

***The Rapid Rise in GST Payable  
on New Homes in Canada***

Completed for:

**RESCON**

By:

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## ***Background***

The Goods and Services Tax (“GST”) was introduced in 1991. It replaced the existing Federal Sales Tax (“FST”) which applied to manufactured goods. Under the Federal Sales Tax, only part of the cost of a new home would be subject to taxation (the building materials and other goods); the majority of the cost of new homes (labour, land costs, professional services, and the various fees paid to municipalities) would not have been subject to the FST.

Therefore, if the GST rate was applied to the full market value of new homes, the result would have been a sharp increase in taxes, which would reduce housing affordability.

At the time, the federal government decided that buyers of new homes would be entitled to a rebate of 36% of the GST paid. Thus, while the GST rate was 7%, after the rebate, the effective rate of GST would be 4.48%. The amount of this rebate was apparently based upon the federal government’s estimate of what would provide a tax-neutral outcome – if the rebate percentage was estimated correctly the result would be that the GST paid would not be higher than would be paid under the FST.

However, the federal government also imposed limits on the amount of rebate. The full 36% reduction was available for homes priced up to \$350,000. The rebate is phased out for houses priced between \$350,000 and \$450,000 (for homes priced at \$450,000 or above there is no rebate and the effective tax rate was equal to the full 7%). Therefore:

- Homes priced above \$350,000 have a higher effective tax rate than do homes priced at or below the \$350,000 threshold.
- For homes priced above \$350,000, taxes paid under the GST are increasingly higher than would have been paid under the FST.

These thresholds have not been adjusted since the GST was introduced in 1991, despite the fact that house prices have increased considerably. The consequence is that the average effective tax rate has increased for new homes, which has reduced housing affordability in Canada.

This research report assesses the implications of the lack of increase of the GST rebate thresholds. It has been completed by Will Dunning Inc. at the request of RESCON. RESCON is a builders’ organization dedicated to removing barriers to new construction and eliminating unnecessary costs. It coordinates a council of trade contractor associations to address issues of common concern.

## ***Summary of Findings***

As is shown below, the conclusion is that the effective amount of GST paid per new home increased by 95% from 1991 to 2007. This is 2.5 times more than the rate of growth for average weekly wages in Canada.

Even with the recent announcement of a reduction in the GST rate to 5%, the effective amount of GST that might be payable in the near future will be 67% higher than in 1991, which remains well in excess of wage growth over the same period (38.6%).

Another perspective compares the GST paid on new homes with the amounts paid for other goods and services:

- For “goods excluding food purchased from stores”, the amount of GST has increased by just 8% compared to 1991 (versus 95% for new homes). After the reduction in the GST to 5% is accounted for, the amount of GST paid will have fallen by 10% (versus a 67% rise for new homes).
- For “services excluding shelter”, the amount of GST has increased by 36% compared to 1991 (versus 95% for new homes). After the reduction in the GST to 5%, the amount of GST paid will have increased by just 13% (versus the 67% rise for new homes).

Because the thresholds for the GST new homes rebate remain frozen-in-time at 1991 levels, it can be expected that the effective GST rate on new homes will continue to rise in future.

### ***The Rebate Has Not Kept Up With Housing Costs***

When the GST and the rebate for new homes was introduced in 1991 the federal government made a commitment that it would “review these thresholds at least every two years and adjust them as necessary to ensure that they adequately reflect changes in economic conditions and housing markets”<sup>1</sup>.

However, that commitment has not been met – in the almost 17 years that have passed since the GST came into force, the thresholds have not been adjusted. During 1991 to the present, the average price of new single-detached and semi-detached homes in Canada increased by 96%, according to data from Canada Mortgage and Housing Corporation on prices for newly-completed housing<sup>2</sup>.

Detailed data from CMHC<sup>3</sup> has been used to analyze prices for newly completed homes in Canada. The data, which is summarized in Table 1 below, shows that in 1991, 91% of new single-detached and semi-detached homes were priced below the \$350,000 threshold, and therefore were entitled to the full rebate. Just 5% of homes were priced from \$350,000 to \$449,999 (and were entitled to partial rebates). Only 4% of homes were priced at \$450,000 or more and therefore were not entitled to any rebate.

In 2007, much has changed: just 52% of new homes are entitled to full rebates (down from the 1991 figure of 91%); 22% are eligible for partial rebates (versus the prior 5%); and 26% are not eligible for any rebate (far in excess of the prior figure of 4%).

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<sup>1</sup> As reported by The Canadian Home Builders’ Association in its various reports on this issue, this commitment was made in the Technical Paper on the GST released in 1989 (page 19).

<sup>2</sup> The average price for 1991 was \$202,430; for the first nine months of 2007, the average was \$396,721. These figures apply to urban areas with populations of 50,000 or greater. An alternative measure of house price change is from Statistics Canada’s New House Price Index. This shows an increase of 50.5% (comparing the average index for all of 1991 to the average for the first nine months of 2007). The NHPI is widely considered to under-estimate actual increases in house prices, because it does not capture increases that occur when new developments are brought to market (it captures only increases that occur within a development after marketing has started).

<sup>3</sup> Information on the data provided by CMHC is contained in the Appendix below.

<b>Table 1</b>		
<b>Distribution of Price Ranges for Newly Completed Single-Detached and Semi-Detached Homes, in Canada, 1991 versus 2007</b>		
<i>Price Range</i>	<i>1991</i>	<i>2007 (9 months)</i>
% Below \$350,000	91%	52%
From \$350,000 to \$450,000	5%	22%
% Above \$450,000	4%	26%
Total	100%	100%
Source: Will Dunning Inc. using data from Canada Mortgage and Housing Corporation		

### ***GST Paid on New Homes***

The data from CMHC has been used to estimate how much GST would be paid by these homes as of 1991 and 2007, including the gross amounts (before the rebates) and what is of more interest, the net amounts after the rebates. Table 2 (below) summarizes the estimates. For 2007, two estimates have been developed, reflecting the GST rate of 6% that was in effect for most of the year. The second scenario provides an indication of the amounts of GST that might be paid in the near future (at current house prices), due to the reduction in the GST rate (to 5%) that was announced on October 30. The methodology is summarized in the Appendix.

As the table shows, in this dataset the average price of newly-completed single-detached and semi-detached homes in Canada has increased by about 93% since 1991. The gross amount of GST paid has increased by a smaller amount (about 66%). This slower increase for the amount of gross taxes occurred because at mid-2006 the GST tax rate was decreased to 6% from the prior 7%. At the newly-announced GST rate of 5%, the amount of gross GST will have increased by 43%.

As is shown, the average rate of GST rebate has fallen from just over 2% in 1991 to just under 1% for the first nine months of 2007 (and even lower after the reduction in the GST rate to 5%).

The dollar amount of GST rebate has fallen. For the first nine months of 2007 compared to 1991, the amount has fallen by 6%, despite the 93% rise in house prices. Based on the new GST rate of 5%, the amount of rebate would have fallen by about 18%.

The consequence is that in the first nine months of 2007, the net amount of GST has increased by 95% since 1991, and now averages more than \$19,000 per home. This 95% rise in GST paid per home has occurred despite the fact that the GST rate has been reduced to 6%.

With the reduction in the GST rate to 5%, the gross amount of tax has been reduced compared to what it was at the 6% rate. However, the amount of the subsidy is also reduced. The consequence is that the net amount of GST that might be paid in the near future (at current house prices) is 67% higher than in 1991 (at an average of about \$16,500 per home).

	1991	2007 (6% GST Rate)	% Change Versus 1991	2007 (5% GST Rate)	% Change Versus 1991
Estimated Average Price in Dataset	\$198,831	\$384,525	93.4%	\$384,525	93.4%
GST Paid In \$s					
Gross	\$13,918	\$23,072	65.8%	\$19,845	42.6%
Rebate	\$4,038	\$3,785	-6.3%	\$3,324	-17.7%
Net	\$9,880	\$19,286	95.2%	\$16,521	67.2%
GST as % of Selling Price					
Gross	7.00%	6.00%	-1.00 (1)	5.00%	-2.00 (1)
Rebate	2.03%	0.98%	-1.05 (1)	0.84%	-1.19 (1)
Net	4.97%	5.02%	0.05 (1)	4.16%	-0.81 (1)

Source: Will Dunning Inc. using data from Canada Mortgage and Housing Corporation  
 Note: (1) change in percentage points

To put these increases in the net GST per home into context, during the same period:

- Consumer prices in Canada have increased by 34.4%.
- The average weekly wage in Canada has increased by 38.6%.
- Since 1991, the amount of net GST payable on a new home has increased 2.5 times more rapidly than the average weekly wage in Canada (based on the 6% rate that applied for most of 2007). Even after the reduction of the GST rate to 5%, the amount of GST payable on a new home has increased much more rapidly than wages – by 67% for the GST versus about 39% for wages.

	1991	2007 (9 months)	% Change
Effective GST Per New Home			
Based on 6% rate for 2007	\$9,880	\$19,286	95.2%
Based on 5% rate		\$16,521	67.2%
Consumer Price Index (1)	82.8	111.3	34.5%
Average Weekly Wage (2)	\$553	\$767	38.6%

Source: Will Dunning Inc. using data from Statistics Canada

Notes:  
 (1) from Consumer Price Index all-items for Canada (2002=100).  
 (2) from Statistics Canada Survey of Employment, Earnings, and Hours. Average weekly earnings, Canada; All employees; Including overtime; Industrial aggregate excluding unclassified; average wage for 2007 is based on first 8 months

### ***GST Paid on Other Goods and Services***

Another perspective looks at the amounts of GST that paid by consumers for other goods and services.

The first comparison is with the category of “goods excluding food purchased from stores”.

- From 1991 up to the first nine months of 2007, inflation within this category totalled 24.7%. Combining this inflation with the GST rates that applied for 1991 (7%) and 2007 (6%) it is calculated that the average amount of GST paid increased by just 8% (versus the 95% increase in GST paid on new homes).
- After the October 30, 2007 reduction of the GST rate to 5%, the amount of GST paid will have actually fallen by 10% for this category of “goods excluding food purchased from stores”. The GST paid on new homes will have increased by 67%.

A second broad comparison is with the category of “services excluding shelter services”.

- Inflation within this category totalled 56.8% during 1991 to the first nine months of 2007. Combining this inflation with the GST rates for 1991 and 2007, the average amount of GST paid increased by 36% (versus the 95% increase in GST for new homes).
- After the October 30, 2007 reduction of the GST rate, the amount of GST paid will have increased by just 13%. The GST paid on new homes will have increased by 67%.

### ***About Will Dunning Inc.***

Will Dunning Inc. is an economic research firm. Based in Toronto, the firm specializes in housing market analysis, including project-specific market feasibility studies and expert witness testimony. The firm is led by Will Dunning, who has been honing his housing market analysis skills since 1982. Following 16 years with the federal housing agency (Canada Mortgage and Housing Corporation), Will joined a real estate consulting firm in 1997, where he was second-in-command. In September 2000, he established his own firm. Will has completed several hundred consulting studies, including economic analysis and forecasting studies as well as feasibility studies for proposed residential developments. He is frequently quoted in the news media on the housing market and speaks to industry forums, associations, and other interest groups. His website [www.wdunning.com](http://www.wdunning.com) provides a variety of reports and presentations, including Housing Market Digest, a monthly review of the housing market in the Greater Toronto Area.

### ***Disclaimer***

This report has been compiled using data and sources that are believed to be reliable. RESCON, Will Dunning, and Will Dunning Inc. accept no responsibility for any data or conclusions contained herein. The opinions and conclusions in this report are those of the author and do not necessarily reflect those of RESCON.

### ***Appendix - Using CMHC House Price Data to Estimate GST Amounts***

CMHC provided a custom tabulation of data on the numbers of units completed, by price range, for 1991 and the first nine months of 2007. The price ranges start at “less than \$100,000” then increase in increments of \$10,000 until a price of \$700,000 is reached, leaving the top range as \$700,001 and over.

For each of these ranges, the amounts of GST paid were calculated:

- “Gross” GST equals 7% of the price in 1991 and 6% of the price in 2007 (with another set of estimates based on the 5% rate that was announced on October 30). The calculation assumes that within each price range, the average price is at the mid-point of the range; for prices of \$100,000 or less, the assumed price was \$80,000; for prices greater than \$700,000, the assumed price was \$950,000 (these latter two assumptions are based on other CMHC data).
- The GST rebate is based on 36% of the gross GST, and is phased out for prices between \$350,000 and \$450,000,
- “Net” GST is the gross amount minus the rebate.

The data provided by CMHC covers urban centres with populations of 50,000 and over. For 1991, the dataset includes 66,655 units, or 72% of the 93,066 single-detached and semi-detached units that were completed in all areas of Canada. For the first nine months of 2007, the dataset includes 64,582 units, or 70% of the 92,328 single-detached and semi-detached units that were completed in all areas of Canada.

Housing units that are not included in this dataset would, in all likelihood, have lower prices and would on average pay GST at a lower effective rate than has been calculated for the sample.

Within the dataset provided by CMHC for this research, data is recorded as of the date of completion. In other data published by CMHC, the data is as of the date of absorption. The consequence is that the data in this set may vary slightly from that published elsewhere by CMHC, in terms of numbers of units and average prices. The differences between the two datasets are not large enough to materially alter the conclusions.