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Income Tax Rules For Aboriginal People

In general, Aboriginal people in Canada are required to pay taxes on the same basis as other people in Canada, except where the limited exemption under Section 87 of the Indian Act applies. Section 87 says that the "personal property of an Indian or a band situated on a reserve" is tax exempt. Métis and Inuit are not eligible for this exemption.¹

Public Perception

The Canadian public perceives that all Aboriginal people are exempt from the payment of any taxes, including income tax. This perception is not accurate, as Aboriginal people are required to pay taxes on the same basis as other people in Canada, except where the limited exemption under section 87 of the *Indian Act*² applies.

Summary Response

Only those Aboriginal people that meet the following five basic requirements qualify for an exemption from the payment of income tax:

1. The person is an "Indian" as defined in the *Indian Act*;
2. The status Indian lives on a "reserve" as defined in the *Indian Act*;
3. The status Indian performs her/his employment duties on a reserve;
4. The status Indian's employer resides on a reserve; and
5. The activity generating the income was intimately connected to the reserve or an integral part of reserve life.

These five requirements are only partially found in the express language of section 87. The requirements flow from both the language of section 87, together with judicial interpretation of section 87

¹ Indian and Northern Affairs Canada, "Status Indians and Taxes," at http://www.ainc-inac.gc.ca/pr/info/info113_e.html, February 2002.

² R.S.C. 1985, c.1-5.

The Context of Aboriginal People

While section 87 of the *Indian Act* provides an exemption from taxation to status Indians in the limited circumstances set out above, the actual number of Aboriginal people that potentially qualify for the exemption is very limited.

As noted on the chart below, according to 2001 census data, the total Aboriginal population was 976,305. The section 87 exemption from taxation only applies to persons who are entitled to be registered as "Indians" under the *Indian Act*. As Métis and Inuit are not "Indians" as defined in the *Indian Act* or entitled to be registered as Indians, they are not eligible for the section 87 exemption. In other words, only 62.4% of the 976,305 persons who identify themselves as belonging to an Aboriginal group potentially qualify for any exemption from taxation that may be afforded by section 87 of the *Indian Act*.

Aboriginal Population ³		
Total Aboriginal identity population	976,305 ⁴	Percent of total
Indian	608,850	62.4%
Métis	292,305	29.7%
Inuit	45,070	4.6%

The percentage of Aboriginal people that potentially qualify for the section 87 tax exemption is further reduced by the distinction between "status" and "non-status" Indians. The term "status" Indians refers to those persons of Aboriginal ancestry who meet the requirements for registration as an "Indian" under the *Indian Act*. Only those persons who are "registered" or status Indians potentially qualify for the section 87 exemption. As noted on the chart below, of the total number of Indians in Canada, only 558,175 are status Indians. This further reduces the potential pool of "Indians"

³ Aboriginal Origin, Age Groups and sex for Population, for Canada, Provinces, Territories, Census Metropolitan Areas and Census Agglomerations, 2001 Census - 20% Sample Data. Ottawa: Statistics Canada, January 21, 2003. 2001 Census of Canada Catalogue number 97F0011XCB01004.

⁴ The Aboriginal identity population comprises those persons who reported identifying with at least one Aboriginal group, that is, North American Indian, Métis or Inuit, and/or who reported being a Treaty Indian or a Registered Indian, as defined by the *Indian Act* of Canada, and/or who reported being a member of an Indian Band or First Nation.

that qualify for the section 87 taxation exemption from 608,850 to 558,175 or 57.1% of the total Aboriginal population.

Total "Indian" Identified Population⁵		
	Total	Percent of total
Total "Indian" identified population	608,850	
Status Indian	558,175	91.68%
Non-Status Indian	50,675	8.32%

The distribution of the population of status Indians between on-reserve and off-reserve locations further reduces the potential pool of Aboriginal people that qualify for the section 87 exemption from taxation. In order to qualify for the section 87 taxation exemption, an "Indian must live on a "reserve" as defined in the *Indian Act*. As noted on the chart below, only 29.3% of status Indians live "on reserve". This effectively reduces the potential pool of Aboriginal people that qualify for the section 87 exemption from 57.1% (which represents the total population of registered status Indians) to 29.3% (which represents the total population of registered status Indians living on reserve).

⁵ Aboriginal Origin, Age Groups and sex for Population, for Canada, Provinces, Territories, Census Metropolitan Areas and Census Agglomerations, 2001 Census - 20% Sample Data. Ottawa: Statistics Canada, January 21, 2003. 2001 Census of Canada Catalogue number 97F0011XCB01006.

Reserve Data ⁶	
On Reserve	29.3%
Off Reserve	70.7%

The potential pool of Aboriginal people that qualify for the section 87 taxation exemption is further reduced by the limited number of employment opportunities on Indian reserves. As noted above, in order to qualify for the exemption from income taxation, the employment duties must be performed on a reserve. As noted on the chart below, only 54,365 of status Indians living on a reserve perform their employment duties on reserve. In other words, of the total Aboriginal population of 976,305, only 54,365 or 5.6% of Aboriginal people potentially meet the five basic requirements that must be satisfied in order to qualify for the exemption from income taxation afforded by section 87 of the *Indian Act*.

On Reserve Employment ⁷		
Category	Total	Percent of Total
Total Labour Force	76,305	
Employed	54,365	71.2%
Unemployed	21,935	28.8%

General Historical Overview of the Exemption and Its Purpose

Many Canadians feel that it is unfair that the *Indian Act* provides any form of tax exemption to Aboriginal people that is not also available to all Canadians. Why does

⁶ Derived from Canada West Foundation from 2001 Census data. These data are for the "Aboriginal Identity Population" and do not include incompletely enumerated Indian reserves or settlements. Statistics Canada defines the Aboriginal Identity Population as "those persons identifying with at least one Aboriginal group, i.e. North American Indian, Métis or Inuit (Eskimo), and/or those who reported being a Treaty Indian or Registered Indian as defined by the Indian Act of Canada and/or who were members of an Indian Band or First Nation" (Statistics Canada 2003b; 2003a).

⁷ Source: Statistics Canada, DIAND Core Census Tabulations, 1996, T-11.

the *Indian Act* provide an exemption from taxation to Aboriginal people who fall within the definition of "Indian" set out at section 2 of the *Indian Act*?

The historical origin of the section 87 tax exemption can be traced back to Canada's early policy of protecting Indians and their lands from alienation. As commented upon by a legal historian, the "root of the purpose is derived from the second original components of Canadian Indian policy, to protect the Indians and their land from abuse and imposition of European settler populations".⁸ The first component was 'civilizing' the Indian population and achieving assimilation and integration as soon as possible.

The goal of protecting Aboriginal lands from alienation was clearly evidenced in early legislation passed in 1850 by the then Province of Canada entitled - *An Act for the protection of the Indians in Upper Canada from imposition, and the property occupied or enjoyed by them from trespass and injury*.⁹ Section 4 of the Act reads:

4. That no taxes shall be levied or assessed upon any Indian or any person intermarried with any Indian for or in respect of any of the said Indian lands, nor shall any taxes or assessments whatsoever be levied or imposed upon any Indian or any person inter-married with any Indian so long as he, she or they shall reside on Indian lands not ceded to the Crown or which having been so ceded may have been again set apart by the Crown for the occupation of Indians.

The language of the *Indian Act*, as amended in 1876 also clearly demonstrates that there was never any intention to give preferential treatment to Aboriginal people, except in connection with protecting Aboriginal lands from alienation. For example, section 64 of the *Indian Act* of 1876 provided:

64. No Indian or non-treaty Indian shall be liable to be taxed for any real or personal property, unless he holds real estate under lease or in fee simple, or personal property, outside of the reserve or special reserve, in which case he shall be liable to be taxed for such real or personal property at the same rate as other persons in the locality in which it is situate.

In commenting on the purpose of the section 87 *Indian Act* tax exemption, the courts have similarly ruled that the purpose of the tax exemption is not to give preferential treatment to Aboriginal people, except in connection with protecting Aboriginal land and personal property from alienation. For example, in *Mitchell v. Peguis Indian Band*, the Court stated that the purpose of the exemption is not to cure poverty or place

⁸ Richard H. Bartlett, "The Indian Act of Canada" (1978) 27 Buffalo Law Review 581 at 583.

⁹ S.C. 1850, c.74.

Indians at a competitive advantage, but to protect Aboriginal land and personal property from alienation.¹⁰

The Statutory Basis

The *Indian Act* tax exemption operates through two pieces of federal legislation, the *Indian Act* and the *Income Tax Act*.¹¹

Indian Act

Sections 87 and 90 are the relevant sections of the *Indian Act* that provide the framework for an exemption from taxation for status Indians.

Section 87 provides:

87.(1) Notwithstanding any other Act of Parliament or any Act of the legislature of a province, but subject to section 83, the following property is exempt from taxation, namely,

(a) the interest of an Indian or a band in reserve lands or surrendered lands; and

(b) the personal property of an Indian or a band situated on a reserve.

(2) No Indian or band is subject to taxation in respect of the ownership, occupation, possession or use of any property mentioned in paragraph (1)(a) or (b) or is otherwise subject to taxation in respect of any such property. (emphasis added)

Section 90 provides:

90. (1) For the purposes of sections 87 and 89, personal property that was

(a) purchased by Her Majesty with Indian moneys or moneys appropriated by Parliament for the use and benefit of Indians or bands, or

(b) given to Indians or to a band under a treaty or agreement between a band and Her Majesty,

shall be deemed always to be situated on a reserve.

¹⁰ *Mitchell v. Peguis Indian Band* [1990] 2 S.C.R. 85 at p. 131.

¹¹ R.S.C. 1985, c. 45.

There is nothing in the language of section 87 that specifically exempts the income of status Indians from taxation. Section 87(1)(b) merely exempts from taxation, the “personal property of an Indian or a band situated on a reserve.” Accordingly, it is clear that Parliament never intended to extend a general exemption from income taxation to status Indians.

Rather, the courts have held that employment income is “personal property” for the purpose of section 87(1)(b) of the *Indian Act*.¹² In other words, it has been through judicial interpretation of the *Indian Act* that the general exemption from taxation found at section 87(1)(b) has been extended to employment income earned by status Indians.

Section 87 also requires that the personal property exempted from taxation be “situated on a reserve”. The requirement for personal property to be “situated on a reserve” has been considered by the courts and has given rise to legal tests that offer guidance in determining when property is “situated on a reserve” for the purpose of section 87 of the Act. These legal tests together with a review of recent case law are discussed in greater detail at sections 6 and 7 of this paper.

Section 90 of the *Indian Act* also offers some guidance in determining when property is “situated on a reserve”. In particular, section 90 of the Act deems property that was “purchased by Her Majesty with Indian moneys or moneys appropriated by Parliament for the use and benefit of Indians or bands,” or “given to Indians or to a band under a treaty or agreement between a band and Her Majesty” to be situated on a reserve for the purpose of section 87 of the Act.

Income Tax Act

Paragraph 81(1)(a) of the Income Tax Act excludes from the income of a taxpayer:
... an amount that is declared to be exempt from income tax by any other enactment of Parliament, other than an amount received or receivable by an individual that is exempt by virtue of a provision contained in a tax convention or agreement with another country that has the force of law in Canada.

The *Indian Act* is an “enactment of Parliament” and section 87 is an exemption established under that federal legislation. In other words, section 81(1)(a) of the *Income Tax Act* incorporates the *Indian Act* exemption into the federal tax system. Generally stated, the *Indian Act* exempts personal property of a status Indian on reserve from taxation and the *Income Tax Act* confirms this exemption.

The Legal Test

¹²*Nowegijick v. R.* [1983] 1 S.C.R. 29 at p. 38

The “Residence of the Debtor” Test

Section 87 of the *Indian Act* requires that the personal property of an Indian be “situated on a reserve” before it can qualify for an exemption from taxation. Until 1992, the residence of the employer or “residence of the debtor” was the primary factor that the Courts would consider when determining whether income earned by an Aboriginal person was “situated on a reserve” for the purposes of section 87 of the *Indian Act*. The “residence of the debtor” test was adopted by the Supreme Court of Canada in *Nowegijick v. The Queen*.¹³

The “Connecting Factors Test”

In 1992, the Supreme Court of Canada adopted the “connecting factors test” in the case of *Williams v. Canada*¹⁴ for determining whether employment income is “situated on a reserve”. The “connecting factors test” requires that there must be “sufficient connecting factors” between the employment income and the reserve for the income to be considered “situate on a reserve” and thus eligible for exemption.

Unfortunately, the Court in the *Williams* case did not identify the specific connecting factors that must be considered in applying the test. However, the Court did offer the following guidance in identifying the location of property for the purpose of section 87 of the *Indian Act*:

*The first step is to identify the various connecting factors which are potentially relevant. These factors should then be analyzed to determine what weight they should be given in identifying the location of the property, in light of three considerations: (1) the purpose of the exemption under the Indian Act; (2) the type of property in question; and (3) the nature of the taxation of that property. The question with regard to each connecting factor is therefore what weight should be given that factor in answering the question whether to tax that form of property in that manner would amount to the erosion of the entitlement of the Indian qua Indian on a reserve.*¹⁵

The Court offered the following guidance on determining what weight should be given to each connecting factor:

A connecting factor is only relevant in so much as it identifies the location of the property in question for the purpose of the Indian Act.

¹³ Ibid.

¹⁴ [1992] 3 C.N.L.R. 181.

¹⁵ Ibid at 191.

*In particular categories of cases, therefore, one connecting factor may have much more weight than another. It would be easy in balancing connecting factors on a case by case basis to lose sight of this.*¹⁶

“Intimately Connected to a Reserve” or “An Integral Part of Reserve Life”

In *Recalma v. R.*¹⁷ the Federal Court of Appeal added an additional factor to consider when examining the various factors that connect employment income to a reserve, namely whether the activity generating the income is “intimately connected to” a reserve or an “integral part” of reserve life. In particular, Linden, J.A. stated:

*It is also important in assessing the different factors to consider whether the activity generating the income was “intimately connected to” the Reserve, that is, an “integral part” of Reserve life, or whether it was more appropriate to consider it a part of “commercial mainstream” activity ((see *Folster v. The Queen*) (1997), D.T.C. 5315 (F.C.A.)). We should indicate that the concept of “commercial mainstream” is not a test for determining whether property is situated on a reserve; it is merely an aid to be used in evaluating the various factors being considered. It is by no means determinative. The primary reasoning exercise is to decide, looking at all the connecting factors and keeping in mind the purpose of the section, where the property is situated that is whether the income earned was “integral to the life of the reserve”, whether it was “intimately connected” to that life, and whether it should be protected to prevent the erosion of the property held by Natives qua Natives.*¹⁸

Canadian Customs and Revenue Agency Guidelines

The Canadian Customs and Revenue Agency (“CCRA”) is the Government authority that is responsible for the administration and collection of taxes in Canada. The CCRA has published plain language documents entitled; *Information for Status Indians*,¹⁹ and *Indian Act Exemption for Employment Income Guidelines*.²⁰ These represent the CCRA’s interpretation of section 87 of the *Indian Act* and relevant case law.²¹

¹⁶ Ibid at 190.

¹⁷ [1998] 3 C.N.L.R. 279.

¹⁸ Ibid at p. 282.

¹⁹ Canada Customs and Revenue Agency, *Information for Status Indians* (Ottawa: 2003).

²⁰ Canada Customs and Revenue Agency, *Indian Act Exemption for Employment Income*

In the *Indian Act Exemption for Employment Income Guidelines*, the CCRA sets out the following guidelines for determining whether income is “situated on a reserve” and therefore exempt from taxation:

*When at least 90% of the duties of an employment are performed on a reserve, all of the income of an Indian from that employment will usually be exempt from income tax.*²²

*When the employer is resident on a reserve and the Indian lives on a reserve, all of the income of an Indian from an employment will usually be exempt from Income Tax.*²³

*When more than 50% of the duties of an employment are performed on a reserve; and the employer is resident on a reserve, or the Indian lives on a reserve, all of the income of an Indian from an employment will usually be exempt from income tax.*²⁴

When the employer is resident on a reserve, and is:

An Indian Band which has a reserve, or a tribal council representing one or more Indian Bands which have reserves, or

An Indian organization controlled by one or more such bands or tribal councils, if the organization is dedicated exclusively to the social, cultural, educational, or economic development of Indians who for the most part live on reserves; and

The duties of the employment are in connection with the employer’s non-commercial activities carried on exclusively for the benefits of Indians who for the most part live on reserves;

Guidelines (Ottawa: 2003).

²¹ The Guidelines state the following in reference to *Williams* “In 1992, the Supreme Court of Canada decided that all factors connecting income to a reserve must be examined in determining whether or not the income is situated on the reserve. To determine whether employment income is situated on a reserve, the courts follow the approach described in the decision called *Glenn Williams v. Canada*.”

²² *Ibid.*

²³ *Ibid.*

²⁴ *Ibid.*

*All of the income of an Indian from an employment will usually be exempt from income tax.*²⁵

The Guidelines clearly capture three of the five basic requirements set out at section 2 of this paper. In particular, the Guidelines affirm that a status Indian must reside on a reserve, perform his or her employment duties on a reserve and his “or her” employer must reside on the reserve in order to qualify for an exemption from income taxation. However, the Guidelines also go beyond the direction provided by the courts by offering formula for identifying the percentage of work that must be performed on a reserve before income can be exempted from taxation.

Recent Judicial Interpretation of the Test

Judicial interpretation of the “connecting factors test” clearly evidences how difficult it is for a status Indian to obtain an exemption from taxation, particularly when employment duties are performed off a reserve, unless the five basic requirements set out at section 2 of this paper are met.

Folster

In *Folster v. Canada*,²⁶ the Court considered whether income earned by a status Indian at a hospital located off-reserve, but near reserve lands was exempt from taxation. The Government of Canada built the hospital and 80% of the patients were Indians. Funds for the Indians who used the hospital came from Health and Welfare Canada. The Court held that Ms. Folster’s earnings were deemed to be situated on a reserve pursuant to section 90(1)(a) of the *Indian Act*.²⁷

The *Folster* case appears to represent one of the rare exceptions to the general rule that the employer must reside on a reserve and the employee must perform all or most of his or her employment duties on a reserve. While the various factors connecting the income to the reserve were considered in *Folster*, the case was decided on the basis of the deeming provisions in section 90(1)(a) rather than on application of the “connecting factors test”.

Bell

In *Bell v. R.*²⁸, the Court considered whether income earned by status Indians from employment in the commercial fishing industry was exempt from taxation. The

²⁵ Ibid.

²⁶ [1997] 3 C.T.C. 157.

²⁷ Ibid at p. 171.

²⁸ [2000] 3 C.N.L.R. 32.

plaintiffs resided on a reserve, but performed most of their employment duties on a fishing boat and dock that was located off the reserve. However, the fishing company that employed the plaintiffs was located on a reserve. In other words, the plaintiff's employer resided on a reserve. The Court held that income earned by the plaintiffs was not exempt from taxation as the plaintiffs were not engaged in a business that was "integral to the life of the reserve", but in a business that was in the commercial mainstream.²⁹

Southwind

In *Southwind v. Canada*,³⁰ a status Indian lived on a reserve and owned and operated a logging business that was also located on a reserve. In 1990, the status Indian was paid for logging work performed for a non-Aboriginal company at three off-reserve cutting locations. In other words, although the status Indian resided on reserve, his employment duties were performed off-reserve. The Federal Court of Canada considered the various factors connecting the income to a reserve and concluded that his income was not exempt from taxation. The Court reached this conclusion on the basis that Mr. Southwind was not engaged in a business "integral to the life of his reserve", but in a business that was in the "commercial mainstream."³¹

Shilling

In *Shilling v. MNR*,³² a status Indian was employed by a company named Native Leasing Services (NLS), whose head office was located on an Indian reserve. NLS contracted Ms. Shilling's services to Anishnawbe Health Toronto (AHT), which was a social agency situated at a location off the reserve. AHT delivered programs to assist Aboriginal people reconnect with their culture. Ms. Shilling lived off-reserve and performed most of her employment duties for AHT off-reserve.

Although AHT was responsible for delivering programs to assist Aboriginal people to reconnect with their culture, the Court found that Ms. Shilling's job was in the "commercial mainstream"³³ and not "integral to the life of the reserve."³⁴ The Court found that the factors connecting the income to a reserve location were outweighed by those factors connecting it to an off-reserve location and consequently held that Ms. Shilling's employment income was not exempt from taxation under section 87 of the

²⁹ *Bell v. R.*, *supra* note 38 at para 42.

³⁰ [1998] 2 C.N.L.R. 233.

³¹ *Ibid* at p. 238.

³² [1999] 176 D.L.R. (4th) 226.

³³ *Ibid* at para 71.

³⁴ *Ibid* at para 71.

Indian Act. This decision reinforces the general premise that if a status Indian resides off reserve and performs the majority of her employment duties off reserve, she will not be exempt from taxes.

Monias

In *Monias v. R.*,³⁵ the appellants were status Indians who worked for an organization located off-reserve that was responsible for the welfare of Aboriginal children living on reserves. None of the appellants lived on reserves and most of the employment duties were performed in an off-reserve office. On appeal, the Court held that the income was not exempt from taxation under section 87 of the *Indian Act*.³⁶ On application of the connecting factors test, the Court concluded that the benefits to Aboriginal children living on reserve from services provided by the appellants was outweighed by the fact that the appellants resided off reserve and performed their employment duties off reserve.

Amos

In *Amos v. R.*,³⁷ an Indian Band leased reserve land to a pulp mill on the condition that the mill would provide job opportunities for band members. The Minister assessed tax on income earned by band members from the mill. The band members appealed the assessment.

At trial, Bell T.C.J. the Tax Court dismissed the band member's appeal on the basis that the mill's operation was purely a commercial endeavour and wholly unrelated to any reserve activity.³⁸ On appeal, Strayer J.A. reversed the Tax Court's decision. Strayer J.A. stated that the "employment was directly related to the realization by the Band and its members of their entitlements to the reserve land and, in accordance with the purpose of the tax exemption in section 87, the government should not be able through income taxation to erode income from such use, direct and indirect, of their land".³⁹

³⁵ [1999] 4 C.T.C. 2354.

³⁶ *Ibid* at para 70.

³⁷ [1999] C.N.L.R. 7.

³⁸ *Ibid* at p. 13.

³⁹ [1999] Carswell Nat 925, 99 D.T.C. 5333 (F.C.A.) at pp.7.

Concluding Remarks

While section 87 of the *Indian Act* provides an exemption from taxation to status Indians in limited circumstances, the purpose of the exemption is not to give Aboriginal people preferential treatment. Instead, the purpose of the exemption is to protect Aboriginal land from alienation. Furthermore, only 5.6% of the entire Aboriginal population are status Indians who live and work on a reserve. Accordingly only 5.6% of the Aboriginal population meet the requirements that must be satisfied in order to qualify for the section 87 exemption from income taxation. A review of the case law also clearly demonstrates how difficult it is for a status Indian to obtain an exemption from taxation, particularly when employment duties are performed off a reserve, unless the five basic requirements set out at section 2 of this paper are met. All of these factors clearly demonstrate that there is no blanket exemption from the payment of income taxes available to people of Aboriginal ancestry.

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