

Tax Administration Agreements with Aboriginal Governments: Federal Approach

Presented to Dehcho First Nations
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**Finance Canada
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- This presentation will discuss Canada's approach to implementing taxation by Aboriginal governments
 - Federal interests
 - Scope of Aboriginal gov'ts' taxes
 - How existing tax administration arrangements operate:
 - GST
 - Personal Income Tax

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Federal Interests: Taxation by Aboriginal Governments

- Greater self-reliance for Aboriginal governments, through raising their own tax revenues
- Promote good governance and political accountability between an Aboriginal government and its citizens
- Protect Parliament's tax powers
- Safeguard the fairness, integrity, efficiency and neutrality of the Canadian tax system
- Protect interests of non-member taxpayers

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Scope of Self-Governing First Nation Tax Powers

- Direct tax powers over citizens within the FN's settlement lands and, in some cases, within communities outside the FN's settlement lands
- FN tax jurisdiction concurrent with federal and provincial tax powers - not exclusive
- Can extend FN taxes to other persons (non-members) through separate agreements
- Canada willing to coordinate federal tax with FN tax (e.g., vacate tax room in favour of FN tax)
 - Prevents potential double taxation
- Canada can administer harmonized taxes for FN
 - no charge to FN; CRA acts as agent of FN
- FN tax must apply to FN's own members

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FN Tax Powers -- Communities Outside Settlement Lands

- Direct tax powers over citizens within communities outside a FN's settlement Lands where:
 - All or substantially all of the FN's "people jurisdictions" under the Final Agreement can be exercised in those communities (i.e., the tax jurisdiction is one of many jurisdictions that can be exercised in those communities)
 - A majority of the seats in the community government are reserved for FN citizens

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Tax Administration Agreements (TAAs)

- Negotiated gov't-to-gov't contracts
- Set terms and conditions for administration and sharing of tax room
- FN tax fully harmonized with federal tax
- Agreements outside of Treaty
- Since 1997, Canada and various Aboriginal Governments have concluded over 40 TAAs:
 - FNGST: full GST base
 - FNPIT - Personal Income Tax (individuals)
 - FNST – 3-Product Tax (older approach)

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TAA's -- Communities Outside Settlement Lands

- Where a FN has a direct tax power over citizens within a community outside its settlement lands:
 - TAA could provide for the FN tax to apply to FN citizens in the community
 - TAA could also provide for the FN tax to apply to other persons in the community if FN citizens make up the majority of residents in the community

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First Nations Goods and Services Tax - FNGST

- FNGST now in place with 22 FNs
- Available to and under negotiation with *Indian Act* bands and self-governing Aboriginal governments
- 5% tax on consumption on FN lands
- Canada vacates equivalent GST room
- Imposed under FN's law – FN's decision
 - Framework legislation: *First Nations GST Act*

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FNGST Features

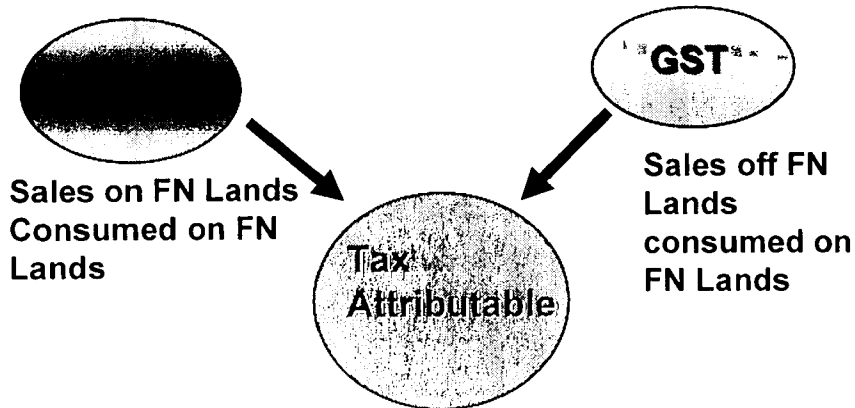
- FNGST applies to full GST base on FN lands
- Payable by all FN citizens & others on FN settlement lands and within qualifying FN communities
- Federal GST not payable where FNGST applies
- Administered by Canada Revenue Agency (CRA)
- No cost or charge to FN gov't
- Operates seamlessly with GST - mirrors GST:
 - Same rules, rate, base, forms, credits
 - No additional compliance burden for businesses & consumers
 - *Cost-effective & efficient revenue generation* ⁹

First Nation Revenues

- Revenue of participating First Nation based on tax attributable to consumption of goods and services on FN's lands, as estimated by formula
 - **Not based on actual sales on FN lands**
 - **Avoids cost & complexity of tracking individual sales**
- Consumption approach allows rural, remote FNs with few stores or businesses to benefit fully
- Revenues paid monthly by Canada to FN, subject to audit and adjustment

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Tax Attributable to First Nation Lands



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Revenue Estimation Formulas (SRM/DRM)

Simplified Revenue Estimation Method:

- SRM suitable for rural and remote FNs
- Where consumption on FN lands mainly attributable to residents of FN lands

Detailed Revenue Estimation Method:

- DRM suitable for urban FNs with flow-through commerce, shopping malls, hotels, resorts, casinos, public golf courses, etc.
- Where significant consumption on FN lands attributable to non-residents of FN lands (e.g., tourists, visitors)

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FNGST – Simplified Revenue Estimation Method (SRM)

Under SRM, tax attributable to FN =

Average net GST paid per capita in
Province/Territory by population aged 15+
years (c.\$1000)

X

Number of residents (FN citizens and non-
citizens) aged 15+ years on First Nation's
lands

X

Relative income factor

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SRM Example

Assume:

- Average Net GST per Capita = \$1000
- Population aged 15+ on FN lands = 500
- Relative incomes on FN lands = 70% of provincial average, per best statistical data

\$1000 X 500 X 70% =
\$350,000 FNGST revenues

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Detailed Revenue Estimation Method (DRM)

- Requires detailed consideration of First Nation's circumstances, demographic & economic profile
- DRM begins with SRM: consumption by residents of First Nation's lands
- Where relevant, DRM adds in immediate consumption on FN Lands by non-residents
- DRM may also adjust for:
 - Exempt supplies (health, financial)
 - Housing base
 - Sector-specific factors
- Uses data from tax filers and StatsCan

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Limits on GST Sharing: Revenue-Sharing Mechanism

- Canada foregoes GST where FNGST applies
- Need limits on sharing in some circumstances
- Purpose: limit unreasonable sharing and revenue loss where consumption on FN's lands largely attributable to non-FN members
- Not intended to affect revenues from tax attributable to consumption by First Nation citizens/members w/n FN lands: FN keeps 100%
- But limits could apply where large numbers of non-member residents or if commercial/retail draws transient, non-resident consumers
- Most FNs will not be affected by RSM

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Overview of FNGST Revenue Sharing Mechanism (RSM)

3-Zoned Revenue Sharing Mechanism:

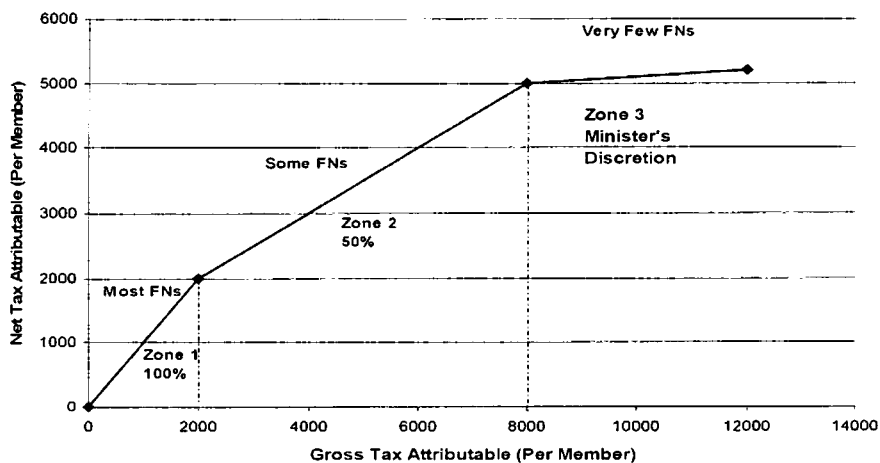
Zone 1: FN receives 100% of revenue attributable to consumption on FN lands, up to 2 times the net GST per capita (c.\$2000) times the number of FN member-residents of all ages

Zone 2: For revenue above Zone 1, 50/50 sharing between FN & Canada, up to 8 times the net GST per capita (c.\$8000) times the number of FN member-residents of all ages

Zone 3: For revenue above Zone 2, most, but not all, revenue to Canada – 5% to FN or Minister's discretion (i.e., 95% to Canada, 5% to FN)

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GST RSM Structure



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Personal Income Tax: First Nation PIT Arrangements

- Canada has concluded TAAs in respect of Personal Income Taxes:
 - Since 1999 with self-governing Yukon First Nations (YFNs) – now 10 TAAs
 - 2005: PIT TAA with Tlicho First Nation
 - 2006: PIT TAA with Labrador Inuit
- Willing to negotiate PIT TAAs with other self-governing First Nations, to give effect to their direct tax powers within their lands

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FN PIT -Tax Impact

- TAAs enable FNs to impose a PIT on all individuals (FN Citizens and others) resident on FN settlement lands and within qualifying FN communities
- Canada vacates its PIT tax room in favour of FN PIT
- Individuals on and off FN lands, in equivalent circumstances, pay the same amount of tax
 - Off FN's Lands, Canada occupies all of its PIT room
 - On FN's Lands, FN PIT applies – and Canada vacates equivalent amount of tax room so that tax burden is the same as off-FN's Lands

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FN PIT – General Approach

- Canada proposes to vacate 95% of its PIT tax room in favour of participating FN's PIT
- Canada will retain minimum 5% of tax room
- TAAs also include mechanism to limit revenue-sharing in some circumstances
 - Revenue-sharing mechanism discussed below
- Payments: Canada pays monthly instalments to FN based on estimates
- Audited annual reconciliation of payments based on actual tax return data

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Mechanics of FN PIT

- FN PIT taxpayers use the same CRA tax form as all other residents of Province or Territory
- Taxpayers self-identify on T1 as residents of a particular FN's Lands at year-end
- Federal *Income Tax Act* rules, rates, credits & deductions apply
- Simple calculation (by taxpayer or CRA) of FN tax as % of federal PIT otherwise payable
- Credit for FNPIT payable against federal PIT
- Same "bottom line" tax payable as for residents outside FN's Lands

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Limits on PIT Sharing: Revenue-Sharing Mechanism

- Similar approach & rationale as for FNGST RSM
- Limits on tax sharing in certain circumstances
- Especially, where significant % of PIT revenues from all residents of FN's land would be derived from non-members of the First Nation
- Avoids unreasonable sharing and contains Canada's costs (foregone tax revenues)
- Reflects respective service responsibilities of governments
- Most FNs will not be affected by FNPIT RSM

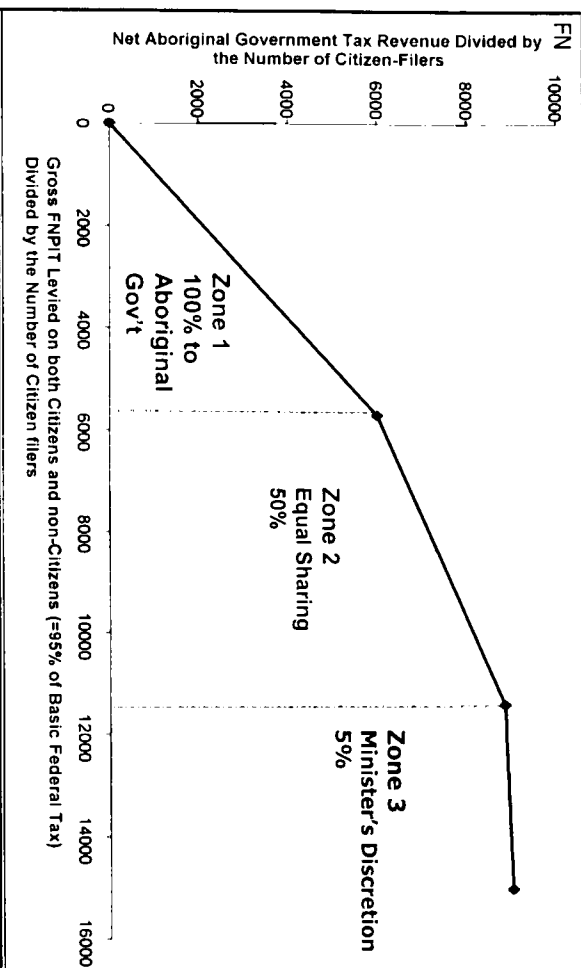
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How FNPIT RSM Works:

- **Starting Point (A):** FNPIT = 95% of federal PIT o/w payable by all residents of First Nation's lands, subject to the following 3-Zoned RSM:
- **Zone 1:** FN receives 100% of (A), up to the number of FN citizens who are tax filers, times 1.5 times the average PIT paid per Canadian (c.\$4200 X 1.5 = \$6300 X 95%)
- **Zone 2:** FN receives 50% of (A) above Zone 1, if any, up to the number of FN citizens who are tax filers times 3 times the average PIT paid per Canadian (c.\$4200 X 3 = \$12,600 X 95%)
- **Zone 3:** FN receives 5% (or % at Minister's discretion) of (A), if any, above Zone 2

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FNPIT RSM Structure



Benefits of Harmonized, Coordinated Approach

- FNPIT & FNGST TAAs illustrate advantages of:
 - tax coordination (vacating of tax room)
 - harmonization (using the same rules, rates and base as federal taxes, and sharing administration)
- Harmonized, coordinated FN taxes promote:
 - Simple, stable, cost-effective FN revenue source
 - Economic neutrality – level-playing field
 - Easier compliance by individuals and employers
 - Simplified administration by CRA – free of charge to FN

Conclusion

- These TAAs (FNGST, FNPIT) are clear expressions of the federal interest in:
 - Facilitating revenue generation by Aboriginal governments through the exercise of tax powers in an effective, efficient way
 - Workable taxation arrangements with interested Aboriginal Governments
 - Enabling Aboriginal governments, if they so choose, to benefit as partners in the national tax system