

Aboriginal Resource Tax – Closing the Infrastructure Gap

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Prepared for the First Nations Tax Commission

This paper reflects the views of the authors only and not necessarily those of the First Nations Tax Commission



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Disclaimer

The Aboriginal Resource Tax (ART) is a proposal led by First Nations to formally tax resource and resource infrastructure projects and expansions taking place on their (traditional) territories.¹ The ART would replace the present practice of negotiating unique financial arrangements every time a project infringes on First Nations title or potentially a Treaty right. The First Nations championing this proposal have requested the support of the First Nation Tax Commission (FNTC). This paper summarizes the rationale and concept for ART. It has been prepared for the review of the FNTC and proponent First Nations. It is being shared in this forum for discussion purposes.

Overview

The ART is being proposed, in part, to help First Nations address their infrastructure deficit, which is far more acute than in the rest of Canada.² However, the ART also serves broader goals such as defining and implementing Treaty and title rights, improving the investment process in Canada, and shifting the approach for resolving First Nation disparities from program driven to economic driven approaches.

The original impetus for the ART was the specific challenges and opportunities that recent Court decisions concerning Aboriginal title have created for investors and First Nations with respect to resource development. The decision created the requirement for First Nations consent before a project can proceed on land under claim. A "consent" process evolved as a result of the decision, however, it is simply taking too long to navigate, and this is deterring investment.³ The length of the process could cause otherwise acceptable projects to leave Canada and that has implications for the future standard of living as well as the ability of Canada to fund infrastructure and public services.

The ART would simplify the consent process. However, it would not lower the bar of what is acceptable to a First Nation with respect to a project. For example, it would not lower

¹ The term "territory" will be used throughout this paper to refer to the entire area occupied and used by a First Nation.

² Infrastructure issues on reserves are in many cases posing major threats to health and safety. <http://www.cbc.ca/news/canada/clean-running-water-still-a-luxury-on-many-native-reserves-1.1081705>. Some estimates are that the First Nations infrastructure gap is more than \$40 billion, an enormous fund for relatively small First Nations. http://www.wawataynews.ca/archive/all/2011/9/1/huge-first-nations-infrastructure-gap-reported_21819

³ <http://www.theglobeandmail.com/globe-debate/the-world-wont-wait-for-bcs-lng/article24674728/>



environmental standards. It would not reduce the ability of a First Nation to negotiate employment provisions or to protect important sites. It would replace the currently separate negotiations about financial compensation that take place with both provinces and companies, with a pre-specified tax regime.⁴ Existing revenue sharing and revenue agreements would be converted into a new tax and other governments would adjust by vacating a roughly “revenue equivalent” amount of tax room. In addition to reducing the scope of a negotiation, it would allow the ongoing management of multiple agreements to be replaced by a single tax administration.

While the ART was originally designed to meet the challenges created by Aboriginal title, there is some commonality between the issues raised by Aboriginal title and those raised by Treaty rights. Accordingly, many Treaty First Nations have also expressed an interest in developing an ART as a method of implementing their rights.

The most common issue is that opposition to a project, from Treaty First Nations can cause investments to be slowed or substantially delayed just like in a title context.⁵ Treaty First Nations also assert a right to share in the revenues generated by projects on their territories. The resource industry would like to see evidence of support for projects from Treaty First Nations before committing substantial funds on investment, just like in a title case. They wish to avoid any agenda that is based on the extinguishment of pre-existing title or rights and instead, prefer an approach that is based on defining their jurisdiction.

Canada needs the Aboriginal resource tax

Canada needs the ART because it needs resource investment. Resource investment will work better if the First Nations upon whose territory it takes place support the project. In some cases, this is preferable, but in a title context it is a necessity. This support depends upon First Nations receiving a share of the revenues that are generated by the project. Finally, and this is the point of this paper, the “best” mechanism for sharing is the ART. It

⁴ Typically, there is a two stage process that occurs whenever Aboriginal title is infringed upon. Companies must first negotiate the consent of First Nations for a project and then there is a separate negotiation between the First Nation and the province. Both these negotiations culminate in either rejection or agreements that typically include financial agreements. These agreements will be termed “revenue agreements” when they are made with companies and “revenue sharing agreements” when they involve the sharing of the relevant provincial resource tax.

⁵ <http://www.theglobeandmail.com/globe-debate/first-nations-dont-have-a-pipeline-veto-but-they-do-have-options/article547673/>



corrects the flaws that are inherent in existing approaches such as royalty sharing⁶ or securing contributions directly from companies through negotiations.

These points are explained in more detail below.

1. Canada needs resource investment to fund infrastructure

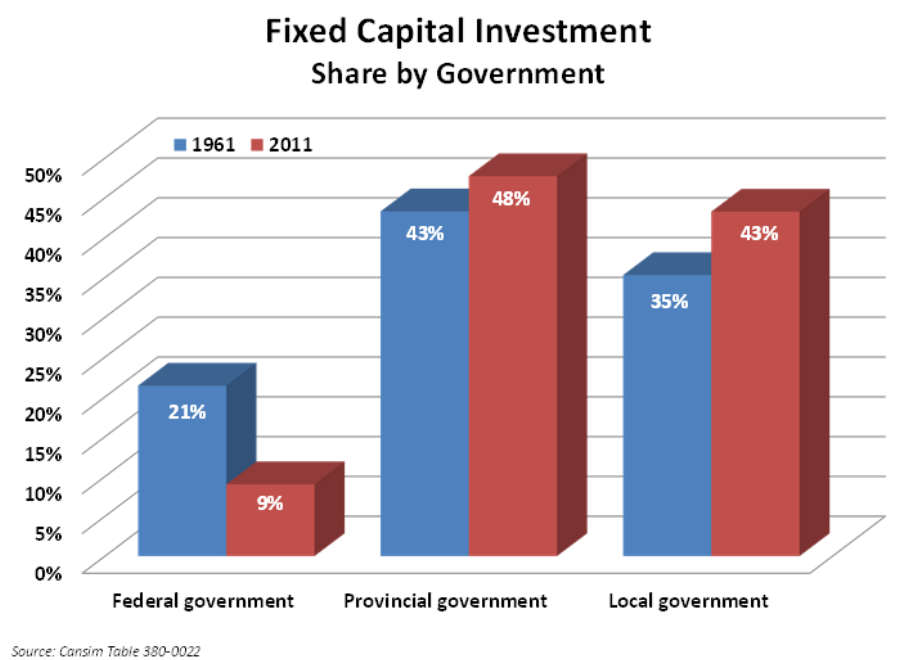
Canada needs the revenues that resource investment could deliver. The Parliamentary Budget Office (PBO) has analyzed the fiscal challenges facing Canadian governments. It has concluded that federal expenditure obligations are sustainable under existing levels of taxation. However, unless productivity improves considerably, present levels of provincial-local services are not fiscally sustainable without some combination of large expenditure cuts or tax increases.⁷ In light of this fiscal challenge, it is going to become increasingly difficult to fund new public infrastructure or even maintain the existing stock.

The fact that the fiscal challenge is going to be acute at the provincial level is particularly problematic because the majority of infrastructure expenditures are performed by the provincial-local sector.

⁶ The term “royalty sharing” will be used in this paper for the sharing of any provincial resource tax or royalty.

⁷ <http://news.nationalpost.com/news/canada/canadian-politics/ottawas-overhaul-of-health-care-funding-has-left-enormous-fiscal-gap-for-provinces-pbo-warns>



Figure 1. Fixed Capital Investment (share by government)

The challenges and unpleasant fiscal choices facing provincial governments can, as was already noted, be ameliorated by some combination of greater federal contributions to the cost of provincial services or productivity improvements. Productivity improvements would cause government revenues to grow faster than forecast and this would create the additional fiscal room needed to fund infrastructure without either tax increases or cuts to other expenditures. Resource projects are particularly well suited to the task of improving productivity because they produce resource revenues as well as high paying private sector jobs that are strong net contributors to the tax base.

The importance of resource investment to the task of alleviating fiscal challenges is illustrated in the two figures below. They show the net contribution of resource sector workers to the fiscal balance in Canada. Some rudimentary estimates of the net tax contribution per worker are compared to the average government expenditures made per person.

The bar on the left of each graph shows the income tax and royalty contribution per worker during the development or construction phase of a mine and a pipeline respectively. The middle bar shows the income, sales and property tax and royalty contribution per worker during the operation phase of a mine and pipeline. The bar on the right compares this to average government expenditure per capita.





Figure 2. The figure illustrates the average net revenue produced per worker by an average mine during its development and then operations phases.

Average Annual per PYE Mining Government Revenues vs. per capita Government Expenditures

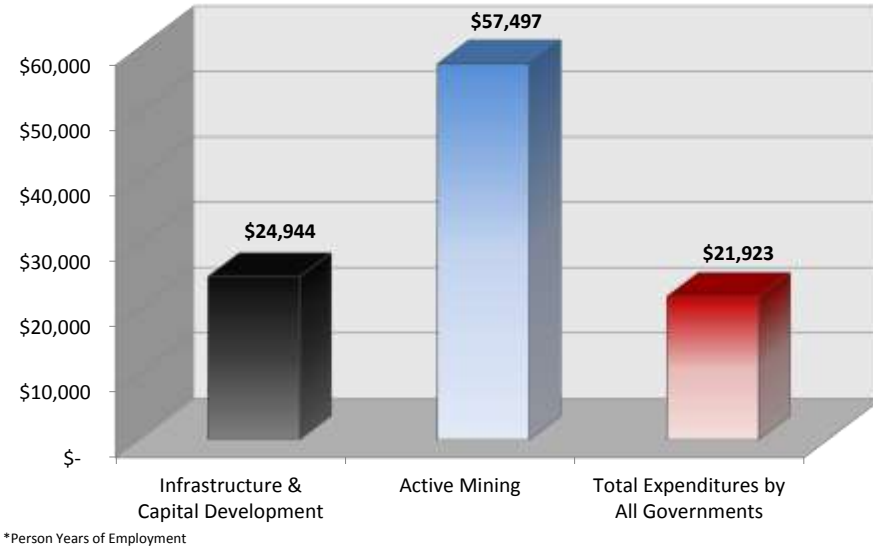
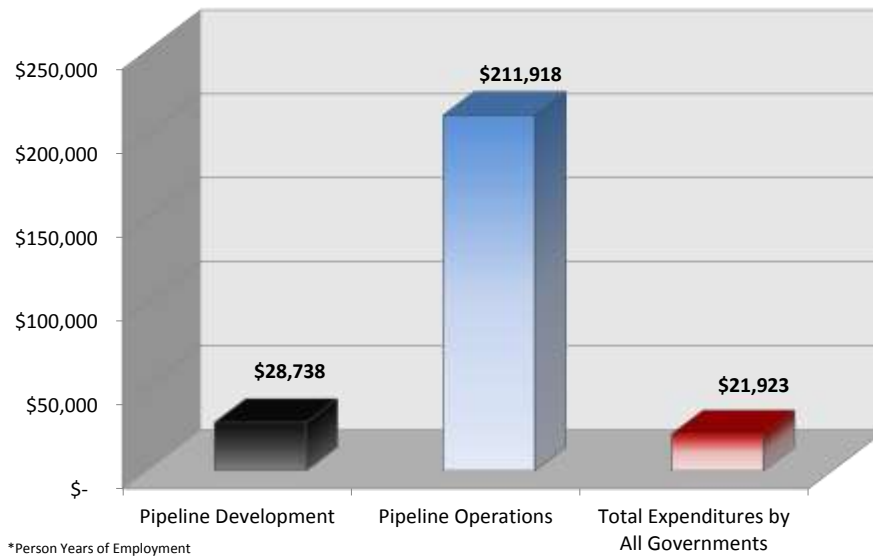


Figure 3. The figure shows the average net fiscal contribution per worker of a pipeline project during its construction and then operating phase.

Average Annual per PYE Pipeline Government Revenues vs. per capita Government Expenditures



2. First Nations need a fiscal stake in resource investment

The demonstration above showed how a resource strategy would contribute to a Canadian productivity strategy. However, by some accounts, Canada is getting a poor reputation as a place for resource investments.⁸ A large part of the reason is the perceived lack of resolution of outstanding First Nations issues.⁹ Investors are not sure what will be required to get First Nations consent; how long it will take to get that consent; or, in many cases, whether it is even possible to ever gain consent. The problem is that the “consent” process is opaque and uncertain.

It is uncertain because there is no “one size fits all” solution to the First Nation issues that arise with specific projects. Every project raises unique issues and every First Nation has distinct interests and many of these issues are not financial. Nonetheless, it is fair to say that in virtually every case, **First Nations want to share in the government revenues generated by projects on their territory.** This is the “fiscal issue” and its resolution is a necessary, but not a sufficient, condition for gaining First Nations support.

The First Nations perspective on the fiscal issue bears some elaboration. Consider the situation in a First Nation where a resource project is proposed for its territory, but there is no royalty sharing. The revenues generated by a hypothetical mine were estimated to illustrate this example.

The mine will generate millions of dollars in new tax revenues over its lifetime. Estimates are shown in the attached graph.¹⁰ These revenues will be shared between the federal and provincial/local orders of government. However, when there is no royalty sharing, the First Nations upon whose (traditional) territory these projects take place will receive no direct revenues. They will be shared between the provincial-local and federal sectors as illustrated.

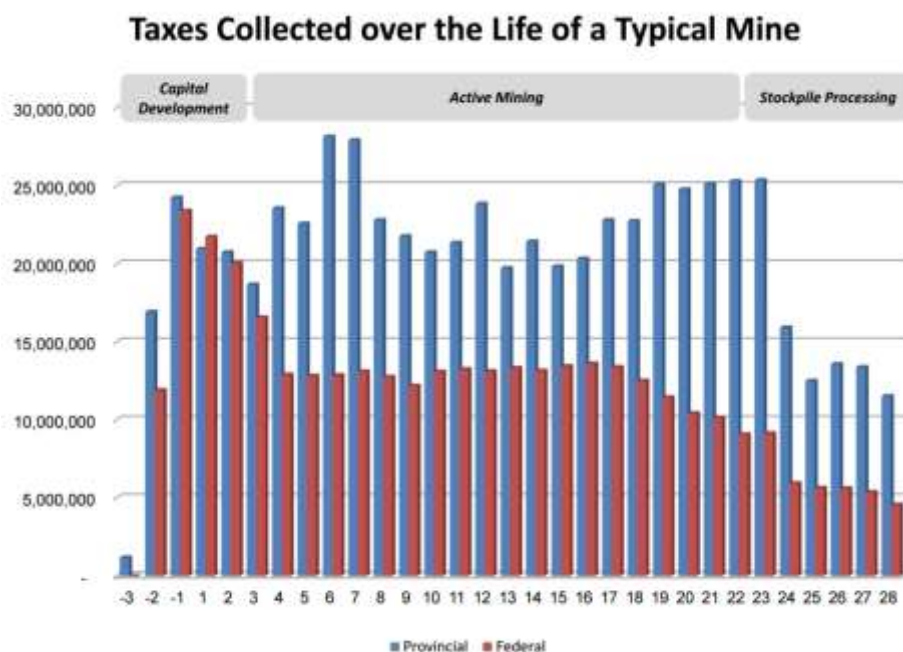
⁸ <http://www.timminspress.com/2015/03/05/cda-gaining-poor-rep-starting-up-mining-projects--charest>

⁹ http://business.financialpost.com/news/energy/170-legal-victories-empower-first-nations-in-fight-over-resource-development?__lsa=2d40-46b2

¹⁰ The revenues that were estimated include: mining taxes and also the income, sales and property tax paid by workers and the company. The methodology used in producing these revenues is in an attached appendix).



Figure 4. Taxes collected over the life of a typical mine



In fact, not only will the First Nation not receive any of the direct revenues, it will also not typically receive any of the indirect fiscal benefits generated by these revenues. For example, it is unlikely to enjoy increased programming or transfers from other governments.

The “provincial” part of the reason it does not share indirectly is that the provincial position is that “provincial” services¹¹ to First Nation persons on reserve are a federal responsibility. First Nation persons on reserve are therefore specifically excluded from sharing the, now enhanced, provincial services. The only benefit received by these people as a result of the new provincial revenues would be through enhancements to generally available provincial services, such as highways.

The “federal” part of the reason is that the federal government does not typically link its transfers to First Nations to the development of federal revenues on that First Nation’s territory. Instead, they have implemented what First Nation leaders call a “cap” on transfers. The “cap” is a 2 per cent per annum growth rate. The growth of the transfer is not keeping pace with population growth and inflation. This cap is also below the minimum

¹¹ “Provincial services” refers to all the services that non-First Nation persons normally receive from provincial governments. This would include health care and education.



projected growth of federal transfers to provincial governments as specified in recent medium term federal fiscal plans.

The bottom line is that, when there is no royalty sharing, *new resource projects on their territory actually contribute to a widening of service and infrastructure disparities*. So long as this phenomenon persists, it is going to be difficult to secure First Nations support for projects.

This will be termed the First Nations “fiscal issue”.

3. The limitations of royalty sharing

“Royalty sharing” has emerged in some provinces as a mechanism to address the fiscal issue identified above. It is a convention whereby a provincial government will agree to share the relevant royalties generated by a resource project with the First Nation upon whose territory it takes place. Sharing is typically implemented according a formula specified in an agreement. In some cases, revenue sharing is packaged with a complementary approach whereby a First Nation will secure revenues directly from the company that is proposing the project. This complementary approach is implemented through, “revenue agreements”.¹² Revenue agreements are the subject of the next section.

Revenue sharing and revenue agreements are obviously a vast improvement over a First Nation receiving no revenues at all. They provide First Nations with a real fiscal stake in the success of projects on their territory. Also, resource taxes are clearly linked to the wealth created by the land and resources itself and not necessarily the value created through labour and capital. This aligns them closely with the practical meaning of Aboriginal title. However, both approaches contain flaws and limitations that could be addressed and improved upon through the development of the ART.

Some of these limitations are listed below:

- i) There are many projects that infringe on title that don’t generate royalties. Consequently, royalty sharing is unavailable. In these cases, the onus of a fiscal

¹² Revenue agreements will be used as a generic term to capture the full range of cash payments and payments-in-kind that are made by companies.



accommodation is therefore placed on revenue agreements. This is an issue with the current pipeline proposals.

- ii) Some projects span multiple provinces and, because of this, these projects are often not well suited to the sharing of a provincial royalty. Most of the new revenues may be earned in a different province from the one where a fiscal accommodation is necessary. Again, this is an issue with respect to pipelines.
- iii) Royalties are essentially a tax on profits and profits are more volatile than other revenues. Hence, royalties are often more revenue volatile than other taxes. This is problematic because First Nation governments are small and undiversified and are less able than other governments to bear this volatility. It would be more logical to develop a different sharing mechanism, whereby revenue volatility is borne by the larger and more diversified provincial and/or federal governments.
- iv) Royalties are not earned over the entire life of a project. They are often not generated until several years after construction begins and sometimes substantial revenues are not generated until after the first few years of operation. Most First Nations wish to see their remuneration begin as soon as a project impacts the land. This would show that payment is explicitly tied to infringement of title. It also makes it more likely that the Chief and Council, who advocated a project, will still be in office when the community receives its revenues.
- v) The revenue potential of the shared royalty stream will be largely determined by provincial, and not First Nations, policy once a project is up and running. Provinces will control rates and other factors such as allowable costs and taxable interests. Some First Nations are already familiar with the consequences of unintended policy change as a result of their experiences with GST sharing. They occupied the GST tax room on their lands and took a revenue loss when the federal government reduced the GST rate.¹³.
- vi) Revenue agreements are made with provinces and not the federal government. This raises two considerations. Provinces are going to have less revenue room than the

¹³ The First Nations Goods and Services tax is a federal program whereby a First Nation can collect the GST that is earned on its reserve lands. There are two important conditions. It must charge the tax to Status Indians and it must mirror the federal GST exactly. The federal government assumes all the costs associated with collecting the tax.



federal government over the long term as was already noted. Hence agreements with provincial governments may be less secure in the future. Provinces will be looking for savings as their fiscal challenges increase. Revenues diverted to First Nations may be a logical target, particularly given their position that First Nations are primarily a federal responsibility.

- vii) If royalty sharing becomes widespread, it will create moral hazard for provincial governments. Provinces will begin to find it “cheaper” to offer royalty reductions or holidays relative to other investment inducements. The reason is that much of the fiscal cost of the former will be borne by the First Nations with whom they are sharing revenues whereas, the cost of other inducements will be borne entirely by the province in question.

4. The limitations of revenue agreements

In addition to revenue sharing with provinces, many First Nations strike agreements with companies under which they receive direct financial payments. These payments can take many forms such as signing bonuses, milestone payments, lump sum payments and different formula based approaches. Regardless, they will all be lumped together under the term “revenue agreements” in this paper.

Revenue agreements all constitute a form of “pseudo-taxation” because they have many of the attributes of taxation without being formally recognized as such. For example, they are collected by a government for the general purpose of its community. Payments are not linked to the provision of any specific good or service, as would be the case with a market exchange.

First Nations engage in pseudo-taxation because they need the revenues but do not have formal tax powers. However, while pseudo-taxation raises revenues, it has many shortcomings relative to formal taxation.

- i) Revenue agreements are a hidden tax. They may not increase the official tax rate, but companies will consider them when they make an assessment of the effective tax burden. If they must estimate the likely cost of these agreements before a negotiation, there may also be a substantial risk premium included in their assessment. Consequently, this practice increases opacity and risk and deters investment.



- ii) The negotiations that produce revenue agreements may take a long time. This is particularly true if they are entangled with other issues. There are also additional costs associated with managing a legacy of revenue agreements versus a single tax system.
- iii) It is uncertain how pseudo-tax revenues will be treated relative to tax revenues under different scenarios. For example, in the event of a bankruptcy would taxes owed a First Nation be given a higher priority than monies owed under an agreement? It is also uncertain as to what fiscal treatment these revenues might receive from other governments.

Why the ART is an improvement

ART would be an improvement over both royalty sharing and/or revenue agreements.

1. The ART would signal a recognition of First Nation Treaty rights and/or Aboriginal title.

Most First Nations prefer an approach to title that is based on implementing title and recognizing the attached jurisdictions. Royalty sharing addresses the fiscal issue but it does not implement the attached jurisdiction. Instead, it is an agreement under the Common law, based on sharing revenues collected under a provincial revenue jurisdiction. It therefore contributes to a widely held apprehension that revenue sharing is based on agenda of ultimately extinguishing jurisdiction and/or title.

By contrast, the ART would be viewed as implementing a First Nations jurisdiction. It would signal a shift of the Provincial agenda from one of extinguishing title and denying jurisdiction to implementing title and delineating jurisdiction. That would help facilitate agreements over all issues.

2. The ART would provide many First Nations with their first opportunity to directly share in the fiscal benefits brought by resource development on their territories.

The participation of the federal government in the ART would allow First Nations all over the country to share the revenues generated by resource development on their territories. This would be a first for all those First Nations who are presently not able to even share royalties. If the federal government goes beyond simply providing revenue room to support an ART and designs a program that induces provincial participation, these benefits will be



amplified and it will be possible to develop an internally consistent and seamless national approach to First Nations participation in resource projects.

3. The ART would improve the investment facilitation process

The present processes for gaining consent or First Nations support do not work in a timely enough fashion to properly support resource investment in Canada. Investment can move no faster than the capacity of relatively small First Nations to analyze complex projects, conduct community processes, and then negotiate complex matters. This is further complicated by the entwining of financial and non-financial issues and the two stage process. Furthermore, these processes must be repeated every time there is a new project or project expansion on a First Nation's territory. If a project spans multiple territories, the complexity of the process rises still further. Yet another issue is that the demands placed on First Nation administrations by reporting requirements from federal agencies are already very high.¹⁴

It is not only First Nations that need a better process but also Canada. In fact, improvements are also needed in the reporting requirements.

The ART could help bring this about. To illustrate how the ART would help, the investment facilitation process envisioned under the ART will be compared to the process that has evolved in BC as a result of the recognition of Aboriginal title.

¹⁴ http://www.oag-bvg.gc.ca/internet/English/parl_oag_200212_01_e_12395.html



The Current Process

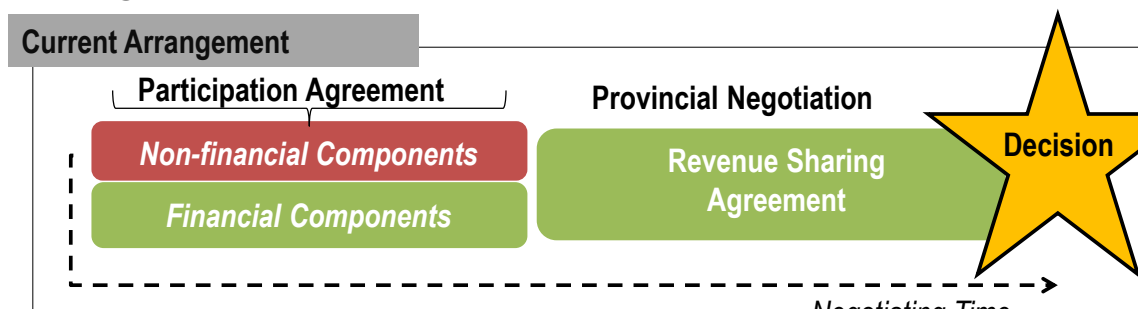
The BC process is a two stage negotiation. Financial arrangements must be concluded with the company proponent (along with other issues), and only if this is successfully completed, are negotiations then conducted with the provincial government. Figure 5 illustrates the process.

The figure shows that the company negotiation encompasses both financial and non-financial issues and these issues are entwined. Non-financial components typically include a negotiation about how to address impacts on the environment and traditional way of life. Other non-financial issues might include preferential job placement for Members, access to contracting opportunities for Members and Band owned entities, or mechanisms for dispute resolution and ongoing participation by the First Nation in the management of the project.

Only when this stage is complete, does negotiation with the Province begin. The negotiation with the Province also mixes purely financial issues with non-financial issues. The financial issues are typically about the nature of a royalty sharing agreement.

The bottom line is that it can take a considerable amount of time to get to final approval.

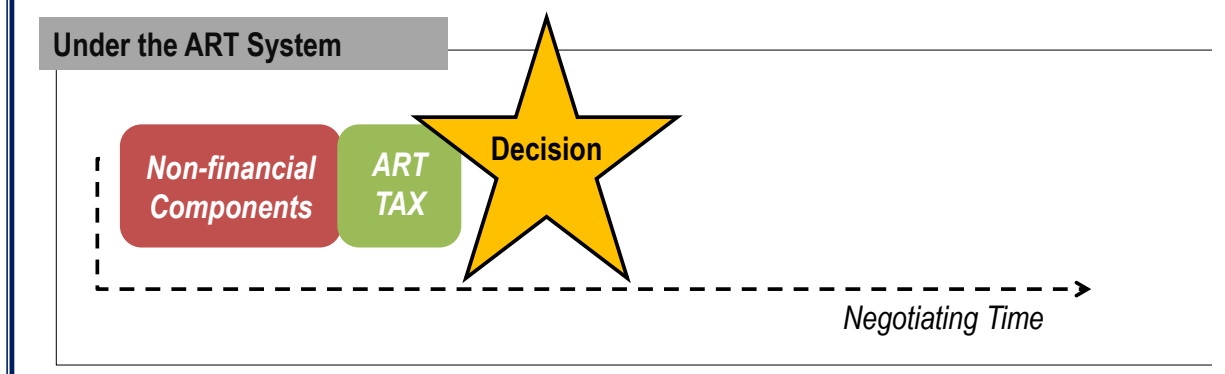
The timeline of a typical agreement under the revenue sharing approach to Aboriginal title.



The Process under ART

The ART would not change the entire “consent” process. However, it would simplify the process by removing the need to negotiate two separate financial components. These would be replaced by a single transparent and pre-specified tax regime. As was noted above, the non-financial components of a project would still need to be negotiated. However, the ART would have simplified both stages of the negotiation.

Streamlining of this approach as a result of the implementation of the ART



There are four sub points to the argument that the ART would improve investment facilitation.

- a. **It would signal a shift in the government agenda from “extinguishment” of title or rights to “definition and delineation” of a recognized jurisdiction.**

The implementation of the ART and the coordination of it with other taxes would signal a recognition by other governments that they no longer believe their interests can only be met through the extinguishment of First Nations title and jurisdiction. It would show a willingness to assert government interests by working out terms for concurrent jurisdictions. This shift would help facilitate agreements based on mutual interests over the full range of issues raised by Aboriginal title. It would also reduce the complexity of agreements by removing the need for First Nations to create contractual alternatives to the security offered by jurisdiction.



b. Reduces the administrative burden on First Nations

First Nation administrations are relatively small and overburdened.¹ This is making it difficult for them to expedite consent decisions because these projects are often very complex. The ART would replace the need to negotiate and then manage multiple agreements with an automatic pre-specified tax and a single tax administration.

c. Reduces the cost and complexity of negotiations

A principal goal of the ART is to reduce the complexity of consent negotiations with First Nations. The ART would do this by removing the need to negotiate major financial aspects from both stages of the negotiation. It would mean the financial aspects of a deal could be separated from the other aspects and further simplify the negotiation.

d. Creates greater transparency

Companies considering major investments would prefer to understand their likely tax burden at the beginning of the process. This type of transparency is not possible so long as the practice of negotiating unique pseudo-taxation arrangements persists.

4. Politically reliable revenues for First Nations

Revenue sharing is based on a First Nation sharing of a tax stream that is still controlled by a provincial government. The province in question will be solely responsible for setting tax rates, establishing the tax base and all the other parameters that collectively determine the revenue potential of the tax in question. They will likely make changes in these policies without reference to their impact on First Nation revenues. This creates revenue uncertainty for the First Nation.

5. Economically reliable revenues for First Nations.

Royalties are one of the most volatile tax sources. They work essentially as a profit tax and profits are more volatile than other tax bases such as income and sales tax. First Nations have relatively small and undiversified revenue bases and are less able to bear such volatility. The ART would allow First Nations to design a more stable and suitable tax out of vacated tax room.



6. It would support a broader range of projects

Many types of project are not well suited to a royalty sharing solution because they do not generate royalties. In other situations, like pipelines, they enhance royalties but not in the province where the fiscal accommodation must take place.

Why the ART should be cost shared

First Nations across the country are advocating for royalty sharing. However, royalties are a provincial revenue while First Nations are a federal responsibility. Therefore, royalty sharing implies using provincial revenues to meet federal responsibilities. Provincial governments are also likely apprehensive that royalty sharing will lead to a gradual offloading of federal responsibilities for First Nation services. When these revenues are applied to housing and infrastructure on reserve, or lead to improve socio-economic outcomes, they reduce federal rather than provincial liabilities.

Royalties were targeted for sharing simply because, more than any other revenue stream derived from resource development, royalties are based on the value of the land and resource themselves. The issue of who has the responsibility for providing First Nation services was not a factor.

The fact that transferred provincial revenues may be subsidizing federal responsibilities, and are certainly reducing federal liabilities, raises the question of whether the federal government should contribute to the costs of resolving the First Nations fiscal issue. In fact, there are many policy reasons that the federal government should share the direct costs of fiscally accommodating First Nations.

This raises a key difference between the ART and royalty sharing. Rather than requiring First Nations to share an existing revenue stream, the ART envisions the creation of a unique tax. The ART would therefore allow both governments to share the costs of fiscally accommodating First Nations.

The rationale for federal participation in the creation of tax room to support the ART is listed below:



1. First Nations are a federal responsibility and the ART will reduce federal financial liabilities.

The ART will generate revenues that primarily fund areas of currently federal responsibilities. It will reduce federal liabilities attached to First Nations poverty, housing and substandard infrastructure.

2. Addresses trans-provincial issues.

Some projects, such as pipelines, span multiple provinces. The First Nations that need to be accommodated, in order for a project to proceed, may not even be within the province where most of the additional revenues are generated. Federal participation in a program to create tax room for the ART would help address such issues.

3. The ART will generate new revenues for both orders of government.

The ART will generate revenues for both orders of government if it improves the investment climate. The ART will result in the diversion of income tax paid by First Nation persons to provincial governments who have no responsibility to supply services to reserves.

4. Reduce fiscal imbalance

Provincial governments and the PBO argue that the federal government is going to have more fiscal room than either provincial or local governments over the medium to long term. If the costs of a fiscal accommodation of First Nations are limited to royalty sharing, this imbalance is going to be worsened since it will divert provincial revenues towards federal responsibilities. On the other hand, if the fiscal accommodation of First Nations is accomplished through a vacation of tax room by both orders of government, it will not substantially worsen the fiscal imbalance and could conceivably improve it.

5. Federal inducement may be necessary

A national approach to the fiscal accommodation of First Nations would work better than a province by province approach. This would ensure that projects that span multiple provinces can be facilitated. It would promote equity among provinces and among First Nations in different provinces. However, this is unlikely to happen without the leadership of the federal government.



Conclusions

Canada's infrastructure challenge can be met by meeting the productivity challenge. If productivity does not improve it is going to be difficult to meet the infrastructure challenge because health care costs will consume most new government revenues.

Part of the solution to this challenge is improving the investment climate for resource projects. Resource development produces very high government revenues through both royalties and taxes. However, investors all would prefer to see the support of local First Nations before going forward with any investment project. In some cases, this is only a preference brought on by uncertainty about the extent of Treaty rights. In other cases, it is a legal necessity brought on by claims of Aboriginal title.

There is no simple solution to the challenge of gaining First Nations support for a project. Every project raises unique issues and every First Nation has unique interests and perspectives. However, in virtually every case, there is a "fiscal issue". First Nations see other governments receiving revenues from the projects while they remain subject to a 2 per cent annual increase in transfers, which they refer to as the "cap". This is part of the reason that the infrastructure deficit facing First Nations far exceeds, at least in per capita terms, that facing Canada as a whole. So while there is no simple solution, the fiscal issue needs to be addressed with virtually every project before First Nations support will materialize.

Royalty sharing has helped address the First Nations fiscal issue in some provinces. However, it is limited in several respects. It calls upon provincial governments to bear the costs of accommodating First Nations, yet the federal government is a major fiscal beneficiary of the projects and the federal government has the primary responsibility for funding the services and infrastructure that the new revenues will subsidize. Royalties are unreliable revenue and not well suited to relatively small and undiversified First Nation revenue bases. Also, royalty sharing is not available as a solution to projects that do not generate royalties. In these cases, the entire onus for a fiscal accommodation is placed on companies through pseudo-taxation. Unfortunately pseudo-taxation has very negative consequences for investment.

The ART could provide a better way. (a) It would shift the perceived agenda for First Nation issues from "extinguishment" of title or rights to "articulation" of jurisdiction. (b) It



would provide many First Nations with a relatively simple way to share revenues whenever a new project or expansion takes place on their territory. (c) It would remove the need for complex negotiations about these matters with both companies and provinces. (d) It would reduce the need for a First Nation to manage an ever growing portfolio of unique agreements. (e) It would reduce the opacity created by the fact that fiscal arrangements are not currently pre-specified. (e) It would allow a fiscal solution to be applied to projects that do not directly generate royalties. (f) It would allow First Nations to design a tax that is more reliable than current arrangements and better suited to their status as small and financially undiversified governments. (g) It would open the door for the federal government to share the costs of the fiscal accommodation which would better address provincial issues and apprehensions that are currently inhibiting solutions. (h) It would create a useful revenue stream for the financing of First Nations infrastructure

improvements.



The key to making the ART would be: (a) the creation of revenue room by other governments and a federal-provincial agreement to this effect; (b) institutional support for the implementation of the ART by participating First Nations; and, (c) institutional support for the fiscal coordination of the new tax within Canadian fiscal arrangements.

Figure 5. Creating a fiscal stake for First Nations in resource projects on their territory is a key to solving Canada’s productivity challenge.



Recommendations

The ART should be developed along two tracks: (a) The FNTC should work with SSN and other interested First Nations on developing the ART as a “thin” interim Treaty measure for implementation in BC. The ART would be developed as a formal tax and an alternative to royalty sharing. Part of the ART regime would also be made applicable to projects that do not generate direct royalties. (b) The FNTC should work with SSN, other interested First Nations, and potentially provincial governments on developing a complementary federal initiative on the ART. This would likely involve the federal government offering additional tax room to match that offered by a province, subject to program limitations. Federal participation would help address provincial apprehensions about the potential for a provincial only ART to lead to an offloading of responsibilities for Status Indians on reserve. It could also be part of a package for addressing provincial claims of a widening fiscal imbalance emerging as a result of federal reductions in the Canada Health and Social Transfer (CHST) escalator. Finally, it would be a logical complementary measure for enhancing federal infrastructure initiatives and providing the basis for a solution to the First Nations infrastructure deficit.

The BC Track

- The FNTC should work with interested First Nations and the Province on the design of an ART. The specifications should be for a tax that presents: low administration costs; relative transparency; and, does not conflict with the need of major developments for upfront capital.
- The FNTC should work with interested First Nations and the Province on an administrative framework for the ART. This should include model laws, administrative training, expenditure laws, rates laws, fiscal and capital planning, and support for service agreements.
- The FNTC should work with the Province on the development of an approach to tax coordination. Some possibilities include a tax credit based on eligible ART paid or a rates reduction.



The Federal Track

- A paper should be developed for presentation to provincial and federal governments about the desirability of a federal component to creating tax room for the ART.
- The paper would emphasize the importance of federal participation in providing assurances that the development of the ART from provincial tax room will not worsen the fiscal imbalance.
- It should emphasize the importance of the ART in meeting federal obligations such as First Nations infrastructure.
- It should emphasize the importance of federal participation in ensuring a national transportation infrastructure.
- Federal participation would ensure that the federal government does not profit from pseudo-taxation through offsets and, in fact, creates tax room to eliminate this practice.
- Federal participation should go beyond creating tax room. Federal participation could also help ensure a fair fiscal treatment among provinces and among First Nations in different provinces. There are three important elements to the federal approach to the ART in addition to tax room. (a) Creating a cost sharing program to encourage provincial involvement; (b) ensuring that adjustments are made to Equalization to reflect the reality that adjustments to provincial revenue capacity or tax effort to make room for the ART do not create Equalization penalties; and, (c) Developing an offset policy based on federal tax room provided to ART that encourages a reduction in AAND oversight and the administrative burden it creates.



Appendix

The table below shows the expected tax revenues per employee from the proposed Kinder Morgan pipeline expansion project in BC. This is an under estimate in that several major taxes such as sales tax induced per worker have been excluded.

Category	Federal	Provincial	Total
Expected Annual Increase in Revenues (Associated with 2-Year TMEP Development)	\$ 322,900,000	\$284,300,000	\$607,200,000
Expected Annual Increase in Revenues (Over 20 Years of TMEP Operation)	\$ 29,333,894	\$19,277,242	\$48,611,136
Expected Annual Increase in Revenues (Associated with Increased Producer Profits Over 20 Years)	\$144,997,343	\$195,113,394	\$340,110,737
Expected Total Annual Increase in Revenues (Development)	\$ 322,900,000	\$284,300,000	\$607,200,000
Expected Total Annual Increase in Revenues (Operations)	\$ 174,331,238	\$214,390,635	\$388,721,873
Annual Fiscal Benefit from Development per Direct/Indirect PYE	\$ 15,283	\$ 13,456	\$ 28,738
Annual Fiscal Benefit from Operations per Direct/Indirect PYE	\$ 95,040	\$ 116,879	\$ 211,918

- Conference board estimates were reduced by the difference between the WCS and Brent spread from November 2013 (publication date) & February 2015 – 52.22% reduction of base case estimates.
- Base case suggests employment of 14,101 PYE direct and 7,028 PYE indirect (21,129 PYE) annually for development and 342 PYE direct and 1,492 PYE indirect (1,834 PYE) annually for operations.
- Revenues only include Corporate Income Tax and Personal Income Tax. Property tax, Indirect Taxes and “Other” Taxes have been excluded.
- Expected increase in revenue from producer profits include corporate income tax (+ royalties for provinces)



Mining Revenues Methodology

A typical mineral mine's technical and feasibility study is used extensively to model government revenue impacts for this study.

Where the technical and feasibility estimates could not accurately model government revenues, economic impact ratios are used. The economic impact multipliers are based on the Mining Association of British Columbia's *Economic Impact Analysis* for government revenues. Economic multipliers for direct and indirect effects of the mining industry were calculated. Multipliers were also further broken down between capital and operating expenditures.

Outward transportation, exploration and development, environmental control, and public interest and other expenditure multipliers are not included in the calculations of government revenue impacts.

Corporate Income Tax

Provincial corporate income tax impacts from the mine are calculated using the provincial revenue multipliers. A provincial revenue impact is first calculated, and then broken down between corporate, income, and sales taxes. Based on Government of British Columbia 2011 Estimates, it was calculated that corporate income represents 12 per cent of the sum of the three taxes.

It was assumed that there would be no direct corporate income tax paid by the mine until after cumulative cash flow (running sum of all operating costs, capital costs, and revenues) was positive. Indirect corporate income tax from other businesses in the region was assumed to be positive from the beginning of construction.

Personal Income Tax

Direct personal income tax was modeled using employment numbers from a typical mineral mine's Technical Report and Feasibility Study. Direct Employment was broken down into two groups, mine employees, and construction employees.

Wages for the mine's process plant manpower requirements and general and administration staff were found in the Technical Report and Feasibility Study. Wages for construction employees were based on a 2009 BC survey of wages under National Occupations



Classifications; 1) trades, 2) transport & equipment operators and 3) related occupations. These wages were inflated to 2012 dollars.

Indirect employment numbers were calculated using economic multiplier ratios for mine employment. Wages are assumed to be the average of mine or construction employees.

Provincial personal income tax was modeled using 2011 tax rates. It was assumed that non-taxable deductions from income would equal 5 per cent of total income. Personal income tax per employee was assumed to increase by 2.5 per cent per year.

Sales Tax

Provincial sales tax impacts from the mine are calculated using the provincial revenue multipliers. A provincial revenue impact is first calculated, and then is broken down between corporate, income and sales taxes. Based on Government of British Columbia Estimates, it was calculated that sales tax represents 44 per cent of the sum of the three taxes.

Mineral Tax

The mineral tax estimate was made using provincial mineral tax rates and extensive use of a typical mineral mine's Technical Report and Feasibility Study's cash flow estimates. The provincial mineral tax is a two part tax, including a Net Current Proceeds Tax and a Net Revenues Tax. A Net Current Proceeds Tax of 2 per cent was applied to cash flow excluding capital until the cumulative cash flow was positive and tax credits were used.

After invested capital is paid for and tax credits are exhausted, a 13 per cent Net Revenues Tax is applied to cash flow including both operating and capital costs.

Mineral Lease

The mineral lease revenue is calculated at \$10 per hectare based on the current lease rate set by the provincial government. The typical mine used is estimated to be 42,636 hectares in size. It was assumed that every 10 years the lease amount would increase by 5 per cent.



Closing the Institutional Gap - The Role of the First Nations Tax Commission (FNTC) in Supporting Taxation and Infrastructure

The **Indian Act** replaced First Nation governing institutions with the Indian Act and the Department of Aboriginal Affairs. The result has been the creation of a large legal, administrative, and institutional gap between First Nations and local and provincial governments. An indicator of this gap are the number of provincial and local laws governing property rights, public services, fiscal relations, land development and environmental management compared to the number governing such matters on First Nation lands.

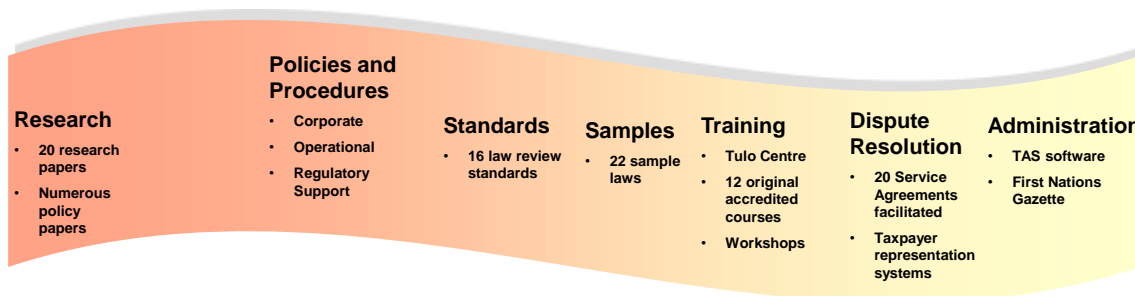
Some First Nations have been working to close this gap by creating legislation and supporting local, regional, and national institutions of First Nations governance. One such institution is the FNTC. It was originally started as the Indian Taxation Advisory Board in 1989 but became the FNTC after the 2005 First Nations Fiscal Management Act (FMA).

The mission of the FNTC is to maximize the benefit of First Nation tax systems to First Nations and their taxpayers. It helps First Nations develop, implement, and administer tax systems that deliver quality services and infrastructure at a fair rate of taxation.

In 1989 it was estimated that only 20 First Nations could establish tax systems. This was wrong. There are now over 170 First Nation tax systems in all provinces and territories except PEI. It is estimated that about \$1 billion in First Nation tax revenues have been generated since 1990. These revenues have been used to provide local services and build a significant amount of community (gyms, government offices, health centers) and economic (roads, water and sewer) infrastructure.

To demonstrate how such an institutional framework could support an aboriginal resource tax it is instructive to review the FNTC. As is illustrated, the FNTC approach is to support First Nation governments using a continuum that begins with quality research. This research informs the design of legislation and regulations and eventually contributes to sound policies and standards which form the basis for laws. Research also informs the curriculum under which the FNTC trains tax administrators. The illustration also summarizes some of the work completed by the FNTC in each element of the continuum.





It is beyond the scope of this paper to discuss all the components of the FNTC and First Nation taxation institutional and regulatory framework but three elements are particularly important:

Standardized regulatory framework – The FNTC provides a series of 16 law review standards for First Nation tax administrations and reviews their tax laws to ensure compliance. The FNTC also provides a series of 22 sample First Nation laws that meet the law review standards for tax enforcement, assessment, expenditure, rates, development cost charges, infrastructure financing and business activity taxes. The result is that the First Nation tax system is highly standardized which reduces transaction costs for investors and improves First Nation credit ratings for potential borrowing. The FNTC also provides the online **First Nations Gazette** which is the largest repository of First Nation laws in the country.

Accredited training and capacity support – Standardization facilitates training and system development. The FNTC has developed the first university accredited certificates in First Nation Tax Administration and First Nation Applied Economics with the Tulo Centre of Indigenous Economics and Thompson Rivers University. There are 12 original courses in these certificate programs which have been taken by over 100 First Nation students and administrative staff. The result has been an increase in tax laws and a greater focus on the fiscal benefits from land development. In addition to these certificate programs the FNTC has developed cloud based tax administration software (TAS) which is used by many First Nation tax systems to collect and enforce their taxes.

Infrastructure planning and financing – The fiscal benefits generated by taxation are amplified when these revenues are re-invested into the development, maintenance, repair, and replacement of business grade infrastructure. This enables further investment which increases tax revenues.



The FNTC supports the process of continuous improvement by supporting infrastructure development and financing. The FNTC is working to increase First Nation revenue options and then provide a framework that supports long term financing and the development of whole infrastructure systems where revenues are set aside to maintain the stock of infrastructure. It is with this in mind, that the FNTC requires infrastructure plans to be integrated with medium term fiscal plans. The FNTC also encourages First Nations to use the full range of infrastructure options that includes borrowing, development cost charges, local improvement taxes, property taxes, business activity taxes and joint development with adjacent communities using comprehensive service agreements.

