The Supreme Court Changes the Landscape of Banking and First Nations

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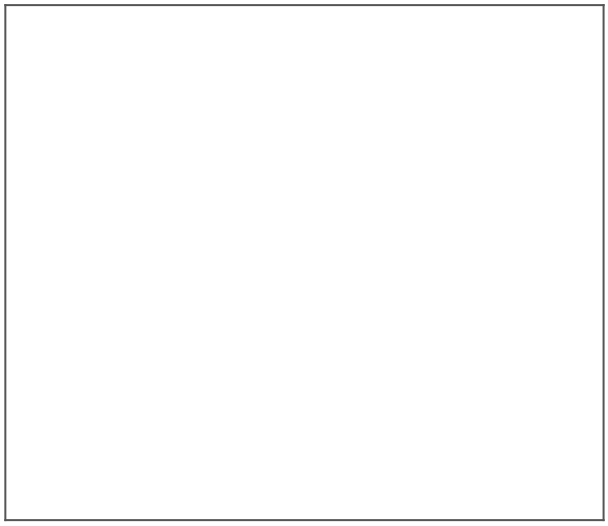
Outside the Supreme Court of Canada, after arguing in the appeal of the *Bastien and Dube* cases, I was approached by a member of the gallery and asked how important these cases were. Having only a brief moment before the fellow's taxicab shuttled him away into the bustle of downtown Ottawa, I responded in full sophisticated legalese: "pretty darn important".



The cases of *Bastien v. The Queen* and *Dube v. The Queen* (heard jointly - there was some difference between the two which I won't go into here) are as important in telling the story of how remarkably our case law can change as they are for the way in which they may affect banking and commerce on First Nations reserves. The issue on appeal was whether interest income earned from a financial institution on a reserve is exempt from taxation pursuant to the *Income Tax Act* and section 87 of the *Indian Act*. Section 87 provides an exemption from taxation for property situated on a reserve. Both the Tax Court and the Federal Court of Appeal concluded that such interest income was not property situated on a reserve. Not only did the lower courts rely on established principles from previous Supreme Court of Canada decisions dealing with connecting factors - factors that are to aid in the court's determination of whether intangible property is situated on reserve - they relied on several other Tax Court and Federal Court of Appeal decisions, all of which specifically held that interest income earned on reserve is not

exempt from taxation. The underlying premise of these decisions was that since the income used to pay the interest on reserve was generated off of the reserve in the "commercial mainstream," it could not be said to be situated on reserve.

Our argument was that all of the lower court decisions were wrongly decided. Rather than focusing on how the lender would generate the funds to pay the interest, the courts should look to the nature of interest income and how it is taxed. It is the lending agreement itself which creates the right to interest income. How the financial institutions generate those funds, and whether they are earned in the commercial mainstream are irrelevant. Notwithstanding the weight of a number of authorities favouring the lower courts' decisions, the Supreme Court of Canada allowed the appeal and found that the interest income was property situated on a reserve. Among other things, the Court agreed that the notion of the income being generated in the commercial mainstream had been misapplied by the lower courts.

The impact of the Court's decision and how it will affect commerce with First Nations, is a matter for tax planners, lenders, those who do business with First Nations, and the members of First Nations to now consider. The obvious immediate effect is that interest income that was previously taxed by the Canada Revenue Agency will now be exempt from taxation. The secondary benefits are much broader. The inherent transactional costs of loaning funds off of the reserve and into the commercial mainstream are reduced by the taxes saved. Such cost savings can now be used to leverage a myriad of transactions that require financing. The spectrum of advantages are limited only by the creativity of tax and business planners, having regard to the proper interpretation of the principles laid down by the Court.

The lessons of this decision also go beyond the subject area of taxation of on-reserve interest income. Concepts employed in tax law are not static and unchanging nor are they immune from persuasive reasoning. By properly framing the issues and articulating the errors in the existing jurisprudence, "established" law was effectively changed for the benefit of the taxpayer/client.

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