INSTITUT C.D. HOWE INSTITUTE
Trusted Policy Intelligence | Conseils de politiques dignes de confiance

Intelligence MEMOS

February 27, 2026

From: Sahar Hamdam

To: Federal Policymakers and Tax Policy Analysts

Re: Targeted GST Reform is More Effective Than Broad Elimination on Essentials

Canadians are facing sustained increases in the cost of groceries, household goods, and hygiene products.

In response, the federal government has expanded and renamed GST Credit as a central pillar of its affordability strategy. This policy emerged despite numerous **calls** to remove the GST from all "essential" goods.

While attractive, exempting more goods from the GST and narrowing its base would be fundamentally flawed. Broad exemptions are neither fair nor effective and have numerous downsides.

For instance, eliminating GST on a broad scale would pose a significant risk to already-strained federal government finances. In 2024-25, the GST generated $52.5 billion, accounting for 10.3 percent of **total federal revenue**. With federal deficit of **$78 billion** projected for the 2025-26 fiscal year, no balanced budget in sight, and federal debt standing at 41.2 percent of GDP following an actual **$36.3 billion deficit** in 2024-25, this is not the time for broad based consumption tax relief. If anything, pressures on the federal bottom line are going to grow support for an **increase** in the GST rate.

The recently announced Canada Groceries and Essentials Benefit (the renamed and expanded GST Credit) alone will cost an estimated **$12.4 billion** over five years (2025-26 to 2030-31), including a one-time payment of $3.1 billion and ongoing annual costs of $1.7-1.9 billion. Combined with the First-Time Home Buyers' GST Rebate (**$3.9 billion** over five years), these measures represent more than $16 billion in foregone revenue and increased expenditures.

This substantial fiscal commitment underscores the need to protect the remaining tax base. Removing GST from food alone would increase the deficit by billions more annually.

Not only would broad-based GST removal be fiscally irresponsible, but it would also be inequitable. Universal exemptions **disproportionately benefit**, higher-income households which spend more on high-ticket item non-essentials. The highest earners would save nearly twice as much in GST as lower earners. This approach would reward consumption rather than genuine need.

Fiscal federalism also complicates GST exemptions. In provinces with the Harmonized Sales Tax (HST), federal and provincial tax bases are linked. Federal action without provincial agreements could result in significant provincial revenue losses and intergovernmental tensions. Provinces already face financial strain from infrastructure, housing, and healthcare demands, which are eroding their bottom lines.

Any federal action must therefore be closely coordinated with provinces to maintain stability and revenue.

Defining what constitutes an "essential" good also presents a significant policy challenge. Broad exemptions can lead to boundary disputes, lobbying, increased administrative complexity, and a reduced tax base.

The GST Credit is more effective than exemptions at targeting low- and modest-income Canadians without eroding the tax base or sparking debates over what counts as 'essential.' However, given the substantial fiscal commitment this expansion represents, maintaining a broad GST base becomes even more critical. Future rate adjustments may be necessary within five years due to federal fiscal challenges, requiring recalibration of the credit to maintain its effectiveness as a progressive offset.

Zero-rating under the GST must be reserved exclusively for goods that meet clear and consistent principles. A good must be essential, directly linked to basic needs or dignity, and impose a disproportionate burden on low-income households.

The risk is that this erodes over time. Canada already zero-rates basic groceries (fresh produce, milk, bread, meat) under **Schedule VI** of the Excise Tax Act and has extended zero-rating to menstrual products and prescription medications. However, recent expansions – including the temporary December 2024-February 2025 **GST holiday on prepared foods and the new First-Time Home Buyers' GST Rebate** (effectively zero-rating via rebate mechanism) – illustrate the risk of ad hoc, politically-driven expansion without consistent principles.

To prevent erosion of principled tax design, any additional zero-rating must meet rigorous necessity tests.

The government must address affordability challenges, but blanket removal of the GST is not the solution. The GST Credit better targets support to those most in need and upholds sound tax design principles. This is essential to maintain fiscal responsibility as pressures will grow on the federal government to increase revenues in future years, which may even require an increase in the GST rate.

Sahar Hamdam is a student at the Munk School of Global Affairs and Public Policy. This Memo was the winning entry in a contest.

*To send a comment or leave feedback, click **here**.*