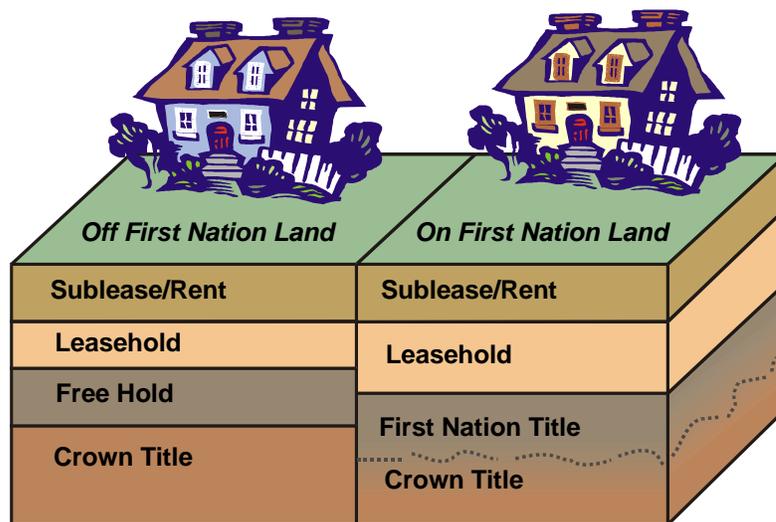


Expanding the First Nation Property Tax Base

Context

This paper is a successor to *Expanding Commercial Activity on First Nation Land* and *Turning on the Taps*. It will focus on the role of the lease document, in the context of the larger land administration system, in facilitating economic development on reserve. Clear, concise, and equitable lease documents can help reduce the cost of doing business on reserve, thereby stimulating economic development and increasing the First Nation property tax base. Furthermore, the Glass decision, which held that that land interests in the Musqueam reserve are worth 50% of comparable fee simple lands off reserve, has important implications for the ITAB, since First Nation Taxation Authorities could potentially lose 50% of the value of their property tax base. This paper will examine how the use of good lease documents can increase property values on reserve and reduce the gap between on reserve and off reserve assessed values.



Policy Environment

Other aspects of the policy environment surrounding the First Nation land leasing issues that have been addressed, in addition to Glass, include the Indian Act; Bill C-115, which established First Nation property tax jurisdiction and provides additional motivation for First Nations to have good leasing practices; Bill C-49, the First Nation Land Management Act, which is another means by which individual Nations can increase their control and the certainty over their own lands; and Delgamuukw; which helps to clarify what aboriginal title means.

The International Experience

First Nations in Canada are not the only jurisdictions struggling to implement an efficient, effective, and equitable leasehold system. Other jurisdictions around the world, such as England, Hawaii, Belize, and Hong Kong all have leasehold systems, which are operating with varying degrees of success. Among other things, these cases show large rent increases in other jurisdictions, leading us to conclude that the Musqueam issue is not necessarily a First Nation issue but rather a lease issue. There are three main lessons to be learned from the international case studies: the importance of appropriate methods of lease renewal and extension, the need for an effective and efficient land

| Leasehold Rent Increases | |
|--------------------------|----------------|
| Hawaii (1990s) | 1000% to 2285% |
| California (1970s) | 3233% |
| Musqueam (2000) | 4800% |

market, and the need for appropriate lease documents. Although none of these systems are perfect, these international examples demonstrate that a leasehold system of land tenure is feasible, and provide examples, both positive and negative for First Nations in Canada to learn from.

Leases, Property Rights, and Economic Development

Capital is necessary for economic development, yet all assets are not capital. Capital is assets that can be used to generate revenue. For example, a house is an asset, but a house that can be mortgaged is capital. The mechanism for converting assets into capital is the property rights system. Similarly, a hydro-electric dam can be used to generate power from a lake. Not only is the water still there, but there is also an additional benefit being produced. For First Nations, that additional benefit would be increased economic development. The turbines in the dam each represent a component of the property rights system. If all of the turbines are not functioning effectively and efficiently, maximum benefit will not be produced. First Nations have limited ability to convert their assets into capital due in part to an unclear and immobile system of property rights. Leases can be used to clarify property rights. Investors must have both motivation and ability to create economic development on First Nation lands. The complexity, higher costs, uncertainty, and negative image associated with reserve lands are stifling investor motivation, and the extended time it takes to do business and lack of infrastructure are reducing the ability of those who wish to invest in First Nation lands to do so.

The Role of an Effective Property System in Converting First Nation Land Assets to Capital & Economic Development



Valuation

Property assessment methods that are currently used across Canada have also been explored. There are three main methods for valuing fee simple property: the direct comparison approach, the cost approach, and the income approach. The Glass decision that reserve property should be valued as fee simple property in the particular reserve has created implementation issues. Fee simple First Nation land is an imaginary construct, and few, if any, reserves have enough leasehold sales to produce reliable comparison data. So in terms of valuation it appears that there are more questions than answers at the moment. Market valuations cannot be abandoned, as would be the case if the terms of the lease were simply modified to stipulate off reserve comparisons, yet valuing the sum of the leasehold and remaining aboriginal interests is difficult if not impossible. Could the uncertainties

associated with First Nation leases be reduced through provisions such as mandatory renewal, so that First Nation leases more closely resemble freehold interests? The value of these leases could then be a proxy for the freehold interest, if there is a relatively long term remaining on the lease. Estimating the remaining aboriginal interest may prove too difficult to be feasible. What other alternatives exist? These options will continue to be explored.

First Nation Experience

An examination of different types of First Nation leases currently in place across Canada has shown that First Nations are needing to include provisions in their leases to provide increased certainty and comfort to leaseholders. Examples of these provisions include the following:

- a guarantee by the Band to remove any roadblocks that occur;
- comfort provisions to ensure that property taxes raised against the leased property are the same as for other properties of the same property class in the reserve, as well as being similar to the property tax rates in the adjacent municipality;
- a comfort provision to the effect that if the property taxes imposed by the Band exceed the property taxes imposed in the neighboring municipality by more than 5%, the excess amount will be deducted from the land rent owing
- comfort provisions regarding future Band laws, in that if there is a future conflict between Band laws and the development agreement associated with the lease, the development agreement will prevail
- a preferential employment clause to modify the tenant's hiring policy to facilitate the preferential hiring of Band members, to notify the Band employment officer of vacant positions, and to interview all Band members that apply for such positions.
- The need for separate development cost-sharing agreements due to a lack of established DCC policy

These provisions are not necessary in off-reserve leases, because off reserve leaseholders are familiar with the municipal system of governance. Also, image problems associated with individual First Nation governments are generalized to all First Nations in the minds of leaseholders and potential leaseholders.

Lessons for DIAND Policy

First Nations and DIAND have much to gain by making the First Nation leasing process as easy as possible, by structuring lease documents to provide leaseholders with as much certainty as possible, and by ensuring leases are as financeable as possible. Previous research has shown that



it takes experienced developers much longer to plan and develop a business on First Nation land than in neighboring jurisdictions. This is a barrier to economic development on First Nation land. If First Nations and DIAND have access to model leases that are appropriate for the proposed type of development, they should be used, along with other methods to ensure that leases are concluded relatively quickly. Certainty can be increased by minimizing the number of references to Ministerial consent and notification, through the inclusion of comfort clauses, and through the inclusion of renewal provisions. While the Minister does have a fiduciary obligation to the First Nation, he probably would not care to be notified every time a golf course applied fungicide, as would be the case if the wording of a particular lease was taken literally. Comfort clauses are there to reassure the leaseholder that the First Nation government will not abuse its powers. Care should also be taken to ensure that leases are as financeable as possible. The majority of both homeowners and business investors require bank financing. Increasing the amount certainty provided to leaseholders, as well as other lender-specific provisions, will expand the market for First Nation leases. However, effective lease documents are only one part of a land administration system. All parts of that system need to be functioning effectively and efficiently in order to remedy the relative lack of economic development on First Nation land.

Next Steps

The final report will consist of two components: a brief policy paper, consisting of approximately 25 pages, and an accompanying reference binder.

The policy paper will include sections on the First Nation context, the importance of a good lease and leasehold system for economic development, the policy environment, lessons from experience/Best Practices, and Getting There from Here which includes recommendations.

The reference binder will include sections on the key elements of a lease, special First Nations provisions, case studies of international leasehold systems, case studies of First Nation lease documents, the role of DIAND in the leasing process, methods of valuing leasehold property, the difference between freehold and leasehold property interests, the difference between on reserve and off reserve land tenure, the difference between a recording system and a Torrens system land registry, and the possible uses of title insurance.

This study addresses the lease document and suggests some ways in which it can be structured or drafted to provide certainty to investors and increase the value of First Nation land. The lease is just one part of a land tenure system. In order to further increase certainty to investors other components of the land tenure system may need to be addressed.