



BRINGING BACK FEE FAIRNESS

The Implications of Rushed Changes to Federal Cost
Recovery Rules



Canadian
Chamber of
Commerce

Chambre de
Commerce
du Canada

The 2017 federal budget introduced a largely unnoticed legislative change that will have long-term implications for Canadian businesses. It overhauled the cost recovery rules that govern how federal departments and agencies set user fees charged to businesses and individuals.

The budget replaced the 2004 *User Fees Act* with the *Service Fees Act*. The *Service Fees Act* makes it much easier for departments and agencies to introduce and increase the fees for their goods and services. For some fees, the budget legislation went a step further and, without explaining why, exempted fees under the *Food and Drugs Act* from the new rules, giving the Minister of the Health the authority to increase fees via Ministerial Order. These exemptions and the *Service Fees Act* were included in an omnibus budget bill, meaning the changes received far less parliamentary and public scrutiny than they would have as stand-alone legislation.

User fees play an important role in how departments and agencies are funded. Like taxes, they affect the competitiveness of businesses that pay them. Given the hasty implementation of changes to federal cost recovery rules, it is worth examining how the government and Health Canada, specifically, have exercised these new authorities.

Why User Fees?

The principle of cost recovery is a reasonable one: that some government goods or services should be paid by the user that benefits from them instead of from general tax revenues. When the benefit is entirely private, some fees recover the entire cost to departments of providing the service. Some fees recover a portion of the service delivery cost when there are benefits to both private interests and the broader public.

Canadian businesses are accustomed to paying fees to all levels of government to comply with regulatory requirements, including a seemingly endless number of registrations, licences and permits. Individual Canadians are also used to paying federal user fees for things such as passports and admission to national parks.

While user fees are generally not compulsory like taxes, many businesses cannot obey existing laws and regulations without paying them. These requirements are from a public monopoly, meaning there are no alternatives for businesses that are unhappy with the service or the fee. As a result, it is crucial departments provide the highest levels of transparency and accountability in setting fees and ensure fees are strongly connected to the services they fund.

The 2004 User Fees Act

As Canada was wrestling with enormous deficits in 1995, that year's federal budget made large cuts to program spending and announced that the government would increase the usage of user fees to recover costs and finance programs.¹ The budget incentivized departments to meet user fees revenue targets by linking spending allocations to cost recovery projections. This meant that if a department fell short of projected cost recovery revenue, its spending would be cut to make up the difference.²

Following a significant expansion in the use of fees, the government tried to improve the rules for fee setting through the 1997 Cost Recovery Policy, with a goal of establishing a more consistent framework and equitable application of fees across the federal government.³ The policy did not achieve its goals as subsequent business consultations and reports revealed that departments and agencies were not following its guidelines and not providing appropriate information to justify the level of user fees they were charging.⁴

The Standing Committee on Finance examined this growing problem in [a 2000 study](#). During the committee hearings, industry witnesses spoke repeatedly about inadequate consultations and transparency in fee setting processes. Many noted that departments and agencies were increasing user fees to unreasonable levels and often without a reference to any service standards.⁵

In 2002, Roy Cullen, a Member of Parliament who participated in the study, introduced a private members bill, the *User Fees Act*, to deal with these problems. In his 2011 book, *Beyond Question Period: Or What Really Goes on in Ottawa*, Cullen outlined his rationale:



I introduced the Bill because of a certain level of frustration with the lack of progress on this issue. The House of Commons Standing Committee on Finance in 2000 recommended significant changes to the cost recovery/user fee policy, but progress by our Liberal government had been slow to non-existent.

In the book, Cullen goes on to cite his concerns about the lack of analysis, transparency, stakeholder participation and parliamentary oversight that business groups had raised in the 2000 study. The legislation was passed in 2004 with all party support and established a new legal framework for introducing and adjusting fees. Specifically it mandated:

- Compulsory consultations with stakeholders.
- Identifying which costs the user fee will address and the costs to departments and agencies of delivering that service.
- Establishing service standards and performance measurements comparable to other jurisdictions.
- Establishing a panel to address complaints if they arise.
- Annual reporting to parliament.

The *User Fees Act* mandated rigorous new processes for departments and agencies that wanted to recover costs through fees. However, after it became law, many departments were discouraged from applying for fee increases due to these conditions. In particular, the lengthy consultation requirements provided opportunities for stakeholders to oppose fee increases. The irony of federal regulators being concerned about burdensome processes has not been lost on the Canadian business community.

1 Office of the Auditor General of Canada, 2008 May Report of the Auditor General of Canada, Chapter 1 – Management of Fees in Selected Departments and Agencies

2 Finance Canada, 1995 Budget Plan

3 Treasury Board Secretariat, Cost Recovery (accessed July 2019)

4 Standing Committee on Finance, Challenge for Change, A Study of Cost Recovery (2000)

5 Standing Committee on Finance, Challenge for Change, A Study of Cost Recovery (2000)

2017 Service Fees Act

The government repeatedly cited the *User Fees Act* as the reason why many fees have not been updated since 2004, and in recent years, departments have sought legislative exemptions to get around the rules and introduce or increase fees.⁶ In response to these concerns, the government replaced the *User Fees Act* with the *Service Fees Act* in the 2017 federal budget.

The legislation was included in the omnibus budget bill, meaning it received far less parliamentary debate, committee study or public scrutiny than it would have as standalone legislation. In a submission to the Standing Committee on Finance reviewing the budget bill, Roy Cullen expressed his regret about the change, stating,

It is disappointing and somewhat disconcerting that C-212, An Act respecting user fees, will be repealed and replaced by the Service Fees Act. It took me roughly two years to steer my Bill through Parliament where it received unanimous consent.⁷

The new cost recovery regime reduces the level of scrutiny required for departments and agencies to introduce and increase fees. Most notably, the *Service Fees Act* automatically hikes fees by the level of inflation each year. Where the *User Fees Act* required departments to establish performance standards comparable to other jurisdictions, the *Service Fees Act* has no such requirement. Cullen commented on this in his Finance Committee submission, noting, “Departments will be inclined to set performance standards that they can meet, and in many cases they will be inclined to argue that comparisons with other jurisdictions cannot be made.”⁸ The removal of this requirement is concerning because departments often make intentional user fee comparisons to justify fee increases, so it stands to reason that they should also be required to compare service standards.

The *Service Fees Act* only mandates a minimal amount of consultations before increasing fees, with publication in the *Canada Gazette* deemed to be sufficient consultation for fees that have been established by regulation. Unlike a broad, proactive consultation, the *Canada Gazette* is a reactive regulatory notification process unfamiliar to most Canadians and Canadian companies. In the case of Ministerial Orders, departments have even more latitude to conduct consultations in a manner they see fit without any central agency oversight.

⁶ CBC News, Ottawa looks at user-fee hikes for potential new revenue (February 9, 2017)

⁷ Standing Committee on Finance, Study Bill C-44, An Act to implement certain provisions of the budget tabled in Parliament on March 22, 2017 and other measures

⁸ Standing Committee on Finance, Study Bill C-44, An Act to implement certain provisions of the budget tabled in Parliament on March 22, 2017 and other measures

The *Service Fees Act* also excludes language from the previous *User Fees Act* that specified that fees must result, “in a direct benefit or advantage to the person paying the fee.” While the removal of this language may seem innocuous, it is crucial for businesses that user fees remain distinct from taxes and are explicitly linked to the services they fund.

The *Service Fees Act* also reduces parliamentary input on individual fees, but does require departments and agencies to report annually on their user fee revenues and measurements against performance standards. The *Service Fees Act* also includes a requirement for departments to remit fees to users if performance standards are missed, but only a portion that departments consider appropriate. Overall, Budget 2017 forecasted that the changes would result in an additional \$147M in fees paid to government annually by 2021-2022. If federal budgetary pressures lead to reductions in departmental appropriations, these changes will make it far easier for departments to increase user fees in response, not unlike the mid-1990s.

Health Canada’s Fee Proposal for Drugs and Medical Devices

As part of the 1995 shift towards more fees, Health Canada started collecting fees from pharmaceutical companies for regulatory activities related to human and veterinary drugs and medical devices. These fees fund evaluations the department undertakes to assess the safety, efficacy and quality before drugs or devices are allowed to be sold. Health Canada also charges right to sell fees to fund the ongoing monitoring of all prescription and over-the-counter (non-prescription) drugs once they are available in the market. Before 2017, the drugs and medical devices fees had been most recently updated in 2011.

Even though the *Service Fees Act* simplified the process for Health Canada to increase fees, the 2017 budget also exempted the *Food and Drugs Act* from the *Service Fees Act* altogether and gave the department the ability to set fees through a Ministerial Order without parliamentary or central agency oversight. The budget did not provide a rationale for the exemption, leaving industry guessing about why fees under the

Food and Drugs Act could not abide by the new process. Shortly after receiving the exemption, Health Canada attempted to expedite major fee increases for drugs and medical devices.

The department launched a compressed consultation in October 2017, proposing huge increases. In aggregate, the proposal sought to immediately increase the cost recovery for drugs and medical devices from roughly 50% of Health Canada’s regulatory costs up to 90-100%, well above the OECD average of 75-80%. The proposal would have approximately tripled the cost recovery burden on over-the-counter drugs by 2019. While the consultation document highlighted that Australia and the European Union fund 90-100% of similar regulatory costs from fees, it failed to provide a comparison to Canada’s largest trading partner and competitor where user fees make up 70% of the U.S. Food and Drug Administration’s human drugs budget and 35% for medical devices.⁹ Unlike Canada, the U.S. also has no user fees for over-the-counter drugs or natural health products.

⁹ U.S. Food and Drug Administration, 2018 FDA Budget Appropriation (2018)

Shifting to 100% cost recovery industry would reduce incentives for Health Canada to seek efficiencies in its approach to regulation. Proposing full cost recovery also indicates that the department perceived no general public benefit in the approval and availability of drugs and medical devices in Canada. This is inconsistent with Treasury Board guidance that notes that fees benefiting a direct user can have public benefits:

Government activities may support both public and private (i.e. direct user) interests. In such cases, it may be appropriate to establish fees at levels below full cost. Evaluating or quantifying an activity's mix of public and private benefit can be challenging and subjective. As one input to the analysis, assessing whether the activity primarily benefits the general public or the direct user can help to situate a possible rate of cost recovery. Where regulatory activities are concerned, the individual or organization being regulated is considered the direct user and generally recognized as the primary beneficiary. Naturally, the act of regulating direct users may also serve the health, safety or security interests of a larger contingent of end users or the Canadian public.¹⁰

During consultations, industry raised significant concerns about the magnitude of the increase and rapid implementation timelines. It was also noted that the fee proposal:

- Excluded any analysis on how the revised fee structure would impact product availability, innovation, industry investment or innovation.
- Did not include a concurrent improvement to the department's service standards.
- Did not distinguish between right to sell fees for over-the-counter versus prescription drugs, even though the post-marketing regulatory costs are much lower for over-the-counter drugs.
- Included a companion-costing document that fell well short of providing a comprehensive costing analysis to justify the new fee structures.

In response to industry concerns, the department went back to the drawing board and issued a revised proposal in May 2018. The new proposal included lower but still significant fee increases that would be phased-in and increase program cost recovery from 50% to 71% by 2022-2023. The amended proposal also distinguished right to sell fees between over-the-counter and prescription drugs to reflect the lower level of regulatory effort between the two categories of drugs.

This haphazard approach to major fee increases made it clear that the department was not equipped to responsibly manage the blanket fee setting exemptions granted to it in the budget. In the final fee document, issued in May 2019, the department noted that, "While outside the scope of the proposal to revise fees, some stakeholders shared their concerns regarding the new authorities granted to the Minister to fix fees and Health Canada's exemption to the *Service Fees Act*."¹¹

To date, the government has still not explained why the changes to fees for drugs and medical devices were so urgent that it required an exemption to the streamlined user fee process created in the *Service Fees Act*.

¹⁰ Treasury Board Secretariat, *Guide to Establishing the Level of a Cost-Based User Fee or Regulatory Charge* (2009)

¹¹ Health Canada, *Final Report: Fees for Drugs and Medical Devices* (May 15, 2019)



Cannabis Fees

The Food and Drugs Act is not the only legislation that has received an exemption to the Service Fees Act. The Cannabis Act, passed in June 2018, also provides the Minister of Health the power to fix fees through a Ministerial Order for the department's cannabis regulatory regime. This exemption has been used to establish a range of application, security and import/export permit fees.

In the fall of 2018, following a brief consultation period and only weeks before the legalization of recreational cannabis, Health Canada announced a new user fee of 2.3% of gross cannabis revenue for cultivators and processors. This fee is not linked to any specific service or approval, and there are no performance standards associated with it. The fee, which is effectively an additional 2.3% tax, was also announced after many producers had already signed multi-year supply agreements with provincial wholesalers based on previously announced tax rates. This additional tax was enacted using the Ministerial Order even though Treasury Board guidance on fee setting makes it clear that only parliament can levy taxes.¹²

The department has estimated that this fee will recoup \$383 million from industry between 2018-2019 and 2021-2022.¹³ In addition to not being linked to a specific regulatory activity, the fee makes it more challenging for the legal market to compete with the illegal market on cost, counter to the government's primary objective of legalization.

¹² Treasury Board Secretariat, Guide to Establishing the Level of a Cost-Based User Fee or Regulatory Charge (2009)

¹³ Canada Gazette, Part II, Volume 152, Number 21, Cannabis Fees Order (October 17, 2018)

Conclusion

When the *User Fees Act* was introduced by Roy Cullen in 2002, he stated:

It is time for parliamentarians to take greater ownership of user fees. What began as a legitimate attempt to more fully recover costs for proprietary services and goods has developed into something that is beyond that which was contemplated.¹⁴

Cullen's private members bill, the *User Fees Act* swung the pendulum in the opposite direction to a point where departments found the fee process too burdensome. There are signs that the *Service Fees Act* and the exemptions to it have swung the pendulum too far back the other way. The new unregulated approach to setting industry fees sends a hostile signal to foreign investors and companies looking to do business in Canada. Health Canada's 2017 attempt to dramatically increase fees for drugs and medical devices gave no consideration to business competitiveness impacts and reinforced industry concerns about the federal shift on fees.

2020 will mark three years since the passage of the *Service Fees Act*. Given it was drafted without consultation and received little public scrutiny, it is an appropriate time to conduct a review of the legislation. Doing so provides an opportunity to build business confidence in the federal cost recovery regime and ensure the *Service Fees Act*, like the user fee policies of the mid-1990s, does not develop into something beyond which it was intended.

Recommendations



Remove all current exemptions from the *Service Fees Act*, including authorities that have been provided to Health Canada under the *Food and Drugs Act* and the *Cannabis Act*.



Require that any individual fee increases of more than 25% levels include a business competitiveness impact assessment.



Before the end of 2020, conduct a review of the *Service Fees Act*. The scope of the review and its final recommendations should be approved by the Treasury Board External Advisory Committee on Regulatory Modernization.

Thank you to our report sponsor

Consumer Health
Products Canada

Advancing evidence-based self-care



¹⁴ 37th Parliament, 2nd Session, Hansard Number 035 (November 29, 2002)