA AND MUNICIPAL RELATIONS'
RESPONSE**

Service Nova Scotia and Municipal Relations is in agreement with most of the findings of the audit and agrees with the recommendations. The Department had recognized two of the major areas needing attention — remittance processes and an audit enforcement strategy — and has plans in place for addressing them.

We have applied for capital to implement an integrated revenue control system for all of our revenue lines, including taxes. In the interim, we have requested Internal Audit to review our back office processes and recommend improvements.

In 2001-2002, we carried out more than 3,000 audits and inspections. The focus of this activity has been in areas of fuel and tobacco taxation, where the risk of loss to the Province is highest. Our enforcement strategy includes working closely with the Canada Customs and Revenue Agency, as well as staff from other jurisdictions. We have planned a review of our enforcement program for the 2002-2003 fiscal year, and it will be completed. We have also reserved funding for two more positions should this prove necessary.

While we acknowledge the comments regarding the planning process of our audit program, this is less of a concern than it appears because we have a very experienced audit staff — most with more than 20 years experience. However, the Department will be taking steps to improve the planning process.

In the last two years, staff have replaced and eliminated weaknesses in the licensing system, implemented three tobacco tax increases, and addressed the exemption for purchases of fuel by Natives on reserves. The licensing review covered over 10,000 permits, eliminating over 3,000 that were out of date. The implementation of a three-year renewal period will allow us to keep these permits up to date. The audits and inspections of tobacco inventories after the tax increases yielded over \$3,000,000 in revenue. Now that these projects are largely completed, attention can be placed on the enforcement strategy and documentation issues raised in the report.

The high level outcome for this program is that actual revenues agree with forecasted revenues. Revenues are forecast based on economic activity and changes in consumption patterns (i.e. the rate of people quitting smoking). Except for unusual and one-time events, the actual revenues meet or exceed forecasts, which tells us that there is no significant tax evasion and no increase in tax evasion, in this area.

Finally, the Department would like to express its appreciation to the Auditor General for this review and for the insights that an external review such as this provides.
