Reducing the barriers to Indigenous economic growth:

The First Nations Finance Authority and Monetization

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The First Nations Finance Authority

The First Nations Finance Authority (FNFA) was established as a not-for-profit financier under the *First Nations Fiscal Management Act.* Our mandate is to issue debentures in the financial marketplace to lend to First Nations governments for their community priorities. These debenture proceeds are in turn loaned to individual First Nations to finance infrastructure, health, social, green energy or economic development priorities.

FNFA is governed by the Chiefs and Councillors voted from amongst its membership.

Since issuing our first debenture in 2014, we have raised almost $1.7 billion in the capital markets; by the summer of 2022 we expect to exceed $2 billion. Importantly, all annual loan service payments are made by the First Nations from their own source revenue. No Canada monies are used. Our debentures are seen as safe investments and recent offerings have been oversubscribed. There has never been a default on any loan we have issued and this is reflected in our institutional credit ratings (Moody's, and Standard & Poor's). The FNFA is able to raise money at the same interest rate paid by the Province of Ontario. As a non-profit entity we pass these low rates along to our member First Nations, providing them financing at terms simply unavailable to them through the commercial chartered banks.

More recently, FNFA has secured a 3rd credit rating with DBRS Morningstar for purpose of issuing FNFA Commercial Paper for financing below bank prime rate interim loans to the FNFA borrowing members.

Participation under FNFA's Act is voluntary. To date 317 First Nations have scheduled, 138 have completed FNFA's membership processes; 78 of those have active long-term loans with us. We have provided financing to First Nations in 9 of 10 provinces and 1 territory. Our most high-profile contribution is likely the financing to enable a coalition of First Nations to assume an equal equity interest in Clearwater Seafoods. But most of the projects to which we lend are to help individual communities meet their own immediate needs. The range of projects undertaken with FNFA assistance is impressive and includes community centres, schools, commercial developments, housing, and transportation infrastructure among others. We are seeing an increased number of First Nations using FNFA financing to make the transition to clean energy, including bio-energy and wind energy installations.

Using the Bank of Canada formula for calculating economic impact, we calculate the FNFA's overall economic impact at almost $3.5 billion to date. Also using Statistics Canada guidelines, we calculate the employment impact of the projects we financed at more than 17,000 jobs across Canada. These jobs and economic activity do not benefit only the First Nations carrying out the projects, but businesses, suppliers, contractors, and workers in neighbouring communities.

The challenges

Limitations on the FNFA

As much as the FNFA has achieved so far, we will soon be constrained in the impact we can deliver. To date, all loan service has been from First Nations own revenues. Participation by Canada will be needed to reduce the growing infrastructure gap in the communities.

The *First Nations Fiscal Management Act* limits the eligible revenues we can consider when establishing an individual First Nation's borrowing limit, or the collective borrowing limit of our members. By and large, we are limited to considering those First Nations' own-source revenues.

There are advantages to this approach. First Nations have a greater deal of control over their own source revenues, and their use of those funds is not subject to agreements with the federal government or other parties. Those revenues are arguably more predictable than federal government transfers which, despite the option of 10-year grant agreements for qualifying First Nations, are subject to annual negotiation and uncertainty.

The main disadvantage to this approach is that most First Nations have limited opportunity to generate own-source revenues. This limits the amount that FNFA can raise overall, and limits the amount that can be loaned to any individual First Nation.

Essentially, we have a vicious circle. The lack of economic and infrastructure development limits own-source revenues; this in turn limits the ability to access capital to spur economic and infrastructure development.

In 2021, the federal budget and accompanying implementation legislation did expand the revenue base available for the FNFA to consider, to include certain revenues from the Crown in right of Canada. This is encouraging, and we very much welcomed this, but the potential impact of this remains to be seen.

The "infrastructure gap"

Economic development does not occur in a vacuum. It requires comprehensive and up-to-date infrastructure. We refer not only to the infrastructure that might be top of mind when considering economic issues, such as transportation links, telecommunications, and energy. Communities' social health and infrastructure is also key to economic development.

There is a well-documented "infrastructure gap" between First Nations and other Canadian communities; this is the investment that would be required to bring the average First Nation's infrastructure to the average level of other communities. The figure is widely accepted to be at least $30 billion in current dollars.

This gap is most evident in the communities that have the greatest economic development challenges. Remote and northern First Nations often lack any transportation infrastructure to import or export goods or services. They do not have access to telecommunications considered the bare minimum by the CRTC or ISED. In far too many cases they do not have adequate or reliable power supply – relying on diesel generators that are well beyond their intended lifespan and off-line far too much of the time.

The federal government has established goals to address some of these issues. For several years there has been a commitment to end the reliance on diesel power generation for all remote and northern communities, not just First Nations, by 2030. In the most recent mandate letters, the Prime Minister instructed his Ministers to work towards closing the infrastructure gap in Indigenous communities also by 2030.

Recent budgets have announced new funding for Indigenous infrastructure, but the amounts – and the timeline for rolling funds out are not in line with the scale of the challenge. It is also not clear that funds that have been nominally announced for particular types of infrastructure have been adequately thought through. For example, the Parliamentary Budget Office recently reported on investments in drinking water on First Nations and concluded that if anything, too much has been announced for construction of new facilities, with a dearth of funding for ongoing operation and maintenance.

The current funding approach

The current government approach to funding is possibly the most significant challenge when it comes to infrastructure and economic development.

We and others call this the "pay as you go" model. Essentially, Indigenous Services Canada and other departments and agencies are provided an annual allocation, from which they fund as many projects (at current prices) as they can. This is a very challenging approach to financing, and a very challenging approach to planning and development, and only serves to exacerbate existing challenges. To note:

- Current annual capital funding available through ISC is around $2 billion. Decisions are made annually around how to allocate these monies. This compares to an identified and verifiable need for at least $30 billion.
- Even prior to Covid-19, inflation on capital projects was higher than CPI inflation. As a result, unfunded needs are growing at a faster pace than ISC's annual investments. This means First Nations are falling further behind every year.
- Projects are often funded based on dollars available, rather than need, urgency, or potential impact.
- Communities stand in-line each year, and if not selected then stand in the same line next year. The gap continues to grow.

- Funding provided is generally for initial construction, without any allocation available for ongoing operations and maintenance. Infrastructure in First Nations often does not meet the expected lifespan. As well, no monitoring of the annual maintenance occurs.

Monetization: a potential solution

The FNFA proposes a mechanism we refer to as Monetization. This is essentially the model that municipalities use to fund public works undertakings and is even comparable to how individual Canadians arrange their finances for large purposes like houses or automobiles.

Using an example that Committee members can undoubtedly relate to, very few individuals purchase a family home with cash on hand. For most people, money they could save each year would be outstripped by the increase in average home prices, leaving them farther and farther away from home ownership. Instead, they get pre-approved for a mortgage – with the lending institution doing a risk assessment and approving an amount based on ability to make payments over time. This allows the individual to purchase a home today, at today's prices. In essence, future pay cheques are Monetized into house mortgages.

Most governments make capital expenditures in a similar manner. Municipalities issue debentures, with payments funded through future property tax and other revenues. Provincial governments, and the federal government, issue debt to cover current expenses, or negotiate long-term contracts with suppliers to provide capital goods.

Monetization would see the federal government partner with the FNFA to allow First Nations to make capital and economic development expenditures in a similar manner. The federal government would decide on the priorities and the total costs of the approved projects. A contract would be negotiated with the FNFA to raise the necessary financing in the capital markets. The FNFA would in turn loan the debenture proceeds to the qualifying First Nations who would undertake the projects. Canada would direct annual monies to FNFA to service the debenture payments.

The FNFA was created through all-party support in 2005, and with 317 First Nations voluntarily joining our Act, is a natural choice to achieve reconciliation and close the infrastructure gap. One of our Act's mandate areas is the leveraging of agreed-to Canada monies into First Nations projects.

The FNFA does not propose to raise the full $30 billion needed to significantly address the infrastructure gap. We acknowledge that Monetization is a new approach to financing First Nation development and it needs to be tested. To that end, we have proposed that the federal government partner with us to deliver one or more pilot projects to test the concept prior to considering its broader applicability. We believe that pilot projects can be either thematic or place-based, but the parameters of both would be broadly similar.

One example of a thematic pilot project relates to diesel generator replacement. As noted above, the federal government's stated goal is to complete this by 2030 but there has not been a specific and sufficient allocation of funds, nor has a comprehensive plan been developed. A pilot project could involve:

- The federal government sets a target of funds to be raised immediately. We believe that a FNFA debenture of $500 million would generate a critical mass allowing a number of projects across Canada to move forward.
- The federal government and FNFA agree to the broad parameters of projects to be funded, with an emphasis on emissions-reduction, reliability and sustainability.
- The federal government and FNFA enter into repayment contract that allows FNFA to raise $500 million, and for Canada to provide the annual loan service to FNFA.
- The FNFA solicits proposals from First Nations for projects that can be carried out expeditiously and works with the federal government to approve those projects.
- The FNFA provides the funds to the successful First Nations, which carry out the projects.

A place-based pilot would see the FNFA and the federal government partner to identify communities, or groups of communities, and use Monetization to advance their infrastructure and economic development needs on a wider basis. It would work in a very similar manner but instead of a "theme" such as diesel replacement, the federal government and FNFA would agree to work with one or more communities and use Monetization to fund a mutually agreed upon set of infrastructure or economic development projects.

In either case, Monetization would allow the federal government to see the benefits of immediate investment, without the short-term impact that a "pay as you go" approach would have on current expenditures. The repayments would be predictable and could be incorporated into future budget allocations.

The advantages and disadvantages of Monetization to the federal government

There are numerous advantages to the federal government in a Monetization approach.

1. As noted above, it reduces short-term fiscal pressure on the federal government. A much higher volume of investment can be made at today's prices than is likely under the "pay as you go" approach. As long as the interest rates paid by the federal government to finance Monetization are lower than the inflation rate, it is cheaper than a "pay as you go" approach.
2. It allows the federal government, working with the FNFA and First Nations, to advance policy commitments that have already been made, such as diesel replacement, while taking the pressure off the federal government to develop complex programs and funding mechanisms.
3. In some cases, the nature of the projects will allow the federal government to make repayments from future savings. For example, a diesel replacement program, with the

initial capital outlay made by the FNFA, could be financed by federal savings in supplying fuel to affected communities.

4. The FNFA is a voluntary institution governed by contract law. It is First Nation governed and led, and all member First Nations have agreed to maintain and uphold its terms.
5. Because the FNFA is a voluntary, contract-based system, it is able to include and enforce obligations related to maintenance, upkeep, and operations of facilities so that those facilities meet or exceed their anticipated lifespan.
6. Accelerating development on First Nations will contribute towards meeting Canada's obligations under the United Nations Declaration on the Rights of Indigenous Peoples, particularly Article 21.
7. Utilizing and strengthening a First Nations governed and led financial institution like the FNFA, will contribute towards meeting Canada's obligations under UNDRIP Articles 34 (relating to institutional structures) and 39 (relating to access to capital).
8. A financial partnership like this, with the FNFA and the federal government each bringing unique and complementary strengths, would be a significant achievement towards reconciliation.

The FNFA has had a number of discussions with officials and decision-makers that have identified potential disadvantages to Monetization. We do not believe that any of these are insurmountable, but they also need to be considered by the Committee.

1. While the FNFA has access to low borrowing rates, the federal government can borrow at an even lower rate. We acknowledge this but we believe the disadvantage is outweighed by several of the advantages noted above, particularly the short-term impact on Canada's fiscal position and the ability of the FNFA to impose stricter obligations on participants through contract provisions than the federal government generally can through its grant and contribution programs.
2. Departments do not have authorities to finance expenditures today by booking future savings. This is potentially problematic for a potential diesel replacement pilot where one of the advantages to the federal government is being able to use future savings to allow the FNFA to raise funds today. That being said, we believe that the Privy Council Office (through the Impact and Innovation Unit) can authorize special authorities for line Departments to enable new service delivery methods. We also do not believe that the current lack of a Treasury Board authority is a convincing argument; if Monetization is a good idea, authorities can be evolved to reflect that.
3. There is no identified source of funds. While ISC has around $2 billion a year allocated for capital investments in First Nations, discussions would be needed prior to utilizing some of these funds. While FNFA's membership has grown steadily, approximately half of First Nations are eligible to utilize our services, and we do not want some First Nations to benefit at the expense of others. We believe that, especially at the pilot stage, a specific envelope of funds should be set aside each year for loan service repayment. (The amount required annually would depend on the loan term period agreed between the FNFA and the federal government.)