HUU-AY-AHT FIRST NATIONS
Economic Development Structuring

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June 14, 2012
Port Alberni, BC

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Agenda

- Introduction
- Liability Protection
- Avoiding Tax
- Own Source Revenue
- Corporate Structure
- Business and Politics
- Governance Model 1 and 2
- Recommendations

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Introduction

Why we're here…

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Introduction

- Governments getting out of business
- Except aboriginal governments
- Considerations
  - Reduce liability
  - Maximize profits
    - Minimizing taxes
    - Avoid OSR claw backs
  - Separate politics from business

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Introduction

- How best should First Nations structure their economic development?
- Two components for economic development structuring for First Nations
  - Corporate Structure
  - Governance Structure
- Considerations determine corporate and governance structure

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Liability Protection

How we reduce the risk…

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Liability Protection

- Carry out economic development through a separate legal entity
- Corporations provide the best liability protection for economic development
- Creates limited liability protection
  - Shareholders only liable for what they have
    - invested in the company
    - loaned to the company

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Liability Protection

- The ability to isolate liability in the corporation is its primary advantage for First Nations economic development
- Disadvantages of a corporation
  - Corporations are taxable
  - Corporations separate from Treaty Nation
  - Loss of tax advantage
- Profits not maximized because of taxes

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Liability Protection

- Loss of liability protection – "piercing the corporate veil"
- Not using proper legal name
  - Distinctive element
  - Descriptive element
  - Corporate designation
  - Limited partnership for LPs
- Confusion over who is doing business

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Avoiding Tax

How we don't lose the tax advantage…

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Avoiding Tax

- Maximize profits by minimizing taxes
  - Huu-ay-aht tax exemption ITA s.149(1)(c)
  - "Public body performing the function of government"
  - Subsidiaries for business on treaty lands
    - ITA s.149(1)(d.5)
    - 90% owned 90% income from on treaty lands
- Not for multiple owners or off of treaty lands

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Avoiding Tax

- Using corporations off of treaty lands
  - Provides limited liability protection
  - Does not provide tax advantage
- Other structure required
- Limited partnerships can be utilized to avoid or reduce tax and maintain tax advantage

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Own Source Revenue

Why we avoid it…

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Own Source Revenue

- OSR is a mechanism for Canada to reduce its funding contribution as a First Nation develops its own sources of revenue
- Intended to emulate provincial transfer payments from Canada
- OSR Agreement
  - 5 year exemption; +3.3%/year; maximum 50%
- Claw back time lag (claw back for year 6 calculated year 7 deducted year 8)

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Own Source Revenue

- OSR rate is applied to defined own source revenues to determine annual claw back amount
- Variable base amount exempted from OSR calculation
- Own source revenue subject to claw back
  - Property taxes, fees and other listed revenue
  - Income from “business and property”

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Own Source Revenue

- Business and property income
  - Income from businesses owned directly by Huu-ay-aht (not through a corporation, trust or partnership)
  - Dividends received from a corporation (regardless of percentage of ownership or location where corporate income earned)
  - Distributions from a trust or partnership (excluding return of capital)
  - Capital gains on the disposition of capital property owned directly by Huu-ay-aht and used for commercial purposes

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Own Source Revenue

OSR Revenue	$500,000
Basic Exemption	- $124,000 +/-
Net OSR Revenue	$376,000
Inclusion Rate (y10)	X 16.5%
Claw back	**$ 62,040**

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Own Source Revenue

- Dividends/distributions not subject to OSR until actually paid
- Unpaid dividends/distributions never subject to OSR under current arrangements
- Possibility of change in the treatment of business and property income in future arrangements

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Own Source Revenue

- Direct ownership of commercial enterprises should be discouraged
- Percentage of ownership and location where income earned not relevant to OSR (unlike ITA 149(1)(d.5) & (d.6))
- Anti-avoidance provision prevents using business and property funds for Public Services without flowing through Huu-ay-aht government

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Corporate Structure

How we achieved the results…

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Corporate Structure

- Partnership: relationship between two or more legal entities
- Governed by the Partnership Act and partnership agreement
- Limited partnership must have one general partner and one or more limited partners
- General partner: assets and liability
- Limited partner: liability protection

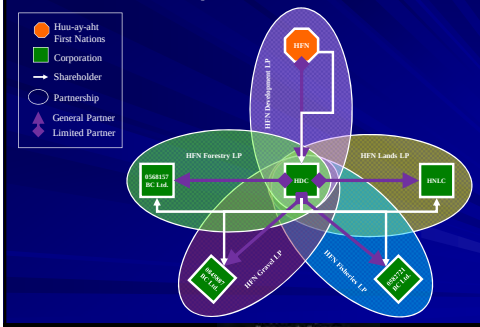
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Corporate Structure

- HFN Development LP
  - HFN as limited partner and HDC general partner
- Operating LPs
  - Forestry LP, Gravel LP, Fisheries LP, Lands LP
  - HFN Development LP as limited partner and corporate general partner for each Operating LP
- Each active business conducted through its own Operating LP
  - Isolates failed business and protects successful businesses

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Corporate Structure

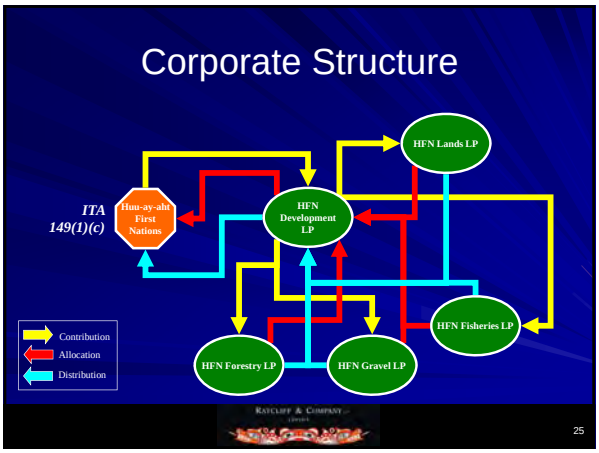


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Corporate Structure

- Allocation of 99.99% of profit to limited partner for tax purposes
- Distribution does not affect allocation
- Profit
  - Retained for expansion of current business
  - Retained for investment in new opportunity
  - Distributed

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Corporate Structure
ITA 149(1)(c)
Huu-ay-aht First Nations
HFN Development LP
HFN Lands LP
HFN Fisheries LP
HFN Forestry LP
HFN Gravel LP
Contribution
Allocation
Distribution
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Business and Politics
Why we think they don't mix…
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Business and Politics
Harvard Project – leading research on successful aboriginal businesses
– Two decades, hundreds of research projects
Keys to economic development success
– Sovereignty: asserted right to self-government
– Capable, ethical and determined leaders
– Integrated culture and traditions into institutions
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Business and Politics

- Strong institutions
  - Laws and policies that are clear, stable and predictable with conflict of interest rules
  - Dispute resolution processes that are efficient, independent and fair
  - Capable, professional and stable public service free from political interference
  - Competent business management free from political interference but held accountable

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Business and Politics

- Roles and responsibilities must be clearly defined for
  - First Nation government
  - Board of directors for companies
  - Senior management of companies
- Appointments/removals must be fair
  - Directors should not be removed just because a new government is elected

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Business and Politics

- Role of First Nation
  - Vision and mission for economic development
  - Strategic planning/development objectives
  - Citizens involvement with the above
- Role of Board of directors
  - Overseeing senior management
  - Approving major operational decisions
  - Approving operational policies/procedures
  - Reporting to the First Nation

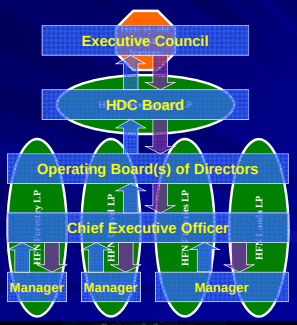
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Business and Politics

- Role of Senior management
  - Responsible for day-to-day operations
  - Human resources for businesses
  - Expenditures within approved budget
  - Accuracy of financial and accounting records
  - Advising and reporting to board of directors
- PA s.64 prohibits limited partner from engaging in management

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Business and Politics



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Business and Politics

- Success requires separation of politics and business
- Business must be accountable to First Nation as owner
  - Shareholder common law rights
    - Financial reporting
    - Election and removal of Directors
    - Right to profits
    - Share in assets on wind-up/dissolution

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Governance Model 1

How we currently make decisions…

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Governance Model 1

- Financial Administration Act
  - Economic Development Committee (s.8)
    - Chair appointed by Chief Councillor
    - 3 to 5 other members
  - EDC mandate (s.9)
    - Advise Exec. Council on economic development
    - Give direction to administration and consultants
    - Identify and research opportunities
    - Monitor and review performance

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Governance Model 1

- Financial Administration Act (continued)
  - Huu-ay-aht Development Corporation (s.57)
    - Note: not HFN Development LP
    - EDC board of HDC
    - Hold HFN business interests
  - Economic development policy regulation required (s.71)

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Governance Model 1

- Economic Development Policy Regulation (EDPR)
  - Principles (s.4)
    - Business plans
    - Business case analyses
    - Reasonable expected return on investment
    - Capable management for day-to-day operations
    - Strategic direction from HFN

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Governance Model 1

- EDPR (continued)
  - Principles (s.4) (continued)
    - Partnerships considered if increased return, warranted risk shared and sustainable
    - Risks must be understood and mitigated
    - Accountability through financial disclosure and performance reports
    - Decisions must take into account limited resources and competing opportunities
  - Emphasis on strategic planning (R&D)

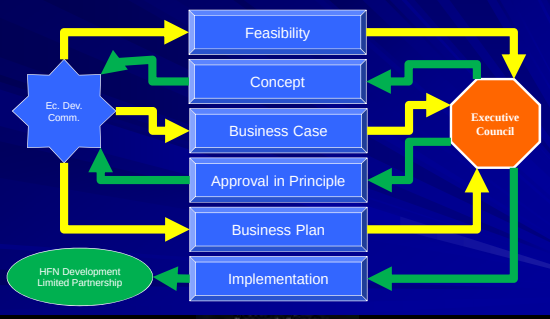
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Governance Model 1

- EDPR (continued)
  - Project stages (s.6(1))
    - Feasibility study by EDC (ss.2)
    - Concept list approved by Exec. Council (ss.3)
    - Business case by EDC – HDC resources (ss.4,5)
    - Approval in principle by Exec. Council (ss.6)
    - Comprehensive business plan by EDC (ss.7,8)
    - Approval to proceed by Exec.Council (ss.9)
    - Implementation by HDC (ss.10,11)

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Governance Model 1



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Governance Model 1

- EDPR (continued)
  - CEO of HDC responsibilities (s.7)
    - Manage HFN businesses [PA s.64 concern]
    - Represent HFN in partnerships
    - Monitor performance of businesses
    - Report to EDC
  - Distribution (return on investment)
    - 15% for 5 years
    - 20% thereafter

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Governance Model 1

- Purchasing Policy Regulation
  - Applies to HFN businesses (s.2(c))
  - Purchases over $1,000 require 3 quotes
  - Purchases over $25,000 require open competition with an evaluation committee
- Risk Management Policy Regulation
  - Applies to HFN businesses (s.1(c))
  - Annual risk assessment and mitigation

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Governance Model 1

- EDPR (continued)
  - Profits of HDC
    - Required dividends on shares or under shareholder agreement [OSR concerns]
    - Retained for sustainability
    - Businesses approved by Exec. Council for implementation
    - Extraordinary dividend (distribution?) – OSR concern?

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Governance Model 1

- Cash Management Policy Regulation
  - Applies to HFN businesses (s.2(d))
  - Annual cash forecast and cash management plan adjusted monthly
  - HDC responsible for all HFN businesses (s.4(3))
  - Required internal short term borrowing

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Governance Model 2

How we could make decisions…

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Governance Model 2

- Alternate governance structure model
- Based on
  - Harvard Project
  - Experience
- Designed for Treaty First Nations
  - Law making authority
  - Economic Development Act
  - Governance and Fiscal Agreement

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Governance Model 2

- Why have an Economic Development Act and Governance and Fiscal Agreement?
  - First Nation policies and procedures can be changed without Business involvement
  - Policies and procedures not enforceable
  - Policies and procedures can diverge
  - Act has force of law
  - Agreement is legally enforceable and change requires agreement of all parties

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Governance Model 2

- First Nation government responsible for strategic planning, research and development – EDA
  - Economic Development Office, Economic Development Committee, Executive Council and Council
- Business operations responsible for implementing approved business – GFA
  - HFN Development LP and Operating LPs

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Governance Model 2

- Economic Development Act
  - Mission & values for economic development
  - Research and development requirements
    - Feasibility studies identify new business opportunities to be approved in principle
    - Five year economic development plan
      - Sets out opportunities approved in principle
      - Updated annually
    - Business plans to implement new businesses

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Governance Model 2

- Economic Development Act (cont.)
  - Role of Council
    - Approve Economic Development Plan
    - Approve in principle new business opportunities
    - Coordinating citizen's input
  - Role of Executive Council
    - Recommend economic development plan
    - Recommend feasibility studies
    - Determine which opportunities in economic development plan are implemented

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Governance Model 2

- Economic Development Act (cont.)
  - Role of Economic Development Committee
    - Oversight of economic development
    - Serve as holdings board
    - Recommend economic development plan, feasibility studies and business plans to Executive
    - Provide information to Huu-ay-aht government
    - Provide direction to economic development officer

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Governance Model 2

- Economic Development Act (cont.)
  - Role of Economic Development Officer
    - Manage economic development office
    - Supports Economic Development Committee
    - Help prepare Economic Development Plan
    - Prepare feasibility studies and business plans
    - Provide entrepreneurial information to members
    - Negotiate new business relationships, as directed

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Governance Model 2

- Economic Development Act (cont.)
  - Process and content for developing
    - Economic Development Plan
    - Feasibility Studies and Business Plans
  - Process for approving and implementing new business opportunities
  - Adherence to business mandates
  - No interference by politicians or senior administration in business operations

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Governance Model 2

- Governance and Fiscal Agreement
  - Role of Executive Council in operations
    - Exercise common law shareholder rights
    - Appoint holdings board (EDC)
    - Approve structural changes in HFN Development Limited Partnership
    - Approve operational anomalies in HFN Development Limited Partnership
    - Approve annual plan and financial statements of HFN Development Limited Partnership

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Governance Model 2

- Governance and Fiscal Agreement (cont.)
  - Role of HDC board
    - Appoint operating board(s)
    - Approve structural changes in operating limited partnerships
    - Approve operational anomalies in operating limited partnerships
    - Approve annual plans and financial statements of operating limited partnerships

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Governance Model 2

- Governance and Fiscal Agreement (cont.)
  - Role of operating board(s)
    - Overseeing senior management
    - Approving major operational decisions
    - Approving operational policies/procedures
    - Reporting to First Nation
  - Role of Senior management
    - Responsible for day-to-day operations
    - Human resources for businesses
    - Advising and reporting to board of directors

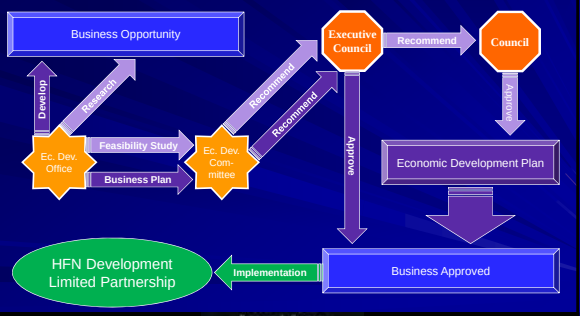
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Governance Model 2

- Governance and Fiscal Agreement (cont.)
  - Processes for
    - Appointments to HDC board
    - Appointments to Operating boards
    - Developing annual plans
    - Removal of board members
    - Major decisions requiring Exec. Council approval
    - Major decisions requiring HDC approval
    - Reporting requirements
    - Profit sharing expectations

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Governance Model 2



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Recommendations

Where do we go from here…

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Recommendation 1

- Section 64 and CEO employment
  - S.64 PA "engages in the management of the business"
  - Have CEO hired by Operating LP
  - HFN Management Services LP (see Recommendation 7)
- Benefits
  - Avoid loss of liability protection for HFN Development LP

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Recommendation 2

- Section 64 and the Operating Boards
  - Currently overlap between HDC board and Operating boards
  - Separate HDC Board from Operating Board(s)
  - Only 1 common director for liaison purposes
- Benefits
  - Avoid loss of liability protection for HFN Development LP because of s.64 PA

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Recommendation 3

- Separate business administration
  - Separate bank accounts and reporting
  - Separate financial administration
  - Separate signage, invoices, letterhead
- Benefits
  - More accurate financial reporting and accountability
  - Avoid loss of liability protection for HFN and HFNDLP because of s.64 PA
  - Corporate veil less likely to be pierced

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Recommendation 4

- Legislative references to HDC/dividends
  - Change “HDC” to “HFNDLP”
  - Change “dividends” to “distributions”
- Benefits
  - Accurate reflection of corporate structure
  - Clarity so as to avoid tax and OSR (limited partnerships/distributions)

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Recommendation 5

- Governance Structure Model
  - Economic Development Act
  - Governance and Fiscal Agreement
- Benefits
  - Clear, detailed roles and responsibilities reduces conflict and success more likely
  - Transparency and accountability provisions
  - Business mandates
  - Force of law and contract

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Recommendation 6

- Role of Council
  - Mission & vision through Economic Development Act
  - Strategic planning through Economic Development Plan updated annually
- Benefits
  - Ensures Council their proper role

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Recommendation 7

- Create HFN Management LP
  - HFNDLP and new general partner
  - HDC appoints board of general partner
  - Hires CEO and senior managers
  - Provides management, development and financial administration services

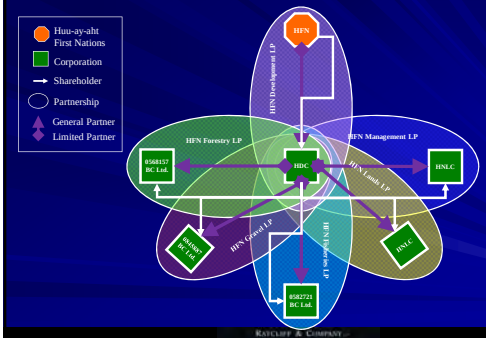
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Recommendation 7

- Benefits
  - Avoid loss of liability protection for HFN and HFNDLP because of s.64 PA
  - Separates business administration from government administration
  - Corporate veil less likely to be pierced
  - No personnel duplication in other operations
  - More accurate financial reporting and accountability as fees reflect true cost

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Recommendation 7



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Recommendation 8

- Application of laws to businesses
  - Revoke application of Cash Management Regulation, Purchasing Policy Regulation and Risk Management Policy Regulation to business enterprises
  - Require boards to have own policies in consultation with EDC
- Benefits
  - Separate politics from business
  - Business better able to adapt to changing circumstances

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Conclusion

- Corporate structure
  - Double liability protection
  - 99.98% of operating profits allocated to First Nation which should be tax exempt
  - OSR can be avoided
- Governance structure
  - Separates business from politics
- Easily add other operations
- One operating failure won't affect others

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Questions



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