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DEPARTMENT OF THE TREASURY

Alcohol and Tobacco Tax and Trade Bureau

27 CFR Parts 40, 41, 44, and 45

[Docket No. TTB–2009–0002]

[T.D. TTB–104; Re: T.D. TTB–78, Notice No. 95 and Notice No. 98; T.D. TTB–80; T.D. TTB–81 and Notice No. 99]

RIN 1513–AB72

Implementation of Statutory Amendments Requiring the Qualification of Manufacturers and Importers of Processed Tobacco and Other Amendments Related to Permit Requirements, and the Expanded Definition of Roll-Your-Own Tobacco

AGENCY: Alcohol and Tobacco Tax and Trade Bureau, Treasury.

ACTION: Final rule; Treasury decision.

SUMMARY: The Alcohol and Tobacco Tax and Trade Bureau is making permanent, with some changes, temporary regulatory amendments promulgated in response to certain changes that the Children’s Health Insurance Program Reauthorization Act of 2009 made to the tobacco provisions of the Internal Revenue Code of 1986. The regulatory amendments adopted in this final rule include permit and related requirements for manufacturers and importers of processed tobacco, requirements for manufacturers of tobacco products who also manufacture processed tobacco, and regulations related to the expansion of the definition of roll-your-own tobacco.

DATES: Effective June 21, 2012, the temporary regulations published in the **Federal Register** at 74 FR 29401 on June 22, 2009, at 74 FR 37551 on July 29, 2009, and at 74 FR 48650 on September 24, 2009 are adopted as final, and these regulations will no longer have a sunset date of June 22, 2012. The amendments to 27 CFR parts 40 and 41 contained in this rule are effective June 21, 2012.

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SUPPLEMENTARY INFORMATION:

Background

TTB Authority

Chapter 52 of the Internal Revenue Code of 1986 (IRC) sets forth the Federal excise tax and related provisions that apply to manufacturers and importers of tobacco products, processed tobacco, and cigarette papers and tubes, and to export warehouse proprietors who hold such products, upon which tax has not been paid, pending export. The Alcohol and Tobacco Tax and Trade Bureau (TTB) administers chapter 52 of the IRC pursuant to section 1111(d) of the Homeland Security Act of 2002, codified at 6 U.S.C. 531(d). The Secretary has delegated various authorities through Treasury Department Order 120-01 (Revised), dated January 21, 2003, to the TTB Administrator to perform the functions and duties in the administration and enforcement of this law.

Section 5701 of the IRC (26 U.S.C. 5701) sets forth the excise tax rates that apply to domestic and imported tobacco products and cigarette papers and tubes. Section 5702 of the IRC (26 U.S.C. 5702) defines tobacco products as cigars, cigarettes, smokeless tobacco, pipe tobacco, and roll-your-own tobacco and separately defines each of these terms. That section also defines other relevant terms, such as “manufacturer of tobacco products,” “importer,” and “export warehouse proprietor.”

Sections 5712 and 5713 of the IRC (26 U.S.C. 5712 and 5713) provide that manufacturers and importers of tobacco products and processed tobacco and export warehouse proprietors must obtain a permit to engage in such businesses. Section 5712 also allows for the promulgation of regulations to prescribe minimum manufacturing and activity requirements for such permittees. Sections 5721, 5722, and 5741 of the IRC (26 U.S.C. 5721, 5722, 5741) authorize the promulgation of regulations to require inventories, reports, and recordkeeping, respectively. Section 5723 of the IRC (26 U.S.C. 5723) includes authority to promulgate regulations regarding standards for packages, and for marks, labels, and notices on such packages of tobacco products, processed tobacco, and cigarette papers and tubes.

Regulations implementing the provisions of chapter 52 of the IRC are contained in 27 CFR parts 40 (manufacture of tobacco products, cigarette papers and tubes, and processed tobacco), 41 (importation of tobacco products, cigarette papers and tubes, and processed tobacco), 44 (exportation of tobacco products and cigarette papers and tubes, without payment of tax, or with

drawback of tax), and 45 (removal of tobacco products and cigarette papers and tubes, without payment of tax, for use of the United States). These regulatory provisions are administered by TTB.

Children's Health Insurance Program Reauthorization Act of 2009

On February 4, 2009, the President signed into law the Children's Health Insurance Program Reauthorization Act of 2009, Pub. L. 111-3, 123 Stat. 8 ("CHIPRA"). Section 701 of CHIPRA amended the IRC to increase the Federal excise tax rates on tobacco products and cigarette papers and tubes. Section 701 also imposed a floor stocks tax on such articles held for sale on the effective date of the tax rate increases (April 1, 2009). On March 31, 2009, TTB published in the **Federal Register** (74 FR 14479) a temporary rule, T.D. TTB-75, to amend the TTB regulations to reflect the section 701 changes. On July 22, 2010, TTB published in the **Federal Register** (75 FR 42605) T.D. TTB-85 which adopted those temporary regulations as a final rule. The section 701 statutory and regulatory changes are not the subject of this document.

Section 702 of CHIPRA also made some significant changes to the IRC, some of which are reflected in the description of TTB's authority above. These changes were principally with regard to "roll-your-own tobacco" and "processed tobacco." Section 702 amended the definition of "roll-your-own tobacco" in section 5702 of the IRC by including in its scope tobacco for making cigars and tobacco for use as wrappers of cigars and cigarettes. Section 702 of CHIPRA also set forth a statutory framework for regulating "processed tobacco" by:

- Amending section 5702 of the IRC to add a definition of "manufacturer of processed tobacco;"

- Amending sections 5712 and 5713 of the IRC to require that manufacturers and importers of processed tobacco, like manufacturers and importers of tobacco products, apply for and obtain a permit before commencing such businesses. Section 702 included a transitional rule under which manufacturers and importers of processed tobacco who were engaged in such a business on April 1, 2009, and who file a permit application with TTB on or before June 30, 2009, could continue in business pending final TTB action on the application;

- Amending sections 5721, 5722, and 5741 to make manufacturers and importers of processed tobacco subject to the inventory, reporting, and recordkeeping regulatory authority already applicable to manufacturers and importers of tobacco products; and

- Amending section 5723 of the IRC to make processed tobacco subject to the packaging (including mark, label, and notice) regulatory authority already applicable to tobacco products and cigarette papers and tubes.

The changes made by section 702 of CHIPRA clearly brought processed tobacco within the statutory and regulatory framework administered by TTB under chapter 52 of the IRC but did not establish processed tobacco as a commodity subject to excise tax. The regulatory actions taken by TTB in response to these statutory changes are outlined below.

Publication of Temporary Regulations and Notices of Proposed Rulemaking

On June 22, 2009, TTB published in the **Federal Register** (74 FR 29401) a temporary rule, T.D. TTB-78, setting forth amendments to parts 40, 41, 44, and

45 of the TTB regulations to reflect the changes made by section 702 of CHIPRA; those temporary regulations went into effect on the date of publication. On the same day, TTB published in the **Federal Register** (74 FR 29433) a notice of proposed rulemaking, Notice No. 95, that invited comments from the public on the amendments contained in that temporary rule.

The principal regulatory changes contained in the T.D. TTB-78 temporary rule are as follows:

- Numerous provisions within parts 40, 41, and 44 were amended by the inclusion of references to “processed tobacco” to reflect the entry of that commodity into the regulatory framework administered by TTB.
- A new subpart L was added to part 40 and a new subpart M was added to part 41, setting forth qualification, operation, and related requirements for manufacturers and importers of processed tobacco. These provisions included permit application, recordkeeping, reporting, and minimum activity requirements. Inventory requirements also were included for manufacturers of processed tobacco.
- Definitions of “manufacturer of processed tobacco” and of “processed tobacco” were added to §§ 40.11 and 41.11 to assist in distinguishing between activities related to farming and the handling of processed tobacco, which do not fall under the regulatory provisions, and activities related to the processing of tobacco, which must be undertaken in compliance with statutory and regulatory requirements.

- The definition of “roll-your-own tobacco” in §§ 40.11 and 41.11 was amended to reflect the expanded definition of that term in section 5702 of the IRC, and corresponding changes were made to the notice requirements for roll-your-own tobacco specified in §§ 40.216b and 41.72b.
- In §§ 40.11 and 41.11 the definition of “package” was revised, and a definition of “packaging” was added, in order to make clear that “processing of tobacco” does not include placing processed tobacco in consumer packaging. A manufacturer of processed tobacco may not place processed tobacco in a consumer package because to do so would result in a product that fits the definition of a taxable commodity. Accordingly, such packaging may not occur on the premises of a person who is qualified only as a manufacturer of processed tobacco but may only be undertaken on the bonded premises of a tobacco product manufacturer.
- Sections 40.25a and 41.30, which specify the tax rates that apply to pipe tobacco and roll-your-own tobacco, were amended by the addition of standards for distinguishing between these two classes of tobacco products on the basis of their packaging and labeling, including rules under which a product is deemed to be (and thus subject to the tax rate applicable to) roll-your-own tobacco.
- The notice requirements for pipe tobacco in §§ 40.216a and 41.72a were amended by removing “Tax Class L” as a specified designation on a pipe tobacco package, thus leaving “pipe tobacco” as the only specified designation.

- The notice requirements for roll-your-own tobacco in §§ 40.216b and 41.72b were amended by removing “Tax Class J” as a specified designation on a roll-your-own tobacco package (thus leaving “roll-your-own tobacco” and “cigarette tobacco” as specified designations) and, to reflect the expanded definition of “roll-your-own tobacco” mentioned above, by adding “cigar tobacco,” “cigarette wrapper,” and “cigar wrapper” as specified designations.

- Sections 40.216c and 41.72c were revised to set forth a use-up period, until August 1, 2009, for the removal of pipe tobacco and roll-your-own tobacco in packages that bore the “Tax Class L” and “Tax Class J” designations.

On July 29, 2009, TTB published in the **Federal Register** (74 FR 37551) a temporary rule, T.D. TTB–80, to correct several inadvertent errors that appeared in the T.D. TTB–78 temporary rule; these corrections were effective on the date of publication. Subsequently, on August 25, 2009, TTB published in the **Federal Register** (74 FR 42812) a notice of proposed rulemaking, Notice No. 98, to reopen the comment period specified in Notice No. 95 in order to extend that comment period for an additional 60 days, that is, until October 20, 2009.

During the initial Notice No. 95 comment period, TTB received three comments requesting an extension of the package use-up period beyond the August 1, 2009, date specified in T.D. TTB–78. One commenter also pointed out that the temporary regulations set forth additional factors related to the packaging of the pipe tobacco and roll-your-own products that bears on the classification of those products, but those provisions were not subject to a use-up period in the temporary regulations. The commenter asked that TTB provide a use-up

provision that applied to both the classification and the notice-related packaging provisions. On September 24, 2009, TTB published in the **Federal Register** (74 FR 48650) a temporary rule, T.D. TTB–81, which: (1) Further amended §§ 40.216c and 41.72c, discussed above, in order to extend the specified use-up period for packages bearing the “Tax Class L” and “Tax Class J” designations to March 23, 2010; (2) amended §§ 40.25a and 41.30, discussed above, in order to delay application of the new standards for distinguishing between pipe tobacco and roll-your-own tobacco, also to March 23, 2010; and (3) corrected two minor errors of omission in the T.D. TTB–78 regulatory texts. These regulatory amendments took effect on the date of publication. Also on September 24, 2009, TTB published in the **Federal Register** (74 FR 48687) a notice of proposed rulemaking, Notice No. 99, inviting the submission of public comments, until November 23, 2009, on the additional regulatory amendments contained in T.D. TTB–81.

Discussion of Comments

Comment Overview

TTB received 19 responses to the solicitation of comments regarding the temporary regulations contained in T.D. TTB–78 and 1 response to the solicitation of comments regarding the regulatory amendments contained in T.D. TTB–81. TTB had also received 2 comments to an earlier temporary rule (T.D. TTB–75, implementing the new tax rates and floor stocks tax imposed by CHIPRA) that are relevant to the issues raised in T.D. TTB–78.

The 19 responses to the publication of T.D. TTB–78 included comments submitted by or on behalf of the following industry members, trade organizations, consulting firms, and law firms: R.J. Reynolds Tobacco Co. (R.J. Reynolds), John Middleton Co., National Tobacco Co. LP (National Tobacco), Altadis USA, Inc., Universal Leaf Tobacco Co., Inc., Schweitzer-Mauduit International, Inc. (Schweitzer-Mauduit), the Pipe Tobacco Council, Inc., Customs Advisory Services, Inc., Venable, LLP, the law offices of Barry Boren, and the companies of the Altria Group, Inc., consisting of John Middleton Co., Philip Morris USA, Inc. and U.S. Smokeless Tobacco Manufacturing Co. LLC (the Altria Group). The comment received in response to T.D. TTB–81 was submitted on behalf of the Campaign for Tobacco-Free Kids. The two comments received in response to T.D. TTB–75 and referenced below were submitted on behalf of Domestic Tobacco Co., and National Tobacco.

Two individuals submitted comments that were not pertinent to the regulations at issue and therefore are outside the scope of this final rule. One comment discussed techniques for quitting smoking and the other discussed subsidies for health insurance. These comments are not discussed further in this document. Descriptions of the remaining comments, along with TTB’s responses, are set forth below, with the exception of the comments on the package use-up period that were addressed in T.D. TTB–81.

General Comments

Comment

The Altria Group commented that TTB should, in the future, consult with industry through roundtable discussions, or stakeholder meetings, prior to issuing "this type of broad regulatory program." National Tobacco commented that TTB should consider establishing an advisory committee, consisting of a panel of industry experts, for providing TTB with industry input on a variety of issues, including distinguishing between pipe tobacco and other tobacco products and simplifying the recordkeeping requirements.

TTB response: Because of the short time period between enactment of CHIPRA and the effective date of its provisions, expedited adoption of the implementing regulations was necessary and precluded advanced consultation with industry. Moreover, publication of the notice inviting comments on the temporary provisions is an effective means to obtain public input to be taken into account at the final rule stage.

With regard to the suggestion that TTB set up an advisory group, TTB agrees that obtaining input from the regulated industry as well as other members of the public, prior to rulemaking, is valuable. TTB often receives and considers information from industry members, State and Federal regulators, and other interested parties, which assists in the development of policy positions. TTB is also currently evaluating additional ways of obtaining input from all interested parties beyond notice and comment rulemaking and ad hoc communications.

Specifically in regard to the distinction between pipe tobacco and roll-your-own tobacco, TTB has found that the publication of an advance notice of proposed rulemaking (Notice No. 106, 75 FR 42659, published in the **Federal**

Register on July 22, 2010) and the reopening of the comment period for that rulemaking (in Notice No. 120, 76 FR 52913, published in the **Federal Register** on August 24, 2011) has been an effective method of receiving thoughtful and substantive written comments from industry members and other interested parties.

Definitions of “Processed Tobacco,” “Package,” and “Packaging”

Comment

National Tobacco requested that TTB amend the definition of “processed tobacco” in §§ 40.11 and 41.11 in such a way that the permit requirement would not apply when processed tobacco is used in the flavoring industry, in ceremonial Native American and other religious activities, in chemical extractive industries, in pharmaceuticals, and in agricultural pesticides and fertilizer.

TTB response: TTB believes that the legislation is concerned with processed tobacco that could be used to make a tobacco product. At this point, TTB has no regulatory standard that would distinguish the “processed tobacco” that could be used to make a tobacco product from “processed tobacco” that could not be used to make a tobacco product. However, TTB does make a determination on a case-by-case basis, considering the particular circumstances of a processing operation and consistent with the statutory language. TTB will consider future amendments to the regulations in this matter.

Comment

R.J. Reynolds expressed concern that the definition of “package” treats all packages of processed tobacco weighing 10 pounds or less as a taxable

product. R.J. Reynolds asserted that this does not account for the “legitimate needs” companies have of shipping small samples of processed tobacco and proposed that TTB amend the definitions of the terms “package” and “processed tobacco” to better accommodate such shipments. Specifically, R.J. Reynolds proposed that the second sentence of the definition of package in § 40.11 be revised to read as follows: “For purposes of this definition, a container of processed tobacco, the contents of which weigh 10 pounds or less, that is removed within the meaning of this part and offered for sale or delivery to the ultimate consumer is deemed to be a taxable tobacco product as referenced with this part.” [Emphasis in the original.] R.J. Reynolds also suggested that TTB consider package graphics (that is, markings and designations) and the way that the product is marketed and offered for sale.

TTB response: The issue R.J. Reynolds raised of shipping small samples of processed tobacco is addressed below in the recordkeeping and reporting requirements section of this comment discussion. With regard to the specific language proposed by R.J. Reynolds, TTB believes that adopting the proposal would be problematic as it would only recognize a container as a “package,” and therefore, a taxable commodity, if the container is *actually* offered for sale or delivery to the consumer by the manufacturer. This would be inconsistent with the statutory language for pipe tobacco and roll-your-own tobacco which only requires that the packaging of a product make it suitable for use and *likely* to be offered to, or purchased by, consumers.

With regard to the proposal that TTB consider package graphics and marketing in determining when processed tobacco is deemed a taxable product, TTB believes that the consideration of package graphics, along with physical characteristics, is appropriate for further consideration and notice and comment in a separate rulemaking action. Setting forth specific, potentially limiting, standards for package graphics in this final rule without providing the general public, including other industry members, an opportunity to comment on such standards would not be appropriate. Similarly, how a product is marketed and offered for sale also warrants further consideration and notice and comment.

Comment

The Altria Group requested clarification of the last sentence of 27 CFR 40.61(c), which states: “For the purposes of this section, the activity of packaging processed tobacco may be sufficient to qualify as a manufacturing activity.” The emphasis was added by the commenter who asserted that this phrase is vague and discretionary, both for those who seek to obtain permits and for those who might contract with such entities for packaging services. The Altria Group expressed concern that, as written, § 40.61(c) “could be interpreted to allow a permit for the packaging of pipe tobacco or snuff (loose tobacco that could be called processed tobacco), but not the packaging of cigarettes or cigars (clearly fashioned into an actual product).” The commenter stated that if TTB intended for the tobacco to be considered processed tobacco until it is put into a package, then the Bureau should clarify that intent in the regulations.

TTB response: The regulatory text at § 40.61(c), as amended by T.D. TTB-78, states that the activity of packaging processed tobacco may be sufficient to qualify as a manufacturing activity, for the purposes of requiring the packager to obtain a permit as a tobacco product manufacturer. The text is not ambiguous as to whether it applies to cigars and cigarettes. It should be noted that the activity of packaging cigars and cigarettes is not sufficient to qualify a person as a manufacturer of tobacco products as both cigars and cigarettes already clearly meet all the considerations in the applicable statutory definitions (at 26 U.S.C. 5702(a) and (b), respectively) prior to their packaging. A cigar or cigarette is distinguishable as a roll of tobacco wrapped in paper, tobacco, or a substance not containing tobacco, before the products are put up in consumer packages.

Single Entities Operating Multiple Locations Under the Same Permit

Comment

Two industry members (National Tobacco and Schweitzer-Mauduit) and Customs Advisory Services Inc. suggested that TTB allow a single legal entity to operate multiple factories under a single permit for the manufacture of processed tobacco. National Tobacco argued that “[r]equiring separate permits for each location is anachronistic in an age when central recordkeeping and global information sharing are the norm.” National Tobacco further suggested that the “person” who must qualify for a permit under § 40.61(a) should refer to an individual, company, corporation, partnership, or other legal entity, rather than to a location. Schweitzer-Mauduit requested clarification of its understanding that

the TTB regulations require “one application for permit and one monthly report from each corporation that manufactures processed tobacco at more than one facility.” R.J. Reynolds asked whether a manufacturer of tobacco products could store processed tobacco in warehouse facilities not located in the vicinity of its manufacturing facilities or whether those facilities had to be located in the vicinity of the factory. Customs Advisory Services Inc. asserted that “[c]onfusion exists in the trade regarding the number of permits required and the tobacco reporting requirements for companies operating multiple factories for the manufacture of processed tobacco,” and that the reporting requirements for intercompany movements of tobacco between factories and storage warehouses operated by the same legal entity are not clearly described by the regulations. The commenter recommended that the regulations be clarified to allow a single legal entity to operate multiple facilities under a single permit.

Finally, National Tobacco extended the suggestion of a single permit to cover multiple locations to also apply to manufacturers of tobacco products. Specifically, National Tobacco suggested that TTB also amend §§ 40.61 and 40.62 to allow each manufacturer of tobacco products to obtain a single permit covering multiple locations, as well as the importation of tobacco products, to eliminate any duplication of records that results from operating under multiple permits.

TTB response: The issue of allowing the permit of a manufacturer of tobacco products to cover multiple manufacturing locations and also importation is not an issue appropriate for resolution in this final rule document because it

was not raised in, and goes beyond the scope of, T.D. TTB-78. With regard to the comment that a person, rather than a location, must qualify for a permit, TTB points out that the IRC at 26 U.S.C. 5712 and 5713 requires that the determination of whether an applicant is qualified to obtain a permit depends on, among other factors, consideration of the premises. In very general terms, section 5712 requires that an application for a permit be evaluated on three factors: (1) The premises upon which business will occur, (2) the proposed business activities, and (3) the person intending to engage in such business. Specifically, section 5712 provides that an application for a permit may be rejected and the permit denied if the Secretary finds that “the premises on which it is proposed to conduct the business are not adequate to protect the revenue.” This provision obligates TTB to evaluate the premises upon which business is proposed to be conducted in order to determine whether to issue a permit. Similarly, an existing permit may be revoked or suspended under 26 U.S.C. 5713 if the permittee has failed to maintain the premises in such manner as to protect the revenue. As a result, a permit authorizes a person to engage in business only at a specific location. The location where business may take place under the permit may be changed, where authorized under the TTB regulations, but the permit continues to be tied to a specific location under the statute.

TTB agrees with the comments that point out that TTB needs to address the activities that may be undertaken on, and the boundaries of, the physical premises delineated by the permit of a manufacturer of processed tobacco. In considering this matter, TTB reviewed the regulations that apply to the premises

of manufacturers of tobacco products to determine whether and to what extent those provisions may be appropriate to the activities of manufacturers of processed tobacco. The regulations at § 40.72(a) specifically prescribe the scope and use of a tobacco product manufacturer's premises. Under that section, the premises used by a manufacturer of tobacco products for the factory are to be used exclusively for the purposes of manufacturing and storing tobacco products; storing materials, equipment, and supplies related thereto or used or useful in the conduct of the business; and carrying on activities in connection with business of that manufacturer. Further, § 40.69 addresses premises that incorporate portions of buildings and multiple non-contiguous buildings, and when diagrams of such premises must be submitted to TTB. Under that section, the premises used by a manufacturer of tobacco products may consist of more than one building, or portions of buildings, which need not be contiguous but must be located in the same city, town, or village. Where not so located, the appropriate TTB officer may authorize the inclusion of buildings, or portions of buildings, that are so conveniently and closely situated to the general factory premises as to present no jeopardy to the revenue or hindrance to the administration of the regulations. The buildings or portions of buildings must be described in the application for permit and the regulations require the submission of a diagram in certain circumstances. If the factory premises are to be changed to an extent that will make inaccurate the description of the factory set forth in the last application, § 40.114 requires that a manufacturer of tobacco products

submit an application for an amended permit before changes are made to the premises.

The current regulations described above speak to the delineation of the factory premises of a manufacturer of tobacco products but the temporary regulations do not, as the commenters point out, address issues regarding the factory premises of a manufacturer of processed tobacco. In addition, since publication of the temporary regulations, TTB has fielded a number of questions from industry members regarding whether the existing concepts applicable to the premises of manufacturers of tobacco products apply to the premises of manufacturers of processed tobacco.

TTB believes that the provisions of § 40.72(a) regarding the activities that may take place on the factory premises of a manufacturer of tobacco products are appropriate to apply to the factory premises of manufacturers of processed tobacco, with some modification. Similar to the provisions set forth for manufacturers of tobacco products, for manufacturers of processed tobacco, the premises must be used for the manufacturing and storing of, in this case, processed tobacco; storing materials, equipment, and supplies related to the processing of tobacco or used or useful in the conduct of the business; and carrying on activities in connection with business of the manufacturer of processed tobacco. Just as with the manufacturing of tobacco products, TTB believes that any activity related to the business of processing tobacco must be undertaken only on premises delineated by a TTB permit. The physical premises delineated by the permit must include all buildings or portions of buildings in

which such activities take place. TTB believes that in the context of a manufacturer of taxable tobacco products, it is necessary and appropriate to require that only buildings in close proximity to the factory be included as part of the factory in which such products are manufactured. In that context, extending the factory premises to include buildings not within geographic proximity would allow for the inappropriate deferral or “downstreaming” of the payment of tax beyond the point of manufacture. The same consideration does not apply to processed tobacco, and in that context TTB believes that extending the factory premises to allow for it to include all buildings, even those not within geographic proximity, would allow for more efficient recordkeeping and reporting, as described in several comments, without any readily-apparent revenue or administrative burden consequence. Therefore, this final rule provides that the factory premises of a manufacturer of processed tobacco may consist of more than one building, or portions of buildings, which need not be contiguous nor must they be located in the same city, town, village, or State. The manufacturer of processed tobacco in its permit application must identify and describe all buildings or portions of buildings where any activity related to the processing of tobacco, as described under § 40.11, takes place and also where any processed tobacco is stored pending removal for transfer to another entity. The manufacturer must also designate a central location as a repository of records sufficient to incorporate all activities involved under the permit.

As a result, TTB sets forth in this final rule a new section, § 40.502, which in paragraph (a) is similar to the regulations at § 40.72 regarding what buildings

and activities are to be covered by the factory premises and what location information must be submitted with the permit application. Section 40.502 differs from § 40.69 in that it provides that the buildings that make up a factory for manufacturing processed tobacco need not be within a certain proximity to each other; and, in paragraph (b), mirrors the regulations at § 40.114 regarding changes (extensions and curtailment) of factory premises. A paragraph (b) is added to require that manufacturers of processed tobacco operating under a permit issued prior to the effective date of this final rule submit the required location information within 180 days of the effective date. In addition, the requirements set forth at § 40.521 regarding the records that a manufacturer of processed tobacco must keep are amended to include records of transfers between buildings that are covered under the same permit but that are not located in the same city, town, village, or State.

TTB believes that this new section, § 40.502, provides a result consistent with that requested by the commenters, and adds clarification with regard to the point at which TTB F 5250.2 (Report of Removal, Transfer, or Sale of Processed Tobacco) must be submitted, that is, when a “removal,” for purposes of the reporting requirement, takes place.

Similar considerations also apply to importers of processed tobacco. Under the IRC at 26 U.S.C. 5702(k), an importer of processed tobacco is any person in the United States to whom any processed tobacco manufactured in a foreign country, Puerto Rico, the Virgin Islands, or a possession of the United States is shipped or consigned. An importer of processed tobacco may obtain

release from customs custody of processed tobacco and store the tobacco until it is sold or transferred to another entity. Such a sale or transfer must be reported on TTB F 5250.2, in accordance with § 41.262(d). As a result, this final rule amends the TTB regulations at §§ 41.237 and 41.253 to specifically require that the application for a permit to be an importer of processed tobacco set forth the location to be used as the principal business office and the locations in which the importer stores processed tobacco and that any change in the designated locations be submitted to TTB as an amendment to the importer's permit. This final rule also adds a new § 41.264 to specify that the importer of processed tobacco is subject to inventory requirements at the same times as those required of manufacturers of processed tobacco under § 40.523, that is, at the time of commencing business, at the time of transferring ownership, at the time of changing the location, at the time of concluding business, and at such other time as any appropriate TTB officer may require. These new provisions provide that an importer of processed tobacco holding a permit issued prior to the effective date of the final rule has 180 days to submit to TTB the information regarding the location and inventory now required. The recordkeeping requirements applicable to importers of processed tobacco, set forth at § 41.261, are also amended to require that the records of an importer of processed tobacco include information on transfers between buildings that are covered under the same permit but that are not located in the same city, town, village, or State.

Use of Factory Premises for Other Business

Comment

National Tobacco suggested that TTB amend 27 CFR 40.47 and 40.72 to authorize the storage and manipulation of non-tobacco smoking products such as tobacco-free herbal hookah/shisha on the premises of tobacco product manufacturers. National Tobacco commented that tobacco-free herbal hookah/shisha is typically marketed and distributed through the same channels as tobacco products, and thus is an appropriate adjunct to a line of smoking products. National Tobacco stated that TTB's regulations are not clear as to whether herbal hookah/shisha would be regarded as materials or supplies related to a permit holder's tobacco business.

TTB response: TTB believes this issue is beyond the scope of the temporary rule, as it does not relate to the CHIPRA-related regulatory changes. However, TTB notes that § 40.47(a) provides that a TTB-permitted manufacturer of tobacco products that wishes to engage in any other business on the premises of a tobacco factory may apply to TTB to do so. TTB frequently receives requests from manufacturers of tobacco products to operate varied businesses on their premises. These requests are evaluated on an individual, case-by-case basis. This process eliminates the need for TTB to amend the regulations to authorize each type of "other business." The process set forth at § 40.47(a) is appropriate and adequate to address the scenario described in the comment. A specific regulatory amendment is unnecessary.

Recordkeeping and Reporting Requirements

Comment

R.J. Reynolds, Universal Leaf Tobacco Co. Inc., and Schweitzer-Mauduit all suggested that TTB consider accepting reports electronically.

TTB Response: TTB recognizes the value of accepting reports electronically, and we intend to do so as resources and logistics allow.

Comment

Altadis USA, Inc. proposed that the records required under §§ 40.182 and 40.521 should be monthly records, rather than daily records. According to the commenter, daily reconciliation of processing runs is impossible, and monthly, rather than daily, recordkeeping “makes sense in light of current monthly reporting requirements already in place for manufacturers with respect to shipped tobacco products, and is consistent with the good business practices endorsed by TTB in the temporary rule.” Additionally, Altadis USA, Inc. asserted that the recordkeeping requirements in §§ 40.182 and 40.521 should only apply to leaf tobacco that is received at a facility and that leaves the facility in the form of a tobacco product, or, under § 40.521, is otherwise removed from the facility. Altadis USA, Inc. stated that “the requirements of the temporary rule will not achieve the intended result; indeed the information will be either misleading or meaningless,” explaining in this regard that it is not technologically feasible to measure quantities of processed tobacco at every stage of the manufacturing process because no product exists during the intermediate steps of processing.

The Altria Group similarly argued that the §§ 40.182 and 40.521 daily recordkeeping requirements for manufacturers of tobacco products who also process tobacco are unduly burdensome, although, beyond that, the incremental addition of a monthly report and documentation of transfers from the permitted facility are not significantly onerous. They suggested that it would be appropriate, and would impose a more reasonable burden, to require recordkeeping for all transfers of processed tobacco from the permitted facility by the manufacturer but only require submission of the reports to TTB for shipments to unpermitted facilities. The Altria Group asserts that jeopardy to the revenue comes when processed tobacco is transferred to a nonpermitted manufacturer in an untracked manner.

According to R.J. Reynolds and National Tobacco, TTB F 5250.2 (Report of Removal, Transfer, or Sale of Processed Tobacco) imposes a significant administrative burden on industry members. To remedy this, R.J. Reynolds recommended that TTB exempt from the TTB F 5250.2 reporting requirements both shipments of processed tobacco to government agencies and export shipments of processed tobacco. Additionally, the commenter suggested that TTB change the reporting deadline in § 40.522(d) from the close of business the day after the transfer to one week after the transfer.

Schweitzer-Mauduit and Universal Leaf Tobacco Co. Inc. requested that TTB eliminate the requirement to provide details on export shipments of processed tobacco. In support of this, Universal Leaf Tobacco Co. Inc., asserted the following: exports are non-taxable; permitted manufacturers of processed

tobacco maintain export records on their premises that provide sufficient information regarding export movement; and processed tobacco movements are tracked through other TTB forms as well as by other Federal agencies. These two commenters recommended that TTB require submission of TTB F 5250.2 on a monthly, rather than daily, basis. Universal Leaf Tobacco Co. Inc., further suggested amending TTB F 5250.2, and the related regulations, to allow for aggregate reporting of multi-container shipments to a single recipient within any 10 business day period. Customs Advisory Services Inc. also proposed that recordkeeping related to shipments of processed tobacco for export should be done on a daily basis, with summary reporting on a monthly basis. In addition, they proposed that TTB accept commercial records, such as invoices and bills of lading in lieu of the recordkeeping requirements specified in §§ 40.521(b) and 41.261(b), and the reporting requirements specified in §§ 40.522 and 41.262.

TTB response: Based on these comments, TTB has concluded that it would be appropriate to revise the recordkeeping requirements in §§ 40.182 and 40.521 to remove the requirement that tobacco product manufacturers and processed tobacco manufacturers maintain daily processed tobacco records. Tobacco product manufacturers will be required to account for processed tobacco on hand at the beginning and end of each month and will also be required to account for, and provide dates for, receipts of processed tobacco, use of processed tobacco in the manufacture of tobacco products, and any loss or destruction of processed tobacco. Manufacturers of processed tobacco and manufacturers of tobacco products who are required to obtain authorization to

engage in another business within the factory under §§ 40.47(b) and 40.72(b) will also still be required to maintain records of the date on which processed tobacco is received at the factory, removed from the factory, or lost or destroyed. The records of removals must still be made for each day by the close of the business day following the day on which the removal occurs. TTB believes that these changes address the concerns of the commenters regarding the recordkeeping burden, without jeopardizing the revenue.

In addition, TTB has reinstated in this final rule a requirement that was removed by T.D. TTB-78 that manufacturers of tobacco products maintain records of tobacco received and disposed of. Prior to CHIPRA, the requirement set forth at § 40.182 regarding records of “tobacco,” would have included records of what would now be considered “processed tobacco” as well as of tobacco that had not yet been processed. In T.D. TTB-78, TTB amended § 40.182 to reflect the new category of “processed tobacco” by replacing references to “tobacco” with the term “processed tobacco.” Records of tobacco (unprocessed) were no longer required. However, TTB experience since the publication of the temporary rule has shown that the absence of such records hinders TTB’s ability to determine whether the volume of products manufactured in a factory is consistent with the amount of tobacco received, used, and disposed of by the manufacturer. As a result, this final rule amends the recordkeeping requirements set forth at § 40.182 to require that the records of manufacturers of tobacco products include the quantity of tobacco (unprocessed) on hand at the beginning of each month and the quantity received, used, removed, lost, and destroyed

during the month. Section 40.521 is also amended to extend this requirement to manufacturers of processed tobacco.

TTB does not concur with the suggestion by Altadis USA, Inc. that recordkeeping should only apply to leaf tobacco that is received in the factory and that is removed from the factory in the form of a tobacco product. TTB believes that the type of recordkeeping recommended by the commenters is the same recordkeeping that was in place prior to the statutory amendments of CHIPRA, that is, before TTB was mandated by Congress to regulate processed tobacco. The regulation of processed tobacco consistent with the goals of CHIPRA, that is, to prevent its being provided to entities operating illicit manufacturing operations, requires that manufacturers of tobacco products who remove processed tobacco for shipment to other entities be required to keep records of such shipments and that those records be made available to TTB. Thus, records of the movement of processed tobacco from a tobacco product manufacturer's facility, and not only records related to tobacco products, are necessary. However, TTB believes that changing the recordkeeping requirements as described above, from a daily to a monthly or situation-specific accounting of certain processed tobacco, may also address the concerns raised in this comment to the extent that it reduces the burden of accounting for processed tobacco within a continuous manufacturing process.

With regard to exports of processed tobacco, TTB agrees that submission of the TTB F 5250.2 may not be necessary in some cases. We are amending the regulations at §§ 40.522 and 41.262 to provide that manufacturers and

importers that remove processed tobacco for export may, in lieu of submitting the TTB F 5250.2 by the close of business the day after the removal, submit a monthly summary report of removals upon written approval of the appropriate TTB officer. A manufacturer or importer that wishes to operate under such an alternative must apply for authorization to do so by submitting a written request to the appropriate TTB officer. The request must be accompanied by an example of the format intended for the monthly summary report. Such exporters are still required to maintain on their premises records of all export shipments, including records of the circumstances surrounding those shipments. At this time, we believe that if manufacturers and importers of processed tobacco maintain records related to export transactions on their premises, which must be made available to TTB for review upon request, TTB will have sufficient access to information related to exports to follow potential leads for diversion and thus protect the revenue. We note that manufacturers and importers of processed tobacco will, except in certain cases discussed below, still be responsible for submitting TTB F 5250.2 for all other (domestic) removals by the close of the business day following the removal, sale, or transfer. We believe that to do otherwise, such as to delay reporting by one week or longer to allow for aggregate reporting to a single recipient, would remove an important enforcement tool, that is, timely and detailed information about shipments of processed tobacco to entities not operating under a TTB permit.

With regard to recordkeeping, as is general practice, TTB will consider requests for alternate methods or procedures related to records of processed

tobacco, provided that the proposed alternate method or procedure is consistent with the effect intended by the required procedure and it provides equivalent protection of the revenue. However, for clarity, a new sentence is added to §§ 40.521(c) and 41.261(c) specifically providing industry members with the option of applying for an alternate method or procedure with regard to recordkeeping related to shipments using commercial carriers.

Comment

TTB received comments from the Altria Group and Customs Advisory Services Inc. requesting clarification of whether importers of processed tobacco may receive domestic processed tobacco and, if so, how such receipts should be reflected in the required records and reports. The Altria Group also asked TTB to clarify the recordkeeping and reporting requirements for importers of processed tobacco who are also manufacturers of tobacco products.

Customs Advisory Services Inc. requested clarification of the meaning of the recordkeeping requirements at § 41.261(a)(2) that apply to importers of processed tobacco. That paragraph requires importers of processed tobacco to maintain records of the date and quantity of processed tobacco received “otherwise than through importation.” Customs Advisory Services Inc. asserts that, when that section is viewed alongside the monthly report form (TTB F 5220.6), it is unclear whether Line 8 of TTB F 5220.6, which requires accounting of tobacco products and processed tobacco “received from other sources,” would cover processed tobacco received from a domestic manufacturer or processed tobacco received from another importer. Customs

Advisory Services Inc. recommended that TTB expand and clarify the scope of § 41.261(a)(2) and provide separate lines on TTB F 5220.6 “to show imported tobacco received from other importers of processed tobacco and processed tobacco received from domestic producers of processed tobacco.” Finally, Customs Advisory Services Inc. recommended that TTB modify the removals section of the monthly report required of the domestic manufacturer of processed tobacco (TTB F 5250.1) to provide a specific line for reporting removals of processed tobacco shipped to an importer of processed tobacco. The commenter believes that the failure to account for these removals would result in substantial quantities of processed tobacco not being reported.

With regard to the issue of an importer of processed tobacco also being a manufacturer of tobacco products, the Altria Group states that it is unclear whether the recordkeeping and reporting requirements for an importer of processed tobacco that is also a manufacturer of tobacco products apply with regard to the imported tobacco consumed in the company’s manufacturing operations. According to the Altria Group, to the extent that the temporary regulations are intended to apply to such internal consumption, they are unduly burdensome for the importer, stating in this regard as follows: “Where a large volume of tobacco is imported and the vast majority is consumed in the manufacturing process of the importer, it is an onerous requirement to record and report each and every transaction of transfer to the manufacturing facility.” The Altria Group further asserts that the TTB regulations, presumably in § 41.261, do not clearly state whether records must be maintained for the transfer of imported

processed tobacco from storage to the manufacturing facility, suggesting that TTB require recordkeeping and reporting only of transfers of imported processed tobacco outside the company.

Finally, R.J. Reynolds stated that, like manufacturers of processed tobacco, importers of processed tobacco should be required to complete the TTB F 5250.2 (Report of Removal, Transfer, or Sale of Processed Tobacco).

TTB response: Regarding the transfer of domestic processed tobacco to an importer of processed tobacco, we agree that the regulations in question are ambiguous and, therefore, in this final rule we are amending §§ 40.521(a)(4) and (a)(5) and 40.522(d) setting forth recordkeeping and reporting requirements to specifically incorporate language showing that a manufacturer of processed tobacco may transfer domestic processed tobacco to an importer of processed tobacco. Such transfers are recorded and reported in the same way that transfers of processed tobacco are made from a manufacturer of processed tobacco to another manufacturer of processed tobacco or to a manufacturer of tobacco products or an export warehouse proprietor. In addition, in response to Customs Advisory Services Inc.'s suggestion, we intend to amend TTB F 5250.1 to specifically provide for the reporting of removals of processed tobacco shipped to an importer of processed tobacco.

We do not believe at this time that § 41.261(a)(2) needs to be amended to clarify its scope with regard to an importer of processed tobacco receiving processed tobacco from a domestic manufacturer of such tobacco. The regulatory text currently requires that records be maintained reflecting the date

and quantity of processed tobacco “received otherwise than through importation,” and that phrase includes any receipt such as the type in question. Similarly, we do not believe that TTB F 5220.6 needs immediate amendment to provide for receipts from domestic manufacturers of processed tobacco or from other importers, as it currently requires accounting of processed tobacco “received from other sources” and this phrase also includes any receipt that is not a direct importation. However, we do intend to provide clarifying instructions to TTB F 5220.6 after publication of this final rule.

In addition, TTB acknowledges that there is no line on the monthly report of importers of processed tobacco (TTB F 5220.6) specifically dedicated to reporting the amount of imported processed tobacco consumed in the manufacturing process, as noted in the Altria Group’s comments. TTB regulations consider importing and manufacturing to be two distinct businesses whose operations are covered by two separate permits, with their own respective recordkeeping and reporting requirements. Accordingly, where processed tobacco is imported by the same entity that uses it in the manufacture of tobacco products, to create a complete record, the importation must be reflected in the records and on the monthly report of the importer, under that importer’s permit number, and such report and records also must show the processed tobacco as transferred to the records associated with the permit of the manufacturer, even if the entity that holds the importer permit and the manufacturing permit are the same entity.

In response to the Altria Group's comments that this is an "unreasonable burden" on importers of processed tobacco who are also manufacturers of tobacco products, we note that the recordkeeping and reporting requirements for manufacturers of tobacco products who import tobacco for use in such manufacture are similar in scope to the requirements that were in effect prior to the amendments made in response to CHIPRA. Previous regulations at §§ 40.181–40.183 required that a manufacturer of tobacco products maintain records of the date and quantity of all tobacco other than tobacco products received, together with the name and address of the person from whom received. The new provisions require accounting for processed tobacco, but also require records that connect the processed tobacco imported under an importer's permit to that transferred to and used by a manufacturer of tobacco products under a different permit. We believe this tracking of processed tobacco between the importation and the use in manufacture is necessary to regulate processed tobacco as required by CHIPRA.

In response to R.J. Reynolds's suggestion that TTB require importers of processed tobacco to submit TTB F 5250.2 when they make shipments to entities that do not possess a permit, we note that the regulations already require such submissions. Section 41.262(d) requires an importer who transfers or sells processed tobacco to someone other than a person holding a TTB permit to report such sale or transfer on TTB F 5250.2 by the close of the business day on the day following the transfer or sale.

Comment

We received five comments from industry members requesting that TTB revise the regulations to allow an exemption from certain reporting and recordkeeping requirements related to shipments of processed tobacco as samples or for experimental and other small quantity purposes, or allow an exemption from the requirement that a manufacturer of tobacco products must obtain authorization to operate as a manufacturer of processed tobacco if that manufacturer removes processed tobacco for purposes other than destruction. A few comments addressed in particular that portion of the definition of “package” in § 40.11 that provides that a container of processed tobacco weighing 10 pounds or less (including any non-tobacco ingredients or constituents), that is removed within the meaning of that term in the regulations, is deemed to be a package for sale or delivery to the ultimate consumer.

Schweitzer-Mauduit and R.J. Reynolds both asserted that the “10 pounds or less” weight specified in the § 40.11 definition is unduly restrictive because manufacturers ship small amounts of processed tobacco that are samples for testing or analysis and thus are not intended to be used as roll-your-own tobacco, pipe tobacco, or any other taxable tobacco product. Similarly, National Tobacco asserted that most shipments of processed tobacco are “of a limited noncommercial nature, such as test samples to labs, batch samples for export, batch samples from new importers, samples direct from farmers for evaluation.” National Tobacco recommended that TTB require weekly rather than daily reporting of such transfers, or, as an alternative, that TTB create an exception to

the reporting requirement for sample shipments of a certain weight, for example, two pounds.

In addition to the transfer of samples of processed tobacco for experimental purposes, Universal Leaf Tobacco Co. Inc., commented that “the sale of processed tobacco is often carried out through the delivery of a representative sample of the processed tobacco to a prospective buyer” as a “slice” of processed tobacco, which typically weighs between five and 10 pounds. Universal Leaf Tobacco Co. Inc., explained that the samples are extremely small portions of the processed tobacco being sold and are not fit for direct consumption in the marketplace; they therefore requested that the regulations be amended to exclude samples from the reporting requirements on TTB Forms 5220.6, 5250.1, and 5250.2. R.J. Reynolds alternatively suggested that TTB add lines to the monthly report, TTB F 5250.1, to report tobacco shipped as samples to potential customers or government agencies not intended for sale and tobacco shipped off of the premises for experimental purposes.

In its comments, the Altria Group claimed that because there is no tax on processed tobacco, there is no immediate jeopardy to the revenue related to the transfer of processed tobacco unless the processed tobacco is transferred to an unpermitted facility. Accordingly, the comment suggested that TTB exempt manufacturers of tobacco products that also manufacture processed tobacco from the requirement to obtain authorization to engage in either the removal of processed tobacco for experimental purposes or the transfer of processed tobacco between permitted facilities, by providing manufacturers of processed

tobacco with exceptions similar to those provided for manufacturers of tobacco products, such as the experimental purposes provision in § 40.232, and the exemption for transfer in bond (between permitted facilities) provided for in § 40.233. The Altria Group stated that these provisions provide an opportunity for a manufacturer to test machinery using tobacco products, conduct testing of tobacco products, and transfer tobacco products among permitted facilities for product development or other legitimate business purposes without payment of tax so long as certain records are maintained. With regard to removals for experimental purposes, the Altria Group suggested that the manufacturer of tobacco products be exempt from the requirement to obtain authorization to operate as a manufacturer of processed tobacco under 27 CFR 40.72(b) if that manufacturer removes processed tobacco for experimental purposes or for transfers between permitted facilities. The comment recommended requiring recordkeeping of all such transfers and also requiring that the processed tobacco either be destroyed in the testing process or be returned to the manufacturer for documented destruction. The Altria Group also proposed that a manufacturer submit to TTB an initial notice that the manufacturer intended to engage in such transfer activities.

TTB response: TTB believes that the basic point made by these commenters is valid. Accordingly, in this final rule document we have amended § 40.72(b) to provide that a manufacturer of tobacco products that processes tobacco on the factory premises solely for use in the manufacture of tobacco products under that permit and that removes the processed tobacco from those

premises only for purposes related to the business of a manufacturer of tobacco products, and not for purposes related to the business of a manufacturer of processed tobacco, may engage in those operations without obtaining prior authorization from TTB. Under the new text of § 40.72(b)(2), removals of processed tobacco that are considered removals for purposes related to the business of a manufacturer of tobacco products, and therefore do not require TTB authorization, include removals of samples for soliciting orders of tobacco products and removals of processed tobacco for destruction, for scientific testing or testing of equipment, and for transfer between permitted premises of the same manufacturer. A manufacturer of tobacco products who engages in any of these removals and who maintains adequate records of the disposition of such processed tobacco may engage in such removals without first obtaining authorization from TTB. Any removal not adequately supported by records and any other type of removal other than those listed will be treated as a removal related to the business of a manufacturer of processed tobacco, for which the manufacturer of tobacco products must first obtain authorization to engage in another business within the factory under § 40.47 and keep records and submit reports under §§ 40.521 and 40.522, unless the manufacturer can show to the satisfaction of the appropriate TTB officer that the removal is connected with the business of a manufacturer of tobacco products. In this final rule TTB has amended §§ 40.47(b), 40.202(b), and 40.491 to conform to the changes made in § 40.72(b).

TTB also amended § 40.522(d) to provide exceptions from the reporting of certain removals on TTB F 5250.2. TTB F 5250.2 is used by a manufacturer or importer to report certain removals of processed tobacco; the form must be submitted to TTB by the close of the business day on the day following the removal. Under the temporary regulations, § 40.522(d) requires manufacturers to report on TTB F 5250.2 any removals of processed tobacco for shipment to any person not holding a TTB permit as a manufacturer of processed tobacco, a manufacturer of tobacco products, or an export warehouse proprietor. The final regulations no longer require manufacturers of tobacco products to report removals of processed tobacco to entities not holding such permits if those removals are for purposes related to the business of a manufacturer of tobacco products, such as removals for destruction, for scientific testing or testing of equipment, for soliciting orders of tobacco products, or for transfer between permitted premises of the same manufacturer. These exceptions to the reporting requirement are described in § 40.72(b)(2). In addition, manufacturers of processed tobacco will not be required to report on TTB F 5250.2 any removals of processed tobacco for destruction, scientific testing, or testing of equipment that result in the destruction of the processed tobacco or the return of the tobacco to the factory premises. Similarly, TTB has added a new paragraph § 41.262(d)(3) stating that an importer of processed tobacco that ships or transfers processed tobacco for scientific testing which results in the destruction of the processed tobacco is not required to report such shipment or transfer on

TTB F 5250.2. Manufacturers and importers must still report such removals on their respective monthly reports.

Comment

We received two additional comments from R.J. Reynolds regarding recordkeeping and reporting requirements for manufacturers of processed tobacco. R.J. Reynolds requested confirmation that physical possession (and not ownership) of processed tobacco is the primary criterion used to identify the permit holder responsible for reporting the associated activity. Additionally, R.J. Reynolds asked that TTB acknowledge the likelihood of variations in the weight of processed tobacco as it is blended with other ingredients and as it gains and loses moisture due to the atmospheric conditions of the manufacturing process. R.J. Reynolds asks that TTB provide guidance on how these variations are to be reported.

TTB response: In response to the first point, as a general principle, TTB agrees that physical possession and control over the removal of the processed tobacco triggers the recordkeeping and reporting requirements, rather than only legal ownership of the processed tobacco. The permittee is responsible for the physical movement of the processed tobacco and the permittee who removes the processed tobacco from its factory is responsible for reporting the transfer. With regard to the second point, we acknowledge that there can be significant variations in the weight of processed tobacco. Because the variation in the weight of processed tobacco is specific to each industry member's manufacturing process, any standardized guidance by TTB would be too limiting on industry

members to include in this final rule or too general to account for individual variations. Accordingly, manufacturers of processed tobacco should maintain records supporting any variations in weight throughout their manufacturing process.

Comment

Universal Leaf Tobacco Co. Inc., requested that TTB remove the signature requirement from TTB F 5250.2 because no signature is required under the pertinent regulatory provisions at § 40.521. Schweitzer-Mauduit and Universal Leaf Tobacco Co. Inc., requested that TTB remove the requirement for personal information about the person picking up the processed tobacco for delivery, that is, lines 16, 17 and 18 of TTB F 5250.2. These lines require the person be identified by name, address, and government-issued identification number (such as a driver's license number) and that the vehicle be identified by license tag number. According to Universal Leaf Tobacco Co. Inc., "this requirement infringes on certain privacy matters." Schweitzer-Mauduit asserts that such collection of information is burdensome for its employees, while the drivers about whom information is collected find the inquiry intrusive and objectionable.

TTB response: With regard to the requirement that TTB F 5250.2 bear a signature, the IRC at section 6061 provides that any return, statement, or other document required to be made under any provision of the internal revenue laws or regulations shall be signed in accordance with forms or regulations prescribed by the Secretary of the Treasury. The TTB regulations at 27 CFR 40.41 provide

that the appropriate TTB officer is authorized to prescribe all forms required by part 40 and that all of the information called for in each form shall be furnished as indicated by the headings on the form and by the instructions on or pertaining to the form. In addition, § 40.41 states that information called for in each form shall be furnished as required by part 40 and that, when a return, form, claim, or other document called for under part 40 is required by part 40, or by the document itself, to be executed under penalties of perjury, it shall be executed under penalties of perjury. The same provisions apply to part 41, with regard to importers, under § 41.21. The form itself is required under §§ 40.522(d) and 41.262(d), which state, in pertinent part, that the TTB F 5250.2 must be submitted "in accordance with the instructions on the form." Accordingly, the signature requirement need not be specifically restated in the regulations.

Also, information about the driver and vehicle involved in the removal of processed tobacco from the regulated premises provides TTB with information that has been found effective in tracking processed tobacco and preventing diversion to illegal manufacturers. TTB believes that the information we require at that point is the minimum necessary to ensure protection of the revenue by tracking processed tobacco. It remains the position of TTB that both importers and manufacturers must provide TTB with certain information regarding the person involved in the delivery of the processed tobacco to a person who does not have the appropriate TTB permit. The information that we are requiring is consistent with similar recordkeeping required under the Contraband Cigarette Trafficking Act (CCTA), 18 U.S.C. chapter 114, which deals primarily with

contraband cigarettes and smokeless tobacco and is administered by the Department of Justice, Bureau of Alcohol, Tobacco, Firearms, and Explosives (ATF). However, in considering these comments, TTB has determined that, rather than the personal address of the person picking up the shipment, a more appropriate requirement would be the business address of the company for which the driver works. As a result, in the final rule, the word “business” is added in §§ 40.521(b)(2) and 41.261(b)(2) to clarify that records of the business address of the driver picking up the processed tobacco must be kept, rather than the driver’s personal address. Further, in this final rule both §§ 40.521 and 41.261 have been amended to specify that an alternate method may be approved for the collection of such information in the case of shipments by common carrier. Section 41.261 has also been amended to incorporate some technical changes for clarity and for consistency with the language contained in § 40.521.

Comment

Customs Advisory Services Inc. recommended that the inventory reporting requirement be clarified, specifically with regard to how often TTB F 5210.9 (Inventory—Manufacturer of Tobacco Products or Processed Tobacco) must be submitted. The commenter points to the temporary regulations at 27 CFR 40.523 that require a manufacturer to make an inventory “at the time of commencing business, at the time of transferring ownership, at the time of changing location of the factory, at the time of concluding business, and at such other time as any appropriate TTB officer may require,” and asserts that reporting

of inventory only upon the opening and closing of business operations “could be meaningless reporting for companies with ongoing operations” but that the phrase “* * * and at such other time as any appropriate TTB officer may require” is vague and undefined.

R.J. Reynolds asserted that there are “major inconsistencies” within the proposed regulations regarding the reporting of inventories. Under § 40.523, a manufacturer of processed tobacco operating under the transitional rule set forth in § 40.493 must make a true and accurate inventory on TTB F 5210.9 within 10 days of the date of TTB's written acknowledgement of the receipt of the application filed under § 40.492. R.J. Reynolds points out that importers of processed tobacco are not required to provide a similar inventory and, as these entities could easily have inventory in their possession, a similar reporting should be required. In addition, R.J. Reynolds believes that, because the date of the initial inventory and the dates that must be covered by a manufacturer's first monthly reports do not correspond, the relationship between the two types of reports is unclear.

TTB response: With regard to the comments from Customs Advisory Services Inc., under § 40.523, the phrase “at such other time as any appropriate TTB officer may require” provides TTB with the authority to require an inventory when necessary, for example, in connection with an audit or investigation of an industry member, which is the most common use by TTB of the authority to require an inventory. The same language appears in § 40.201 which sets forth inventory requirements for manufacturers of tobacco products and has been an

effective tool for TTB in regulating the industry without the burden of monthly inventories. Neither the regulatory text at § 40.523 nor the form TTB F 5210.9 mentions a requirement to submit to TTB an inventory monthly and none is deemed necessary for TTB purposes.

In response to R.J. Reynolds' comments, we agree that for the same reasons a manufacturer of processed tobacco must perform an inventory at specified times, an importer of processed tobacco should also perform an inventory. The omission of this requirement was an oversight. Importers of tobacco products are not currently required to submit inventories because the products that they store and ship could only be taxpaid tobacco products, the tracking of which has been seen as needing less regulatory oversight. However, importers of processed tobacco must account for all processed tobacco imported and also must report on the TTB F 5250.2 processed tobacco shipped to a non-permittee. The inadvertent omission of an inventory requirement for importers of processed tobacco in the temporary regulations is corrected in this final rule through the addition of a new section 27 CFR 41.264 that mirrors the inventory requirement applicable to manufacturers of processed tobacco appearing at § 40.523. TTB authority to require such inventories is set forth in the Internal Revenue Code of 1986 at 26 U.S.C. 5721, and applies equally to manufacturers and importers of processed tobacco.

With regard to the other comments related to TTB F 5250.1 and TTB F 5210.9, we have addressed issues relating to the use of those forms with individual industry members, on a case-by-case basis, since the publication of

T.D. TTB-78, and we do not believe that any further regulatory action is necessary on these points.

Applicants for Permits to Manufacture Processed Tobacco

Comment

Two commenters suggested that we amend our regulations to address whether, and to what extent, TTB will consider specific factors when evaluating a tobacco processor's permit application.

The Law Offices of Barry Boren asserted that the regulations addressing "Investigation of Applicant" at 27 CFR 40.498(b) and 41.238(b) imply a life-time ban from obtaining a permit for applicants with a felony conviction. The commenter stated that, in the past, TTB has determined that a felony conviction should not necessarily be a life-time ban to obtaining a permit and that, rather than a life-time ban, five years is a "reasonable ban" in such cases so long as the agency does not have other reasons for denying an application for a permit.

Venable, LLP requested that TTB amend its regulations to clarify that we will only deny a permit to an applicant based on the conduct of an officer, director, or principal stockholder of a company, and only if that person is actively involved in the day-to-day management or operations of the applicant. Venable, LLP referenced two Federal cases from the 1930s to demonstrate that TTB's predecessors, such as the Internal Revenue Service, "primarily based their decisions to deny a permit to an applicant on the level of involvement of the officer, director, or principal stockholder at issue in the day-to-day management or operations of the applicant." Venable, LLP also described the standards for

denial of permits applied by other Federal agencies. Venable, LLP suggested that TTB adopt a “present responsibility” standard, in which “[t]he government frequently finds that companies are ‘presently responsible’ so long as the officer does not control or manage the day-to-day operations of the company, or where the company has instituted sufficient controls to prevent the officer from becoming involved in future government contracts.” In evaluating an officer’s conduct, Venable, LLP recommended that TTB consider mitigating factors, including: (1) The nexus between the activity for which the officer, director, or principal stockholder is under indictment and the applicant’s business operations; (2) whether the officer, director, or principal stockholder is involved in the day-to-day management or operations of the applicant; (3) the applicant’s cooperation with TTB and willingness to take actions to address TTB’s concerns; (4) the applicant’s willingness to implement remedial or monitoring measures determined necessary by TTB; (5) whether the applicant has, or will shortly, implement policies to prevent the future occurrence of offenses; and (6) the likelihood that any legal proceedings against an officer, director, or principal stockholder are likely to be resolved in the person’s favor.

Venable, LLP also requested that TTB consider extending the transitional rule under § 40.493, which provides that manufacturers and importers of processed tobacco already in operation who applied to TTB for a permit by June 30, 2009, could continue to engage in that business pending final action by TTB on the permit application. Venable, LLP stated that the purpose of transitional rule was “to ensure that long-standing manufacturers and processors

that have operated successfully and in compliance with the law are not unfairly denied the right to continue their business.” The commenter suggested an extension to this rule to stay denial of any processed tobacco manufacturer’s or importer’s permit application until there is a final administrative and/or judicial review of their application, or a final resolution of any judicial proceedings involving an officer, director, or principal shareholder of the company.

TTB response: First, the regulations at §§ 40.498(b) and 41.238(b) repeat the standards of review that TTB may use to deny a permit under 26 U.S.C. 5712; the regulatory and statutory texts state that a permit may be denied if TTB finds that the applicant is, by reason of his business experience, financial standing or trade connections or by reason of previous or current legal proceedings involving a felony violation of any other provision of Federal criminal law related to tobacco products, processed tobacco, cigarette paper, or cigarette tubes, not likely to maintain operations in compliance with the provisions of title 26, United States Code, chapter 52, or has been convicted of a felony violation of any provision of Federal or State criminal law relating to tobacco products, processed tobacco, cigarette paper or cigarette tubes, or has failed to disclose any material information required or made any material false statement in the application for permit. The fact that a permit may now be denied for reasons related to a felony conviction does not imply that the permit will necessarily be denied for such a conviction or that such a conviction will result in a life-time ban from obtaining a TTB permit. Rather, as has been the case historically, TTB believes that an individual, case-by-case determination is necessary for each

applicant, given the variability of circumstances. TTB will apply these provisions, as it has applied the provisions related to determining qualification for a permit, by considering all relevant factors. A five-year limitation, as suggested by Mr. Boren, would eliminate TTB's flexibility to individually evaluate each applicant's particular situation. With regard to the mitigating factors suggested by Venable, LLP, although it would not be appropriate to include specific mitigation standards in the regulations, those suggested by Venable, LLP are factors that TTB could reasonably consider when evaluating an application for a permit.

Section 702 of CHIPRA merely adds manufacturers and importers of processed tobacco to the list of persons in sections 5712 and 5713(a) of the IRC who must apply for and obtain a permit from TTB in order to engage in business, while it amends sections 5721, 5722, 5723, and 5741 to add references to processed tobacco with regard to requirements for making inventories, keeping records, packaging and labeling, and reporting. As a result, the same regulatory authority in these areas applies to activities involving tobacco products and processed tobacco.

As for the request that TTB stay the denial of any processed tobacco manufacturer or importer permit application, TTB has no authority to extend the statutory transitional rule reflected in § 40.493. However, TTB does have an administrative process in place in 27 CFR part 71, consistent with Federal administrative law, through which an applicant for a permit may contest TTB's denial of a permit application. Under 27 CFR 71.59, an applicant may request a hearing before an administrative law judge, within 15 days of receipt of notice of

the contemplated disapproval of the application. Thus, TTB's regulations already provide an appropriate administrative process for all permits administered under TTB's authority under the IRC.

Roll-Your-Own and Pipe Tobacco Issues

Comment

John Middleton Co. asserted that the regulations addressing the packaging of pipe tobacco, specifically 27 CFR 40.25a(b)(3)(i), are not authorized by CHIPRA because CHIPRA only mentions pipe tobacco in reference to its tax rate increase. That section deems a product to be roll-your-own tobacco rather than pipe tobacco if the package does not bear the declaration "pipe tobacco" in a specified manner everywhere on the package that the brand name appears. These comments were made in the context of a request for an extension of the time manufacturers and importers could use up existing packaging before being required to come into compliance with the new packaging standards. John Middleton Co., along with the rest of the Altria Group companies, further argued that the temporary regulations place an onerous burden on pipe tobacco products because "the focus on regulation of the pipe tobacco industry is not anticipated, authorized or required by the CHIPRA legislation nor is there anything in CHIPRA that would have alerted manufacturers of pipe tobacco that such requirements would be forthcoming."

TTB response: First, TTB notes that the package use-up period was extended from the original date of August 1, 2009, until March 23, 2010 (see T.D. TTB-81, 74 FR 48650). With regard to the certain points made about the

classification of pipe tobacco and roll-your-own tobacco based on package statements, although CHIPRA did not specifically highlight pipe tobacco beyond the section 701 tax rate increase, as noted in T.D. TTB-78, TTB determined that because of the revenue implications resulting from the tax rate changes made by CHIPRA, there was a need for more regulatory detail to clarify the difference between the two products. Further, as described above, the statutory definitions of pipe tobacco and roll-your-own tobacco both require consideration of the packaging and labeling of the product—specifically, whether the packaging or labeling causes it to be “suitable for use and likely to be offered to, or purchased by, consumers as” tobacco to be smoked in a pipe or as tobacco for making cigarettes or cigars or for use as wrappers thereof. In T.D. TTB-78, TTB set forth regulations regarding how that statutory language would be applied. Those regulations were promulgated under 26 U.S.C. 5723(a) and (b), which provide the authority to prescribe regulations regarding the packaging and labeling of tobacco products, and under 26 U.S.C. 7805(a), which confers on the Secretary of the Treasury the broad authority to prescribe “all rules and regulations as may be necessary by reason of any alteration of law in relation to internal revenue.”

Comment

TTB received two comments that requested that we define “conspicuousness” as it is used in § 40.25a(b)(3)(i). That regulatory provision refers to a package that does not bear the “pipe tobacco” declaration “in substantially the same conspicuousness of type and background as the brand

name,” the result of which is that the package would be deemed roll-your-own tobacco rather than pipe tobacco for tax purposes.

The Law Offices of Barry Boren suggested that, because the term “conspicuousness” is not defined in TTB’s regulations, TTB should adopt the definition of conspicuousness used in the U.S. Customs and Border Protection (CBP) regulations, noting in this regard that in 19 CFR 134.1(k), “conspicuous” is defined as “capable of being easily seen with normal handling of the article or container.” By adopting the same conspicuous standard as CBP, TTB would “help manufacturers and importers better understand their obligations under the statute and promote compliance and enforcement,” and prevent confusion and unintentional noncompliance, which would result from agencies adopting different definitions and policies for the same term. Further, TTB should adopt a policy that articles need not be marked in the most conspicuous place but must be marked in any conspicuous place. Finally, the commenter suggested that TTB adopt provisions from the CBP regulations at 19 CFR 134.41 regarding the methods and manner of marking.

National Tobacco suggested that, due to the inherently ambiguous nature of the “conspicuousness” standard in § 40.25a(b)(3)(i), TTB should set up a process allowing tobacco companies to get prompt, advance TTB approval of new packaging designs. Under this approval process, packaging designs submitted to TTB for review would be deemed approved if TTB did not specify any objections within a 15-day time period. Alternatively, TTB should further define “conspicuousness” by specifying a minimum font size for the term “pipe

tobacco” relative to the font size of the product brand name each time the brand name appears on the packaging.

National Tobacco also suggested that TTB clarify § 40.25a(b)(3)(ii), under which processed tobacco removed from a factory in a package is deemed to be roll-your-own tobacco if the package or accompanying materials bear any representation that would suggest a use other than as pipe tobacco. National Tobacco asks that TTB state that the term “accompanying materials” used in that section includes any point of sale advertising and all other printed product communications issued by the manufacturer of pipe tobacco products.

TTB response: TTB does not believe that it is appropriate to define the word “conspicuousness” in this final rule because any attempt to do so without first going through a period of public notice and comment could prove to be unnecessarily limiting. The current regulatory text in § 40.25a(b)(3)(i) allows for sufficient flexibility depending on the design and size of the package, and TTB believes this is the preferable approach at this time. In this regard, TTB notes that, after the enactment of CHIPRA, Congress passed and the President signed the Family Smoking Prevention and Tobacco Control Act (Pub. L. 111–31) affecting the graphics and warning statements required to appear on certain tobacco products. These additional issues now faced by the tobacco industry regarding packaging and labeling requirements underscore our belief that a flexible approach, particularly with regard to size and placement of certain information on a tobacco product package, is necessary for the near future. Rather than establishing a new process of review and prior approval by TTB of

each tobacco product package, TTB will consider whether clarifying the conspicuousness standard in future guidance is needed.

With regard to the request that TTB amend § 40.25a to specify what may be “accompanying materials,” we agree with the comment. The final regulations at § 40.25a(b)(3)(ii) and § 41.30(b)(3)(ii) provide that “accompanying materials” includes, but is not limited to, any point of sale advertising or other printed product communications issued by the manufacturer or importer of pipe tobacco products. In addition, the inclusion of cigarette papers or tubes in a package bearing a “pipe tobacco” declaration will suggest a use other than pipe tobacco.

Comment

We received a comment from Geoffrey Ranck of Domestic Tobacco Co., recommending that TTB add a line to the monthly report required of importers of tobacco products or processed tobacco (TTB F 5220.6) to account for cigar tobaccos (filler, binder, and cigar wraps) separately from roll-your-own tobacco. Mr. Ranck noted that, although CHIPRA amended the definition of roll-your-own tobacco so that cigar tobacco must now be included in the accounting of roll-your-own tobacco, cigar tobacco is still considered to be distinct from traditional roll-your-own cigarette tobacco by the U.S. Department of Agriculture (USDA) in its implementation of the Fair and Equitable Tobacco Reform Act (commonly referred to as the “Tobacco Buyout”) and by the various states in their implementation of the Master Settlement Agreement.

TTB response: Although the categories on TTB F 5220.6 correspond directly to the types of tobacco products recognized under the IRC definitions

(small cigarettes, large cigarettes, small cigars, large cigars, snuff, chewing tobacco, pipe tobacco, and roll-your-own tobacco), we recognize that other Federal agencies have different definitions of these tobacco products. Mr. Ranck's suggestion has merit and, when updating TTB F 5220.6, TTB will explore the extent to which such a change would meet the needs of industry members and be consistent with and facilitate reporting required by other Federal agencies or the Master Settlement Agreement.

Comment

Two commenters addressed the designations that must appear on tobacco product packages, under § 40.216b and 41.72b, to identify those products for tax purposes. National Tobacco noted that the temporary regulations removed "Tax Class L" and "Tax Class J" as approved designations for packages of pipe tobacco and roll-your-own tobacco, respectively, and suggested that TTB also eliminate all "Tax Class" designations for the other tobacco products in favor of accurate descriptive terms. This would remove "Class A" and "Class B" as alternatives for the term "small cigarette" and "large cigarette," "Tax Class C" as an alternative for the term "chewing tobacco" and "Tax Class M" as an alternative designation for "snuff". National Tobacco and the Law Offices of Barry Boren requested that TTB also authorize the use of a number of designations for roll-your-own tobacco in addition to those prescribed in § 40.216b and 41.72b. The Law Offices of Barry Boren stated that the labeling requirements proposed for cigar wrappers are unduly restrictive; that cigar wrappers have been known throughout the industry and the general public under

names such as “cigar wrappers,” “cigar wraps,” “blunts,” “leaf wraps” and “flat wraps;” and that any of these names should be acceptable for marking purposes. National Tobacco proposed adding “tobacco cones” and “cigar tubes” as designations, stating that the use of the term “roll-your-own tobacco” to designate such products may cause confusion between products used for making cigars and products used for making cigarettes, particularly because roll-your-own tobacco used for making cigarettes is subject to State excise taxes and the payment obligations of the Master Settlement Agreement.

TTB Response: First, TTB notes that the designations required on tobacco product packages are intended to identify the product for purposes of Federal excise tax. The designation indicates the tax category under which the taxpayer removed the product domestically or obtained release of an imported product. The regulations have traditionally allowed industry members a choice between using a descriptive term and using a “Tax Class” reference. For example, under the previous version of § 40.216a, a package of pipe tobacco had to bear either the designation “pipe tobacco” or the designation “Tax Class L.” Although we agree that descriptive terms for all tobacco products may be preferable in some regards, the removal of the options to use “Tax Class L” to designate pipe tobacco and “Tax Class J” to designate roll-your-own tobacco was specific to those products and to the ways those products are defined by statute. The designations “Tax Class L” and “Tax Class J” were removed as authorized designations because the IRC definitions, as discussed above, require consideration of the packaging and labeling of pipe tobacco and roll-your-

own tobacco—specifically as to whether packaging, labeling, appearance, or type of the tobacco, cause the product to be “suitable for use and likely to be offered to, or purchased by, consumers” as either of those products. The statutory definitions of the other products do not require a similar consideration of the packaging and labeling. Accordingly, because TTB does not have a compelling reason to adopt the requested change within the scope of administration and enforcement of the Federal excise tax, and because the alternative notices are currently in use by industry members, it would not be appropriate to adopt the proposed changes in this final rule without notice to, and opportunity for comment by, industry members.

With regard to the designations authorized for roll-your-own tobacco, under the temporary regulations, the following terms may be used: “roll-your-own tobacco,” “cigarette tobacco,” “cigar tobacco,” “cigarette wrapper,” and “cigar wrapper.” TTB believes these alternative designations are sufficient for administering and enforcing the Federal excise tax provisions. The designations are used for tax purposes and are not intended to reflect the scope of terms used for marketing the product. TTB notes that the regulations do not prohibit additional terms from appearing on tobacco product packages that also bear one of the prescribed designations. Such additional information may appear so long as it does not contradict or conflict with the tax designation.

Comments to be Addressed in a Future Rulemaking

TTB received additional comments that relate to pipe tobacco and roll-your-own tobacco issues, particularly with regard to distinguishing between the

two products for tax purposes. Comments from the South Dakota Attorney General's Office, National Tobacco, the Law Offices of Barry Boren, Altadis USA, Inc., and the Campaign for Tobacco-Free Kids suggested that TTB clarify the characteristics that distinguish pipe tobacco from roll-your-own tobacco to prevent mislabeling of roll-your-own tobacco as pipe tobacco. Altadis USA, Inc. expressed concern about "massive tax cheating in the form of misclassification of RYO tobacco as pipe tobacco" and submitted a "Draft Revision of Temporary/Proposed Regulation on Classification of Pipe Tobacco and Roll-Your-Own Tobacco."

The Pipe Tobacco Council, National Tobacco, and Altadis USA, Inc. requested that TTB "grandfather" pipe tobacco brands that were on the market prior to the enactment of CHIPRA in 2009. Although various "grandfather" proposals have been suggested to TTB, they differ in details. In general, under those various proposals, brands that were marketed as pipe tobacco prior to a certain date, for example, April 1, 2009, would continue to be deemed pipe tobacco after that date so long as the product remained sufficiently similar to the product that was produced under that brand name before April 1, 2009. As a result, under the various proposals, any standards that TTB might find to distinguish between pipe tobacco and roll-your-own tobacco would not be applied to "grandfathered" brands.

The Pipe Tobacco Council also expressed concern about the importation of cut tobacco that was not put up into consumer packages, specifically that there would be a disparity in treatment between packaged and unpackaged imported

tobacco. The Pipe Tobacco Counsel recommended that cut tobacco imported under a certain subheading of the Harmonized Tariff Schedule of the United States (HTSUS) be categorized as roll-your-own tobacco, with excise tax due upon release from customs custody. That subheading (2403.10.30.90) applies, in general terms, to smoking tobacco that is to be used in products other than cigarettes and that is not prepared for marketing to the ultimate consumer in the form and package in which it's imported.

The issues involved in distinguishing between pipe tobacco and roll-your-own tobacco merit separate treatment. To obtain public input specifically on those issues, TTB published in the **Federal Register** on July 22, 2010 (75 FR 42659), an advance notice of proposed rulemaking, Notice No. 106, referred to earlier in this comment discussion. After the close of the Notice No. 106 comment period, TTB received a request to meet with an industry member and its legal representation to present TTB with a proposal to use certain physical characteristics to distinguish between pipe tobacco and roll-your-own tobacco that differ from the standards proposed by the other commenters. That new proposal, which was submitted as a slide presentation, is now posted with the comments on Notice No. 106 as Comment 23 and may be viewed at the Regulations.gov Web site (www.regulations.gov) within Docket No. TTB-2010-0004. Through publication in the **Federal Register** of Notice No. 120 on August 24, 2011 (76 FR 52913), TTB reopened the public comment period for Notice No. 106, until October 24, 2011, in order to provide an opportunity for public feedback

to the new proposal. TTB is currently reviewing the comments and determining the appropriate rulemaking action in response.

Other Changes to the Temporary Regulations

In addition to those changes noted in the above discussion of comments, this final rule document makes the following changes to the temporary regulations published in T.D. TTB-78 and T.D. TTB-81:

- In §§ 40.11 and 41.11, the definition of “package” is amended to provide for several exceptions to the statement that “[a] container of processed tobacco, the contents of which weigh 10 pounds or less (including any non-tobacco ingredients or constituents), that is removed within the meaning of this part, is deemed to be a package offered for sale or delivery to the ultimate consumer.” Those exceptions are provided to recognize that manufacturers and importers of processed tobacco may remove processed tobacco in small amounts for purposes related to the business of a manufacturer or importer of processed tobacco; the exceptions allow the removal of such small amounts without that removal being deemed a removal of a taxable product and thus triggering the tax. The exceptions are similar to those provided to manufacturers of tobacco products who remove tobacco products without payment of tax for specified purposes. The definition of “package” is also amended to add references to § 40.25a and 41.30, respectively, to direct the reader to the tax rates that apply to processed tobacco that is placed into a package and removed. Also, in §§ 40.11 and 41.11, TTB is amending the definition of “packaging” to clarify that, when used in the context of an action, the term “packaging” refers to

the activity of placing processed tobacco or a tobacco product in a package.

This differentiates the use of the verb form of “packaging” from that of the noun form, as both appear in the regulatory text.

- In §§ 40.25a(b)(2) and 41.30(b)(2), a sentence has been added that mirrors text in the definition of “package” in §§ 40.11 and 41.11 described in the first bullet above. Specifically §§ 40.25a(b)(2) and 41.30(b)(2) now state that a container of processed tobacco, the contents of which weigh 10 pounds or less (including any added non-tobacco ingredients or constituents), that is removed within the meaning of this part, is deemed to be a package offered for sale or delivery to the ultimate consumer. The same exceptions are provided in those regulatory sections to recognize that manufacturers and importers of processed tobacco may remove processed tobacco in small amounts for purposes related to the business of a manufacturer or importer of processed tobacco; the exceptions allow the removal of such processed tobacco without that removal being deemed a removal of a taxable product and triggering the tax. The added text in §§ 40.25a(b)(2) and 41.30(b)(2) is for ease of reference.

- In § 40.256, the reference to “§ 40.61(b)” is corrected, so that it reads “§ 40.61(c).”

- In § 40.521(a), TTB is removing the requirement to keep records showing the quantity of processed tobacco processed, because we believe this requirement could result in counting the same tobacco multiple times where the tobacco is subject to more than one processing activity.

- In § 40.521, paragraphs (b)(6) and (b)(7) are removed, thereby removing the requirement that manufacturers of processed tobacco obtain a declaration by the purchaser of the processed tobacco of the specific purposes for the purchase and a declaration by the purchaser of the name and address of the principal if the purchaser is acting as an agent. TTB has not to date obtained any useful information from such requirements. Corresponding changes are made to the recordkeeping requirements applicable to importers of processed tobacco at §§ 41.261(b)(6) and (b)(7).

- In § 40.531, which concerns approvals of alternate methods or procedures for manufacturers of processed tobacco, TTB is amending paragraph (a)(2) by adding a reference to affording equivalent security to the revenue, as an additional condition for TTB approval.

- A new § 41.203a is added to correct an oversight. Importers of tobacco products are subject, under 26 U.S.C. 5713(b), to the same permit suspension and revocation provisions as those in the regulations applicable to manufacturers of tobacco products and processed tobacco and to importers of processed tobacco, at 27 CFR 40.332, 40.528, and 41.273 respectively. However, no such provision mirroring this statutory text appears in the current regulations applicable to importers of tobacco products. The new section sets forth permit suspension and revocation provisions for importers of tobacco products that mirror the permit suspension and revocation provisions for importers of processed tobacco in § 41.273.

- In 27 CFR 41.232, TTB is adding language to clarify that, although the permit of an importer of tobacco products can be amended to allow for the importer to import processed tobacco under the same permit, that importer qualifies to do so only when TTB authorization of the amendment is received in response to the application.

- Finally, TTB has made several non-substantive editorial changes to improve the readability and the clarity of the regulatory texts that appear in this document.

Adoption of Final Rule

Based on the foregoing, TTB has determined that the temporary regulations published in T.D. TTB-78 and T.D. TTB-81 should be adopted as a final rule with the changes discussed above.

Regulatory Flexibility Act

We certify that these regulations will not have a significant economic impact on a substantial number of small entities. The regulatory obligations and relevant collections of information which are the subject of this rule derive directly from the Internal Revenue Code of 1986, as amended, and the regulations in this rule concerning these obligations and collections merely implement and provide necessary standards for complying with the statutory requirements. Likewise, any secondary or incidental effects, and any reporting, recordkeeping, or other compliance burdens flow directly from the statute. Accordingly, a regulatory flexibility analysis is not required.

Paperwork Reduction Act

TTB has provided estimates of the burden that the collection of information contained in these regulations imposes, and the estimated burden has been reviewed and approved by the Office of Management and Budget (OMB) in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507) and assigned control numbers 1513–0024, 1513–0032, 1513–0033, 1513–0035, 1513–0068, 1513–0070, 1513–0078, 1513–0106, 1513–0107, and 1513–0130. TTB notes that this final rule contains a number of amendments to the regulations that alleviate the recordkeeping and reporting required by the temporary rule that this document replaces. In several provisions, alternate procedures are provided that allow for monthly summary reporting rather than daily or per-shipment reporting, and in two provisions, the requirement to record certain information has been removed. In addition, this final rule allows manufacturers of processed tobacco to submit one permit application to cover all locations at which they conduct business, rather than one application for each location. This final rule does, however, add an additional requirement that manufacturers and importers of processed tobacco submit location information to TTB as part of the permit application. This information was not previously specifically required under the regulations but could have been required by TTB under its authority to require submission of any “additional information” required to determine whether an applicant is entitled to a permit. (Set forth at 27 CFR 40.497 and 41.237.). This final rule reinstates recordkeeping of certain

unprocessed tobacco and also extends certain inventory requirements to importers of processed tobacco.

Under the Paperwork Reduction Act of 1995, an agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a valid OMB control number. Comments concerning suggestions for reducing the burden of the collections of information in this document should be directed to Mary A. Wood, Alcohol and Tobacco Tax and Trade Bureau, using any of these points of contact:

- P.O. Box 14412, Washington, DC 20044-4412
- 202-453-2686 (facsimile); or
- formcomments@ttb.gov (e-mail).

Effective Date

This document finalizes temporary regulations that were effective on June 22, 2009, which implemented changes made to the Internal Revenue Code of 1986 by the Children's Health Insurance Program Reauthorization Act of 2009. Because industry members have been operating for almost three years under the temporary regulations finalized in this document, and because many of the final regulations set forth in this document lessen reporting and recordkeeping burdens for industry members, TTB finds good cause under 5 U.S.C. 553(d)(3) to dispense with the effective date limitation in 5 U.S.C. 553(d). This final rule will be effective on June 21, 2012.

Executive Order 12866

It has been determined that this rule is not a significant regulatory action as defined in E.O. 12866. Therefore, it requires no regulatory assessment.

Drafting Information

This document was drafted by several members of the Regulations and Rulings Division, Alcohol and Tobacco Tax and Trade Bureau, with assistance from personnel in other divisions within TTB.

List of Subjects

27 CFR Part 40

Cigars and cigarettes, Claims, Electronic funds transfers, Excise taxes, Imports, Labeling, Packaging and containers, Processed tobacco, Reporting and recordkeeping requirements, Surety bonds, Tobacco products.

27 CFR Part 41

Cigars and cigarettes, Claims, Customs duties and inspection, Electronic funds transfers, Excise taxes, Imports, Labeling, Packaging and containers, Puerto Rico, Reporting and recordkeeping requirements, Surety bonds, Tobacco, Virgin Islands, Warehouses.

The Regulatory Amendment

For the reasons discussed in the preamble, the temporary regulations published in the **Federal Register** at 74 FR 29401 on June 22, 2009, as T.D. TTB-78, the temporary regulations published in the **Federal Register** at 74 FR 37551 on July 29, 2009, as T.D. TTB-80, and the temporary regulations published in the **Federal Register** at 74 FR 48650 on September 24, 2009, as T.D. TTB-81, are adopted as final, with the changes as discussed above and set forth below:

PART 40—MANUFACTURE OF TOBACCO PRODUCTS, CIGARETTE PAPERS AND TUBES, AND PROCESSED TOBACCO

1. The authority citation for part 40 continues to read as follows:

Authority: 26 U.S.C. 448, 5701-5705, 5711-5713, 5721-5723, 5731-5734, 5741, 5751, 5753, 5761-5763, 6061, 6065, 6109, 6151, 6301, 6302, 6311, 6313, 6402, 6404, 6423, 6676, 6806, 7011, 7212, 7325, 7342, 7502, 7503, 7606, 7805, 31 U.S.C. 9301, 9303, 9304, 9306.

§ 40.11 [Amended]

2. In § 40.11:

- a. The definition of “package” is amended by adding, after the word “part,” the words “for any purpose other than destruction, export, delivery as a sample to a manufacturer of processed tobacco or tobacco products for the purpose of soliciting orders of processed tobacco, or scientific testing or testing of equipment which results in the destruction of the processed tobacco or the return of the

processed tobacco to the factory premises,” and by adding, at the end, the sentence, “For appropriate tax rate, see § 40.25a.”;

b. The definition of “packaging” is amended by removing the word “The” and adding, in its place, the words, “When used in the context of an action, the”; and

c. The definition of “sale price” is amended by adding, after the words “sold by the”, the words “U.S.”.

§ 40.25a [Amended]

3. In § 40.25a:

a. Paragraph (b)(2) is amended by adding a sentence at the end to read as follows: “A container of processed tobacco, the contents of which weigh 10 pounds or less (including any added non-tobacco ingredients or constituents), that is removed within the meaning of this part for any purpose other than destruction, export, delivery as a sample to a manufacturer of processed tobacco or tobacco products for the purpose of soliciting orders of processed tobacco, or scientific testing or testing of equipment which results in the destruction of the processed tobacco or the return of the processed tobacco to the factory premises, is deemed to be a package offered for sale or delivery to the ultimate consumer.”

b. Paragraph (b)(3)(ii) is amended by adding two sentences at the end to read as follows: “The term ‘accompanying materials’ includes, but is not limited to, any point of sale advertising or other printed product communications issued by the manufacturer or importer of pipe tobacco products. In addition, the

inclusion of cigarette papers or tubes in a package bearing a 'pipe tobacco' declaration will suggest a use other than pipe tobacco.”

4. In § 40.47, paragraph (b) is revised to read as follows:

§ 40.47 Other businesses within factory.

* * * * *

(b) Processed tobacco. A manufacturer of tobacco products may engage in certain activities related to processed tobacco without an approval under paragraph (a) of this section. Section 40.72(b) specifies the activities and circumstances that do not require authorization to engage in another business as well as those activities and circumstances that do.

5. In § 40.72, paragraph (b) is revised to read as follows:

§ 40.72 Use of factory premises.

* * * * *

(b) Processed tobacco. (1) A manufacturer of tobacco products that processes tobacco or receives processed tobacco on its factory premises solely for use in the manufacture of tobacco products under its permit, that removes processed tobacco from the factory premises only for purposes related to its business of manufacturing tobacco products as set forth in (b)(2) of this section, and that maintains records sufficient to show the final disposition of any processed tobacco removed from the factory premises may engage in such activities on the factory premises under the authority of its existing permit without prior authorization from TTB under § 40.47. If a manufacturer of tobacco products removes processed tobacco for purposes other than those specified in

paragraph (b)(2) of this section, that manufacturer must obtain prior authorization from TTB in accordance with § 40.47 and must keep records and submit reports as prescribed in §§ 40.521 and 40.522.

(2) The following activities are considered to be activities related to the manufacture of tobacco products: removal of samples of processed tobacco for the purpose of soliciting orders of tobacco products; removal of processed tobacco for destruction; removal of processed tobacco for scientific testing or testing of equipment which results in the destruction of the processed tobacco or the return of the processed tobacco to the factory premises; and transfer of processed tobacco between permitted premises of the same manufacturer. Any removal of processed tobacco other than those listed above requires the manufacturer to first obtain authorization to engage in another business within the factory under § 40.47 and to keep records and submit reports under §§ 40.521 and 40.522, unless the manufacturer can show to the satisfaction of the appropriate TTB officer that the removal is connected with the business of a manufacturer of tobacco products rather than with the business of a manufacturer of processed tobacco.

6. Section 40.182 is revised to read as follows:

§ 40.182 Record of tobacco and processed tobacco.

(a) Except as provided in paragraph (b) of this section, a manufacturer of tobacco products must maintain a record that shows the total quantity in pounds of all:

- (1) Processed tobacco on hand at the beginning of each month;
- (2) Processed tobacco received, together with the name and address of the person from whom received and the date of receipt;
- (3) Processed tobacco used in the manufacture of tobacco products, together with the date of use;
- (4) Processed tobacco lost, together with the date and other circumstances of the loss;
- (5) Processed tobacco destroyed, together with the date and other circumstances of the destruction;
- (6) Processed tobacco removed, together with the date of the removal and reason for the removal; and
- (7) Tobacco (unprocessed) on hand at the beginning of each month and used in the manufacture of tobacco products, lost, destroyed, or removed during each month.

(b) A manufacturer of tobacco products that is required to obtain authorization to engage in another business within the factory under §§ 40.47(b) and 40.72(b) must keep records as prescribed in § 40.521, in addition to those required elsewhere in this part.

(Approved by the Office of Management and Budget under control number 1513-0068)

7. In § 40.202, paragraph (b) and the parenthetical OMB approval are revised to read as follows:

§ 40.202 Reports.

* * * * *

(b) Report of processed tobacco. In addition to complying with the requirements set forth in this part relating to the reporting of tobacco products, a manufacturer of tobacco products that is required to obtain authorization to engage in another business within the factory under §§ 40.47(b) and 40.72(b) must also make and submit reports as prescribed in § 40.522.

(Approved by the Office of Management and Budget under control number 1513–0033)

§ 40.256 [Amended]

8. In § 40.256, the first sentence is amended by removing the reference “§ 40.61(b)” and adding, in its place, the reference “§ 40.61(c)”.

9. Section 40.491(b)(3) is revised to read as follows:

§ 40.491 Factory premises.

* * * * *

(b) * * *

(3) Any person that holds a TTB permit for the manufacture of tobacco products and that removes processed tobacco from the factory must apply for authorization to engage in that activity, when required to do so under § 40.47.

10. A new § 40.502 is added under the undesignated center heading “Qualification Requirements for Manufacturers of Processed Tobacco” to read as follows:

§ 40.502 Factory premises.

(a) General. The premises used by a manufacturer of processed tobacco to conduct such business must be described on its permit and such premises must include any physical location or building used for: manufacturing and storing processed tobacco; storing materials, equipment, and supplies related to or used in the manufacturing and storage of processed tobacco; and carrying on activities in connection with the manufacturing and storage of processed tobacco. The premises may consist of more than one building, or portions of buildings, which need not be contiguous or located in the same city, town, village, or State. The manufacturer must designate a central location as a repository for the records required under this subpart. The application for the permit filed under § 40.492 must describe the buildings or portions of buildings by street address (number, street, city or equivalent, and State). The permit application must include a diagram, in duplicate, showing the following information, if applicable:

(1) The identification of each building by a letter, number, or similar designation if the factory is in more than one building and each building is not identifiable by a separate street address; and

(2) The particular floor or floors, or room or rooms, comprising the factory if the factory consists of, or includes, a portion of a building or portions of buildings.

(b) Permits issued prior to June 21, 2012. A manufacturer of processed tobacco operating under a permit issued prior to June 21, 2012, must submit the information required under paragraph (a) of this section within 180 days after June 21, 2012.

(c) Extension or curtailment of factory. If a manufacturer of processed tobacco wishes to change the premises delineated by its permit to an extent that would be inconsistent with the description or diagram of the premises that was submitted with the manufacturer's last permit application, the manufacturer must submit an application on TTB Form 5200.16 for, and obtain, an amended permit before the change in the premises occurs. The application must describe the proposed change in the premises and must be accompanied by a new diagram if required under paragraph (a) of this section.

11. Section 40.521 is revised to read as follows:

§ 40.521 Record of tobacco and processed tobacco.

(a) Every manufacturer of processed tobacco and every manufacturer of tobacco products required to obtain authorization to engage in another business within the factory under §§ 40.47(b) and 40.72(b) of this part must keep records of operations and transactions that show the total quantity of all:

(1) Processed tobacco on hand at the beginning of each month;

(2) In the case of a manufacturer of tobacco products, processed tobacco used in the manufacture of tobacco products during each month;

(3) Processed tobacco received, together with the date of receipt and the name and address of the person from whom it was received;

(4) Processed tobacco removed from the factory for shipment to a person holding a TTB permit as a manufacturer of processed tobacco, as a manufacturer of tobacco products, as an importer of processed tobacco, or as an export warehouse proprietor, together with the date of removal and the name and address of the person to whom shipped or delivered;

(5) Processed tobacco removed from the factory for shipment, other than for export, to a person not holding a TTB permit as a manufacturer of processed tobacco, as a manufacturer of tobacco products, as an importer of processed tobacco, or as an export warehouse proprietor, together with the date of removal;

(6) Processed tobacco removed from the factory for export, together with the date of removal;

(7) Processed tobacco removed for any purpose not referred to in paragraphs (a)(4), (5), (6), and (7) of this section, together with the date of removal;

(8) Processed tobacco lost, together with the date and other circumstances of the loss;

(9) Processed tobacco destroyed (either on factory premise or removed from factory premises for destruction), together with the date and other circumstances of the destruction;

(10) Processed tobacco transferred between buildings that are covered under the same permit but that are not located in the same city, town, village, or State; and

(11) Tobacco (unprocessed) on hand at the beginning of each month and used in the manufacture of tobacco products, lost, destroyed, or removed during each month.

(b) Any manufacturer of processed tobacco and any manufacturer of tobacco products that are required to obtain authorization to engage in another business within the factory under §§ 40.47(b) and 40.72(b) and that engage in

removals of processed tobacco described in paragraph (a)(5) or (a)(6) of this section must also keep records that show the following information about each such removal:

(1) The full name and business address (including city and State) of the purchaser (if there is a purchaser) and the full name and business address of the recipient, or personal address if the purchaser or recipient is not a business;

(2) The full name, business address (including city and State), and driver's license number of the person picking up the processed tobacco for delivery;

(3) The license number of the vehicle in which the processed tobacco is removed from the manufacturer's premises;

(4) The street address of the destination (not including any in-transit stops) of the processed tobacco; and

(5) The quantity of processed tobacco in the shipment;

(c) The entries in the records of removals required under this section must be made for each day by the close of the business day following the day on which the removal occurs. There is no particular format prescribed for the records required under this section (and commercial records may be used) although the required information must be readily ascertainable from the records kept. In the case of a removal under paragraph (a)(5) or (a)(6) of this section that involves shipment by a common carrier, the appropriate TTB officer may approve an alternate method or procedure pursuant to §§ 40.45 or 40.531 through which the manufacturer may keep records regarding the common carrier

and its means of tracking (including pick up and delivery) of the shipment in lieu of the information required by paragraphs (b)(2) and (b)(3) of this section.

12. In § 40.522, paragraph (d) is revised to read as follows:

§ 40.522 Reports.

* * * * *

(d) Reports of removals. (1) Except as otherwise provided in paragraphs (d)(2) or (d)(3) of this section, a manufacturer who removes processed tobacco for export or for shipment to someone other than a person holding a TTB permit as a manufacturer of processed tobacco, as a manufacturer of tobacco products, as an importer of processed tobacco, or as an export warehouse proprietor must report each such removal on TTB F 5250.2 by the close of the next business day following the day of removal, in accordance with the instructions on the form.

(2) In the case of removals for export, as an alternative to the procedure prescribed in paragraph (d)(1) of this section, the manufacturer may submit to TTB a monthly summary report of such removals in a format approved by the appropriate TTB officer. Prior to the use of such an alternate procedure, the manufacturer must obtain written approval from the appropriate TTB officer.

(3) A manufacturer of tobacco products who removes processed tobacco for any of the purposes related to the manufacture of tobacco products set forth under § 40.72(b)(2) is not required to report such removals on TTB F 5250.2. Records of such removals must still be kept pursuant to § 40.521.

* * * * *

§ 40.531 [Amended]

13. In § 40.531, paragraph (a)(2) is amended by removing the word “, and” at the end and adding in its place, the words “and affords equivalent security to the revenue; and”.

PART 41—IMPORTATION OF TOBACCO PRODUCTS, CIGARETTE PAPERS AND TUBES, AND PROCESSED TOBACCO

14. The authority citation for part 41 continues to read as follows:

Authority: 26 U.S.C. 5701–5705, 5708, 5712, 5713, 5721–5723, 5741, 5754, 5761–5763, 6301, 6302, 6313, 6402, 6404, 7101, 7212, 7342, 7606, 7651, 7652, 7805; 31 U.S.C. 9301, 9303, 9304, 9306.

§ 41.11 [Amended]

15. In § 41.11, the definition of “package” is amended by adding, after the word “part” the words “for any purpose other than destruction, export, delivery as a sample to a manufacturer of processed tobacco or tobacco products for the purpose of soliciting orders of processed tobacco, or for scientific testing or testing of equipment that results in the destruction of the processed tobacco or the return of the processed tobacco,” and by adding, at the end, the sentence, “For appropriate tax rate, see § 41.30.”; and the definition of “packaging” is amended by removing the word “The” and adding, in its place, the words, “When used in the context of an action, the”.

§ 41.30 [Amended]

16. In § 41.30:

a. Paragraph (b)(2) is amended by adding a sentence at the end to read as follows: “A container of processed tobacco, the contents of which weigh 10 pounds or less (including any added non-tobacco ingredients or constituents),

that is removed within the meaning of this part for any purpose other than destruction, export, delivery as a sample to a manufacturer of processed tobacco or tobacco products for the purpose of soliciting orders of processed tobacco, or for scientific testing or testing of equipment that results in the destruction of the processed tobacco or the return of the processed tobacco, is deemed to be a package offered for sale or delivery to the ultimate consumer.”

b. Paragraph (b)(3)(ii) is amended by adding two sentences at the end to read as follows: “The term ‘accompanying materials’ includes, but is not limited to, any point of sale advertising or other printed product communications issued by the manufacturer or importer of pipe tobacco products. In addition, the inclusion of cigarette papers or tubes in a package bearing a ‘pipe tobacco’ declaration will suggest a use other than pipe tobacco.”

17. New § 41.203a, is added immediately before the undesignated center heading “Required Records and Reports” to read as follows:

§ 41.203a Suspension and revocation of permit.

When the appropriate TTB officer has reason to believe that an importer of tobacco products has not in good faith complied with the provisions of 26 U.S.C. chapter 52, and regulations thereunder, or with any other provision of 26 U.S.C. with intent to defraud, or has violated any condition of the permit, or has failed to disclose any material information required or made any material false statement in the application for the permit, or is, by reason of previous or current legal proceedings involving a felony violation of any other provision of Federal criminal law relating to tobacco products, processed tobacco, cigarette paper, or cigarette

tubes, not likely to maintain operations in compliance with 26 U.S.C. chapter 52, or has been convicted of a felony violation of any provision of Federal or State criminal law relating to tobacco products, processed tobacco, cigarette paper, or cigarette tubes, the appropriate TTB officer shall issue an order, stating the facts charged, citing such person to show cause why the permit should not be suspended or revoked. Such citation shall be issued and opportunity for hearing afforded in accordance with part 71 of this chapter, which part is applicable to such proceedings. If, after hearing, the Administrative Law Judge, or on appeal, the Administrator, finds that such person has not shown cause why the permit should not be suspended or revoked, such permit shall be suspended for such period as the appropriate TTB officer deems proper or shall be revoked.

18. In § 41.232, paragraph (b) is amended by adding, before the period, the words, “and receiving TTB authorization”.

19. Section 41.237 is amended by designating the existing text as paragraph (a), adding a heading to newly designated paragraph (a), and adding a new paragraph (b). The additions read as follows:

§ 41.237 Additional information.

(a) General. * * *

(b) Business premises. Every person that files an application for a permit required by § 41.231 as an importer of processed tobacco must furnish, with its application for the permit, the address to be used as the principal business office where the records and reports required by the subpart must be maintained pursuant to § 41.263. The applicant must also include the location (by physical

address or other means if there is no physical address) of any premises used for the storage of processed tobacco imported or received. For permits issued prior to June 21, 2012, the permittee has 180 days from June 21, 2012, to submit the information required under this paragraph.

20. In § 41.253, a sentence is added at the end to read as follows:

§ 41.253 Change in location or address.

* * * Whenever the importer wishes to change the location of the premises used for the storage of processed tobacco imported or received by the importer to an extent that would be inconsistent with the location information submitted with the importer's last permit application, the importer must apply for, and obtain, an amended permit before such a change in premises takes place.

21. In § 41.261:

a. Paragraph (a)(2) is amended by adding at the end before the semicolon the words “, together with the name and address of the person from whom it was received”;

b. Paragraph (a)(3) is amended by adding at the end before the semicolon the words “or exported”;

c. Paragraph (a)(5) is amended by removing the word “Transferred” and adding, in its place, the words “Except in the case of returns to customs custody or exportations, transferred”;

d. Paragraph (a)(6) is amended by removing the period at the end and adding in its place the word “; and”;

e. New paragraph (a)(7) is added;

f. Paragraph (b)(1) is amended by removing the words “address (including city and State) of the purchaser (or recipient, if there is no purchaser)” and adding, in their place, the words “business address (including city and State) of the purchaser (if there is a purchaser) or the full name and business address of the recipient (if there is no purchaser), or personal address if the purchaser or recipient is not a business”;

g. Paragraph (b)(2) is amended by adding before the word “address” the word “business”;

h. Paragraph (b)(5) is amended by removing the semicolon and adding in its place a period;

i. Paragraphs (b)(6), (b)(7), and (d) are removed; and

j. Paragraph (c) is revised.

The revision and addition read as follows:

§ 41.261 Records.

(a) * * *

(7) Transferred between buildings that are covered under the same permit but that are not located in the same city, town, village, or State.

* * * * *

(c) The entries in the records required under this section must be made for each day by the close of the business day following the day on which the transfer or sale occurs. There is no particular format prescribed for the records required under this section (and commercial records may be used), although the required information must be readily ascertainable from the records kept. In the

case of a removal under paragraph (a)(5) of this section that involves shipment by a common carrier, the appropriate TTB officer may approve an alternate method or procedure pursuant to § 41.26 of this part through which the importer may keep records regarding the common carrier and its means of tracking (including pick up and delivery) of the shipment in lieu of the information required by paragraphs (b)(2) and (b)(3) of this section. No records are required to be kept under this part regarding processed tobacco within customs custody, although this will not preclude TTB review of records related to such processed tobacco as may be appropriate for purposes of the enforcement of the provisions of this part.

* * * * *

22. In § 41.262, paragraph (a) is amended by adding at the end of the paragraph the sentence, "The importer need not include in the reports under this part information regarding processed tobacco that is in customs custody."; and paragraph (d) is revised to read as follows:

§ 41.262 Reports.

* * * * *

(d) Reports of sales and transfers. (1) Except as otherwise provided in paragraph (d)(2) of this section, an importer that exports processed tobacco or transfers or sells processed tobacco to someone other than a person holding a permit as an importer or manufacturer of processed tobacco or tobacco products or as an export warehouse proprietor must report each such exportation, sale, or transfer on TTB F 5250.2 by the close of the next business day following the day of exportation, sale, or transfer, in accordance with the instructions on the form.

(2) In the case of removals for export, as an alternative to the procedure prescribed in paragraph (d)(1) of this section, the importer may submit to TTB monthly summary reports of such removals in a format approved by the appropriate TTB officer. Prior to the use of such an alternate procedure, the importer must obtain written approval from the appropriate TTB officer.

(3) An importer that ships or transfers processed tobacco for scientific testing or testing of equipment which results in the destruction of the processed tobacco or the return of the processed tobacco is not required to report such shipment or transfer on TTB F 5250.2.

* * * * *

23. New § 41.264 is added immediately after § 41.263, to read as follows:

§ 41.264 Inventories.

Every importer of processed tobacco must provide a true and accurate inventory of any processed tobacco stored on premises designated pursuant to § 41.237. The importer must make such an inventory at the time of commencing business, at the time of transferring ownership, at the time of changing the location of facilities in which processed tobacco is stored, at the time of concluding business, and at such other time as the appropriate TTB officer may require. A specific format is not prescribed. For permits issued prior to June 21, 2012, the permittee has 180 days from June 21, 2012, to make an inventory as required under this paragraph.

Signed: April 12, 2012.

John J. Manfreda,

Administrator.

Approved: June 12, 2012.

Timothy E. Skud,

Deputy Assistant Secretary
(Tax, Trade, and Tariff Policy).