

Certain services are expected to come down in price. Both Bell Canada and Unitel Communications Inc. stated that the cost of telecommunications services would decline as the 11% Telecommunications Services Tax is replaced by the 7% GST. The cost of a long distance telephone conversation, for instance, would fall with the shift in tax regime.

While the government and the homebuilding industry, represented primarily by the Canadian Home Builders' Association, both suggested that the price of new housing would be negatively affected, there was a considerable difference of opinion about the extent. The Association suggested that the price of the average new home (\$150,000) would rise by 2%, whereas the government suggested it would be by less than 1%. Such a variation in the expected impact can be attributed to differences in estimates of effective tax rates on housing inputs and in assumptions regarding the passthrough of FST savings.

Rental housing, according to the government, should be relatively unaffected by the tax change, given the tax exemption of short-duration and long-term residential rents and the fact that new construction adds less than 2% annually to the total rental housing stock. While the GST will be charged against operating costs, it is argued that this effect will be offset to some extent by the provision of GST tax credits to families with low and moderate incomes.

The effect of the GST on home renovation will be largely a function of the labour-intensiveness of the activity in question. Since labour was previously not taxed, renovation involving proportionately few building materials may be adversely affected. The Canadian Home Builders' Association expressed some concern lest additional renovation costs would cause individual renovators to evade taxes imposed chiefly on labour.

Finally, gasoline, alcohol and tobacco should not be affected by tax reform as the government intends to alter the tax structure to maintain the present revenue.

D. Potential Impact On Inflation and On Ensuing Monetary Policy

1. Concerns about Inflation

It is important to distinguish between (a) a one-time effect on the price level brought about by the introduction of the GST and (b) an inflationary effect, which can be broadly characterized as a continuing increase in the broad level of prices. This is a key point, since it is the perception of inflationary pressures that is so important. If labour and business (who set prices) mistake the one-shot effect for an increase in inflation, serious inflation-causing forces could actually set in and undermine the positive benefits of the GST.