

# Taxation Considerations in Structuring Real Estate Transactions on First Nations Land

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# Overview

- Overview of tax exemptions
- Types of taxes to be considered
- Conflict between security and taxation issues

# Overview (cont.)

- Structures to consider
- Planning techniques
- Hybrid structures

# Overview of tax exemptions

- Section 87 of the Indian Act
  - Available to Indians and Bands if income arises from an on-reserve source
  - Available in respect of income allocated from "flow-through" entities
  - N/A to corporations, trusts, etc.

# Overview of tax exemptions (cont.)

- Cannot be shared
- All facets of management, control and day to day operations should occur on reserve
- 149(1)(c) of the Income Tax Act ("ITA")
  - Public body performing a function of government in Canada
  - Need to assess the status of the First Nation

# Overview of tax exemptions (cont.)

- Exemption applies to all income and not just income earned on reserve
- Only available to Bands
- 149(1)(d.5) of the ITA
  - Only available to those Bands who qualify as Canadian municipalities for Income Tax purposes

# Overview of tax exemptions (cont.)

- Not all Bands qualify
- Only available in respect of corporations that do not earn more than 10% of income outside of geographical boundaries (taken to mean "reserve" for Bands)

# Overview of tax exemptions (cont.)

- Exemption may be uncertain and at risk due to Tawich case
- May be difficult to argue for other First Nations
- 149(1)(1) of the ITA
  - Based on the Gull Bay case
  - non-profit organizations only

# Overview of tax exemptions (cont.)

- Cannot distribute profits to members or shareholders
- Profit cannot be the main objective
- If the purpose is to create a normal business then this exemption should not be considered
- Exemption restrictive in how the corporation must behave

# Types of Taxes

- Income tax

- GST

- Can represent a real cost in respect of residential real estate
- Self-supply rules cause GST to be assessed on leased land

## Types of taxes (cont.)

- If contractor is other than an Indian or band, then contractor liable for GST on the FMV of the building and leased land
- If development on reserve, then an the self-assessment may result in no GST to a Band

## Types of taxes (cont.)

- Provides possible competitive advantage for pricing
- However, new home rebate lost with respect to value of building
- Exemption from self-assessment not available to corporations

# Types of taxes (cont.)

- Social Services Tax ("PST")
  - Builder/contractor is consumer
  - Thus PST may apply to building supplies, even if project is on reserve, or even if building materials are delivered on reserve

## Types of taxes (cont.)

- If band takes delivery on reserve and either a separate contract for building supplies or if building supplies separately identified and billed for
  - PST may not apply
  - Where materials used may not be relevant

# Security and Taxation Conflicts

- Off reserve developments can be secured (even if owned by a band)
- On reserve developments can only be secured via a designation or other leasehold interest

# Planning Techniques

- Band acts as contractor
  - If materials purchased on reserve, then no PST
  - No GST applies if delivery occurs on reserve
  - Potentially no GST on self-supply rules (if on-reserve)

# Planning techniques (cont.)

- If development off reserve, then Band should be contractor
  - PST and GST may not apply if materials purchased on reserve
  - No exemption from GST self-supply rules, however
  - Band may still be exempt from income tax if subject to 149(1)(c) of the ITA

# Structures to consider

- Unincorporated structures preferable
- Limited partnerships may afford flow-through mechanisms while possibly covering off security matters

# Conflicts (cont.)

- Issuers of leases and lessees will prefer corporate lease holders in order to issue security interests
- First Nations will prefer unincorporated structure

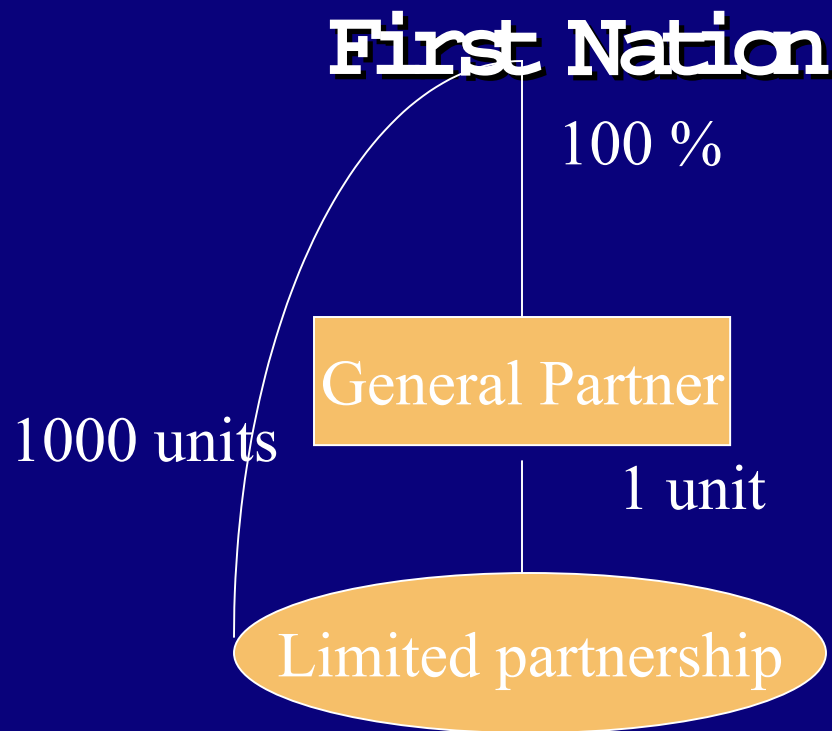
# Types of taxes(cont.)

- Fuel tax
- Property Purchase Tax
- Property taxes
- Municipal levies
- Whether or not taxes apply can severely impact pricing of development

# Hybrid Structure for on-reserve development

- Use limited partnership ("LP") with general partner holding head lease
- LP is contractor and pays fee to developer
- LLP purchases all materials and services on reserve
- GP issues mortgages of lease on behalf of LP

# Hybrid Structure (cont.)



# Hybrid Structure

## (cont.)

- GP holds 1 unit while band holds 1000 units
- 1000/1001 of income may potentially be exempt from income tax
- GST may not apply as a consequence of TIB B-039R as one of the partners would be a band

# Hybrid Structure (cont.)

- 1/1001 of PST may apply on account of Seven Mile Dam decision and on account of Consumer Taxation Branch's administrative position
- Legal advice critical

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