

# **Building a Competitive First Nation Investment Climate**

**Tulo Centre of Indigenous Economics**



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## FOREWARD

BY CHIEF MICHAEL LÉBOURDAIS,  
CHAIR OF THE TULO CENTRE OF  
INDIGENOUS ECONOMICS

**I** am the Chief of the Whispering Pine/Clinton Indian Band. We are a small community. Most of our members live on a reserve just north of Kamloops, BC. We were moved there in the 1970s to make way for a hydro project.

We are a young and entrepreneurial community. More than 60% of our population is less than 25. Our members include ranchers, tradespeople, nurses and engineers.

They have the same dreams as other young people – to receive primary and secondary education at the same standard as other residents of Canada and the United States, to have post-secondary opportunities to acquire skills and education, to find meaningful employment, to live in a healthy safe community, to raise a family, to own their own home and retire comfortably.

I became a chief to help realize the dreams of our youth helping to create economic opportunities. I recognize the barriers they face on our lands.

They do not have the same access to capital or equity in their homes, as they would off our lands. They don't have the same quality of roads, water and environmental infrastructure, as they would off our lands. It

takes 4 to 6 times longer to complete an investment transaction on our lands than off because we are missing the laws, procedures, access to financing, infrastructure and administrative capacity that exists off our lands.

I appreciate the challenges our youth face on a personal level. I come from the First Nations Brady Bunch. When my mother and father were married, they each brought three children into the relationship. The larger family meant my father had to build another house beside the one he already had.

My father had a ranch and two houses but when he went into a bank in the 1980s and applied for a credit card (so he could rent a car and reserve a hotel, like any other Canadian), he was turned down; because he was told he didn't have any collateral.

His two houses and his ranch were insufficient collateral because in Canada the *Indian Act* states that an Indian reserve is "a tract of land, the legal title to which is vested in Her Majesty". We don't even own our own lands. We don't have the legal and administrative framework to make our lands valuable. We don't have sufficient secure independent revenue streams to build competitive infrastructure and provide quality services. In short, we do not have the necessary investment climate to meet our community objectives.

This is why I am the chair of the Tulo Centre of Indigenous Economics. Our purpose is to help tribes and First Nations fill these gaps preventing us from participating in the economy. Our purpose is to provide the knowledge and skills to develop our laws, establish our property rights, generate independent revenues to build infrastructure and lower the costs of doing business on our lands. We want to learn from and share our successes.

This is why we have created this open electronic textbook. It is available for all interested students. It compiles all the knowledge we have gathered so far about building a successful First Nation and tribal investment climate.

I hope it is helpful to you. I hope you can contribute your successes to this textbook to expand our knowledge. Most of all I hope it helps restore the values that federal legislation like the *Indian Act* took away.

### **What is the Tulo Centre of Indigenous Economics?**

The Tulo Centre of Indigenous Economics (Tulo Centre) is a not-for-profit institution, based in Kamloops, British Columbia, whose mission is to help interested indigenous governments build legal, administrative, and infrastructure frameworks that support markets on their lands. Tulo is the Chinook word for “earned profit”. Chinook was an aboriginal trading language used between Alaska and California, and profits were earned by innovating to best serve trading partners in indigenous markets.

The Chair of the Tulo Centre is Chief Michael LeBourdais from the Whispering Pines/Clinton Indian Band. The other Board Members are Bud Smith (former Attorney General of British Columbia) and Dr. Robert Bish (Professor Emeritus, Economics and Public Administration, University of Victoria). The Director of the Tulo Centre is Andre Le Dressay (an adjunct Professor of Economics at Thompson Rivers University) and the administrator is Sarah Jules. The Tulo Centre was founded by Clarence T. (Manny) Jules, the Chief Commissioner of the First Nations Tax Commission.

### **What is the Tulo Centre’s philosophy?**

The engine of economic growth is private investment. Investment can be generated from local residents through savings, through home equity or from outside sources. In Canada, private sector investment outweighs public sector investment by five to one.<sup>1</sup> Three times as many jobs are created in the private sector as in the public sector.<sup>2</sup> Attracting private investment is thus the key to economic growth.

The role of investment in building First Nation economies is direct; markets are the basis for economic prosperity. The critical components of markets include well-defined systems of law that create certainty for property rights, provide an environment for entering into and enforcing

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<sup>1</sup> Statistics Canada. (2011). Table 032-0001 Public and private investment, summary by sector, annual (dollars x 1,000,000). Data from 2000 to 2009. Online at <http://estat.statcan.gc.ca/>.

<sup>2</sup> Statistics Canada. (2011) Table 282-0012 Labour force survey estimates (LFS), employment by class of worker, North American Industry Classification System (NAICS) and sex, annual (persons x 1,000). Data from 2000 to 2010. Online at <http://estat.statcan.gc.ca/>.

contracts and allow individuals to pursue their own interests with success. Ultimately, investment creates jobs and business opportunities. This, in turn, builds the fiscal capacity of governments to support social improvements and build infrastructure. It also encourages a natural constituency for accountable, fiscally responsible government as the investment climate is enhanced.

Indigenous governments must participate in federations and market systems to provide fiscal and economic opportunities for their governments and members. Although First Nations were largely legislated out of the economy, during the past twenty-five years this exclusion has begun to change. While First Nations are not fully recognized as constitutionally entrenched entities within the Canadian federal system, there are recent Supreme Court decisions, treaties and legislation that integrate their role in the federal system and provide a basis for supporting markets on their lands. Some of the important pieces of legislation that directly facilitate market-oriented development include the *Kamloops Amendment to the Indian Act (1988)*, the *First Nations Land Management Act (1999)* and the *First Nations Fiscal Management Act (2005)*. This legislation has begun enabling First Nation participation in the market with over 200 First Nations implementing control over the taxing and servicing of their lands but there remains much to be done. The Tulo Centre was established to further these efforts and help First Nations maximize the benefits from legislation and institutions so they can participate in the Canadian federation and economy.

### **Which five premises inform the Tulo Centre's mission?**

1. An important cause of First Nation economic underdevelopment is that the costs of doing business on many First Nation lands are significantly higher than they are off First Nation lands. This reduces private investment and contributes to disparities between First Nations and other Canadians.
2. These high costs of doing business are mainly a result of First Nations not being able to develop the legal and administrative frameworks and the necessary infrastructure to support markets because the *Indian Act* has effectively frozen First Nation institutional development for the last 140 years.
3. Recent legislation such as the *First Nations Fiscal Management Act*,



the *First Nations Land Management Act*, the *First Nations Commercial and Industrial Development Act (2005)* and the proposed *First Nation Property Ownership Act* provide an opportunity for First Nations to create competitive markets on their lands, generate economic growth, build infrastructure, increase confidence in their governments and raise their own revenues to achieve their community objectives.

4. There is a demand from First Nations and indigenous groups for practical training and accredited education on how to realize the economic benefits from recent legislation.
5. There is a demand from the private sector to work more closely with First Nations and indigenous groups on economic opportunities (e.g. in the resource sector).

### **What is the context for this text?**

In 1975, a meeting was held at Chilliwack, British Columbia, Canada by the Union of British Columbia Indian Chiefs, which at the time represented all First Nation communities in the province. The purpose of the meeting was to restore First Nation independence and reject government funds. The First Nations who attended did not want the *Indian Act* to apply to their lands and they did not want the Department of Indian Affairs to administer the *Indian Act* on their lands. They felt that getting rid of the *Indian Act* was the best way to reduce their poverty. A number of prominent Indian leaders at the time, including Phillip Joe, Forrest Walkem, and Don Moses, spoke. One particular speaker, Willis Morgan representing the Kitamaat Indian Band, cautioned that First Nations were not ready for this because they lacked the economic base and tax systems to pay for local services, education, health, and welfare.<sup>3</sup> Morgan's caution was ignored, and First Nations throughout BC rejected government funding in the late spring of 1975. By the fall of 1975, Willis Morgan was proved right. First Nations had neither the capacity to deliver local or other services, nor the jurisdiction or systems to collect revenues, nor the infrastructure to attract investment. Within six months, most communities began accepting government funding again.

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<sup>3</sup> Union of British Columbia Indian Chiefs, 7th Annual General Assembly, DVD Format, (1975).

At this time, two First Nation strategies emerged to achieve the 1975 Chilliwack objective. The first was a political and legal strategy to achieve the constitutional recognition of the rights and responsibilities of First Nation governments and individuals. The second was an economic strategy to incrementally legislate and implement the jurisdictions and systems related to taxes, lands, property rights and service provision needed to support First Nation participation in the market economy.

The two strategies are complementary. The political and legal strategy is well covered in: *Law and Aboriginal Peoples in Canada* (Elliot, 2005), *Aboriginal Legal Issues: Cases, Materials and Commentary* (Borrows & Rotman, 2007), *Aboriginal Law Handbook* (Olthius, Kler & Townshend, 2008) and *Canada's Indigenous Constitution* (Borrows, 2010) and is taught in programs such as the Aboriginal Law Program at the University of Toronto, the Program of Legal Studies for Native People at the Native Law Centre (University of Saskatchewan) and the Indigenous Legal Studies Program at the University of British Columbia. However, there are no texts on the economic strategy. The purpose of this text is to fill that gap.

### **Who is the audience for this text?**

This textbook is for students who are First Nation and tribal government employees or students who would like to work for or with First Nation and tribal governments. The purpose of this textbook is to help interested First Nation and tribal governments build a competitive investment climate. Following from the premises that inform the Tulo Centre's mission, the main premise of the textbook is that the costs of doing business on First Nation and tribal land are too high because the public sector component of the First Nation and tribal investment climate is not competitive within their regional economies. The secondary premise of this book is that some First Nation and tribal governments are interested in establishing a competitive investment climate. The objective of the textbook is to develop the skills for students to build successful First Nation and tribal investment climates, recognizing that many of the elements of a successful investment climate have regional variations. There is a link between the text and the courses offered by the Tulo Centre. Many of the elements of this textbook are drawn from APEC 2640 – *Commercial and Residential Developments on First Nations*

*Lands and APEC 2650 – Facilitating Private Investment on First Nation Lands.* The efforts of the Tulo Centre, including this text, are devoted to enhancing economic opportunities for indigenous governments and their members by enabling them to join and reap the benefits of participating in the federal and market systems.



CHAPTER 1

# INTRODUCING INSTITUTIONAL AND INDIGENOUS ECONOMICS

**I**n 2010, C.T. (Manny) Jules wrote a forward to *Beyond the Indian Act: Restoring Aboriginal Property Rights*.<sup>4</sup> A truncated version of that foreword sets the context in this chapter:

*In the fall of 1997, I travelled to eastern Mexico. It was the first time I had been there. The reason I had was to visit Chichen Itza where every year during the spring and fall equinox the sun casts a shadow, which resembles a snake descending to the ground. The shadow joins up perfectly with the carved stone snakes head at the base of the pyramid. The pyramids, monuments and other public*

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<sup>4</sup> Flanagan, Tom, Christopher Alcantara, and Andre Le Dressay. 2010. *Beyond the Indian Act: Restoring Aboriginal Property Rights*. McGill-Queen's University Press.

*infrastructure at Chichen Itza were built around 600 AD or 1500 years ago. As I stared, I had an epiphany. Our people built this without the aid of federal government funding. We had governments that financed themselves. Our governments were able to provide the infrastructure and institutions to build a thriving economy that supported millions of us ....*

*Market economies were not foreign to us. We created them ourselves. We traded goods over hundreds of miles. The Mayan had a complex trade network. How could pipestone, dating back to before contact end up in my territory in South Central British Columbia when it only comes from a few places such as Pipestone, Minnesota if we did not trade? How could corn be used all throughout the Americas before contact, if we did not trade?*

*Trade cannot be financed without capital. We had to build transportation methods such as boats. We had to build large public buildings and maintain armies to provide order. These required community investments based on a future return to the community and to individuals. Markets need institutions to facilitate trade. From Alaska to California, we agreed to a common trade language, Chinook. We recorded transactions relating to labour and goods. We build roads and trails that are still being used today. We used money such as dentalium shells and wampum strings. We had individual property rights. Our clothes and shoes were not made to fit everyone. Our winter homes belonged to certain families. If you came into my home before contact, you definitely would have learned who owned it. According to our written history, my community had individual property*

*rights dating back to the early 1800s to specify where our potato crops were.*

*Do you think this was all achieved through divine intervention from the Gods? Or was it because we somehow created a socialist system that lasted thousands of years? Both of these ideas are nonsense. We achieved success because we created balance between our individual creativity and our collective responsibility. We created systems that supported and encouraged individual initiative and ensured we generated public resources to sustain our communities and advance our cultures.*

### **What two questions does this chapter address?**

This chapter asks: What are the major institutional elements that are required to support a market economy; and Are there examples of pre- or early-contact indigenous market institutions? These two questions will be answered by discussing seven factors: the market, specialization in peoples and trade, rule of law, infrastructure, property rights, mediums of exchange, and taxation. The seven factors are illustrated by indigenous groups' activities in the past and related to First Nations and tribes in the modern context.

### **What is a market?**

There is a widespread consensus across a broad economic spectrum as to what constitutes a market; from Adam Smith's *The Wealth of Nations* to Karl Marx's *Das Kapital* to Milton Friedman's *Free to Choose* to Alfred Marshall's *First Principles of Economics*. For our purposes, a market exists where voluntary exchange between a buyer and a seller takes place and this exchange is facilitated by informal or formal rules and infrastructure.

Markets are social institutions. They facilitate and support voluntary exchanges between parties. These exchanges are voluntary because for them to occur, both parties have to derive a benefit. Therefore, there is an incentive for trade. If both parties do not anticipate some benefit from trade, the trade would not occur. That is, the market neither foists nor

thwarts. This explains the pervasiveness of markets as social institutions throughout time and space. They exist everywhere because there are mutual gains from voluntary trade.

In most transactions, the buyer does not know the seller. Strangers can interact because markets (and their supporting institutions) support them. Thus, institutions that allow transactions are a beneficial.

### **What are the characteristics of markets?**

The foundation to support market-driven economic growth was first articulated by Adam Smith in *An Inquiry into the Nature and Causes of The Wealth of Nations* (1776). Smith was neither anti-government nor pro-business; he granted government some important regulatory roles and believed businesses preferred to be monopolists. Throughout, Smith was pro-consumer, believing that citizens should have choices as to where to shop and how to earn their incomes. To Smith, the two most important market characteristics were specialization and trade, both of which are predominantly private sector characteristics.

1. *Specialization*: When workers specialize in what they produce, they innovate (i.e. they think of new and more productive ways to produce).
2. *Trade*: If workers are to specialize, they must be able to trade. At a fundamental level, even farmers must trade for tools to work their farms and coal to heat their houses.

These two characteristics lead to higher productivity if there is a market for exchanging what one produced for what one did not produce. The key limit on specialization is the size of the market, the larger the market, the greater the opportunity for specialization. This is why Smith believed transportation by water was important; it reduces the cost of trading over a large area. This enlarges the market, which leads to specialization, more innovation and higher productivity – the process of economic growth.

Production is critical to specialization and trade. Almost everything that is produced requires physical and human capital, ranging from land and buildings to machinery to the people who design, build, and operate machinery and software. It is difficult to accumulate physical capital without property rights and a good banking and financial system.

Individuals who need to be able to organize production and to think about how to be more productive undertake production, innovation and trade. This is human capital.

**What market characteristics does government generally provide?**

Markets are not just private phenomena. They also need governments because government provides the legal and administrative framework to support trade and reduce the costs of buying and selling. Governments educate so that individuals can innovate and produce. When governments get this institutional framework right, market transactions increase which, subsequently, creates growth and prosperity. When governments get this institutional framework wrong, markets can fail leading to recession and poverty. There are four characteristics that are generally maintained by the public sector:

1. *Standards and the Rule of Law*: Producers and traders need certainty in the legal framework. They need to know that contracts can be enforced. They require honest, reliable and timely courts to resolve disputes.
2. *Public Infrastructure*: Public infrastructure (e.g. local roads, water systems and sewer systems) are important to facilitate health and trade. Urban areas with public infrastructure often have higher rates of economic growth because of their larger markets, which facilitate increased specialization and innovation.<sup>5</sup>
3. *Property Rights*: Private property, protected by government and law, provides the foundation for trade. There are two different kinds of governments, inclusive and extractive. Inclusive governments are characterized by democracy with broad

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<sup>5</sup> Smith, Adam. 1909. *Wealth of Nations*. Harvard Classics, Vol. 10. New York: P.F. Collier & Son Company. Available at <http://www.bartleby.com/10/>; Duranton, Gilles, Peter M. Morrow, and Matthew Turner. 2013. *Roads and Trade: Evidence from the US*. Forthcoming in *Review of Economic Studies*. Available at [http://homes.chass.utoronto.ca/~mturner/papers/unpublished/Duranton\\_Morrow\\_Turner\\_RES\\_2014.pdf](http://homes.chass.utoronto.ca/~mturner/papers/unpublished/Duranton_Morrow_Turner_RES_2014.pdf).



participation and protected private property rights.<sup>6</sup> Elites who offer little protection of private property rights and run the government for their own benefit dominate extractive governments.

4. *Money and Banking*: Traders need money to facilitate transactions. Barter is simply too inefficient for economic activity on any significant scale. Banking has two critical functions. First, it facilitates transactions (e.g. paying by cheque) so that a merchant who receives payment in one place can cash it in another. Second, it allows banks to collect small amounts from many savers and then lend those funds to investors who wish to purchase capital equipment to engage in production. There also needs to be financing institutions to facilitate arrangements for financing capital. Banks now extend lending secured by home mortgages so people can own their home and use it as security for a loan to start a business.

The six factors (specialization, trade, standards and rule of law, public infrastructure, property rights, and money and banking) are linked and multi-dependent. For instance, money, banking and finance are also dependent on the rule of law, especially property rights as a source of security for a loan and courts for enforcement of agreements. Institutions that support markets are the most important determinants of economic development.

### **What is specialization in an indigenous context?**

Specialization can result from using an advantage in resources, labour, location or an innovation. Because of trade, it is not necessary for each society or group to produce all their requirements. Instead, each society or group will specialize in the production and export of those goods and services in which they have a comparative advantage. They will create a surplus from this specialization and trade with others who have developed specialization in other goods and services. Specialization is a

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<sup>6</sup> Acemoglu, Daron, and James A Robinson. 2012. *Why Nations Fail: The Origins of Power, Prosperity, and Poverty*. New York: Crown Publishers. Learn more at <http://whynationsfail.com/>.

function of comparative advantage.

For example, Canada and China frequently trade with one another. About 80% of Canada's export shipments to China are resource products (mostly industrial materials and forestry products).<sup>7</sup> This is because Canada has stuff - a comparative advantage in resources as a result of natural endowments. From China, Canada receives machinery, electronic equipment and consumer goods. China has developed an advantage in the production of these goods and has acquired a comparative advantage in their production - due to relatively low labour costs. This is because China has people.

Consequently, exports have risen for both countries as the income levels of both countries have increased. Such free trade allows both countries to become better off than they would have been if they isolated themselves and produced the traded goods on their own. By trading, both countries concentrate on developing efficiencies in producing their specialty. Free trade agreements are put in place when two or more countries reach a consensus on the standards and taxes they will use to facilitate more trade.

Refer to this Chapter's Appendix for a hypothetical example of comparative advantage for two First Nation groups in Canada.

### **To what extent did indigenous people specialize pre-contact?**

Many indigenous groups understood specialization and comparative advantage pre-contact found in the following table of Historical Specialization Examples.<sup>8</sup>

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<sup>7</sup> Roy, Francine. 2004. *Insights on the Canadian Economy: Canada's Trade with China*. Micro-economics Analysis Division: Statistics Canada. Available at <http://dsp-psd.tpsgc.gc.ca/Collection/Statcan/11-624-M/11-624-MIE2004007.pdf>.

<sup>8</sup> See Teit, J. & Franz Boas. 1900-1909. *Memoirs of the American Museum of National History* Collection. Available at <http://digitallibrary.amnh.org/dspace/>; Fortier, J.M. 2003. *Ojibway History*. Available at <http://turtle-island.com/ojibway.html>; Ignace, Ron. 2008. *Oral Histories are our Iron Posts: Secwepemc Stories and Historical Consciousness*. Dissertation: Simon Fraser University – Department of Sociology and Anthropology; Manataka: American Indian Council. 2007. *Algonquin History*. Available at <http://www.manataka.org/page386.html>; Royal Commission on Aboriginal Peoples. 1996. *Report of the Royal Commission on Aboriginal Peoples*. Available at [http://www.ainc-inac.gc.ca/ch/rcap/sg/sgmm\\_e.html](http://www.ainc-inac.gc.ca/ch/rcap/sg/sgmm_e.html); UCLA Language Materials Project. *Ojibwe*. Available at <http://www.lmp.ucla.edu/Profile.aspx?menu=004&LangID=197>;

<i>Historical Specialization Examples</i>	
Indigenous Group	Example of Specialization and Comparative Advantage
Algonquian: Eastern and Woodland (Piegan)	Hunting and trading
Assiniboine	Skin preparation
Beothuk	Fishing (seal hunting, fishing and shellfish collection)
Blackfoot	Elk-antler bow production
Chipewyan	Ice fishing, agriculture (wheat)
Coast Salish	Iron extraction
Copper Eskimos	Copper (and soapstone) extraction
Haida	Tobacco farming
Haisla	Eulachon fishing and oil production
Huron	Agriculture
Kutenai	Horse trading
Kwakiutl	Wood-working/iron and metal extraction
Lillooet (Lower Division)	Orchard development
Nisga'a	Eulachon fishing services
Nootka	Whaling and seal/otter hunting
Ojibwa	Hunting and trapping (beaver)
Petun	Tobacco farming
Potawatomi	Agriculture
Sarsi	Beaver hunting, agriculture (wheat)
Shuswap (Cañon Division)	Salmon fishing, trading, and oil preparation
Shuswap (Fraser River and Lake People)	Iron extraction, cedar-root basket production
Skolahun	Fish-weir production
Thompson	Cedar canoe production, agriculture (wheat)
Tlingit	Copper extraction
Tsimshian	Abalone-shell accumulation
Western Woods Cree	Pemmican production

These few examples show that indigenous peoples were active pre-contact traders. They recognized their comparative advantages and organized their economic systems around these specialties. It is worth

noting that some of these pre-contact advantages related to technology (canoe, baskets, pemmican), others related to access to resources (fishing, whaling, iron, and hunting) and others to location (trade and agriculture). In the modern context, a number of First Nations and tribes currently have comparative advantages because of their location and access to resources.<sup>9</sup> However, such comparative advantages in location, resources or labour will not be realized without trade. Seizing trade opportunities makes their communities more economically self-reliant.

### **What were some indigenous trade networks?**

Economic benefits from specialization arise when an individual, group or country sells their product or service to people outside their region or country. These are exports. The benefits accrue to the exporter because the costs of production and transportation are lower than the price received. These are the producers' profits. An increase in exports is a principal driver of economic growth. Indigenous pre-contact trade networks indicate social connections to other trading nations. They indicate that trading partners appreciated and realized the mutual gains from trade. There are numerous examples of indigenous bilateral and trading networks:

- *Mayan trade network*<sup>10</sup> – Trade between two divisions of the Mayans (who occupied present-day Guatemala, Belize, El Salvador, Honduras, and parts of Mexico) is well documented. Trade between the Northern Lowlands and the Highlands was well established via water routes on the Gulf of Mexico and the Gulf of Honduras as well as various inland routes. The Northern Lowlands Maya imported

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<sup>9</sup> To list a few examples, consider the demand for commercial and residential development in Canada on Squamish, the Stó:lō Nation communities, Penticton, Lower Kootenay, Tsuu T'ina, Enoch Cree Nation, Whitecap Dakota Sioux, Mosquito, the Brokenhead Ojibway, Kettle and Stoney Point, the Huron Wendake, and Millbrook. Consider also the demand for resource partnerships with Yukon First Nations, the Inuvialuit, Fort McKay and Treaty 3 First Nations. This short list demonstrates that there is a strong opportunity for First Nations and tribes to specialize in a comparative advantage.

<sup>10</sup> For more information see Adams, R.E.W. 2005. *Prehistoric Mesoamerica: 3rd Edition*. University of Oklahoma Press.; Mann, A.J. 1973. *The Economic Organization of the Ancient Maya*. The Americas, Vol. 30, No. 2, pp. 209-228; and Fowler, W.R. 2007. *Maya Civilization*. Microsoft Encarta Online Encyclopedia: Vanderbilt University. Available at <http://encarta.msn.com>.

corn, fruit, cacao, flint, game, cotton, cloth, obsidian, metates, manos and various manufactured goods. The Highland Maya imported honey, salt, ceramics, various tools, salted fish, marine shells, dye, incense, jade, and rubber.

- *Pipestone network in North America*<sup>11</sup> – Pipestone is a soft stone that was used to manufacture Aboriginal smoking pipes, used in most ceremonies with indigenous people in the upper Midwest (e.g. to ratify treaties and various agreements). The only known pre-contact mine for pipestone can be found at what is now known as Pipestone National Monument in Minnesota. The pipes that were manufactured were of religious importance and were widely traded. Several archeological surveys have found pipestone artifacts in South Dakota, Ohio and Kansas. Distribution then expanded owing to the use of waterways, the introduction of the horse and the increased number of indigenous people quarrying pipestone.
- *Secwepemc – Tsilhqot'in trading*<sup>12</sup> – A division of the Secwepemc Nation, the Cañon division, specialized in salmon fishing, preparing oil and trading. Trade occurred with the Tsilhqot'in (Chilcotin) Nation because they were proficient hunters and trappers.
- *Internal Secwepemc Trade*<sup>13</sup> – Cedar-roots were used frequently by the Lake division of the Secwepemc Nation, who gathered the roots in the mountainous regions to manufacture baskets. As cedar was scarce elsewhere, most baskets were woven of lesser quality spruce-root. The Lake division traded the superior baskets to divisions such as the Kamloops and Bonaparte for various animal furs, salmon, and game (seasonal food).

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<sup>11</sup> For more information see Rothman, H.K. 1992. *Managing the Sacred and the Secular: An Administrative History of Pipestone National Monument*. U.S. National Park Service, Midwest Region. Available at [http://www.nps.gov/history/history/online\\_books/pipe/adhi.htm](http://www.nps.gov/history/history/online_books/pipe/adhi.htm).

<sup>12</sup> For more information see Teit, James & Franz Boas. 1909. *The Jesup North Pacific Expedition: The Shuswap*.

Memoirs of the American Museum of Natural History, Volume II, Part VII. New York: Leiden, E.J. Brill Ltd. Available at <http://hdl.handle.net/2246/38>.

<sup>13</sup> For more information see Teit & Boas, 1909.

- *Nootka – Kwakiutl trading*<sup>14</sup> – The Nootka specialized in whaling. Whales yielded a number of tradable food products including blubber, flesh and oil. Their primary trade partners were the Kwakiutl, who were located northeast of the Nootka on present-day Vancouver Island. The Kwakiutl traded knives, chisels, nails, buttons, iron, and any kind of metal (their land provided these types of resources and they obtained some from trade with the Coast Salish) as well as carved works, spears, fish hooks and other such implements.

### **What of current trade networks?**

Trade networks are now global and they involve goods, services, capital and labour. Modern tribal and First Nation trade networks require being open to imported goods and services so that tribes and First Nations can export their goods and services. Tribal and First Nation trade networks involve importing labour expertise as required and exporting tribal and First Nation labour where a demand exists for it. A number of tribes and First Nations have already demonstrated the benefits of open markets.

To cite a few examples: property values have risen from \$8,000 per acre in 1995 to \$750,000 per acre in 2007 on the Sun Rivers development on the Kamloops reserve in British Columbia, and from \$10,000 per acre in 1990 to \$1,000,000 per acre in 2007 on the Westbank First Nations land near West Kelowna, British Columbia. This represents a 100-fold increase in value. Other properties in the area at best rose by a factor of four during this time. These First Nations used their comparative location advantages, created a competitive investment climate and welcomed new investors to their lands. Likewise, a number of First Nations throughout Canada are reaching accommodation agreements with industry and resource developers on their traditional territories. They recognize that by being open to trade within their treaty or traditional areas, their communities will benefit from increased employment, incomes, better services and reduced poverty.

In the United States, the Southern Ute tribe has been successfully developing its energy resources for decades. Located within an extensive

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<sup>14</sup> For more information see Northwestern University Library. 2003. *Edward S. Curtis's: The North American Indian*. Available at <http://digital.library.northwestern.edu/curtis>.

oil and gas basin, the tribe has developed a stellar reputation for energy management and other business activity. Outside companies as well as tribal-owned energy companies extract oil and gas resources. Several of its tribal-owned energy companies are even engaged in oil and natural gas production beyond the reservation's boundaries. Red Willow Production Co., for instance, operates energy leases in the Gulf of Mexico. By developing skills in resource development, and by engaging in trades for those skills and resources, the tribe has experienced widespread economic growth.<sup>15</sup>

### **What are examples of indigenous legal frameworks that support markets?**

Markets, more specifically trade, require rules, certainty and dispute-resolution mechanisms. The absence of such a regulatory framework requires traders to negotiate the rules and certainty for each trade. This raises the costs associated with facilitating a trade of goods or services. To put this in perspective, imagine if there was no agreement on the quantum (size) of one gram and you wished to purchase a box of cereal sold in grams. The costs associated with buying cereal would be high because you could not be sure how much cereal you were getting. Efficient trade requires standards, laws, and in some cases a trading language. A legal and administrative framework that is reliable and promotes standards reduces transaction costs for producers, exporters and importers and, as a result, increases trade. Modern free trade on First Nation and tribal lands is hampered because there is an absence of standards and a stable rule of law. The rules relating to construction, development processes, land use, environmental matters, business activities, and taxation are either different between First Nations and tribes within the same region or non-existent. They are also different from those of adjacent jurisdictions such as municipalities whereby having similar land use regulations that are familiar to developers make them more willing to invest on First Nation lands.

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<sup>15</sup> Grogan, Maura. 2011. *Native American Lands and Natural Resource Development*. Revenue Watch Institute.

### **How about that Aztec Commercial Code?**

There is evidence that indigenous people understood the importance of the rule of law and standards. Consider the Aztec commercial law system, which was enforced by a group known as the *Pochteca*.<sup>16</sup> The *Pochteca* were a group of Aztec merchants who paid tax to the Aztec government for the ability to regulate the marketplace, judge all lawsuits relating to the merchant class and punish those who violated their laws. Regulations applied to Aztec markets including restricting trade outside of the markets for fear of offending the market gods and restricting the sale of goods outside the designated market areas assigned by a *Pochteca* market judge. In addition, those who sold their goods inside the market areas were required to pay a market tax to the *Pochteca*. Inspectors mixed in the crowd to protect consumers (e.g. to ensure that items were being sold at proper exchange rates, that goods were of a certain standard and that they were not counterfeit). If identified, counterfeit items were confiscated. If there were evidence of false measures, inspectors would destroy the items of that merchant.

The *Pochteca* also established the legal jurisdiction of contracts within the Aztec commercial law system and commercial court. They recognized the importance of different types of contracts: for sales, commissions, leases, work and loans. All contracts were created orally and became binding when witnessed by four people. Collateral for the contracts was in the form of goods, property or a promise to become a slave upon default. The *Pochteca* enforced contracts through their market courts. Market inspectors brought those who broke the law to court before a panel of judges for judgment and sentencing. These courts governed all contract disputes between traders as well as any issue that arose in the marketplace or was related to a *Pochteca* member. Those who were convicted of crimes were fined, and families were charged with the payment of those fines. Restitution was common in theft (minor), fraud or personal injury cases. In some cases, the offender was made the slave of the victim. Moreover, as an example to others, serious offenders were beaten to death in the centre of the marketplace.

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<sup>16</sup> See Andrade, Dale F. 2004. *The Aztec Legal System*. School of Law: Santa Clara University and Avalos, Francisco. 1994. *An Overview of the Legal System of the Aztec Empire*. Lexis Nexis.



Of course, harsh legal punishments of this type are cruel, but they underscore the importance of the rule of law in lowering transaction costs and encouraging market exchange.

### **What are examples of indigenous public infrastructure?**

Trade requires infrastructure to support transportation, communications and public health. Without this infrastructure, the costs of trade are higher. Unfortunately, a private sector provider cannot generally capture the benefits from this infrastructure so infrastructure provision is usually a public function. When infrastructure is poor, trade is hampered.

Much of the recent legislation in Canada and the United States related to First Nation and tribal taxation, property rights, land management and competitive infrastructure aims to reduce market transaction costs on First Nation and tribal lands.<sup>17</sup> Today, First Nations and tribes cannot attract investment to their lands or participate in resource development opportunities without business-grade water, sewer, hydro, communications and transportation systems. Infrastructure is financed by a combination of local revenues (including taxation), reserve funds, debentures and contributions from other governments.

*Oolichan Grease Trails:* Oolichan is a type of ocean smelt found along the Pacific coast of North America from northern California to Alaska. First Nations, such as the Haisla Nation and the Nisga'a Nation, caught this fish and extracted oolichan grease (or oolichan oil). This grease/oil was used as salve, sauce, seasoning, food preservative, laxative, lamp oil and leather-tanner. The oolichan grease was a source of vitamins A, C and E, and was used as medicine to treat colds and flu. According to Fisheries and Oceans Canada, "one box of grease could be bartered for four blankets, two beaver skins, or two boxes of dried halibut... [Two

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<sup>17</sup> During the 1980s and 1990s, as constitutional debates involving First Nations were pervasive in Canada, a group of First Nations began to fight behind the scenes for incremental federal legislation giving them power over taxes, lands, and local services. This incremental legislation includes the 1988 *Indian Act* amendment (property tax), FNST and FNGST (1997 & 2003), First Nation Land Management Act (1999), First Nations Fiscal Management Act (2005) and First Nations Commercial and Industrial Development Act (2005).

boxes] of grease had the value of one canoe.”<sup>18</sup>

The grease was so highly valued by western First Nations that a comprehensive network of oolichan grease trails accommodated trade between coastal and inland Nations, across Vancouver Island, from Yukon to northern California, and east to central Montana and Alberta. Horses were not available to support trade until the late 1700s, so the grease was slung on the backs of individuals wishing to trade it. The grease trails were usually the easiest routes across plateaus, highlands and over mountains. Between 1821 and 1846, the grease trails were converted into fur trails as the demand for fur increased.

*Upper Missouri Trade Networks:* By the mid-eighteenth century, the villages of the Mandans, Hidatsas, and Arikaras in the upper Missouri River had become extensive trading centers for a wide variety of items. Foods such as corn, beans, and squash from farming villages were exchanged for dried meats and hides. Eventually, European goods, such as horses and guns, were exchanged. As historian James Ronda points out, “a great circle of hands” made up this trading network<sup>19</sup>, which extended in all directions of the continent through the hands of various tribes.

To appreciate the extent of the North American trading networks, consider how far and how fast items crossed the continent. When the Lewis and Clark expedition reached the Mandan villages in 1804, the men of the expedition crafted war hatchets. By the time the expedition made it farther westward, one of the hatchets was already in the hands of indigenous people in Idaho. The expedition also saw Spanish horse gear in the upper Missouri and British teapots on the Columbia—a testament to how far and wide indigenous trading networks reached.<sup>20</sup>

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<sup>18</sup> Government of Canada – Fisheries and Oceans Canada. 2013. *Eulachon Fishery Overview – Pacific Region*. Available at <http://www.pac.dfo-mpo.gc.ca/fm-gp/commercial/pelagic-pelagique/eulachon-eulakane/overview-apercu-eng.html>.

<sup>19</sup> Callaway, C.G. 2003. *One Vast Winter Count: The Native American West Before Lewis and Clark*. Nebraska: University of Nebraska Press.

<sup>20</sup> Ibid.

*Norte Chico:* The Norte Chico or Caral-Supe Civilization of north-central Peru is the oldest known civilization in the Americas and represents one of the first instances of modern government in the world. Given that there are no real governments without taxation, it is possible the concept of taxation was invented in the Americas.<sup>21</sup> Their public infrastructure supported trade in cotton and seafood.

*Incan Roads:* The Inca road system was one of the most extensive road/trail systems created in South America before the arrival of Columbus. As the Inca did not use wheeled vehicles or horses, the roads were essentially dirt paths, with some stone-paved sections. In some areas, suspension bridges were built over ravines and bodies of water. The trails were intended to be travelled by foot with llamas used to pack goods.

*Mayan Warehouse:* The Mayan people built public infrastructure such as warehouses, trade routes (some roads made of stone) and rest houses for goods carriers in order to facilitate trade and generate wealth. The scale of Mayan public infrastructure supports theories of centralized government and taxation (tribute).

### **To what extent did indigenous property rights exist?**

A property right is the ability to exercise a decision about a good, service or labour. This means that trade is an exchange of property rights. Without property rights individuals have no incentive to engage in trade because they cannot be sure of their rights of use as a purchaser or their rights of profit as a seller. Governments must provide and protect property rights to ensure there is sufficient individual incentive to engage in trade. In addition, property rights allow individuals to make profitable contracts with others, provide incentives to encourage conservation or resource maintenance, and allow for enough certainty of ownership that individuals can transfer rights to resources through trade.

Indigenous property rights have always existed. Many rules governing property rights were created in agreement with customs,

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<sup>21</sup> Mann, Charles C. 2006. *1491: New Revelations of the Americas Before Columbus*. New York: Vintage Books.

culture and resource scarcity. Property rights did not exist everywhere; they were created only where and when individuals could capture economic gains by going to the effort of defining and enforcing property rights. They developed in small group settings where each member benefited from institutions that reduced the costs associated with trading and prevented resource values from being dissipated. Property rights were thus created because of incentives to protect resources.

Personal property was most often privately owned because it required a significant amount of time to produce and maintain. Clothes, weapons, utensils and housing were often the property of those who made them. A specific tipi, for example, was owned by an individual or a group who collected, tanned, scraped and sewed the hides. Bows, arrows and arrowheads were also privately owned because of the considerable amount of time they took to construct. High-quality stones used to make arrowheads and knives were privately owned. Wood for bows was privately owned because it usually came from distant locations and could only be obtained through trade.

Property rights in indigenous societies, however, extended beyond personal items. In the Pacific Northwest, tribes had exclusive and well-defined property rights to fishing sites. To capture salmon returning from the ocean to spawn in freshwater streams, Indians used elaborate fish weirs and other traps in areas where fish were naturally channeled. Tribal ownership of streams and family ownership of specific sites provided secure property rights to native salmon populations, which the tribes actively managed to ensure the health of the salmon in future years. By carefully selecting which salmon should be harvested and which should be left to spawn, the tribes could ensure an adequate supply of fish in the future.<sup>22</sup>

### **What are mediums of exchange?**

A medium of exchange is a commodity or other item that is widely accepted as a way of paying for goods or services during transactions in

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<sup>22</sup> Anderson, Terry L. 1996. Conservation Native American Style. *PERC Policy Series*. PS-6. July. Available at <http://perc.org/articles/conservation-native-american-style-full>; Johnsen, D. Bruce. 1986. *The Formation and Protection of Property Rights among the Southern Kwakiutl Indians*. *Journal of Legal Studies*. 15(1): 41-67

a given market. Currency is the present medium of exchange in our economy. A medium of exchange is important because it facilitates the exchange of one good for another and eliminates what is known as a double coincidence of wants in a barter economy. A double coincidence of wants involves a situation whereby two people coincidentally each have a good the other wants at the right time and make a trade. This situation rarely occurs and because of this, a barter economy is limited to only simple transactions. On the other hand, an economy that uses a form of medium of exchange can facilitate the occurrence of more indirect transactions. Individuals sell their outputs for “money” which they use to buy other goods for consumption. This allows people within the economic system to specialize in labour, produce goods with relatively lower opportunity costs and then sell those goods to individuals who assign the greatest value to them.

*Dentalium Shells:* Among the Coast Salish First Nations of northern Washington State and southern British Columbia, dentalium shells were used as a medium of exchange in trade with other coastal indigenous groups. These groups ranged from Northern California all the way up the Pacific coast to South-East Alaska. Dentalium shells are variously sized (up to two inches in length) tubular mollusks. Dentalium shells were more prevalently used as currency before the coming of the fur traders and the use of their blankets as a medium of exchange.<sup>23</sup> The Cowichan people (located near present-day Duncan, British Columbia) used dentalium shells for smaller transactions, with the goat-hair blanket being the primary medium of exchange for larger transactions.<sup>24</sup>

Regarding value, the larger an individual dentalium shell or the longer a string of shells, the greater the purchasing power. A fathom long string of dentalium shells alone could buy up to two ocean travelling canoes. As another example, a fathom long string plus eight or ten shells was worth a slave or a large sea-otter skin. Moreover, about a thousand of the

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<sup>23</sup> Stearns, R.E.C. 1869. *Shell-Money*. The American Naturalist, Vol. 3, No. 1, pp. 1-5. The University of Chicago Press for the American Society of Naturalists.

<sup>24</sup> Northwestern University Library. 2003. *Edward S. Curtis's: The North American Indian*. Vol. 9; pp. 91. Available at <http://digital.library.northwestern.edu/curtis>.

smaller shells were required to buy one blanket. The tribes of the high North Pacific coast area did not value dentalia as much as the southerly peoples. Before being replaced by pelts and then blankets introduced by the Hudson's Bay Company, elk, moose and other animal skin seemed to have substituted dentalium as a medium of exchange and standard of value.

*Made Beaver:* Beaver pelts in Canada are an example of how, in most indigenous societies “either a staple consumption good, principal export item, or traditional obligatory gift frequently emerged as an early medium of exchange”.<sup>25</sup> Pelts were a definite principal export good during the fur trade in Canada and constituted a medium of exchange among the fur traders and indigenous people, owing to supply and demand. North America had an abundance of beaver with valuable fur pelts (the supply) which were used to make hats and other items greatly sought after in Europe (the demand). Subsequently, the fur trade became a large-scale industry. Even on the Atlantic coast, beaver fur was used as a medium of exchange side by side with wampum, and it eventually evolved as the basis of all trade between the French of Canada and First Nations. As the beaver became scarcer in eastern Canada, the fur trade pushed westward.

According to the Hudson's Bay Company, “a Made Beaver was a prime beaver pelt which had been worn for at least one season and from which most of the long outer hair had worn off.”<sup>26</sup> Felters shaved the beaver wool from the skin in order to manufacture hats. In central Canada, the Made Beaver became the basis of value first between French and indigenous people, and afterward between English and indigenous people. The Hudson's Bay Company used the Made Beaver<sup>27</sup> as a unit of

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<sup>25</sup> Jones, R.A. 1976. *The Origin and Development of Media of Exchange*. The Journal of Political Economy, Vol. 84, No. 4, Part 1, pp. 757-775. The University of Chicago Press.

<sup>26</sup> Hudson's Bay Company. 2013 (accessed). *Our History: Business; Fur Trade*. Available at <http://www.hbc.com/hbcheritage/history/business/fur/standardtrade.asp>.

<sup>27</sup> Although this example occurred post-contact it still presents a case of Indigenous people responding to incentives and understanding the importance of market supporting institutions.

currency that could be traded at their posts for various European trade goods. The value of other animal pelts such as otter, squirrel and moose were usually quoted in Made Beaver as well as the prices of all trade goods at Hudson's Bay Company's posts. The Made Beaver rates generally depended on market conditions in Europe and the extent of fur trade competition in Canada.

***Examples of Made Beaver Pricing at Hudson's Bay Company Posts***<sup>28</sup>

Commodity	York Factory Price in Made Beaver in 1740	Fort Albany in Made Beaver in 1733
1 gun	14	10 to 12
1 pistol	7	4
1 blanket	7	1
1 knife	0.250	0.125
1 hat	4	1
1 file	1	1
20 fish hooks	2	1
1 gallon of brandy	4	1
1 pair of looking glasses	1	0.5
1 ice chisel	1	0.5
1 yard of cloth	3.5	0.5
1 shirt	2.5	0.5
1 kettle	2	1

There were significant increases in the price of furs between 1732 and 1756 at York Factory and Fort Albany (located in Ontario/Manitoba).<sup>29</sup> These price increases were attributed to a response to higher beaver prices in London and Paris and greater French presence within the main fur trading areas.

<sup>28</sup> Hudson's Bay Company. 2013 (accessed). Our History: Business; Fur Trade. Available at <http://www.hbc.com/hbcheritage/history/business/fur/standardtrade.asp> and Carlos, A.M. & F.D. Lewis. 2008. *The Economic History of the Fur Trade: 1670 to 1870*. Net Encyclopaedia, edited by R. Whaples. Available at <http://eh.net/encyclopedia/article/carlos.lewis.furtrade>.

<sup>29</sup> Carlos, A.M. & F.D. Lewis. 2008. *The Economic History of the Fur Trade: 1670 to 1870*. Net Encyclopaedia, edited by R. Whaples. Available at <http://eh.net/encyclopedia/article/carlos.lewis.furtrade>.

*Blankets:* During the early 19th century, as fur-bearing animals became scarcer, blankets began to be used as a medium of exchange, because they were easy to count and compare with other goods.<sup>30</sup> During this era, “blankets were in demand everywhere as articles of trade and standards of value.”<sup>31</sup> The use of blankets was particularly important during potlatch ceremonies as a measure of wealth.<sup>32</sup> The difference in beadwork and a “point system” by the Hudson’s Bay Company indicated a blanket’s value. Under the point system, each blanket was graded as to weight and size. Lines were then woven into the blanket to represent the amount of points it was worth (ranging from one to six). A full point measured four to five and a half inches; a half point measured half that length. The number of points was equivalent to the number of full-sized beaver skins it was worth – one point equaled one skin. The point system later expanded to encompass all trade goods.<sup>33</sup> In addition, there was also a blanket trade in the west and southwest among indigenous groups that further supports the trade blanket’s role as a medium of exchange.

### **What about indigenous taxation?**

Market economies rely on free trade to flourish, but all societies also must engage in some form of taxation. In the historical context, systems of sharing resources may be analogous to taxation, which is defined as an individual’s compulsory or voluntary contribution of wealth to the larger society. Based on this definition, taxation has been found to be present in all organized societies, including tribes and First Nations prior to colonization by Europeans. The potlatch as practiced on Canada’s west coast, for example, was used as a form of taxation—a formalized system

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<sup>30</sup> Warburton, R. & S. Scott. 1985. *The Fur Trade and Early Capitalist Development in British Columbia*. Brandon University. Available at <http://www.brandonu.ca/library/CJNS/5.1/Warburton.pdf>.

<sup>31</sup> Belanger, Claude. 2004. *The Quebec History Encyclopedia: Indian Blankets*. Marianopolis College. Available at <http://faculty.marianopolis.edu/c.belanger/QuebecHistory/encyclopedia/blanket.htm>.

<sup>32</sup> Kapoun, Robert W. & Charles J. Lohrmann. 2006. *Language of the Robe: American Indian Trade Blankets*. Gibbs Smith.

<sup>33</sup> Ibid.



of wealth redistribution.<sup>34</sup>

The Aztec empire was built on a foundation of city-states.<sup>35</sup> City-states were independently organized societies ruled by kings who controlled surrounding areas from their capital towns. All of the land within a city-state belonged to the ruler of the city-state. The king granted estates to high lords and allocated land in order to build temples. The high lords were in charge of wards or groups, which were collections of commoner families who lived near one another (i.e. a neighbourhood). The governing Council and the high lord divided the land among the families. Plots of land within the area were passed across generations. In addition, if new land opened up or if an existing plot was left abandoned, the Council reallocated the land. Land could also be reassigned if it was neglected or if a user died without heirs. The rights of use for individual plots could be sold, but the land remained under the jurisdiction of the group and the city-state. For the privilege of farming the granted land, the commoners paid a form of tax or tribute to the high lords, who paid some of the tribute back to the king. The tribute was usually paid in the form of goods such as textiles and clothing, food, military supplies, building materials and animal products. Sometimes labour was used as a form of tribute as commoners supplied their labour for the construction of large public projects such as the building of temples.

## Conclusion

Indigenous groups have always understood incentives and have long been connected to trades and markets. However, the economic history of indigenous populations in the Americas offers a puzzle: the societies that were historically very prosperous are now relatively poor.<sup>36</sup> The evidence

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<sup>34</sup> Johnsen, D. Bruce. 1986. *The Formation and Protection of Property Rights among the Southern Kwakiutl Indians*. *Journal of Legal Studies*. 15(1): 41-67.

<sup>35</sup> Smith, Michael E. 1996. *The Aztecs*. Malden, Massachusetts: Blackwell Publishers.

<sup>36</sup> Acemoglu, Daron, Simon Johnson, and James A. Robinson. 2002. Reversal of Fortune: Geography and Institutions in the Making of the Modern World Income Distribution. *The Quarterly Journal of Economics*. 117(4): 1231-1294. Available at <http://economics.mit.edu/files/4127>.

of market institutions related to trade, specialization, taxation and public infrastructure, laws and standards and even property rights seems to have been strongest in the countries in Central and South America. As a result, these regions were the wealthiest in the western hemisphere – perhaps even in the world. The Mayan economic empire was present in modern-day Mexico, Honduras, Belize, El Salvador and Guatemala, the Aztec in Mexico, and the Incas and Norte Chico were present in modern-day Peru, Chile, Ecuador, Bolivia, Argentina and Colombia. Although market institutions were certainly present, and in many cases impressive, in what are now Canada and the United States, evidence of public infrastructure was not the same as the Mayans, Incas, Aztec and Norte Chico. In other words, by some measures, there was greater wealth south of the United States before European contact.

After contact, however, the presence and accumulation of wealth changed. The United States and Canada now have much higher income per capita than any country south of the United States.<sup>37</sup> This textbook suggests that the countries that have developed market institutions are most efficient and effective. Modern indigenous populations throughout the Americas have largely been excluded from the development of market institutions and are generally the most impoverished in their respective countries. The purpose of this textbook is to help interested students build and restore the market institutions for indigenous populations that will help them rebuild their economies, generate business and employment opportunities for their citizens and provide the public infrastructure and services that will sustain their communities and cultures. As this chapter demonstrates, these market institutions—rooted

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<sup>37</sup> This is consistent with the observation that Spain did not develop security of property rights to promote business as did England. When the Spanish came to Latin and South America they simply expropriated wealth from the indigenous people and kept the Spanish approach. In North America there was less expropriation by English settlers (except for land itself), but their bringing the English legal system with them has facilitated the economic growth of the United States and Canada relative to the growth further south (see Acemoglu & Robinson, 2012 and North, D.C., William Summerhill & Barry R. Weingast. 1999. *Order, Disorder and Economic Change: Latin America vs. North America. Governing for Prosperity*. Yale University Press. Available at <http://www.international.ucla.edu/CMS/files/weinga.pdf>). The issue is that indigenous people were not given the opportunity to participate in the United States and Canadian market systems while their own systems were destroyed by the colonists who wanted their land.

in trade, specialization, property rights, and the rule of law—were well-understood by indigenous societies long before European contact.

**Questions:**

1. Why is it significant to identify historical trade networks among indigenous groups?
2. What is a trade network in the modern context? How is it similar to an historical trade network? How is it different?
3. Explain why public infrastructure is important to a community.
4. Identify four examples of public infrastructure in your community.

**Chapter 1 Appendix**

Consider a hypothetical example involving the cost of producing rabbit hair robes and salmon oil for two First Nation groups in Canada.

***Hypothetical First Nation Specialization Example***

	Rabbit Hair Robes Per Day	Salmon Oil Units Per Day
Chilcotin	30	10
Cañon Division (Shuswap)	10	30

Firstly, we will consider each group's opportunity cost of producing a product. The opportunity cost is simply what is given up, or foregone, by doing something. Based on the table above, for the Chilcotin the opportunity cost of producing one unit of salmon oil is three rabbit hair robes. Conversely, the opportunity cost of producing one rabbit hair robe is only 1/3 of a unit of salmon oil.

Looking at the Cañon Division opportunity costs, the production of one unit of salmon oil costs the Cañon Division only 1/3 of a unit of rabbit hair robes. Conversely, the opportunity cost of the production of one rabbit hair robe is three units of salmon oil. This shows that their comparative costs differ and specialization and trade will be mutually advantageous. The Cañon Division is relatively better at producing salmon oil (1/3 compared to three) while the Chilcotin is relatively better at producing rabbit hair robes (1/3 compared to three). The Cañon Division has a competitive advantage in the production of salmon oil and the Chilcotin has a competitive advantage in the production of rabbit hair robes.

Next step is to assume an exchange rate for rabbit hair robes and salmon oil in the market. Let's assume that the exchange rate is one unit of salmon oil for one rabbit hair robe. Since trade is mutually advantageous, both groups will specialize. However, since they desire both products and not solely the product they specialize in, they will execute a trade with each other. Additionally, at our assumed exchange rate both groups have an incentive to trade in the market as the Chilcotin can obtain a unit of salmon oil (only one unit of rabbit hair robe) for less than their opportunity cost to produce it (three units of rabbit hair robes). The opposite is true for the Cañon Division. Therefore, in this case, the

Chilcotin will allot a whole day to producing rabbit hair robes and they will produce 30 units. The Cañon Division will allocate a whole day to produce salmon oil and they will also produce 30 units. The table below shows how production of both products increases in this specialized situation.

***Production in Non-Trading and Trading Situations***

	Production Per Day					
	Non-Trading Situation		Specialization Situation		Trading Situation	
	Rabbit Hair Robes	Salmon Oil	Rabbit Hair Robes	Salmon Oil	Rabbit Hair Robes	Salmon Oil
Chilcotin	15	5	30	0	15	15
Cañon Division	5	15	0	30	15	15
<b>Total</b>	<b>20</b>	<b>20</b>	<b>30</b>	<b>30</b>	<b>30</b>	<b>30</b>

Trade and specialization allows the combined output between the two First Nation groups to increase by ten units of rabbit hair robes and ten units of salmon oil. Both groups end up better off when they trade at this exchange rate. Both groups will end up with 15 units each of rabbit hair robes and salmon oil (final two columns in the table). This is better than a situation in which they each allocate half of their day to producing each good (first two columns in the table). The Chilcotin obtain ten more units of salmon oil and the Cañon Division obtain ten more units of rabbit hair robes after trading with one another. The principle of comparative advantage underlies all trade.



CHAPTER 2

# THE INVESTMENT CLIMATE AND TRANSACTION COSTS

**S**ometimes it takes great courage and perseverance to make markets work. An example of this is Clarence Jules Sr., who worked to establish a pioneering industrial park on the Kamloops Indian Reserve (Tk'emlúps te Secwépemc) in Kamloops, British Columbia, Canada. In 1962, under his leadership, the Kamloops Band Council passed a by-law to establish an industrial park on their lands. Clarence Sr. made sure the necessary infrastructure was built and convinced a number of businesses to invest and lease land on the reserve. Fourteen applications to lease lands were received, but securing a property right on First Nation lands in the 1960s was difficult. There was uncertainty about tenure, lease registration, tax liability and local service provision. There were also many options on non-First Nation lands. From the 11 businesses that eventually leased land in 1964, this industrial park has grown to over 150 today, with annual sales of over \$250 million.

To put Clarence Jules' accomplishment in perspective, consider what he said in 1968:

*We feel that we are in a better position to judge the needs of our people than officials of the Department located in Ottawa... To give just one illustration: We operate an Industrial Subdivision on part of our reserve and lease lots in the Sub-division to various individuals and companies. Before a lease can be granted not only must the Band Council pass its resolution but the lease is then routed through the Kamloops Indian Agency, then to the Vancouver office and finally to Ottawa. The same process is followed on the return trip.*

*We can document instances where months have gone by before a lease is finally issued. In many cases by the time the lease has been returned the lessee has gone elsewhere because people today require almost instantaneous decisions. These delays cost us money and we don't like it. There must be a change to grant more power and authority to Indian Band Councils. After all, our Indian people elect us to represent them; they do not elect officials of the Indian Department.<sup>38</sup>*

To our knowledge, Clarence Jules Sr. was the original First Nation leader to recognize the high costs of doing business on First Nation lands. Out of practical experience, he arrived at the same conclusion that the discipline of economics has reached, namely that if the cost of doing business is too high, then people will do business elsewhere.<sup>39</sup> This

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<sup>38</sup> Government of Canada. 1968-1969. *Report of the Indian Act Consultation Meeting.*

<sup>39</sup> See Backhouse, Roger E. 2002. *The Ordinary Business of Life: A History of Economics from the Ancient World to the Twenty-First Century.* Princeton: Princeton University Press; Cooter, Robert B. & Thomas Ulen. 2011. *Law and Economics.* Prentice Hall; and Allen, Douglas W. 1988. *What are Transaction Costs Anyway?* Carleton Industrial Economics Research Unit, Carleton University, Department of Economics, Ottawa.

simple observation is the source of much of the underdevelopment on First Nation and tribal lands. This chapter is about understanding the source of these high costs. The rest of the text is about how to reduce them.

### **Learning Objectives**

There are five learning objectives in this chapter:

1. Describe how investment generates economic growth.
2. Identify questions asked by investors.
3. Explain transaction costs and develop an explanation of why the cost of doing business is high on First Nation and tribal lands.
4. Describe the role of governments in raising or lowering transaction costs.
5. Outline the investment climate equation and the institutional framework to facilitate investment.

### **What is the Engine of Economic Growth?**

Economic growth usually begins with an investment that creates a new business or expands an existing one. The investment occurs because a business anticipates a profit. In this way, if private investment is the engine of economic growth, then the profit motive is the gas that makes it go. There would be no private investment if the private sector did not envision a profit from doing so.

Investment creates jobs and business opportunities. It builds homes. It creates new businesses and expands existing ones. It stores and generates wealth for individuals. It implements technological and business innovations. It unleashes creative, artistic and scientific potential.

Investment includes businesses that put resources into new plants and equipment or the expansion of existing facilities. It also includes investment by individuals into their homes, education and businesses. The underlying strength of the economy along with its ability to generate revenues for the public sector depends upon this investment. An economy's ability to attract investment depends upon a number of factors such as access to resources, location and transportation costs which, in sum, are termed the "investment climate."

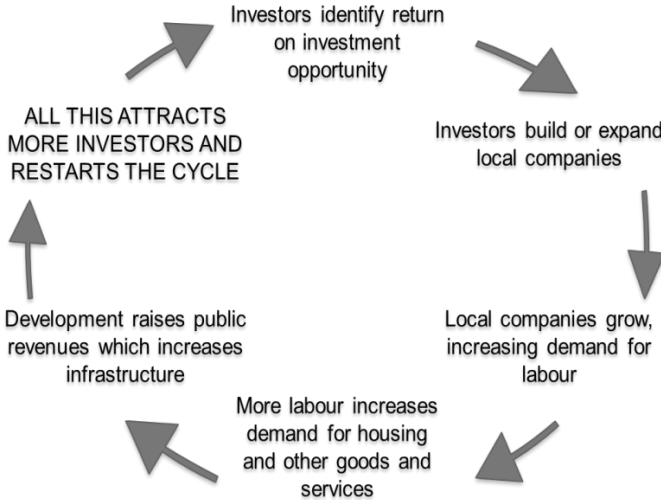
We sometimes forget how private investment benefits the public at



large. The public revenues from private investment help to build such things as parks, schools, roads, sewer and water systems, libraries, museums and art galleries. These revenues permit a social safety net. Consider that the level of public health care provided in Canada and the United States is dependent upon the amount of tax revenue generated from the private sector to pay for it. Private investment also supports charities, religions and non-profit service agencies. In other words, our communities and the values and ideals they encompass are in large part a result of successful private investments.

Stated differently, it is not the charity of the baker, the butcher or the tailor that has created all this public good from private investment.<sup>40</sup> It is the development of institutions like fiscal federalism, in which revenues and responsibilities are divided among governments and democracy that ensure that tax revenues from private investment serve the public good. To help provide an understanding of these relationships, the figure below depicts the virtuous circle of investment.

***The Virtuous Circle***



<sup>40</sup> Paraphrased from Adam Smith, who wrote: "It is not from the benevolence of the butcher, the brewer, or the baker, that we can expect our dinner, but from their regard to their own interest." Smith, Adam. 1776. *An Inquiry into the Nature and Causes of the Wealth of Nations*. Edited by Edwin Cannan. Chicago: University of Chicago Press, 1976. Available online at: <http://www.econlib.org/library/Smith/smWN.html>.

### **Private Investment on First Nation and Tribal Lands**

Most First Nation and tribal communities do not represent a balanced mixed economy. Generally, their public sectors are too large and their private sectors are too small. In other words, the balance between private and public sectors in the rest of the United States and Canada is not evident on reserves. There are very few privately held businesses on reserves and there is little retail. At least 90 per cent of all expenditures by on-reserve households in Canada are made off-reserve<sup>41</sup>, and U.S. reservations experience similar amounts of tribal income spent off reservation.<sup>42</sup>

In Canada, many on-reserve businesses require significant First Nation, federal and provincial support. Almost all employment is with the First Nation public sector. Some estimates suggest that on-reserve First Nation employment is almost 80 per cent public, whereas the majority of new jobs created in Canada are in the private sector.<sup>43</sup> Currently, it is about a three to one ratio of total new private sector jobs to total new public sector jobs in Canada.<sup>44</sup> Stated another way, Canadians are about three times more likely to find work in the private sector than the public sector. Private sector activities and sales also provide the majority of public revenues through both corporate taxes and personal income taxes from those newly employed in the developed commercial enterprises – together they make up approximately 60 per cent of public revenues annually.<sup>45</sup> Any strategy of providing jobs for the

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<sup>41</sup> Fiscal Realities Economists. 2004. *Expanding the First Nation Private Sector: The Rule of Investor Codes*. Prepared for FNTC and AANDC.

<sup>42</sup> For instance, the Navajo tribe in the United States estimates that more than 76 per cent of the tribe's total personal income is spent outside of the reservation. See Miller, Robert J. 2012. *Creating Economic Development on Indian Reservations*. PERC Reports. Volume 30, No. 2. Available at <http://perc.org/articles/creating-economic-development-indian-reservations>.

<sup>43</sup> Fiscal Realities Economists. 2004. *Expanding the First Nation Private Sector: The Rule of Investor Codes*. Prepared for FNTC and AANDC.

<sup>44</sup> Statistics Canada. 2011. *Table 282-0012 Labour force survey estimates (LFS), employment by class of worker, North American Industry Classification System (NAICS) and sex, annual (persons x 1,000)*. Data from 2000 to 2010. Available at <http://estat.statcan.gc.ca>.

<sup>45</sup> Statistics Canada. 2011. *Table 385-0001 Consolidated federal, provincial, territorial and local government revenue and expenditures, annual (dollars)*. Data from 2000 to 2009. Available at <http://estat.statcan.gc.ca>.

First Nation labour force must consider the role of the private sector. Plainly stated, the strategy must be to increase the size of the private sector on First Nation lands; otherwise, off-reserve migration will increase. The impact of not attracting investment is not just the lost investment itself; it is lost job opportunities as well. It is migration away from the community. It is poverty and all the health, housing and social problems associated with poverty. In short, the consequences of a failure to attract investment include:

- Lack of job or business opportunities in community;
- Minimal tax base for the community;
- Poor services;
- Poverty; and
- Out-migration

A lack of investment results in a deficiency of employment opportunities. Consequently, this leads to a dependency on governments for basic service provision to citizens (with minimal tax bases) as opposed to fostering self-sufficiency within the community. The lack of employment, poor services and impending poverty force individuals to seek opportunities outside of the community.

### **Understanding Investors**

Investment occurs because a business anticipates a profit. There would be no private investment if those in the private sector did not anticipate this profit. Therefore, investors make decisions based on information about opportunities. When considering whether a jurisdiction will attract investment, it is useful to think from the investor's perspective.

Thinking from an investor's perspective means understanding the questions that investors generally ask and the information they seek. Throughout the remainder of this book, we will outline the questions that investors generally ask in accordance with the overarching theme of the particular chapter. Keep these questions in mind as you read the contents of every chapter and try to answer every one before moving on to the next chapter. Typical questions include:

- In general, are the private and public sector conditions favorable for investment on First Nation and tribal lands?
- What developable land is available?

- Is the location suitable for investment?
- What are the risks associated with investing in this location?
- Are transactions costs high on First Nations and tribal lands?
- What is the government doing to reduce these risks and costs?
- Are all public sector elements, including services to the land, in place or could be developed in a timely manner?

Investors want to know whether a location is good before they invest. If the investment climate is poor, then only investors with a relatively higher tolerance for risk and enough resources and time to get over the poor investment climate will invest. It could also mean that private investment has to be heavily subsidized by public funds.

Potential investors will simply jump from location to location until they find the right property and certainty they are looking for, much like channel surfers flip through television channels until they find what they like. In this sense, there is competition for investment among different jurisdictions. Investors are looking for properties they can develop successfully and with a competitive return. Successful property developments are usually defined as those that overcome all the barriers between the initial proposal and final approval.

Preliminary answers to these investor questions would not be satisfactory in most First Nation and tribal communities. It is often difficult for developers to obtain the information needed to analyze the suitability of a site when First Nation and tribal lands are under consideration. If developers do not know how to search for sites on these lands, then even the most attractive sites will fail to attract investment. This is the most basic of development information required. Detailed demographics, investment processes and contacts are also seldom present when a potential investor searches on First Nation or tribal lands. As a result, it is difficult to estimate the return on investment. Investors must have certainty over processes, recourse, land tenure, returns to investment and service quality. This generally means clear land management rules and processes, land registry and tenure security, clarity relating to property, sales, income and corporate tax rates, and sufficient and certain revenue to ensure public service and infrastructure quality. Certain types of investments, such as buildings, pipelines and other infrastructure, can be particularly risky from an investor's point of

view. These investments often require high fixed costs but are non-mobile. From the investor's perspective, these investments cannot be relocated if the investment climate changes, becomes more uncertain or if property rights are weakened in any way.<sup>46</sup>

As a result, even if the business/industrial investment on First Nation and tribal lands were initially successful, the First Nation or tribe would still not be part of the virtuous circle for very long. In the event that more labour was attracted, there would be no growth in the housing market if the investment climate for housing were poor. Indeed, the housing market is often thwarted on reserves because there is little land tenure certainty for financial institutions.

### **What are Transaction Costs?**

Transaction costs refer to the costs of carrying out an economic exchange, or in other words, the cost of doing business. For example, the costs of buying a car are straightforward. The car may cost \$20,000. However, these are not the full costs. This exchange is also subject to transaction costs. A person will spend time looking for the right car; this time is a transaction cost incurred by that person. There may be a cost to have a mechanical inspection done; there would also be a cost to register the car title; these are transaction costs.

Most economic analysis assumes that exchange is costless. This assumption, while not technically true, generally does not cause significant problems. If transaction costs are low, trade occurs. However, in some cases, transaction costs are high. At times, transaction costs can be so high that an otherwise profitable exchange would not go forward at all. This is essentially known as market failure. Entrepreneurs seek to avoid market failure by attempting to minimize the transaction cost of conducting any given volume of trade.<sup>47</sup>

Transaction costs can make or break an investment. Furthermore,

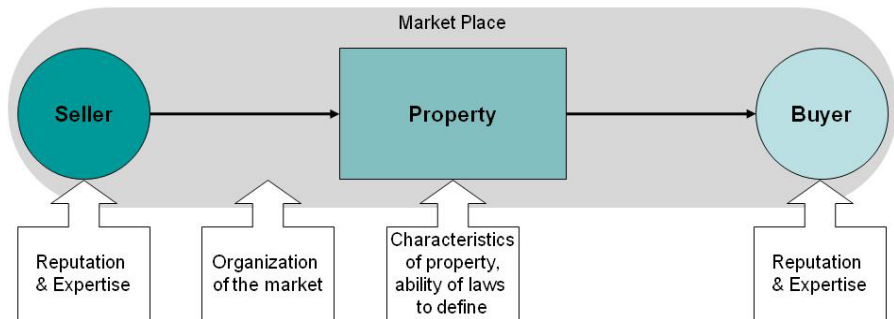
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<sup>46</sup> For an example, see Anderson, Terry L. 2013. The Grand Canyon of Property Rights. *Defining Ideas: A Hoover Institution Journal*. April 17. Available at <http://perc.org/articles/grand-canyon-property-rights>. See also Haddock, David D., and Robert J. Miller. 2006. Sovereignty Can be a Liability: How Tribes Can Mitigate the Sovereign's Paradox. In *Self-Determination: The Other Path for Native Americans* eds. Terry L. Anderson, Bruce L. Benson, and Thomas E. Flanagan. Stanford University Press. 194-213.

<sup>47</sup> Casson, Mark. 2003. *The Entrepreneur: An Economic Theory*. Massachusetts: Edward Elgar Publishing, Inc.

transaction costs are affected by policy and differ from jurisdiction to jurisdiction. If a person feels reasonably confident about the consumer protection laws in a jurisdiction, then costs of carrying out an economic exchange there will be lower. If not, they may simply go elsewhere to another jurisdiction with lower transaction costs. This point is the key; it suggests the transaction costs associated with investing are determined by the state of governance and other factors, such as the existence or non-existence of different types of regulation.

***What Affects Transaction Costs? The Factors Influencing Economic Exchange Costs***



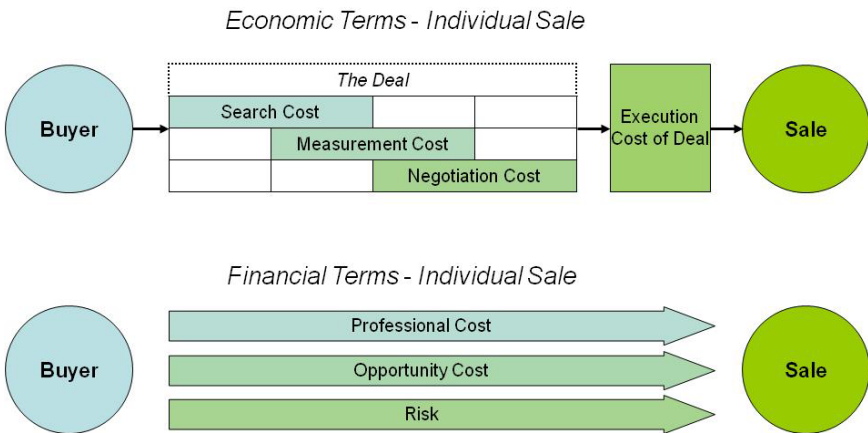
The figure above helps to illustrate this. This figure shows a simple economic exchange. Property is being sold, and the arrows that run from seller to buyer represent this. The marketplace for this exchange is illustrated by the shaded grey area. For example, if the product was groceries, the marketplace would be a supermarket but also all the rules about food safety, labeling, etc., that govern the sale of groceries. The arrows below the diagram identify some of the generic factors that would influence the extent of transaction costs: the reputation of buyer and seller (if a buyer does not trust the seller then much more inspection will be required), the organization of the market (is it straightforward or difficult to find property you wish to purchase?) and the nature and clarity of the property itself (is it simple or difficult to determine its quality; is the property protected by law; are its salient features easily measured?).

At least four types of transaction costs are incurred in almost any transaction. These are specified below with respect to a land sale

(property investment).

1. *Search costs*: these are incurred when the proponent of the development searches for a seller with an appropriate site. This would include any time and money that is spent identifying different sites and doing preliminary assessments as to their suitability.
2. *Measurement costs*: these are incurred when measuring the property in question. This includes the costs of measuring the physical and geographical parameters of the land. It also includes measuring pertinent factors related to the proposed use. For example, it could include the cost of a geotechnical report and the measurement of legal factors such as the permitted and restricted uses of the land, covenants, and easements.
3. *Negotiation costs*: costs of determining the terms under which the property in question will be transferred. This would obviously include the price. It would also refer to which property rights are to be transferred, including stipulations, contingencies, and related agreements.
4. *Execution costs*: costs of formally drawing up contracts, processing approvals and, if necessary, enforcing the contract.

**Types of Transaction Costs**



The figure above illustrates two ways of understanding the four types of transaction costs. The top chart shows the four basic transaction costs that would be incurred during the process of making a sale. These are

partly, but not necessarily completely, sequential. For example, measurement costs may be incurred at different points through the progress of an economic exchange. Generally, search costs are borne early in the process, and execution costs are incurred late. These transaction costs are incurred in different ways. In some cases, they may be financial costs and in other cases, they may be the cost of a person's time or the opportunity cost of delaying a project.

The bottom chart translates these transaction costs into more familiar financial terms: opportunity costs, professional costs and risk.

Opportunity costs refer to the other uses the investor could make of his time and money while he is pursuing the development in question. Lengthy delays in project approval can create significant opportunity costs because this moves the eventual payback period that a project will earn revenues into the future. Since revenues earned in the future are valued less than revenues earned today, opportunity costs can be quite significant.

Professional costs are direct costs incurred in order to clear the hurdles between conception and final approval. Most proposals incur substantial legal, engineering, accounting and other costs.

Risk is related to opportunity costs. Simply put, the longer a project takes to transit from proposal through to final approval, the higher the financial risks associated with that project. For example, market or cost conditions are all more likely to change and adversely affect profitability during an approval process if it takes significantly longer. To reduce risk, investors prefer to transit the approval process as quickly as possible. Risk will also increase if investors perceive that a project is unlikely to ever be completed at all—perhaps due to uncertainty about the security of property rights or legal institutions.

Measuring investment in property involves assessing the potential investment by evaluating the impact of the above costs and determining the best ways of reducing their significance. If the perceived barriers (or costs) are too high (higher than the benefits/capital gains of a project), investments will move elsewhere. The time and money spent completing a transaction equates to higher opportunity costs, professional costs and more risk associated with a project. Each of these costs will raise the perceived costs of pursuing a project.

The above framework illustrates how a typical property transaction is



analyzed from a transaction cost perspective. The structure of property rights and the organization of the market provided by the jurisdiction are assessed to determine the extent of search, measurement, negotiation, and execution costs.

It is often possible to infer the extent of transaction costs simply by looking at the number of exchanges that occur. A high number of exchanges indicate that transaction costs are likely low. On First Nation lands in Canada and Native American reservations in the United States, there are relatively few economic exchanges, especially with those living off reserves or reservations. This suggests that the transaction costs associated with economic activity on reserve lands are high.

### **Transaction Costs on First Nation and Tribal Lands**

Many transaction costs arise in land development on First Nation and tribal lands. In many cases, the transaction costs are so high that they limit investment to only the largest investors that can afford to support high levels of development costs and extended timeframes.

For First Nations and tribes to compete with other jurisdictions for investment, the costs of doing business on First nation and tribal lands will have to become competitive. This is challenging because a principal determinant of the high costs of doing business is the *Indian Act* in Canada and the federal trusteeship of Native Americans in the United State - as well as the requirements of Aboriginal Affairs and Northern Development Canada and the U.S. Bureau of Indian Affairs.

What are the differences in transaction costs on and off reserve land? To answer, we turn to a method called transaction cost analysis to study the development process on First Nation reserves in Canada.<sup>48</sup> Based on a series of First Nations case studies, the Fiscal Realities consulting firm has mapped out the seven steps required to bring about development. The table below provides descriptions of the stages and summarizes the differences between the transaction costs associated with establishing marketable property rights off and on First Nations land. Although their analysis focused on First Nations, the differences in transaction costs on and off U.S. reservations are quite similar.

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<sup>48</sup> Flanagan, Tom, Christopher Alcantara, and Andre Le Dressay. 2010. *Beyond the Indian Act: Restoring Aboriginal Property Rights*. McGill-Queen's University Press.

*Development Stages and Transaction Costs*

STAGE	DESCRIPTION	OFF FIRST NATIONS LAND	ON FIRST NATIONS LAND (UNDER INDIAN ACT)
Project Initiation/ Concept	Developer and/or community leaders identify suitable land and pitch the idea to the community. Includes initial due diligence and feasibility studies (economic and financial).	Search available real estate and approach local government development services office.	Little or no real estate information and generally no development service office.
Land Tenure Certainty	Community creates land tenure certainty for the development.	Defined and managed through provincial legislation and bureaucracy (land use planning and zoning).	Requires land designation for long-term certainty and Indian Affairs bureaucracy.
Land Leasing	Negotiation of land lease agreement between the developer and community or developer and Certificate of Possession holder.	Transaction usually facilitated by real estate industry and through a provincial land titles office.	Modify Indian Affairs lease as required (can include unique features like employment policies or guarantees of tax rates).
Financing	Financing the costs of the development.	Financial industry has substantial experience with many financing models.	Little or no experience of financial industry. It is common for on-reserve developers to pledge the title to off-reserve property as part of their financing (both FN and non-First Nations developers).
Infrastructure Development and Services	Most significant projects require upgrading the	Local governments have many infrastructure	Fewer financing options for First Nations and service

STAGE	DESCRIPTION	OFF FIRST NATIONS LAND	ON FIRST NATIONS LAND (UNDER <i>INDIAN ACT</i> )
	existing physical infrastructure, building new infrastructure, or obtaining access to services and infrastructure in other jurisdictions.	financing options and deliver local services.	agreement with local government usually required.
Legal Framework for Markets	Investors need certainty with respect to development costs and taxes, local service quality, local land-use and other laws and rules, and recourse in the event of a dispute.	Investors generally know their expected costs and taxes, the local laws, investor recourse, and land use.	Much of this legal framework has not been established by the <i>Indian Act</i> or First Nations; therefore significant investor uncertainty.
Construction	Includes all the regulations associated with building standards, development approval processes, and risk, heritage, and environmental assessments.	Building and engineering standards and bonded construction are common.	Building and engineering standard uncertainty and possible bonding issues.

As can be seen from the table above, every development stage is hindered by transaction costs on First Nations lands. Native American reservations in the United States experience nearly identical barriers to development. These high transaction costs are the fundamental source of underdevelopment of First Nations and Native Americans. In addition, it occurs on even the best First Nation and tribal lands. The origin of this problem lies in a lack of market-oriented governance institutions. Markets need governments, and government policies impact transaction costs. Government policies can impact search costs by providing or not

providing reliable information that buyers and sellers need to assess economic opportunities. Policies can make it easier or harder to measure a product (metric vs. English measurement system). They can make it easier or harder to negotiate an agreement for purchase by providing or not providing quality assurance provisions, for example. The completion of a transaction may require government registration or other requirements that raise or lower these transaction costs.

The impact of government policies on transaction costs should always be considered. As we will discuss, the role of governments in making markets work should be to develop a legal and administrative framework that protects property rights, ensures quality, provides standards, reliable information and security for buyers and sellers and builds the public infrastructure necessary to facilitate trade.

### **Case Study – High Cost of Doing Business**

How long does it take to establish a secure property right on First Nation and tribal lands compared to off those lands? A 1999 study for Canada's Indian Taxation Advisory Board and the Department of Indian Affairs and Northern Development, investigated real estate transaction costs under Canada's *Indian Act*.<sup>49</sup> Three case studies of successful commercial and residential real estate deals on First Nations lands were examined and compared with similar deals in the nearby provincial/municipal setting.

In general, assuming community interests and regulatory safeguards are met, the shorter the period for finishing each component of a land deal, the lower the costs and the greater the net benefit produced. In addition, in general, the shorter the time from concept to construction, the lower the opportunity costs and the greater the net benefit. Thus, the time from start to finish was used as a measure for the professional and opportunity costs (or, more broadly, the transaction costs) associated with each real estate transaction.

It is important to note that the First Nations in the case studies are

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<sup>49</sup> Fiscal Realities Economists. 1999. *Expanding Commercial Activity – Reducing the Costs of Doing Business on First Nations' Lands*. Prepared for ITAB and DIAND. See also Le Dressay, C. Andre, Greg Richard & Jason Calla. 2008. *The High Costs of Doing Business on First Nation Lands in Canada*. Journal of Academy of Business and Economics.

not typical First Nation communities in Canada. The First Nations discussed in the case studies have favourably located reserves, a history of active management of their land and resources, and additional capacity and sophistication in terms of administration (from their experience with all aspects of major commercial and/or residential developments). Nonetheless, they provide an opportunity to examine the theory that the costs of doing business on reserve are relatively high.

The three case studies were:

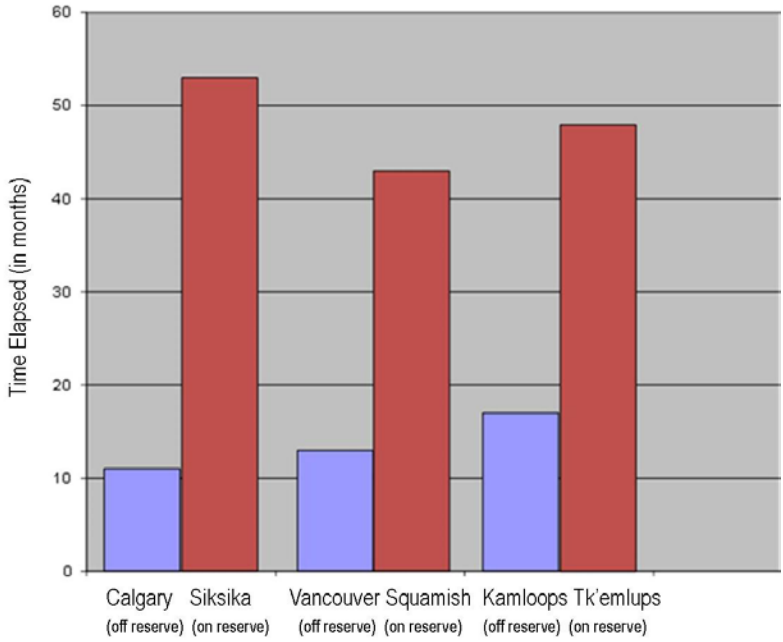
1. Real Canadian Superstore at Seymour Creek I.R. No. 2, a Squamish First Nation reserve in North Vancouver, British Columbia.
2. Sun Rivers golf course and residential development at Kamloops I.R. No. 1, a Tk'emlups te Secwepemc reserve in Kamloops, British Columbia.
3. Mixed use development (commercial/office) at Siksika I.R. No. 146, a Siksika Nation reserve near Calgary, Alberta.

The time elapsed in completing development approval processes is illustrated in the figure below. Comparisons made include Calgary/Siksika, Vancouver/Squamish, and Kamloops/Tk'emlups. Developers confirmed that these time frames were roughly indicative of the higher professional costs they incurred in the project approval process. Additionally, these time frames precisely matched the opportunity costs of foregoing the revenue earning stages of the development. For the most part, developers confirmed that these differences and their related uncertainty were significant and would continue to be a factor in site location decisions where First Nation sites are under consideration.

The experiences of these developers suggest that considerable amounts of time, uncertainty and professional costs can be expected in clearing project approval processes on First Nation lands. This conclusion held up in First Nations in two different provinces when compared to adjacent municipalities. While the three case studies are a relatively small sample, they likely underestimated the average cost differences between on- and off-reserve projects. Only successful developments were studied, and these were conducted by developers who had some experience with First Nation processes and First Nations

who had some experience with developers.

***Comparison of Development Timeframes***



The study identified several causes of high transaction costs that act as general impediments to successful development on First Nation lands:

- *Incomplete leadership, governance and administration.* Because of resource limitations, qualified persons are often called upon to perform both political and administrative roles. This can create a perception of political influence on projects. There are virtually no mechanisms in place to ensure the separation of politics from the administration of government.
- *Political uncertainty.* Many investors are reluctant to do business on First Nation and tribal lands because they lack a business history, and there is often little consistency in policies after regime changes. This has created a need to seek more certainty through contractual arrangements than is the case in other settings. There is also a lack of communication as to how a strong economy supports community goals.

- *Lack of information for investors.* It is often difficult for developers to obtain the information needed to analyze site suitability when First Nation and tribal lands are under consideration. Information that is generally available through title search and linked information systems is generally not available to them. Statistical information is also often not available.
- *Difficulties establishing property right certainty.* Appropriate property right certainty is often difficult to establish owing to difficulties in securing approvals from the Department of Indian Affairs and Northern Development in Canada or the Bureau of Indian Affairs in the United States and the inadequacy of the current land registry systems. (In addition, the current property right system does not adequately support collateralization<sup>50</sup>.)
- *Absence of an appropriate legal framework.* First Nation and tribal jurisdiction has for the most part not established either the laws and regulations needed to eliminate investment uncertainty or it is subject to jurisdictional uncertainty.
- *Poorly devised fiscal relationship and project financing.* Many on-reserve projects must be financed through retained earnings and this reduces the pool of potential investors. They do not have secure and stable revenue sources in order to provide quality services and infrastructure to support investment.
- *Federal trusteeship constraints.* The Canadian and U.S. federal governments are required to improve the welfare of indigenous people, but they must operate within inefficient bureaucracies that have little ability—or incentive—to achieve meaningful progress. This problem manifests itself in the negotiation of lease documents and contributes to lengthy delays in approval times. The division of responsibilities between First Nations/tribes and federal/provincial governments is inefficient and unclear.
- *Non-competitive infrastructure.* Most large investment projects on First Nation and tribal lands require extensive infrastructure improvements. In Canada, First Nations only have access to property taxes and a few other local revenues and reserves. Moreover, they

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<sup>50</sup> Collateralization occurs when a borrower pledges an asset as recourse to a lender in case of loan default.

are in a catch 22 where they need revenues to finance infrastructure but cannot generate revenues without infrastructure. The result is that most economic infrastructure on First Nation lands is sub-standard.

These case studies suggest that the cost of establishing a marketable property right on First Nations and tribal land is at least four times more expensive than establishing the same property right off First Nations and tribal land. Transaction costs this high are likely to lead to market failure. The implications of this conclusion for First Nation and Native American policy are significant. Any effort to improve the well-being of First Nations and Native Americans through economic development will fall short of its goal unless these transaction costs are reduced.

### **Case Study – Energy Development On and Off U.S. Reservations**

U.S. Indian reservations contain almost 30% of America’s coal reserves west of the Mississippi, 50% of potential uranium reserves, and 20% of known oil and gas reserves.<sup>51</sup> According to the U.S. Department of the Interior, there are 15 million acres of potential energy and mineral resources that are undeveloped on tribal lands but only 2.1 million acres of tribal land are currently being developed for their energy resources.<sup>52</sup>

The Crow Reservation in Montana contains coal and other assets valued at nearly \$27 billion, making the tribe one of the largest coal owners in the world. Yet the tribe’s annual rate of return on coal assets is a mere 0.01%.<sup>53</sup> In fact, the tribe has reported unemployment rates as high as 78%. Similarly, the Fort Berthold Reservation in North Dakota sits atop one of the nation’s largest oil and gas plays, but the development of resources on the reservation is slower than off the

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<sup>51</sup> Grogan, Maura. 2011. Native American Lands and Natural Resource Development. Revenue Watch Institute: 3.

<sup>52</sup> Middleton, Robert W. 2008. Hearing before the Committee on Indian Affairs, US Senate. Indian Energy Development: Statement of Dr. Robert W. Middleton, 110th Congress, Second Session, May 1. [http://www.indian.senate.gov/public/\\_files/May12008.pdf](http://www.indian.senate.gov/public/_files/May12008.pdf).

<sup>53</sup> Cornell, Stephen, and Joseph Kalt. 2000. Where’s the Glue? Institutional and Cultural Foundations of American Indian Economic Development. *Journal of Socio-Economics* 29(5): 443-70.



reservation.<sup>54</sup> Simply put, energy resources on reservation lands are substantial, and the potential wealth that could be derived from such resources presents an opportunity for significant economic growth for tribes and the U.S. economy.

However, given such energy wealth, why do reservations often remain poor? The answer has a lot to do with the transaction costs associated with doing business on reservations. As two scholars, Stephen Cornell and Joseph Kalt, explain, a “tribe’s resources can be wasted or go untapped unless that tribe can establish an incentive environment that channels them into productive ends.”<sup>55</sup> If transaction costs on tribal lands are high, resources will not be channeled to their most productive ends, and may even go undeveloped.

Crossing a reservation boundary means entering a very different set of legal institutions, including property rights and the rule of law. Outside of reservations, local, county, state, and federal governments provide stable property rights through law enforcement and judicial institutions conducive to economic growth. Inside of reservations, however, property ownership is a mosaic of private lands and trust lands. Under trust tenure, the federal government holds title to individual Indian lands and to tribal lands and oversees their use. This trust status raises the transaction costs of doing business with tribes and prevents tribes from fully capitalizing on their natural resource wealth.

To see how high transaction costs affect tribes, consider a developer looking to explore for energy resources in an area that includes both reservation and non-reservation land. Where is the developer likely to invest resources? The developer must go through only four steps to drill outside the reservation, compared with 49 steps and four federal agencies to drill on the reservation.<sup>56</sup> Tribes must also acquire approval from the secretary of the U.S. Department of Interior for each lease or agreement,

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<sup>54</sup> Crane-Murdoch, Sierra. 2012. The Other Bakken Boom: A Tribe Atop the Nation’s Biggest Oil Play. *PERC Case Study*. Available at <http://perc.org/articles/other-bakken-boom>.

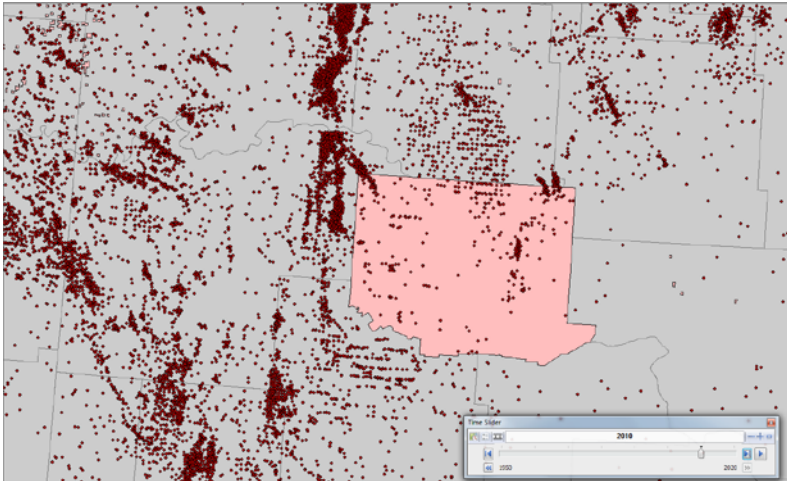
<sup>55</sup> Cornell and Kalt, 2000: 446.

<sup>56</sup> Crane-Murdoch, Sierra. 2012.

a process that is notoriously slow and cumbersome.<sup>57</sup> In addition, the tribal legal and fiscal frameworks may be perceived by the investor as unknown or uncertain.<sup>58</sup> In short, the transaction costs associated with development of tribal lands will likely lead the developer to invest in areas outside of reservations.

The extent to which transaction costs can discourage development on tribal lands can be shown visibly by comparing the amount of energy exploration on and off reservations. The map in Figure \_ shows the number of oil wells on and near the Fort Berthold Reservation in the oil-rich Williston Basin of North Dakota. Twice as many wells are drilled per square mile off reservation than are drilled on the Fort Berthold Reservation, largely due to the relatively high transaction costs of developing energy resources on tribal lands.<sup>59</sup>

### ***Oil Wells On and Near the Fort Berthold Reservation***



<sup>57</sup> See Royster, Judith V. 2008. Practical Sovereignty, Political Sovereignty, and the Indian Tribal Energy Development and Self-Determination Act. *Lewis and Clark Law Review*. 12(4): 1065-1101. See note 71, noting that an agreement on the Fort Berthold Reservation that took “over three years,” and testimony from a Crow tribal member noting “an extremely slow BIA approval process.”

<sup>58</sup> See, for example, Anderson, Terry L. 2013. The Grand Canyon of Property Rights. *Defining Ideas*. Hoover Institution. April 17. Available at: <http://perc.org/articles/grand-canyon-property-rights>.

<sup>59</sup> Regan, Shawn, and Terry L. Anderson. 2013. The Energy Wealth of Indian Nations. Property and Environment Research Center. Available at: <http://perc.org/articles/energy-wealth-indian-nations>.

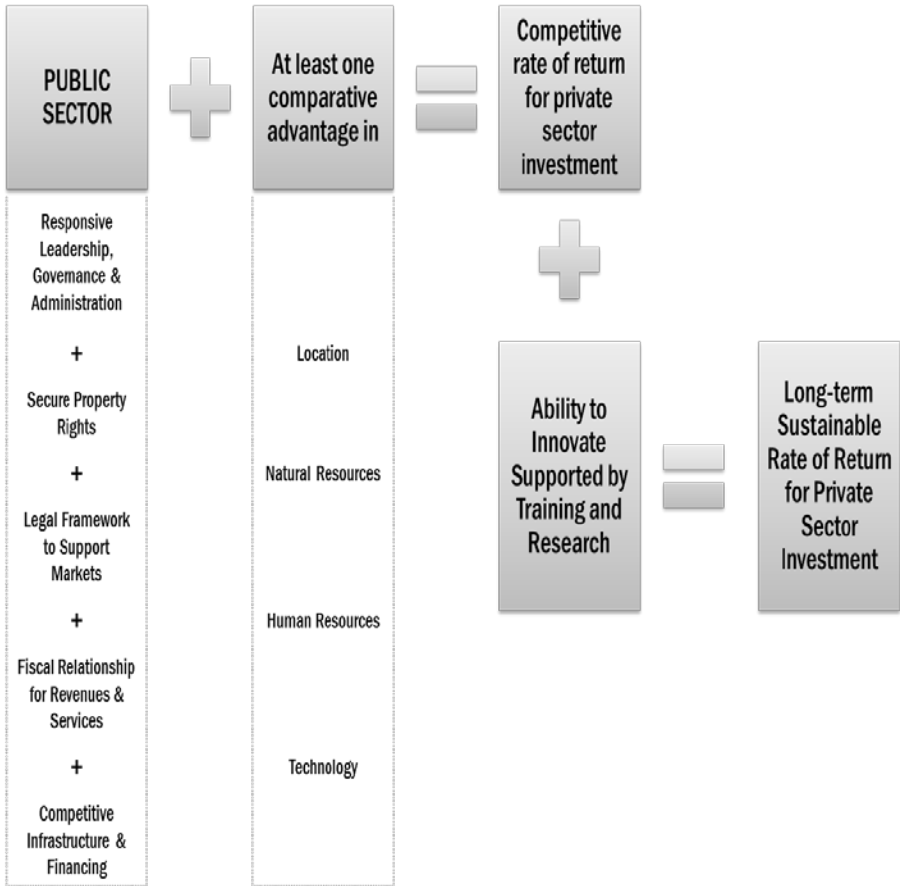
### **The Investment Climate**

The conditions have to be right in order to facilitate private investment. This means that the environment or climate must be accessible and attractive to investors. The transaction costs for investment have to be competitive with surrounding jurisdiction.

The investment climate is a combination of two elements: a public-sector framework and a private-sector comparative advantage:

1. To attract investment through a competitive rate of return, the public sector (government) must be able to provide all of the following:
  - Responsive leadership, governance and administration;
  - Secure property rights;
  - The legal framework to support markets;
  - The fiscal relationship for revenues and services; and
  - Competitive infrastructure and financing.
2. Additionally, a jurisdiction must also possess at least one of the following comparative advantages:
  - A competitive location for markets or technology;
  - A natural resource endowment or access to natural resources;
  - A human resource advantage either in skills, demographics or location; or
  - Competitive access to or ability to use a new productivity-enhancing technology.

*The Investment Climate Equation*



The figure above illustrates the components of a successful investment climate. If a jurisdiction supports innovation in its comparative advantage, the competitive rate of return can be sustained in the long run. Governments can support innovation and the private-sector rate of return through education and basic research support.

Some parts of the investment climate are a product of geography or geology such as access to resources and location. Others are a product of conscious decisions by the public sector. A supportive public sector is therefore a necessary, but not necessarily sufficient, condition for economic development. Investors need cost, service, infrastructure and property ownership certainty. This is what the public sector provides.

The question for First Nations and tribal communities wishing to escape poverty is - what is wrong with their investment climate that prevents more private investment?

Most First Nations and Native Americans have at least one of the following comparative advantages: location, human resources, technological or innovative strengths and access to natural resources. It is important to note, however, that First Nations and tribes that lack some of these comparative advantages are not prevented from achieving economic growth. For instance, possessing access to resources or having a good location is important, but it is not enough to create economic growth. Both Russia and Peru are well endowed with natural resources; indeed, Russia is also well endowed with technology and human resources. However, neither country provides a high standard of living because they have been unable to offer the supportive public sector input that is also required. By contrast, countries such as Singapore and Japan have achieved very high standards of living with relatively poor natural resources. Japan, until the rise of China, was the second largest economy in the world, despite being natural resource poor, by virtue of public institutions that created and supported human and technological advantages. The barrier to prosperity on First Nation and tribal lands is an inability to provide sufficient certainty to investors. The investment climate is the result of an economy's public sector mix of its property right system, legal framework, fiscal relationship, economic infrastructure and economic and governance institutions. These factors are uncompetitive or sub-standard for almost all First Nations and Native American tribes. As a result, a plan to facilitate investment must focus on building a public sector that reduces the transaction costs of investment on their lands. This means diminishing the power of the *Canadian Indian Act* or the U.S. Bureau of Indian Affairs and establishing greater control for First Nations and tribes over themselves. In addition, they must use the powers available to them now to lower the transaction costs of investment.

The following section will describe the appropriate institutional framework for getting the public sector side of the equation right.

### **The Institutional Framework to Facilitate Investment**

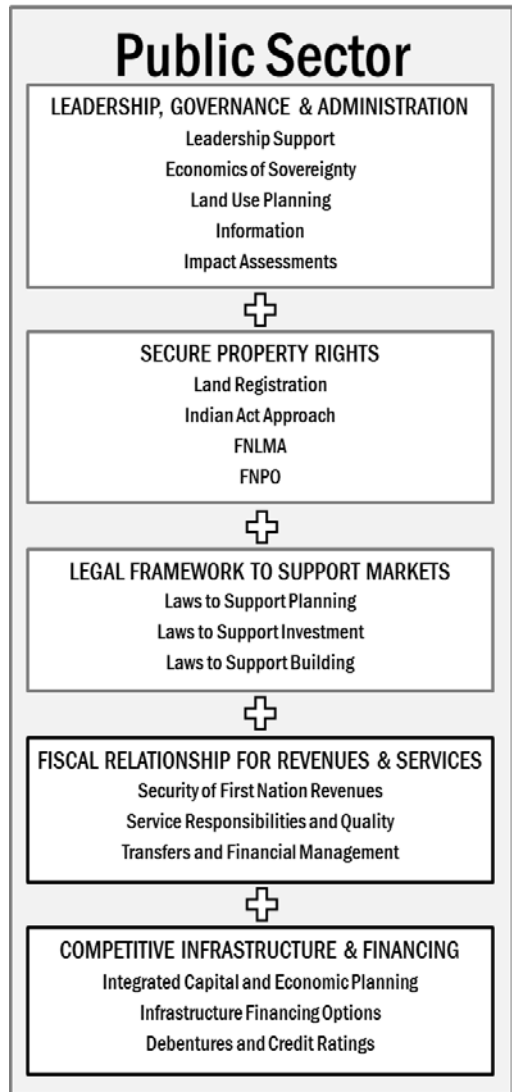
The institutional framework to support investment on First Nation and tribal lands was largely supplanted by the *Indian Act* in Canada and the Bureau of Indian Affairs (BIA) in the United States. The power to raise revenues to build a public sector that supports markets was effectively removed by elements of the *Indian Act* and BIA during the nineteenth and twentieth centuries. The result is that the institutional development of tribes and First Nations has been frozen in time. During the last century, provincial, state and local governments have created supportive investment climates while tribes and First Nations have not. The figure below provides an expanded view of the public sector component of the investment climate equation that is often missing or incomplete for tribes and First Nations.

**Public Sector component of the Investment Climate Equation**

*Secure Property Rights:* Investors need to know the security of their property right to assess its market potential. Different types of developments (commercial or residential) require different types of property rights (rental, lease, fee simple). Chapter 3 describes how to develop appropriate property rights on First Nation and tribal lands using different methods.

*Land Registration:* The legal document assigning title to land is known as a land title, and the system used for the registration of land titles is called a land titles system. The system must make clear if and how a property right is transferred, how ownership is secured with certainty and how ownership is registered, protected and managed. The Torrens registry system is commonly perceived to be superior to the deeds registry system as it does away with the need for a chain of titles to a property. In a Torrens system, the registrar is responsible for assessing the legal validity of the instrument being registered

and the information is recorded in relation to a legally surveyed parcel of land with a distinct identifier. A very important component of a Torrens system is that it provides total security to the person holding the title. If there was a previous example of fraud in a title transfer, the government compensates whoever was defrauded, but the title remains in the name of



the person holding the title. This means that transfer costs are reduced because in a deeds system previous transactions must be examined to be sure the deed is accurate.

*Indian Act Approach:* First Nations' lands are defined as "reserves" under the *Indian Act*. The legal title to reserve land is held by Her Majesty the Queen in Right of Canada, as represented by the Minister of Aboriginal Affairs and Northern Development Canada. Similarly, in the United States, the federal government is the trustee of Indian lands and owns the legal estate in the land. Under this structure, development may not be viable without a proper lease. Chapter 3 will address the land designation process for long-term leasing.

*First Nation Land Management Act (FNLMA):* The *First Nation Land Management Act* is the formal legislation in Canada that ratifies and brings into effect the Framework Agreement on First Nation Land Management. The Framework Agreement provides First Nations with the opportunity to opt out of the land administration sections of the *Indian Act* and to establish their own regimes to manage their lands and resources. A First Nation signatory to the Framework Agreement exercises its land management option by drafting a land code (and enacting associated land management laws). Chapter 3 addresses leasing under an FNLMA land code as it relates to potential investors.

*First Nations Property Ownership (FNPO):* The First Nation Property Ownership initiative has been underway since 2006, led by the First Nations Tax Commission, under the leadership of Chief Commissioner C.T. (Manny) Jules, and supported financially by Aboriginal Affairs and Northern Development. As a result of the proposed *First Nation Property Ownership Act*, First Nations would have the option to replace the existing Crown ownership and include First Nation reversionary rights and expropriation powers. Chapter 3 addresses how this would enable all types of land tenure, including individual fee-simple ownership.

*Legal Framework to Support Markets:* Investors need to know the process that tribes and First Nations follow to approve and amend development plans. Investors need to know what will guide the decisions of tribes or First Nations about future land allocation. Investors need to know about permitted uses for potential development sites and



neighbouring lands. Investors need to be confident that changing future land uses will not reduce their potential profits. Investors need to know about any environmental laws or heritage laws that may impact how the potential investment will proceed. Chapter 4 will address the laws supporting markets.

- *Laws to Support Planning*: Land-use planning is a conception about the spatial arrangement of land uses to guide decisions about current and future land allocation. The process should be integrated with and informed by an economic development strategy. Zoning describes the permitted uses of land within the context of the plan. The development approval process lays out the processes and procedures for planning, reviewing, approving and amending development and subdivision proposals. Laws that provide clear planning, zoning and approval processes give confidence to potential investors.
- *Laws to Support Investment*: An investor code is a legal framework for economic transactions that seeks to encourage, facilitate, and streamline private investment projects through the creation of investor certainty. Potential investors look for certainty about the rules that bind both the First Nation and investors in addition to regulations that make the investment process clear.
- *Laws to Support Building*: Land management laws will make the rules regarding the development, conservation, protection, management, use and possession of tribal or First Nation lands and resources clear to potential investors. Environmental laws provide standards for environmental assessments and methods for environmental management and protection. Construction codes (building codes, fire codes, plumbing codes, and energy codes) regulate the design and construction of new buildings and significant renovation of existing buildings. Heritage laws define heritage areas and sites of cultural interest, provide procedures for managing and protecting them, and provide confidence to potential investors related to any potential impacts heritage matters may have on intended investments.

### **The Fiscal Relationship for Revenues and Services**

Investors need to know which revenues a First Nation or tribe has the power to collect. They need to know how tax rates are determined. They need to know about First Nation or tribal service responsibilities and how quality is assured. It is important for them to know how transfers from other governments influence First Nation or tribal revenues and services. Investors need to know how government finances are reported and managed. Chapter 5 describes these First Nation and tribal fiscal elements in more detail and explains how they can be clarified to improve the First Nation or tribal investment climate.

- *Security of First Nation Revenues:* The more secure and stable a First Nation or tribal revenue source, the better it can be used to provide quality services and infrastructure to support investment. First Nations and tribal governments have a number of revenue options that range from more to less stable and secure.
- *Service Responsibilities and Quality:* It is important that the local government services provided by First Nation and tribal governments have sufficient revenues and are of appropriate scale to ensure competitive service quality can be provided. In this regard, the division of service and financial responsibilities between First Nation-provincial-federal or tribal-state-federal is particularly important to the investment climate.
- *Transfers and Financial Management:* Transfers from other governments to First Nation or tribal governments can close the service quality gap and improve the business climate. The ability of an investor to understand these transfers depends upon the transparency of First Nation or tribal financial reporting and the legal requirements for financial management.

### **Infrastructure and Financing**

Developments require infrastructure and on-going local services. Basic physical infrastructure such as water, sewer, roads and telecommunications are important prerequisites for investment. Investors need to understand the current state of infrastructure and if they can be improved upon easily. They need to know if infrastructure financing is available and how financing options differ from other jurisdictions. They need to know if there is a development cost charge system in place.

Chapter 6 describes the importance of infrastructure as well as how it is built and financed on First Nation or tribal lands.

- *Integrated Capital and Economic Planning:* The First Nation or tribal government's economic development strategy should guide decision making with respect to capital planning. The First Nation or tribal government's financial plan must also support capital planning. These documents must be developed in coordination with one another. First Nation or tribal governments that integrate their capital planning with their economic development planning will improve their stock and quality of infrastructure, and thus, their ability to attract private investment.
- *Infrastructure Financing Options:* Most local infrastructure is financed by a combination of current revenues, savings or reserve funds, payments from developers, transfers from other governments and long-term financing. The legal and economic ability of First Nation or tribal governments to generate these revenues determines their ability to provide investment-grade infrastructure.
- *Debentures and Credit Ratings:* First Nation and tribal governments need to access infrastructure credit at competitive rates so they can obtain infrastructure financing through debentures. This depends on being able to obtain a good credit rating that in turn is dependent upon their fiscal framework.

### **Leadership, Governance and Administration**

Investors need to know the First Nation or tribal government is committed to the economic development of its lands. Investors also need to know the First Nation or tribal government has mechanisms in place to ensure the separation of politics from the administration of government. Chapter 7 will address these elements as they relate to the facilitation of greater private investment.

- *Leadership Support:* Leadership should strive to offer potential investors an attractive investment climate. Chief and Council are responsible for communicating key messages to the market and potential investors to establish a pro-development reputation.
- *Economics of Self-Government:* First Nation and tribal leadership needs to lead and effectively communicate how a strong economy supports community and government objectives.

- *Impact Assessments:* The leadership and administration needs to communicate the public benefits of private investment to the community. This is best accomplished through impact assessments, cost benefit analysis or long-term fiscal plans.
- *Investment Facilitation Strategy:* First Nation and tribal governments must ensure community planning is connected with economic development strategies. Leadership should also communicate how their economic vision will lead to the achievement of the community's economic development objectives.
- *Information:* First Nation and tribal administrations must be able to support and coordinate research and preliminary negotiations and provide technical support to leadership during the development process. They must also provide information to potential investors, such as information about available land, types of tenure, market and demographic data, the approval process and dispute resolution.
- *Integrating Investor Interests into Legal Framework:* Facilitating investment should be a key consideration in the development of the tribal or First Nation legal framework. It is important to be able to advocate for investor interests within First Nation administrations. The investor code is a good example of incorporating investment facilitation into the legal framework.

## **Conclusion**

This chapter is intended to demonstrate two key points. First, private investment is required to grow First Nation and tribal economies but many are not receiving adequate private investment. Second, the lack of private investment on First Nation and tribal lands can be explained because many of the supportive market institutions that they had pre-contact (property rights, legal framework and infrastructure) are now missing or sub-standard. The result is that the transaction costs (the cost of completing an investment) on First Nation and tribal lands are now much higher than they are off their lands. Until these transaction costs are reduced, First Nations and tribes will continue to receive less private investment, have less developed economies and continue to experience

below-average health, education and other social indicators commonly associated with poverty.

In this chapter, we also present the theory that will guide the rest of the book. Transaction costs can be reduced if First Nations establish a competitive institutional framework that includes the following elements orientated towards facilitating investment:

- Property right clarity and property registration security;
- Legal framework to provide certainty for investment, construction and land management;
- A fiscal framework to provide stable revenues and quality services;
- The ability to finance and build business-grade infrastructure; and
- Leadership, governance and administration.

The rest of this textbook describes how to build each element of this institutional framework.



CHAPTER 3

# ESTABLISHING PROPERTY RIGHTS SYSTEMS TO FACILITATE INVESTMENT

Perhaps no issue is more important to indigenous people than property rights. As was discussed extensively in Chapter 1, First Nation and tribal property rights existed before contact. For example, the Iroquois of southern Ontario organized themselves into bounded villages of about four hectares, with populations of 2,000 and palisades of 10m in height.<sup>60</sup> The Acolhua-Aztec of central Mexico demarcated the boundary and calculated the areas of farms within a 10% error range, for purposes of taxation and land redistribution.<sup>61</sup> The Coast Salish peoples of the south coast of British Columbia and Vancouver

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<sup>60</sup> Birch, J. (2010) Coalescence and conflict in Iroquoian Ontario. *Archaeological Review*. v25-n1. p38.

<sup>61</sup> Williams, B.J. & Jorge y Jorge, M. (2001). Surface area computation in Ancient Mexico: Documentary evidence of Acolhua-Aztec proto-geometry. *Symmetry: Culture & Science*. v12-n1. p185.

Island recognized two types of rights in parcels of land.<sup>62</sup> Individuals and extended families through inheritance privately held small parcels, such as root and clam beds, productive fishing spots, and hunting ranges. Larger parcels, such as a strip of coastline or a drainage basin, were held in common by the community for hunting and fishing purposes. These territorial boundaries of parcels used collectively by entire villages were “vigorously defended”. Oral histories are replete with such tales. Indeed, boundary is translated by the words for “marker, index or indicator” and “fence or enclosure”.<sup>63</sup>

*“Almost every First Nations community [in Canada] is located on a reserve, which is a tract of land – usually the size of a postage-stamp – set aside by the federal government for specific bands of Indian people. No one particular Indian person “owns” the land; it is held by the Crown for the collective benefit of everyone in the Indian band. The notion that First Nations lands, which we have occupied since before contact, must now be held by the government on our behalf is both bizarre and insulting.”*

- Ovide Mercredi, 1992.<sup>64</sup>

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<sup>62</sup> Wadewitz, L.K. (2012). The nature of borders: Salmon, boundaries and bandits on the Salish Sea. UBC Press.

<sup>63</sup> Thom, B. (2000). Territory, boundaries and overlapping claims on the Northwest Coast. Proceedings of the 99<sup>th</sup> Annual Meeting of the American Anthropological Association. San Francisco.

<sup>64</sup> Mercredi, O. & Turpel, M.E. (1992). In the Rapids: Navigating the Future of First Nations. Penguin Group: Toronto, Ontario.

*“My people were part of the Canon and Fraser divisions of the Secwepemc. We were known as the greatest traders of our nation before contact. We traded with the Tsilhqot’in and other divisions of the Shuswap for profit. We understood markets and the institutions that support markets like property rights. We had property rights for fishing sites and deer fences. We had inheritance rules to distribute the property of fathers among their children and closest relatives. We fought wars to protect our boundaries and property. Our elders have been seeking ownership of our lands since the 1870s. In 1910, we suggested to the Prime Minister that we would share ownership of our territory on a 50/50 basis. We knew the value of our lands before contact and we continue to understand that value.”*

- Chief Mike Lebourdais, 2014<sup>65</sup>

First Nation and tribal property rights were the basis for wars before and during contact. It is the main subject of numerous treaties throughout Canada and the US. Forty percent of the *Indian Act* in Canada is about lands. Control of land was the basis of the US Indian wars in the late nineteenth century, ultimately relegating Indians to reservations. Even there tribes, such as the Blackfeet, established individual property rights to cattle while herding the land communally. Thereafter, the US government tried to establish private property rights for individual Indians under the *Dawes Act* of 1887, but the ultimate result (and perhaps even the intended one) was a significant transfer of reservation land to non-Indians as private property.

First Nations and tribes appropriately assert their property rights have been unjustly taken from them and they have been working for

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<sup>65</sup> Lebourdais, M. (2014). Band Proposal Seeks to Regain Land Ownership, Restore Value. The StarPhoenix. Available at <http://www.thestarphoenix.com/business/Band+proposal+seeks+regain+land+ownership+restore+value/10193634/story.html>.



centuries to restore them. As a result, property rights continue to be the basis for protests, blockades, legal claims and challenges by First Nations and tribes. There has been some success. For example, the Supreme Court of Canada, in what is known as the William Decision (2014), declared that the Tsilhqot'in had Aboriginal Title (ownership and perhaps jurisdiction) over 1750 km<sup>2</sup> of their traditional territory.

The economic importance of property rights is difficult to overstate. As the world-renowned economist Hernando de Soto phrased it “to not have property rights is to condemn a people to poverty.” Further, in their comprehensive study entitled *Why Nations Fail: The Origins of Power, Prosperity and Poverty* (2012), Acemoglu and Robinson conclude that inclusive institutions, such as individual property rights, supported by the rule of law are the key factor as to why some nation states succeed and others fail?<sup>66</sup>

The desire for land is part of who we are as a species. Evolutionary biologists and cognitive scientists have long asserted that the endowment effect (or divestiture aversion) is innate in all individuals.<sup>67</sup> People value a thing, such as a parcel of land – “it’s mine, I tell you” – more when they have possession than when they do not have possession. There are two explanations. The first holds that strength of the endowment effect is a function of the evolutionary salience of an item.<sup>68</sup> food is valued more than paper, and land is valued more than sewage. The second holds that the effect evolved in the absence of efficient markets. In the absence of a market, you are psychologically predisposed to retain an item that you possess and to hold out for a higher price from a buyer.<sup>69</sup>

This chapter is an introduction to the economics of property rights and how they are a necessary condition to support investment on First

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<sup>66</sup> Acemoglu, D., & Robinson, J.A. (2012). *Why Nations Fail: The Origins of Power, Prosperity and Poverty*. New York: Crown.

<sup>67</sup> The Economist. (June 21, 2008). The Endowment Effect. p.95.

<sup>68</sup> Jones, O.D., & Brosnan S.F. (2008). Law, Biology and Property: a new theory of the endowment effect. *William and Mary Law Review*. v.49 – n.6. p.1935.

<sup>69</sup> Huck, S., Kirchsteiger, G., & Oechssler, J. (1997). Learning to like what you have: Explaining the endowment effect. *Game Theory & Information*. Available at <http://edoc.hu-berlin.de/series/sfb-373-papers/1997-38/PDF/38.pdf>.

Nation or tribal lands. It is divided into seven questions providing a template for what is necessary for First Nations to restore their property rights. Those questions are:

1. What are property rights?
2. What is the relationship between individual property rights and the collective exercise of property rights (also called jurisdiction)?
3. What are the features of property right systems that support economic growth?
4. What is the *Indian Act* regulatory framework for property rights in Canada?
5. What are the types of individual rights under the *Indian Act*?
6. How well does the *Indian Act* System promote economic growth and property values?
7. What are the opportunities to improve the property right systems on First Nation lands?
  - The *First Nations Land Management Act*
  - The *First Nations Commercial and Industrial Act*
  - Modern treaty and comprehensive claim arrangements
  - The Proposed First Nation Property Ownership legislation
  - Aboriginal Title for the Tsilhqot'in

### **Learning Objectives**

The learning objectives for this chapter are:

- Define and describe property rights;
- Explain why it requires both individual rights and an effective regulatory system derived from clear jurisdiction to establish a property right system that facilitates investment;
- List the factors of good property right systems that support economic growth;
- Describe the *Indian Act* individual property right and supporting regulatory framework;
- Analyze the *Indian Act* property right system based on the characteristics of effective property right systems and its impact on property values;

- List the options for creating more market orientated First Nation property right systems; and
- Develop a benefit and risk assessment of each property right system improving option.

### **What are Property Rights?**

Property rights are a bundle of uses and responsibilities defined through a legal and administrative system. When you buy a digital song, you purchase a property right to listen to the song on a limited number of devices as often as you want. You do not have the right to claim the song as your own and sell it. If you do, there could be legal consequences because you exceeded your property rights for this piece of (intellectual) property. This property right allows you to derive value from the song you have purchased and gives the artist an incentive to produce songs.

Property rights are everywhere. We have property rights to tangible objects such as our cars, furniture, income and even pets as well as intangible objects such as intellectual property. Property Rights are the bedrock of all exchange or trade in an economy. Most of us trade our income (or in some cases future income) for property. Property rights make economic gains from trade possible.

For the purposes of this textbook, we are mainly interested in the property rights for land and structures on that land. In this context, property is a bundle of rights governing the use of land. At first glance, property rights seem to apply to lands or things that are owned, but in fact, they apply to human conduct. Hence, by itself land has no economic value, which means that value is created by the worth people place on the land for either productive or aesthetic purposes. Property rights establish what owners can do and what non-owners cannot do, under threat of retaliation from owners or enforcement by the governing authority.

There are three big sticks in the bundle known as property<sup>70</sup>: the right to exclude others from the parcel, and the right to use the parcel, the right to dispose of the parcel. The owner of land in fee simple (known as a freehold estate) can exercise all these rights within certain limits (e.g.

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<sup>70</sup> Epstein, F. (2008). *Supreme Neglect: How to Revive Constitutional Protection for Private Property*. New York: Oxford University Press. p. 20.

your spouse has certain rights to your estate, and you cannot knowingly rent your property for criminal purposes); but other forms of ownership has restrictions.

*Exclusion* – If you own a home, you can decide whether to let someone in the door or not, but you cannot exclude the police with a search warrant. Or, if you own a farm, you can exclude other farmers from plowing your land; but you cannot stop a municipality from using eminent domain to use a corner of a field for the widening of a road. If you do not pay your property taxes, you cannot exclude the government from taking your land and selling it to someone who will pay their property taxes. Therefore, the right to exclude is never absolute; it is qualified by the government's power, which includes protecting your rights and ensuring that you exercise your rights in ways that do not harm other individuals or the general public.

*Use* – Land use can mean simply the right to be present, construct a building or plant crops to farm, but it also includes other rights (i.e. the right of a condominium owner to use the complex recreation centre). It can also mean the right to extract resource units, as in the case of a fishing club member. Or it could mean the right to receive a share of the profits, as in owning stock in a corporation. Still another dimension of use is the right to manage or share in the management of the property.<sup>71</sup>

*Disposition* – Permanent disposition can take place by sale, gift or inheritance, while temporary disposition involves leasing or renting to others for their use.

### **What is the relationship between individual property rights and collective (jurisdiction) property rights?**

Most people are familiar with individual residential property rights. They can be in their homes as a renter or a lessee or as an owner with

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<sup>71</sup> Eggertsson, T. (2003). "Open Access versus Common Property." In Anderson, T.L. & McChesney, F.S. *Property Rights: Cooperation, Conflict, and Law*. Princeton University Press. p 74.

indefeasible or fee-simple ownership<sup>72</sup>. Most people also recognize the hierarchal nature of individual property right values based on the security and length of the tenure associated with the property right. Usually renting is less valuable than leasing which is less valuable than fee simple in the context of residential properties.

However, as Hernando de Soto has observed, we take for granted the legal, governmental, and fiscal framework that supports individual property rights. When this support system is absent, as with many First Nations and tribes, the result is high transaction costs. This is because the buyer and seller must create these rules for themselves. It is no coincidence, therefore, that the costs of completing a real estate transaction on some of the best-located First Nation lands in Canada are high, as was discussed in the previous chapter.

*“The effect of insecure property rights is evident on a drive through any western reservation. When you see 160 acres overgrazed and a house unfit for occupancy, you can be sure the title to the land is held by the federal government bureaucracy. In contrast, when you see irrigated land in cultivation with farm implements, a barn and well-kept house, you can be sure the land is held in fee simple, whether by an Indian or non-Indian.”*

- Terry L. Anderson, William A. Dunn  
Distinguished Senior Fellow at the  
Property and Environment Research  
Centre (PERC)<sup>73</sup>

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<sup>72</sup> According to Flanagan, T., Alcantara, C., & Le Dressay, C.A. (2010). *Beyond the Indian Act: Restoring Aboriginal Property Rights*. McGill-Queen's University Press, “most extensive [land tenure] and allows the tenant to sell or to convey by will or transfer to the tenant's heir upon death intestate. In modern law, almost all land is held in fee simple. This is as close as one can get to absolute ownership in common law. Legal fiction, indeed, because the owner in fee simple can do what he or she pleases with the land including sale to another and the ability to pass it on to next-of-kin ad infinitum.”

<sup>73</sup> Anderson, T.L. (2009). *Native Americans Need the Rule of Law*. The Wall Street Journal. Available at <http://online.wsj.com/articles/SB123716186521735641>.

One of the limitations on property rights on some First Nation and tribal lands is “collective ownership.” Collective ownership makes it difficult or impossible to dispose of rights in a market framework because consent is necessary either from every owner or from the band or tribal government with the legal status to represent all of the owners. Collective ownership can arise from three sources. First, the collective holds some rights because it held underlying title and did not transfer all rights of ownership to individuals who occupy it. Second, in some cases, the term “collective ownership” is used to define a trust relationship where leaders in a government are responsible to ensure the property is used for the benefit of its members. Third, other times the term “collective ownership” is not really defined and may really refer to a situation where a government has jurisdiction to regulate the property.

A special problem that may arise when property rights are collective is that there may be many individuals involved, including people who inherit rights from original holders and may not reside on or near the property.<sup>74</sup> Two problems can result from group or collective ownership. The first is the free rider problem who let the others do the work to manage and raise the property value but demand their share of the benefits.<sup>75</sup> The second is the holdout who disagrees with the other owners. Holdouts and free riders can prevent the property from being used efficiently, including the overuse of natural resources and the prevention of market transactions (transactions where members of the group would benefit from leasing or even transferring the property to a purchaser).

Whether property rights are held collectively or individually, property rights by themselves are insufficient to create property value. Property rights must co-exist with a legal system that clearly defends and specifies the uses of the property. Most off-reserve individual property

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<sup>74</sup> This problem is particularly acute in some First Nations. This is evidenced by situations such as those experienced by the Mohawks from Kahnawake, just south of Montreal, Quebec, whereby there are a large amount of heirs for some properties and homes. It has been claimed that in some cases heirs, and subsequently those with an interest in the property, are in the thousands. Parliament of Canada. (2012). *Standing Committee on Aboriginal Affairs and Northern Development*. N.032, 1<sup>st</sup> Session, 41<sup>st</sup> Parliament. Available at <http://www.parl.gc.ca/HousePublications/Publication.aspx?Language=E&DocId=5499882>.

<sup>75</sup> It should be noted that collective regulation and other means can be used to overcome free rider problems.

rights in Canada are governed by local government rules such as zoning, building codes, property taxation and provincial rules associated with property rights, surveying, and registration of land interests. These rules must be stable and predictable.

Few First Nations have the legal and administrative framework to support effective property rights. As de Soto points out in his book, *The Mystery of Capital: Why Capitalism Triumphs in the West and Fails Everywhere Else* (2000)<sup>76</sup>, it is not the lack of individual ownership that causes poverty in much of the world, it is the absence of the legal and administrative framework to support those rights. This is particularly important for First Nations and tribes wanting to create competitive investment climates. Providing better individual property rights is insufficient. They must also restore their collective jurisdiction in order to implement a regulatory framework that provides sufficient investor certainty to facilitate trade and increase property values. Moreover, First Nations and tribes must maintain their jurisdiction regardless of whether property is owned collectively or owned individually by members or non-members of the band or tribe.

Individual property rights are ineffective without the structure of law about who owns what. From this, capital can then be created, investment facilitated and property values boosted. These rights are essential in utilizing assets to their full potential and generating sustainable economic development. The strength of an economy's property rights fundamentally underlies its prosperity and success. As de Soto puts it, "Creating the rule of law [to support property rights] is, of course, not a silver bullet. Development is very complex, like life itself. You've got education that's involved, you've got health that's necessary, you've got enforcement that is all part of it. But if you do not have an order that tells you who owns what, who is where, and who is accountable for what, none of the rest works."<sup>77</sup>

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<sup>76</sup> De Soto, H. (2000). *The Mystery of Capital: Why Capitalism Triumphs in the West and Fails Everywhere Else*. New York: Basic Books.

<sup>77</sup> De Soto, H. Property Rights & Rule of Law. Poverty Cure. Available at <http://www.povertycure.org/voices/hernando-de-soto/>

### **How do property rights support economic growth?**

The essence of a market is the exchange of property rights. If property rights are poorly described or incomplete, even the most basic transactions become onerous the creation of value through markets becomes limited. There is no such thing as money or capital without property rights and clear and stable rules to create them. Houses without ownership rights that are ineffectively recorded cannot readily be turned into capital, traded or sold outside of narrow local circles. They cannot be used as collateral for a loan or used as a share against investment. Poorer communities may possess the resources, but unless they have a property system with clear and stable rules, their assets will be dead capital.<sup>78</sup>

Conversely, in communities where every piece of land, equipment and structure is legally documented, an unseen process that connects these assets to the rest of the economy is established. As such, assets can appreciate, be used as collateral, and be readily tradable. They can also provide a link to the owner's credit history, provide an accountable address for the collection of debts and taxes, provide the basis for the creation of reliable and universal public utilities, and establish a foundation for the creation of securities that can be sold in secondary markets.<sup>79</sup>

Without property rights and stable governments, tribes and First Nations forgo both foreign and domestic investment. Foreign investment originating from outside their communities is deterred by the high transaction costs associated with establishing effective property rights (long-term tenure). Domestic investment by members of tribes and First Nations is lost because of high transaction costs. Their homes and property assets have no equity so they usually cannot access capital without a third-party guarantee for the loan. Further, in regards to off-reserve Canadian businesses, the most common collateral used to start a

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<sup>78</sup> De Soto, H. (2000). *The Mystery of Capital: Why Capitalism Triumphs in the West and Fails Everywhere Else*. New York: Basic Books.

<sup>79</sup> *Ibid.*



business is home equity.<sup>80</sup> As such, a lack of clear property rights to homes on First Nation lands limits home equity and therefore limits the formation of businesses.

*Under the Indian Act, the title to our land is held by the Crown. My home - just like all homes on Indian reserves - is owned by Canada and controlled by the Minister of Indian Affairs. I paid \$150,000 in mortgage payments for my home on reserve, but it has no value. I can't use the equity in my home to start a business, support my kids in university or support my retirement. "*

- Chief Mike Lebourdais<sup>81</sup>

Poorly defined or non-existent property rights breed uncertainty and deter the necessary investment required for development and growth. The result is undercapitalized resources, lack of opportunity, and poverty. According to de Soto, there are six essential affects that communities with inadequate property rights fail to realize:

1. *Knowing the Economic Potential of Assets* – Good property right systems make property values clear and allow these property values to be used in possible transactions. The market value matters in a home equity loan for example. On many First Nation lands, it is impossible to determine the market value of an asset.
2. *The Integration of Dispersed Information* – Property right registry systems that provide information about ownership/use facilitate easier asset evaluations and exchanges. It provides the easy measurement of an asset's attributes that significantly reduces transaction costs related to moving and comparing assets. This is

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<sup>80</sup> Approximately 75% of business startups utilize savings, credit or home-equity financing in Canada. Weaver, R. (2013). Five Tips to Help Startups Maximize their Chance of Financial Success. Tech Vibes. Available at <http://www.techvibes.com/blog/five-tips-startups-financial-success-2013-10-02>.

<sup>81</sup> Lebourdais, M. (2014). *Band Proposal Seeks to Regain Land Ownership, Restore Value*. The StarPhoenix. Available at <http://www.thestarphoenix.com/business/Band+proposal+seeks+regain+land+ownership+restore+value/10193634/story.html>.

difficult to accomplish on First Nation lands because the dispersed information about property rights has not been integrated in a manner that is comparable to other similar assets on or off First Nation lands.

3. *Accountability* – Well-defined property rights facilitate contracts between strangers by establishing that each party has “something to lose” if the contract is not adhered to. It creates commitments that protect the parties involved and establish trust. “People who do not pay for goods or services they have consumed can be identified, charged interest penalties, fined, embargoed, and have their credit ratings downgraded.”<sup>82</sup>
4. *Fungible Assets* – Sound property rights allows assets to be used and adapted to produce continually higher valued combinations based on any economic circumstance. This means standard property descriptions, whereby anyone who wants to buy, rent or give credit against an asset does not have to expend enormous resources comparing and evaluating it against other assets. This allows assets to be split up and combined in many different ways.
5. *Networking* – Strong property right systems using a stable, reliable land registry system establishes a network where all property records are continually tracked and protected. The legal property system is essentially the center of the connections between citizens, governments and the private sector. This networking allows for the adequate and accurate provision of utilities and other services and easier bill collection.<sup>83</sup>
6. *Transaction Protection* – Modern property right systems allow individuals to provide secure transactions for large and small assets. This is illustrated by de Soto in his example regarding the trading of pigs, “in developing and former communist nations people are still taking their pigs to market and trading them one at a time... in the West, traders take representations of their rights over pigs to the market. Traders at the Chicago commodities exchange, for example, deal through representations, which give them more information

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<sup>82</sup> Ibid.

<sup>83</sup> Ibid.

about the pigs they are trading than if they could physically examine each pig.”<sup>84</sup>

### **What is the property right regulatory system under the *Indian Act*?**

Most First Nations do not own the reserves on which many of their people live. According to section 91(24) of the *Constitution Act (1867)*, Parliament has jurisdiction over “Indians, and Lands reserved for the Indians.”<sup>85</sup> The *Indian Act* further specifies that reserves are held by Her Majesty for the use and benefit of the bands for which they were set apart, and subject to this Act and to the terms of any treaty or surrender, the Governor in Council may determine whether any purpose for which lands in a reserve are used or are to be used is for the use and benefit of the band.<sup>86</sup>

“Her Majesty” does not refer to the Queen as a person; it refers to the Canadian government. Subject to the terms of the *Indian Act* and of any treaty or land surrender, the federal cabinet (“the Governor in Council”) has authority over the use of the reserves, but it has to be “for the use and benefit of the band.” This is somewhat similar to the trust relationship that is created when a person dies and leaves property to a minor heir who is not yet old enough to manage the inheritance. A trustee will be appointed to manage the property until the heir becomes an adult. The trustee has authority to make decisions, but they must be for the benefit of the heir.

The *Indian Act* has a number of regulatory sections relating to lands and environmental management. It also provides for measures relating to estates and the creation of some individual property interests (described below). The trust relationship requires that the federal bureaucracy (the Department of Aboriginal Affairs) oversee and in some cases administer land regulation for First Nations.

Prior to the 1990s, First Nations were restricted to managing land interests at the band level via informal/customary allotments, legally

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<sup>84</sup> Ibid.

<sup>85</sup> Government of Canada. (2014). *Constitution Act, 1867*. Justice Laws Website. Available at <http://laws-lois.justice.gc.ca/eng/const/page-1.html>.

<sup>86</sup> Government of Canada. (2014). *Indian Act, 1985*. Justice Laws Website. Available at <http://laws-lois.justice.gc.ca/eng/acts/i-5/>.

recognized land interests under the *Indian Act*, and a delegated land management responsibility under s. 53 & 60 of the *Indian Act* (an option that very few First Nations participated in).<sup>87</sup>

Legal interests under the *Indian Act* are registered in the Indian Land Registry System (ILRS). At present, there are over 100 different instrument types comprising some 400,000 documents in total. The instruments range from common documents like liens, leases, mortgages and quit claims to lesser-used documents such as ministerial loan guarantees and sub-sub-subleases. The ILRS serves as a repository of information. It is not a modern land registry where property interests are linked with other databases to make assets marketable, measurable or fungible or to protect transactions. Further, it does not facilitate the desirable property right features suggested by de Soto.

### **What are individual property rights under the *Indian Act* in Canada?**

There are three types of individual property rights possible under the *Indian Act*.

1. *Customary allotments* – Informal interests are generally referred to as “customary allotments” and individuals (or families) come to hold these rights through “occupation, community recognition, or inheritance”.<sup>88</sup> Historically, these rights were not recorded in a centralized repository but relied on oral histories and community recognition to keep track of ownership. This is still the case today on many reserves. The Canadian courts have been very reluctant to recognize any level of informal interest that is not (at the very least) allotted by the Band Council.<sup>89</sup>

Much of what we know of customary allotments on First Nation reserves is anecdotal. Customary allotment systems run the gamut from bare recognition to high levels of formalization. As examples of this spectrum: the Sandy Lake First Nation of Ontario have almost

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<sup>87</sup> There were few self-government discussions pre-1990 (e.g. *James Bay & Northern Quebec Agreement*).

<sup>88</sup> Flanagan, T., & Alcantara, C. 2003. Individual property rights on Canadian Indian reserves. *Queen's LJ*, 29.

<sup>89</sup> Canadian Case Law. (2000). *Lower Nicola Band v. Trans-Canada Displays Ltd.* 4 CNLR 185 (BCSC). Available at <http://caselaw.canada.globe24h.com/0/0/british-columbia/supreme-court-of-british-columbia/2000/08/10/nicola-band-et-al-v-trans-can-displays-et-al-2000-bcsc-1209.shtml> and *Mathias et al. v. Findlay* 4 WWR 653 (BCSC). 1978.

no formalization of customary allotments – they are recognized by the community but allotments are not documented through a Band Council Resolution (BCR), nor do they have any dispute resolution system in place; the Cowichan Tribes of British Columbia also don't take any steps to documenting customary allotments but do have a non-political dispute resolution body made up of elders; and the Siksika Band in Alberta has customary allotments “recognized by the community, allotted to members through a BCR, surveyed, recorded in a registry, and are subject to a non-political dispute resolution body”.<sup>90</sup>

2. *Certificate of Possession* - By far the most used legal interest under the *Indian Act* is a certificate of possession (CP). A CP is generally considered the strongest form of property right an individual can hold on an reserve: it can be subdivided, sold (to another band member), leased to off-reserve residents or corporations under s. 58(3), transferred to an heir, and Canadian courts will hear and settle disputes related to them. The most recent estimate is that over 145,000 CPs have been issued on over 300 reserves<sup>91</sup>; of which some 55,000 are currently valid.

While the legal defensibility of a CP makes it a much more securely held property right, it still falls short of a fee simple estate (the norm off-reserve). For example, mortgages under a CP require First Nation or government guarantees as the land is immune from seizure; the CP cannot be transferred to non-First Nation members; and if a CP holder ceases to be entitled to reside on the reserve, they have six months to transfer their right to possession to another member or it reverts automatically to the First Nation. The extent of CP use varies across the country: some reserves have no CPs, some no longer allow CPs, and some (such as the Six Nations reserve in Ontario) have over 10,000 CPs. Additionally, CPs can have high transaction costs. Like customary allotments, both the band council

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<sup>90</sup> Flanagan, T., & Alcantara, C. 2003. Individual property rights on Canadian Indian reserves. *Queen's LJ*, 29.

<sup>91</sup> Alcantara, C. (2003). Individual Property Rights on Canadian Indian Reserves: The Historical Emergence and Jurisprudence of Certificates of Possession. *The Canadian Journal of Native Studies* 23.

and the Minister of Aboriginal Affairs and Northern Development Canada (AANDC) must approve CPs. The process of applying and navigating all the administrative approvals has been documented to take anywhere between 6 months and 11 years.<sup>92</sup>

3. *Leases* - Section 38(2) of the *Indian Act* allows a First Nation to “conditionally surrender” or “designate” parcels of land to the Government of Canada for leasing purposes. A designation does not extinguish the underlying First Nation interest and it must be assented to by a majority of First Nation members eligible to vote. Following a successful designation, the federal government (on behalf of the band) can lease the land to third parties.

Leasing under the *Indian Act*, however, differs substantially from off-reserve leasing in at least three capacities. First, the level of approval needed is substantially greater. As examples: for designations, the majority of eligible voters must agree to the proposed lease area; for leases on CP held land under s. 58(3), the Minister of AANDC must approve it. While Band Council approval is not required under 58(3) the courts have held that the Minister must not approve leases on CP lands that conflict with concerns of the band.<sup>93</sup> Likewise, the Minister cannot refuse leases on CP land for not complying with policy requirements. The Canada Human Rights Tribunal has ordered that AANDC must accept “that a mentally competent, adult Indian...proposed lease is in that individual’s best interest”, to not to so would be “paternalistic” and “discriminatory”.<sup>94</sup>

Second, leases on designated land are managed by AANDC, not the band council. This has created problematic situations like the conflict between the Musqueam First Nation of British Columbia and

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<sup>92</sup> Alcantara, C. (2005). Certificates of Possession and First Nation Housing: A Case Study of the Six Nations Housing Program. *Canadian Journal of Law and Society* 20, 183-205.

<sup>93</sup> Office of the Commission for Federal Judicial Affairs Canada. (2000). *Tsartlip Indian Band v. Canada (Minister of Indian Affairs and Northern Development)*, 2 FC 314. Available at <http://reports.fja.gc.ca/eng/2000/2000fc25588.html>.

<sup>94</sup> *Louie and Beattie v. Indian and Northern Affairs Canada* CHRT 2. 2011.

AANDC where the former wanted the latter to “enforce the terms of its leases against tenants who had defied the rent review provision”.<sup>95</sup>

Third, as the Supreme Court of Canada identified, reserve lands have a tendency to be valued substantially lower than off-reserve equivalents. At Musqueam, leases on reserve were valued at 50% of equivalent off-reserve land due to “uncertainty related to property taxation, publicized unrest, and limitations on non-natives’ entitlement to stand for election to the reserve’s governing body”.<sup>96</sup>

Kesselman (2000) echoes this view, noting that non-aboriginal resident leaseholders feel left out of the decision making process as they “lack the channels for participation, influence, and restraint that are conventional in institutions for democratic governance”.<sup>97</sup>

### **What are the perils of informal interests (customary land-holdings)?**

Leonard and Mary Anne Johnstone were members of the Mistawasis First Nation in Saskatchewan. They had been farming on the reserve since about 1960. In that period, they acquired control of 33 quarter sections of land, more than one-sixth of the 192 quarter sections on the reserve. They held 13 of these quarters under CP issued by the Minister of AANDC, while the other 20 were “ad hoc” or “customary” holdings approved by BCR at various points in the past. For about ten years (1986-96), they also had a “Certificate of Right of Use and Occupation” for 17 out of 20 of these customary quarters, issued by AANDC so that the Johnstone’s could borrow money from the Farm Credit Corporation; but these certificates were temporary in nature, not permanent like Certificates of Possession:

“The Johnstones improved, maintained, nurtured and sustained the lands in their occupation and possession. The applicants have given their whole lives to nurturing the land. They have picked roots, cleared stones,

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<sup>95</sup> Flanagan, T. & Alcantara, C. (2004). Individual Property Rights on Canadian Indian Reserves. *Queens Law Journal* 29.

<sup>96</sup> Judgments of the Supreme Court of Canada. (2000). *Musqueam Indian Band v. Glass* SCR 633. Available at <http://scc-csc.lexum.com/scc-csc/scc-csc/en/item/1816/index.do>.

<sup>97</sup> Kesselman, J.R. (2000). Aboriginal Taxation of Non-Aboriginal Residents : Representation, Discrimination, and Accountability in the Context of First nations Autonomy. *Canadian Tax Journal* 48, 1525.

fenced, drained and nurtured piece by piece, quarter by quarter, bush by bush, pasture by pasture, slough by slough to create a farming environment which would be an all-encompassing economic, family and community lifestyle.”<sup>98</sup>

Notwithstanding this decades-long investment by the Johnstone family, the Mistawasis Band Council decided in 2002 to take back the 20 customary quarters. The Johnstones applied to the Court for an interlocutory injunction to block the reversion, but lost. Justice Barclay held that “it is clear that the proper approval of the Minister, or his lawful designate, was never acquired with respect to the 20 quarter sections of land in issue”.<sup>99</sup> The Johnstones might have a claim for financial damages, he allowed, but that could be litigated later, and meanwhile the reversion of the land could proceed. This is the kind of uncertainty that reduces the incentives to improve land so it contributes to economic development.

### **How well does the *Indian Act* property right system promote economic growth?**

There is little evidence that the *Indian Act* property right system was intended to support economic growth. In fact, there is historical evidence to suggest the purpose of the *Indian Act* property right system was to prevent economic growth. First, individual property rights were not granted to First Nations because they were not considered responsible enough to use it in their best interest.<sup>100</sup> Second, the land management

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<sup>98</sup> Canadian Case Law. (2003). *Johnstone v. Mistawasis*, SKQB 240. Available at <http://caselaw.canada.globe24h.com/0/0/saskatchewan/court-of-queen-s-bench-for-saskatchewan/2003/05/23/johnstone-v-mistawasis-first-nation-2003-skqb-240.shtml>.

<sup>99</sup> *Ibid.*

<sup>100</sup> “The Bagot Commission documented a case in where the Mississauga [of New Credit] had wanted ‘to obtain from Her Most Gracious Majesty, the Queen, a written assurance or Title Deed, securing to them....forever’ their rights to land in which they had already made improvements. Their position was backed by Wesleyan Missionaries. However, General Samuel Jarvis opposed the move. If alienable titles should not be given to any one [Indian], it would be difficult to avoid the necessity of conferring them on all. The majority are decidedly unfit to receive them, and would most clearly comprehend the propriety of their being withheld, or of a distinction being made. Those who are not competent to receive Titles might entertain a desire to dispose of them and how provident however they may be, they may become subject to prosecution.”



intent was to maintain First Nations as wards of the state.<sup>101</sup> Third, the land registry system was not intended to facilitate transactions or provide security to investors.<sup>102</sup> The result is a centralized federal bureaucracy that manages the collective property rights associated with First Nation lands, there are few tradable individual property rights and the land registry provides little security or certainty to lenders and investors. The table below evaluates the *Indian Act* property rights system using the features of successful property right systems defined by Hernando de Soto.

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This excerpt is from the Treaties and Treaties and Historical Research Centre. (1978). *The Historical Development of the Indian Act*. P.R.E Group, Indian and Northern Affairs. Available at [http://www.kitselas.com/images/uploads/docs/The\\_Historical\\_Development\\_of\\_the\\_Indian\\_Act\\_Aug\\_1978.pdf](http://www.kitselas.com/images/uploads/docs/The_Historical_Development_of_the_Indian_Act_Aug_1978.pdf).

<sup>101</sup> Deputy Superintendent-General Vankoughnet's memorandum on 22 August 1876 at the time the Indian Act was drafted, "The legal status of Indians of Canada is that of minors, with the Government as their guardians." This is from Treaties and Historical Research Centre. (1978). *The Historical Development of the Indian Act*. P.R.E Group, Indian and Northern Affairs. Available at [http://www.kitselas.com/images/uploads/docs/The\\_Historical\\_Development\\_of\\_the\\_Indian\\_Act\\_Aug\\_1978.pdf](http://www.kitselas.com/images/uploads/docs/The_Historical_Development_of_the_Indian_Act_Aug_1978.pdf).

<sup>102</sup> The ILRS is created by seven words in the *Indian Act*. There are no accompanying regulations or connections to other legislation for the ILRS. Land registry and title systems in provincial jurisdictions are significant pieces of legislation with accompanying regulations and are connected to upwards of 50 other pieces of legislation.

***Indian Act Property Rights System Evaluation***

Property Right System Attribute	Indian Act Evaluation	Consideration/Caveat
Asset economic potential evaluation	Land and property value difficult to determine  Some leases connected to assessed value but not available in ILRS	Land registry and property tax connection possible but not developed yet.
Integration of information	ILRS not integrated with other information common in provincial systems  Survey information becoming more available	Difficult to integrate without regulations and legislation.
Accountability	Indian Act prevents use of collateral in loans  Many loans requires third-party guarantees	Some leases have created more accountability
Asset Fungibility	Difficult to combine property assets owing to poor information integration, missing accountability etc.  More difficult to assess First Nation credit	Leases provide more options
Networking	Property information is not networked into many other systems  Utilities less common on First Nation land	Requires legislation and regulations
Transaction Protection	Few examples of individual property combined with other properties for significant investments	Possible with leases under Indian Act

The *Indian Act* property right system does not support investment. It does not provide secure and tradable individual property rights for members to access capital (with the exception of leases in some cases). It does not provide sufficient regulation to provide investor certainty. It

does not integrate information through a modern registry to reduce transaction costs. The results are predictable – high transaction costs (see Chapter 2) and the socio economic indicators of poverty.

Nonetheless, there has been successful *Indian Act* development thanks to the innovation of First Nations and a number of policy and legal technicians. The Osoyoos Indian Band successfully runs a luxury resort with a hotel, golf course, RV park, spa, cultural centre, and winery. The tourism revenue alone at Osoyoos is estimated to be \$40M annually and employs 1200 people.<sup>103</sup> Likewise, the Wendake First Nation of Quebec runs a four star hotel and museum on-reserve that employs roughly 300 people.<sup>104</sup> The Blood Tribe of Alberta runs agricultural leases on much of 200,000 acres currently under cultivation, including a 20,000-acre state of the art irrigation project – one of the largest of its kind in Canada.<sup>105</sup> The Tk'emlups te Secwepemc has also developed a large successful golf resort residential development under the *Indian Act*. These examples represent the exception and not the rule.

### **What is the impact of the *Indian Act* on Individual Property Values?**

The impact of the *Indian Act* on the market values of CPs and informal holdings has never been estimated, but two facts suggest that the value is low. First, in most cases the markets for these types of individual property rights is tiny as they can only be sold or transferred to another band member. When there is restricted demand, market values are low. Second, in almost all cases banks will not provide loans using these interests as collateral because the *Indian Act* legally restricts them from seizing and selling the asset in the event of default. Moreover, their market value for security is low anyway. There is also some anecdotal

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<sup>103</sup> Aboriginal Affairs and Northern Development Canada (AANDC). 2011. *A taste of success: Nk'Mip Cellars, Osoyoos, British Columbia*. Available at <https://www.aadnc-aandc.gc.ca/eng/1311873422517/1311873529478>.

<sup>104</sup> Aboriginal Affairs and Northern Development Canada (AANDC). 2010. *Tourism in Wendake First Nation, Quebec*. Available at <https://www.aadnc-aandc.gc.ca/eng/1100100014517/1100100014523>.

<sup>105</sup> Blood Tribe Agricultural Project (BTAP). 2012. *An Agri-business Opportunity: 2012 Prospectus*. Available at <http://www.btap.ca/prospectus.pdf>.

evidence from actual sales of CPs to suggest that their market value is significantly less than 50% of their fee simple value.<sup>106</sup>

There has, however, been a legal case that provides an estimate of the *Indian Act's* impact on leaseholds. Musqueam Indian Band in Vancouver surrendered 40 acres of land for leasing in 1960. The Crown in turn leased the land to a development company, which subdivided the land and sold 99-year leases to individuals who subsequently built houses. Contained in the leases was a rent review clause stating that after the first 30 years and every 20 years thereafter, annual rent would be re-assessed at 6% of the current land value. The dispute was over the method of determining the “current land value” of reserve land designated for long-term lease. The trial court held that designated land remained Indian land, and that such land must be valued in terms of a leasehold interest rather than freehold. The court also considered that the unique nature of Indian land would have an effect on its current value; meaning that the value of the land in question should be reduced by 50% as compared to similar property in the City of Vancouver.

The Supreme Court of Canada agreed with assessing a 50% reduction in value for these particular lands. The restrictions on sale and use that come with being reserve land, coupled with the power of the band council to levy property taxes and to pass by-laws such as zoning laws, reduce the current value of designated land:

“The value of a hypothetical interest in fee simple ownership on the reserve must reflect the legal restrictions on land use, as opposed to restrictions found in the lease, and market conditions. Like municipal zoning, restrictions on land use imposed by a band can either increase or decrease land value depending on how the market responds to them. Since the legal environment on a reserve must be taken into account

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<sup>106</sup> See Fiscal Realities Economists. (2007). *The Financial Impact of Effective Real Estate Markets on First Nation Lands*. Available at [http://www.tulo.ca/docs/apec163\\_m1\\_financial\\_impact\\_of\\_effective\\_fn\\_real\\_estate\\_markets.pdf](http://www.tulo.ca/docs/apec163_m1_financial_impact_of_effective_fn_real_estate_markets.pdf) and Flanagan, T., & Alcantara, C. 2003. Individual property rights on Canadian Indian reserves. *Queen's LJ*, 29.

when appraising land value, fee simple off-reserve value cannot simply be transposed to the Musqueam lands.”<sup>107</sup>

Property rights can be held by individuals, by groups such as partnerships, trusts or corporations, by communities such as First Nations or municipalities, or by provincial or federal governments (Crown land). From the point of view of outside investors, it does not matter very much whether land is owned by individuals, partnerships, corporations, or governments, as long as the owner is in effective control and is able to negotiate legally enforceable agreements for use of the land. Oil companies are happy to purchase drilling rights from the Government of Alberta, where the Crown owns most mineral rights. Housing developers will lease land from the band council on at Tk'emlups te Secwepemc or from owners of CPs on the Westbank First Nation, as long as they can negotiate enforceable agreements.

What tends to discourage or even drive away investment (and thus lower property values) is risk due to uncertainty, which can take various forms:

- *Disputes Over Title* – An investor, renter or buyer has to know with whom to deal.
- *Multiple levels of control* – Some rights on reserves must be approved by various authorities – members, community as a whole (through referendum), Chief and Council, Minister of AANDC – leading to delays.
- *Unpredictable law enforcement* – Disputes are inevitable; investors merely crave impartial adjudication. Some tribes in the United States have their own tribal courts, but tribes that agree to be bound by state courts do better economically because investors are reluctant to put their fate in tribal courts.<sup>108</sup>

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<sup>107</sup> Judgments of the Supreme Court of Canada. (2000). *Musqueam Indian Band v. Glass*, S.C.R. 633. Available at <http://scc-csc.lexum.com/scc-csc/scc-csc/en/item/1816/index.do>

<sup>108</sup> Anderson, T.L. & Parker, D.P. (2006). *The Wealth of Indian Nations. Self-determination: The Other Path for Native Americans*. Stanford, CA: Stanford University Press.

### **What are the opportunities to improve the First Nation property right system in Canada?**

The poor property right system of the *Indian Act* has spurred a number of actual and proposed legislative changes. The intent of each of them was to improve the collective (jurisdiction) property rights, create a more modern land registration system, provide more marketable individual property rights, and ultimately reduce transaction costs and facilitate investment. These options are presented in chronological order according to when they were legislated or proposed:

- *The First Nations Land Management Act*
- *The First Nations Commercial and Industrial Development Act*
- Modern Treaties, Comprehensive Claims and Property Rights
- The Proposed First Nations Property Ownership legislation
- The Tsilhqot'in Aboriginal Title Decision

### **The First Nations Land Management Act (FNLMA)**

The FNLMA was enacted in 1999 to allow First Nations to manage lands within their respective reserves. It was the result of some 10 years of discussions between First Nations and Canada about how to make devolution policy meaningful, and had two sets of precedents.

The first set involved co-management and delegation under the *Indian Act*. Co-management was allowed through the Regional Land Administration Program, although accountability for land management functions continued to reside with the Minister of Indian Affairs. The Land Management Delegation Program allowed First Nations some responsibility for land management on reserves pursuant to s. 53 and 60 of the *Indian Act*.

However, the more significant precedent was the Framework Agreement on First Nation Land Management, signed between Canada and 14 First Nations in February 1996. The Framework Agreement allowed First Nations to opt out of the land management sections of the *Indian Act*, such that they assumed such responsibility. The FNLMA ratified the Framework Agreement three years later. As of 2013, 39 First Nations have passed land codes and are operational under the FNLMA.

A further 30 First Nations are listed as developmental<sup>109</sup> and funding for 33 more First Nations was included in the 2013 federal budget.

The FNLMA requires First Nations to decide for themselves to participate in the act and subsequently develop a land code, which deals with land management jurisdiction including revenues from lands and natural resources, conflicts of interest and dispute resolution, existing and new interests granted on reserve, marriage breakdown, First Nation's laws, and the use (occupation and protection) of the lands. The FNLMA also contains a regulation to develop a new land registration system that creates priorities for registration to provide more security to lenders, investors and lessees. The FNLMA also has some potential to provide more leasehold property right certainty and clarity but its impact on other individual property rights is limited.

Both anecdotal and empirical results relating to the FNLMA are encouraging. For instance, since opting into FNLMA the Whitecap Dakota First Nation in Saskatchewan “have a land use plan and a zoning bylaw, grants 49-year commercial and 99-year residential leases, has a real property tax bylaw, enters into partnerships with abutting municipalities, and is negotiating to access the debenture and bond markets like a municipality. As a result, they suggest, “there is a seamless transition from municipality to Reserve.”<sup>110</sup> In addition, Alcantara (2007) performed a comprehensive review of the land codes of the Scugog Island First Nation of Ontario and the Muskoday First Nation of Saskatchewan and found that both made strong strides towards reducing transaction times (i.e. red tape) for development projects on reserve.<sup>111</sup>

In a study of 40 reserves, Knauer (2010) compared eight First Nations that had moved to the FNLMA regime to 32 control First Nations that remained under the *Indian Act*. Geographic location was

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<sup>109</sup> First Nations Land Management Resource Centre (FNLMRC). *Member Communities*. Available at <http://www.labrc.com/member-communities/>.

<sup>110</sup> Ballantyne, B. & Rogers, S. (2012). Ascertaining First Nations Communities for Optimism Fabric Renewal: Parcels as Enablers. *Annual World Bank Conference on Land and Poverty*.

<sup>111</sup> Alcantara, C. (2007). Reduce transaction costs? Yes. Strengthen property rights? Maybe: The First Nations Land Management Act and economic development on Canadian Indian reserves. *Public Choice*, 132(3).

controlled by choosing four non-FNLMA First Nations from within the same province as each FNLMA First Nation. The adoption of FNLMA was found to have positive, economically significant effects on median income, average earnings and net growth in dwelling units.<sup>112</sup>

### **The *First Nations Commercial and Industrial Development Act* (FNCIDA)**

FNCIDA is a First Nation led initiative that began in 2005 between five partnering First Nations in British Columbia, Alberta, Saskatchewan and Ontario. It provides a mechanism by which a First Nation can request that Canada develop regulations for a specific commercial or industrial development on reserve. It does not extend provincial regulations onto reserve, but it tends to mimic such regulations. This gives potential partners and private sector investors greater certainty by “ensuring that they are dealing with regulations and regulators that they know and understand”.<sup>113</sup>

It also bridges a regulatory gap, where federal laws do not match the needs of commercial activity on reserve, and where provincial regulations are not permitted on reserve for constitutional reasons. In 2010, FNCIDA was amended by the *First Nations Certainty of Land Title Act*, which entitled First Nations to request that the Government of Canada: “make regulations respecting the establishment and operation of a system for the registration of interests and rights in reserve lands”.<sup>114</sup> The intention of this amendment was to adapt many elements of the provincial system to provide to potential investors a regulatory and registry system similar to that which exists off First Nation lands to potential investors. In particular, a regulation could create a similar regulatory framework to the province on FNCIDA lands with respect to

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<sup>112</sup> Ballantyne, B. & Rogers, S. (2012). Ascertaining First Nations Communities for Optimism Fabric Renewal: Parcels as Enablers. *Annual World Bank Conference on Land and Poverty*.

<sup>113</sup> Aboriginal Affairs and Northern Development Canada (AANDC). 2012. *Frequently Asked Questions – First Nations Commercial and Industrial Development Act*. Available at <https://www.aandc-aandc.gc.ca/eng/1100100033564/1100100033565>.

<sup>114</sup> Justice Laws Website. (2010). *First Nations Certainty of Land Title Act s.c. 2010, c. 6*. Available at [http://lois-laws.justice.gc.ca/eng/AnnualStatutes/2010\\_6/page-1.html](http://lois-laws.justice.gc.ca/eng/AnnualStatutes/2010_6/page-1.html).



land title, building codes, fire protection, services, environmental management and land use and enable properties on First Nation lands to be registered in the provincial land title system.

The FNCIDA 2010 amendment, therefore, has the potential to overcome two challenges facing the *Indian Act* property right system. First, it could provide more regulatory certainty to create tradable property rights. Second, it replaces an inefficient and poorly integrated registry system with a modern land title registry system.

The Squamish First Nation of British Columbia is proposing to use the 2010 version of FNCIDA on reserves in West and North Vancouver for large scale commercial and condominium developments that could house up to 25,000 residents.<sup>115</sup> This would be the first use of the 2010 legislation but it has not been completed and implemented yet so it is difficult to evaluate FNCIDA as a property rights improving option.

Further, implementing FNCIDA for a project on reserve can be both costly and time consuming. Before the agreement between the developer and the First Nation fell through, the Fort McKay First Nation of Alberta passed new regulations under FNCIDA.<sup>116</sup> The new regulations as well as an accompanying agreement between the Province of Alberta, Canada, and the First Nation set out “a comprehensive framework that ensure the project will meet provincial environmental, health, safety and operational standards”.<sup>117</sup> The development of the agreement and regulations is estimated to have taken over 2 years and cost over a million dollars.<sup>118</sup>

### **Treaties, Comprehensive Claims and Property Rights**

Another First Nation option to establish marketable property rights is through the negotiation of treaties (where none previously existed such as British Columbia) or the settlement of a comprehensive claim

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<sup>115</sup> Lower Mainland Treaty Advisory Committee (LMTAC). (2011). *Briefing Note*.

<sup>116</sup> Justice Laws Website. (2007). *Fort McKay First Nation Oil Sands Regulations, SOR/2007-79*. Available at <http://laws-lois.justice.gc.ca/eng/regulations/SOR-2007-79/page-1.html>.

<sup>117</sup> Aboriginal Affairs and Northern Development Canada (AANDC). (2007). *Fort McKay First Nation oil sands project one step close to realization*. Available at [www.ainc-inac.gc.ca](http://www.ainc-inac.gc.ca).

<sup>118</sup> Flanagan, T., Alcantara, C., & Le Dressay, C.A. (2010). *Beyond the Indian Act: Restoring Aboriginal Property Rights*. McGill-Queen's University Press

arrangement. Since 1975, there have been 24 modern treaty agreements<sup>119</sup> and 99 comprehensive claim agreements<sup>120</sup>. These have since been referred to as the modern treaties to differentiate them from the peace and friendship treaties signed before confederation and the numbered treaties signed just after confederation.

All modern treaties and comprehensive claim agreements have three common features. First, they transfer fee simple title to the First Nation or aboriginal group. Second, they create self-government arrangements to implement First Nation or aboriginal jurisdictions<sup>121</sup>. Third, the lands and agreements are constitutionally recognized and protected. This combination provided the legal authority but not necessarily the interest or capacity to develop and implement a property right system to support investment and trade. Three brief examples of how a negotiated treaty or claims agreement was used to establish a property right system are presented below.

*Cree-Naskapi* – In 1975, the Cree, Naskapi and Inuit of Northern Quebec negotiations culminated in the James Bay and Northern Quebec Agreement.<sup>122</sup> The agreement included “more limited land rights, hunting rights and financial compensation” but “outright self-government provisions were not included”<sup>123</sup>; however, the *Cree-*

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<sup>119</sup> Land Claims Agreements Coalition. (2014). Modern Treaties. Available at <http://www.landclaimcoalition.ca/modern-treaties/>.

<sup>120</sup> Aboriginal Affairs and Northern Development Canada. (2014). Comprehensive Land Claim and Self-Government Negotiation Tables. Available at <http://www.aadnc-aandc.gc.ca/eng/1346782327802/1346782485058>

<sup>121</sup> Outside of land claims agreements, self-government has also been negotiated as a stand-alone process. The Westbank First Nation Self-Government Agreement explicitly mentions that it is not a treaty and contains no land component. Westbank did not receive fee-simple title as part of their Self-Government agreement in 2003 but instead established “the most comprehensive system of community laws for any First Nation in Canada”. The benefit of the Westbank agreement and its by-laws is that “the cost and time for facilitating investment in Westbank is as low as elsewhere in Canada”. For more see Flanagan, T., Alcantara, C., & Le Dressay, C.A. (2010). *Beyond the Indian Act: Restoring Aboriginal Property Rights*. McGill-Queen’s University Press.

<sup>122</sup> Later accompanied by the 1978 Northeastern Quebec Agreement.

<sup>123</sup> Dalton, J. E. (2006). Aboriginal Title and Self-Government in Canada: What Is the True Scope of Comprehensive Land Claims Agreements. *Windsor Rev. Legal & Soc. Issues*, 22.

*Naskapi (of Quebec) Act* replaced nearly all of the *Indian Act* (save for provisions about Indian Status) and provided for a separate Cree-Naskapi Land Registry. The Registry is run by the First Nation and covers all rights and interests in the 14,000 km<sup>2</sup> of land designated as Category I lands. The Cree-Naskapi Land Registry, however, must report to AANDC as the lands are still under federal jurisdiction.

*Tsawwassen Treaty* – The Tsawwassen Final Agreement included 662 hectares of land in fee simple that the Tsawwassen First Nation will have law-making authority over. Over 50 acts and regulations have been passed by the First Nation covering fisheries, natural resources, land use planning, economic development and taxation. All fee-simple interests are registered in the British Columbia Land Title Office. To achieve this goal, the provincial *Land Title Act* had to be amended to accommodate the recognition of Tsawwassen First Nation fee simple title. For a transfer or sale of Tsawwassen land to occur in the BC Land Title system, the registrar of land titles must receive a Certificate of Transfer issued in accordance with Tsawwassen law.<sup>124</sup>

*Nisga'a Treaty* – In the Nisga'a Final Agreement, over 1,900 km<sup>2</sup> of land in the Nass River Valley was granted in fee simple, subsurface rights were granted, and the Nisga'a Central Government (and village governments) was established. Nisga'a established its own land title system. The transactions on Nisga'a land are registered in the Nisga'a Land Titles Office. The Nisga'a Constitution sets out land transaction, land use planning and expropriation rules.<sup>125</sup> The *Nisga'a Land Title Act* provides the rules for registering and transferring interests in fee simple, subdividing, easements, mortgages and tenancies. In 2010, the Nisga'a passed the *Nisga'a Land Title Holding Act* to facilitate fee simple title for members. In October 2013, the first fee simple titles to First Nation members on First Nation land were issued. “If I leave it as it is (not

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<sup>124</sup> British Columbia. (2009). Tsawwassen First Nation Final Agreement Implementation Report. Available at [http://www.gov.bc.ca/arr/reports/down/tsawwassen\\_first\\_nation\\_final\\_agreement\\_implementation\\_report\\_0910.pdf](http://www.gov.bc.ca/arr/reports/down/tsawwassen_first_nation_final_agreement_implementation_report_0910.pdf).

<sup>125</sup> Nisga'a Nation. (1998). *The Constitution of the Nisga'a Nation*. Available at [http://nisgaalisims.ca/files/nlg/The\\_Constitution\\_of\\_the\\_Nisga\\_a\\_Nation\\_\\_October\\_1998\\_.pdf](http://nisgaalisims.ca/files/nlg/The_Constitution_of_the_Nisga_a_Nation__October_1998_.pdf).

having title) it closes doors to me. I want to own the land like anyone in Terrace or (Prince) Rupert does and use it for equity. The good thing about this is if someone wants to get into business, they could borrow money against their home,” noted one Nisga’a member slated to receive title to his property.<sup>126</sup>

It is still too early to evaluate the property right systems established through treaty and comprehensive claim settlement but a few anecdotes suggest positive results. The Cree Naskapi have benefitted fiscally and economically from the production of hydroelectricity in their territory because their agreement recognizes their collective property rights. There is considerable development interest in Tsawwassen because of the property right certainty created by their legal framework. The first member recipients of Nisga’a fee simple title are excited about the potential. The second person to receive title on Nisga’a lands, stated, “I’ve been chomping at the bit for quite a few years asking for fee-simple (title).” His plan is to take equity out of the property he estimates is worth about \$320,000 and reinvest in rental property.<sup>127</sup>

There are however two caveats with respect to negotiating treaties and comprehensive claims agreements. First, the First Nation claim has to be recognized for negotiations. Second, they are expensive<sup>128</sup> and time consuming. The Nisga’a agreement, for instance, is estimated to have cost anywhere from \$190 million to \$1 billion depending on the factors included in the measurement.<sup>129</sup>

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<sup>126</sup> Pemberton, K. (2013). *Nisga’a become first Aboriginals able to hold title to their own property*. Vancouver Sun. Available at <http://www.vancouver.sun.com/news/Nisga+become+first+aboriginals+able+hold+title+their+property/9124623/story.html>.

<sup>127</sup> Ibid.

<sup>128</sup> The BC Treaty process financing method can raise these costs because Canada and British Columbia lend First Nations money and charge interest to support their negotiations which is repaid out of the final settlement.

<sup>129</sup> Hurley, M. (1999). *Nisga’a Final Agreement*. Parliament of Canada. Available at [www.parl.gc.ca](http://www.parl.gc.ca).

### **The proposed First Nation Property Ownership Initiative**

The First Nations Property Ownership (FNPO) initiative proposes an opt-in and First Nation-driven legislative concept that would transfer ownership of a reserve from Canada to the First Nation and the jurisdiction over those lands from Canada to the First Nation. This mechanism would enable the First Nation to grant any part of their lands in fee-simple ownership to individuals and register those interests in a First Nation land titles system. The framework for FNPO builds on other initiatives that opt out of the regulatory portions of the *Indian Act*. Like the FNLMA, First Nations would have a number of lands related regulatory powers and they would have tax powers under the proposed FNPO legislation. A ready-to-use legal framework built through regulations would be available to First Nations to implement these powers in a cost and time effective manner should they choose, since they would also have the option to implement their own laws for these jurisdictions. The proposed legislation would also establish a First Nation land title registry system to replace the ILRS as indicated previously.

In order to participate in FNPO, a First Nation community must hold a referendum. This vote must be accompanied by a plan showing how existing rights will be converted to fee-simple. If the vote is positive, FNPO would replace about 40% of the *Indian Act*.<sup>130</sup> FNPO is being driven by the First Nations Tax Commission, and about a dozen First Nations have indicated interest via band council resolution.

The conceptual legislation like other initiatives discussed in this chapter is optional for First Nations. FNPO was expressly mentioned in the 2012 federal budget as a priority because of its potential to “address barriers to economic development on Reserve”.<sup>131</sup> Despite this commitment, no legislation has been introduced so it is impossible to evaluate the proposal.

Theoretically, the proposal could address all the property right challenges on First Nation lands. It could establish the clear jurisdiction

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<sup>130</sup> Ballantyne, B., & Le Dressay, C.A. (2013). *From observation to hypothesis for First Nations property rights in Canada: The role of institutions, taxes and surveys*. Paper presented for the Annual World Bank Conference on Land and Poverty. Washington, DC.

<sup>131</sup> Government of Canada. (2012). *Economic Action Plan 2012*. Available at <http://www.budget.gc.ca/2012/plan/pdf/Plan2012-eng.pdf>.

over property rights and provide a mechanism to implement them quickly and cost effectively. It could enable the full range of individual property rights including indefeasible or fee simple title. It could create a land title registry system that is integrated with other databases to facilitate property “fungibility” and transaction protection. The proponents of this legislation assert by solving these problems it will raise property values; reduce transaction costs; facilitate access to capital; and increase investment, employment, income and government revenues. Using a sample of 68 First Nations in British Columbia, the First Nations Tax Commission estimates that FNPO would increase property values by about \$4 billion over 15 years.<sup>132</sup>

Critics have noted that FNPO could contribute to greater economic disparity on reserve, most notably in cases where the First Nation lands are covered by CP holdings held by a minority of members. These CPs would probably be converted to fee simple ownership under FNPO. The net increase in property value accruing from the fee simple conversion would mainly benefit the CP holder although the First Nation could share in this increase in value through taxation.

Further criticism of FNPO often focuses on the potential alienation of the reserve land base through sale. These comparisons generally compare FNPO to the mass sale of Reservation land in the United States under the *Dawes Act* of 1887. Indeed, Flanagan et al. (2010) forecasted this comparison as a criticism.<sup>133</sup> FNPO differs in a significant way from the *Dawes Act* in that, upon sale, jurisdiction over the land would remain with the First Nation as the sovereign entity governing taxation, regulation, and provision of certain governmental services. The difference under the *Dawes Act* is that land transferred out of trust status generally no longer remains under the sovereign jurisdiction of the tribe. It cannot be taxed by the tribe and can only be regulated under certain limited conditions. In this sense, FNPO is less about alienation and more about moving the underlying title and important components of

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<sup>132</sup> First Nations Tax Commission (FNTC). (2009). *Towards a First Nation Property Ownership Act*. Briefing Note to the House of Commons Standing Committee on Finance.

<sup>133</sup> Flanagan, T., Alcantara, C., & Le Dressay, C.A. (2010). *Beyond the Indian Act: Restoring Aboriginal Property Rights*. McGill-Queen's University Press

jurisdiction from Canada to the First Nation. As Quesnel (2012) notes, this “is the opposite of the Dawes Act...as the land would always remain under First Nation jurisdiction.”<sup>134</sup>

### **The Aboriginal Title Decision for the Tsilhqot’in**

In 1983, the province of British Columbia issued a timber license within the territory of the Tsilhqot’in Nation (represented by four existing communities) without Tsilhqot’in consent. Blockades and negotiation were unsuccessful so a court challenge was launched and the Supreme Court of Canada issued a final ruling in June 2014. The Supreme Court built on previous decision such as Delgamuukw Decision and the Haida Nations Decision and unanimously deciding that the Tsilhqot’in had Aboriginal Title to 1750 km<sup>2</sup> of land. The main elements of the decision describing the nature of the Aboriginal Title property right are:

- Aboriginal Title holders have the right to decide how the land will be used; the enjoyment and occupancy of the land, possession of the land, the economic benefits of the land; and the use and management of the land.
- Aboriginal Title is a collective right, so the land cannot be used by Aboriginal Title holders in a way that would prevent the use and enjoyment of the land by future generations, but that does not mean that uses are restricted to traditional practices. Aboriginal Title holders may put the land to modern uses if they consent to that choice.
- Aboriginal Title is subject to the federal and provincial government’s right to encroach, if the infringement can be justified under the constitution using the infringement and justification test from the previous *Sparrow* Decision. Any First Nation jurisdiction on Aboriginal title lands must be reconciled with the jurisdiction of other governments.

There has been a large amount of commentary regarding the implications of the decision but for this chapter two potential impacts from this decision are particularly important. First, there is considerable economic

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<sup>134</sup> Quesnel, J. (2012). *First Nation land ownership isn't a cure all*. Winnipeg Sun. Available at <http://www.winnipegsun.com/2012/11/23/first-nation-land-ownership-isnt-a-cure-all>.

uncertainty surrounding this decision. This uncertainty arises from three sources and involves a number of questions:

*Property rights Certainty* – Who owns Aboriginal Title land? How much land is subject to a\Aboriginal Title? Are pre-confederation treaty areas (Maritimes, Quebec and parts of Ontario) considered Aboriginal Title lands? Does Aboriginal Title apply to post-confederation treaties? What type of individual ownership if any does Aboriginal Title enable? Which government(s) has the collective (jurisdiction) property right on Aboriginal Title land?

*Jurisdictional Certainty* – Which government(s) makes the rules on Aboriginal Title lands? What are the rules on Aboriginal Title lands if two governments make different laws? Where are individual property interests on Aboriginal Title lands registered?

*Fiscal Certainty* – Which government collects which taxes, fees and charges on aboriginal title lands? How will federal, provincial, municipal and Aboriginal governments resolve fix jurisdictional overlap? How are tax rates and charges determined?

The second key implication of this decision is the best method to reduce the economic uncertainty of Aboriginal Title. In this regard there are three options; further court challenges, negotiate treaties for traditional territories or interim resolutions on selected lands with clear Aboriginal Title supported by legislation. Court challenges will be time consuming and expensive and may not reduce uncertainty. Treaty negotiations and resolution are also lengthy and expensive and First Nation acceptance is not always assured.<sup>135</sup> The third option to incrementally address Aboriginal Title where all parties accept it offers some potential to reduce economic uncertainty if it is supported by legislation similar to the FNPO proposal.

The FNPO legislation could help implement Aboriginal Title as defined by the Supreme Court in at least five ways. 1) FNPO would

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<sup>135</sup> The Lheidli T'enneh First Nation community rejected a treaty settlement agreement in 2007 after 14 years of negotiation.



require First Nation consent. 2) It would transfer title to the First Nation. 3) It would prevent Aboriginal title lands from alienation because the underlying title cannot be transferred and 4) by doing this it also protects the interests of future generations. Finally, 5) it provides First Nations regulation and fiscal powers over these lands to ensure that a collective economic benefit is realized and that these powers are reconciled with federal and provincial jurisdictions.

### **Summary of Options to Restore Effective Property Right Systems**

What is the best approach for a First Nation to establish a market orientated property right system? The answer depends on the First Nation's circumstances but the following six generalizations are possible.

1. The larger the market for individual property rights the higher their value. Options that can possibly or significantly increase the market size for individual property are superior to those that do not.
2. A modern land registry system is superior to the ILRS. Options that continue to use the ILRS are inferior to those that do not because the ILRS is not integrated with other databases.
3. A regulatory framework to support property rights that minimizes transaction costs is superior to one that does not. Some options provide a regulatory framework that lowers transaction costs others ask First Nations to create one that accomplishes this. It is uncertain if First Nations will be successful in lowering transaction costs when they develop their own legal framework. Some options have been developed in legislation or regulations or established in law through the courts. Other options are merely proposals or have not been developed as legislation or regulations. Those that exist in law are superior to those that do not. Faster and cheaper regulatory options to implement are preferable to slower expensive ones to implement. The more of the legal framework that the First Nation has to develop and implement itself, the more expensive and slower is the option.
4. Any option that facilitates the addition of lands closer to markets and resources are superior to locations farther away because of higher property values. This refers to those options that provide property rights over lands in additions to reserves and reservations. Some options can reduce the distance to markets and resources and others have no impact.

- Locations closer to markets and resources are superior to locations farther away. Some options can reduce the distance to markets and resources and others have no impact.

The table below summarizes the First Nation property right system options using these generalizations. Each option has its benefits and possible costs so their application depends on the situation for each First Nation.

***Property Right System Options***

Option	Individual property rights	Modern Registry System	Low Transaction Cost Legal Framework	Available	Faster, Cheaper	Market Distance
FNLMA	Not significantly	Part of ILRS	Uncertain	Yes	Possibly yes <sup>136</sup>	No impact
FNCIDA	Not significantly	Yes	Yes	Not Yet	No	No impact
Modern Treaty	Possible	Possible	Uncertain	Yes	No	Can reduce
FNPO	Yes	Yes	Yes	No	Yes	No impact
Aboriginal Title	Possible	Uncertain	Uncertain	Possible	No	Can reduce

For example, the FNLMA does not improve individual property rights significantly but it could reduce transaction costs and be implemented in timely cost effective manner. FNCIDA can provide a modern land registry and low transaction costs but there is no model yet so it is neither fast nor cheap. Modern treaties could establish effective individual property rights supported by an efficient legal framework but they would be expensive and time consuming to establish. Aboriginal title and FNPO may yet be a property right panacea but FNPO does not exist yet in legislation and cost effective methods to establish and implement aboriginal title are not available.

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<sup>136</sup> FNLMA First Nations can save time by using examples from other FNLMA First Nation models but no study has been undertaken on this.

Another approach is to not compare these options directly, but instead to consider them as a hierarchy of opportunities to create an improved First Nation property rights system. A First Nation could begin by using the FNLMA to develop the regulatory system to support improved property rights. For specific projects on desirably located lands, it could use a FNCIDA regulation (if a sufficient model has been developed). The best approach to obtain better access to markets or resources may be negotiating a modern treaty or proving aboriginal title on a comprehensive claim area. The proposed FNPO is the most efficient (lowest cost and least time) method to create a property rights system that facilitates investment. FNPO also might be an effective method to implement aboriginal title. At this stage however, it is only a proposal and not a law.

### **Conclusion**

First Nations and tribes had collective jurisdiction and individual property rights systems before contact. In Canada, First Nation property rights systems and the economic benefits they created were legislated away by the *Indian Act*. The objective of the *Indian Act* was to take away First Nation title and treat First Nations like minors who were wards of the state. The *Indian Act* accomplished this by creating a property right system that provided no regulatory certainty, a land registry system that was slow and cumbersome and individual property rights that were mostly not marketable. The results were a poor investment climate with high transaction costs, low property values and poor access to capital.

For the last 25 years, First Nations have been pursuing a number of legislative, negotiated and legal means to restore their property right systems and jurisdictions to support them. Legislative initiatives like the FNLMA and FNCIDA can improve property right systems on existing lands but they can be costly and time consuming to implement. Negotiated treaties and claims settlements can establish collective ownership and create better property right systems on traditional First Nation lands but they cost millions of dollars and years of time. Legally proving Aboriginal title can establish collective ownership but it creates property right and investment uncertainty. The proposed FNPO legislation could establish an effective property right system quickly and cheaply and reduce the uncertainty of Aboriginal title but it is still just an

idea supported by some First Nations. Regardless, the common objectives for each option are (1) to restore First Nation property rights and (2) establish the regulatory framework to support marketable individual property rights and facilitate investment. The next chapter focuses on the second objective – creating the legal framework to facilitate investment on First Nation land.



CHAPTER 4

# THE LEGAL FRAMEWORK TO SUPPORT INVESTMENT

**L**aws matter in the investment climate. On the one hand, they can support a strong regional investment climate by providing certainty and security to investors, protecting property rights, attracting financing for infrastructure, and reducing the costs of doing business. On the other hand, laws- or the lack of laws- can impede investment and entrench poverty in a region.

Economists and lawyers must work together to develop a legal framework that supports rather than impedes investment. Lawyers need economists to identify the economic incentives and costs inherent in the laws they develop. Economists need lawyers to develop the legal framework needed to achieve the certainty that investors require. This chapter introduces students to the field of law as it relates to the First Nation investment climate, by asking: How do we develop a legal framework that supports investment? This question will be answered by exploring these seven topics:

- How does an investor assess a legal framework when making an investment decision?

- Why are there gaps in the legal framework on First Nation and tribal lands?
- What legal framework is needed to support investment?
- What options exist for First Nations wanting to create a legal framework to support investment?
- How do the existing options for creating legal frameworks compare?
- Why should First Nations use a standardized approach to develop their legal framework?
- What type of a lawyer can best develop a legal framework that supports investment?

**How does an investor assess a legal framework when making an investment decision?**

Suppose an investor is considering two identical properties for investment- one on First Nation or tribal land and one off First Nation or tribal land. Further, suppose they cost the same amount. How would the investor decide? Regardless of the type or size of the investment, be it a small commercial investment such as a store, or a large business venture such as resource development, investors evaluate an opportunity by estimating their potential rate of return on investment.

The rate of return is the difference between revenues and costs; in other words, it is the profit an investor can realize. This is the difference between how much time and money an investor has to put in to the investment, and how much money an investor generates from the investment. An investor will need to analyze a number of factors in order to determine an investment's potential rate of return. Although the specific factors will vary depending on the specific type of investment, an investor will invariably ask the following three questions:

1. *What are the laws related to property rights and use?* Property rights are the bedrock of the market economy. Without clear property rights over land, investors will not buy land and invest in development and infrastructure because they risk losing their investment. Without clear rights over personal property, trade is impeded because it is difficult to sell what you do not own. The legal framework for property rights both define and protect individual property rights,

and provide clarity and certainty about the government's ability to interfere with those rights.

Government control over private property is extensive. For example, the government can expropriate property, can seize property if taxes are not paid, and can impose restrictions on the use of property through zoning laws. These laws can have a significant impact on property values, and on an investor's cost of doing business. For example, zoning laws restricting land use and development potential can lower land values and reduce an investor's return on investment.

Local laws can influence the certainty of property rights and can raise or lower the ability to calculate future rates of return. Laws that reduce uncertainty about future costs, processes and services will encourage investment. A legal framework that protects property rights and creates transparent processes respecting property uses creates certainty and strengthens investor confidence.

2. *What are the quality of services and infrastructure available for my investment or business?* Different investments need different types of services and infrastructure, such as roads, fire protection, and water. If required services and infrastructure are not available, investors need to know if the legal framework exists to allow them to be provided or built in the future, and at what cost. If these services and infrastructure are available, investors need to know that the legal framework ensures their long-term provision.

Laws affect the quality of local services and the financing, construction and maintenance of local infrastructure. A legal framework that supports and ensures cost effective and reliable local service delivery, and facilitates the provision of required infrastructure through low-cost financing, strengthens investor confidence.

3. *What are the rules and procedures for investment and do I have recourse?* Investors need to know the required rules and procedures for a project from planning to completion. Who do they meet with? How are decisions made? What is the time line for decisions? Clear and transparent processes allow investors to know the rules of the game before they decide to invest, and to assess the costs involved. Investors also need to know what their options are in case something

goes wrong. Is there an appeal process? Who makes the decisions and are reasons for decisions given?

The legal framework can support investment by creating transparent, efficient and fair processes for all aspects of a development, from planning through to completion and operation. Having these processes in place will reduce transaction costs and create the certainty required to encourage investment. Not having any set processes, or having incomplete or unclear processes, deters investment because it creates uncertainty. Without clear processes, an investor may be unable to determine whether the project can proceed, may be unable to determine costs, and may be concerned that the project costs will increase because of resulting administrative delays.

Investors ask these three questions because they directly impact an investor's rate of return. Although governments generally let investors determine the best way to make revenues, the government's legal framework has a direct impact on business and investment costs. Governments influence direct business costs through their tax laws and policies, including property taxes, business taxes, transfer taxes, sales taxes and others. Governments influence indirect business costs through the processes they require for developments.

A government's legal framework can support and encourage investment by doing three key things: creating certainty, lowering transaction costs and supporting a comparative advantage.

1. *How do laws create certainty?* Laws create certainty by providing clear and transparent rules that apply to all investors. Laws that, for example, establish property rights, delineate governmental powers, enforce contractual terms, and create processes for seeking required approvals, provide investors with confidence and clarity in the system. These laws enable investors to assess their costs, risks and timelines for investments with confidence that the system will support their investment now and in the future. Poorly constructed laws, or no laws, create uncertainty. Uncertainty deters investment because investors are less able to assess their costs, risks and timelines, which results in lower investor confidence.
2. *How can laws lower transaction costs?* Laws can raise or lower the transaction costs of an investment by establishing processes or rules



that enable or disable investment. For example, in the event investor-required laws are missing, transaction costs are significantly higher because they have either to be developed in order to enable the investor, or captured in a contract that must be negotiated on a case-by-case basis. Laws that create processes that are familiar to investors also lower transaction costs because investors do not need to learn a new system in order to invest. Laws that lower transaction costs are good for investors because they lower the cost of doing business and increase the rate of return.

3. *How can laws support a comparative advantage?* Laws can influence the short and long-term profitability of a particular investment by increasing or decreasing the costs associated with establishing and operating a business or other types of investment. For example, changes in tax laws can lower or raise the costs to businesses. Changes in tax expenditure policy can favor one industry or business over another. Legal frameworks that support investment by lowering costs and creating continuity support a comparative advantage.

The legal framework to support investment should provide certainty to investors. The table below considers the possible gaps in the legal framework on First Nation land for an investor considering a land development project. The table considers the law and contract requirements for a typical land development deal as it progresses through the planning, approvals, financing and construction stages. The table is based on the process discussed previously in Chapter 2 – setting the terms of the deal, securing the necessary property rights, obtaining necessary approvals, building necessary infrastructure and securing services, and financing and construction.

BUILDING A COMPETITIVE FIRST NATION INVESTMENT CLIMATE

Investment Process	Legal Framework Requirement	Possible Gaps in the Legal Framework
Setting the terms of the deal	<p>Governance (who to work with)</p> <p>Property right acquisition costs (rental, lease, fee simple)</p> <p>Property right terms and conditions (rental, lease, fee simple)</p> <p>Taxes, fees and charges (property taxes, business taxes, service taxes, fees and charges)</p>	<p>Off First Nation/tribal land: The processes, costs, timelines and applicable taxes, fees and charges are clear.</p> <p>On First Nation/tribal land: Processes for development and costs of obtaining approvals and acquiring property rights, including timelines and clear information on taxes, fees and charges may be missing.</p>
Securing a property right	<p>Agreement to acquire property right (rental, lease or sale)</p> <p>Securing tenure (designation, approvals or other requirements)</p> <p>Registration in land registry</p>	<p>Off First Nation/tribal land: Clear provincial laws for acquiring property rights and registration in land title registries usually with guaranteed title.</p> <p>On First Nation/tribal land: Property rights may be more limited, and registration systems may not guarantee title.</p>
Government Planning and Approvals	<p>Land Use laws</p> <p>Development approval processes</p> <p>Development servicing standards</p> <p>Environmental requirements</p> <p>Heritage management and protection</p>	<p>Off First Nation/tribal land: Land use bylaws, and clear laws and processes for development applications, subdivision approvals, servicing requirements, and environmental and heritage requirements.</p> <p>On First Nation/tribal land: Laws and process often missing</p>
Government Services and Infrastructure	<p>Local services laws</p> <p>Financial management laws, Core service requirements, including fire, water and sewer</p> <p>Infrastructure financing</p>	<p>Off First Nation/tribal Land: All of these laws are in place.</p> <p>On First Nation/tribal land: Significant variation and only a few have all these laws.</p>
Financing and Construction	<p>Mortgaging and financing requirements for rentals, leases and sales</p> <p>Building codes and permitting</p> <p>Builder's lien rights</p>	<p>Off First Nation/tribal Land: Clear local and provincial/state legal framework.</p> <p>On First Nation/tribal Land: Financing and construction legal framework piecemeal on most lands. Unclear application of provincial/state laws can create additional uncertainty.</p>

The table illustrates the uncertainty that may arise when investing on First Nation land. The possible gaps in the legal framework create uncertainty in key areas such as property rights, the ability to obtain necessary approvals, the provision of quality infrastructure and servicing, and the ability to obtain financing. This in turn leads to potentially significantly higher transaction costs, greater risk, and a resulting lower return on investment. Unless the development offered a substantially higher return on investment, most investors would chose to invest off First Nation lands based on this evaluation. The rest of this chapter explains how this investment-destroying legal framework gap occurred and some options to close it.

### **Why are there gaps in the legal framework on First Nation land?**

The vast majority of First Nation lands in Canada have significant and substantive gaps in the legislative framework that is necessary to support investment. Although there are additional contributing factors, there are two main historical reasons for these gaps: first, the legal status or nature of reserve lands, and second, the division of powers under Canada's constitutional structure. Understanding why there are legislative gaps is an important first step in determining how best to fill them.

### **How does the legal status of reserve lands impact the legal framework?**

In Canada, most First Nation lands located south of the 60th parallel are, or were at some point, reserve lands. Under the *Indian Act*, reserves are lands set apart by Canada for the use and benefit of a First Nation, the legal title to which is held by Canada. This means that although First Nations have the use and benefit of their reserve lands, it is Canada that legally owns the lands and holds them in trust for the First Nation. In addition to holding legal title to reserve lands, in the majority of cases it is Canada that is responsible for the administration, control and management of a First Nation's reserve lands. In these cases, although the First Nation government plays a role in approving land management decisions, it is the officials at the federal department of Aboriginal Affairs and Northern Development Canada (AANDC) who ultimately approve certain proposed uses of reserve lands by non-members of the First Nation, such as permits or leases, the amount that will be charged to

third parties for those uses, and any financing of those interests in lands. The impact on investment related to how reserve lands are owned and managed cannot be understated. Because reserve lands are held in trust by Canada, it is significantly more difficult and time-consuming to negotiate agreements in respect of those lands, to create interests in those lands, to transfer those interests, and to finance the land for investment. AANDC must be involved in all stages of land-related agreements; in fact, very little can be done with reserve lands without the direct, ongoing involvement and approvals of AANDC.

Not only are reserve lands owned by Canada, reserve lands, and rights and interests in those lands, are not registered land title systems that guarantee title and protect the priority of interests. Instead, rights, interests and other documents may be deposited in one of three deed registries operated by the federal government.<sup>137</sup> These registries do not provide guaranteed title, have different approaches to determining priority for interests, and deliver varying levels of efficiency in registrations (from days to months). These registration systems do not provide the level of legal certainty and confidence that is provided in most provincial land title systems in Canada.

### **How does Canada's constitution impact the legal framework?**

Canada is a federal state in which governmental powers are divided between the federal and provincial levels of government. Under a federal system, each level of government is equal, in the sense that neither is subordinate to the other, and each has its defined and exclusive areas of jurisdiction. In Canada, the specific and exclusive powers of each level of government are set out primarily in sections 91 and 92 of the Constitution Act, 1967.<sup>138</sup> The powers allocated to each of the

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<sup>137</sup> The three registries are: The Indian Land Registry System for reserve and surrendered lands that are administered under the *Indian Act*; the First Nations Land Registry System for the land records of First Nations who operate under *First Nations Land Management Act*; and the Self-Governing First Nations Land Register for documents that grant an interest in self-governed First Nation lands.

<sup>138</sup> The *Constitution Act, 1982* renamed the *British North America Act, 1967* to the *Constitution Act, 1967*. The "Constitution of Canada" is not a single document, but includes a number of instruments, including the *Constitution Act, 1967*, the *Constitution Act, 1982*, the *Canada Act, 1982*, and a number of other amendments and orders, as defined in section 52(2) of the *Constitution Act, 1982*. For ease of reference, in this Chapter the term Constitution will be used to refer to the *Constitution Act, 1982*.

federal and provincial governments by the constitution, and how the courts have interpreted those powers, determines how and when provincial laws apply to First Nation lands. This in turn has a direct impact on the legal frameworks existing on First Nation lands.

Section 91 of the constitution sets out a number of specific and exclusive legislative powers of the federal government. Section 91(24) gives the federal government the exclusive legislative authority over “Indians, and lands reserved for Indians.” This power is in fact two powers: a power to make laws in relation to Indians, regardless of location, and a power to make laws in relation to lands reserved for Indians, regardless of whether Indians or non-Indians reside on such lands. It is under the jurisdiction set out in section 91(24) that the federal government has enacted legislation that relates to aboriginal people and First Nation lands, including the Indian Act, the *First Nations Fiscal Management Act* (FMA), and the *First Nations Land Management Act* (FNLMA).

It should be noted that Canada’s power to legislate in respect of Indians and lands reserved for Indians means that Canada can, in effect, legislate in areas that would otherwise be within provincial jurisdiction. As long as the main or primary aspect of the legislation relates to Indians or lands reserved for Indians, it is within Canada’s exclusive jurisdiction. For example, the *Indian Act* includes provisions respecting the use of reserve lands which would fall under the provincial “property and civil rights” power if not relate to Indian land.

The specific and exclusive areas of provincial jurisdiction are set out in section 92 of the constitution, which includes jurisdiction over matters respecting “property and civil rights in the province” under section 92(13). It would not be an overstatement to say that this head of power is by far the most important of the provincial powers, because it encompasses the entire body of private law between persons in Canada, including property, succession, family, contracts and torts. It is under this head of power that provinces have enacted virtually the entirety of the legal framework that supports economic development off First Nation lands, as well as other federal lands.

How does the constitutional division of powers, the provincial power over property and civil rights, and the exclusive federal authority over Indians and lands reserved for Indians, impact the legal framework on

First Nation lands? It impacts the legal framework by limiting the application of provincial laws on First Nation lands, such that key aspects of the provincial legal framework for economic development do not apply on First Nation lands. Further, not only do aspects of the legal framework not apply, in many areas, there is uncertainty as to which aspects apply and which do not.

The general rule for the application of provincial laws to Indians and lands reserves for Indians is that they apply, subject to some important qualifications and exceptions. First, provincial laws validly falling under a provincial head of power (such as 92(13)) apply of their own force, provided the law is a law of general application that is not directed specifically at Indians, and provided it is not inconsistent with a federal law on the same subject matter. For example, provincial laws respecting motor vehicle licensing are laws of general application that apply to Indians and on Indian lands. These laws are general laws applicable to everyone in the province, and are not aimed specifically at Indians or to the use of Indian lands. A second example is provincial laws relating to wills and estates. These are also provincial laws of general application that apply to everyone in the province; however, because the *Indian Act* contains specific provisions respecting the wills and estates of Indians residing on reserve lands, the provincial wills and estates laws do not apply to Indians residing on reserve lands.

A second exception to the general rule is that provincial laws relating to the use of Indian lands (as opposed to Indians) are inapplicable because of Canada's exclusive jurisdiction in this area. This rule applies even to provincial laws of general application, and in circumstances where Canada has not legislated in the area. This includes municipal land use bylaws, expropriation laws, and any aspect of provincial legislation that relates to the use or possession of land.<sup>139</sup> This exception is significant because it means that provincial laws that are crucial to land development do not apply on First Nation land, even where there are no existing federal laws in that area.

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<sup>139</sup> This has been confirmed in *Surrey v. Peace Arch Enterprises* (1970) 74 WWR 380 (BCCA), *Re Stony Plain Reserve* [1982] WWR 302 (Alta CA) and *Derrickson v. Derrickson* (1986) SCJ No.16. In the latter case, the Court found that the provincial *Family Relations Act* dealing with the ownership and possession of Indians lands cannot apply to an Indian reserve because that is an area of exclusive federal jurisdiction.

In addition to provincial laws applying by their own force, provincial laws of general application also apply to Indians (but not Indian lands) by the operation of section 88 of the *Indian Act*.<sup>140</sup> Section 88 incorporates provincial laws into federal law, which then apply to Indians as federal law unless there is other federal law (including First Nation law) that is inconsistent.<sup>141</sup> For example, the courts have held that provincial child welfare legislation applies to aboriginal children living on reserve lands through the operation of section 88 of the *Indian Act*. The incorporated provincial law will only apply so long as Canada does not enact child welfare law for aboriginal children, or a First Nation does not enact its own child welfare laws.<sup>142</sup>

There are two challenges arising out of the application, non-application or partial application of provincial laws to reserve lands. First, the non-application of land-related provincial legislation creates an extensive legal gap on First Nation lands in areas of land regulation. Second, the possible application of provincial laws creates uncertainty because in many areas the extent that a provincial law may apply cannot be determined with certainty, unless the question has been decided by the courts. A legal and administrative framework does not support investment if the scope and application of the framework cannot be determined with certainty and without recourse to the courts.

### **What legal framework is needed to support investment?**

The provincial jurisdiction over property and civil rights, as well as other provincial powers such as direct taxation, underlie the extensive legal framework that supports investment and economic development on lands other than First Nation lands. These laws provide the legal certainty and

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<sup>140</sup> Section 88 provides as follows: "Subject to the terms of any treaty and any other Act of Parliament, all laws of general application from time to time in force in any province are applicable to and in respect of Indians in the province, except to the extent that those laws are inconsistent with this Act or the *First Nations Fiscal Management Act*, or with any order, rule, regulation or law of a band made under those Acts, and except to the extent that those provincial laws make provision for any matter for which provision is made by or under those Acts."

<sup>141</sup> This was explained by the Supreme Court of Canada in *Dick v R.*, (1985) 2 SCR 309.

<sup>142</sup> Cases include *Alberta (Director of Maintenance and Recovery) v. Potts* [1979] WWR 560 (Alta QB), *Alexander v Maxime* (1995) BCLR (3d) 294 (BCCA).

confidence that enables virtually every business transaction in Canada. For this discussion, these laws can be broadly grouped into three categories: laws that support private property rights, laws that provide public regulation of property rights, and laws that support public services. Provincial laws relating private property rights include numerous laws that support both real property and personal property rights, as well as more general laws that enable business transactions by securing contractual rights. The following table provides an overview of the typical provincial laws that support private property rights, and considers their application on First Nation lands.



Provincial Legislative Area	
Real property law	<p>Description: Laws that create legal rules and principles, and modify common law principles, to provide the foundation for real property dealings. Includes laws respecting how land and interests in land are owned, transferred, pledged, subdivided, leased, and foreclosed. These include property law acts to provide rules for transfers, charges, mortgages and easements.</p> <p>Application: These laws do not apply on First Nation lands. Federal legislation including the <i>Indian Act</i> and the FNLMA address land tenure, and the use and management of reserve lands.</p>
Registration, survey and subdivision of land	<p>Description: Laws that establish the land title system and govern all aspects of land transactions, including rules respecting land surveys and strata subdivision, and transfer procedures, forms, requirements, and assurances.</p> <p>Application: These laws do not apply on First Nation lands. There are federal land deed registries and federal survey legislation.</p>
Civil laws	<p>Description: A broad group of provincial laws that establish the rules regulating civil matters in the province. These include laws respecting personal property security interests, court order enforcement, family matters and child custody and employment standards.</p> <p>Application: Some aspects of these laws will apply on First Nation lands as laws of general application. Some aspects will be inapplicable because of paramount federal legislation or because they relate to Indian land. Importantly, aspects of these laws that tie in with registrations in the provincial land title system will not be operative on First Nation lands.</p>
Wills, Estates and Trusts	<p>Description: laws establishing rules and procedures for making wills, estate administration, creating and settling trusts, and acting as a trustee.</p> <p>Application: Some aspects of these laws could apply on First Nation lands. In some areas, existing federal legislation applies, such as wills and estates of Indians residing on First Nation lands.</p>

Provincial laws that provide public regulation of property rights include numerous laws under which the government regulates the ownership, use and management of property and interests in property. This includes a broad range of regulatory laws ranging from land use and development regulation, to resource use, and environmental protection requirements. The following table provides an overview of the typical provincial laws regulating property rights, and considers their application on First Nation lands.

Provincial Legislative Area	
Expropriation	<p>Description: Laws that set out the processes for expropriation and that set out the specific expropriation powers of governments and other entities.</p> <p>Application: These laws do not apply on First Nation lands. Federal laws govern expropriation on First Nation lands.</p>
Natural Resource Regulation	<p>Description: Laws that govern the exploration, development and exploitation of natural resources including water, mines, minerals, forestry, and oil and gas.</p> <p>Application: The application of provincial laws varies depending on the province but generally do not apply. There is specific federal law in some areas.</p>
Land use regulation and development control	<p>Description: Provincial laws create an extensive regulatory framework that governs the use and development of land. This is achieved through a combination of direct provincial regulation, and delegated local government regulation. The laws include planning, zoning, building size and siting, development permitting, sign regulation, tree-cutting regulation, and subdivision servicing and control.</p> <p>Application: These laws do not apply on First Nation lands. There is limited federal enabling legislation for zoning and other regulatory powers.</p>
Environmental Management and Assessment	<p>Description: Laws setting requirements for environmental management and protection (including investigations, completion of site profiles, and remediation of contaminated sites) and environmental assessments for projects.</p> <p>Application: These laws do not apply on First Nation lands. There is federal legislation in these areas.</p>
Heritage conservation	<p>Description: Laws setting out rules and procedures for identification, designation and conservation of heritage sites and artifacts.</p> <p>Application: These laws do not apply on First Nation lands.</p>

Provincial laws that support public services include numerous laws under which the government provides both hard and soft services to lands within the province. These services are essential to support economic development and growth, and support higher private land values. These laws include the full range of servicing laws typically made by local government, as well as building codes and other health and safety laws. The following table provides an overview of the typical provincial laws supporting public services, and considers their application on First Nation lands.

Provincial Legislative Area	
Building regulation	<p>Description: Laws applying building codes and systems of building permitting and inspection, and providing for the registration of builders' liens.</p> <p>Application: These laws do not apply on First Nation lands. There are some federal regulations including the federal Building Code that apply on First Nation lands.</p>
Fire regulation and Safety Standards	<p>Description: Laws creating the fire code, appointing fire personnel, and establishing fire safety requirements &amp; inspections. Laws setting standards for electrical, gas, boilers, refrigeration, pressure valves &amp; pipes, amusement rides etc. and persons doing regulated work.</p> <p>Application: These laws do not apply on First Nation lands. There are some federal regulations including the federal Fire Code that apply on First Nation lands.</p>
Local Services	<p>Description: Laws providing for services to lands and regulations respecting those services usually provided by local government. Services include water, sewer, drainage, and waste management.</p> <p>Application: These laws do not apply on First Nation lands. Federal legislation enables the provision of local services.</p>
Health and safety	<p>Description: Laws to ensure the health, safety and the protection of persons and property and to regulate the use of public places.</p> <p>Application: These laws do not apply on First Nation lands. There is limited federal enabling legislation for some of these powers.</p>
Land Taxation and Assessment	<p>Description: Laws setting out the powers and framework for real property assessment and taxation of land. These taxes raise revenues for local services, schools and health services.</p> <p>Application: These laws can apply to non-Indian occupants of reserve lands, although only 2 provinces tax reserve lands. There is federal enabling legislation for First Nations to tax their reserve lands.</p>

It was stated above that Canada has exclusive jurisdiction over Indian lands, and that Canada can legislate within areas that would otherwise be provincial, provided the main or primary aspect of the legislation is within its jurisdiction. This means that Canada could legislate in virtually all of the “provincial” legislative areas on First Nation lands and fill all the gaps in the legal framework. However, there is no requirement to legislate. Although Canada has legislated in some of the above areas, either through direct federal legislation, such as federal building and fire codes, or by enabling First Nation governments to make laws applicable to their lands, there remain extensive gaps in key areas such as land use, property governance, and service provision.

There are a number of possible factors that contribute to the lack of federal regulations on First Nation lands. One may be that Canada lacks the legislative experience, expertise or interest in many of the key areas because it is the provinces that generally create those frameworks. Many of these legislative areas are complex and inter-related to other areas, requiring extensive policy and legislative development by provincial governments. Another reason may be that Canada does not have the resources to directly legislate in all required areas. Filling all of the gaps would be a significant legislative task, in particular because there may not be a single legislative approach that would be suitable for all First Nations.

Regardless of the reasons, First Nations wanting to facilitate investment on their lands need to determine how best to fill legislative gaps, and what available options best suit their individual community’s needs.

### **What options exist for First Nations wanting to create a legal framework to support investment?**

For many years after its creation in 1876, the *Indian Act* was the sole source for the federal legislative framework on First Nation lands. All “Indians” and “Indian Bands” operated exclusively under that Act, and it contained all of the rules and powers relating to reserve lands. More recently, additional options have been created. These include comprehensive legal frameworks such as modern treaties, and sectoral legislation that enables First Nations to use powers in specific legislative areas. Comprehensive approaches give First Nations greater control and

law-making powers over a broad range of jurisdictions, including governance, lands, economic development, education, health and resource allocation. Sectoral legislation is aimed at a specific legislative area or jurisdiction, and can supplement or replace existing *Indian Act* provisions. For example, the FMA provides a framework for taxation, financial management and pooled borrowing that does not exist under the *Indian Act*.

This topic provides an overview of the existing options for building legal frameworks on First Nation lands. It also discusses the proposal for a new *First Nations Property Ownership Act* (“FNPOA”) that would provide a new sectoral option for First Nations wanting to own and manage their existing reserve lands.

### ***The Indian Act***

The *Indian Act* continues to provide the legal framework for most First Nations in Canada. It provides for the creation of reserves, for creating and transferring interests in reserve lands, and for the taxation of interests in reserve lands. With respect to land regulation, it enables First Nations to make certain regulatory bylaws that apply on their reserve lands. These include, under section 81 of the *Indian Act*, the ability to regulate:

- the health of residents on the reserve;
- traffic;
- pounds and pound-keepers;
- construction and maintenance of watercourses, roads, bridges, ditches, fences and other local works;
- zoning and the prohibition of the construction or maintenance of any class of buildings;
- the construction, repair and use of buildings; and
- water services.

The regulatory powers in the *Indian Act* are limited to those specifically set out, as a result it does not provide sufficiently broad powers to enable a First Nation to create a comprehensive legal and administrative framework similar to those existing in adjacent provincial jurisdictions. Although the specified powers include key regulatory areas, such as zoning and building regulation, they do not include the scope and breadth

of regulatory powers given to adjacent local governments. For example, local governments generally have a broad power to provide any service they determine necessary, and to regulate, prohibit and impose requirements in respect of that service. Section 81, in contrast, does not give a broad authority to provide services, but rather a specific power to construct and maintain local works, and to construct and regulate water services.

Despite its limitations, the *Indian Act* continues to provide First Nation Councils with certain core bylaw-making powers that are used by many First Nations across the country. If a First Nation exercises the full scope of its jurisdiction under the *Indian Act*, it could have in place a number of key bylaws that would fill many - but not all- legal gaps on its reserve lands. However, most First Nations do not exercise the full scope of their regulatory powers, likely due largely to a lack of administrative capacity. First Nation communities in Canada have relatively small populations - with a mean population of 700 - making it unrealistic in many cases for a community to have sufficient resources to build their own comprehensive legal frameworks from the ground up.

### **Comprehensive Legislation**

Comprehensive legislative approaches consist of modern treaties (also known as comprehensive land claims agreements) and comprehensive self-government agreements. In both cases, the negotiated agreements are reflected in legislation, and provide the First Nation will significantly expanded jurisdiction, including extensive law-making powers over their lands.

### **Nisga'a Final Agreement and Tsawwassen Final Agreement**

Both of these Agreements represent final, comprehensive and binding treaty agreements among the governments of Canada, British Columbia and the respective First Nations. Modern treaty negotiation is a lengthy, costly and multi-stage process. In British Columbia, only a few treaty agreements have been ratified since the beginning of the modern treaty process. For First Nations that enter into treaties, those agreements include extensive rights and powers including the right to self-government, the transfer of land and resources, and the authority to manage those lands and resources.

Although the specific provisions of the Tsawwassen and Nisga'a agreements differ, both include extensive and comprehensive governance and law-making powers. In addition to self-government powers, these First Nations have regulatory powers in areas that include land ownership and registration, fiscal powers (including taxation), forestry, fisheries, wildlife management, environmental management and assessment, the administration of justice, and heritage protection.

Both of these agreements provide sufficient law-making powers for the First Nations to fill regulatory gaps on their lands. The Agreements also provide clarity respecting the extent that provincial laws apply to the treaty lands. Finally, the Agreements remove these communities from the *Indian Act* and its reserve land system. Their existing reserve lands, as well as additional lands, were transferred to the First Nation in fee simple and registered in a land title registry. The Tsawwassen lands are registered in the provincial system, while Nisga'a has created its own land registry.

Modern treaties provide the jurisdiction, land ownership and certainty necessary for First Nations to fill legislative gaps and support investment. However, in many areas, First Nation must make the necessary laws to fill those gaps, and the issue of administrative capacity may remain a barrier to the full exercise of a First Nation's jurisdiction. The Nisga'a Final Agreement came into force and effect on May 11, 2000, and the Nisga'a Lisims Government, governed by a 36-member legislature, has enacted approximately 35 laws.

The Tsawwassen Final Agreement came into force and effect on April 3, 2009, and the Tsawwassen Government, governed by a 12 to 16 member legislative assembly, has enacted approximately 24 laws since that time, as well as regulations under those acts. Although in both cases this represents significant law development, the work is on-going.

### **Sechelt Indian Band Self-Government Act and Westbank First Nation Self-Government Act**

The Sechelt Indian Band and the Westbank First Nation operate under self-government agreements that, although not comprehensive treaties, enable these First Nations to exercise greater governance and law-making powers. In both cases, *Indian Act* powers continue to apply to some extent, but the First Nations primarily operate under their self-

government powers.

In the case of Sechelt, the former reserve lands were transferred to the Band in fee simple for the use and benefit of the Band and its members.<sup>143</sup> The *Sechelt Indian Band Self-Government Act* (“Sechelt Act”) provides Sechelt with broad governance powers relating not only to the regulation of land and property (including access, zoning, expropriation, building regulation, property management, roads and public order), but also in areas such as health, education and natural resources. In addition to the powers specifically enumerated, the Council may exercise any legislative power granted to it by or pursuant to an Act of the legislature of British Columbia.<sup>144</sup> This allows Sechelt the potential to access a full range of provincial and municipal powers with respect to its lands. Finally, Council has the power to adopt any laws of British Columbia as its own law if it is authorized by its constitution to make laws in relation to the subject matter of those laws. This power enables the Band to adopt by reference existing provincial laws, without having to make its own laws. The *Indian Act* continues to apply to the Band and to its lands, except to the extent of any inconsistency with the Sechelt Act, the Band constitution and any Band laws.

In the case of Westbank, the *Westbank First Nation Self-Government Act* (“Westbank Act”) provides for jurisdiction in relation to the management, administration, government, control, regulation, use and protection of Westbank Lands. This jurisdiction includes:

- procedures for the transfer or disposition of interests in Westbank Lands;
- zoning and land use planning;
- use, construction, maintenance, repair and demolition of buildings and other structures; and
- access to Westbank Lands and trespass on Westbank Lands.<sup>145</sup>

Westbank has enacted over 35 laws in key areas include land use, service

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<sup>143</sup> See sections 22-25 of the *Sechelt Indian Band Self-Government Act SC 1986 c.27*.

<sup>144</sup> Section 15 of the SIBSGA

<sup>145</sup> *Westbank First Nation Self-Government Agreement*, s. 103.



provision, subdivision, development and servicing, building regulation, water, sewer, traffic, fire, garbage, noise and nuisance. With respect to land ownership, Westbank lands remain reserve lands owned by Canada and interests in those lands are registered in the Westbank First Nation Land Registry, a sub-registry of the federal Self-Governing First Nations Land Registry.

Both of these self-government agreements provide sufficient law-making powers for the First Nations to fill regulatory gaps on their lands. In both cases, these First Nations have made laws in a number of areas that have filled regulatory gaps, particularly in relation to land management. However, as with treaties, it is the First Nation that must make the necessary laws to fill the legislative gaps, and capacity can hinder law development. As well, these agreements do not provide clarity respecting the application of provincial laws to the First Nations' lands.

### **Sectoral Legislation**

Comprehensive legislation is a result of individual First Nations undertaking negotiations with federal and provincial governments to reach agreements that will apply only to that First Nation. In contrast, recent sectoral legislation can have broader application because it creates frameworks that are then available for First Nations to use in the future. In addition to providing expanded jurisdiction to fill legislative gaps, sectoral legislation can offer administrative efficiency through standards, sample laws and harmonization with provincial jurisdictions. Modern sectoral legislation includes the FNLMA and the FMA discussed above, and the *First Nations Commercial and Industrial Development Act* (FNCIDA). The use of these legislative frameworks is optional for First Nations.

### ***First Nations Land Management Act***

First Nations that choose to come under the FNLMA can exercise broad law-making powers over their reserve lands in respect of land use, resource and environmental management, and the provision of services. Under this legislation, First Nations essentially take over the management of their lands from the federal government, and a number of provisions of the *Indian Act* cease to apply. These include sections 53 to

60 of the *Indian Act*, which deal with the management of reserves and surrendered and designated land.<sup>146</sup> Although the bylaw-making powers in section 81 of the *Indian Act* continue to apply, any laws a First Nation makes under the FNLMA prevail over bylaws made under section 81.<sup>147</sup> First Nations choosing to enter into the FNLMA regime begin by making a Land Code, a core document that includes key aspects of how the lands will be managed by the First Nation. The FNLMA also includes expanded powers to make laws related to land management, including laws respecting:

- interests or rights in and licenses in relation to first nation land;
- the development, conservation, protection, management, use and possession of first nation land;
- the regulation, control or prohibition of land use and development including zoning and subdivision control;
- the creation, acquisition and granting of interests or rights in and licenses in relation to first nation land and prohibitions in relation thereto;
- environmental assessment and environmental protection;
- the provision of local services in relation to first nation land and the imposition of equitable user charges for those services; and
- the provision of services for the resolution of disputes in relation to first nation land.<sup>148</sup>

Importantly, the law-making powers in the FNLMA are broadly drafted and set out a non-exhaustive list of powers within the broad authority. As well, the FNLMA specifies that the powers include matters arising out of or ancillary to specific law-making powers. The approach taken in the FNLMA marks an important advance in how powers are given to First Nation governments, one that ensures First Nations have sufficient authority to create the scope of laws necessary on their lands.

First Nations operating under the FNLMA have the ability to fill many significant legal and administrative gaps on their reserve lands, and

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<sup>146</sup> See section 38 FNLMA.

<sup>147</sup> See section 20(4) FNLMA.

<sup>148</sup> Section 20, *First Nations Land Management Act*.

have the on-going support of the First Nations Land Management Resource Centre, a First Nations institution established under the legislation. However, each community must find the resources to develop their own land code and each additional law or policy necessary to fill these gaps. Although federal funding is provided, developing a full complement of laws that are enabled under the legislation can be hindered by a lack of financial and administrative capacity. First Nation lands remain reserve lands held by Canada, and interests in those lands are registered in the federal First Nations Land Registry System.

### ***First Nations Fiscal Management Act (FMA)***

First Nations that choose to come under the FMA benefit from a comprehensive property taxation framework that provides a broad range of fiscal and governance powers. When a First Nation opts in the FMA, certain taxation-related sections of the *Indian Act* cease to apply.<sup>149</sup> In its place, the FMA provides First Nations with expanded authority to make taxation laws that include property value tax, service taxes, development cost charges and business activity taxes. First Nations also have the express authority to make delegation laws and taxpayer representation laws to support the taxation regime.

In addition to expanded taxation powers, the FMA enables First Nations to make financial administration laws, and leverage property tax within a borrowing pool for long-term financing of infrastructure. The FMA also established three institutions to oversee and provide support for taxation (the First Nations Tax Commission), financial management (the First Nations Financial Management Board) and borrowing (the First Nations Finance Authority).

First Nations opting into the FMA can benefit of expanded fiscal powers from those under the *Indian Act*, and have access to additional fiscal management resources as well as pooled borrowing opportunities. These additional tools build and administrative structure support investment on First Nation lands. Another important aspect of the FMA is the use of standards and sample laws, which is discussed below. The use of sample laws and other supportive tools in the administration of the

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<sup>149</sup> Sections 83(1)(a) and (d) to (g) and 84, as well as regulations under s.73(1)(m) of the *Indian Act*.

FMA supports efficiency and harmonization and can assist First Nations in overcoming administrative capacity issues.

***First Nations Commercial and Industrial Development Act (FNCIDA)***

FNCIDA creates a framework under which the federal government, on the request of a First Nation and with the agreement of the province, can apply specified provincial acts and regulations to reserve lands by incorporating those laws by reference into a FNCIDA regulation.<sup>150</sup> When a FNCIDA regulation is made, it has the effect of taking provincial laws and making them into federal laws by incorporating those laws into a federal regulation that applies to specified reserve lands. FNCIDA itself does not contain any substantive regulations, and has no impact unless a First Nation works with Canada and a province to create a regulation that applies to the First Nation's lands.

To date, the FNCIDA regulations apply provincial regulatory regimes in areas that include oil and gas development, environmental protection, environmental assessment and forest regulation.<sup>151</sup> In each case, the regulations incorporate specified provincial acts and regulations, subject to adaptations, and apply those regimes to the specified reserve lands.

FNCIDA enables First Nations to, in effect, extend provincial regulatory regimes onto reserve lands to fill important regulatory gaps. FNCIDA is project based, in that regulations are made to enable a specific commercial or development project. In some areas, adopting existing provincial regimes, including enforcement mechanisms and staff, is by far the most efficient approach for First Nation communities. As well, harmonizing the on-reserve regulatory regime with the adjacent provincial regime creates efficiency and may increase investor confidence on reserve. However, the cost of regulatory development to

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<sup>150</sup> Section 5 of FNCIDA sets out the two conditions: regulations cannot be made unless the Minister has received a council resolution requesting the regulations and, if the regulations specify a provincial official by whom, or body by which, a power may be exercised or a duty must be performed, an agreement has been concluded between the Minister, the province and the first nation council for the administration and enforcement of the regulations by that official or body.

<sup>151</sup> See the Fort Mckay Oil Sands Regulations, the Fort William First Nation Sawmill Regulations and the Haisla Nation Liquefied Natural Gas Facility Regulations.

the First Nation, as well as to Canada and the province, are high and such regulations may only be appropriate for investments with very high rates of return.

### **The proposed First Nations Property Ownership Act (FNPOA)**

In 2006, a number of First Nation communities put forward a new legislative proposal to the federal government that will, if implemented, provide an expanded framework for First Nations to own and govern their lands. The proposed FNPOA would be optional, sectoral legislation that includes the following key aspects:

- *First Nations would own their current reserve lands in fee simple.* Existing reserve lands would be transferred to the First Nation and its members in fee simple. Although these lands will remain federal lands under section 91(24), they will no longer be held in trust for the First Nation. As fee simple owners, First Nations and their members will no longer have their lands owned by Canada and administered by AANDC.
- *First Nation lands would be registered in a Torrens land title system.* Once under the FNPO system, First Nation lands would be registered in a federal Torrens land title system that would guarantee title and provide rules respecting the registration of charges and their priority. This system would provide an efficient, electronic registration system modeled on provincial Torrens systems.
- *First Nations and their members could choose to transfer or leverage their lands.* First Nations and their members will have the ability to decide if they wish to sell or lease their lands to third parties. Lands can also be used as security for financing. These decisions will be made by the First Nation and its members rather than by the federal government. Importantly, lands would remain First Nation lands under the First Nation's jurisdiction regardless of ownership.
- *First Nations would have expanded governance and jurisdiction over their lands.* FNPOA would provide expanded jurisdiction to First Nations to govern and exercise jurisdiction over their lands. These powers would include expanded law making to enable comprehensive land management and the regulation and provision of local services. First Nations would also have the power to

expropriate land for community purposes, and the right to have escheated land returned to the First Nation.

- *First Nations will have access to a “ready to use” legal framework.* FNPOA would provide a new approach to filling legislative gaps on First Nation lands, using a combination of First Nation law-making powers and federal regulations, as well as express powers to incorporate provincial laws by reference. In key law-making areas, federal regulations will create “ready to use” frameworks based on best practices and harmonization with provincial jurisdictions where appropriate. First Nations can decide to apply these frameworks to their lands or they can make their own laws. This would enable First Nations to overcome limitations in administrative capacity and move forward with implementation rather than law development.
- If implemented, the FNPOA legislative framework will enable First Nations that choose to opt in to efficiently and effectively build the legal frameworks necessary to facilitate investment on their lands. The FNPOA proposal addresses the key issues that support investment on First Nation lands. First Nations would own the land, have a title system that guarantees title, and have expanded law-making jurisdiction and governance powers. The provision of “ready to use” laws and the ability to incorporate provincial laws will assist First Nations to build legal frameworks despite issues of financial and administrative capacity.

**How do the existing options for creating legal frameworks compare?**

Each of the above frameworks provides additional jurisdiction for First Nations to build legal frameworks on their lands. In this topic, these options are assessed against four objectives that build investor confidence:

1. *Protecting jurisdiction:* First Nation governments should have the authority to create or implement their legal frameworks on their lands. This enables First Nations to preserve their government jurisdiction over their lands, and to provide the legal framework that best promotes their comparative or competitive regional advantage.
2. *Increasing administrative efficiency:* Regulatory options should be administratively efficient and cost effective, and minimize switching costs (the costs of moving from the old system to the new one). This

can include providing for standardization, using best practices, and harmonization with other jurisdictions. Regulatory options should reduce transaction costs for investors.

3. *Increasing market value:* Regulatory options should raise market value of First Nation lands, including by being more familiar to users and improving property right certainty.
4. *Strengthening access to capital and improve local services:* Regulatory options should improve financing opportunities, including by providing greater certainty to investors. They should also provide certainty and a revenue stream to raise the quality of local services.

The following table assesses each of the frameworks against these four objectives.

	Protect jurisdiction	Administrative efficiency	Increase market value	Access to capital & local services
Comprehensive Treaty Agreement	Expanded, broad governance & jurisdiction.	First Nation makes its own legal framework.	Fee simple title to all lands & increased certainty.	Property taxation of non-members by agreement with the province. No access to pooled borrowing under FMA except by regulation.
Comprehensive Self-government Agreement	Expanded, broad governance & jurisdiction.	First Nation makes its own legal framework. In some cases can adopt some existing provincial laws.	Usually remain reserve lands. Market value can increase because of direct administration by First Nation.	Property taxation usually under <i>Indian Act</i> . No access to pooled borrowing under FMA except by regulation.
FMA	Expanded jurisdiction over property taxation and other fiscal matters.	Uses standards, sample laws, software development to facilitate law development and administration, and provincial harmonization.	Remain reserve lands. Market value may increase due to taxation.	Access to pooled borrowing under statutory framework.



	Protect jurisdiction	Administrative efficiency	Increase market value	Access to capital & local services
FNLMA	Expanded jurisdiction over land management.	First Nation makes its own land code and associated laws.	Remain reserve lands. Market value may increase due to direct administration by First Nation.	Access to FMA. Increased control over their services.
FNCIDA	Creates federal regulations on First Nation lands.	Regulations directly apply specified provincial legal and administrative frameworks.	Remain reserve lands. Market value may increase due to improved legal framework.	Not applicable.
FNPOA	Expanded, broad, governance & jurisdiction.	First Nation can use the ready to use framework, and can incorporate provincial laws by reference. Frameworks will reflect best practices and harmonization.	Fee simple title to all lands. Lands registered in a Torrens registry with guaranteed title. All land decisions made by the First Nation.	First Nations can borrow under the FMA, and can waive s.89 of the <i>Indian Act</i> to enable securitization of lands. Increased control over their services.

## **Why should First Nations use a standardized approach in developing their legal framework?**

In business, efficiencies are created by the use of standards. Standards are everywhere. They can relate to the size of a shipping container or a standard process for making a car's engine. Private sector standards can be established by a company for internal use or by a corporate sector for voluntary compliance by corporations within that sector. Standards can be public sector standards established by government, public agencies, or regulatory or self-governing bodies, and can be established by statute, regulation or under specific standard-making authority.

Standards can be classified based on many different criteria, including their purpose (i.e. what are they intending to achieve?), scope (such as international, national or provincial), intended user group (who are they intending to reach?) and whether they are voluntary or mandatory.

This discussion focuses on standard procedures, laws and services that help facilitate investment. The reason that standards are so important is that they offer many benefits, including the following:

- *Standards can reduce uncertainty and transaction costs.* Standards do this by allowing users to have confidence in a particular product, service or process, which then reduces costs associated with searching for information, assessing quality, and developing contracts or relationships. A common example is the use of standardized currency. We trust the value of our currency and this confidence reduces our costs for transactions because we do not need to assess its value before we use it. Standardized currency has significantly reduced the transaction costs of trade, reduced the costs of products and services, and improved economies. This is one of the reasons that countries seek standards in trade agreements and try to harmonize their systems. This economic benefit is so significant that almost all countries in the world are willing to accept common standards and forgo some of their sovereignty in exchange for the economic benefits of increased trade.
- *Standards can create network externalities.* As the number of users of a standard increases, so do the number of further innovations that use the standard. A good example is the number of applications associated with the iPhone operating system. As there are more users of the iPhone, there is a greater incentive for developers to create

more applications for the technology. Each of these applications builds on the value of the existing technological standard.

- *Standards can reduce the costs of production.* Established standards allow users to learn by doing and become more proficient at a task or process. This is known as specialization. The more times you do something the better you get at it and production costs fall, creating economies of scale.

An economic objective of the FMA was to reduce the costs of doing business on First Nation lands by promoting standards. It accomplishes this by creating a legislative framework supported by standard-making powers for the FNTC and the FMB. These standards form part of the legislative framework, and complement the requirements of the FMA and the regulations under the act. The FNTC uses its standard-making powers to promote standardized local revenue laws and local revenue administrative systems. The standards create requirements that must be met by First Nations when making their local revenue laws under the FMA. The FMB uses its standard-making powers to encourage standardized financial management laws and financial management systems.

For the FNTC and the FMB, standards are an integral part of a service continuum. Sample laws, developed to reflect all legal requirements under the FMA, support the FNTC and FMB standards. The use of standards and sample laws has in turn supported the development of standardized tax administration software for use by First Nations taxing under the FMA. The combination of the legislation, regulations, standards, sample laws and software provides a foundation for curriculum and training.

The FNTC and FMB standards provide benefits to First Nations, taxpayers and investors. First Nations benefit in at least four ways from FMA standards. First, it significantly lowers their cost of law development. Second, it supports common professional standards and training among tax administrators. Third, it provides a strong political base in the event of a legal challenge. Fourth, it improves the First Nation credit rating by enhancing the confidence of lenders.

Investors benefit from the FMA standards because the standards support harmonization with adjacent jurisdiction and consistent

approaches among First Nations. When FMA standards achieve national or regional harmonization, an investor's cost of doing business decreases because they are not required to learn a new system for each First Nation. This can reduce research and legal costs, because approaches the investor has taken off reserve or on other First Nation lands can be more readily adapted. Standards also reduce investment risks. For example, FMB standards for financial management raise investor confidence in the management of the First Nation fiscal system.

Taxpayers benefit from FMA standards because it provides them certainty about future costs and gives them confidence that they will receive quality local services at a tax rate comparable to other jurisdictions. Standards provide taxpayers with confidence of equal treatment in assessment methodology and appeal processes, and provide certainty regarding rates, expenditures and financial management.

**What type of a lawyer can best develop a legal framework that supports investment?**

Building the legal frameworks necessary to encourage and facilitate investment on First Nation lands requires significant legal resources and time. In other words, First Nations will be investing their time and money in legal counsel to provide advice and draft the laws and procedures required to create the legal frameworks. Choosing legal counsel for this work will be one of the first and most important decisions a First Nation will make when it chooses to opt into a legislative framework and undertake law development.

All Canadian lawyers must have certain requirements in order to practice law. These are a law degree, completion of an articling year, passing the qualification exams, and having a practice license with the applicable provincial law society. However, once these requirements are met, a lawyer may offer services in any area of law, regardless of specific expertise or experience. There are a number of different areas of law, some of which are well known (family, criminal, tax, corporate, civil litigation), and others that are more obscure (admiralty, aviation, construction, health, securities). Many lawyers have general practices where they offer a wide range of legal services, while others become specialized in one or more areas. Finding a lawyer is generally not difficult; however, it can be challenging to find the right lawyer for a

specific project.

First Nations use legal counsel for a variety of different tasks, each of which will require certain skills and knowledge in one or more areas of expertise. The following table sets out different types of projects and considers what skills and areas of legal expertise would be required:

Type of Project	Legal area and skills required
A First Nation wishes to incorporate an economic development corporation. The First Nation wishes to be a majority shareholder and will partner with a corporate partner. The corporation will then lease lands for a business development.	Areas: corporate law, business law, real estate law Skills: negotiation, contract drafting, lease drafting
A First Nation wishes to commence a legal action against Canada to make a claim for aboriginal title to certain lands.	Areas: aboriginal law, litigation Skills: advocacy
A First Nation wishes to negotiate and draft a service agreement with the adjacent municipality to provide water and sewer services to its lands.	Areas: business and commercial law, municipal law Skills: negotiation, contract drafting
A First Nation wishes to borrow money to finance a construction project. It needs to negotiate the terms of the loan, and find a general contractor to oversee the project.	Areas: banking and finance law, construction law Skills: negotiation, contract drafting
A First Nation has decided to enter into the FNLMA and needs to draft a Land Code and associated laws and policies.	Areas: business and commercial law, administrative law, land use and planning law, finance law, real estate law, aboriginal law Skills: legal drafting
A First Nation has decided to build the legal framework necessary to support investment on its lands.	Areas: business and commercial law, administrative law, land use and planning law, construction law, finance law, real estate law, environmental and natural resource law, aboriginal law Skills: legal drafting

It is unlikely that one lawyer would have all of the expertise and skills necessary to advise or represent a First Nation on all of the above matters.

Importantly, First Nations should expect to use different legal counsel for different matters, and should not feel obliged to use only one lawyer or law firm for all of its needs. When a First Nation decides to build the legal framework necessary to support investment, the necessary expertise and skills required for its legal counsel will depend on the specific law development it will undertake. It may be that more than one lawyer would be necessary to meet all of the requirements.

In each case where a First Nation requires a lawyer, the following questions should be considered:

- What areas of legal expertise are required for this work?
- What skills are required for this work?
- Have we undertaken similar work in the past? If yes, would our legal counsel on that matter be a good choice for this work? If no, have we worked with a lawyer on other matters that may have this expertise and skills?

If a First Nation does not have a lawyer for a project and needs to find one, consider:

- Asking for a recommendation from lawyers the First Nation has used for other matters, explaining what areas of expertise and skills are required.
- Asking other First Nations, governments or businesses that have implemented similar projects for recommended lawyers.

If a First Nation is considering using a lawyer they have not worked with previously, it will be important to first speak with the lawyer and ask questions to determine if he or she has the expertise and skill set necessary. Questions to ask include:

- How long have you been practicing law?
- What are your areas of expertise?
- What projects have you done that are similar to the First Nation's project?
- Do you have the interest and the time necessary for this project?

In addition to ensuring a lawyer has the necessary expertise and skills, it is also important that the First Nation administration have confidence

that they can develop a strong working relationship with the lawyer. Simply put, the lawyer needs to be someone they can and want to work with.



CHAPTER 5

# ELEMENTS OF A COMPETITIVE FIRST NATION INVESTMENT CLIMATE: FISCAL FRAMEWORK

**S**ince the failed 1975 effort to reject government funds, First Nations in Canada have begun to build their economies, collect revenues and deliver services to their citizens – activities many tribes in the United States had already begun. In other words, First Nations in Canada have begun to assert their jurisdiction over their lands. This chapter focuses on one basic question – how do First Nation and tribal governments pay for the cost of delivering services that support community well-being and economic growth? Stated differently, what kind of fiscal relationships do First Nations and tribes need to ensure that the quality of their public services and infrastructure are similar to those in the rest of Canada and the United States? Competitive infrastructure and public services are necessary for First Nations and tribes to attract more private investment. Rooted in these questions are a number of related questions that guide this chapter:

- What is a fiscal relationship?
- Why is a fiscal relationship important for economic development?



- How does the fiscal relationship work off reserve in Canada and the United States compared to on reserve?
- What is wrong with the First Nation or tribal fiscal relationship?
- What is necessary to fix the First Nation or tribal fiscal relationship?
- What revenue options are available to First Nations and tribes?
- How can First Nations and tribes implement their transfer options?
- How can First Nations and tribes use their independent revenues to implement their service responsibilities?
- Which service responsibilities should First Nations and tribes implement?
- What are the problems with the First Nation and tribal transfer system?
- What can be done to improve these transfer systems?

Although most of the context of this chapter will be based on the fiscal relationship amongst First Nations and governments in Canada, some of the same questions, issues and solutions can be applied to tribes in the United States.

### **Learning Objectives**

- Explain why investors care about a government's fiscal relationship.
- Describe how services and infrastructure are paid for by non-First Nation, non-tribal governments.
- List the problems of the First Nation or tribal fiscal relationship.
- Develop a briefing note about First Nation or tribal revenue options to increase financial self-sufficiency.
- Analyze possible service responsibilities and identify which ones First Nations or tribes should assume.
- Describe the role of transfers in a fiscal relationship and identify effective transfer elements.

### **What is a Fiscal Relationship?**

In its simplest form, a fiscal relationship is essentially the answer to the question, “How are public services to citizens provided, produced and paid for?” Imbedded in this question are four simple questions that encompass what a fiscal relationship actually is:

1. Which government provides which services?
2. Which government pays for these services?
3. Which government has which revenue jurisdiction?
4. How does the system of transfers protect national service standards?

### **Why is the Fiscal Relationship Important for Economic Development?**

Investors look at a government’s fiscal system to:

- Gauge certainty over future levels of taxation and costs;
- Ensure local services and infrastructure can be financed and maintained; and
- Assess transparent and reliable government financial information and statistics to facilitate the development of revenue and cost projections.

### **Investors need to know many things about the fiscal relationship, most notably:**

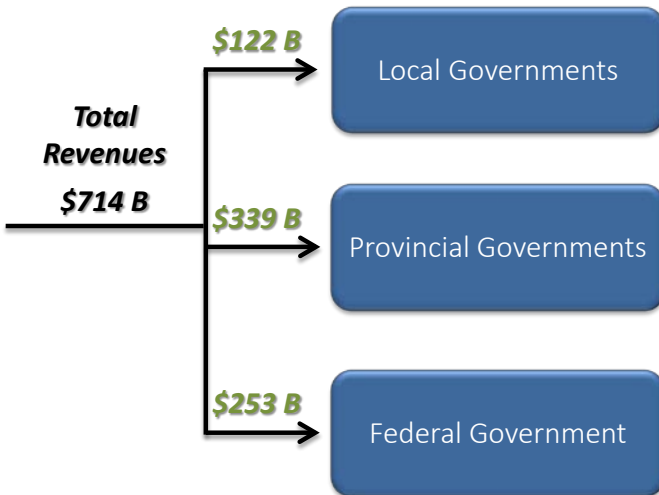
- Which revenues the government collects and which revenues it has the power to collect;
- How secure and stable those revenues are;
- How tax rates are determined;
- Service responsibilities;
- How quality is assured;
- If infrastructure development is supported;
- The division of service and financial responsibilities between governments; and
- How government finances are reported and managed.
- A fiscal relationship that provides this information and is transparent and stable will provide investors with sufficient

certainty and assurance. A flawed fiscal relationship leads to uncertain investors, subsequently under-investment, and market failure for the particular jurisdiction.

**How does the Fiscal Relationship Work for Non-First Nations in Canada?**

The federal, provincial and local governments in Canada have been refining the answers to the fiscal relationship questions since Confederation. The resulting answer to these questions in a federation like Canada (or the United States) is called fiscal federalism. As a result, many Canadians know, for example, who is responsible for their public health care, education, street cleaning and statistics and which government pays for these services. The figures below will provide a broad overview of how Canadian fiscal federalism works.

*Consolidated Revenues by all Governments in Canada*<sup>152</sup>



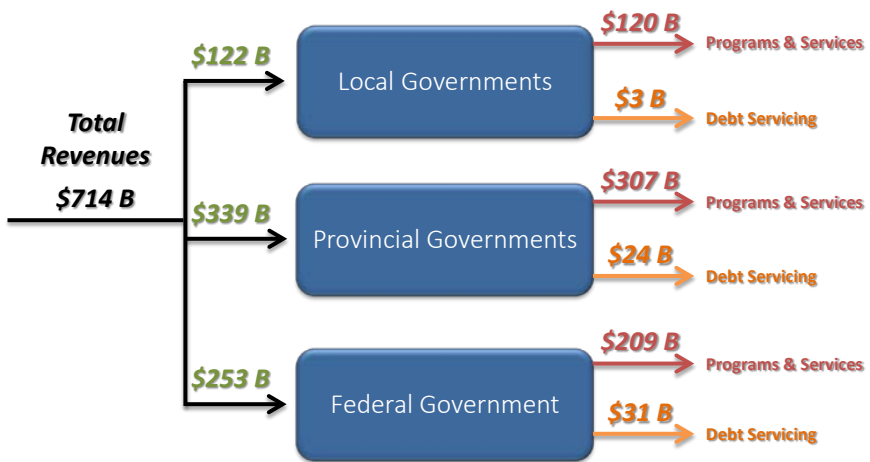
The figure above shows that in 2008-2009 there was \$714 billion in

<sup>152</sup> Statistics Canada. 2010. *Cansim Tables, General Government Revenues, Financial Management System.*

revenues collected by all governments in Canada.<sup>153</sup> Revenue comes into the system from taxes and other public sources. The federal government collected \$230 billion in revenue, and its main source was income taxes followed by consumption taxes. Provincial governments took the largest share of the tax pie at \$339 billion. The provinces derive revenue from personal and corporate income taxes, provincial sales taxes, property and resource related taxes. Local governments collect the smallest share of taxes. Their main source is property taxes. Most local governments collect property taxes for education on behalf of the provincial government. These revenues are divided among the three levels of governments to pay for their services.

The figure below shows in broadest terms the expenditures of the three levels of government in Canada.

***Expenditure Responsibilities of all Governments in Canada<sup>154</sup>***



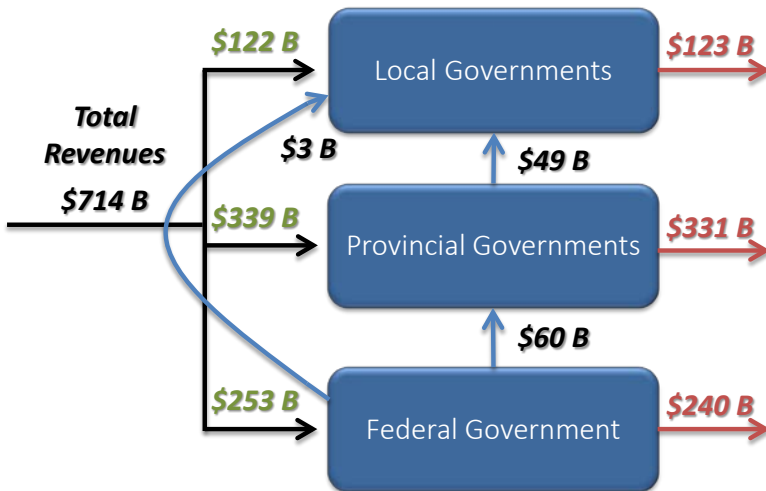
Each government also has expenditures. Their specific expenditure

<sup>153</sup> This is the latest year that Financial Management System (FMS) Government statistics were developed by Statistics Canada for all three levels of government.

<sup>154</sup> Statistics Canada. 2010. *Cansim Tables, General Government Revenues, Financial Management System*. These figures represent fiscal year 2008 when provincial governments had an \$8 billion surplus and the federal government had a \$13 billion surplus.

responsibilities are partially defined in the constitution but there is some overlap. As can be seen above, the federal government receives more revenues than its costs of services. This is because each level of government has to make expenditures on servicing past debts. The amount of debt servicing they pay depends on how much they borrowed in the past and the interest rate on that debt. Additionally, this fiscal room means that it can transfer revenues to the provincial and local governments and provincial governments transfer resources to local governments. This ability to transfer resources is the glue of fiscal federalism. These transfers are used to top up provincial and, subsequently, local government revenues so that national and provincial standards can be maintained, national and provincial interests can be aligned and third-party affects between jurisdictions can be minimized. The figure below shows the way in which fiscal transfers occur between governments in Canada.

*Fiscal Transfers between Governments in Canada*



The federal government transfers about \$60 billion to the provinces each year. These are considered social service expenditures. The provinces in turn transfer about \$40-50 billion to the local governments to help pay for their costs of government and infrastructure. The federal government

also transfers about \$3-5 billion directly to local governments to help cover the costs of infrastructure. The difference between one government's ability to pay for its services with its own revenues has been called the fiscal imbalance in Canada.

One of the key characteristics of this imbalanced system is that the federal government takes a relatively larger share of tax revenues relative to its service responsibilities than the provinces. These differences are then reconciled through the system of federal cash transfers to the provincial governments. These transfers allow the provincial governments to generally spend more money than they receive through direct taxation. Major federal transfers are comprised of two principle elements: the Canada Health and Social Transfer (CHST) and the Equalization program. Health and social transfers are paid to every province. Equalization is paid only to provinces that qualify because the value of their tax room is below a provincial average. However, in both cases, the amount of cash actually transferred is determined by formula.

### **What is wrong with the First Nation Fiscal Relationship in Canada?**

First Nations and First Nation governments were an afterthought in the design of the Canadian fiscal framework. They were viewed as being federal responsibilities. Gradually, over time however a relationship began to emerge. Indian Band Councils were developed that began to assume some delegated responsibilities and jurisdiction and these were financed through the federal government. The federal government also began to define its responsibilities with respect to First Nations more narrowly over time, which forced many First Nations to rely on provincial service agencies rather than federal ones. In an attempt to foster greater efficiency, a diverse web of agreements was established between the federal and provincial governments to provide services to First Nations. Moreover, gradually First Nations began to develop their own revenues and the administrative capacity and service responsibilities that go with them.

However, the developments all came after the architecture of the overall Canadian fiscal framework had been developed. As a result, improvements from the First Nation perspective have been slow in arriving, have often-required major political effort and arose only in response to large contradictions within the existing system. The chief

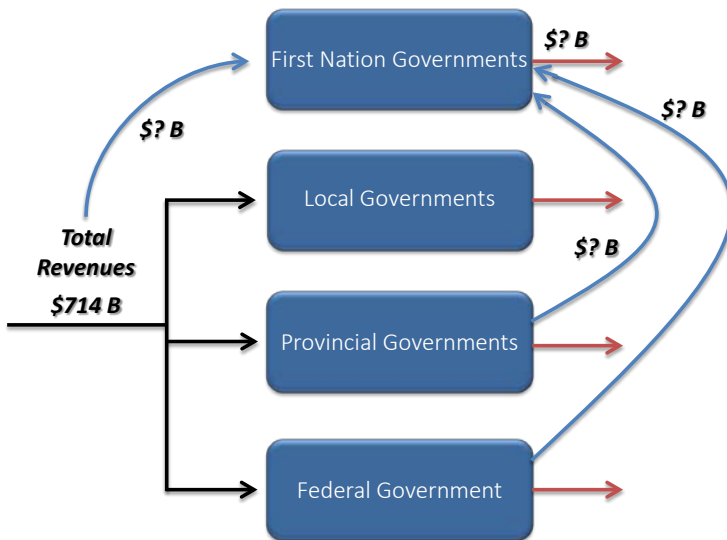
problem remains. The Canadian fiscal framework was never designed to accommodate the aspirations of First Nation people. The current fiscal relationship between First Nations and Canada is not adequately supporting First Nation aspirations to develop stronger economies and improve their lives. It is also not allowing First Nations to become self-governing by preventing them to make choices, decisions and plans over the long-term. Therefore, there are strong concerns over whether the current fiscal relationship is able to help First Nations escape from the cycle of poverty and sub-standard community infrastructure and services. The following are examples of the many problems have emerged with respect to the existing fiscal relationship:

- *First Nations lack access to their own revenues.* This includes resource revenues and related tax jurisdictions. As a result, they are stymied in asserting their own interests, obstructed in developing capacity and handcuffed in terms of developing services that meet their own unique needs.
- *There is no link between support for First Nation and non-First Nation services.* Under the existing system of transfers, there is no explicit link between support for First Nation services and support made for similar services in the rest of the country. As a result, there are issues with respect to comparability of services and a sense that First Nations must compete against the rest of the country for resources.
- *There are disputes surrounding service responsibilities.* There are considerable disputes between the federal and provincial governments regarding service responsibilities for First Nation citizens and appropriate payment for services. When neither government can agree on who is responsible, no one is responsible and service quality suffers as a result.
- *First Nations are too dependent on federal transfers.* A much larger share of First Nation government revenues come from transfers from other governments than any other government in Canada. As a result, spending decisions are largely determined by other governments rather than at the community level. Additionally, federal funds come with strings attached and, in some cases, terms and conditions that inhibit a First Nation government from making a practical decision for the community.

- *The existing transfer system in support of First Nation governments is cumbersome.* It is short-term and not transparent. In fact, it appears highly subjective and conditional. It creates large administrative burdens and it is focused on control-oriented accountability conditions because it has failed to support incentives for good government. It is clearly insufficient to support services and infrastructure comparable to the rest of the country and is viewed by many First Nation leaders as providing very limited flexibility.
- *First Nations lack access to capital.* The existing relationship has not allowed First Nation communities to access capital for capital improvements on anything close to the terms available to other communities. This has severely limited their development prospects.

The result is that First Nation governments do not fit into the fiscal framework in Canada. The challenge is illustrated in the figure below when adding First Nation governments to the top of the fiscal framework figure.

**The Challenge: A Fiscal Framework for Self Government**



There are many questions marks in the figure because there is no



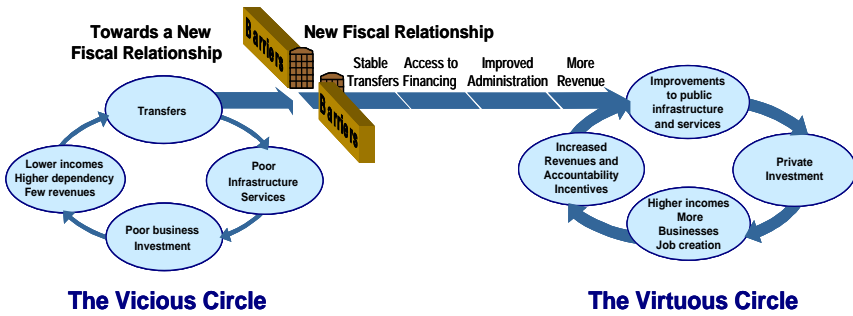
consistent reporting standard for First Nations and subsequently a great deal of statistical uncertainty. The table below describes these uncertainties.

**Uncertainty under the First Nation Fiscal Framework**

Questions	Uncertainty
How much revenue do First Nation governments generate on their own?	It is not clear how much own source revenue from taxation and other sources First Nation governments are receiving because much of this is not reported.
What are the expenditures of First Nation governments?	First Nation expenditures on goods and services and debt servicing are not clear because these responsibilities are not always outlined and not reported in any standardized statistics.
What are the cost drivers of these expenditures?	
How do First Nation expenditure levels and service quality compare to other governments?	
What are the formulas governing the transfer of money to First Nation governments from the federal government?	It is not clear the amount of transfers they are receiving from the federal and provincial governments because there are no transparent formulas like the CHST and Equalization.
What are the deficits and debts of First Nation governments?	

**What is needed to fix the First Nation fiscal relationship?**

The current First Nation fiscal relationship features unstable federal transfers, unimplemented treaty rights and aboriginal title, poor or untrustworthy services, no access to long-term funds for infrastructure and small amounts of discretionary revenues. The figure below shows that an improved fiscal relationship could lead to a virtuous circle for First Nations.



The circle on the left characterizes the condition of most First Nations. Due to limited revenue, infrastructure and services are sub-standard, which creates a poor investment climate and limited incomes for First Nations members due to limited revenue raising options. This is the vicious circle of transfer dependency.

The improved fiscal relationship could be the gate to a virtuous circle for First Nations (circle on the right). As illustrated in a previous chapter, the virtuous circle is characterized by more stable, certain and secure revenues for First Nation governments which allows them to provide better services and infrastructure to their communities. This, in turn, will lead to higher levels of investment into First Nation communities that would create higher incomes for First Nations members and, at the same time, higher revenues for First Nation governments. This would complete the circle and kick-start another iteration of the process.

First Nations require a new fiscal relationship. The new fiscal relationship would have to increase First Nation government revenues, lower the costs of doing business on First Nation land, provide access to long-term capital through stable revenues, clarify jurisdictions, increase local decision-making powers, and improve the standards and delivery of services. This would allow First Nation governments to exercise increased autonomy and greater self-reliance, First Nations fiscal authority, resource-revenue sharing, and incentives for enhancing First Nation own source revenue capacity.

In order to establish a new fiscal relationship, the three central elements of any fiscal relationship must be improved: revenues, services or service responsibilities, and transfers. The specific elements of an improved fiscal relationship are:

1. *First Nations should be allowed to assume jurisdiction over services that the First Nation decides it can perform best to satisfy First Nation citizens.* This includes all aspects of land management, most local services and it should be up to the First Nation to develop programs and relationships in treaty functions such as education and health. Creating the institutions to undertake this will require agreements among provincial and national as well as First Nation governments.
2. *Share more direct revenue room with First Nations roughly commensurate with their service responsibilities.* Once again, provide a First Nation institutional framework to facilitate the sharing of greater revenue room with First Nations.
3. *Develop a First Nation transfer system that ensures service quality comparable to other Canadians without destroying the incentives First Nations have to engage in economic development.*
4. *The assumption of jurisdiction over services must be accompanied by revenue generation.* First Nations need access to direct revenues that are able to create incentives for better government, create a better business environment and ultimately foster First Nations' economic growth. Subsequently, this will reduce the fiscal pressures created by First Nation poverty and make it easier for all governments to meet their particular fiscal challenges.

The next section will briefly describe specific First Nation revenue sources and how they have evolved to their current state within the First Nation fiscal framework. The following section will outline service responsibilities, the importance of clarifying which government is responsible for which services and the significance of linking those responsibilities to revenues. The last section will outline the current government transfer system and how it affects First Nation communities.

### **A Brief History of First Nation Revenue Generation**

From 1876 until 1918, First Nations were prevented from raising tax revenues to fund local governments that could have developed local rules and supplied commercial-grade infrastructure.<sup>155</sup> In 1875, the Mohawk

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<sup>155</sup> Bruhn, Jodi & John Graham. 2008. *In Praise of Taxation: The Link between Taxation and Good Governance in a First Nations Context*. Institute on Governance. Available at [www.iog.ca](http://www.iog.ca).

community of Tyendinaga tried to create a tax system, collecting property taxes from their lessees to pay for local services but the Department of Indian Affairs ordered it stopped.<sup>156</sup> Additionally, traditional methods of redistributing wealth among First Nations were also banned: thirst dances due to the permit and pass system of 1881, preventing First Nations from leaving their reserves or trading outside their communities;<sup>157</sup> potlatches in 1884;<sup>158</sup> sun dances, giveaways, and similar ceremonies in 1890.<sup>159</sup> Agricultural production was diminished by the 1889 policy of peasant farming, whereby each family on western reserves was supposed to become self-sufficient with one acre of wheat and one acre for vegetables and a cow or two.<sup>160</sup> A 1918 amendment to the *Indian Act* enshrined many of these previous restrictions. The legislation effectively turned First Nations into economic wards of the state with no ability to raise revenue or redistribute funds.<sup>161</sup>

However, the *Indian Act* was amended to remove many of the restrictive revenue provisions, and First Nations began developing their revenue sources. The modern era of First Nation revenue generation began in 1951.

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<sup>156</sup> National Archives of Canada. RG10, volume 1975, reel C-11125, file: 5683; National Archives of Canada. RG10, volume 2350, reel C-11206, file: 70,077.

<sup>157</sup> Leslie, John & Ron Macguire. 1972. *The Historical Development of the Indian Act*. Indian and Northern Affairs Canada, Treaties and Historical Research Centre. Second Edition; Buckley, Helen. 1992. *From Wooden Ploughs to Welfare: How Indian Policy Failed in the Prairie Provinces*. Montreal and Kingston: McGill Queen's University Press; Royal Commission on Aboriginal Peoples. 1996. *Report of the Royal Commission on Aboriginal Peoples*. Volume 1, Part 2, Chapter 9. Available at [www.ainc-inac.gc.ca](http://www.ainc-inac.gc.ca).

<sup>158</sup> Debates of the Senate of the Dominion of Canada. 1884. Fifth Parliament, Second Session; Tobias, John. 1991. *Protection, Civilization, Assimilation: An Outline History of Canada's Indian Policy*. In J.R. Miller, ed., *Sweet Promises: A Reader on Indian-White Relations in Canada*. Toronto: University of Toronto Press.

<sup>159</sup> Tobias, John. 1991. *Protection, Civilization, Assimilation: An Outline History of Canada's Indian Policy*. In J.R. Miller, ed., *Sweet Promises: A Reader on Indian-White Relations in Canada*. Toronto: University of Toronto Press.

<sup>160</sup> Carter, Sarah. 1991. *Two Acres and a Cow: Peasant Farming for the Indians of the Northwest, 1889-1897*. In J.R. Miller, ed., *Sweet Promises: A Reader on Indian-White Relations in Canada*. Toronto: University of Toronto Press.

<sup>161</sup> In a recent interview, Clarence Jules Sr. recounted how as a six year old in 1932 he can remember the RCMP breaking up a local potlatch ceremony where revenues were collected for community purposes. That would be the last local potlatch ceremony he could remember.

**How can First Nations generate more independent revenues?**

First Nation independent revenues are collected by First Nation governments either through the assertion of tax jurisdiction, a revenue sharing arrangement with another government related to tax jurisdiction or the operation of commercial enterprise. The tables below summarize these three sources of independent revenues available to First Nation governments based on the legal authority, the administrative arrangement, favorable circumstances and some examples. Select revenue sources are further explained following each table.

## Jurisdictional Revenue Sources Available to First Nation Governments

Revenue	Authority	Administration	Favorable Circumstances	Examples
Property Tax	Fiscal Management Act (FMA)	First Nation	Commercial, residential or industrial development	170 FNs collecting property taxes
Federal Sales Tax	First Nation Goods and Services Tax Act (FNGST)	Tax Collection Agreements	All circumstances favorable	40 First Nations collecting FNGST
Provincial Sales Tax		Tax Collection Agreements	Sale of goods on First Nation lands	Alcohol tax in Saskatchewan Sales tax in New Brunswick
Income Tax	Yukon agreement Nisga'a agreement	Tax Collection Agreement	Comprehensive Agreement	14 Yukon Self-Governing First Nations Nisga'a Nation
Tax for services	FMA	First Nation	Sale of local services (water, sewer, etc.)	Shuswap Nation in BC
Development Cost Charges	FMA	First Nation	Pending development	Tk'emlúps te Secwepemc, Tsawout
Royalties	Indian Act First Nation Oil and Gas and Moneys Management Act	Indian Affairs; First Nation	Oil, gas or mining on First Nation lands	Many First Nations in Alberta and Saskatchewan
Business Activity Taxes	FMA	First Nation or Tax Collection Agreement	Commercial developments	Some First Nations in BC

## Property Taxes

The modern era of First Nation property tax began in 1988 when a significant amendment was made to section 83 of the *Indian Act* to clarify First Nation jurisdiction. It allowed First Nation councils to levy property taxes on leased reserve lands. Furthermore, in 2005, the *First Nations Fiscal Management Act* (FMA) was passed which provided First Nations with access to a more comprehensive property taxation framework, additional revenue raising tools, such as development cost charges and the ability to use property tax for debenture financing. The number of First Nations levying property tax grew from 11 in 1991 to 111 in 2006 and to 170 in 2013. There are now 99 First Nations on the FMA schedule as of 2013.<sup>162</sup> Moreover, 99 First Nations have passed section 83 bylaws under the *Indian Act* as of 2013.<sup>163</sup>

In order to build capacity for implementing taxation using the FMA, programs like the Certificate in First Nation Tax Administration offered by the Tulo Centre of Indigenous Economics<sup>164</sup> in Kamloops, BC, provide training for First Nation tax administrators. The program also assists those wanting to learn more about First Nation tax administration or those working under s.83 of the *Indian Act*.

## First Nation Goods and Services Tax

The First Nation Goods and Services Tax (FNGST) is a tax on all consumption of items deemed taxable under the GST that occur on reserve or settlement land (Yukon Territory). The rate of the FNGST is equal the rate of the GST and the federal portion of the Harmonized Sales Tax (HST). The Canada Revenue Agency administers the FNGST on behalf of the taxing First Nation and acts as the agent of the First Nation for collecting and administering the tax and for enforcing the

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<sup>162</sup> Government of Canada. 2013. *First Nations Fiscal Management Act* (S.C. 2005). Available at <http://laws-lois.justice.gc.ca/eng/acts/F-11.67/>.

<sup>163</sup> First Nations Tax Commission. 2013. Available at [www.fntc.ca](http://www.fntc.ca).

<sup>164</sup> Founded in 2008, the Tulo Centre of Indigenous Economics is a not-for-profit institution dedicated to delivering certificate and diploma programs in First Nations Tax Administration, First Nations Economics and other areas of administration. Tulo creates capacity to build the legal and administrative frameworks for markets to work on indigenous lands.

First Nation tax law. There are also no exemptions from the FNGST. In 2011, 23 First Nations had introduced the FNGST and, at that time, they were receiving tax revenues that totalled approximately \$12 million per year.<sup>165</sup>

**Revenue Sharing Sources Available to First Nation Governments**

Revenue	Authority	Administration	Favorable Circumstances	Examples
Utilities	Hydro Agreements	Provincial Crown Corporations; First Nations	Hydro projects on First Nation lands	First Nations in BC, Ontario, Manitoba and New Brunswick
Traditional Territories	Agreements with federal government	Indian Affairs; Province; Resource Company; First Nation	Oil, gas or mining on First Nation lands	13 comp, claims in effect
	Agreements with Province			Some agreements in place in Saskatchewan and Alberta
	Impact Benefit Agreements (IBA)			Approximately 50 IBAs
Aboriginal Title Taxation	Proposals for taxation presumed aboriginal title lands	To be developed	Pipelines, mining, oil and gas on aboriginal title lands	To be developed

<sup>165</sup> Aboriginal Affairs and Northern Development Canada. (2012). *Fact Sheet – Taxation by Aboriginal Governments*. Online at <http://www.aadnc-aandc.gc.ca/eng/1100100016434/1100100016435>.



### **Revenue Sharing in Traditional Territories**

This includes comprehensive claims, royalty revenue sharing and Impact Benefit Agreements (IBAs). Comprehensive claims are negotiated in areas where Aboriginal title has not been dealt with by other legal methods. They are negotiated among the federal, provincial or territorial and First Nation governments. Many Comprehensive Claims agreements contain provisions regarding the sharing of resource revenues. A good example is the Gwich'in Agreement signed in 1992. This agreement provided the Gwich'in First Nation 7.5 per cent of the first \$2 million of resource royalty received by the government for that year and 1.5 per cent of any additional resource royalties received by the government in that year from the Mackenzie Valley.

Since 1987 there have been 49 IBAs, most of which are currently either in the exploration phase or in the development or producing phase.<sup>166</sup> IBAs are intended to ensure that First Nations benefit from mining projects and are compensated for the negative impacts of mines on their communities, their land and their traditional way of life. IBAs are different from other agreements in that they are private contracts between non-governmental parties and are subject to confidentiality provisions.

### **Aboriginal Title Taxation**

Resource development companies have been consulting with First Nations about proposed projects for a number of years. Often these discussions have led to impact or mutual benefit agreements between the companies and First Nations on matters related to employment, procurement, environmental matters, and revenues. In some cases, provinces (BC) have also engaged in resource royalty revenue sharing arrangements with First Nations.

The recent Supreme Court William decision on aboriginal title<sup>167</sup> has changed the dynamics of these discussions and agreements in two

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<sup>166</sup> IBA Research Network. (2013). *List of Known IBAs*. Available at [http://www.impactandbenefit.com/IBA\\_Database\\_List/](http://www.impactandbenefit.com/IBA_Database_List/).

<sup>167</sup> Supreme Court of Canada judgement in *Tsilhqot'in v. British Columbia* case at <https://scc-csc.lexum.com/scc-csc/scc-csc/en/item/14246/index.do>

fundamental ways. First Nations have a stronger ownership and possibly jurisdictional claim to lands that have proven aboriginal title. As a result, there is considerable property right, regulatory, and fiscal uncertainty on aboriginal title lands for all governments (including First Nations) and companies. This has impacted the investment climate on possible aboriginal title lands.

Some First Nations in BC want to assert tax jurisdiction over resource development and transportation projects in their traditional territory based on their aboriginal title claim. In particular, they are proposing to combine revenues obtained in agreements with companies and resource revenues obtained from provinces into a single First Nation aboriginal title tax. They have expressed a preference for a tax because it provides them greater revenue certainty, saves negotiation time, and provides the framework and resources for negotiating a new fiscal and governance arrangement with other governments.

**Commercial and Other Revenue Sources Available to First Nation Governments**

Revenue	Authority	Admin	Favorable Circumstances	Examples
Leasing	Bill C-115 amendment to the <i>Indian Act</i> <i>First Nations Land Management Act</i>	First Nation	Commercial, residential or industrial development	Many First Nations in Canada
Gaming	Agreements with province	Provincial government; First Nation	Commercial development	Some First Nations in Manitoba, Saskatchewan and Ontario
Commercial Ventures	<i>Indian Act</i> ; <i>First Nations Land Management Act</i> (FNLMA) <i>First Nations Commercial and Industrial Development Act</i> (FNCIDA)	First Nation	Commercial development	74 First Nations are on the FNLMA schedule Fort McKay First Nation and Squamish First Nation have used FNCIDA

**Leasing**

Under the 1895 version of the *Indian Act*, First Nations were able to lease reserve land. However, lands had to first be “surrendered” to the Crown. The Crown would then lease the land on behalf of the First Nation. It would collect the lease revenue and remit that revenue to the First Nation. The land was no longer considered part of the reserve. In 1988, Bill C-115 amended the *Indian Act* to make clear that leased lands were still part of an Indian reserve. Subsequently, the surrender process

was abandoned and replaced by a designation process (a form of zoning, specifying land use). In 1996, the Government of Canada and a group of 14 First Nation chiefs signed the Framework Agreement on First Nations Land Management. It provided the signatories with the opportunity to opt out of the *Indian Act* land administration sections and establish the legal status and powers required to manage and govern their lands and resources. The Framework Agreement was brought into effect by the passage of the *First Nations Land Management Act* (FNLMA) in 1999. There are currently 74 First Nations on the FNLMA schedule.<sup>168</sup>

### **Gaming**

In 1987, a Memorandum of Understanding was reached by provincial First Nations, the province of Manitoba and the federal government to establish a framework for negotiating specific agreements for gaming on reserve. In January 1990, the Opaskwayak Cree Nation (OCN) became the first in Canada to sign a First Nation Gaming Agreement. This agreement formerly designated the Opaskwayak Cree Nation Gaming Commission as the licensing authority responsible for the regulation of bingos, lottery and break open ticket sales, Monte Carlo casinos, etc. Shortly after this agreement was signed, the province legalized the placement of video lottery terminals in rural Manitoba, including a policy allowing their use on reserve. The OCN also signed the first Video Lottery Terminal Agreement in 1992. This led to negotiations with five Manitoba First Nations to host casinos on reserve land. These events were then mirrored in Saskatchewan and Ontario.

### **Commercial Ventures**

The environment for commercial developments has continued to improve over the last twenty years. The FNLMA allows First Nations the ability to use modern tools of governance. The elements that have helped lower the cost of doing business on First Nation lands include land codes, environmental and real matrimonial property law, improved law enforcement, agreements with provincial and municipal governments and legal status as a person for First Nations and First Nation councils. The

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<sup>168</sup> Government of Canada. (2013). *First Nations Land Management Act* (S.C. 1999). Online at <http://laws-lois.justice.gc.ca/eng/acts/F-11.8/>.

next major legislative development supporting commercial ventures on First Nation lands was the *First Nations Commercial and Industrial Development Act* (FNCIDA). This Act was prompted by the recognition that there was an inadequate regulatory regime for commercial and industrial development on First Nation lands. The lack of regulation was creating uncertainty that was discouraging investment. The Act allows a First Nation to ask the federal government to essentially import provincial regulations for commercial and industrial development projects on reserve. This subsequently provides an understandable and proven regulatory regime on reserve.

### **How should First Nations' service responsibilities be determined?**

There are four factors for a First Nations to consider when deciding if it should assume a specific service responsibility.

1. *Community preferences* – Each First Nation has the right of self-determination and will make service responsibility decisions based on political, historical, cultural and legal dimensions among other factors. As with all governments in a federal system, jurisdiction over specific activities must be clearly defined in relation to the national, provincial and local government activities. Within this system, community preferences, however, may be seriously constrained by fiscal realities and sound public finance.
2. *Fiscal Realities* – Service responsibilities have to be fiscally sustainable. The challenge that First Nation governments face is to determine the cost of delivering a particular service and then matching that up with a secure revenue source. A useful strategy for First Nations is to divide service responsibilities into three categories:
  - Service responsibilities provided by a First Nation that can be entirely paid from independent First Nation revenues. The First Nation must be secure that it can generate revenues to sustain the delivery of these services.
  - Service responsibilities that are provided by another government and entirely paid for by that other government.
  - Service responsibilities shared by First Nations and other governments and with a shared financial responsibility.
3. *Economic Growth* – First Nations should assume service responsibilities over areas that will facilitate investment and promote

economic growth. Services that reduce the cost of doing business by being in local control are ideal services to consider because more private investment generates more First Nation independent revenues.

4. *Principles of Public Finance* – Service responsibilities should also be selected based on some basic public finance principles: Within Canada two public finance principles are most important; there are several lesser criteria, and for First Nations there are also treaty obligations that need to be taken into account. The two primary criteria are “fiscal equivalence” and “equalization.”

### **Fiscal Equivalence**<sup>169</sup>

Fiscal equivalence means that the group that benefits from the provision of a service makes the decisions on that service and pays for it. This criterion encourages efficiency in deciding what is to be provided to citizens. It provides an incentive system where beneficiaries pay and they get to make the decisions on how much service to provide in comparison with its costs.

Most government services benefit only subsets of the Canadian population. For example, people in Vancouver will not frequent a library in Toronto and thus decisions over libraries and payment for those libraries should be made by the government of Toronto. If there are people who benefit but do not pay, then the service will tend to be under-provided and if there are people who pay but do not benefit then the service will tend to be over-provided. Some services are better provided by local governments, some by provincial and some by federal depending upon the size of the public that is able to utilize those services. This is what a federal system as well as the system of municipalities and other local governments within each province provides. First Nations need to be part of this system.

### **Equalization**

Within Canada, there is a long accepted tradition that residents in different provinces should all be able to afford an equivalent level of government services regardless of the tax base within the province. This

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<sup>169</sup> Olson, Mancur. 1969. The Principle of Fiscal Equivalence: The Division of Responsibilities among Different Levels of Government. *American Economic Review* 59 (2):479-487.

principle results in large transfers from those provinces with large tax bases to those with lesser tax bases. Unfortunately, this principle can encourage recipient provinces to spend inefficiently because their citizens do not have to pay for those services. It also appears that recipient provinces have not used the equalization revenues to make investments that would encourage economic development and end their status as a “have-not” province.

### **Treaty Obligations**

The government of Canada has treaty obligations to most First Nations. These obligations were created when First Nations gave up their rights to most of the land now occupied by non-First Nations. Treaty rights have not been honoured for many First Nations, and where they are honoured, it is primarily for functions like education and health. There are no treaty rights for creating the infrastructure and institutional rules to facilitate First Nation economic development. The focus in this text is precisely on those functions that will facilitate economic development, where First Nations have to assume responsibility. Within the three primary criteria that apply to the Canadian federal system, there are also lesser principles of public finance that include:

- *Equity* – This is based on the principle of ability to pay. That is, richer people pay more than poorer people do for the same service. This principle can be difficult for small governments to implement because wealthier people may simply move out to a jurisdiction with lower taxes. This is why large governments like provinces or the national government usually undertakes income redistribution.
- *Adaptability* – This is the ability to recognize and respond to changes in demand. The level of government that can adapt the quickest should provide the service. Typically, this argument supports local government provision, as a small bureaucracy is likely able to move and adjust to changes faster than a larger one.
- *Transparency* – This refers to a process that is open, understandable, honest and able to be questioned. The level of government that is able to provide the service in the most transparent manner should do so. In some cases this favors provision by the largest government so that rules are consistent throughout the country and in some cases this favors provision at the local level since local governments can

better respond to questions.

- *Contestability* – This refers to the use of competition to achieve the best value for money. The level of government that best encourages contestability should provide the service. This factor usually favors local provision.
- *Consistency* – There are some services where the same level of service is desired for all the citizens in a province or the entire country instead of having smaller governments adjust service levels to their own preferences. Provision of these services is usually by a higher-level government.
- *Certainty and Stability* – Revenue sources should be certain and stable to facilitate planning for future capital expenditures and infrastructure needs. Among traditional sources, property taxes, sales, and excise taxes tend to be most stable, with income taxes, especially progressive income taxes and taxes on capital gains tend to be least stable as they fluctuate more than the economy itself in upturns and downturns. Transfers need to be designed to be stable and predictable as well, something that is not the case with the current system.

It is important to note that all of the criteria are for the “provision” of services. Provision decisions include who benefits and makes the decisions, usually through an elected council, how services are to be financed, and how the services will be produced. How services will be produced involves a different set of criteria, among which are economies of scale. Some services are most efficiently produced by small organizations; others are most efficiently produced by large organizations. Some can be produced efficiently for a small area; others are most efficiently produced for very large areas. Different services, and the separate activities that make up a service, have different economies of scale. Thus, First Nations should expect to produce some services themselves, but many will be obtained through contracts or joint agreements with other governments or private firms.

A recommended strategy for First Nations choosing service responsibilities is the following. Firstly, use the incremental approach. Assume responsibility (jurisdiction) over those services that are most important for community preferences, economic growth and the ability to finance. It is especially important that First Nations interested in using



economic growth to obtain political independence should assume service responsibility over investment- cost reducing functions such as land use planning and management, property rights, local infrastructure. It may be appropriate to postpone the assumption of responsibility for services such as education and health where there are treaty obligations unless an agreement can be made to assume decision making with federal government financing. Second, as the First Nation economy and public revenues grow assume more service responsibilities from the category of shared responsibilities with other governments. Third, a First Nation government should recognize that the delivery and financing of some service responsibilities should remain with other governments in the federation for reasons related to public finance efficiency and fiscal realities.

### **What are the opportunities for First Nations to assume Service Responsibilities?**

First Nations have at least three concurrent options to assume service responsibilities.

1. *Comprehensive Agreements* – First Nations can create service clarity and new transfer systems through self-government negotiations and modern Treaties. The three most recent cases are the Nisga’a, Yukon and Westbank models. Examples of services responsibilities assumed by these First Nations include:
  - *Nisga’a Nation* – Community health programs and services, non-insured health benefits, payment of medical service plan premiums and BC ambulance fees, and income assistance and services. These involve treaty obligations and federal financing is included in the agreement.
  - *Yukon First Nations* – Social and welfare services, health care, training programs, adoption, guardianship, custody, care and placement of children, education programs, inheritance, wills, intestacy, administration of estates, solemnization of marriages and administration of justice. Again, these involve some treaty obligations and other areas where the national government provides income redistribution. A problem with both the Nisga’a and Yukon agreements is that historically the Canadian government has

not provided sufficient financing for the First Nation to provide service levels equivalent to those in the rest of Canada.

- *Westbank First Nation* – The WFN has passed bylaws under their Self-Government Agreement in regards to garbage collection, noise and disturbance control, fire protection, business licensing, land use, disorderly conduct and nuisances, health services and community protection. These primarily local services are critical to economic development. Westbank will provide most of the financing and can determine the service level that will promote economic development.
2. *Own Source Revenue Negotiations* – The federal government has recently developed an own source revenue (OSR) policy<sup>170</sup>. The main purpose is to reduce federal transfers to First Nations based on the amount of First Nation independent revenues. The policy is complicated based on a number of variables such as exempting some revenues, partially including others and phasing in the policy but the intent is to make First Nations more financially responsible for services. The policy does not address which services First Nation should be more financially responsible for, however its potential application provides an opportunity for First Nations to implement the recommended strategy. In particular, First Nations could choose to assume complete jurisdiction (delivery and financial responsibility) over selected services and forgo contributions from other governments for those services. The net fiscal result may be the same as the OSR policy but First Nations could gain important jurisdictions that could reduce investment facilitation costs and generate First Nation growth and revenues.
  3. *Sectoral Self-Government* – First Nations can also assume service responsibilities through sectoral self-government legislation that includes the *First Nations Land Management Act*, *First Nations*

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<sup>170</sup> Canada has indicated that it is reconsidering the application of this policy in response to the Supreme Court William decision. No new policy has been presented yet but there remains interest from First Nations and Canada in developing methods for First Nations to contribute to the costs of their government.

*Fiscal Management Act* and the *First Nation Oil, Gas and Money Management Act* (FNOGMMA). The FMA and FNOGMMA provide First Nations with revenues and expanded service responsibilities. The FNLMA provides more service responsibilities but only has limited revenue-raising abilities. Only the FMA explicitly links revenues and expenditures.

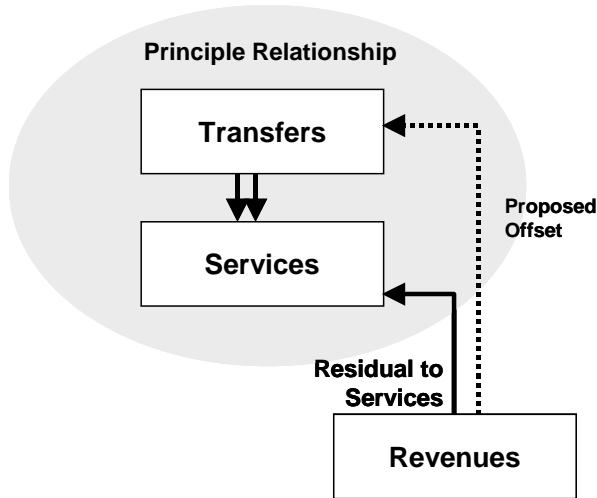
### **What are the problems with the current system of transfers to First Nations?**

The current system of financing for First Nations meets none of the criteria for a good public finance system that would encourage efficiency and result in the conditions that would promote economic growth on First Nation Lands.

The figure below illustrates in broad terms how the current system of First Nation transfers supports their fiscal relationship (this is known as a transfer based relationship). It is divided into the three central elements of any fiscal relationship – services or service responsibilities, revenues and transfers. The starting place for the current fiscal relationship is the transfer to First Nation governments.

In a transfer-based relationship, the starting point is a determination by the transferring government of the revenue requirements of the recipient government. This amount is then adjusted if other revenues are developed. Often this arrangement characterizes governments who are heavily dependent on transfers (as illustrated by the revenue object being located outside of the grey circle that is representative of the principle relationship).

## The First Nation Transfer Based Fiscal Relationship



Transfers to First Nation governments are intended to pay for services. There does not appear to be any public finance reason for which service responsibilities are assigned to First Nations. In addition, since these services are paid for by transfers it is difficult to call them responsibilities as they are more like service delivery contracts. Furthermore, the terms and conditions associated with these transfers make it difficult to assert that First Nations are delivering First Nation public services but instead are delivering the federal interpretation of First Nation public services. Finally, it is virtually impossible to determine whether these services are of a quality comparable to other Canadians given these overlapping service responsibilities between federal, provincial and First Nation governments. This system has five principle faults:

1. *Poor Transparency* – This system leads to few accountability incentives because without transparency between service responsibilities and governments, it is impossible to hold any one government responsible for poor First Nation public services. There is also little transparency in transfer formulas.
2. *No First Nation Jurisdiction* – A transfer dependent fiscal relationship means that the transfer recipient exercises little authority over program design, delivery or quality. First Nations do not have

the fiscal ability to implement independent public decisions and policies. They have neither clear revenue options nor clear service responsibilities. Until First Nation government transfer dependency is brought in line with Canadian norms, they are governments in name only. It could be argued that this transfer dependent relationship is a major contributor to the political frustration that First Nations feel. What is most troubling is that the proposed federal OSR policy threatens to entrench this situation permanently by always treating revenues as the residual.

3. *Poor Investment Climate* – The First Nation fiscal system is nothing like the rest of Canada. Their fiscal relationship is confusing to potential investors. It also creates concerns about financial and subsequently political stability, the high costs of doing business, the First Nation’s ability to finance competitive infrastructure, and the First Nation’s capacity to provide tax rate and service quality certainty. The results are a poor investment climate, little private investment and high fiscal costs of First Nation poverty for all governments. Little investment causes the vicious circle of transfer dependency to repeat.
4. *Poor Service Quality* – Between 1994 and 2006 the Auditor General of Canada undertook an extensive study of First Nation programs and services and concluded that virtually all First Nation services and infrastructure were below national standards.<sup>171</sup> This assessment of a system that has little transparency, accountability and jurisdictional clarity is hardly surprising.
5. *Inefficient* – When services are mainly financed through transfers from one government to another, the resulting reporting requirements and financial management accountability bureaucracy are large. The extensive reporting requirements for First Nations are confirmed in a number of Auditor General Reports. There has been no study about the size of the federal and First Nation financial management bureaucracy to support the transfer system but it is certainly larger than the financial management bureaucracy to support the federal-

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<sup>171</sup> Auditor General Reports on First Nation Programs are available at [http://www.oag-bvg.gc.ca/internet/English/parl\\_lpt\\_e\\_1703.html](http://www.oag-bvg.gc.ca/internet/English/parl_lpt_e_1703.html) and <http://www.aadnc-aandc.gc.ca/eng/1338471861166/1338472088479>.

provincial transfer system. In this regard, it is interesting that the federal government transfers about ten times more money to provincial governments than it does to First Nation governments.

### **What can be done to improve the First Nation transfer system?**

The model for an improved First Nation transfer system is the model taken for granted everywhere in Canada and in most federations. It involves three simple steps:

1. Identify service responsibilities for First Nation, tribal and other governments based on the fiscal principles discussed earlier.
2. For services identified as federal or provincial service responsibilities for reasons related to treaty or other legal obligations or for efficiency reasons, determine if the service is best delivered through a transfer to First Nation governments.
3. For these services which are the responsibility of another government but are delivered by a First Nation government, the responsible government should transfer the necessary resources to deliver the service up to an agreed upon standard.

This proposed transfer system would correct the five faults of the current system.

1. *Improved Transparency and Accountability Incentives* – The proposed system would have a stronger relationship between public revenues and public expenditures. This means people are more aware of whom they are paying and what they are paying for. This transparency between payment and services creates the basis for public accountability.
2. *Jurisdictional Clarity* – In this improved system, service responsibilities and revenue room will have been divided appropriately within the federal fiscal framework. Further, because First Nations have the opportunity to raise most of their own revenues to pay for their services, they are able to protect their jurisdictions. Clear jurisdictions coupled with the ability to pay for these services primarily themselves provide an incentive for governments to be innovative and develop more efficient and cost effective methods for service delivery.
3. *Strong Investment Climate* – The link between revenues and services means governments are interested in developing a strong investment

climate to ensure public revenues can sustain public expenditure requirements. This provides an incentive to work towards better governance structures, improved infrastructure and the right mix of taxes and services. Getting government right means more revenues and better public services.

4. *Better Service Quality* – Service quality improves for at least four reasons. First, clear service responsibilities mean citizens can hold the right government to account. Second, because this system is similar to the rest of Canada it is easier to compare service costs and outcomes. Third, service quality is a factor in attracting investment, and more First Nation revenue options provide a stronger incentive to compete for investment by improving service quality.
5. *Greater Efficiency* – This transfer approach would be more efficient because it would make the reporting and financial administration requirements for First Nations similar to those of other governments.

### **What are the options for First Nations to improve transfers?**

First Nations have a number of options to improve the transfer system. Some of these have been previously discussed so they will just be briefly reiterated. First, the FMA provides the nucleus for a new fiscal relationship with an improved transfer formula. It clearly links local revenues and local services. The more First Nations expand their local revenues the more they can assert jurisdiction over services. Second, First Nations can use the implementation of the federal OSR policy to advance a new transfer relationship by clarifying their (a) sole service responsibilities, (b) shared service responsibilities and (c) the service responsibilities of other governments and linking their independent revenues to (a) and (b) and basing their transfers on (c).

Two other options to develop a better First Nation transfer system that will be discussed in more detail in other sections of this book include service agreement negotiations and improved statistics. First Nations should develop service agreements with other governments to provide quality services at a fair price to their service eligible populations. Institutional support options to develop effective service agreements are discussed in the next chapter.

First Nations should also utilize opportunities to improve the reliability and timeliness of their statistical information. First Nations are

the only government not included in the national public accounts in Canada and this makes it difficult or even impossible to include them in national transfer formulas. The final chapter discusses opportunities for First Nations to improve their statistical information through administrative means and participation in the census.

One other option for First Nations to improve transfers is to participate in the periodic review and revision of the Canadian transfer system. Canadian fiscal federalism is flexible because it can reinvent itself as the result of fiscal, economic or political pressures. Federal-provincial forums provide a vehicle to coordinate changes to the Canadian fiscal system and for First Nations to advance their inclusion in this system.

### **Conclusion**

Improving the First Nation fiscal relationship in order to facilitate more investment on First Nation lands involves three elements:

1. Take advantage of options to clarify First Nation service responsibilities and those of other governments and provide a First Nation institutional and capacity development framework so First Nations can effectively assume these responsibilities.
2. First Nations should assert their revenue raising powers to generate resources roughly commensurate with the service responsibilities they choose to deliver. The FMA provides a mechanism to accomplish this and the institutional support to implement these new jurisdictions.
3. Begin to implement a First Nation transfer system based on the service responsibilities of other governments by combining strategies (1) and (2) with more service agreements and better statistics.

The benefits of this strategy could improve the First Nation investment climate by:

- Effectively implementing First Nation self-governing jurisdictions that support investors and capacity to implement these jurisdictions;
- Providing First Nations with the revenue raising options to pay for quality services and competitive infrastructure (as will be discussed in the next chapter); and



- Building confidence in First Nations as places to invest by improving financial transparency and creating financial stability.

The next chapter builds on the work in this chapter and discusses how to plan and finance the construction of business grade infrastructure in First Nation and possibly tribal communities.



CHAPTER 6

ELEMENTS OF A COMPETITIVE  
FIRST NATION INVESTMENT  
CLIMATE: BUILDING  
INFRASTRUCTURE

**T**he Westbank First Nation, located near Kelowna, B.C., provides an excellent example of economic development potential on First Nation lands and the returns from investing in public water, sewer and road infrastructure. In 1991, WFN collected annual property tax revenues of about \$1.5 million. They used a portion of these funds to develop business grade water, sewer and roads infrastructure. Following this investment and the establishment of the legal framework to support markets, WFN attracted roughly \$1 billion in private investment. As a result of this private investment, WFN collected roughly \$10 million in property taxes in 2009. In addition, WFN now enjoys an unemployment rate of virtually zero.

The Tk'emlups First Nation near Kamloops, BC is currently extending its sewer system agreement with the city to open up many more lands for investment. They are doing this because they will collect

more property taxes and development cost charge levies from investors. From their perspective, the initial public investment in infrastructure pays for itself through increased private investment and tax revenues.

The Squiala First Nation near Chilliwack has seen transportation infrastructure and a service agreement with a local government lead to new commercial projects on its lands. In 2011, Squiala collected less than \$100,000 in property tax revenues and in 2014; they collected over \$500,000 in property taxes.

For these three First Nations, infrastructure improvements have allowed them to attract considerable private investment, which has greatly increased land values, enhanced their fiscal self-sufficiency and created job and business opportunities for their people. This chapter is about the provision of economic infrastructure (water, sewer, and roads) within First Nations and tribes and how it is planned for and financed. It focusses on the following questions:

1. What is public economic infrastructure? What are some benefits of infrastructure?
2. Why is there not competitive infrastructure on First Nation lands? What is the impact of less First Nation infrastructure on private investment?
3. What is the First Nation infrastructure financing gap? How can it be reduced?
4. Why are credit ratings important? How does government affect credit ratings?
5. What is the First Nation infrastructure planning gap? How can it be reduced?
6. What is an economic strategy? What is a capital plan? What is a financing plan?
7. Why is it important to integrate economic, capital and financial planning?
8. How can service agreements help First Nations close the infrastructure financing and planning gaps?

### **Learning Objectives**

There are seven learning objectives in this chapter.

- Explain how infrastructure supports investment.
- List the main types of economic infrastructure.

- Develop a presentation on the financing and planning problems associated with First Nation or tribal infrastructure.
- Itemize the key elements of a First Nation or tribal credit rating.
- Explain the importance of integrating land use, economic and capital plans.
- Describe how to borrow through the FMA.
- List the steps to complete a service agreement between a local government and a First Nation or tribal government.

### **What is Public Economic Infrastructure?**

Public economic infrastructure is physical infrastructure provided by the public sector and paid for by public revenues that will raise the return to private investment. Research shows that some of the most effective public infrastructure investment includes transportation, water and sewer infrastructure.

In his 2000 paper *Is All Public Capital Created Equal*; Alfredo Pereira examined the affects of public investment in different types of infrastructure on private sector performance. Pereira found that infrastructure investment in energy systems and transit systems have the highest rates of return. He found sewage and water systems to be the second most valuable types of infrastructure investments, as measured by marginal productivity (i.e. the dollar value of the increase in output per dollar invested).

In this chapter, we focus on transportation, water and sewer infrastructure.

- *Transportation* – This includes roads (including signage and traffic lights, curbs and sidewalks, street lighting, and bike paths and pedestrian walkways); highways (including structures like bridges and tunnels); mass transit systems (like commuter rail systems and subways); railways; airports; and ferries.
- *Water* – This includes drinking water infrastructure (including the filtration and treatment facilities, the system of distribution pipes, storage reservoirs, pumps, and valves); and major irrigation systems (like reservoirs and irrigation canals).
- *Sewer* – This includes sewage infrastructure (including the treatment facilities, the system of collection pipes, and the infrastructure for the disposal of wastewater).

### **Why is Infrastructure Important for Private Investment?**

Infrastructure is a precondition to economic development. Initial investments in sewer, water and road systems provide the highest economic return to public investment. There is a positive relationship between the presence of core public infrastructure (roads, streets, bridges, highways, water treatment and distribution systems, sewers, airports and mass transit) and productivity growth. Economic infrastructure improves the health of workers, reduces the costs of transportation and information and raises the value of land by converting it from raw to serviced land.

- *Improved health* – Investments in better water and sewer infrastructure leads to improved health and safety. Investments in better transportation infrastructure can keep people safer.
- *Improved labor markets* – Investments in better transportation infrastructure can reduce traffic congestion and reduce travel costs and time. This enables workers to seek employment opportunities further from home. This can improve the matching of available skills in the labour pool and job requirements.
- *Higher land values* – Investments in water, sewer, roads and other types of infrastructure turn raw land into serviced land. This increases the market value of land.
- *Reduced travel and communication times* – Better transportation systems support better communication systems that reduce travel and communication times and costs.

### **What is the State of First Nation Infrastructure?**

In their 2012 report, “Recommendations on Financing First Nations Infrastructure,” the cabinet appointed National Aboriginal Economic Development Board made the following statement about First Nations infrastructure:

*“Infrastructure in First Nations communities is deteriorating rapidly and the cost of maintaining and upgrading existing infrastructure is increasing. The current identified on-reserve infrastructure gap is estimated to be in the range of \$3 to 5 billion, including projected upgrades of assets and identified infrastructure needs across First Nation*

*communities, but not the operations and maintenance of existing assets. This infrastructure gap continues to have a significant and direct impact on the quality of life on reserve and the ability of First Nations to realize their full potential, both socially and economically.”*

### **Why is Typical First Nation Infrastructure Substandard?**

First Nation infrastructure is substandard because there is a financing gap and a planning gap with other governments.

The financing gap refers to the gap in infrastructure financing options available to First Nations and tribes, relative to those available to local governments in Canada and the US. Typical local governments have a variety of methods of financing infrastructure, whereas First Nations and many tribes do not. The gap in financing options available to First Nations and tribes contributes to the substandard state of infrastructure on reserve and reservations.

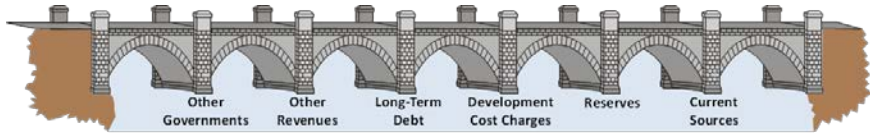
The planning gap refers to the gap in planning practices utilized by typical First Nation governments, relative to those used by most local governments in Canada. Local governments attempt to utilize planning practices that integrate economic planning, with land use planning, capital planning, and capital financing planning, whereas First Nations seldom engage in integrated planning.

### **What is the Infrastructure Financing Gap?**

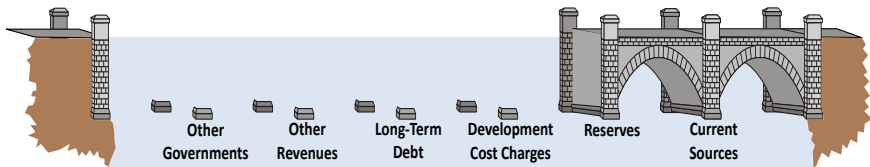
There are six basic vehicles for financing improvements in physical infrastructure for local governments: (1) annual property tax and other local revenues; (2) saved local revenues; (3) long term debentures; (4) development cost charges; (5) public-private partnerships; and, (6) transfers from other governments.

Multiple sources of revenue enable a local government (sometimes in co-operation with other local governments) to build the initial infrastructure system, to extend the system to undeveloped areas, and to maintain the system. The diagram below shows a bridge that represents the provision of infrastructure. Each of the supports of the bridge represents the different methods of financing that infrastructure. In the case of local governments in Canada, there are sufficient supports

(revenue options) to complete the bridge (provide the infrastructure).



First Nation governments on the other hand, have limited financing options to provide basic core infrastructure on their lands. The diagram below represents the ability of First Nation government to provide core public infrastructure that is necessary to facilitate investment and to generate economic activity and output. First Nations do not have the supports (revenue sources) needed to complete the construction of the bridge (provide infrastructure). Simply put, First Nations lack the revenue options needed to provide infrastructure comparable to other jurisdictions (where local governments enjoy access to greater revenue options).



In summary, local governments in Canada make use of several different financing options for infrastructure. First Nations do not.

### What is the Impact of the First Nation Financing Gap?

Economic development involves both the public and private sectors. The public sector’s role begins with the provision of infrastructure.

Governments use their revenues to pay for local services and infrastructure such as roads, water and sewage systems. A typical Canadian community can finance \$6 million in new infrastructure from \$1 million in annual revenues.<sup>172</sup> This ratio is based on typical terms for local governments in Canada. This is illustrated above.<sup>173</sup>

Typical Canadian Community	\$1 Million Annual Revenues = \$6 Million Infrastructure
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Local governments use their infrastructure and services to entice investors to build residential, commercial, and industrial developments on their land. A typical Canadian community will entice \$5 million in private investment for every \$1 million it invests in infrastructure improvements. Private investment is about 5 times larger than public investment in Canada.<sup>174</sup>

Typical Canadian Community	\$1 Million New Infrastructure = \$5 Million New Investment
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This private investment generates public revenues, employment, improved services and the ability to finance more public infrastructure.

<sup>172</sup> This ratio was determined, in part, by examining debt limit regulations under the Alberta Municipal Government Act. Under these regulations, a municipality's total debt is limited to 1.5 times the revenue of the municipality, and debt service is limited to 0.25 times the revenue of the municipality. Therefore, \$1 of annual property tax revenue can build \$6 in infrastructure. A survey of BC local governments also contributed to the determination of this ratio. The survey found that for every dollar devoted to infrastructure had the potential of increasing infrastructure 7.5 times through borrowing. To be conservative, \$6 was used.

<sup>173</sup> Ten Times Harder – Helping First Nations Get Into the Game, First Nations Tax Commission, [http://fntc.ca/index.php?option=com\\_docman&task=doc\\_details&gid=10&Itemid=36](http://fntc.ca/index.php?option=com_docman&task=doc_details&gid=10&Itemid=36).

<sup>174</sup> This ratio was based on StatsCan data on capital and repair expenditures (representing investment) for 1994 to 2001. Over the period, the ratio of private investment to public investment was 5 to 1. Therefore, a ratio of \$1 in public investment to \$5 in new private investment was used.



This virtuous circle is how most local economies grow.

However, a typical First Nation community with \$1 million in annual revenues may finance only about \$2 million of infrastructure because of concerns about collateral and risk.<sup>175</sup> In other words, typical First Nation governments are required to commit three times as much revenue as a non-First Nation community, to finance the same amount of infrastructure.

Typical First Nation Community	\$1 Million Annual Tax Revenue = \$2 Million Infrastructure
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A typical First Nation community will entice only about \$1.5 million in business investment from that same investment in public infrastructure.<sup>176</sup> This lower number is a result of the costs of investment facilitation on First Nation lands being 4 to 6 times higher on average than on non-First Nation lands.

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<sup>175</sup> This ratio was based on a 1998 report completed for the First Nations Finance Authority. In the case reviewed, Westbank had to finance a \$3.1 million project. Terms for financing were from one year to four years with various financial institutions. Westbank used several revenue sources and collateral to secure the required loans. Based on the complicated financial arrangement it is estimated that property tax revenues secured very little of this infrastructure requirement. It is probable that \$1 of property tax revenue secured less \$2 of infrastructure associated with this project. Of course, Westbank is a bit of an anomaly since it actually had valuable land to use as collateral in the first place. Most First Nations that collect property taxes do not have this advantage. As a result, most of these First Nations finance infrastructure with a large down payment, and/or with a significant private sector contribution and smaller short-term loans. It is possible that for these First Nations that few if any property tax dollars are used to secure infrastructure financing. As a result, we are confident that our estimate is if anything generous for most property tax collecting First Nations.

<sup>176</sup> Due to a lack of statistics, this ratio was based number of anecdotal statistics. For example, selected research suggests that over 80% of all on-reserve household expenditures are made off reserve indicating a lack of on-reserve business presence. Other research suggests that the costs of doing business on the best located First Nation lands is four to six times higher than it is off reserve (see Fiscal Realities Economists research from 1999). This would lead one to assume that the level of private sector development would be 4 to 6 times less on reserve than off reserve. Based on these anecdotes we thought a generous approach would be to suggest that the private sector investment on First Nation land is 30% what it is off First Nation land. We strongly believe that this is a generous estimate based on the readily observable minimal presence of a private sector on most First Nation land.

Typical First Nation Community	\$1 Million New Infrastructure = \$1.5 Million New Investment
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First Nations pay “triple” the going price for infrastructure and receives only one quarter the economic payoff from infrastructure investment.

A typical Canadian local government with \$1 million in annual tax revenue can finance \$6 million in infrastructure, which can attract \$30 million in new investment. However, the typical First Nation government with \$1 million in annual tax revenue can finance \$2 million in infrastructure, which can attract \$3 million in new investment – only one-tenth the new investment attracted by the typical local government in Canada.

The bottom line is wealth is roughly ten times harder to create on First Nation lands than elsewhere in Canada.

Typical Canadian Community	\$1M Annual Tax Revenue = \$6M Infrastructure = \$30M New Investment
Typical First Nation Community	\$1M Annual Tax Revenue = \$2M Infrastructure =\$3M New Investment

For First Nation governments, the solution must include improved access to capital and improved planning.

**How to Close the Financing Gap with the First Nations Fiscal Management Act (FMA)**

In Canada, the FMA was designed specifically to close the First Nation infrastructure financing gap. It provides First Nations with the revenue options of other local governments and a few additional infrastructure financing methods to potentially close their infrastructure gap. Local revenues defined by the FMA include:

- *Taxation for the Provision of Services* – These types of taxes are often used to pay for water and sewer system infrastructure and

operation costs. Many local water and sewer systems are completely self-financing because they generate sufficient revenues from these charges on users to pay for the operation, maintenance and replacement costs of their infrastructure.

- *Development Cost Charges* – These charges are levied on developers for the off-site costs of hooking them up to existing infrastructure. DCCs can be charged for water, sewer, roads and parks. The revenues are usually saved in an account to pay for future infrastructure system extensions. The costs are usually passed onto commercial and residential investors.
- *Property Taxes* – Property taxes are another important source of revenues to pay for infrastructure. These taxes support infrastructure costs either from revenues in the current year to pay for immediate capital and infrastructure projects, or revenues in past years saved in reserve funds for infrastructure replacement.
- *Other Revenues* – The FMA also provides First Nations with access to other revenues such as business activity taxes and more recently property transfer taxes. These revenues can be used for infrastructure or saved into reserve funds.

First Nations also have two options to lever revenues into long term infrastructure financing through the First Nations Finance Authority (FNFA) They can finance debentures using local revenues or they can finance debentures using other revenues.

*Local Revenue Financing* – First Nation governments that have implemented property taxation and local revenue systems under the FMA use these revenues to secure loans through the FNFA. The First Nations Tax Commission (FNTC), First Nations Financial Management Board (FMB) and FNFA all work together with borrowing First Nations to provide a regulatory framework that improves their credit rating and provides assurances of good fiscal and capital planning to taxpayers.

*Other Revenues* – As a result of a recent FMA regulation, First Nations can pledge tax revenues and fees (other than local revenues), certain types of royalty income, revenues from leases or permits, revenues derived from contracts, business income or dividends and certain transfers from other governments to support an other revenues infrastructure debenture. As a result, virtually any First Nation income

may be used to secure FNFA debentures. The regulatory framework for other revenues is provided for by the FNFA and the FMB.

### **How to Improve First Nation Credit Ratings**

Credit ratings for bonds are an assessment by an independent agency of the likelihood that people who buy bonds from specific entity will receive their payments according to schedule. When a First Nation or tribe chooses to borrow money on the bond market the terms they receive or whether they are able to borrow at all will depend on their credit rating, although there are rare exceptions where bonds are issued without a credit rating.

Credit ratings are used to support entry into the bond market. However, they have a greater utility. A good credit rating can also improve access to bank finance. It can be used as evidence that the bond issuer also provides a good place to invest. A good credit rating gives assurance to an electorate about the performance of their government. Moreover, the actions undertaken by an entity in order to improve its credit rating have been found to strengthen the accountability and governance regimes of public entities.

### **Methodologies of Credit Ratings**

The methodologies used in determining credit ratings are quite comprehensive and detailed. The precise methodologies will vary from rating agency to agency. However, the fundamentals are always the same. A typical framework usually reviews budget performance; debts liabilities and liquidities, fiscal relationships with other governments, institutional and regulatory arrangements and economic and demographics. The example of Southern Ute tribe below shows how good planning and sound financial management results in a good credit rating.

### **Sound Financial Planning Improved the Southern Ute Indian Tribe's Credit Rating**

The Southern Ute Indian Tribe in Colorado is the only tribal government in the US to receive a AAA rating. This government has resource revenues and a strong balance sheet with business holdings throughout

the US and even Canada. However, this success has come because of sound planning in the first place. The credit rating reflects the strength of their planning function and the demonstrated commitment of the tribal government to the plan.

When profits increased dramatically in the 1990s, instead of dividing the cash among their members, tribal leaders sought to improve services and create a financial plan. The plan was approved by Council in 1999 despite displeasure among members. Nearly five years later, profits continued to soar and the Southern Utes earned the highest credit rating possible from two national credit rating agencies: AAA from Fitch Ratings and AAA from Standard & Poors. They are the first and only American Indian tribe to do this.

Fitch Ratings was the first to assign the AAA rating. The Southern Ute Indian Tribe earned the rating, in part, by having, “strong financial management.”<sup>177</sup>

Standard & Poor’s assigned a AAA rating in June 2001. The rating is based, in part, on “well thought out financial and capital plans.”<sup>178</sup>

The keys to the Financial Plan are as follows: (a) revenue streams are set aside for the provision of services into the future; (b) business enterprises are separated from these core revenues. The plan also provides a guaranteed liquidity function for the bonds and debt servicing limits.

This example illustrates how sound financial planning and stable revenue sources can lead to improved credit ratings. This enables infrastructure financing at lower costs.

The Southern Ute example, however, may not be the best example for smaller First Nations and tribes. A better example for them is the cooperative model of the First Nations Finance Authority. As was previously discussed, the FNFA is based on a successful municipal cooperative financing model in BC. In both cases, smaller governments

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<sup>177</sup> [http://www.sugf.com/Docs/TheBondBuyer\\_ColoradosUteIndianTribeFirstToReceiveTripleARating.pdf](http://www.sugf.com/Docs/TheBondBuyer_ColoradosUteIndianTribeFirstToReceiveTripleARating.pdf)

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[http://www.sugf.com/Docs/StandardAndPoorsCreditWire\\_SouthernUteIndianTribeColoAssignedAAAIssuerCreditRating.pdf](http://www.sugf.com/Docs/StandardAndPoorsCreditWire_SouthernUteIndianTribeColoAssignedAAAIssuerCreditRating.pdf)

pool their debt requirements to provide access to capital at lower rates and longer terms. The credit rating of the FNFA is based on the collective diversity of their members, the strength of the regulatory framework and the methods to protect creditors in the event of a default. As recently as 2014, the FNFA received an investment grade credit rating (A) from Moody's and Dominion Bond Rating Services for its debenture issue.

### **What is the First Nation Planning Gap?**

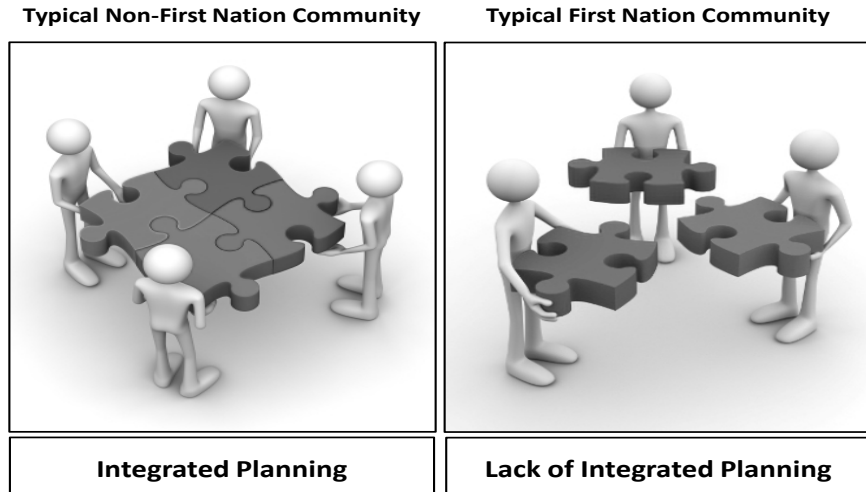
In non-First Nation communities, an Official Community Plan (OCP) usually guides infrastructure planning. Usually, the OCP is based on the economic strategy of the community. The OCP creates a land use plan designed to implement the economic strategy. A capital plan is then developed to implement the OCP, the land use plan and the economic strategy. A capital-financing plan is formed that includes the establishment of savings or reserve funds so that the necessary infrastructure can be built in a fashion that supports the economic growth of the community. In other words, non-First Nation communities integrate a number of plans to support infrastructure planning.

This is not the case in typical First Nation communities. There is a planning gap in most First Nation communities. That is, infrastructure planning in most First Nation communities does not include a process that integrates the economic strategy, land use plan, capital plan, and financing plan.

### **An Analogy: Integrated Planning**

Planning can be thought of like doing a puzzle. The puzzle pieces are the individual capital projects. One piece might be a road-resurfacing project. Another piece might represent an upgrade to a particular portion of the wastewater collection system. The community's economic development strategy is like the picture on the box. It guides the manner in which the pieces come together. The economic development strategy is there to guide the manner in which the government executes the various capital projects. Without the picture on the box, it is difficult to assemble the pieces. The only approach is to blindly try putting random pieces together to see if they fit. Some may fit together, but without the picture, it is impossible to execute an efficient strategy.

Capital planning without an economic development strategy is similar. A government’s capital program will include a number of projects, but will lack the management and direction required to guide their efficient execution. Without the economic development strategy, bringing those projects together in the most efficient manner will be impossible.



There are three consequences of these deficiencies or gaps faced by First Nations.

1. Infrastructure development is often done in a piece meal uncoordinated fashion. First Nations are often unable to work with partners to develop projects of the proper scale. They are often forced to use inappropriate financing tools that result in inefficiencies.
2. First Nations often face large start up hurdles that prevent them from building competitive infrastructure or any infrastructure at all despite having significant economic development potential.
3. First Nation property values and rates of investment are much lower owing to substandard infrastructure and local services.

### **The Potential Costs of the Planning Gap**

A First Nation in western Canada contracted an engineering firm to design a wastewater collection system and treatment plant on its largest

reserve. As planning was completed, the First Nation began working with a consultant to identify possible revenue streams to pay for the capital project. Based on the initial number of users, the consultant determined the capital project, as designed, was not feasible. The consultant was unable to obtain the First Nation's economic development strategy, and ultimately found that one did not exist. Without an economic development strategy, the consultant could not determine how the treatment plant would lead to the achievement of the community's economic development objectives. Fortunately, the First Nation had an existing wastewater treatment agreement with the adjacent municipality, which included provisions for additional future capacity. The consultant recommended the First Nation install the collection system and assisted in setting appropriate tax rates and local improvement fees. However, the consultant recommended against the construction of the treatment plant. In the consultant's estimation, the treatment agreement with the adjacent municipality satisfied the community's economic development objectives. The First Nation accepted this recommendation.

In this case, isolated capital planning almost cost the First Nation tens of millions of dollars by undertaking a non-essential 'wish list' capital project that would not have appreciably contributed to the community's economic development objectives. This savings means other higher-benefit capital projects can be undertaken.

### **How to Close the First Nation Planning Gap**

To close the planning gap, First Nations should develop economic strategies and ensure the strategy is developed in coordination with and informs other plans, including the land use plan, the capital plan and the capital-financing plan.

There are several dimensions to planning. Its quality depends upon an economic plan that is consistent with capital development, a thorough capital plan that identifies future infrastructure requirements and their associated costs and a capital-financing plan that identifies how infrastructure will be paid for. If these are in place, they will ultimately support a fiscal plan that identifies future costs and projected revenues. A quality fiscal plan will also identify risks to the plan and contingencies for dealing with such risks.



### **What are the Elements of an Economic Plan?**

Economic strategies present an economic vision for a community, estimate the potential benefits of realizing the vision, identify any potential barriers to achieving the vision, and a strategy to overcome the barriers identified. First Nation economic development strategies generally contain a regional market assessment, an estimate of the investment potential of the First Nation, the fiscal and economic benefits of realizing that potential, a First Nation investment climate assessment, a strategy for improving the investment climate, an estimate of the costs of implementing the described strategy and a work plan with performance measures. Each of these elements is described below:

- *Leadership and Vision* – All successful tribal and First Nation economic strategies begin with a vision and are led locally. Administrations and outside experts can provide good advice but the economic strategy must originate from the community. The principle advocate for the strategy must be a community leader. Without community consent and leadership, the strategy will usually fail. The implementation of an economic strategy will take several years or longer and during that, time members of council will change. Only if there is widespread agreement will investors expect future councils to continue to work within the strategy. (The next chapter discusses how to support tribal and First Nation leadership and generate informed community consent in more detail.)
- *Regional Market Assessment* – The strategy should include an assessment of existing market conditions facing the First Nation's land (reserve lands as well as any off reserve parcels). The potential for sustainable economic development in a First Nation community is usually tied to the regional economy. The assessment should focus on dominant industries within the region.
- *Estimate of the Investment Potential of the First Nation* – Private investment is the driving force of economic development. The strategy should identify the potential of the First Nation's lands to take advantage of investment opportunities in the region.
- *The Fiscal and Economic Benefits from Realizing that Potential* – The strategy should estimate the fiscal and economic benefits associated with realizing the private investment potential identified.

The strategy should also begin to identify any possible barriers to realizing this potential.

- *A First Nation Investment Climate Assessment* – The strategy should assess the First Nation’s investment climate. This assessment will indicate how well positioned the First Nation is to take advantage of the identified investment opportunities. Where appropriate, this assessment could consider public services (including infrastructure, local service provision, and service agreements), the legal framework (including property tax and other taxes, land management, the development approval process, financial management, land tenure rules, investor codes, and governance procedures), and the administrative framework (including available investor information, planning practices, and investment facilitation support). The assessment should identify any gaps or weaknesses in the legal framework, the administrative framework, missing property rights, and inadequate infrastructure, services or revenues.
- *A Strategy for Improving the Investment Climate* – The economic development strategy should be designed around capitalizing on those opportunities with the greatest potential benefits and the lowest potential barriers. The strategy should be based on filling the gaps identified in the investment climate assessment required to realize these opportunities. It should identify strategic investments and infrastructure requirements that might be needed to overcome the potential barriers. It should also explore how partnerships with the private sector or government can be used to reduce the cost of investments and reduce other barriers present in either the First Nation or the region as a whole.
- *An Estimate of the Costs of Implementing that Strategy* – The strategy should include estimates of the costs of strategic investments and infrastructure requirements outlined.
- *A Work plan with Performance Measures* – As part of the strategy, a work plan should be prepared. The work plan should include milestones and completion dates to implement the economic development strategy.

### **Key Skill – Writing an RFP**

The Request for Proposals (RFP) is a tool to communicate to a consultant what is required and how quickly it is to be completed. A well-prepared RFP should clearly layout the specifics of the project, timelines and responsibilities. If the RFP is clear, the proposals will include all the information required to decide if the consultant can meet your needs at a cost you can afford.

An RFP should include the following information:

- **Background Information:** Community description, existing planning tools (i.e. Official Community Plan), mission, vision, goals and other relevant growth plans.
- **Scope:** Why proposals are sought, goal of project, issues to resolve, barriers to the project, applicable history, other related projects and interim/final products required.
- **Timelines:** Overall timeline for project, milestones/deadlines and project schedule or work plan (if time is vital).
- **Responsibilities:** Expectations for administering and managing project, coordination of public consultations, preparing/printing materials, presentations and final reports.
- **Budget:** Outline the budget. Request detailed estimates for each product/phase and contingency factor from consultants.
- **Information about the Consultant:** Request information on expertise and experience, resumes, summaries or examples of similar work performed, references from similar clients and identification of any subcontractors (as well as their expertise/experience).
- **Submission Requirements:** RFP must provide contact information, closing date/time, copies required, any templates or forms developed, acceptable formats, interviews required, reference checks to be completed and review/decision dates.
- **Criteria for Proposal Evaluation:** Outline the criteria that may include factors such as related experience, proposed approach, submitted work plan and costs/outputs.
- **Terms and Conditions:** Outline terms and conditions applying to the proposal or product/project such as: Not pay for bids, retain right not

to select any consultants and require a contract before a certain date. Also, include terms and definitions as necessary.

A good source for guidance on developing an RFP is located on the Saskatchewan Ministry of Municipal Affairs site at <http://www.municipal.gov.sk.ca/RFP-Guide-PDF>.

In addition, an example of an RFP completed by the Snuneymuxw First Nation in British Columbia for a Forestry Economic Strategy, Business Plan and Harvesting Plan is located at [http://www.canadian-forests.com/Forestry%20Jobs%20SFN%20Forestry%20may17\\_13.pdf](http://www.canadian-forests.com/Forestry%20Jobs%20SFN%20Forestry%20may17_13.pdf)

### **What type of land use planning supports economic development?**

Tribes and First Nations face different conditions for potential economic development depending on their location, the regional economic advantages, amount of current development and community support. These differences impact investment decisions and land use decisions that do not consider these differences can and in some cases have prevented investment.

*Location* – Some tribes and First Nations may be well situated for residential development, others for commercial, some for a destination resort and still others may be situated as an appropriate site for industry. In some cases, the potential uses will be obvious and supported by the community. In other cases, community objectives may not fit with an analysis of potential. In addition, in other cases, the First Nation or tribe may have undeveloped lands where multiple development options are possible.

*Regional Economic Advantages* – First Nations and tribes are part of their regional economies. Regional economies can have competitive advantages related to location, resources, technology or labour or a combination of some or all these advantages. Potential investors will be aware of these advantages and will locate accordingly. Land use decisions intended to facilitate investment should reflect investor interests and economic realities.

*Amount of development* – Some tribes and First Nations have considerable development and others have none. Existing development influences future development. In these situations, zoning may be more predictable. The absence of development means zoning could prevent possible investment because the tribe or First Nation is guessing about possible investors.

*Community support and vision* – Some tribes and First Nations support most types of investment and others support fewer types of investment. Some support restrictions on land use for specific types of development and others support fewer restrictions. The nature of the community vision and support for that vision affects different land use approaches.

As a result of these differences, tribes and First Nations must be careful about the use of traditional planning and zoning approaches. In many cases, it is common to hire a consultant that does a preliminary analysis and presents detailed maps. These maps are supposed to guide zoning and infrastructure decisions, but too often, the maps reflect either a community dream or economic development that does not attract actual investors willing to undertake development projects. It is very difficult for planners to substitute for what really happens in the market place by those who have the resources to make the real decisions. Depending on the circumstances, two approaches to land use planning and zoning should be considered:

*Broad Land Use Zones* – In this approach a tribe or First Nation would establish broad categories of possible land uses. It is best applied when there is considerable development already in place or the tribe or First Nation is near an urban location where the corresponding land zones are obvious or it is a requirement of a First Nation service agreement with a local government. Broad zoning is recommended because specific zoning often leads to high switching costs. These costs occur because, whenever there is a small variation in a proposed use within a zone, rezoning is required. For example, some local governments have created unnecessary amounts of different zones have been created to address all possible circumstances. This is something tribes and First Nations wishing to facilitate investment should avoid.

*Subdivision and Development Regulations* – These regulations inform developers as to what is expected for different types of development. Those regulations can require access to different capacities of infrastructure and thus infrastructure plans can guide development without the detail of zoning. With a development, regulations approach each major type of land use has a list of criteria that must be met before a development is approved. Most of the requirements are related to availability of the appropriate infrastructure. This does not mean that the

entire infrastructure has been built, but it does mean that the government must have created a preliminary infrastructure plan that has a combination of certainty and flexibility. These regulations are relevant when there is a large amount of developable land that is common for many tribes and First Nations.

First Nation and tribal governments must ensure the land use planning process is connected with the community vision, upon which the economic development strategy is based. Leadership should also communicate how land use planning decision will lead to the achievement of economic development objectives.

The infrastructure plan and the land use regulations should be developed to support the economic plan. The plan should contain a statement that identifies the relationship between land use and the economic development strategy. In addition, the plan should describe how it connects with the regional plan.

The land use plan should include a growth management strategy. This should be based on making the most efficient use of existing infrastructure. This could include growth strategies to accommodate different projected population horizons and different population growth rates. This may also include implications on infrastructure costs associated with these levels and rates of growth.

### **What are the Elements of a Capital Plan?**

The capital plan should be developed to support the economic development strategy. The degree to which it should contain the following elements will depend on the situation within the First Nation and how specific it can be about future development opportunities on its lands

- *General servicing strategy* – This strategy should address how services can be provided in a cost-effective and efficient manner, and how to balance service demands with affordability. The strategy might address infill vs peripheral development and methods to maximize existing service systems.
- *Transportation strategy* – This strategy should address methods to maintain or improve mobility levels while remaining affordable. This strategy may also include measures to pattern development to

minimize travel demand and promote alternatives like public transit, cycling and walking.

- *Water system plan* – This might include distribution as well as treatment. Other components might include any conservation measures planned or emergency water supply plans.
- *Sanitary sewer system plan* – This might include collection as well as treatment and disposal. Other components might include septic fields and septic tanks. The plan might address any other methods of treating and disposing of effluent under consideration.
- *Storm water drainage plan* – This might include planning to ensure development does not interfere with natural watercourses to maximize natural drainage patterns. This might also include other drainage infrastructure like detention ponds.
- *Waste management strategy* – This might include landfill sites, compost facilities, education initiatives, and recycling operations.
- *Environmental management strategy* – This may address environmental issues related to climate, energy, air quality, pollution, watershed, liquid waste, drinking water, etc.

### **What are the Elements of a Capital Financing Plan?**

The capital-financing plan should be developed to support the capital plan, land use plan, and economic plan. The introduction to the capital-financing plan should include the following:

The identification of a funding source (revenue stream) is the first step in paying for capital projects (infrastructure). Some types of infrastructure directly generate revenue through user fees. Toll roads, parkades and water and sewer systems are good examples. Other types of infrastructure do not directly generate revenue. For example, local roads and sidewalks do not directly generate revenue. To pay for this type of non-revenue-generating infrastructure, governments typically rely on taxes, fees, and other sources.

Once a funding source is identified, governments can pay for infrastructure on a “pay-as-you-go basis” or by financing.

- In a *pay-as-you-go approach*, a capital project is undertaken only once enough revenue has been collected to cover its cost. Sources include current taxes and revenue, funds from capital reserves, special assessments or impact fees, or grants from other

governments. There are no interest charges related to this approach, but projects must be delayed until sufficient funds are accumulated.

- In a *financing approach*, a capital project is paid for before enough revenue to meet to its full cost has been collected. Typically, this is done by borrowing against the future revenue source identified. This usually means issuing bonds that are paid back over time with taxes, user fee payments, or other revenue sources.

For most capital projects, it is a mix of current sources and financing that is used. The government needs to determine the best mix of resources to finance both its operations and its capital program. The cash and debt financing profile identifies the annual use of current cash, existing reserve funds (savings) and debt to fund capital expenditures. The cash and debt financing profile seeks to maintain a level of cash investment into new capital and the renewal and replacement of existing capital that maintains equity among taxpayers. The inclusion of cash funding ensures that current users are contributing funds toward the capital investments they are benefiting from, and not just deferring these costs entirely onto future generations.

With respect to debt, financing governments have to make some choices. First, they must consider the risks and benefits of fixed-rate and variable-rate debt within the context of prevailing interest rates. Fixed-rate debt offers the advantage of a set debt service payment schedule upon which budgets and projections can be based, but typically requires higher interest rates. Variable-rate debt typically offers lower interest rates because interest rate risk is borne by the issuer not the investor. Often, variable-rate debt represents the longest term bonds in a debt portfolio, as the interest rate savings are greatest when compared to the fixed-rates of a comparable long-term bond. Second, the government has to determine the timing of debt. Generally, governments structure each bond issue to provide a smooth and level total debt service payment schedule over the period. This enables greater stability in rates and charges and a more equitable division of repayment responsibility between current and future ratepayers.



The capital-financing plan should include the following elements and forecasts:

- *Local Revenue Streams and Forecast* – It should identify all local revenues available for financing capital and provide a forecast of these future revenues based on expected economic development and population growth. It should also include future rates and charges for use of the capital project should be forecasted over the planning period.
- *Growth Assumptions* – It should state the assumptions to support revenue growth forecast and the rationale to support those assumptions.
- *Local Service operating expenditure forecast* – The capital-financing plan should contain a forecast of local operating service costs that would require local revenues. These costs include the operation of government, policy and fire protection, parks, recreation and culture costs and operation of environmental health facilities related to water, sewer and solid waste. The assumptions related to inflation and growth should be stated.
- *Projected Use of Funds* – The uses for all funds in the capital-financing plan should be projected over the planning period.
- *Funds and Reserves* – The capital-financing plan should include descriptions of the various capital funds related to the capital projects in the capital plan. This might include:
  - A PAYGO fund – which would be established to collect specific charges related to specific capital projects and used to fund specific capital expenditures (including debt service).
  - A Construction Fund – that would be funded with proceeds from the sale of debt and expended over the following year (or several years) on specific capital projects.
  - A Debt Service Reserve Fund – that would be held for making an annual debt service payment, in the event the government became unable to do so out of other funds.
  - The capital-financing plan should also include a table of the projected balance for each fund over the planning period.

### **How can Service Agreements Help First Nation Governments Close the Financing and Planning Gaps?**

The infrastructure planning and financing gap is not as prevalent for local governments. First Nations and tribes can often quickly close this gap through service agreements with nearby local governments that contain infrastructure-sharing arrangements.

A service agreement is a contractual relationship between two governments for the provision of services and sharing of infrastructure. It is often efficient for First Nations or tribes to purchase services from nearby larger governments. Service agreements can result in reduced duplication of service, reduced costs, reduced capital requirements and improved relationships. Some of the most common services purchased are water, sewer, and fire protection. Each government decides what local services and infrastructure to provide for the community, how those services and infrastructure will be provided and how they will be paid for. Potential investors, including commercial and residential developers, homebuyers, and lenders also have questions about services and infrastructure:

1. How will water, sewer treatment, roads and road maintenance, parks, garbage collection and snow removal be provided?
2. What tax rates will I have to pay now, and in the future to ensure the provision of services and infrastructure?
3. How certain is the continued delivery of these local services and infrastructure?

A lack of confidence in the answers can deter potential investors. Service agreements can provide answers to these questions and give confidence to investors regarding the quality, continuity, and pricing of local services within a region. It also serves as the platform for developing broader agreements regarding region-wide capital planning, land use planning, economic development planning, protocols, and regulatory standards.

Service agreements and infrastructure sharing arrangements provide at least the following benefits:

- *Lower Costs* – The combined service populations of the First Nation and local government together will be larger than the First Nation or local government alone. Cost savings occur when the cost of

servicing an additional taxpayer decreases as the number of taxpayers increases. This is usually true for any service with large fixed costs or initial costs such as sewer or water services. This benefits both parties as the service provider gains revenues and the service purchaser saves large initial costs.

- *Access to Capital Infrastructure* – The local government will likely already have significant capital infrastructure in place and have acquired the necessary skills, people, and equipment to maintain that infrastructure. Traditionally, local governments have also had greater access to local infrastructure financing than First Nations or tribes. In some cases, the costs per taxpayer would be so high that the project would not be feasible. For example, since signing the Squiala-Tzeachten-Chilliwack service agreement, Squiala First Nation has seen considerable land development. Squiala First Nation was able to build the necessary transportation infrastructure and provide the local services to support the new Eagle Landing Shopping Centre because of the coordination of services with the City of Chilliwack.
- *Less Duplication* – Service agreements allow governments to make more efficient use of existing services with less impact on the environment, rather than having duplicate services in the same local area. A good example of this is a recent decision by the Tk'emlúps te Secwepemc regarding their sanitary sewer system. They chose to build and operate a wastewater collection system that sends wastewater to the City of Kamloops treatment facility as opposed to developing their own complete wastewater treatment system, as the City of Kamloops already had the treatment infrastructure in place.
- *Utilization of Excess Capacity* – When a local government builds capital infrastructure or acquires the capacity to provide a service, it usually ends up with excess capacity, partly to accommodate future growth, and partly due to the indivisibility of some components. For example, a town with a population of 25,000 may build a water supply large enough to meet the needs of a population of 50,000. Another example is that a town may hire a full time animal control officer and build one-pound facility when really it only needs animal control services 3 days a week, but the impounded animals still have to be cared for each day. Selling these services to the First Nation or tribe would mean that the local government could make use of some

of that excess capacity and receive some additional revenues in return.

- *Positive Relationships* – A service agreement is a major building block in developing and strengthening a positive relationship between a local government and a First Nation or tribe. A service agreement addresses many areas of common concern and future opportunity. With an agreement, the parties form a larger community signaling that they want to work together well into the future in a spirit of cooperation.
- *Additions to Reserves* – A service agreement may be a prerequisite for the addition to reserve (or reservation) process. This is true for Treaty Land Entitlement First Nations in Saskatchewan and Manitoba.
- *Regional Cooperation to Support Economic Development* – Service agreements between First Nations or tribes and local governments can expand infrastructure and make more land available for investment. Service agreements can create a standard of regional service quality and indicate regional economic cooperation between First Nations or tribes and local governments.

### **Negotiating a Local Government Service Agreement**

The First Nations Tax Commission has facilitated over 30 service and infrastructure agreements between First Nations and local governments. They recommend these steps for negotiating an effective and fair service agreement.

- *Facilitation* – In many cases, it is useful to have a neutral third party assist in the negotiation of a service agreement. A facilitator is trained to help parties negotiate productively. A facilitator uses a professional approach to help groups hold constructive meetings that can be especially useful with large groups, complex issues, or emotional conflicts.
- *Principles Statements* – First Nation or tribal and local government negotiating teams should consider basing negotiations on principles that support a positive long-term business relationship. The initial approach to a service agreement negotiation should include the development of a principles statement that would be ratified by the respective parties or agreed to by the negotiating teams.

- *Ground Rules* – These rules are helpful for guiding the negotiation process, providing a framework for order, and ensuring there is a mechanism to deal with disputes. By establishing ground rules at the outset of negotiations, participants also provide rules of procedure and conduct for new members and advisors who may join the process.

The FNTEC has developed ground rules that address the following elements:

- *Identifying Objectives* – There are many types of service agreements including comprehensive service agreements and agreements regarding specific services. It is important to understand the objectives of each party at the outset and to discuss opportunities for mutual gains. The facilitator may want to meet separately with the parties during this part of the discussion.
- *Work Plans and Agenda* – The facilitator should develop a work plan, timeline, and agenda for the parties that establish project milestones and achieve as many objectives as possible. The work plan should include topics or tasks, start dates and due dates, and identify the leader of each task. The parties and facilitator should agree to the work plan, meeting schedule and timelines.
- *Technical Working Groups* – These working groups can be used to delegate certain tasks and make good use of expertise that can develop options and provide reports to the negotiation process. The role and objectives of a technical working group should be clearly articulated. If parties agree to a working group’s goals, they are more likely to accept the results. Both parties should participate, or have at least one representative participate in any established working group on their behalf. Possible examples of working groups for a service agreement negotiation might include service selection, feasibility formula selection (finance), or contract development (legal).
- *Identifying Services* – Local government services are generally divided into general government, protection services, transportation, recreational and cultural, community development, environmental health services and fiscal and other services. There are some service categories that the local government cannot provide for the First Nation government such as general government administration or

law enforcement. These types of services would therefore not be included in a service agreement.

- *Service Costs* – A number of service costing methods have been developed in First Nation–local government agreements. The most common method depends on which services are being purchased and what portion of the seller's budget those services comprise. A simple costing method applies the proportion from the second answer to the buyer's local government property tax revenues to determine the service price. For example, a First Nation or tribe purchases fire protection, transportation service and water services from a local government. These services represent 35% of the local government's budget. The First Nation or tribe would then apply the same local service tax rate as the local government to its tax base and pay 35% of its resultant revenues to the local government.

### **Conclusion**

Public economic infrastructure is physical infrastructure provided by the public sector and paid for by public revenues. It is called economic infrastructure because it helps to attract investment. Poor First Nation infrastructure contributes to low rates of private investment and under development of First Nation lands. First Nation infrastructure is substandard because there is a financing gap and a planning gap with other governments.

- *Financing Gap* – Local governments in Canada make use of several different financing options for infrastructure. First Nations do not.
- *Planning Gap* – Local governments in Canada integrate planning processes. Most First Nations do not.

This chapter has described how to close these gaps while recognizing the need to create some certainty while remaining flexible because it is investors who will make the final land use decisions with their proposals.

- *Closing the Financing Gap* – The FMA completely closes the First Nation infrastructure-financing gap. It provides First Nations with the revenue options of other local governments and a few additional infrastructure-financing methods to potentially close their infrastructure gap.

- *Closing the Planning Gap* – To close the planning gap, First Nations and tribes should develop planning processes that integrate economic plans with land use alternatives, capital plans and capital financing plans.
- *Closing Both Gaps* – Another method to close both the planning and financing gaps are service agreements between First Nations or tribes and nearby local governments. These agreements can facilitate cost effective and efficient infrastructure, promote integrated regional capital planning and generate economic growth for the whole region.

The following chapter discusses the administrative requirements to accomplish this.



CHAPTER 7

# ELEMENTS OF A COMPETITIVE FIRST NATION INVESTMENT CLIMATE: ADMINISTRATION FRAMEWORK

**C**hange is hard. John Stuart Mill, a prominent 19<sup>th</sup> century philosopher, economist and political scientist, once considered the question, “Why are some nations rich and others poor?” Now remembered as one of history’s great thinkers in social and political theory, he argued that people are essentially equal and entitled to liberty no matter their ethnic background. Unfortunately, he was criticized at the time for being seen as supporting the emancipation of slaves and, subsequently, this criticism led to the discipline of economics being labelled the “dismal science”.<sup>179</sup> Despite this, he commendably arrived at the conclusion that it was institutions, and not

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<sup>179</sup> Levy, D.M. & Peart, S.J. (2001). *The Secret History of the Dismal Science. Part I. Economics, Religion and Race in the 19th Century*. Library of Economics and Liberty. Available at <http://www.econlib.org/library/Columns/LevyPeartdismal.html>.



race, that explained why specific groups were prosperous and others were poor.<sup>180</sup>

*"Let me be a free man, free to travel, free to stop, free to work, free to trade where I choose, ... free to talk, think and act for myself." 181*

In the present time, this is still a difficult question to answer but the material in this book so far is based on the following points where there is wide-scale agreement among economists.

1. Groups that have less access to capital and markets are poorer than others are. Chapter 1 suggests that tribes and First Nations have traditionally had the institutions to support markets but these institutions were destroyed or not able to evolve because of federal legislation and policies in the United States and Canada.
2. Groups where property rights are not fair, secure, protected and tradable are poorer. This was discussed in Chapter 3.
3. Groups that do not have a legal framework to support commercial and property transactions and access to markets and capital or where the rule of law is not respected or enforced are poorer than others are. This was discussed in Chapter 4.
4. Groups that are unable to raise sufficient public revenues to provide quality public services and infrastructure are more likely to be poorer than others are. This was discussed in Chapter 5 and 6.

The previous chapters provide practical steps about how to build or improve the economic institutions necessary to support growth but they leave one important question unanswered. If we know what factors help to lift people from poverty, why is it so hard to make these necessary changes?

It is not the case that there is not a desire to make changes that

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<sup>180</sup> Ibid.

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<sup>181</sup> Chief Joseph of the Nez Pierce, Lincoln Hall, January 14th 1879. Chief Joseph was asking to restore the property rights and economic and political freedoms that had been taken from him and the Nez Pierce when they were moved by force from their ancestral lands to a reservation in Idaho territory in 1877.

increase prosperity; it is that these changes are difficult to implement. Munk (2013) recounts the largely failed efforts of Jeffery Sachs whilst attempting to implement changes to eliminate poverty throughout a number of African villages.<sup>182</sup> The conclusion of her research is that good intentions, substantial resources and intricate work plans are insufficient to implement poverty reducing changes.

Jeffery Sachs and others did not fully understand the importance of institutional arrangements. This suggests that real change requires getting the balance between public and private sectors right, as was discussed in Chapter 2. It has also been observed that groups that are poorer do not believe their governments will be able to sustain the economic institutions (property rights, rule of law and quality services and infrastructure) that support economic growth. This is the challenge of tribal and First Nation economic growth – building sustainable, adaptive and innovative governments.

The objective of this chapter is to provide some practical advice on how to successfully implement changes to First Nation and tribal governments and their administrations that support economic growth. It is designed around the following questions:

- What makes implementing an investment facilitation strategy so challenging?
- What are the ingredients for successful changes that support investment facilitation?
- What is the administrative framework to support investment?
- How do you build informed consent for an investment facilitation strategy?
- How do you meet the information requirements of investors?
- How do we maintain momentum and continue to innovate?
- How do we learn more from others?
- What are some examples of successful changes?

This chapter is just a start. There is much more to learn about successfully implementing change. After all, if it were easy, it would be done. This is why it is so important to learn from the success and failures

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<sup>182</sup> Munk, N. (2013). *The Idealist: Jeffrey Sachs and the Quest to End Poverty*. New York: Random House Inc.

of others.

### **Learning Objectives**

The learning objectives for this chapter include:

- Understand the factors that make First Nation and tribal changes difficult to implement as well as the lack of progress of particular economic strategies.
- Describe each of the ingredients for successful economic changes.
- List three elements of the administrative framework to support investment facilitation change.
- Draft a plan to develop informed consent of an economic strategy.
- Describe how to create an investment facilitation information system.
- Identify First Nation or tribal innovations that led to successful or unsuccessful economic strategies.

### **What Makes Economic Change Hard?**

Economic growth-related change is difficult for First Nations and tribes for any, some or all of at least the following reasons:

*History Breads Mistrust* - The history of First Nations and tribes is littered with policies that were either purposely intended to prevent change and growth or well-intentioned but poorly designed. For the former, consider the Dawes Act in the United States<sup>183</sup> or outlawing potlatches in Canada<sup>184</sup>. Both policies were intended to stifle growth of tribal or First Nation institutions. As was stated at the time, they were intended to turn Native Americans and First Nation peoples into wards of the state. As for well-intentioned policies consider the impact of First Nation housing policies in Canada which, although intended to help, have resulted in sub-standard housing. The result of bad policies is

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<sup>183</sup> The Dawes Act was passed in 1887. It was a government led initiative that transferred tribal jurisdiction to the state. Under the Act, over half the reservation lands were removed from tribes and sold to settlers under state jurisdiction. It was subsequently amended in 1891 and 1906.

<sup>184</sup> The Potlatch was operated as a formalized system of wealth redistribution. As part of a wave of legislative initiatives that prevented First Nations from raising revenue and redistributing wealth, potlatches were banned in Canada in 1884. The Indian Act of 1951 removed the prohibition on the potlatch and other ceremonies.

mistrust of policy change led by federal governments in the USA and Canada. Trust is reputation driven. Good policies generate institutional trust. For example, most people trust fiat currency and property rights. Bad policies generate institutional mistrust. Tribes and First Nations do not trust the Bureau of Indian Affairs or Aboriginal Affairs and Northern Development Canada so changes initiated by them will be resisted.

*Designing Economic Institutions is challenging* – Building sustainable institutions that support economic growth is difficult. There is general agreement on which institutions are required to support economic growth (see Chapter 2) but there is considerable disagreement about how to go about designing institutions that generate growth. World famous economists such as Hernando de Soto have spent their lives attempting to design economic institutions that facilitate growth. Hernando de Soto has been successful in Peru but not as much in other countries. Some First Nation institutions such as the First Nations Tax Commission, First Nations Financial Management Board and First Nations Finance Authority have been successful; others such as the First Nations Statistical Institute have not. Designing institutions is not easy and because of the challenges associated with institutional design, many proposed changes for tribes and First Nations have not made it past the pilot project stage.

*Switching Costs are high* – The costs to First Nations and tribes of switching to an economic growth focussed public service have the potential to be high for at least two reasons. Firstly, many members of the tribal and First Nation public sector have been trained to administer systems programs and services that are not growth focussed. Retraining is costly and complex and there are simply not many programs that focus on how to provide a public service in a way that generates investment. Second, administrative systems to support economic growth are not generally available. Software companies spend a great deal of time making it easy for users to switch to their products. First Nation and tribal software that implements improvements to the economic system (e.g. Torrens land registry system) are not commercially available. As a result, they must be designed and built by tribes and First Nations at considerable costs.

*Economic Growth-Orientated Change is Politically Controversial* – Individuals can disagree on a number of matters regarding changes

related to economic growth. They can disagree on whether economic growth is desirable. They can disagree on the best opportunities for economic growth. They can disagree on the changes required to realize economic growth. These disagreements can be within local tribes and First Nations, regional or national tribal and First Nation institutions or at the non-indigenous state, provincial or federal level. The result is that these changes are controversial and will be opposed by some. Many tribal, First Nation and non-native leaders seek to avoid controversies and are reluctant to lead economic growth-orientated change.

*Few Independent Revenues for Change* – Change not only requires resources, it requires resources that can be used for that purpose. Most revenues for tribes and First Nations are transfers from other governments and are designated for a specific purpose. First Nations and tribes need to generate their own independent revenues to build a competitive investment climate. It is difficult to generate independent revenues but as was discussed in Chapter 5, revenue options do exist.

### **What are the ingredients for successful economic change?**

Based on the work of the Institute of Liberty and Democracy (ILD)<sup>185</sup>, and some of the institutional success of First Nations and tribes, the following ingredients seem to be necessary for economic change:

*First Nation or Tribal Led* – First Nations and tribes must lead changes. This is the only way to overcome the history of mistrust. First Nation and tribal leadership of new initiatives provides credibility. Only local, credible leadership can generate the necessary community informed consent to implement a particular change. The most successful recent legislative initiatives in Canada; the *First Nations Fiscal Management Act* and the *First Nations Land Management Act* were both First Nation led.

*Incentives Matter in Design* – Individuals respond to incentives. For example, if managers are rewarded in accordance with the quantity of

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<sup>185</sup> The Institute of Liberty and Democracy is a property rights focused think-tank based in Lima, Peru. Its mission is to assist emerging nations in integrating their poor majorities into the economic mainstream under a single rule of law. It was established in 1979 by Peruvian Economist Hernando de Soto who is known for his work regarding informal economies and property rights reform. For more information on Hernando de Soto's work and the ILD, visit [www.ild.org.pe](http://www.ild.org.pe).

people they manage then they will actively try to increase the number of employees. Some economists have argued that much of government has this particular incentive so as a result they may have too many employees. Alternatively, if managers are rewarded in accordance with economic growth then they will actively support economic growth initiatives, such as working to ensure that there is an improved investment climate. Economic strategies should consider economic incentives and be designed in such a way that managers are rewarded for successful economic strategies. This can be challenging but two ideas that show promise are (1) tying funding to an economic growth focussed revenue stream and (2) associating bonuses with increases in economic growth induced annual tax revenues. In the first example an economic institution's funding could be based on revenue streams (e.g. property transfer taxes) that increase when there are more property transactions and when property values rise. This provides strong encouragement to increase economic activity and property values. In the second example, managers and employees receive bonuses based on tax revenue increases that occur because of economic growth (not increased tax rates). This provides an incentive to generate economic growth.

*First Nation or Tribal Institutional Support* – First Nation or tribal led change requires institutional support. Institutions provide the knowledge, expertise and tools to support change. First, institutions can help address the economy of scale issue because many First Nation and tribal governments are too small to have the necessary administrative structure to support change. Institutions provide supportive rationale, materials and presentations to communities. They create sample laws and procedures to build the necessary legal framework. They can build and support administrative software systems to implement taxation or land management. Institutions can also provide training and education to build administrative capacity at the local level. In short, First Nation and tribal institutions are essential to successfully implement changes on a broad scale.

*Political Will at all Levels* – The changes discussed in this textbook can require federal or provincial/state policy changes/legislation or First Nation or tribal policy changes/legislation or a combination of all of these. None of these changes can occur without political will. Generating political will requires a successful communications strategy.

Communication strategies are discussed later in the chapter, but key elements to generate political will include understanding the interests of other governments and communities, identifying mutual interests and successfully communicating mutual gains. There are a variety of methods to successfully communicate mutual benefits and generate political will but it is important that the communication strategy be First Nation or tribal led to reflect the origin of the particular change being advocated.

*Short Term Success* – It is important to generate and communicate short-term success on an economic strategy. This creates momentum and builds trust. Strategies, institutions and leaders that demonstrate beneficial changes create a foundation of trust that allows them to continue with the implementation of the strategy. Short term success can be demonstrated in a number of ways and based on First Nation and tribal experience three possible strategies include (1) implement a performance measurement strategy to ensure that growth and progress is measured and present regular performance measures reports to membership, (2) present a long term fiscal plan to members and report on progress towards community objectives such as a community project devoted to youth, elders or both, and (3) facilitate small scale investment as part of the larger strategy and measure and communicate benefits from this investment. The key skill for each of these strategies is to communicate reasonable expectations while focussing on the long-term objective of creating a competitive investment climate from which everyone benefits.

*Independent Revenues* – Tribes and First Nations need independent revenues to establish property rights, build infrastructure, establish the legal framework to support markets and build an administrative structure that is responsive to investors. These revenues could be from taxes, royalties, business revenues or some other sources. It is critical that tribes and First Nations find a way to break the catch 22 of economic development. They need independent revenues to build the public side of an attractive investment climate but they can only generate these revenues when they attract sufficient private investment. Innovative solutions to this problem include the First Nations Goods and Service Tax and resource revenue sharing in Canada as well as tribal control of casinos in the United States.

*Separating politics from business administration* – In general, it makes good business and political sense to separate the operation of government and the operation of business. The operation of a business by a government poses special political and administrative challenges. It is often difficult to make correct business choices in the face of political pressure - particularly when the correct choice means people are to be laid-off. There is also a risk that governments will end up subsidizing businesses and this will come at the cost of developing infrastructure or other opportunities. Additionally, although control of a business may be tempting for Chief and Council, many political leaders lack the necessary business acumen and experience to properly operate businesses.<sup>186</sup> Doing so may impact their governmental responsibilities as well.<sup>187</sup> Some of the most comprehensive research on governance features that support investment facilitation for First Nation or tribal governments has been completed by the Harvard Project on American Indian Economic Development. They clearly advocate for this separation. Jorgensen & Taylor (2000) of the Harvard Project state, “Indian enterprises that are subject to undue political influence – especially the influence of elected officials who serve as members of enterprise boards-frequently fail to thrive.”<sup>188</sup>

*Cultural relevance* – Another element stressed strongly by the Harvard Project<sup>189</sup> is that consideration of culture is important because the foundations of successful economies are culturally grounded institutions. Successful First Nation or tribal governments set up governing structures, economic systems, policies and procedures that are

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<sup>186</sup> Cornell, S. (2006). *What Makes First Nations Enterprises Successful: Lessons from the Harvard Project*. Joint Occasional Papers on Native Affairs; 2006-01. Available at [http://nni.arizona.edu/resources/pubs/jopna%202006\\_01\\_success.pdf](http://nni.arizona.edu/resources/pubs/jopna%202006_01_success.pdf).

<sup>187</sup> Ibid.

<sup>188</sup> Jorgensen, M. & Taylor, J.B. (2000). *What determines Indian Economic Success? Evidence from Tribal and Individual Indian Enterprises*. Harvard Project on American Indian Economic Development. Malcolm Wiener Centre for Social Policy; PRS 00-3. Available at <http://hpaied.org/images/resources/publibrary/PRS00-3.pdf>.

<sup>189</sup> For more information on the Harvard Project on American Indian Economic Development visit [www.hpaied.org](http://www.hpaied.org).



congruent with their culture and practices. This reduces switching costs. Supporting private investment and markets is a part of First Nation and tribal culture and history.

These elements for successful change represent a list of necessary conditions as opposed to sufficient ones. There are certainly other elements necessary for change but when one of these elements is missing the likelihood of successful change is reduced. The end of this chapter includes two examples in which some of these elements are missing and the results are predictable – less investment, fewer community benefits and more poverty.

### **How do you start to build administrative framework to support investment facilitation?**

The economic role of government administration is to facilitate private investment at the lowest cost and least amount of time. It does this by responding to the information requirements of investments and ensuring there is broad based community support for greater private investment. Administrations that fail in this area raise three types of investment transaction costs: search, negotiation and contracting. The most important factor in search cost is the availability and reliability of information. Negotiation costs are influenced by community support for investment and administrative procedures and capacity. Contracting costs depend in part on community support and the supportive legal framework but also on administrative experience, procedures and capacity.

An administrative framework to support investment is required because investors do not make decisions about opportunities; they make decisions about information about opportunities. When that information is missing or the cost to accumulate it is too high, they look elsewhere. When it takes too long to negotiate or complete a transaction, the reputation of the jurisdiction suffers and future investment is more difficult to attract and facilitate.

These transaction costs are not only impacted by the administrative system but also the property right system, the legal and fiscal framework and the state of the economic infrastructure. These elements of the overall investment climate were addressed in previous chapters. The following provides three administrative elements to facilitate investment.

- *Communicating the Public Good of Private Investment* – The administration must demonstrate to the community and leadership how they stand to benefit from private investment. The administration needs to build informed community consent for the community economic strategy. This usually involves an economic and fiscal impact assessment of a proposed project or development/economic strategy. The assessment should include benefits such as anticipated investment, number of employment opportunities, anticipated additional public revenues generated and costs (such as additional or new infrastructure requirements, local service requirements and risk mitigation costs related to environmental, heritage or other factors). The administration should also help leadership demonstrate how the strategy is culturally appropriate for the tribe or First Nation or meets other interests related to fiscal independence or jurisdiction. In addition to communicating to their community and leadership, administrations must demonstrate to investors that their jurisdiction is a good place to do business. Communities and regional economies are driven by comparative advantage in location, resources, labour or technology. Investors like to know which comparative advantage a community or region possesses as well as the strategy to realize or enhance that advantage. The absence of this type of strategy can place a community at a disadvantage in working with investors. Furthermore, an inappropriate strategy may also put them at a disadvantage, such as, for example, a strategy based on supporting one investor (the first one) instead of creating a climate for all investors.
- *Reliable Investor Information* – Investors need information that impact their costs (fees, taxes, infrastructure, transportation networks, labour, etc.), their revenues (local market, access to other markets, resources, innovation, etc.) and the rules of developing and operating a business (legal framework and associated procedures). It is expected that this information is available at all times and is frequently updated with the most recent and best available data.
- *Investment Facilitation Support* – Investors need someone to guide them through the rules and procedures of investing in a particular community. Administration should provide the information necessary to investors. They should coordinate the necessary changes

to the First Nation or tribal investment climate necessary to facilitate particular project or types of projects. They should also help ensure that distance is maintained between politics and administration.

The table below summarizes the administrative framework to support investment discussed in this chapter.

*Features and Considerations of the Elements of the Administrative Framework*

Administrative Element	Features of administrative element	Considerations
Communicating the Public Good of Private Investment	Communication to leadership and the community of the benefits of private investment Fiscal and economic benefits of private investment	Should involve an economic and fiscal impact assessment Should be integrated with land and capital plans
Reliable Information	Website providing information on costs, revenues and investment system Mechanism to update and improve information	Many good models exist Start-up costs high but maintenance costs low
Investment Facilitation Support	Guides investors through processes and implements economic strategy Update investor information Coordinate changes to the investment climate	Good models exist Could involve model investor code or approval processes

**How is community and leadership support for an investment facilitation strategy generated?**

Private investment on First Nation land and tribal land creates new businesses and expands existing ones. It stores and generates wealth for individuals. It implements technological and business innovations. It unleashes creative, artistic and scientific potential.

Private investment creates and maintains jobs. The public revenues from private investment helps to build such things as parks, schools, roads, sewer and water systems, libraries, museums, elders homes and cultural centres. These revenues permit a social safety net. Private

investment supports charities, religions and non-profit service agencies. In other words, our communities and the values and ideals they encompass are in large part a result of successful private investments.

First Nation administrations have to communicate the benefits of private investment to their communities and leadership. The objective is to generate informed consent and support for the First Nation investment facilitation strategy. This book contains a number of ideas on how to develop an improved investment climate but implementing these proposed changes will take time and cost money. It is unlikely that an improved investment climate will be realized without the continued support of the community and leadership. This section focusses on two products that are helpful in generating community and leadership support: the economic and fiscal impact assessment and the economic strategy.

### **Economic and Fiscal Impact Assessments**

Estimating the economic impact of a project or development can be a helpful process in regards to understanding the potential benefits of various forms of investment. They generally contain the expected increase in employment, investment and government revenues that will arise from a specific project or development.

These assessments should be divided into economic benefits (employment, business, investment) and fiscal benefits (taxes, royalties, other government revenues). This distinction is important because informed consent is best achieved if both community and individual benefits are realized. It is common practice to seek assistance from firms or consultants that have the ability to provide guidance and expertise on economic impacts as well as experience completing and communicating economic impact assessments.

Three elements of economic impact assessments are important when they are used in communications.

1. *Accuracy* – Economic impact assessments are useful indicators of an order of magnitude (millions vs. tens of millions for example) as opposed to specific amounts. As a result, communication materials should use rounding and ranges to discuss potential impacts.
2. *Methods* – Economic impact assessments estimate how spending associated with a particular investment or development flows

through a regional or First Nation economy. The spending estimate is divided into three types – direct (immediate expenditures on employment, income, investment and taxes resulting directly from the project), indirect (expenditure on employment, income, investment and taxes by suppliers to the initial project or development) and induced (increase in household expenditures because they have more money). The impact assessments are particularly vulnerable to the presence of businesses within the region of impact because this determines the level of “leakage” from the initial investment. Most First Nations have few businesses so have high levels of leakage. The economic impacts of investment on First Nation lands are thus mainly captured by the initial direct affects in most cases. The proposed investors or developers that save considerable time and money often provide direct impact estimates. However, it is important to conduct a review of such estimates to ensure their accuracy before using them in communications.

3. *Framing the Results* – Should economic impact results be presented as gains for community and individuals in the event of community support or potential losses in the event of community rejection? In addition, what results are particularly important to the tribe or First Nation? It may be employment or it may be increased public revenues to fund sidewalks, paved roads, Elders’ assisted living care or a cultural center. It is important to present results in a way that addresses community interests. In addition, it is useful to consider some lessons from behavioral economics. The behavioral economics literature suggests that it is best to frame these assessments as potential losses to individuals and communities and possible gains for another community in the event of community rejection. People are more risk-taking with respect to a potential loss to someone else than they are for a potential gain solely for themselves. Furthermore, Kahneman (2011), suggests two points to consider in regards to communicating risks and loss avoidance. Firstly, most people are willing to take on risk to avoid a loss, “In bad choices, where a sure loss is compared to a larger loss that is merely probable,

diminishing sensitivity causes risk seeking.”<sup>190</sup> Secondly, a relatively small loss is more intense than a larger gain. “For most people, the fear of losing \$100 is more intense than the hope of gaining \$150. We concluded from many such observations that ‘losses loom larger than gains’ and that people are loss averse.”<sup>191</sup>

### **Economic Strategies**

Economic strategies are much more comprehensive than impact assessments. These documents present an economic vision for a community, the potential community benefits of realizing this vision, the potential barriers to that vision and a strategy to overcome these barriers. They generally contain a regional market assessment, an estimate of the investment potential of the First Nation and the fiscal and economic benefits for realizing that potential, a First Nation investment climate assessment, a strategy for improving the investment climate, an estimate of the costs of implementing that strategy and a work plan with performance measures to improve the investment climate. Each of these elements was described in a previous chapter.

Economic strategies can be a powerful communication source. They can be used in briefing notes to Chief and Council. They should be supported and promoted by the Chief and Council and used in community presentations and communications. The First Nation and tribal leadership should secure a community mandate for their economic strategy.

Securing a mandate should incorporate as many ingredients for change discussed earlier as possible. The economic strategy has to be community led. It should provide incentives to individuals and communities. It must be fiscally sustainable and use the resources of other tribal and First Nation institutions when they are available. If required, there should be a strategy on how to generate support and political will from other governments. It has to generate short term success and build on that success. Finally, it should be culturally relevant

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<sup>190</sup> Kahneman, D. (2011). *Thinking, Fast and Slow*. New York: Farrar, Straus and Giroux.

<sup>191</sup> *Ibid.*

and separate business from politics.

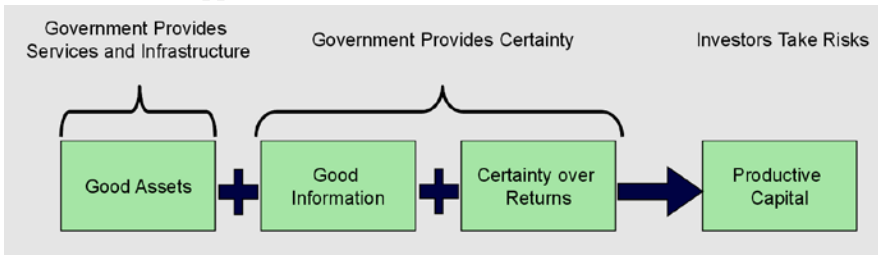
### **How is reliable information provided to investors?**

As mentioned previously in this chapter, investors make decisions on information about opportunities, not opportunities themselves. However, what does this mean? One could have the greatest opportunity in the world, but if an investor is uncertain about it or does not have enough information, the likelihood of the investor taking a risk on the opportunity is quite low.

Since investors make their decisions based on information, there is a great deal of information required for private sector decision-making. Residential, commercial and industrial investors all must have certainty over processes, recourse, land tenure, returns to investment and service quality. This generally means investor codes (discussed later in the chapter); clear land management rules and processes; land registry and tenure security; clarity relating to property, sales, income and corporate tax rates; and sufficient, certain revenue to ensure public service and infrastructure quality. It is also important that information is easily available and accurate.

Primarily, investors want to know what information is available to make their investment decision. How difficult is it to find this necessary information? Is detailed demographic, investment process and contract information available? Investors need information that impacts their costs (fees, taxes, infrastructure, transportation networks, labour, etc.), their revenues (local market, access to other markets, resources, innovation, etc.) and the rules of developing and operating a business (legal framework and associated procedures). It is also expected this is available at all times and updated with the most recent and best available data. The figure below is a simplification of the investment climate equation provided in Chapter 2. It shows that good assets alone cannot generate productive capital. It requires governments to provide services and infrastructure to add value to those assets as well as support in the form of reliable information and certainty over returns.

***Public Sector Supports Private Investment***



When investors are looking for a place to invest, they expect immediate access to reliable information they can utilize to evaluate a potential investment. It is like a person watching TV. If he is not satisfied, he flips the channel.

***Flipping Past Tribes and First Nations***



If information is sparse, that will create uncertainty for the investor and they will be less likely to take a risk on developing in that community or region. To further illustrate this point the figure below shows an example of what a local government provides to potential investors.



### ***Local Government Investor Information***

Community Profile	Tools & Resources	Programs & Support
Sector Fact Sheets	Site Selector	Virtual Job Fair
Overview	Property Finder	About CEPCO
Local Economy	News & Press Releases	CEPCO Partnerships
Lifestyle & Amenities	Publications & Archive	Film Commission
Government Services	Chilliwack Videos	Agricultural Commission
Real Estate Development	Links & Resources	Tourism Chilliwack
		Business Support
		Contact Us

Source: City of Chilliwack, British Columbia, Canada

If you compare many First Nation websites to most local government sites, you will notice that the availability of information relevant to investor’s requirements is quite different. Most First Nations and tribes do not provide information such as:

- Land available for development;
- Economic land use plans;
- Future tax rates and services;
- Current and future infrastructure;
- Demographic and economic statistics;
- Financial administration and reporting;
- Taxpayer and investor relation systems; and
- Investment procedures and processes.

However, a number of First Nations and tribal governments have begun to address this issue. They understand the importance of providing reliable and accurate information. In this regard, the process for filling the information gap usually involves four steps:

1. *Identify the information required* – The list above is a good starting place. Additionally, look to websites of local governments like those referenced.
2. *Administrative data sources* – Much of the required information can be found in existing administrative sources such as developable lands, state of infrastructure as well as financial and taxation information. Base demographic and other economic information may be available in the censuses from national statistics agencies.

However, if possible, administrative sources to update this information should be identified between census years.

3. *Information reliability and currency* – Information must be accurate and current to be useful to investors. It is necessary therefore to determine methods to check and update information as required.
4. *Access* – Investors will expect to find the necessary information on the community website or at least be able to access the information from that website. This means that the administration will need to develop an investor friendly section of the community's website or build a separate site that links to the community site.

The following list provides some links to First Nation and tribal community sites that have been well utilized to convey community information to the public and potential investors.

- Whitecap Dakota First Nation (Saskatchewan, Canada) – <http://www.whitecapdakota.com>
- Squamish Nation (British Columbia, Canada) – <http://www.squamish.net>
- Opaskwayak Cree Nation (Manitoba, Canada) – <http://www.opaskwayak.ca>
- Fort McKay First Nation (Alberta, Canada) – <http://www.fortmckay.com/>
- Cherokee Nation (Oklahoma, USA) - <http://www.cherokee.org>
- Tulalip Tribes (Washington, USA) - <http://www.tulaliptribes-nsn.gov> & <http://www.quilcedavillage.org/>

### **How do you provide investment facilitation support?**

In our experience, there are three key features of successful investment facilitation support services:

1. *Administrative Advocacy for Investor Requirements* – Tribal and First Nation administrations need the capacity to appreciate, communicate and advocate for investor interests. The purpose of this textbook is to provide that understanding and aid in developing the necessary skills for individuals who must communicate investor interests to Chief and Council and rest of the administration. It is through this advocacy and communications that the mandate for a community economic strategy is implemented.

2. *Responsive to Investor Requirements* – Administrations need to steer potential investors through the legal and policy procedures and requirements. They need to respond to questions and provide information. They need to accomplish this efficiently and maintain low transaction costs.
3. *Integrating Investor Interests into Legal Framework and Infrastructure* – Facilitating investment should be an important consideration in the development of the tribal or First Nation legal framework. All the policies imbedded in the laws discussed in Chapter 4 should consider the potential impact on the costs faced by developers and investors. This is why it is so important to be able to advocate for investor interests within the administration. An example of accomplishing this is the investor code framework discussed below.

An investor code is a legal framework for economic transactions that seeks to encourage, facilitate, and streamline private investment projects through the creation of investor certainty. The benefit of this is stimulated economic activity, which will lead to economic growth, increased employment, improved productivity, and ultimately economic development.

In general, investor codes reduce the level of uncertainty potential investor's face. These codes provide details on issues important to investors, including tax rates and services, and the dispute resolution process. Providing necessary clarity in these areas reduces the costs of doing business. Henson and Nathan (1998) make the following points about these types of codes<sup>192</sup>:

1. Legal rules governing commercial transactions.
2. Cover sales and leases, shipping of goods, bank deposits, etc.
3. Outline the rights and obligations in a contract or transaction.
4. De-politicize commercial transaction disputes through standardization.

The following basic principles should be included in an effective investor code, which can be considered the minimum for use on First Nation or tribal lands:

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<sup>192</sup> Henson, E. & Nathan, L. (1998). *Tool of Sovereignty: The Crow Commercial Code*. Harvard Project on American Indian Economic Development. Malcolm Wiener Center for Social Policy; Harvard University.

1. An opening, which should include the short title, the purpose of the code, and a section to provide definitions of specific terms used in the code. The purpose of the code should have three main points:
  - a. To encourage investment;
  - b. To contribute to the economic growth and development; and
  - c. To ensure some benefit is realized by all parties.
2. A description of how the code fits within the existing law, its jurisdictional reach, and any limitations or exemptions.
3. A description of the investment process, including any requirements for notification.
4. Provide information regarding regulations to the code, including where they can be found, and who has the authority to set the regulations.
5. A description of offences, available remedies, potential punishments, the dispute resolution mechanism that will be used, and the recourse available to either party.
6. Details on leases, including the possibility of seizing land or leases to support a First Nation or tribal housing market, as a requirement for access to financing.
7. A closing, which should include a coming into force section and possibly a section to repeal previous laws in this area.
8. Filling the legislative gap with effective investor codes will help to reduce the costs of doing business on First Nation and tribal lands.<sup>193</sup> As in other jurisdictions, this will lead to greater economic activity and ultimately, economic development, which is a primary goal of many First Nation and tribal communities.

## Conclusion

You only get one chance to make a good first impression. This is particularly true for investors because their first point of contact is usually your website and then the administration. If they cannot find

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<sup>193</sup> A good example of a tribal commercial code is that of the Mississippi Band of Choctaw Indians located on their site at [www.choctaw.org](http://www.choctaw.org) and specifically [www.choctaw.org/government/tribal\\_code/Title%2026-%20Uniform%20Commercial%20Code.pdf](http://www.choctaw.org/government/tribal_code/Title%2026-%20Uniform%20Commercial%20Code.pdf).

what they are looking for or perceive that the administration is not helpful then employment and revenue opportunities to the community are lost.

Investors generally look at these elements of the administrative framework to evaluate the investment climate: community support for business, type and quality of information and a responsive administration. In many First Nation administrations, these elements may be missing or inadequate when compared to other investment options and thus potential investors will look elsewhere.

Administrations are the place to start to improve the investment climate but they must first secure a mandate to develop and implement an investment facilitation strategy. Firstly, they need to help Chief and Council develop a viable economic vision. This is best supported by either an economic impact assessment or, better yet, an economic strategy. However, they will need a mandate to implement the investment facilitation strategy. Communicating how private investment supports community objectives is a critical skill for any administration interested in securing a community mandate to support investment facilitation. It is also important to demonstrate to investors that the community politically supports them and recognizes their contribution to the community. With a mandate and community support, the administration can utilize some of the methods described in this chapter to:

- Improve information;
- Design and implement investment facilitation procedures that reduce transaction costs and;
- Generate short-term success and build momentum.