



# Taxation of Aboriginal Business and Investment Income

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# Agenda

- Tax-exempt status
- Business income
- Starting a business off-reserve
- Investment income



# How is income tax-exempt?

- Based on s. 87 of the Indian Act
  - personal property of an Indian **situated on a reserve** *is* exempt from taxation
  - Reserve includes designated land, but not traditional territory or claimed land
- Also must be “Indian” per s. 2 of Indian Act
  - means a person who is registered as an Indian, **or entitled to be registered as an Indian**



- While s. 2 of Indian Act includes person who is entitled to be registered as an Indian, CRA requires evidence of that
- Governed by s. 6 & 7 of Indian Act
  - <http://laws-lois.justice.gc.ca/eng/acts/i-5/page-3.html#h-6>
- Up to the individual to show evidence satisfactory to CRA – otherwise exemption denied for Non-Status person





# Section 87 of the Indian Act

- The personal property can be tangible or intangible *and* must be on a reserve
- Exemption applies to Indians and Bands as defined under the Indian Act
- Corporations not eligible
- Metis and non-status Indians could now also be considered exempt (Supreme Court of Canada – Daniels case)



# Business Income

What determines whether it is exempt or not?



# Business Income – Individual

- Until recently, business income was taxed based on “connecting factors”, as developed from Southwind case (FCA)
- Recent cases have modified that
- Recent Dickie case in July 2012 was decided in favor of taxpayer
  - looked at location of mind and management of the business, not where the work was done
- Federal Court of Canada agreed, said income was earned on reserve, and exempt from tax
- Other prior cases (Ballantyne, Roberson) also considered income as exempt



# Business Income – Individual

Still need to consider connecting factors to connect income to a reserve, such as:

- The location of the business activities
- Where the management decisions are made
- Type of business and nature of the work
- Residence of the business owner
- location of business and of books and records

Likely will still be a contentious area

For reporting purposes, if business income exempt, it is simply not reported – but must have basis to not report, otherwise penalties could be assessed!





# Business Income – Individual

- If business income set up by individual through a corporation, corporate income taxes are payable
- Reasonable salary could be received, and potentially be exempt.
  - While salary of any amount can be paid to owner-managers, and usually accepted by CRA, does not extend to salaries where the salary would be exempt



# Business Income - Individual

- Could pay corporate tax at 15% and distribute earnings via dividend if income not reasonable
  - *If you are a shareholder of a corporation that operates only on a reserve, any dividends you receive from the corporation will be eligible for the tax exemption under section 87 of the Indian Act. This applies when the head office, management, and **principal income-generating activities** of the corporation that pays your dividends are situated on a reserve*
- Corporations also offer a level of asset protection



# Business Income – Individual

- Activities performed in both places?
- Exemption may be prorated if activities are performed both on and off-reserve (examples: electrician, plumber etc.)
- Maintain proper documentation to indicate location of customers
- Other connecting factors still need to be considered



# Dickie v. The Queen 2012 TCC

- Sole proprietor operating on reserve
  - Clearing and slashing timber
  - Almost all slashing work performed off of the reserve
  - Administrative centre was on reserve
    - Recruited workers from that office
    - Orientation and safety meetings
    - Negotiated contracts
    - Completed tenders



# Dickie v. The Queen 2012 TCC

- Court held need to analyze all components of the business
  - Performed contractual obligations from a labour perspective off reserve because that is where the work was
  - This by itself is not determinative of where the location of business income was located





# Dickie v. The Queen 2012 TCC

- Court found –
  - Managerial activities were more than incidental to the business
  - Bid process required great deal of effort, this was all carried out on reserve
  - Commercial mainstream is irrelevant
  - Court ruled income was exempt



# Starting a business off-reserve



# Business structures

- Proprietorship
- Partnership
- Corporation
- Trust



# How are they taxed?

- Proprietorship
  - Individual is taxed and is subject to the marginal personal tax rates
- Partnership
  - Income of the partnership is allocated to the partners and then taxed at the partners level (partnership interest could be in held in a corporation or at the individual level)



# How are they taxed? (cont'd)

- Corporations
  - Taxed at the corporate level (income under \$500,000 taxed at 15%, over at 26.5%)
  - Individual taxed when funds removed from the corporation (salary, dividends)
- Trust
  - Taxed as an individual at the highest marginal tax rate –income can be allocated to beneficiaries and then taxed at their level





# Which to choose?

- Considerations:
  - Type of business
  - Level of risk
  - Income-splitting
  - Profitability
  - Asset protection



# Other selected issues

- GST/HST
- Payroll taxes
- WSIB
- Record keeping
- Due dates



So you have accumulated some wealth from your business activities and you now want to invest it – how is investment income taxed?



# Taxation of Investment Income

- Exemption from taxation starts off with Section 87 of the Indian Act.
- That provision states that the personal property of an Aboriginal or a band situated on a reserve is exempt from taxation.
- So what does that mean for investment income?



# Taxation of Investment Income

- Let's first look at this for an individual.
- Historically, CRA said investment income earned by status Indian was taxable, unless earned from on reserve activities
- Looked at the underlying connecting factors to determine if the income was connected to reserve





# Taxation of Investment Income

- Various “connecting factors” taken into consideration, such as:
  - the residence of the taxpayer;
  - the origin or location of the capital used to buy the securities;
  - the location of the bank branch where the securities were bought;
  - the location where the investment income is used;



# Taxation of Investment Income

- the location of the investment instruments;
- the location where the investment income payment is made; and
- the nature of the securities and in particular:
  - the residence of the issuer;
  - the location of the issuer's income generating activity from which the investment is made; and
- the location of the issuer's property in event of default.



# Taxation of Investment Income

- Where there was a connection to off-reserve income source, CRA's position was that investment income earned off-reserve, and taxable
- Their position was that all of the income had to be earned from on-reserve sources, for exemption to apply
- That position challenged by the cases of Bastien & Dube



# Taxation of Investment Income

## Estate of Roland Bastien:

- Roland was member of Huron-Wendat Nation, lived on reserve, died in 2003
- held term deposits at local Caisse populaire, located on reserve, received interest of \$64, 417 in 2001.
- Cash for the term deposits came from his business income on reserve, and from sale of the business
- CRA assessed this as taxable income, on basis that the Caisse populaire used the funds for investments off-reserve
- Roland appealed to Tax Court of Canada



# Taxation of Investment Income

## Estate of Rolland Bastien (cont'd):

- Roland appealed to Tax Court of Canada, was not successful
- Appealed further to Federal Court of Appeal, also not successful
- In both appeals, courts gave significant weight to the “commercial mainstream” nature of income source (i.e., where the Caisse populaire used the funds)
- Appealed to the Supreme Court of Canada. Decision delivered in 2011, and taxes were reversed.





# Taxation of Investment Income

## Estate of Rolland Bastien (cont'd):

- In its decision, the SCC looked at the location of Roland's interest income, and not the Caisse populaire's use of the funds.
- Held that the investment was on reserve, and therefore the related interest income was earned on reserve and exempt from tax

Dube case was similar, with slightly different facts, but reached the same decision by the SCC in 2011.



# Taxation of Investment Income

So what does that mean for investment income earned by an individual now?

- Connecting factors will still be important, have to consider if the “property” is on or off reserve
- The SCC stated that “connections that are artificial or abusive should not be given weight” – so earning interest income off reserve, but structured as if it was earned on reserve, will likely be challenged
  - e.g., lending funds with interest to a company on reserve, which in turn invests off reserve – is that subject to challenge?



# Taxation of Investment Income

If structure is legitimately on reserve, can arguably be exempt from income tax

- e.g., setting up a company on reserve for business and liability reasons – are dividends paid by the company to an individual resident on reserve exempt from tax?

The decisions in Bastien and Dube likely have made some investment income exempt from tax, but also may result in more challenges by CRA, especially if considered abusive



*Thank you.*  
Questions?



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