Tax opportunities under the Indian Act

April 16, 2024

Authors

Luc Pariseau

Partner, Lawyer

Audrey Pelletier

Senior Associate

François Rizcallah

Lawyer

Although it is not often well-understood in business and tax circles, the *Indian Act* (the "**Act**"), coupled with federal and provincial tax laws, provides several tax planning opportunities for Indigenous taxpayers. These laws provide various tax exemptions for people who qualify as "Indians" under the Act, as well as for "bands" and other "councils." These terms are defined in the Act and require case-by-case analysis, but essentially they refer to people of Indigenous origin who have at least one family member who is registered or entitled to be registered as an Indian within the meaning of the Act.

The criteria for a tax exemption

In particular, those who qualify can benefit from a tax exemption when income is earned on a "reserve." There are several criteria to be met, and although the Canada Revenue Agency ("**CRA**") has issued guidelines on the subject, their application remains a question of fact that varies depending on the particular circumstances applicable to each taxpayer.

In general, the CRA requires that income earned by an "Indian" within the meaning of the Act be sufficiently connected to a reserve to be exempt. This is the case when, for example, income-generating services are performed entirely or almost entirely within the territory of a reserve, when the employer and the employee reside on a reserve, or when income is derived from non-commercial activities carried out by a band. Business income can also be tax-exempt, but the criteria for being considered connected to a reserve are stricter, since generally only income-generating activities situated on a reserve will be tax-exempt. However, it is still possible to organize the affairs of a taxpayer and their corporate entities to ensure that these criteria are met, or to highlight certain connecting factors. Such planning, if done properly, is entirely legitimate and can result in significant tax savings.

In a recent interpretation (CRA Views 2022-0932231I7), the CRA illustrated this principle by considering employment income related to an off-reserve airport to be exempt, even if none of the guidelines are followed, in cases where such an airport is necessary to supply a reserve that has no other means of transportation and delivery. This interpretation shows that the connection between an income and a reserve is not established solely by the physical presence of the income-generating business, and that several other arguments, sometimes more subtle, can be used to support the connection between an income and a reserve.

A few nuances to consider

However, care must be taken when a company is incorporated by someone who qualifies as an “Indian.” A company with its head office on a reserve cannot qualify as “Indian” within the meaning of the Act. Its income therefore cannot be tax-exempt, and will be taxed according to the usual rules. Despite this, certain plans can ease the tax burden on these companies and on shareholders who qualify as “Indians” under the Act, such as paying wages and bonuses to an employee shareholder. But it’s essential to carefully analyze the various pitfalls and risks that such planning entails. Furthermore, certain exemptions exist for companies formed by bands, but the eligibility criteria are strict and require a thorough analysis of the proposed structure.

In addition to the income tax exemption, “Indians” within the meaning of the Act and certain entities mandated by bands may benefit from a tax exemption when they purchase goods on a reserve or have goods delivered to them on a reserve. Different exceptions and nuances apply. However, companies headquartered on a reserve are not exempt from their tax collection obligations and may be required to register for the GST/QST.

To help you understand these rules and ensure optimal tax planning, we invite you to consult our tax team. We look forward to working with you on your business projects.