

## B. Overall Direct Price Effect

The majority of forecasts presented to the Committee indicated that the changeover to the GST is expected to exert a minimal one-time increase in the level of consumer prices. Estimates of the direct price effect vary, from 1.25% (Department of Finance, Informatrica Ltd., Economic Council of Canada, Governor of the Bank of Canada) to 3% (Canadian Union of Public Employees, Canadian Labour Congress). The Department's estimate assumes that there will be full passthrough and that firms know with certainty the amount of FST in their products. Those who produced higher estimates assumed uncertainty about the amount of FST buried in products, about the percentage of tax savings likely to be handed on by businesses, about compliance costs, and the possible attempts of firms to take advantage of consumer confusion.

As Table 2 indicates, most predictions of the overall direct price effect presented to the Committee are near the lower limit. This is important for two reasons. First, it indicates confidence that adequate competitive pressures, particularly evident in a period of soft market conditions like the present, can contribute to responsible pricing decisions. The minor adjustment in price levels expected also suggests that both business and labour need not be overly concerned that wages will have to be adjusted significantly. It should be stressed that the perception of inflationary pressures caused by the implementation of the GST is a critical variable in determining the actual inflationary effect of the tax.

The precise impact of the tax change on consumer prices is virtually impossible to determine. The accuracy of the outcome depends critically on the assumptions used. For instance, while the government has assumed a 100% passthrough of the FST savings, other groups, such as the Canadian Home Builders' Association (66.7% passthrough) and the Canadian Union of Public Employees (30%), have presented alternative scenarios. Ultimately, the marketplace will decide, as it normally does, the pricing decisions that will be taken by industry participants.

Compliance costs must also be addressed in any discussion of price effects. Uncertainty exists about vendors' potential compliance costs, and the extent to which business will be able to pass these additional costs on to consumers. Many firms are currently in the process of planning their adjustment strategies for the implementation of the GST; until they have finalized their compliance response procedures, precise costs will be unavailable. On the question of transferring compliance costs there is some evidence that the current weak state of the economy will force some retailers to absorb a significant proportion of these costs. The full extent of this effect, however, remains unclear.