

LIVING WITH THE GST

INTRODUCTION AND APPROACH

A. Overview of the Operation of the Goods and Services Tax

The existing Federal Sales Tax (FST) applies to goods manufactured in Canada and to finished manufactured goods imported into Canada. A number of goods, however, such as clothing, food, footwear and pharmaceuticals are exempt from the tax. All services except for telecommunications services are also exempt.

The FST is generally levied at the manufacturers' level of the production and distribution chain, although, for some products, it is levied at the wholesale level. The following are the applicable FST rates: 13.5% for most goods, 19% for alcohol and tobacco products, and 9% for construction materials. An 11% tax is also applied to telecommunications services at the user level.

The FST has been widely criticized. The most commonly voiced concerns relate to the very narrow base of products and services to which it is applied, its uneven application, the fact that it can favour imported products over Canadian-made goods and its unreliability as a source of revenue for the government. It is generally accepted that the FST is beyond repair and must be abolished.

The Goods and Services Tax (GST), the tax that the federal government has proposed as a replacement for the FST, is a tax on final consumption. It would apply at a rate of 7% on almost all goods and services consumed in Canada. Unlike the FST or a provincial sales tax, the GST is a value added tax, and would thus apply at each stage of the production and distribution chain.

Businesses will charge GST on the price of their taxable goods and services. Businesses that purchase goods and services and pay the GST will be able to claim an input tax credit for the tax paid. Because the amount of the GST remitted to the government by a business will be the amount of the GST collected from customers minus the GST paid on its purchases, the tax applies to the value added to a product or service. Final consumers, however, will pay the full amount of the GST on the selling price of a product.

The GST will apply to a broad range of goods and services. There are some goods and services, however, on which the tax will not be assessed. These are classified as either exempt or zero-rated. The difference between these categories lies in whether or not a