

*For additional commentary on the topic of tax-inclusive pricing, please see the Canadian Tax Foundation Web site ([www.ctf.ca](http://www.ctf.ca)) for an advance viewing of articles by Richard M. Bird and W. Jack Millar to be published in vol. 58, no. 1 of the Canadian Tax Journal.*

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## Policy Forum: Tax-Included Pricing for HST—Are We There Yet?

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### ABSTRACT

Under Canada's goods and services tax (GST), harmonized sales tax (HST), and provincial retail sales tax (RST), most goods and services are advertised at prices on which taxes are "extra." Taxes are added at the cash register on every purchase, and consumer dislike of (and political opposition to) the GST and HST is due primarily to this high visibility. In all other value-added tax (VAT) countries, prices are shown tax-included. Canada currently does not have mandatory GST- or RST-included pricing for constitutional reasons: legislation dealing with pricing is generally within provincial jurisdiction, and provincial RSTs must be direct taxes, which are understood to require tax-extra pricing. With the pending implementation of the HST in Ontario and British Columbia in July 2010, the conditions will be in place for Canada and most provinces to enact legislation mandating tax-included prices. The author contends that this would be good for the Canadian economy, explores associated technical issues, and discusses whether Canada could impose a flat 13 percent HST across the country for the sake of uniformity in pricing, despite the objections of the provinces.

**KEYWORDS:** GST ■ GOODS AND SERVICES TAX ■ HARMONIZED SALES TAXES ■ PRICING ■ POLITICAL POLICY ■ ADVERTISING

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### CONTENTS

Introduction	840
Background on the GST and HST	840
Are Prices Shown Tax-Extra or Tax-Included?	842
Is Tax-Included Pricing Better Than Tax-Extra Pricing?	843
GST Should Be Visible . . . but Not Too Visible	843
The Political Lesson of 1993	844
Tax-Included Pricing Is Better for the Economy	844
If Tax-Included Pricing Is Better, Why Are Prices Shown Tax-Extra?	846
Constitutional Stalemate No. 1: Provincial Jurisdiction over Pricing	846

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Constitutional Stalemate No. 2: Provincial RST Must Be “Direct”	847
Freedom of Speech in the Charter	848
Summary	849
ETA Sections 364-368: The Unproclaimed Tax-Included Pricing Legislation	849
We Are Over the 50 Percent Threshold—Now What?	852
Technical Issues with Tax-Included Pricing	852
Remaining Inconsistencies If Canada Moves to Tax-Included Pricing	853
Manitoba, Saskatchewan, and Prince Edward Island	853
Alberta	854
British Columbia	854
Quebec	854
Summary	855
A Radical Idea: Could the Federal Government Go It Alone?	855
Conclusion	856

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*Canada’s system of conspicuously adding GST and PST onto everything you buy is like having Brian Mulroney stick his thumbs in his ears and wiggle his fingers every time you buy a chocolate bar.*

Kelly McParland, *Financial Post*, March 2, 1993

*Only in Canada, you say? Pity.*

Television advertisement for Red Rose tea

## INTRODUCTION

Canada’s goods and services tax (and harmonized sales tax) system is essentially the same sales tax system as the value-added tax (VAT) or GST system in more than 140 countries—virtually every country other than the United States. Yet the GST/HST is generally despised by the public, even though the tax rate is far lower in Canada than it is in most other jurisdictions.

The GST’s political unpopularity can be attributed almost entirely to its high visibility. Almost all goods and services are priced “tax-extra” rather than “tax-included.” The consumer who sees a product priced at \$99.00 on a store shelf finds that he or she must pay \$111.87 to take the product home.<sup>1</sup>

In this article, I explain why prices are generally shown as tax-extra, what needs to be done to move to tax-included pricing, and why mandatory tax-included pricing would be beneficial for Canada.

## BACKGROUND ON THE GST AND HST

The GST was introduced in 1991 as a 7 percent VAT, replacing the federal sales tax (FST). The FST was a manufacturers’ sales tax, which applied at 13.5 percent at the

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1 This example assumes a 13 percent HST, which is the rate in effect in Nova Scotia, New Brunswick, and Newfoundland and Labrador, and which will be the rate in Ontario effective July 2010.

wholesale level to a limited number of goods and which was almost entirely invisible to consumers.<sup>2</sup>

The GST applies to most supplies of property and services in Canada, and is imposed on the purchaser.<sup>3</sup> The key feature that makes it a VAT is that most businesses can claim refunds, by way of input tax credit, for most or all of the GST that they pay on purchases.

At the time that the GST was introduced, all provinces except Alberta levied a provincial retail sales tax (RST) at rates that varied from 6.5 percent to 12 percent. Even before the GST was introduced, the federal government sought to have the provinces join the GST system. In April 1997, the HST was introduced in Nova Scotia, New Brunswick, and Newfoundland as a 15 percent tax, combining the federal 7 percent GST with a provincial 8 percent component. Those three provinces repealed their RSTs.

In July 2006, the federal government lowered the GST rate from 7 percent to 6 percent. In January 2008, it lowered the rate further to 5 percent. In the HST provinces, the combined rate thus fell to 14 percent and then to 13 percent (the provincial component remained at 8 percent).

The HST is administered by the Canada Revenue Agency (CRA) as part of the GST, with no separate administration and no separate accounting by businesses. Place-of-supply rules<sup>4</sup> determine whether a particular supply of property or services should bear GST or HST, but all tax collected by a business is remitted on one return with no breakdown. The federal government uses statistical economic data to determine how much of the tax it collects is passed on to the provinces as their share of HST revenues.

The federal government tried for years to persuade other provinces to harmonize their RSTs with the GST. Owing to the political unpopularity of the GST—which, I maintain, was caused solely by prices not being shown as tax-included—this did not happen for a long time. Finally, in March 2009, in the midst of a severe downturn in the economy, Ontario announced that it would join the HST system effective July 2010, with an 8 percent provincial rate.<sup>5</sup> In July 2009, British Columbia announced that it too would join the HST system effective July 2010, but with a 7 percent provincial rate (and thus a 12 percent HST).<sup>6</sup>

Quebec introduced the Quebec sales tax (QST) in July 1992. The QST is similar to the GST and applies generally to the same goods and services, with some exceptions. It is administered by Revenu Québec together with the GST. The tax is not fully harmonized; businesses must file separate GST and QST returns and remit the

2 A consumer would normally see the FST only on the purchase of printing services.

3 Excise Tax Act, RSC 1985, c. E-15, subsection 165(1) (herein referred to as “ETA”).

4 ETA schedule IX.

5 Ontario, Ministry of Finance, 2009 Budget, March 26, 2009, chapter III.

6 British Columbia, Ministry of Finance, “Harmonized Sales Tax To Boost Investment, Job Creation,” News Release no. 2009PREM0017-000141, July 23, 2009.

correct amount of tax on each return. Canadian businesses outside Quebec that are not QST-registered cannot claim input tax credits for the QST that they pay on purchases.

This leaves only three provinces—Manitoba, Saskatchewan and Prince Edward Island—with an RST system as of July 2010. Pressure is building on those provinces to join the HST system. At the same time, a significant amount of public pressure against harmonization is being exerted by consumer groups and others who see harmonization as a tax grab that extends the tax base of the provincial sales tax. At time of writing (November 2009), it was still not absolutely certain that Ontario's and British Columbia's harmonization plans would go forward, and it was still unknown whether the remaining three RST provinces would harmonize.

### **ARE PRICES SHOWN TAX-EXTRA OR TAX-INCLUDED?**

With a few exceptions, Canada is a tax-extra country. Store shelves, window displays, billboards, television ads, Web sites, and catalogues show prices before GST, HST, QST, or RST is added. The notable exceptions are the following:

- Gasoline pump prices, which change daily and are normally posted on large electronic signs at gas stations. If regular unleaded gasoline is advertised at 95.6 cents per litre, then that is what the customer pays. The price includes GST as well as a myriad of other taxes, both federal and provincial. The GST included in the price is shown on the receipt printed at the pump.
- Taxi fares, both metered and flat-rate, are shown inclusive of all taxes.
- Vending machines, pay telephones, parking meters, and other coin- or card-operated machines all display prices tax-included.
- New homes are advertised at prices that include the “net” GST. The price includes tax, but the tax is net of the new housing rebate available to the consumer who buys the home for use as his or her primary place of residence.<sup>7</sup> Suppose, for example, that a new condominium unit costs \$100,000 plus 5 percent GST (\$5,000). A rebate of 36 percent of the GST, or \$1,800, is available to a purchaser who intends to live in the home, and can be credited by the builder on the purchase, thus reducing the “net” GST to \$3,200. The builder will advertise the home for sale at \$103,200. The statement of adjustments provided by the builder's lawyer on closing will disclose both the GST and the rebate.<sup>8</sup>

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7 ETA section 254.

8 The agreement of purchase and sale will state that the purchaser will pay the builder an amount equivalent to the rebate. This makes the total consideration including GST, and including the transferred rebate, equal to \$105,000, sufficient to generate the \$1,800 rebate. See Canada Revenue Agency, *GST/HST Memorandum* 19.3.1.2, “Stated Price Net of Rebate—GST at 5%,” December 2007, and *Trengrove Developments Inc. v. Canada*, [1996] GSTC 35 (TCC); aff'd. [1998] GSTC 49 (FCA); leave to appeal to SCC refused [1999] GSTC 3.

- Movie and theatre tickets, and most other admissions to places of amusement such as museums, zoos, and amusement parks are shown as tax-included, evidently as a result of consumer demand. This practice has possibly been influenced by the large number of tourists who visit such attractions and who might express severe displeasure at having to pay a price higher than posted.

## IS TAX-INCLUDED PRICING BETTER THAN TAX-EXTRA PRICING?

### GST Should Be Visible . . . but Not Too Visible

The pre-1991 FST was replaced with the GST principally because the FST was economically inefficient; it applied to a relatively narrow base of goods and distorted the economy. At the same time, the Department of Finance, in designing the GST, wanted the tax to be visible. The August 1989 technical paper, which first described the GST in detail, stated the following:

#### *Fairness*

After sales tax reform, Canada's tax system will be fairer than it is today. This will be accomplished in three ways. . . .

Third, consumers will, for the first time, be informed in a clear and visible manner that they are paying federal sales tax. One of the great flaws of the existing FST is that consumers do not, for the most part, know they are paying it. Because the GST will extend to the retail level and will apply, with few exceptions, to a very broad base at the uniform rate of 9 percent, consumers will know when they are paying federal tax. . . .

#### *The GST and the Consumer*

From the point of view of the consumer, the existing federal sales tax has some important failings. The vast majority of Canadians are not even aware that they are paying it, and those who are aware cannot calculate the actual amount of tax that is paid on any given purchase. This disservice to consumers stems from the structure of the tax itself. . . .

The GST will be a visible tax. The essence of visibility involves the application of tax at the retail level on a very broad base with a uniform rate. This ensures that Canadians will know when and at what rate they are paying federal sales tax.<sup>9</sup>

Despite these good intentions, the GST became *too* visible. In theory, members of the public may want to know about the taxes they are paying; in practice, however, they do not want to be reminded of it by paying a higher-than-advertised price every time they make a purchase. Indeed, a 1994 poll reportedly showed that 74 percent of the public supported the GST being included in prices.<sup>10</sup>

9 Canada, Department of Finance, *Goods and Services Tax: Technical Paper* (Ottawa: Department of Finance, August 8, 1989). At the time, the GST was proposed to be a 9 percent tax. It was later reduced to 7 percent before it came into force.

10 Geoffrey Hale, *The Politics of Taxation in Canada* (Peterborough, ON: Broadview Press, 2002), cited in Paul Boothe, "The Art of Tax Reform" (2002) vol. 50, no. 6 *Canadian Tax Journal* 2038-44, footnote 10.

### The Political Lesson of 1993

When the GST was introduced in 1991, the CRA hoped that vendors would advertise GST-included prices in most instances. This did not happen, except in the limited cases listed above. A few stores started including the GST in prices,<sup>11</sup> but this practice changed quickly as merchants realized that their prices would appear lower and more competitive if they excluded the GST. It was much easier to let the government take the blame for the tax than to appear to be raising prices.

In all provinces except Alberta, consumers were used to an RST that applied on top of a posted price. The GST, when added to the RST, created sticker shock. Suddenly, actual selling prices were 13 to 20 percent higher than those posted or advertised.<sup>12</sup> A television in Ontario, for example, might be advertised at \$599, but the purchaser would pay \$688.85 to take it out of the store.<sup>13</sup>

The GST was introduced in 1991 by a Conservative government that held 169 out of 295 seats in Canada's House of Commons. In the next federal election, in 1993, the Conservatives were reduced to 2 seats and were almost destroyed as a political party. Public hatred of the GST was a significant reason for the defeat. The lesson was clear: introducing a highly visible GST amounted to political suicide. Government officials acknowledged that having the GST added to every purchase had been a mistake.<sup>14</sup>

### Tax-Included Pricing Is Better for the Economy

In my view, tax-included pricing is better for Canada's economy for several reasons:

1. Tax-extra pricing acts as a drain on the economy by impeding consumer purchases. Anecdotal evidence abounds of instances where the effect of sticker shock causes consumers (especially visitors from outside Canada and the United States) to leave products at the cash register rather than pay the additional tax.
2. Consumers do not like to pay tax. Marketing campaigns that say, "We pay the GST" or "No GST" are far more successful than those that advertise a 5 percent or 7 percent reduction in prices. The GST, especially when combined with an RST, creates grumbling and discontent that feed political opposition to a tax that experts and economists almost universally agree is a "good" tax.

Gas pump prices are an excellent illustration of the problem. As noted above, pump prices are advertised tax-inclusive. If the price is \$1.00 per litre,

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11 The most notable example that I recall is the Zellers chain.

12 The highest RST rate was in Newfoundland, where the nominal rate was 12 percent. Since Newfoundland chose to apply its RST to GST-included prices, the real tax rate became 12.84 percent, which when added to the 7 percent GST created a total tax of 19.84 percent.

13 Ontario had an 8 percent RST in addition to the 7 percent GST.

14 Christopher Page, *The Roles of Public Opinion Research in Canadian Government* (Toronto: University of Toronto Press, 2006), 117-20.

some 30 to 40 cents per litre represents taxes and royalties. Yet one hears almost no daily complaints about the taxes on gasoline (although complaints about the prices themselves abound, and public ire is directed at the oil companies). Because the advertised price is the price that one pays, even though the GST is shown on the invoice and even though information about taxes appears on a sticker on the pump, there is no general public sentiment against the GST included in gas pump prices.

3. I contend that tax-included pricing, if introduced, will provide a psychological boost to spending. This boost will be fuelled by small-business owners who are GST-registered. Small businesses make up a significant portion of the economy, and small-business owners buy many of their supplies and capital goods at the retail level.

Consider the small-business owner who is contemplating the purchase of a new computer for her business. The computer she wants is advertised at \$1,100, including 13 percent HST. Although she must lay out \$1,100 to buy the computer, she is also aware that the purchase will generate an input tax credit of \$126.55 ( $\frac{13}{113}$  of \$1,100). This \$126.55 looks like a windfall—a discount or rebate for buying the computer for business purposes. Psychologically, it encourages the small-business owner to make the purchase.<sup>15</sup>

A GST or a VAT is in place in every OECD country other than the United States, and in virtually every country in the world that has a market economy (more than 140 countries). In all or virtually all of those countries, prices are advertised tax-included.<sup>16</sup> Cash register receipts show the VAT being paid, but the price advertised is the price that one pays. There is a reason for this practice: it is sensible, and it is what consumers want.

Richard Krever of Monash University, an expert on Australia's GST, has noted that

[t]he Canadian/US system has always seemed peculiar to the rest of the world. I have never met anyone from outside North America who has not complained that the worst part of a trip to North America is discovering that the price isn't the price. What's peculiar to me is the selective application of indirect taxes, including some in the price and not others or including it for some products and not others. I go to the service

15 I am not aware of any studies demonstrating the accuracy of this assertion. It is true, however, that relatively small amounts of tax, and tax savings, often drive consumer demand. For example, the home renovation tax credit (Income Tax Act, RSC 1985, c. 1 (5th Supp.), as amended, proposed subsection 118.04(3) (added by Bill C-51, section 4(1), second reading October 7, 2009)) has provided a significant boost to the Canadian construction industry since it was introduced in January 2009. The prospect of a 15 percent credit for expenditures in excess of \$1,000 and up to \$10,000 (to a maximum \$1,350 credit) often encourages homeowners to spend very large sums on renovations.

16 It appears that this is true for all countries except Canada and the United States: e-mails to the author from Fabiola Annacondia, editor, *International VAT Monitor* (International Bureau of Fiscal Documentation), October 6, 2009, and from Richard Krever of Monash University, September 16, 2009.

station and buy gas which has the excise tax and other taxes in the price and oil which has some taxes in the price and not others. Very weird.<sup>17</sup>

In some countries, consumer protection legislation requires that prices be shown tax-included as part of honesty in advertising. In Australia, for example, sections 52 and 53 of the Trade Practices Act 1974 prohibit misleading and deceptive conduct. The Australian Competition and Consumer Commission interprets these provisions as requiring prices to be shown inclusive of GST, and advises that it will prosecute merchants who do not adhere to this requirement.<sup>18</sup> In the interest of protecting consumers, Canadian legislation requiring that air travel prices be advertised inclusive of all taxes and fees has been enacted but has not been proclaimed in force,<sup>19</sup> apparently because of the Canadian government's inability to force foreign suppliers to adhere to such rules.

Admittedly, it is politically easier for governments to increase the rate of a sales tax that is included in prices. Although a rate increase is announced publicly, its effects are less obvious to consumers on a day-to-day basis. Whether this is good or bad depends on one's perspective on the impact of (sometimes irrational) consumer decision making on government and politics.

## **IF TAX-INCLUDED PRICING IS BETTER, WHY ARE PRICES SHOWN TAX-EXTRA?**

GST, HST, and RST have generally been shown as extra for arcane constitutional reasons that few people understand.

### **Constitutional Stalemate No. 1: Provincial Jurisdiction over Pricing**

Merchants appear more competitive if they show prices before taxes. If store A advertises a television for \$599, store B does not want to advertise the same television for \$676 and appear to be charging a higher price. As a result, merchants will advertise tax-included prices only if they are forced to do so, either by legislation or by prevailing custom and consumer insistence.

Under section 92(13) of the Constitution Act, 1867,<sup>20</sup> the provincial governments have jurisdiction to legislate in the field of "Property and Civil Rights in the Province." This jurisdiction includes the power to enact legislation governing the advertising and posting of prices. The federal government has jurisdiction over limited areas of

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17 E-mail to the author, September 16, 2009.

18 See, for example, Australian Competition and Consumer Commission, "Commercial Television Networks To Implement GST Inclusive Pricing," News Release no. MR 231/01, September 19, 2001 ([www.accc.gov.au/content/index.phtml/itemId/87849/fromItemId/378012](http://www.accc.gov.au/content/index.phtml/itemId/87849/fromItemId/378012)).

19 See proposed section 86.1 of the Canada Transportation Act, SC 1996, c. 10, as added by SC 2007, c. 19 (to come into force on a day to be fixed by order of the governor in council).

20 30 & 31 Vict., c. 3 (UK).

commerce, such as banking, telecommunications, and railways. As a result, Parliament likely cannot enact valid legislation requiring prices to be advertised tax-included (except in areas of federal jurisdiction). Such legislation would probably be found *ultra vires* the federal government because it would infringe on provincial jurisdiction.

When the GST was introduced, the provinces generally distanced themselves from what turned out to be a politically disastrous move by the federal Conservatives. The provinces were thus in no mood to enact legislation forcing prices to be shown tax-included. Furthermore, they would not be able to legislate the inclusion of their own sales taxes in posted prices, for the reason explained below.

### **Constitutional Stalemate No. 2: Provincial RST Must Be “Direct”**

Under section 91(3) of the Constitution Act, 1867, the federal government has the power to pass laws for “[t]he raising of Money by any Mode or System of Taxation.” Under section 92(2), the provincial governments have the power to pass laws for “Direct Taxation within the Province in order to the raising of a Revenue for Provincial Purposes.”

A direct tax is one that is demanded from the person who is intended to pay it. An indirect tax is one that is buried in the price of goods and is passed on, “clinging” to the goods.<sup>21</sup> Customs duties are a classic example of an indirect tax.

Provincial RSTs are direct taxes, but only because they are explicitly imposed on the purchaser, with the retailer designated as the province’s agent to collect the tax.<sup>22</sup> To ensure that that tax is explicitly imposed on the purchaser, each province with an RST has provisions in its RST legislation requiring almost all prices to be shown before RST.<sup>23</sup> Furthermore, RST is not imposed on goods, but is imposed on the purchaser’s “consumption or use” of those goods, which theoretically means that it is not passed on any further.

21 See John Stuart Mill, *Principles of Political Economy* (New York: Colonial Press, 1900), quoted in many Canadian cases, including *661881 BC Ltd. v. British Columbia (Attorney General)*, 2009 BCSC 1197. See also Peter Hogg, *Constitutional Law of Canada* (Toronto: Thomson Carswell) (looseleaf), paragraph 31.2. For a detailed discussion, see Simon Thang, “Constitutional Law Aspects of Commodity Tax,” *2009 Commodity Tax Symposium* (Toronto: Canadian Institute of Chartered Accountants, 2009), at pages 4-17. Note that the concept of “direct” and “indirect” described in this paper is the Canadian description; the international understanding of what constitutes a direct tax is rather different. The OECD and other economic institutions consider VAT or GST to be an indirect tax.

22 Hogg, *supra* note 21, at paragraph 31.7.

23 For example, Ontario’s Retail Sales Tax Act, RSO 1990, c. R.31, section 40(1), provides as follows:

No vendor shall advertise or post or otherwise quote a price that includes the tax imposed by this Act unless the vendor specifies separately the amount of the tax payable under this Act, and no vendor shall hold out or state to the public or to any purchaser, directly or indirectly, that the tax or any part thereof imposed by this Act will be assumed or absorbed by such vendor or that it will not be considered as an element in the price to the purchaser or, if added, that it or any part thereof will be refunded.

Limited exceptions are provided by ministerial regulation and in section 40(3).

When the GST was introduced, the constitutional status of the provinces' RSTs did not change. Since prices had to be shown exclusive of RST, merchants showed them exclusive of GST as well. Indeed, in provinces where RST is calculated as a percentage of the pre-GST price,<sup>24</sup> it would have been very awkward to calculate the RST on GST-included prices. (For example, in Ontario, where the RST is 8 percent, the RST on \$10 of goods priced GST-included at \$10.70 would have had to be calculated as 7.47663 percent of \$10.70 for a correct result.)

It is not entirely clear that the RST must be excluded from advertised prices for constitutional reasons. In its 1994 decision approving the constitutionality of the GST, the Supreme Court of Canada stated the following:

[T]hough the GST, for example, can be included in the price and appear only on the final invoice, consumers are fully aware, often to their dismay, that they are paying the tax. Indeed the federal government made it very clear in the background papers to the GST, that in replacing the hidden federal sales tax it was "committed to ensuring that Canadians [be] informed in a clear and visible manner that the GST is being applied." . . . As noted above, such transparency is one of the hallmarks of direct taxation.<sup>25</sup>

Peter Hogg suggests, however, that

[i]f a value-added tax or other form of retail sales tax were embedded in the retail price instead of being charged separately by the retailer, surely this would not convert a direct tax into an indirect one.<sup>26</sup>

Arguably, an RST that required prices to be advertised tax-included might be constitutionally valid if it met certain conditions, such as requiring that the tax be disclosed on receipts. However, this point is uncertain.

Because the HST is legislated by the federal government, it can be an indirect tax. Thus, the HST, including its provincial component, can unquestionably be required to be included in a selling price (although the mandating legislation would have to be provincial), while a provincial RST possibly cannot.

### Freedom of Speech in the Charter

Section 2(b) of the Canadian Charter of Rights and Freedoms<sup>27</sup> provides that "[e]veryone has the following fundamental freedoms: . . . (b) freedom of . . . expression." Merchants may argue that they have the freedom to express prices exclusive of GST or HST.

24 From 1991 to March 1997, Quebec and the four Atlantic provinces calculated their sales taxes on GST-included prices, while Ontario and the provinces west of it used pre-GST prices. Today, only Quebec and Prince Edward Island continue to calculate sales tax on GST-included prices.

25 *Reference re Quebec Sales Tax*, [1994] GSTC 44, at 44-7 to 44-8 (SCC).

26 Hogg, *supra* note 21, at page 31-7, footnote 36.

27 Constitution Act, 1982, being schedule B to the Canada Act 1982 (UK), 1982, c. 11.

This issue has not yet been tested in the courts. If tax-included pricing is adopted across Canada, legislation requiring it might be considered valid as consumer protection legislation, as is the case in Australia. Peter Hogg notes that “[i]n Canada, the balancing of the value of free expression against the value of consumer protection has to take place within s. 1 of the *Charter*.”<sup>28</sup> Thus, in *Irwin Toy Ltd. v. Quebec*,<sup>29</sup> the Supreme Court ruled that advertising is constitutionally protected by section 2(b) of the Charter, but a 3-2 majority of the court ruled that a Quebec restriction on commercial advertising aimed at children was a “reasonable limit” under section 1.

### Summary

Until now, the market has chosen to price goods tax-extra. Under the HST system, this practice can be changed by legislation mandating tax-inclusive pricing, provided that the provinces cooperate in enacting such legislation.

## ETA SECTIONS 364-368: THE UNPROCLAIMED TAX-INCLUDED PRICING LEGISLATION

Most people do not realize that the GST legislation already contains a requirement for tax-included pricing, although the provision has not been proclaimed in force. ETA sections 364 to 368 were enacted in 1997 by Bill C-70,<sup>30</sup> the same bill that introduced the HST.

When the federal government reached agreement with Nova Scotia, New Brunswick, and Newfoundland to implement the HST, those provinces also agreed to enact legislation requiring tax-included pricing. As noted earlier, this is generally a matter of provincial jurisdiction. At the same time, the Department of Finance introduced sections 364 to 368, which require tax-included pricing in certain areas that are under federal jurisdiction:

- supplies by banks;
- interprovincial transportation by air, rail, or bus;
- telecommunications; and
- national catalogues and nationwide advertising.

One can see why sections 364 to 368 apply only to these few areas. Only a province can legislate a requirement for tax-included pricing in other areas.<sup>31</sup>

The key provision requiring tax-included pricing is ETA subsection 365(1):

28 Hogg, supra note 21, at paragraph 43.7(a).

29 [1989] 1 SCR 927.

30 SC 1997, c. 10.

31 See Thang, supra note 21, at 74-75.

Every registrant (other than a prescribed registrant or a government supplier) who makes or offers to make a specified supply of property or a service to a consumer

(a) shall indicate in all price information in respect of the property or service the total of

(i) the consideration for the supply, and

(ii) all taxes imposed on the consumer under Part II and this Part in respect of the supply,

and, where in the price information there is any indication of the consideration without tax, in such a way that the indication of that total is at least as large and prominent as any indication of the consideration without tax; and

(b) where the manner or form of indicating such a total or the standards to be met in indicating such a total are prescribed for the purposes of this subsection, shall indicate that total in that prescribed manner and form and in compliance with those prescribed standards.

The term “specified supply” is defined in ETA section 364 to cover supplies in the areas that, as noted, are under federal jurisdiction:

“specified supply” means a supply (other than a prescribed supply) that is

(a) a supply of a service made by a bank;

(b) a supply of a passenger transportation service

(i) made by a person operating a railway to which Part III of the *Canada Transportation Act* applies,

(ii) made by a person who operates an air service (within the meaning assigned by section 55 of the *Canada Transportation Act*) to which Part II of that Act applies, or

(iii) made by a person who operates an extra-provincial bus undertaking (within the meaning assigned by subsection 2(1) of the *Motor Vehicle Transport Act*);

(c) a supply of a telecommunication service that is within the legislative authority of Parliament; or

(d) a supply of a prescribed property or service.

The retail industry (especially those companies that advertise nationally) strongly opposed ETA sections 364 to 368 and the parallel provincial legislation requiring that tax-included pricing be shown in all advertising in New Brunswick, Nova Scotia, and Newfoundland. The proposals would have required separate catalogues and separate advertising for a market constituting only about 15 percent of Canada’s population. Retailers made extensive submissions to the Department of Finance and to the House of Commons Finance Committee in late 1996 and early 1997 in an attempt to stop the provisions from being enacted. Those submissions fell on deaf ears.

The retail industry had more success with the Senate, however. On March 11, 1997, the Senate Standing Committee on Banking, Trade and Commerce refused to pass Bill C-70 without an amendment to postpone the tax-included pricing provisions.<sup>32</sup> Since the HST was to come into force on April 1, 1997, passage of the

32 David M. Sherman, *GST Times*, supplement to *Canada GST Service* (Toronto: Thomson Carswell) (looseleaf), release no. 88P, March 21, 1997, at 1.

legislation was an urgent priority for the government. An agreement was thus approved by both the Commons and the Senate: the sections were enacted, but were not proclaimed in force. Section 242(2) of Bill C-70, which provides the in-force rule for ETA sections 364 to 368, was amended to read as follows:

Subsection (1) [enacting ETA sections 364 to 368] comes into force on a day fixed by order of the Governor in Council, which day shall not be before the first day on which provinces together having at least 51% of the total population of all provinces that are participating provinces (within the meaning of subsection 123(1) of the Act) or that impose a general retail sales tax at a percentage rate on all goods (other than those specifically enumerated in the legislation that imposes the tax) or a general value added tax at a percentage rate on all goods and services (other than those specifically enumerated in the legislation that imposes the tax) have enacted laws requiring that suppliers include the tax under Part IX of the Act in indications of the prices of property or services supplied.

With this amendment, Bill C-70 was passed and received royal assent on March 20, 1997,<sup>33</sup> just 12 days before the HST came into effect.

The in-force rule is not well understood even by GST experts because the drafting is complex. A careful reading shows that the rule provides as follows:

1. Determine which provinces impose HST, a provincial RST, or a provincial VAT, as follows:
  - a. HST—Nova Scotia, New Brunswick, Newfoundland and Labrador, and (beginning in July 2010) Ontario and British Columbia;
  - b. RST—Saskatchewan, Manitoba, Prince Edward Island, and (until June 2010) Ontario and British Columbia;
  - c. provincial VAT—Quebec.

These categories encompass all provinces except Alberta and the territories.<sup>34</sup>
2. Determine the total population of the nine provinces that impose HST, RST, or a provincial VAT. Call this amount *Y*.
3. Determine which provinces have enacted legislation requiring tax-included pricing.
4. Determine the population of the provinces described in point 3. Call this amount *X*.
5. If *X* is 51 percent or more of *Y*, then ETA sections 364 to 368 may be proclaimed in force. Proclamation will still require an order in council by Cabinet.

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33 SC 1997, c. 10.

34 The term “province” is defined in section 35(1) of the Interpretation Act, RSC 1985, c. I-21, to include the Northwest Territories, Nunavut, and Yukon. However, the territories have no territorial sales tax.

In practice, as explained under the heading “Constitutional Stalemate No. 2,” above, the RST and provincial-VAT provinces may not be able to enact valid tax-included pricing legislation. As a result, point 3 above can be implemented only by the provinces that have joined the HST system. Therefore, until Ontario and British Columbia join the HST system, the conditions for proclamation cannot be satisfied.

## **WE ARE OVER THE 50 PERCENT THRESHOLD—NOW WHAT?**

When Ontario and British Columbia join the HST system in July 2010, more than 51 percent of the population of the nine provinces will be HST provinces that could enact tax-included pricing legislation. If the HST provinces agree to require tax-included pricing, ETA sections 364 to 368 can be proclaimed in force.

The memoranda of understanding that Canada reached with Ontario and British Columbia do not discuss tax-included pricing.<sup>35</sup> I understand that there has been little or no discussion of tax-included pricing in the discussions to date between the Department of Finance and those two provinces.

Tax-included pricing remains the elephant in the room. It can be put into effect, but all parties want to wait for the HST to come into widespread operation first. There will be enough challenges and confusion connected with the new system and with the special rules being introduced for Ontario and British Columbia,<sup>36</sup> without adding tax-included pricing to the mix.

## **TECHNICAL ISSUES WITH TAX-INCLUDED PRICING**

Under a tax-included HST system, cash register receipts and suppliers' invoices would still have to show the amount of HST being paid. This is already done on gas station receipts, and is not difficult to implement. The same mechanism is used in Europe and Australia. Indeed, as noted above, when the GST was first introduced the government anticipated (incorrectly) that many merchants would want to price their goods and services tax-included and show the GST only on receipts.

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35 Memorandum of Agreement Concerning a Canada-Ontario Comprehensive Integrated Tax Co-Ordination Agreement, March 10, 2009, and Memorandum of Agreement Concerning a Canada-British Columbia Comprehensive Integrated Tax Co-Ordination Agreement, July 23, 2009.

36 The significant new rules include the following: (1) the provincial portion of HST does not apply to a range of goods in addition to printed books; (2) input tax credits are temporarily denied for the provincial portion of the HST on certain purchases by large corporations and financial institutions; and (3) British Columbia will impose a different tax rate than the other HST provinces.

Unlike most VATs (including the European VAT and the Australian GST), Canada's GST/HST is explicitly imposed on the purchaser, and only on the purchaser.<sup>37</sup> The vendor or supplier acts as an agent of the federal government in collecting tax from the purchaser.<sup>38</sup> Tax-included pricing can change the balance between who pays the tax and who bears the tax in situations where the application of the tax is uncertain or where it depends on the circumstances of the sale.

For example, if an Ontario bakery sells \$1.00 muffins HST-included, it will need to price a single muffin at \$1.13 but six muffins at \$6.00, since muffins are zero-rated when six or more are sold together.<sup>39</sup> At present, most bakeries price the single muffin at \$1.00 and add tax at the cash register if a customer purchases fewer than six.

Printed books are not subject to the provincial portion of the HST in any HST province or to RST in any RST province. Thus, books that have an "in Canada" price printed on the cover by the publisher will be able to use a GST-included price that is the same across the country. There would be a transitional problem for books that were printed before the tax-included pricing legislation took effect.

## **REMAINING INCONSISTENCIES IF CANADA MOVES TO TAX-INCLUDED PRICING**

Unfortunately, even if Canada moves to tax-included pricing, there will still be inconsistencies between provinces, which will create advertising challenges for merchants. Goods normally bear HST based on the destination to which they are shipped.<sup>40</sup> Thus, a tax-included advertisement that appears on television, on a Web site, or in a catalogue for goods that might be shipped to any province will have to advertise different prices for different provinces. However, ETA section 366 proposes to permit interprovincial advertising to follow "prescribed standards" (as yet unannounced) and to permit national catalogues to state on the cover and on every second page that the prices shown do not include tax.

### **Manitoba, Saskatchewan, and Prince Edward Island**

Manitoba, Saskatchewan, and Prince Edward Island still have RSTs. They likely cannot enact tax-inclusive pricing legislation for their RSTs, although they could enact such legislation for an HST. As noted earlier, there is pressure on these provinces to harmonize, and (as of late 2009) there is still time for each of them to announce harmonization plans to take effect in July 2010.

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37 ETA subsections 165(1) and (2).

38 ETA subsection 221(1).

39 ETA schedule VI, part III, paragraph 1(m).

40 ETA schedule IX, part II, section 1.

Interestingly, in February 1991 Saskatchewan was the first province to announce a plan to harmonize its RST with the GST.<sup>41</sup> Following a change in government and in response to public opposition, the plan was abandoned.<sup>42</sup>

### Alberta

Alberta has the fiscal advantage of revenues from oil and gas royalties; it also has a long tradition of opposition to sales taxes. The province is unlikely to introduce a provincial sales tax or to join the HST system (although Jack Mintz has recently recommended that it do so in order to maintain its competitive advantage over other provinces).<sup>43</sup> Thus, only the 5 percent GST is likely to continue to apply in Alberta.

### British Columbia

British Columbia has announced harmonization, but at a 7 percent rate instead of 8 percent. This introduces an inconsistency that will affect tax-included pricing. An advertisement for an item that costs \$100 before tax will have to show a price of \$112 in British Columbia and \$113 in other HST provinces.

### Quebec

As discussed earlier, the QST is a provincial VAT that is only partially harmonized with the GST. It is not integrated with the HST system, and businesses that are not registered for QST cannot claim input tax credits for the QST they pay on purchases in Quebec. Although joining the HST system would make sense, Quebec is unlikely to give up its control of the administration of the GST and the QST, or of the provincial income tax, for which both individuals and Quebec corporations must file a separate return with Revenu Québec.

In 1994, the Supreme Court ruled that the QST is a valid exercise of provincial powers under the Constitution Act, 1867.<sup>44</sup> The court implied that tax-included QST pricing would be valid, since the tax would still be a direct tax by virtue of its being shown on receipts.<sup>45</sup> Quebec has not indicated whether it might move to tax-included pricing if the rest of Canada does so.

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41 Canada, Department of Finance, "Wilson Announces Sales Tax Reform Agreement with Saskatchewan," News Release no. 91-023 and accompanying Background, February 20, 1991 (available in *Canada GST Service*, supra note 32, vol. P—Historical, "Historical—Dept. of Finance Releases" tab, R687-R694).

42 Saskatchewan, "Legislation Introduced To Repeal PST," News Release no. 91-653, December 6, 1991 (available in *Canada GST Service*, *ibid.*, vol. P-3, "Provincial Taxation" tab, P233).

43 Jack M. Mintz, "Will Alberta Lose Its Tax Advantage?" (2009) vol. 1, no. 3 *SPP Communiqué* 1-7.

44 *Reference re Quebec Sales Tax*, supra note 25.

45 See the quote from paragraph 24 of the decision, *ibid.*, reproduced above under the heading "Constitutional Stalemate No. 2."

The QST rate, which is calculated on GST-included prices, is 7.5 percent (effectively, 7.875 percent), and will rise to 8.5 percent in 2011<sup>46</sup> (effectively, 8.925 percent). Thus, even if Quebec enacts tax-included pricing legislation, its tax-included prices will be different from those in other provinces.

### Summary

While tax-included pricing can be effective locally, the benefits that could result from consistent pricing across Canada would be negated by the different rates in effect in various provinces and by Alberta's refusal to introduce a sales tax.

### A RADICAL IDEA: COULD THE FEDERAL GOVERNMENT GO IT ALONE?

For the sake of consistency in pricing, the federal government could choose to enact the HST so that it applies at the same 13 percent rate across Canada and is administered by the CRA. Such a tax is clearly within Parliament's legal jurisdiction, even though politically it would infringe on taxing room that has traditionally been left to the provinces.

In enacting the HST, the federal government would offer unilaterally to pay over to the provinces an  $\frac{8}{13}$  share of the HST collected in each province. This is already being done for Nova Scotia, New Brunswick, and Newfoundland and Labrador, and will be done for Ontario effective July 2010. Other provinces could choose to accept their 8 percent tax share or not, but the HST rate would remain the same regardless. (Alberta, which does not want to enact a sales tax, could take the money and refund it to its residents through the income tax system, grants, or some other mechanism.)

Effectively, this change would force the remaining provinces to repeal their RSTs; if they did not, the tax burden on sales would exceed 20 percent.

A nationwide HST would offer significant advantages for businesses. Goods and services delivered anywhere in Canada would bear the same rate of tax. Sales tax paid in any province would be eligible for full input tax credits. For consumers who cross provincial borders to shop, sales taxes would no longer create a distortion in buying patterns.

This approach would no doubt trigger a temporary political firestorm. Albertans would not want to see their sales tax increase from 5 percent to 13 percent, and Quebecers would object to tax administration being effectively taken away from Revenu Québec.

Some commentators would say that such unilateral action by the federal government is not the Canadian way. However, steps unpopular with the provinces have

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46 Quebec, Ministry of Finance, 2009 Budget, March 19, 2009.

been taken in the past—for example, the 1980 National Energy Program. Nevertheless, the long-term advantages of a consistent HST across Canada may not be considered sufficient to justify upsetting the provinces by taking away their ability to decide sales tax policy.

## **CONCLUSION**

Canada is apparently the only VAT/GST country in which prices are advertised exclusive of tax. Despite some technical challenges and interprovincial inconsistencies, mandatory tax-included pricing would generally be good for Canada. It would also bring our GST system into sync with VAT and GST systems in the rest of the world.

I encourage the provinces and the federal government to work together to create simultaneous rules requiring GST/HST-included pricing throughout Canada. If Manitoba, Saskatchewan, and Prince Edward Island join the HST system, this process will be even easier.

The ultimate goal of sales tax reform in Canada is a single HST with one administration and one rate. Unfortunately, it is likely that this goal can be reached only if the federal government takes unilateral action to create such a tax and is willing to withstand the resulting political fallout.