

Property Taxation as an Effective Tool of Self Government

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Introduction

First Nations property taxes have the potential to provide an independent, flexible, and stable source of revenue for First Nations communities which can be used to build infrastructure and promote economic growth. Where First Nations property taxation systems are absent, provincial and local governments may tax third party interests on reserve, with no assurance the revenues will be used to provide services to First Nations communities living on reserve.¹ With First Nations in British Columbia raising approximately \$40 million in property taxes a year, First Nations currently not collecting property taxes may be missing out on a considerable revenue opportunity. Moreover, by enacting property taxation by-laws on reserve, First Nations gain taxation jurisdiction of reserves and access important tools for self-government.

Section 83 of the *Indian Act* and the *First Nations Fiscal and Statistical Management Act* (the “FSMA”) each provide First Nation band councils with the legislative authority to pass property taxation by-laws. In 2012, there were approximately 40 First Nations with property taxation by-laws enacted under section 83 of the *Indian Act*² and a further 95 First Nations participating in the FSMA.³ Each legislative scheme offers First Nations a choice between two separate processes for enacting, collecting, and managing property tax revenues. This paper outlines the procedure for enacting property taxation laws under the *Indian Act* and the FSMA and identify the benefits and drawbacks associated with each method.

First Nations’ Taxation under the *Indian Act*

Under section 83 of the *Indian Act*, bands have the power to levy property taxes to interests on reserve land, including rights to occupy, possess or use land on reserve. This includes designated lands, easements, and in some cases, expropriated lands.⁴ First Nations taxation by-laws may apply to all persons utilizing First Nations reserve lands including band members and band owned entities. However, the federal and provincial Crown and their agents, such as BC Hydro, are exempt from band taxation by way of intergovernmental immunity found under s. 125 of the

¹ *Sammartino v. A.G.B.C.* (1971), 22 D.L.R. (3d) 194 (B.C.C.A.)

² First Nations Gazette, 2012 Annual By-laws <<http://www.fng.ca/filelist.php?catid=66>>.

³ First Nations Tax Commission, “Eleven more First Nations added to the First Nations Fiscal and Statistical Management Act Schedule” (December 21, 2012), online: <http://www.fntc.ca/dmdocuments/12-19-2012_news_release.pdf>.

⁴ *Osoyoos Indian Band v. Oliver (Town)*, [2001] 3 S.C.R. 746, 2001 SCC 85.

Constitution Act, 1867.⁵ In spite of this immunity, most Crown agencies provide grants in lieu of taxes to First Nations (and municipal governments) who have enacted their own property tax regime.

Section 83 of the *Indian Act* provides a process for First Nations to enact, *inter alia*, taxation by-laws:

- 83.(1) Without prejudice to the powers conferred by section 81, the council of a band may, subject to the approval of the Minister, make by-laws for any or all of the following purposes, namely,
- (a) subject to subsections (2) and (3), taxation for local purposes of land, or interests in land, in the reserve, including rights to occupy, possess or use land in the reserve;...

It is the policy of the First Nations Tax Commission (“FNTC”) that a First Nation intending to enact a taxation by-law provide advance notice to the provincial government. In British Columbia, First Nations are required to provide notice to the Minister of Aboriginal Relations and Reconciliation pursuant to the *Indian Self Government Enabling Act*, which sets out certain requirements for notice. If the notice complies with section 9, the Minister will then issue a certificate under section 10 of the *Indian Self Government Enabling Act* to the First Nation.

The First Nation is then required to submit a draft taxation by-law to the FNTC. In addition, the FNTC will require copies of the First Nation’s notice of intent to assume taxing jurisdiction, a copy of the certificate from the Ministry of Aboriginal Relations and Reconciliation, a list of proposed ratepayers, copies of correspondence to ratepayers, notices of meetings with ratepayers, and letters to MPs and MLAs. Consultation with ratepayers and local elected officials is not required under either the *Indian Act* or the *Indian Self Government Enabling Act*.

Once the FNTC is satisfied with the draft taxation by-law and that any practical or political issues raised by the First Nation taking on taxation jurisdiction have been addressed, they will make a recommendation to the Minister for by-law approval. Once the Minister has approved the by-law, it becomes a First Nation law. Once approved, the by-law comes into force and it is published in the *First Nations Gazette*.

⁵ *Westbank First Nation v. British Columbia Hydro and Power Authority* [1999] 3 S.C.R. 134

It is important to note that this process ousts the jurisdiction of the province, regional districts or municipalities to tax third parties occupying the First Nation's reserves. However, if the First Nation wishes to start taxing these third parties, it must annually pass a tax rates by-law (which is also reviewed by the FNTC and approved by the Minister). Thus, the enactment of the taxation by-law does not require the First Nation to tax.

In addition to property taxation, section 83 also allows council to pass by-laws addressing expenditures of band moneys, taxation and business licencing. Any of these money by-laws must also be approved by the Minister.

At minimum, a taxation by-law enacted under the *Indian Act* must provide for annual tax rates, property classes, property assessments, an appeal procedure, and the expenditure of property tax revenues.⁶ Aside from these basic requirements, the content of section 83 taxation by-laws can be quite flexible.

The FNTC has developed sample section 83 by-laws, which are available on its website. These sample by-laws can be used by First Nations to reduce the legal costs associated with drafting and reviewing property taxation by-laws. The templates also attempt to create consistency between provincial and First Nations tax rates and property assessment schemes.

Benefits and Drawbacks to Section 83 By-Laws

Enacting property taxation by-laws under the *Indian Act* is a fairly straightforward process. Once enacted, First Nations have administrative flexibility when implementing and managing their property taxation regimes and are not subject to the same ongoing scrutiny and administrative burdens as those First Nations participating in the FSMA. While the process of enacting and administering *Indian Act* by-laws can be relatively straightforward, the process is tempered by the mandatory ministerial approvals. The layers of bureaucracy continue after the by-laws are enacted as subsequent reviews by FNTC and approvals by the Minister are necessary for all amendments—no matter how insignificant the changes as well as annual rates and expenditure by-laws.

⁶ Section 83(3).

The overriding disadvantage of property taxation under the *Indian Act* is the inability of First Nations to pledge revenues to access financing. First Nations must be self-funded or rely on financial institutions to provide financing—which typically offer short term loans with higher rates of interest. This creates difficulties for First Nations wishing to improve infrastructure or invest in economic development opportunities.

First Nations' Taxation under the *First Nations Financial and Statistical Management Act*

Like the *Indian Act*, the FSMA provides First Nations the authority to collect property taxes for interests on reserve lands. Unlike the *Indian Act*, the FSMA provides an overarching framework of financial administration and management laws and policies.

The FSMA's main function is to permit First Nations to access financial markets through equity financing. This voluntary scheme allows First Nations to fund infrastructure improvements by pledging tax and other local revenues as security for financing. In this manner, the FSMA allows First Nations governments to operate in much the same way as municipalities and local governments.

In order to participate in the FSMA, First Nations must request to be added to the schedule of the act by submitting a band council resolution (“BCR”) to the Minister. In order to access funding, however, a First Nation must obtain borrowing member status from the First Nations Finance Authority (“FNFA”). This requires a First Nation to come into compliance with a variety of legal and financial administration standards set by the First Nations Financial Management Board (“FMB”). Broadly speaking, this includes development of a property taxation law, a financial administration law (“FAL”) and obtaining financial management and performance certifications from FMB. These steps are detailed below.

Financial Administration Law and Standards (“FAL”)

Creation and approval of a FAL is the first step toward becoming a borrowing member and must be established before the FMB will issue either a Financial Management Certificate or a Financial Performance Certificate. A FAL is a comprehensive set of rules that govern financial decision making, management, monitoring and reporting of a First Nation government. Together, the FAL standards require a First Nation to comply with wide-ranging governance practices

concerning financial administration, management of tangible capital assets, borrowing, conflicts of interest, land management, and oil and gas moneys management.

The FMB has produced a sample FAL which contains the minimum standards required to obtain approval from the FMB. While the sample FAL is comprehensive from the view of the FMB, its provisions may not be suitable for all First Nations. The appropriateness of the sample FAL will depend on the type and complexity of economic activities a First Nation engages in. As a result, the sample FAL may have to be adjusted in order to ensure it meets the particular circumstances of a First Nation.

Whether a First Nation uses the sample FAL or develops its own within existing policies, compliance approval from the FMB is required. Before submitting a FAL for formal review, a First Nation can submit a draft FAL for an informal review. The FMB will then provide feedback as to whether or not the FAL meets its standards and how to resolve any outstanding issues. This informal review process can be undertaken as many times as required, until full compliance by the First Nation is reached.

Formal review of a FAL requires a First Nation to submit an electronic draft to the FMB along with a BCR approving its submission. FALs are reviewed once per month at a FMB meeting. After its review, the FMB will send a Letter of Notification to the First Nation with its decision. If approved, the FAL will be published in the *First Nations Gazette*. If the FAL is not approved, the FMB will make recommendations for achieving compliance with its standards.

Financial Management System Certification

Financial Management System Certification (“FMC”) allows a First Nation to demonstrate that it has the financial management capacity to become a borrowing member. The FMC ensures that a First Nation is functioning in a manner consistent with sound financial operating, management, and reporting practices. In doing so, a First Nation must demonstrate that it is operating according to its approved FAL.

The FMB recommends that a First Nation review its existing financial management policies and procedures to determine if financial management practices need to be established or improved. To facilitate this process, the FMB has created a Financial Management System Self Assessment

tool, which can be used to identify the gaps in current administrative policies. Currently, the FMB is in the process of developing over 31 sample policies to assist First Nations in establishing comprehensive financial management practices.

Once a First Nation has the required financial management policies in place, it may request an informal review by the FMB. This review is generally limited to assessing the First Nations' completed work plan and self assessment, but may also include a site visit if requested. The FMB will communicate the results of the informal review and provide recommendations in cases of non-compliance.

A First Nation may request a formal FMC review by submitting a BCR. The FMB will then conduct an on-site operational review of the First Nations' records and documents. After the review is completed, the FMB will send a Letter of Notification with its decision on certification.

Financial Performance Certification

Financial Performance Certification ("FPC") is also required to become a full borrowing member under the FSMA, and to receive a specific loan from the FNFA.

The FPC is designed to review the financial health of a First Nation and examine how well financial resources are being used to operate its government. Seven key financial ratios are examined by the FMB, using audited financial statements. These ratios are designed to measure different indicators of a First Nations' financial condition including:

- revenue and expense growth rates;
- ability to meet short term operating obligations;
- ability to generate sufficient annual cash flow for operations;
- ability to maintain a sustainable level of capital investment;
- debt burden;
- ability to manage and execute budgets; and
- efficiency and stability in collecting property taxes.

A First Nation may request an informal FPC review by providing the FMB with its last five years of audited financial statements and the contact information of First Nations staff

responsible for financial administration. The FMB will then contact the First Nation to discuss the scope of the review and any additional information it may require.

A formal request for a FPC can be made by providing the same financial information described above for the informal review, as well as a BCR requesting the review. The FMB will conduct the review against its performance standards and provide a Letter of Notification once complete. This letter will detail its findings, observations and decision on whether or not to issue a certificate. Only First Nations that are in compliance with the FMB standards and have an approved FAL will be issued a FPC. This certification can be undertaken concurrently with FAL approval request.

Certification Options

All First Nations wishing to become borrowing members and secure financing through the FNFA must have an approved FAL and both the FMC and FPC certifications. However, there are two ways a First Nation may do so—either by Full Certification Entry or Fast Track Entry (see summarized process in Table 1 below).

In the Fast Track Entry option, a First Nation applies for compliance approval of its FAL and its FPC certificate concurrently. While core FAL standards must be in force immediately, the Fast Track Entry process allows the First Nation to implement the remainder of the FAL standards over a 36 month period. During this time, the First Nation is expected to obtain its FMC and become a full borrowing member.

The Fast Track Entry responds to First Nations who want to obtain funding as soon as possible in order to support their economic development agenda. Fast Track Entry is only available for first time borrowers with adequate revenue capacity and a history of good financial performance.

The Full Certification Entry option requires that a First Nation have a fully implemented FAL. After the FAL is operational, the First Nation will then apply for FMC and FPC certifications. The Full Certification Entry option is best for First Nations with a longer term economic development agenda that wish to get their financial management systems in good order before becoming a borrowing member.

In order to maintain borrowing membership, First Nations must update their FMC every 36 months and their FPC with every new borrowing request—regardless of what entry option was initially chosen.

Table 1: Certification Options and Process

<p>FAST TRACK</p> <p>Develop FAL</p> <p>FAL Review</p> <p>FAL Compliance Approval</p> <p>Core FAL Provisions in Force</p> <p style="text-align: center;">↓</p> <p>Financial Performance Review</p> <p>Financial Performance Certificate</p> <p style="text-align: center;">↓</p> <p>Qualification as Borrowing Member</p> <p style="text-align: center;">↓</p> <p>Fully Implemented FAL</p> <p>Financial Management System Review</p> <p>Financial Performance Certificate</p> <p style="text-align: center;">↓</p> <p>Maintain Borrowing Member Status</p>	<p>FULL CERTIFICATION</p> <p>Develop FAL</p> <p>FAL Review</p> <p>FAL Compliance Approval</p> <p>Fully Implemented FAL</p> <p style="text-align: center;">↓</p> <p>Financial Management System Review</p> <p>Financial Management System Certificate</p> <p style="text-align: center;">↓</p> <p>Financial Performance Review</p> <p>Financial Performance Certificate</p> <p style="text-align: center;">↓</p> <p>Qualification as Borrowing Member</p> <p style="text-align: center;">↓</p> <p>Maintain Borrowing Member Status</p>
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Benefits and Drawbacks to Taxation under the FSMA

The primary benefit of the FSMA is that it allows First Nations to pool local revenues to access financing tools not available under the *Indian Act*. In doing so, First Nations are able to independently fund economic development activities with lower interest rates and longer terms than with traditional financial institutions. The standards created by the FSMA also encourage

appropriate financial management practices and create opportunities for First Nation governments to access capacity development resources provided by the FMB. First Nations may also become a ‘public body’ under the *Income Tax Act*. This could create considerable income tax exemptions if a First Nation has business and economic interests off reserve. In turn, First Nations communities would retain greater wealth.

Sample by-laws, policies and funding provided by the FMB can reduce costs for First Nations and support the transition to the FSMA. The use of financial administration standards ultimately creates transparency, consistency in First Nations taxation and certainty for investors.

While undoubtedly a step toward more meaningful self-government, the FSMA also has its drawbacks. As is evident from the steps described above, becoming a borrowing member can require a First Nation to expend a considerable amount of time, effort, and money to develop the necessary laws, policies, and administrative procedures. Depending on the economic development activities and capacity of the First Nation, this process may prove difficult. Once certified, First Nations then become subject to ongoing review by the various FSMA entities. First Nations must maintain their financial management systems according to FSMA standards or they risk being placed under co-management or third-party management. The standards set by the FMB have been criticized for creating rigid administrative burdens greater than those on other local governments.⁷

Finally, while the process of becoming a borrowing member is clearly articulated, the process to opt-out of the FMSA is not. This could create difficulties for First Nations who are unable to maintain FMB standards and wish to return to taxation under the *Indian Act*.

Courts’ Consideration of First Nations’ Tax By-Laws

Property taxation is one area where the courts have considered the scope of a band’s by-law making power. The tax cases have explicitly recognized that the power to tax is an exercise in self government.⁸

⁷ See AANDC review of FSMA.

⁸ *Canadian Pacific Ltd. v. Matsqui Indian Band*, [2000] 1 F.C. 325 (F.C.A.).

The *Osoyoos* case considered the phrase “in the reserve” in the context of the band’s ability to tax.⁹ The band purported to impose property taxes on an irrigation canal that bisected its reserve. The lands were subject to an Order in Council issued under section 35 of the *Indian Act*, which consented to the transfer of administration and control of the lands to the province for irrigation canal purposes. The Band purported to tax the irrigation canal. The Town of Oliver objected to the assessment, claiming the lands were not taxable as they were no longer part of the reserve.

The Supreme Court of Canada narrowly held that the nature of the interest conveyed by the Order in Council was ambiguous, and therefore the land remained part of the reserve. The court articulated the principle of “minimal impairment” – that once it is determined that an expropriation of reserve lands is in the public interest, a fiduciary duty arises on the part of the Crown to expropriate or grant only the minimum interest in order to fulfill that public purpose, while preserving the interest in the land to the greatest extent practicable. As a result, the majority of the court held that only an easement was granted and the lands remained “in the reserve” and were therefore taxable.

The *Seabird Island* case considered an Order in Council where the Governor in Council authorized the taking of lands for road purposes.¹⁰ The issue in *Seabird Island* was whether a fibre optic cable within the road right-of-way was taxable. Relying on *Osoyoos*, the Federal Court of Appeal held that the Crown had not shown a clear and plain intention to extinguish the reserve interest and the interests of BC Tel were taxable.

The result of these decisions is that railways, canals, telephone and other rights-of-way which were once thought to be non-taxable, as being outside of the reserve, are taxable and a potential source of income for First Nations.¹¹

Conclusion

Property taxation by First Nation governments has the potential to generate significant revenue opportunities, which can be used to create economic and social benefits for their communities. While there are a growing number of First Nations already collecting tax revenue, these

⁹ *Osoyoos Indian Band v. Oliver (Town)*, [2001] 3 S.C.R. 746, 2001 SCC 85.

¹⁰ *BC Tel v. Seabird Island*, 2002 FCA 288.

¹¹ Provincial interests, such as roads and hydro are not taxable, see *Westbank First Nation v. BC Hydro*, [1999] 3 S.C.R. 134. However, public utilities such as BC Hydro provide grants in lieu of taxes.

communities represent only 20% of the potential tax base of First Nations.¹² Thus, there are many more First Nations communities that could benefit from implementing property taxation schemes, either through the *Indian Act* or the FSMA.

As described above, each system has benefits and drawbacks. The decision of which taxation route to take, is therefore dependant on the unique goals and circumstances of each First Nation. The FNTC provides a number of resources and educational programs to assist First Nations in building the capacity to effectively administer their property tax administration as well as facilitate investment on First Nations lands. While neither the *Indian Act* nor the FSMA provide a perfect model for the development and implementation of property tax laws, each have the potential to support First Nations in generating revenue, building local infrastructure and providing on reserve services to their communities.

¹² First Nations Tax Commission, *First Nations Real Property Taxation Guide*, 2nd ed. (2011), online: <http://www.fntc.ca/dmdocuments/General/property_taxation_guide_2011.pdf>.