

# *Fiscal Aspects of the Nisga'a Final Agreement*

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## INTRODUCTION

May 11, 2000 marked the effective date of the Nisga'a Final Agreement<sup>1</sup> and the realization of a long-sought goal. On that day, the Nisga'a settled their land claim and achieved a measure of self-determination. And, from their perspective, they gained entry into Canada as Canadians.

Throughout the negotiations, the Nisga'a consistently asserted that they were negotiating their way into Canada. That assertion was not mere hyperbole. Rather, it articulated the fundamental philosophy that guided the Nisga'a in their negotiations and that ultimately was reflected in the treaty.

Viewed from that perspective, the Nisga'a fiscal model is fairly easy to comprehend. Under the model, the Nisga'a will participate in Canadian social benefits, and contribute toward the costs of those benefits, to the same extent and on substantially the same basis as their fellow Canadians. That model reflects the Nisga'a "negotiating into Canada" philosophy and is more or less the model reflected in the fiscal and taxation provisions of the treaty.

While the model is simple in concept, it admittedly is difficult to perceive amid the complexities of the fiscal relations and taxation chapters<sup>2</sup> and the tripartite fiscal financing, own source revenue, and taxation agreements. My task is to try to

- trace a path through some of the complexities and show how the Nisga'a philosophy has been given effect; and
- provide insight, where warranted, as to why certain arrangements were made as they were.

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1 Nisga'a Final Agreement, signed by the Nisga'a's Nation and the Government of British Columbia on April 27, 1999, and signed by the Government of Canada on May 4, 1999 (herein referred to as "the treaty"). The treaty became effective on May 11, 2000.

2 The word "chapter" in this article refers to a chapter of the treaty.

## FISCAL ELEMENTS

The fiscal arrangements under the treaty comprise two elements:

- the financial arrangements; and
- the taxation arrangements.

### Financial Arrangements

The financial arrangements for the Nisga'a Nation are derived from

- the fiscal relations chapter of the treaty;<sup>3</sup>
- the Nisga'a Nation Fiscal Financing Agreement (“the fiscal financing agreement”);<sup>4</sup> and
- the Nisga'a Nation Own Source Revenue Agreement (“the OSR agreement”).<sup>5</sup>

### *Fiscal Relations Chapter*

The fiscal relations chapter sets out the principles to be taken into account in negotiating each fiscal financing agreement and own source revenue agreement. The two subsidiary agreements put those principles into effect by defining the specific programs and services that are to be provided to Nisga'a citizens by the Nisga'a Nation and establishing the means by which those programs and services will be funded.

In simplistic terms, under the arrangements, the Nisga'a Nation will be responsible for ensuring the delivery of agreed-upon<sup>6</sup> programs and services to Nisga'a citizens,<sup>7</sup> at levels that are reasonably comparable to those generally prevailing in northwest British Columbia. Funding for these programs and services will be provided

- first, by the Nisga'a Nation itself, to the extent of its “own source revenue capacity” (OSR) (as calculated in accordance with provisions of the OSR agreement); and
- second, by Canada and British Columbia, to the extent that the agreed-upon funding for the defined programs and services exceeds the Nisga'a Nation's OSR.

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3 Chapter 15 of the treaty.

4 *Ibid.*, at paragraphs 3 to 13.

5 *Ibid.*, at paragraphs 14 to 20.

6 Nisga'a citizens will continue to be eligible to participate in federal or provincial programs or services for which the Nisga'a Nation has not assumed responsibility under a fiscal financing agreement. Employment insurance is one obvious example.

7 And, in the case of certain health, social assistance, and local programs and services, to non-Nisga'a persons on Nisga'a Lands.

## ***Fiscal Financing Agreement***

### *Agreed-Upon Programs and Services*

The fiscal financing agreement sets out the program and service responsibilities of the Nisga'a Nation. Under that agreement, the Nisga'a Nation is to ensure the delivery of programs and services in four core areas:

1) health:<sup>8</sup>

a) public health services (such as immunization, communicable disease control, environmental health, occupational health and safety, home nursing, senior care); and

b) non-insured health benefit programs (provincial health plan premium assistance, vision care, dental care, patient transportation, drugs and medical supplies);

2) education:

a) kindergarten to grade 12;<sup>9</sup> and

b) post-secondary education and training support;

3) social services (income assistance for essential food, clothing, and shelter; child and family services; training, education, and employment programs; community programs); and

4) local services, including

a) local municipal services, land management and fisheries, environmental and wildlife management; and

b) residential housing assistance.

For the most part, the Nisga'a Nation's responsibilities affect only Nisga'a citizens<sup>10</sup> on Nisga'a Lands. Certain local services, such as provision of sewer, water, fire protection, etc., and certain social services, such as income assistance and community programs and services, will be provided to all persons ordinarily resident on Nisga'a Lands.

Program standards, including those affecting level of service, program eligibility, equality of access, processes of appeal, and reporting must be comparable with those of the province or, where applicable, those of the federal government.

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8 The Nisga'a Nation has engaged the existing local health board under contract to deliver the agreed-upon health programs and services on behalf of the Nisga'a Nation. The Nisga'a Valley Health Board also provides physician, diagnostic, and treatment services under agreements directly with the province.

9 The Nisga'a Nation purchases its kindergarten to grade 12 education programs and services from provincial school boards at the district per-pupil block rate established by the province.

10 That is, those individuals who apply to become, and qualify as, Nisga'a citizens under the Nisga'a Citizenship Act.

### *Determination of Funding Requirements for Agreed-Upon Programs and Services*

Base-level funding for the above programs and services was established on the basis of the actual audited costs of providing these programs and services to the four Nisga'a bands for the March 31, 1998 fiscal year.<sup>11</sup> That base-level funding was then adjusted by agreed-upon factors to reflect the effects of inflation and population growth since March 1998.<sup>12</sup>

Substantially all of the funding to be provided by the Nisga'a Nation, Canada, and the province during the five-year term of the fiscal financing agreement will be provided on a "block funding" basis. Because of this, the benefits of any cost savings during the term will accrue to the benefit of the Nisga'a Nation. Conversely, any losses caused by operating inefficiencies or other factors will be borne exclusively by the Nisga'a Nation. I suspect that for Canada and British Columbia, this new degree of certainty and the transfer of public accountability are among the more appealing features of the self-government arrangement.

### *Nisga'a Contributions*

As stated earlier, funding of the foregoing programs and services is to be a shared responsibility of the three governments. The Nisga'a will contribute to the cost of programs and services in two ways:

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- 11 There is a widely held perception that program funding for aboriginal people differs substantially from that provided for other Canadians. In fact, actual 1998 expenditures for health, education, and social assistance benefits provided to the Nisga'a were based on standards that applied to all residents in northwest British Columbia in that year. (For instance, the per-capita rate paid to the local provincial school district was in accordance with the norms for school districts in the province. Similarly, health and social income support payments were based on provincial norms.) If the per-capita amounts spent on these programs for aboriginal people are more or less the same as those spent for non-aboriginals, why does the general population perceive the two so differently? One singular difference is that the funding of programs for non-aboriginal Canadians is provided by provincial governments from a variety of government envelopes, while programs for aboriginal people are funded out of a single, and highly visible, federal government envelope. Can it be that the mere *method* of providing funding to aboriginal people in itself contributes to some of the misperceptions held by the public?
  - 12 Specifically, the "effective year funding amount" for each core program or service area was determined by adjusting the base-level funding amount for the program or service area by the percentage growth in funding provided for the Department of Indian Affairs and Northern Development in the federal budgets for the 1999 through 2001 fiscal years. Most (but not all) of the "effective year funding amounts" will be annually adjusted during the term of the fiscal financing agreement to reflect year-to-year changes in the *Canada Final Domestic Demand Implicit Price Index*, series D15613 (as published regularly by Statistics Canada in matrix 6544: Implicit Price Index, Gross Domestic Product, or its replacement series as specified by Statistics Canada). In addition, effective year funding amounts for health, social, income assistance, and education program areas will be annually adjusted by a predetermined factor for expected population growth.

1) Nisga'a citizens will indirectly contribute to the cost of Nisga'a Nation programs and services through the payment of tax to the federal, provincial, and, perhaps, Nisga'a governments; and

2) Nisga'a governments and institutions will contribute to the cost of government programs and services to the extent of their OSR as determined under the provisions of the treaty and the OSR agreement.

### *Taxation of Individuals*

Section 87 of the Indian Act<sup>13</sup> will cease to apply to Nisga'a citizens

- in respect of "transactions taxes"<sup>14</sup> as of June 1, 2008; and
- in respect of all other taxes on January 1, 2013.<sup>15</sup>

This transitional rule will provide little benefit for property situated within Nisga'a Lands, since all such lands ceased to be "reserves," and thus lost their "section 87" status, on the effective date of the treaty. To mitigate that factor, Canada and British Columbia each passed remission orders granting remission of tax imposed or levied in respect of an Indian's interest in former reserves situated within Nisga'a Lands, or in personal property situated on those former reserves, during the 8-year and 12-year periods described above.

For reasons discussed below, I suspect that Nisga'a governments are unlikely to exercise their taxation powers, except perhaps to impose a sales tax during the phaseout of the Indian Act exemption. Thus, I suspect that, once the system is fully mature, Nisga'a citizens will pay most, if not all, of their taxes to Canada and British Columbia, rather than to Nisga'a governments. If so, taxes paid by Nisga'a individuals will be absorbed into the general revenues of the province and Canada, and the value of this important contribution by the Nisga'a people to the cost of their own government will not be readily apparent to the outside observer.

### *Nisga'a Nation Own Source Revenue Capacity*

The second means by which the Nisga'a will contribute to the cost of their own government is through the OSR provisions of the treaty. These were the most contentious and difficult to negotiate of all of the financial provisions in the treaty. At the outset, Canada and British Columbia were reluctant to place any

13 RSC 1985, c. I-5, as amended.

14 The term "transactions taxes" is not defined in the treaty, but is taken to include goods and services tax (GST), provincial retail sales tax, property transfer taxes, and the like.

15 An individual may elect to be deemed to have disposed of, and reacquired, each of his or her qualifying properties at its fair market value immediately before the January 1, 2013 transition date. This election will allow the individual to "crystallize" his or her gain in a period when the individual was still covered by the section 87 exemption or by the remission order referred to below.

upper limit on the amount of the Nisga'a Nation's OSR that could be taken into account in determining their respective net contributions to cost of government. Not surprisingly, they took the position that the business of government is to raise revenues for providing programs and services. Thus, they found it difficult to accept the idea of limiting the extent to which Nisga'a government revenues could be applied to the cost of Nisga'a programs and services.

The Nisga'a took the position that the "normal" government model articulated by the federal and provincial negotiators overlooked three important factors:

1) Without upper limits, Canada and British Columbia could use the OSR provisions to effectively "claw back" much of the cash and land component of the land claim settlement. That is, if the bulk of the economic produce from the land and cash were applied to defray what Canada and British Columbia would otherwise be required to contribute for programs and services, that cash and land would have very little residual economic value for other purposes. Faced with that, the Nisga'a would be put under pressure to distribute their land and cash, if only to preserve its economic worth.

2) The Nisga'a noted that they were more likely to own and, to a significant degree, commercially exploit their forests and other economic resources as a community, rather than as private entrepreneurs. If, for instance, 70 percent of the Nisga'a government's net forest revenues were to be included in OSR, it would be put at a disadvantage relative to other private land owners who would be subject only to taxation under laws of general application. Again, there would be enormous pressure to distribute the resources and put them into private hands.

3) As previously noted, the basic Nisga'a philosophy was that, if they are to participate as Canadians, their contribution to Canada should be made to the same extent and on the same basis as that of other Canadians. If no reasonably certain limits were placed on the quantum of their OSR, the Nisga'a could never be certain that their collective contribution to Canada would never exceed that of their fellow Canadians.

The provisions that emerged from the treaty discussions were designed to ensure that the Nisga'a Nation contributes to the cost of its own governance in an amount equal to the tax revenues that would be raised by other governments if those governments subjected the activities on Nisga'a Lands to tax. In effect, the OSR became a surrogate for tax.

### ***Nisga'a Nation Own Source Revenue Agreement***

The OSR agreement contemplates five principal sources of OSR:

1) commercial and investment activities of the Nisga'a Nation, the Nisga'a Villages, and certain entities in which any of them holds a beneficial interest, where those activities are not otherwise subject to tax;

2) direct taxation by the Nisga'a Nation and Nisga'a Villages;

- 3) incomes from property within a Nisga'a settlement trust;<sup>16</sup>
- 4) charges and fees derived by the Nisga'a Nation, the Nisga'a Villages, and certain entities in which any of them holds a beneficial interest; and
- 5) other revenues derived by the Nisga'a Nation, the Nisga'a Villages, and certain entities in which any of them holds a beneficial interest.

In general, and subject to specific exclusions and transitional rules, OSR in respect of these revenue sources will be an approximation of the tax revenues and other levies that Canadian governments might be expected to derive from similar revenue sources within their jurisdiction.

#### *Excluded Revenues*

Certain items are permanently excluded from OSR. In general, these excluded items represent property transferred to the Nisga'a Nation under the treaty, or proceeds from the sale thereof; incomes specifically dedicated to pre-identified government purposes, such as income earned by the Nisga'a capital finance authority;<sup>17</sup> gifts received from third parties; and intergovernmental transfers of revenues that have otherwise already been contemplated in the determination.

#### *Transitional Rules*

Transactions taxes and other taxes payable by Nisga'a citizens to the Nisga'a Nation, which ordinarily would be included, will be excluded from OSR during,

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16 That is, a trust used to receive and hold funds received out of the cash component of the Nisga'a land claim. The Nisga'a Nation may establish one or more Nisga'a settlement trusts for the benefit of itself, one or more Nisga'a Villages, all Nisga'a citizens, all Nisga'a citizens in any Nisga'a Village, another Nisga'a settlement trust, or any registered charity or other non-profit organization that directly or indirectly benefits the Nisga'a. A Nisga'a settlement trust must be resident in Canada. Contributions to the trust are limited to those made out of the capital transfer payments received by the Nisga'a Nation under the treaty or amounts received from another Nisga'a settlement trust. In general, the trust's funds must be invested in securities that qualify as investments for registered retirement savings plans. If the deed permits, a Nisga'a settlement trust also may make loans to a Nisga'a citizen, the Nisga'a Nation, a Nisga'a Village, or a Nisga'a government corporation if interest is charged at a rate equal to the rate prescribed under regulation 4301(c) of the Income Tax Regulations at the time the loan was made. In addition, a Nisga'a settlement trust may make low-interest or interest-free loans to Nisga'a citizens to assist the borrower in acquiring a home, furthering his or her own education or vocational skills, or carrying on a business on Nisga'a Lands, where the borrower cannot borrow from commercial lenders at normal commercial rates of interest. A Nisga'a settlement trust is not permitted to carry on a business as a proprietor or member of a partnership or to borrow money, except as required to finance the acquisition of qualified investments or to carry out its operations.

17 This is an authority to be established by the Nisga'a Nation for the purposes of financing the major maintenance and ultimate replacement of its government capital infrastructure, as required from time to time.

respectively, the first 8 and 12 years immediately following the effective date of the treaty.

Income and capital gains of a Nisga'a settlement trust will not be included in OSR for the first 12 years commencing on or after the effective date. This is consistent with a principle that OSR in respect of a settlement trust should be commensurate with the tax that would be raised if the trust corpus were directly held and invested by the Nisga'a citizens themselves, rather than by the trust.

All other OSR will be phased in on a staged and incremental basis over the first 12 years following the effective date, so that only a specified percentage<sup>18</sup> of the amount otherwise determined will be taken into account in each of those years.

### *Commercial and Investment Activities*

OSR in respect of commercial and investment activities of the Nisga'a Nation, Nisga'a Villages, and their tax-exempt corporations, in general, will be equal to the sum of the taxes that would be payable by them to a government in Canada if

- each such entity were subject to tax under laws of general application;
- the Nisga'a Nation and each Nisga'a Village were unrelated Canadian-controlled private corporations; and
- the only activities of each entity were its commercial and investment activities, and its only property were the property it employed in a commercial or investment activity in the year.<sup>19</sup>

Each entity will compute the corporate tax that it would pay for the particular fiscal year if it were subject to tax under the rules that apply to private corporations in the commercial mainstream and if the relevant assumptions applied. For that purpose, the entity's tax will be computed in accordance with the rules that are in effect for the particular year under each of the relevant taxing statutes. For instance,

- interest, dividends, and investment income will be treated in the manner prescribed under the Income Tax Act<sup>20</sup> for similar incomes derived by taxable Canadian-controlled private corporations;
- an allowable loss incurred by a particular entity in any particular year will be treated as it would be under normal corporate income tax rules—that is, it will

18 The "specified percentage" is 0 percent for the first 2 fiscal years commencing on or after the effective date; 5 percent for the 3rd and 4th years; 10, 15, 20, 30, 40, 55, 70, and 85 percent for the 5th, 6th, 7th, 8th, 9th, 10th, 11th, and 12th years, respectively; and 100 percent for the 13th and subsequent fiscal years.

19 These provisions ensure that property, revenues, and expenses associated with public programs and services activities of the entity are not taken into account in determining the OSR in respect of the entity's commercial and investment activities.

20 RSC 1985, c. 1 (5th Supp.), as amended.

be carried over and applied against the entity's income for preceding or subsequent years, within the prescribed statutory limits; and

- the losses of any entity will not be available to reduce the income of another without one being wound up into the other or the two being otherwise legally merged.

The parties will be guided, in applying the relevant statutory rules for a particular year, by decided jurisprudence, published interpretations, and published rulings that are available to the public as at the end of that year.

Many Nisga'a government corporations will be subject to tax under laws of general application.<sup>21</sup> In addition, the Nisga'a Nation and Nisga'a Villages may be subject to tax under some taxing statutes. In those cases, the Nisga'a Nation, Nisga'a Villages, Nisga'a government corporations, and Nisga'a exempt corporations will pay those taxes under the normal rules. The bases upon which those taxes are levied will be excluded from the amounts used to calculate OSR.

Rules provide that no deduction will be made in computing income or taxable income, for purposes of computing OSR in respect of commercial and investment activities, for any amount that can reasonably be considered to be an expenditure in respect of

- a program or service for which funding has been provided to the Nisga'a Nation under a fiscal financing agreement; or
- a management, enhancement, or rehabilitation activity in respect of a natural resource, other than a forestry resource, that is reasonably comparable in nature to an activity carried on by another government in Canada in respect of the management, enhancement, or rehabilitation of a similar natural resource.<sup>22</sup>

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21 A Nisga'a government corporation will be exempt from tax under the Income Tax Act only if the Nisga'a Nation and/or one or more Nisga'a Villages directly own at least 90 percent of its issued shares or if it is a wholly owned subsidiary of such a corporation. Thus, for instance, a Nisga'a government corporation that is 50 percent owned by the Nisga'a Nation and 50 percent owned by a company that is wholly owned by the Nisga'a Nation will not be exempt from tax under the Income Tax Act. Moreover, a company that meets the share ownership test will nevertheless be taxable if more than 10 percent of its income is derived from activities carried on outside the geographic boundaries of its shareholders (that is, in the case of a shareholder that is a Nisga'a Village, its Village lands; in the case of the Nisga'a Nation, Nisga'a Lands).

22 This provision recognizes that Nisga'a governments will both govern and exploit the natural resources on Nisga'a Lands, and that certain types of expenses may be common to both roles. The provision attempts to draw a line, for resources other than a forestry resource, to distinguish those expenses that commonly would be regarded as being necessary or ordinary to the exploitation of a natural resource by a private entrepreneur, from other expenses that might be incurred by governments or their agencies in respect of the resource. The express exception for forestry resources recognizes that some forest tenures on provincial Crown land require the provincial government to incur expenditures (for example, silviculture, construction of roads and bridges, etc.) similar to those that a private owner of fee simple forest lands might incur in logging its own lands. The parties agreed that it would be inequitable to deny the deduction

Depletion (and future recapture) in relation to an interest in a forest resource on Nisga'a Lands will be computed as if the interest had originally been acquired by the relevant entity at a cost equal to,

- where the property was last acquired after the effective date of the treaty from a person with whom the entity was dealing at arm's length (other than the Nisga'a Nation, a Nisga'a Village, or a Nisga'a government corporation), the consideration given to the arm's-length party for that acquisition of that interest; or
- otherwise, the fair market value of the interest as at the effective date.

For commercial mining activities, OSR in respect of the exploitation of an interest in a mineral, petroleum, or natural gas resource is to be computed as if the Income Tax Act were read without reference to paragraphs 12(1)(o), 12(1)(z.5), 18(1)(m), and 20(1)(v.1) and subsections 69(6) and (7) thereof.<sup>23</sup>

#### *Nisga'a Taxes*<sup>24</sup>

The Nisga'a Nation will calculate an OSR for each type of Nisga'a tax for each fiscal year in accordance with the rules set out in the fiscal relations chapter of the treaty, as augmented by provisions in the OSR agreement.

The fiscal relations chapter recognizes that any Nisga'a tax will be imposed under two possible circumstances:

- 1) under the authority of paragraph 1 of the taxation chapter, in which case the tax will apply only to Nisga'a citizens on Nisga'a Lands; or
- 2) under delegated authority of Canada or British Columbia to impose the tax on other persons on Nisga'a Lands.

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of such expenditures by a Nisga'a entity in relation to its fee simple forests simply because the expenditures are comparable in nature to those that might be incurred by a provincial government in relation to Crown lands. By the same token, the rules make it clear that forest management and development expenses will be deductible only to the extent that they are incurred for the purpose of earning income and are reasonable in the circumstances.

- 23 Under the Lands chapter of the treaty (chapter 3), the Nisga'a Nation will have exclusive authority to determine, collect, and administer any fees, rents, royalties, or other charges in respect of mineral resources on or under Nisga'a Lands. Nisga'a government entities will not be liable for any provincial Crown royalties in respect of those resources and, as a consequence, the amounts referred to in paragraphs 12(1)(o) and 18(1)(m) and subsections 69(6) and (7) of the Income Tax Act will be nil for those entities in respect of those resources. Similarly, with the elimination of Crown royalty payments, there is no need to compensate the entities for any inability to deduct those payments and, thus, no need for any reference to the "resource allowance" provisions in paragraphs 12(1)(z.5) and 20(1)(v.1) of the Income Tax Act when computing OSR in respect of the resources.
- 24 A "Nisga'a tax" is a direct tax imposed by a Nisga'a government on Nisga'a citizens or on other persons (if authority to tax such other persons has been delegated by Canada or British Columbia under an agreement with the Nisga'a Nation), and includes any fine, penalty, or interest paid to the Nisga'a Nation or a Nisga'a Village in respect of the tax.

In both cases, Nisga'a authority to impose the tax will run concurrently with that of Canada and British Columbia and may be exercised with or without the agreement of those parties to provide the Nisga'a Nation or Nisga'a Village with the room to impose its tax. In practice, it is expected that the Nisga'a Nation will not tax its own people, or be delegated authority to tax others, without a tax coordination agreement that, through an appropriate sharing of tax room, ensures that taxpayers are not taxed excessively relative to their counterparts in similar communities.

Paragraph 16(c) of the fiscal relations chapter, as augmented by the OSR agreement, provides that the OSR in respect of a Nisga'a tax will not exceed the sum of

i) the amount of tax room made available in respect of the tax by Canada or British Columbia; plus,

ii) where the tax is similar to a tax generally imposed by local authorities in British Columbia (such as real property taxes),

A. where the tax is imposed only on Nisga'a citizens, 50 percent of the amount by which the Nisga'a tax revenues exceed the amount determined under (i) above, or

B. otherwise, the amount by which the Nisga'a government's "tax capacity" in respect of the tax exceeds the amount determined under (i) above,

minus the reasonable costs incurred by the Nisga'a government in developing and administering the tax system in respect of the tax and in collecting the tax.

For the purposes of (ii)(B) above, the Nisga'a government's "tax capacity" in respect of the tax is to be determined on a fair and reasonable basis, taking into account the circumstances in the Nisga'a communities and in similar communities in northwest British Columbia.

*Example 1*

Assume that the Nisga'a Nation institutes a sales tax regime on transactions occurring on Nisga'a Lands.

a) If the tax is imposed in full replacement of the 7 percent provincial social services tax (that is, because British Columbia has vacated the sales tax field to the extent required to give the Nisga'a Nation the room to impose a comparable 7 percent tax), and unless the Nisga'a Nation can negotiate a lower OSR inclusion rate, the OSR in respect of the Nisga'a tax will be equal to the social services tax that British Columbia would otherwise have expected to collect had it not given up that tax room (whether the Nisga'a tax is imposed at 7 percent, 10 percent, or not at all), minus the reasonable costs incurred in respect of the tax by the Nisga'a Nation.

b) If British Columbia decides to remain in the field but agrees to drop its own rate to 3 percent, the OSR in respect of the Nisga'a tax will be equal to the additional social services tax that British Columbia would have expected to collect had it continued to impose tax at 7 percent, rather than at the reduced rate of 3 percent (again, regardless of the rate, if any, at which the tax is imposed by the Nisga'a Nation), minus the Nisga'a Nation's reasonable costs.

c) If British Columbia continues to impose its own tax in addition to the tax imposed by the Nisga'a Nation, there will be no OSR in respect of the Nisga'a tax. The tax collected by the Nisga'a Nation will not affect the amount of the net transfer to be received under the fiscal financing agreements. (This most likely could occur only while British Columbia's remission of sales tax paid by Indians on Nisga'a Lands remains in effect—that is, only during the first 8 years following the effective date. Thereafter, the Nisga'a Nation is not likely to impose a sales tax without being delegated the tax room by the province, since to do so would increase the effective tax burden for residents on Nisga'a Lands above that for residents of the surrounding area.)

*Example 2*

Assume that a Nisga'a Village institutes a real property tax regime on its Village Lands.

a) If the tax applies only to Nisga'a citizens, the OSR in respect of the tax could be equal to 100 percent of the tax room made available in respect of the tax by British Columbia, minus the Village's reasonable costs in respect of the tax room, plus 50 percent of any revenues received by the Village in excess of that tax room. If no tax room is granted by British Columbia, the OSR in respect of the tax will be 50 percent of every dollar of tax collected by the Village.

b) If the tax applies to all persons on the Village Lands, the OSR could be 100 percent of the "tax capacity" in respect of the tax, minus the Village's reasonable costs.

The OSR agreement, in general, does not provide any particular incentive for Nisga'a government taxation after the taxation remission orders have expired and the system is mature. As the agreement is written, the OSR in respect of any tax, other than a property tax or other local tax, will simply be equal to the amount of tax room vacated by the relevant senior government. Every dollar of tax raised by the Nisga'a government out of that tax room will be included in its OSR and will thereby reduce, on a dollar-for-dollar basis, the fiscal transfers it would otherwise receive from that senior government. The Nisga'a government would derive no net economic benefit from the tax, unless it were willing to impose, and could collect, tax at a rate in excess of the tax room surrendered by the senior government—in short, at a rate in excess of what the taxpayers otherwise would have to pay under the status quo. This does not seem to be a practicable alternative. Given these factors, I suspect that the Nisga'a Nation will not impose much more than transitional sales taxes within the foreseeable future, unless senior governments provide some incentive for it to do so.

The issue of property tax raises its own particular concerns. Under the OSR agreement, OSR in respect of property taxes, in all cases, will be greater than the tax room given up by the taxing authority:

- Where the Nisga'a tax is imposed only on Nisga'a citizens, the OSR will be an amount equal to the surrendered tax room plus 50 percent of the amount by which the taxation revenues exceed that tax room.

- In any other case, the OSR will be equal to the “tax capacity” in respect of the tax. “Tax capacity” will be determined by comparison with the “tax capacity” of similar communities in northwest British Columbia. That comparison will consider a number of factors, including the capacity to tax in relation to relative levels of income and, more important, the capacity to tax in relation to the relative level of local services provided in each community.

Nisga'a Lands all lie outside municipal boundaries and, hence, are subject to taxation under the Taxation (Rural Area) Act of British Columbia.<sup>25</sup> The Taxation (Rural Area) Act provides for relatively low tax rates, reflecting the low level of local services generally provided by the provincial government within the sparsely inhabited rural areas of the province. That level of local services is far below what is provided by Nisga'a governments within Nisga'a residential communities and by local governments in other comparable communities in northwest British Columbia. Thus, if the “tax capacity” of Nisga'a communities is determined by comparison with that of other residential communities, it will likely be significantly greater than the “tax room” currently occupied by the province in respect of taxes imposed under the Taxation (Rural Area) Act.

The foregoing factors would cause significant difficulties for any Nisga'a government that wished to establish its own property tax regime. If it considered taxing only Nisga'a citizens, it would find that it would derive no net economic benefit, unless it chose to tax its own citizens at rates in excess of what they would otherwise be required to pay to the province under the status quo. This may be particularly difficult to do if there are non-Nisga'a taxpayers within the area who can continue to pay their taxes at the lower provincial rates. If the Nisga'a government were to seek delegated authority to tax all of the residents in its communities, it could be forced by the OSR provisions to tax those residents on a “tax capacity” basis—that is, at rates substantially above what they otherwise would be required to pay to the province under the status quo. It seems unlikely that the Nisga'a government would choose to proceed in either case.

### *Nisga'a Settlement Trusts*

The Nisga'a Nation will determine the taxable income of each Nisga'a settlement trust for the “taxation year” of the trust that ends in the Nisga'a Nation's fiscal year. That “taxable income” will then be multiplied by a “composite tax rate,” to arrive at an OSR in respect of the particular trust.

The terms “taxable income” and “taxation year” have the same meanings as in the Income Tax Act.<sup>26</sup> Thus, “taxable income” will be determined, for example, by including, among other things, taxable dividends from Canadian-resident corporations at their grossed-up amounts and the taxable amount of the trust's

25 RSBC 1996, c. 448, as amended.

26 See the definitions in subsections 248(1) and 249(1), respectively.

capital gains realized in the year, and by deducting, among all other amounts deductible in computing the taxable income of a trust under the Income Tax Act, the amount of the income of the trust that is paid or made payable to its beneficiaries in the taxation year.

The “composite tax rate” is intended to approximate the net change in all income taxes, transactions taxes, and refundable tax credits that would be paid or reduced in respect of all Nisga’a citizens if an amount equal to the trust’s taxable income were paid to them each year in equal shares. By agreement, the “composite tax rate” was set at 18 percent for the term of the first two fiscal financing agreements and will thereafter be determined in accordance with an agreed-upon prescribed method.

### *Charges and Fees*

Charges or fees that are levied in connection with agreed-upon programs and services and are similar to those generally levied in similar circumstances by governments in British Columbia<sup>27</sup> will be included in OSR at the prescribed rate of 46 percent. The prescribed percentage is applied to the amount by which the charges or fees exceed the reasonably deductible costs incurred in the levying of the charge or fee, to the extent that such costs would not have been incurred but for the imposition of the charge or fee.

### *Other Revenues*

Revenues not explicitly contemplated in any of the four foregoing categories will be included in OSR on the same basis as that applied to charges or fees.

### *Amounts Not Included*

Certain items are specifically excluded from OSR. Such items include

- proceeds from the sale of Nisga’a Lands or Nisga’a Fee Simple Lands, other than revenues received in the course of renting or licensing the lands, or taking production from the lands, or revenues that can reasonably be considered to represent a recovery of depletion or depreciation that has been claimed as a deduction in the calculation of OSR;
- for the first 12 years commencing after the effective date, the income or capital gains of a Nisga’a settlement trust;
- transactions taxes or other taxes paid by Nisga’a citizens to their governments during the 8-year and 12-year periods when the relevant federal and provincial remission orders are in effect;

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27 For example, charges in respect of government health programs or services, fishing and hunting licences, park utilization fees, building permits, business licences, moorage, recreation fees, fines, and penalties not relating to tax offences.

- gifts to the Nisga'a Nation, a Nisga'a Village, or a Nisga'a Institution; and
- the taking of a natural resource on Nisga'a Lands for the personal consumption of a Nisga'a citizen for any purpose other than profit.

### **Taxation Arrangements**

The taxation arrangements for the Nisga'a Nation are derived from

- the taxation chapter;<sup>28</sup> and
- the Nisga'a Nation Taxation Agreement (“the taxation agreement”).<sup>29</sup>

### ***Taxation Chapter***

The taxation chapter sets out the core components of the taxation relationship among the Nisga'a Nation, Canada, and British Columbia, including

- the phaseout of the tax exemption currently provided under section 87 of the Indian Act (discussed above);
- the primary taxation powers of the Nisga'a Nation;
- provision for negotiation of delegated tax authority;
- provision of limited tax exemptions; and
- provision requiring the parties to enter into the taxation agreement referred to above.

Under the taxation chapter, Nisga'a Lisims Government<sup>30</sup> has the power to make laws in respect of direct taxation of Nisga'a citizens on Nisga'a Lands.<sup>31</sup> This power to tax Nisga'a citizens is concurrent with that of Canada and British Columbia and does not limit the powers of those governments to make laws in respect of the taxation of Nisga'a citizens or other persons on Nisga'a Lands.

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28 Chapter 16 of the treaty.

29 Referred to *ibid.*, at paragraphs 21 to 23.

30 That is, the government of the Nisga'a Nation.

31 The treaty gives the Nisga'a Nation only the power to impose direct tax on Nisga'a citizens on Nisga'a Lands. It does not give any power to tax Nisga'a citizens off Nisga'a Lands, nor does it confer power to tax any person who is not a Nisga'a citizen, regardless of where that person is or resides. One commentator has suggested that the Nisga'a Nation has been given the power to impose “stumpage taxes” in relation to forest resources taken from their lands. That suggestion may be based on a presumption that any royalties received in respect of production from Nisga'a Lands constitute a “tax.” The Nisga'a hold their lands as owners in fee simple and, like any landowner, can charge royalties in respect of timber that others remove under licence from their lands. The Nisga'a view such royalties as a yield on their capital that will be employed for community purposes, either through the OSR provisions of the fiscal financing arrangements, or otherwise through community investment not contemplated in those arrangements.

Thus, after the 8-year and 12-year transition periods, all Nisga'a citizens will be subject to federal and provincial taxation on the same basis, and under the same laws of general application, as any individual who resides in rural British Columbia. At that time, any taxes paid by individuals under a Nisga'a tax regime will be *in addition* to the taxes they pay to Canada and British Columbia, unless the Nisga'a Nation is able to negotiate tax room under a tax coordination agreement with those two senior governments, as discussed below.

The treaty anticipates the possibility that Canada and/or British Columbia may enter into one or more agreements to give one or more Nisga'a governments delegated direct taxation authority over persons other than Nisga'a citizens, on Nisga'a Lands. Such agreement conceivably could give the Nisga'a Nation a delegated authority to impose tax in a particular area (for example, property tax, sales tax, or income tax) on Nisga'a Lands. Again, any taxes paid to a Nisga'a government under this delegated authority would be in addition to the tax otherwise payable to the affected senior government, unless the Nisga'a Nation were able to negotiate tax room under a tax coordination agreement with that senior government.

The treaty provides that the Nisga'a Nation may negotiate with Canada and/or British Columbia to enter into tax coordination agreements, so as to coordinate Nisga'a government taxation, including provision of tax room, with that of the senior governments. Each tax coordination agreement will have to be negotiated by the parties on the basis of the conditions at the given time. No terms are prescribed or preordained under the treaty. It seems likely that any delegated authority will be limited in its scope to Nisga'a citizens, to occupants of Nisga'a Lands, or to hotel patrons, etc., depending on the nature of the tax involved, ease of administration, and similar factors. In some cases, the tax would be administered and collected on behalf of the Nisga'a Nation by Canada or the province (for example, an income tax imposed on Nisga'a citizens); in others, it may be administered by the Nisga'a Nation on its own behalf (such as a property tax).

A Nisga'a government contemplating entry into the taxation field will have to weigh carefully the impact on OSR and the Nisga'a government's consequent financial obligations under the fiscal financing agreement. Under the treaty and the present OSR agreement, the amount of annual fiscal funding provided by Canada and British Columbia will be reduced by an amount up to the value of the tax room or tax capacity made available to the Nisga'a Nation under a tax coordination agreement. Thus, any possible economic benefit to the Nisga'a Nation from obtaining tax room for its tax under a tax coordination agreement could be taken back as OSR. The Nisga'a government will have to consider the potential financial downside, including the possibility of being unable to collect the amount of tax revenues contemplated in the determination of its tax room or "tax capacity," before it decides to proceed. In these circumstances, the Nisga'a government may not be willing to enter the taxation field unless it is given sufficient incentive to do so through the OSR provisions of its financial arrangements with the two senior governments.

The taxation chapter provides the Nisga'a Nation and the four Nisga'a Villages with a limited exemption from real property tax and taxes on capital or wealth in respect of their interests in Nisga'a Lands on which there are no improvements or on which there is a "designated improvement." Generally speaking, "designated improvements" are improvements used for public purposes, such as public buildings, schools, public health facilities, and the like, or works of public convenience, such as public utilities works, water and sewer systems, public roads, bridges, etc. The definition also includes forest resources and roads; improvements used for the management, protection, or enhancement of a natural resource, other than an improvement used primarily in harvesting or processing a natural resource for profit; and residences of Nisga'a citizens. As noted, this exemption applies only to the interest of the Nisga'a Nation or a Nisga'a Village in the subject property and does not extend to the occupants of such property.

### *Nisga'a Nation Taxation Agreement*

The treaty required Canada, British Columbia, and the Nisga'a Nation to enter into the taxation agreement on the effective date. The taxation agreement does not form part of the treaty, nor does it constitute a separate land claims agreement or treaty. Its provisions, however, have been given effect under federal and British Columbia law.

The taxation agreement

- broadens the set of tax exemptions for Nisga'a governments and, in certain cases, their corporations;
- provides Nisga'a governments and their corporations with rebates, in prescribed circumstances, for federal goods and services tax and British Columbia social services tax and motor fuel tax paid by them in the course of their agreed-upon government activities;
- sets out the taxation rules applicable in relation to Nisga'a settlement trusts; and
- provides rules for the treatment of donations and gifts to the Nisga'a Nation.

The taxation agreement formalizes what, in many instances, has been administrative policy of the Canada Customs and Revenue Agency, by deeming each of the Nisga'a Nation and Nisga'a Villages to be

- a "public body performing a function of government" for purposes of paragraph 149(1)(c) of the Income Tax Act, and
- a municipality in Canada for purposes of paragraphs 149(1)(d.3) to (d.6) and subsections 149(1.1) to (1.3) of that Act.

Status as a "public body performing a function of government" will enable the Nisga'a Nation and the Nisga'a Villages to claim exemption from tax on their income under paragraph 149(1)(c) of the Income Tax Act. The rule deeming the government bodies to be municipalities for purposes of paragraph 149(1)(d.3) and

the other provisions referred to above gives their government-owned corporations the same status as municipal corporations. Such corporations will be exempt from tax under the Income Tax Act, for instance, if the Nisga'a Nation and/or one or more Nisga'a Villages directly owns at least 90 percent of the corporation's issued shares or if it is a wholly owned subsidiary of such a corporation. In addition, the company must derive no more than 10 percent of its income from activities carried on outside the geographic boundaries of its shareholders (that is, in the case of a shareholder that is a Nisga'a Village, its Village lands; in the case of the Nisga'a Nation, Nisga'a Lands).

The income tax exemptions will provide economic benefits to the Nisga'a Nation in the 12-year period during which the OSR provisions come into effect. Thereafter, the Nisga'a Nation's OSR in respect of commercial and investment activities, and, consequently, its contribution to government, will be equal to the tax that it, the Villages, and their corporations would otherwise have to pay if they were Canadian-controlled private corporations subject to tax under laws of general application.

A second, non-economic benefit accrues from having Nisga'a governments and corporations contribute to government through the OSR provisions, rather than through the payment of tax. Income taxes paid to senior governments by Nisga'a citizens and entities will be absorbed into the general revenues of those governments. That Nisga'a "indirect" contribution to the overall cost of government will not be directly taken into account in determining the senior governments' net contributions to cost of Nisga'a government programs and services. In contrast, the Nisga'a Nation's OSR contributions will be directly taken into account in determining the quantum of senior government funding and will be readily apparent to all. In that way, the income tax exemptions and related OSR contribution mechanism will at least allow the Nisga'a people to see directly the extent to which their community's own commercial endeavours contribute to the support of their own government.

The Nisga'a Nation, the Nisga'a Villages, and their eligible institutions and corporations will be entitled to recover federal goods and services tax (GST) and British Columbia social services tax and motor fuel tax paid by them in the performance of their government functions.<sup>32</sup> As previously noted, the Nisga'a Nation's current annual block funding is based on the annual costs incurred by the four Nisga'a bands in the 1997-98 fiscal year. Those 1997-98 costs were incurred when the bands were exempt from tax under section 87 of the Indian Act and thus reflected that tax-exempt status. When negotiating the current funding arrangement, the parties had to choose either to enhance the 1997-98 funding amounts to take into account the provincial and federal sales tax that will apply under the

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32 GST and provincial retail sales taxes paid by the school district and the Nisga'a Valley Health Board are subject to the normal rules.

new regime (the cost of which enhancements would be disproportionately borne by the federal government), or to allow the Nisga'a Nation to apply for a refund of the applicable tax when it was imposed. The parties adopted the latter alternative because it would be easier to reconcile and control.

The taxation agreement also sets out the rules for the taxation of a Nisga'a settlement trust. It provides that, in general, Nisga'a settlement trusts, interests therein, and income or capital distributed therefrom are not taxable<sup>33</sup> under laws of general application, subject to the following exceptions:

- Income or capital distributed to a Nisga'a citizen will be deemed for purposes of subsection 104(13) of the Income Tax Act to be income of the trust that was payable to the citizen; thus, subject to any remission order that might apply, it will be subject to income tax in the hands of the individual recipient in the year of distribution.

- Nisga'a settlement trusts are subject to the provisions of part XI<sup>34</sup> of the Income Tax Act, as if that part were stated to be specifically applicable to Nisga'a settlement trusts and were amended as required to take into account the investments permitted for Nisga'a settlement trusts.

- A Nisga'a settlement trust will be subject to tax under parts I and I.1 of the Income Tax Act and on any amount contributed to the trust that is not permitted under the terms of the trust and on any income it derives from a property, including any taxable capital gain from the disposition of that property, that is not a qualified investment for the trust or that is not acquired in the course of carrying on a permitted activity of the trust.

- GST or similar taxes may be imposed on goods or services consumed by the trustee.

- If a trust fails to comply with any of the terms of its qualification, and the minister of revenue consequently revokes the status of the trust, the trust will be required to recognize and pay tax under parts I and I.1 of the Income Tax Act on all unrealized taxable capital gains accrued in relation to its assets as of the time of revocation.

Finally, the taxation agreement provides that a donation made to the Nisga'a Nation or a Nisga'a Village will be accorded the same income tax treatment in the donor's hands as it would receive if it were a gift made to a registered charity. In addition, the Nisga'a Nation, or a Nisga'a non-profit organization, will be treated as a public authority or institution designated under section 32(2) of the

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33 Instead, the Nisga'a Nation must include an amount in its OSR in respect of income earned by a Nisga'a settlement trust, whether or not such income is distributed to the Nisga'a Nation or a Nisga'a Village, as described more particularly in the discussion above under the heading "Nisga'a Nation Own Source Revenue Agreement."

34 The rules dealing with acquisitions of non-qualifying property.

Cultural Property Export and Import Act.<sup>35</sup> This status will enable the Nisga'a Nation to accept donations of artifacts and other items of cultural property that qualify for the favourable tax treatment that is accorded to donors of "cultural gifts" under the Income Tax Act.

## SUMMARY

The Nisga'a entered into their treaty discussions with the intention "to negotiate their way into Canada." From their perspective, this meant having access to the same education, health, and social safety net that is available to their fellow Canadians who reside in northwest British Columbia. It also meant having to contribute to the costs of these programs, through taxation and the OSR provisions of their fiscal financing arrangements, on the same basis and to the same extent as their fellow northwestern British Columbians.

Under the terms of their treaty and related agreements, the Nisga'a Nation will be responsible for ensuring the delivery of agreed-upon programs and services to Nisga'a citizens, at levels that are reasonably comparable to those generally prevailing in northwest British Columbia. Funding for these programs and services will be provided by Nisga'a citizens through the taxation of those citizens by Canada and British Columbia, by the Nisga'a Nation itself through contributions of its OSR, and—to the extent that the agreed-upon funding for the defined programs and services exceeds the Nisga'a Nation's OSR—by Canada and British Columbia.

The Nisga'a Nation's OSR will be calculated in a manner that results in an amount approximately equal to the tax revenues that would be raised by Canada and British Columbia if those governments subjected all activities on Nisga'a Lands to tax. In effect, the Nisga'a Nation's OSR is a surrogate for tax and is consistent with the Nisga'a philosophy of contributing to Canada on the same basis and to the same extent as their fellow Canadians.

The Nisga'a treaty gives the Nisga'a Nation the power to tax Nisga'a citizens on Nisga'a Lands. This taxation power is concurrent with Canada's and British Columbia's own powers to tax those same citizens. The treaty also anticipates the possibility that Canada and/or British Columbia may enter into one or more tax coordination agreements with the Nisga'a Nation providing the Nisga'a Nation with delegated authority to tax persons other than Nisga'a citizens on Nisga'a Lands. At present, it is unclear if there is any incentive for the Nisga'a Nation to seek such delegated authority, either now or within the foreseeable future.

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35 RSC 1985, c. C-51, as amended. This designation requires that the Nisga'a Nation or a not-for-profit organization established by the Nisga'a Nation has, or has use of, a facility meeting prescribed conditions relating to the storage and display of cultural artifacts.