

FIRST NATION SETTLEMENT TRUSTS THE PATH TO SELF SUFFICIENCY

Presented by:

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INTRODUCTION

Settlement trusts establish a fiduciary relationship between aboriginal communities, trustees of the trust property and the first nation(s) who are the beneficiaries of the trust. Much the same as the aboriginal peoples were custodians of their lands and territories for the benefit of future generations, the settlement trusts record the fiduciary relationship governing those funds settled on the trust. The settlement funds typically arise in settlement of past, present and future impacts, grievances and claims paid by governmental bodies, resource companies and others who have adversely affected the rights of aboriginal peoples.

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INTRODUCTION (Cont'd)

These settlement trusts are intended to act as a form of treasury for the impacted first nations. As such, the trust is structured in such a way as to attempt to ensure its income is not taxable in the same manner as any other government treasury. Because of the lack of formal legislation generally exempting first nation investments from taxation similar to municipal, provincial or federal treasury funds, it is necessary to establish settlement trusts which divert taxable income to tax exempt First Nations. These settlement trusts have not only been designed to provide such tax benefits but, more importantly, have been created to safeguard the investment and use of the settled funds so as to ensure that the settlements create a legacy for future generations.



OUTLINE

- Settlement Trust Overview
- Trustee Oversight of Settlements
- Fund Uses and Distributions
- Financial Administration
- Income Tax Considerations
- Conclusion

SETTLEMENT TRUST OVERVIEW

- What is a Trust?
- Creation of a Settlement Trust
- Trust Purposes
- Flow Chart

What is a Trust?

- Established when a person (as “settlor”) transfers property to another person (as “trustee”) to hold for the benefit of one or more other persons (as “beneficiaries”)
- Not a legal entity like a corporation - is a fiduciary legal relationship - trustees are custodians of property for the beneficiaries
- Sometimes confused as a separate legal entity - Income Tax Act (Canada) treats trust relationship as a separate legal entity
- Trustees are responsible for custodianship of the trust property - ongoing obligation to administer the trust in accordance with terms of the trust indenture

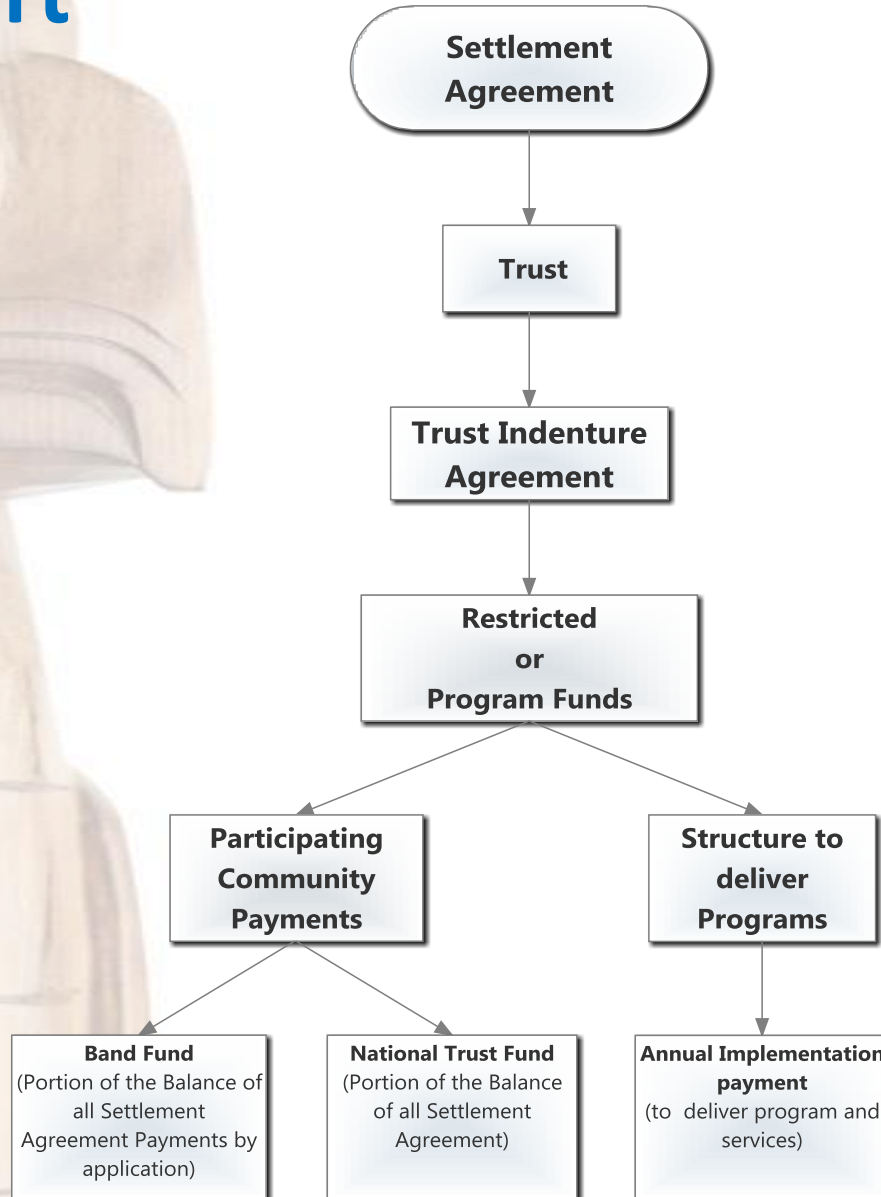
Creation of a Settlement Trust

- First Nation(s) assigns financial entitlements under settlement agreement to trustees
- Settlements irrevocable - trust cannot be cancelled like contract
- Trust Indenture sets term of trust – consider Rule Against Perpetuities under laws of governing jurisdiction
- Trust Indenture sets uses to which trust distributions may be applied by First Nation(s)
- Trust may be established for specific purposes – must not be a “purpose trust”

Trust Purposes

- Settlor First Nation(s) specify the purposes for which trust created – incorporated in trust indenture
- Trust funds must be administered in accordance with stated purposes
- Trust funds must be distributed and used in accordance with trust indenture
- Community at large through a political body such as a band council or council of chiefs determines specific application of trust distributions

Flow Chart





TRUSTEE OVERSIGHT OF SETTLEMENTS

- Responsibility of Trustees
- Powers of Trustees
- Trustee Procedures
- Trustee Appointment and Removal
- Administrative Trustee

Responsibility of Trustees

- Confirms duties of trustees, standard of care, independence
- Sets out specific duties of trustees for clarity
- Affirms ability of trustees to bind trust without liability
- Identifies scope of trustees' liability, validity of acts and indemnification
- Provides rules for conflicts of interest

Powers of Trustees

- Provides legal authority for trustees to act with respect to trust property
- Typically grants powers of natural person with a list of specific powers
- Settlers must determine whether to limit trustees' powers?

Trustees' Procedures

- Sets out decision making authority and process for trustees' meetings
- Determines quorum for trustees meetings
- Establishes procedures for trustee resolutions and special majorities



Trustee Appointment and Removal

- Sets out rules for trustee appointment and removal
- Determines which members of community may not qualify

Administrative Trustee

- Provides for an administrator to oversee the activities of the board of trustees including all financial reporting duties
- Typically no voting power – only power to veto decisions of trustees contrary to terms of trust
- Sets out qualifications of administrative trustee – public trustee or audit firms
- Rules for appointment, replacement and termination
- Term of 3 To 5 years for first administrative trustee



FUND USES AND DISTRIBUTIONS

- Distribution Qualifications
- Procedures for Distribution
- Segregation of Funds

Distribution Qualifications

- Beneficiary restrictions:
 - community member (on or off Reserve)
 - Indian Band(s)
 - status and non-status Indians of common heritage
 - community organizations such as societies
- Further restriction as to qualifying uses:
 - Education
 - Language skills
 - Environment
 - Community development projects, etc.

Procedures for Distribution

- Funds distributed to beneficiaries with agreement to apply to specific uses
- Application by beneficiaries to receive trust funds to be supported by plan and budget
- Trustees approval required
- Beneficiaries to provide audited statement on use of distributions
- Mandate audit of distributions

Segregation of Funds

- Segregated fund balances may be required for:
 - Individual beneficiaries
 - Individual settlors/Indian Bands
 - Specific uses
 - Specific sources of funds
 - Apportionment of legacy funds
 - Minimum balance requirements



FINANCIAL ADMINISTRATION

- Fund Restrictions
- Administrative Trustee Oversight
- Investment Policies and Advisors
- Audit Responsibilities
- Financial Record Keeping

Fund Restrictions

- Trust Indenture to provide restrictions on:
 - Per capita distributions
 - Amount of minimum balance
 - Percentage held as legacy
 - Procedures for applying for distributions
 - Consequences for failure to meet use tests
- Administrative trustee to use veto to enforce fund restrictions

Administrative Trustee Oversight

- Oversees and ensures preparation of
 - Record Keeping
 - Financial Statements
 - Income Tax Returnsto current professional accounting standards
- Approval and co-signing of all cheques on trust funds

Investment Policies and Advisors

- Trustees, with administrative trustee, to establish:
 - Types of authorized investments
 - Types and term of qualified investment managers
 - Investment policies
- Investment advisor and trustees to establish:
 - Prudent investor rules - primary purpose of trust is preservation of capital (ie: equity investments not to form major part of portfolio);
 - Investment policy compliant with Trustees Act of governing jurisdiction - particular attention to investment of trust property;

Audit Responsibilities

- General Scope includes (but is not limited to):
 - Confirmation that funds were used for specified uses
 - Appending to audit the audited schedules detailing the uses of trust funds and/or balances held for credit of beneficiaries
- Compliance Opinion sample as follows:
 - *In our opinion the accounts, records and financial statements are in accordance with principles as set out in parts__ of the Trust Indenture dated _____ to the Settlement Trust for the years then ended*
- Annual audited financials to include:
 - Statement of Financial Position
 - Statement of Operations – Combined
 - Statement of Operations – Operating Fund
 - Statement of Operations – All Funds Provided for in the Agreements
 - Statement of Changes in Fund Balances
 - Statement of Cash Flows
 - Notes to Financial Statements
 - Summary Schedule of Revenue, Expense and Fund Balances by Beneficiaries

Financial Record Keeping

- Trustees responsible for oversight and delegation of:
 - Record keeping - clerical, record keeping and reporting activities associated with trust by maintaining general ledger segregated into fund accounts for all beneficiary funds entrusted to trustees
 - Financial Statements – preparation as determined by Trust Indenture as well as at year end (December 31) – suitable for audit purposes
 - Income tax returns - preparation and the filing of trust income tax returns with approval of a quorum of trustees



INCOME TAX CONSIDERATIONS

- Taxation of Inter Vivos Trusts
- Tax Exempt Status of First Nations
- Attribution of Trust Income to First Nations
- Settlement Trust Exemption

Taxation of Inter Vivos Trusts

- Fully taxable at top marginal personal tax rate
- No exemption for First Nation settlement trusts
- All amounts paid or declared payable by an inter vivos trust to its beneficiaries as a distribution during the year are deductible from taxable income
- Prior to the end of each fiscal year consider payment of distributions from the trust to beneficiaries to the extent of taxable income to avoid income tax liability
- T3 Trust Income Tax and Information Return within 90 days of the end of each calendar year

Tax Exempt Status of First Nations

- Public bodies performing a function of government in Canada are tax exempt under s.149(1)(c) of the Income Tax Act
- The Canada Revenue Agency treats most Indian Bands as exempt under s.149(1)(c)
- Income attributed to settlement funds of an Indian Band are tax exempt regardless of where income is earned

Attribution of Trust Income to First Nations

- Income from property (including money) settled by an Indian Band on a settlement trust will be attributed to the Indian Band under s.75(2) of the Income Tax Act (the “Attribution Rule”)
- The attribution of such income received by a settlement trust will be taxed in hands of the Indian Band notwithstanding that it never receives the income
- Income earned on income from settled property is not subject to the Attribution Rule
- Careful management of income and capital received by trust required to avoid taxation in the trust

Settlement Trust Exemption

- Settlement trusts provide a financial and administrative framework to secure the substantial amounts of financial settlements now being negotiated by First Nations
- Because of the composition of the board of trustees and the ability to appoint well qualified administrative trustees and investment advisers, settlement trusts offer the potential for the establishment of long term legacies
- It is proposed that First Nations, their financial advisers and the federal and provincial governments enter into negotiations to create tax exempt status for First Nation Settlement Trusts

CONCLUSION

First Nation Settlement Trusts should be settled with the objective of benefitting the Beneficiaries involved in the Community Settlement Agreements by providing professional management in the investment and distribution of the Trust Property for the long term well being of the Beneficiaries or Participating Communities.

Morrow & Co and Boughton Law are appreciative of being given the opportunity to assist with the planning stages of this goal.



Thank You Once Again

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Professional Memberships

- Certified General Accountants Association of B. C. and Canada, 1977
- Association of Certified Fraud Examiners, 1997
- Aboriginal Financial Officers Association of B.C. and Canada, 2003
- Licensed by the Ministry of the Attorney General, Province of BC, as a Private Investigator with Morrow Investigations Inc. exclusively for financial investigation matters

Profile

- Norm has a broad range of experience with First Nation, auditing, investigative and taxation issues. He is past president of the Certified Fraud Examiner - Vancouver Chapter, a member of the Private Investigators Association of BC as well as the Canadian Tax Foundation. He is a director of AFOA BC, Chairs the Subcommittee on Taxation, is a member of the Technical Advisory Group as well as a member of the AFOA Canada Audit Committee.
- Norm has participated in numerous conferences and presented such topics as The Benefits of Audits, Audit Preparation, Capital Fund Management, Internal Controls, Technology and Financial System Management as well as Taxation of First Nations tax. Morrow & Co. through Norm's efforts has been instrumental in pushing forward with an AFOA BC campaign to reduce First Nation Reporting through the "New Operational Reporting Method" program.

William (Bill) H. Cooper, CGA, LLB

Professional Memberships

- Certified General Accountant
- University of British Columbia, LL.B.
 - Year of call: 1983 (B.C.), 1988 (ONT)

•Profile

- Bill Cooper has practiced exclusively in taxation matters since being called to the bar in B.C. in 1983. During that time he has had a broad range of experience in tax and related corporate restructuring and finance matters. Bill's tax experience includes a position with the Rulings Directorate of the Canada Revenue Agency (CRA), the Senior Technical and Policy Branch of the CRA in Ottawa where he reviewed transactions of National importance and worked with senior officials of the Department of Finance and the Department of National Revenue developing tax policy and federal income tax legislation.
- Bill has worked with almost 100 different First Nations on a wide variety so socio-economic community development projects involving the development of tax effective investment structures. The First Nation projects in which he has been directly involved include the development of "on reserve" gaming facilities, run of the river hydro projects on First Nation land, joint ventures and partnerships in the forest industry, wineries and mining, as well as a wide variety of general business investments.
- Bill has also provided extensive advice on the establishment of First Nation Trusts and related community oversight bodies established to provide for the preservation and investment of substantial heritage funds arising out of financial settlements related to natural resources.