Indigenous Business Toolkit Project

Legal Structures

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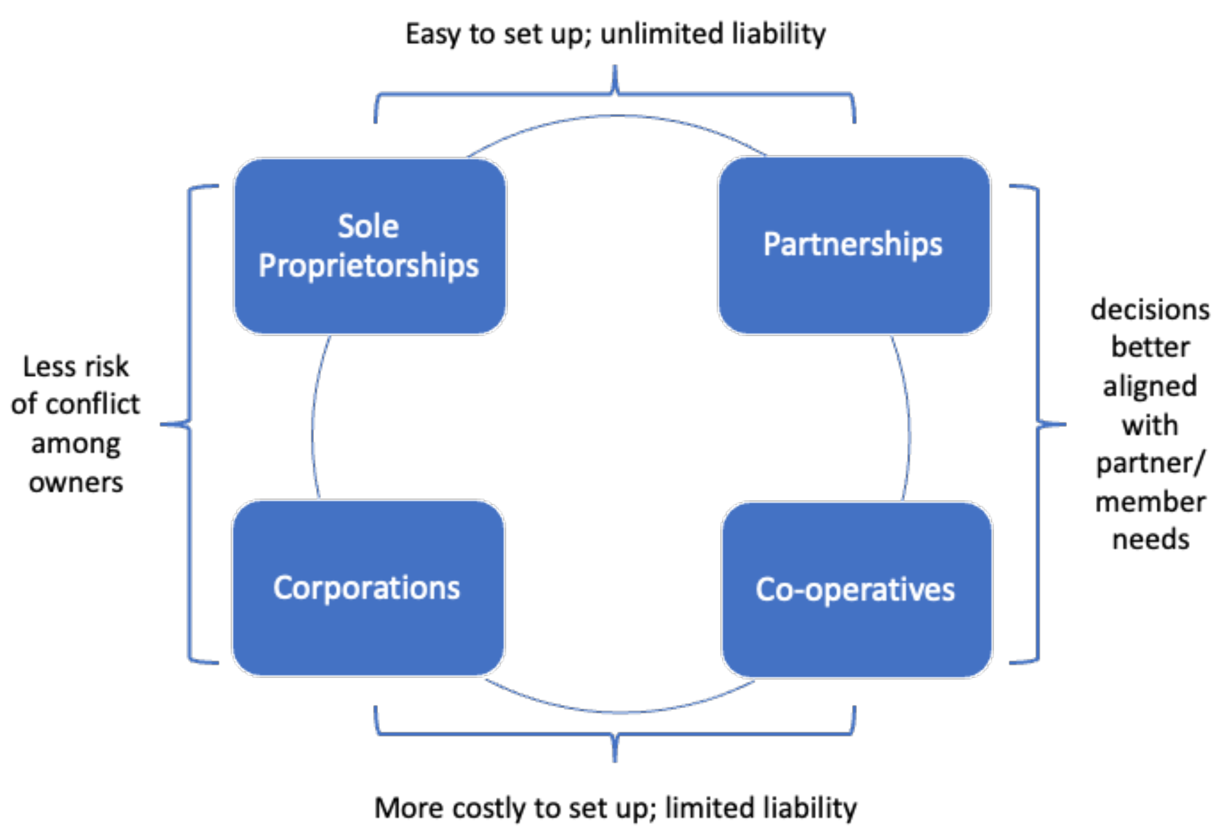
Summary

The purpose of this module is to assist Indigenous Nations in choosing a legal structure for their business. There are four primary legal business structures: (1) Sole Proprietorships; (2) Partnerships; (3) Corporations; and (4) Co-operatives.

The legal structure chosen for a business should be determined by which structure best matches the goals and objectives of the business. The material in this module provides information on the advantages and disadvantages of each structure. The material does not replace the need for professional legal and accounting advice.

The information provided in this module is taken primarily from the SK Startup Institute website.[1] The website is an excellent resource for information on starting a business.



Legal Business Structures

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There are four primary legal business structures: (1) Sole Proprietorships; (2) Partnerships; (3) Corporations; and (4) Co-operatives. The information below outlines the key features and advantages/disadvantages of each structure.

Sole Proprietorship

A sole proprietorship is the simplest and least costly method of establishing a business. However, a sole proprietorship provides no legal separation between the owner and the business entity; the owner assumes full responsibility for all debts and obligations associated with the business. The result is that creditors can make claims against both the business assets and the personal assets of the owner, a condition commonly referred to as unlimited liability.

When Indigenous Nations first got into business, they often used sole proprietorships because of their simplicity and low cost. However, because of unlimited liability, sole proprietorships are the least attractive form of legal business structure for an Indigenous Nation. Because there is no difference between the Indigenous Nation and the business using this model, the Nation assumes all responsibility for business losses and the creditors can go after the Indigenous Nation’s other assets in the event of a business failure. Table 1 summarizes the advantages and disadvantages of sole proprietorships.

Partnerships

A partnership is an agreement where two or more individuals pool their resources to operate a business. Like a sole proprietorship, the business lacks a separate legal identity beyond its owners. To establish business terms and safeguard partners' interests in case of disputes or dissolution, it is advisable to draft a Partnership Agreement with legal counsel. Profits are shared based on the terms outlined in the agreement.

Table 1. Advantages and disadvantages of sole proprietorships

Advantages	Disadvantages
Low initial start-up costs.	Owner personally responsible for all business debts and obligations.
Registration is straightforward with minimal regulatory requirements.	Business lacks continuity in the event of the owner’s unexpected death.
Potential tax benefits for owner, especially during periods of business downturn (e.g., losses can be deducted from personal income).	Conducting international business or engaging with large buyers/suppliers challenging due to the perceived lack of stability and scale
All profits generated by the business directly accrue to the owner.	Expansion beyond the resident province may be restricted, limiting growth.
The proprietor has the option to operate under their own name without the obligation to adopt a separate business identity.	Securing business loans may be difficult, requiring reliance on personal loans and putting personal assets at risk.

In a general partnership, each partner bears joint liability for the partnership's debts. Joint liability, however, can be avoided by using other partnership forms. Limited liability partnerships (LLPs) are used as a way for professionals (e.g., lawyers, accountants, doctors, engineers, and psychologists) to pool their resources while not being liable for negligence on the part of the other partners.

Limited partnerships are used by First Nations and a few northern municipalities to structure their businesses.

Limited partnerships, which are distinct from LLPs (despite the similar name), allow for limited liability for partners who are not active in the management of the business. Limited partnerships are used by First Nations communities and northern municipalities to operate businesses outside their boundaries, to earn income that is exempt from taxation, and to limit the liabilities of the owners.

Limited partnerships are created by a general partner (typically an economic development corporation formed by a First Nation or northern government) and one or more limited partners who contribute capital (the First Nation or northern government is a limited partner). The liability of the limited partners is restricted to the amount of capital they contribute. As a limited partner, however, they cannot participate in the management of the business. Instead, the management role must be carried out by the general partner. While the general partner's liability is unlimited, its ownership is made very small (0.01 percent) and thus its potential loss is very small.

As an example, Misty Ventures Inc. is the economic development corporation formed by Mistawasis Nêhiyawak First Nation. Together, the two entities formed the Misty Ventures Limited Partnership (MVLP). Mistawasis Nêhiyawak is the limited partner, while Misty Ventures is the general partner that operates the business. Through this arrangement, Misty Ventures protects Mistawasis Nêhiyawak from financial liability in the case of business losses.[2]

The module on limited partnerships provides a more detailed explanation of this legal structure.[3] Table 2 summarizes the advantages and disadvantages of partnerships.

Corporations

A corporation is a distinct legal entity separate from its owners, or shareholders. Shareholders typically have limited liability and are thus not personally liable for corporate debts. The corporation is identified by specific suffixes in its legal name, such as "Limited" (Ltd.), "Incorporated" (Inc.), or "Corporation" (Corp.).

The key decision-making entity in a corporation is the board of directors, which is appointed to oversee the business affairs of the corporation on behalf of the shareholders. The board generally does not operate the business, but instead hires key officers like the Chief Executive Officer (CEO), Chief Financial Officer (CFO), and Secretary. Directors can be shareholders or employees of the corporation and may be held personally liable for the legal violations of regulations. Corporations can mitigate this risk by purchasing director and officer liability insurance.

Table 2. Advantages and disadvantages of partnerships

Advantages	Disadvantages
Registration is straightforward with minimal regulatory requirements.	Partners are jointly and severally liable for the debts and obligations of the partnership (unlimited liability)
Potential tax benefits for owner (e.g., losses in downturns can be deducted from personal income).	Finding suitable partners and establishing trust can be challenging, potentially hindering the formation and operation of the partnership.
Business partners contribute additional resources, expanding the pool of available capital and expertise	Conflicts between partners may arise due to differences in opinion, goals, or management styles.
	Conducting international business or engaging with large buyers/suppliers challenging due to the perceived lack of stability and scale
	Business name cannot be reserved outside of the resident province, limiting branding opportunities and expansion prospects.
	Securing business loans may be difficult, necessitating reliance on personal loans and putting personal assets at risk.

Shareholders receive a return on their investment through the payment of dividends. Dividends are paid from after-tax earnings. In addition, dividends are taxed in the hands of the person receiving them. The combined rate of taxation is such that income earned through a corporation is taxed at the same rate as if the income had been earned directly. Shareholders can also be compensated if they work as employees in the corporation. While doing so ensures a stable personal income, it reduces the retained earnings available for reinvestment. Table 3 summarizes the advantages and disadvantages of corporations.

In Saskatchewan, private corporations can be formed by one or more individuals; at least 25% of the directors must be Canadian residents. If none of the directors reside in Saskatchewan, a Power of Attorney in the province is necessary. Private corporations cannot issue shares.

Public corporations, in contrast, distribute shares and securities publicly and are listed on designated stock exchanges. Public corporations must fulfill additional obligations, including filing a prospectus with the Saskatchewan Securities Commission, employing external auditors, and disseminating financial statements and reports.

Businesses, both private and public, can choose to incorporate federally under the Canada Business Corporations Act, which offers the advantage of protecting their business name across the entire country. This means that once a company is incorporated, no other company can use that same name in any province, making it an important option for those operating on a national level or in multiple provinces. However, it's important for federally incorporated businesses to also register in each province where they have significant operations or an office.

Non-profit organizations and condominium associations are required to register as corporations, which helps to formalize their activities and reduce the liability of their stakeholders and directors. Without incorporation, members of a non-profit are personally liable. Additionally, any business looking to own assets like land, vehicles, or stocks, or to hold certain types of insurance policies, must go through the process of incorporation.

Table 3. Advantages and disadvantages of corporations

Advantages	**Disadvantages**
Business is its own legal entity, so owners have limited liability.	High cost to set up.
Business continues even if ownership changes, due to transferable shares and directorships.	Subject to strict regulations including age, decision-making, and residency requirements.
Raising capital is easier, facilitating dealings with big or international companies.	Requires thorough record-keeping, including meeting minutes and annual government filings.
Corporation tax rates are more consistent compared to personal income tax rates	Dividends may be taxed twice (at both corporate and personal levels).

Since corporations are recognized legally as separate entities from their owners, they have a tax status separate from that of their owners. This is an important consideration for Indigenous Nations; while the Nation may be exempt from taxation, the corporations it creates are not. There is an exception, however. If a corporation operates only within the boundaries of the Indigenous Nation, it is exempt from income tax. However, if it goes outside the boundaries of the Nation, then it is subject to income tax.

As discussed above, Indigenous nations and northern municipalities can use a combination of a corporation and a limited partnership to achieve both tax exemption and limited liability. They do so by creating a corporation – typically referred to as an economic development corporation – and then using this corporation as the general partner in a limited partnership in which they invest as a limited partner. In the example provide above, Misty Ventures Inc. is the economic development corporation formed by Mistawasis Nêhiyawak First Nation.

The development of the business corporation was a significant event in the development of the economy of the western world. Corporations revolutionized business by introducing limited liability. Since shareholders only risk the amount they invest, growth and innovation are encouraged. As separate legal entities, corporations can independently enter contracts, own property, and handle legal actions. They also offer perpetual succession, outliving their founders and allowing for stability and long-term planning. The ease of raising capital through issuing stocks or bonds has enabled the funding of large-scale projects. Their ability to pool vast resources and manage them efficiently has spurred technological advances and economies of scale, reduced costs, and boosted economic growth.

Co-operatives

A co-operative is a business where the members both own the business and use the goods and services provided by the business. For example, a co-operative grocery store is owned by the same people that buy groceries from the store. As owners, the members enjoy limited liability – i.e., if the co-op were to fail, the members would only be liable for the amount they have invested. Co-op names often include "Co-operative Limited" or "Co-operative Ltd".

The key decisions in a co-operative are made based on one-member, one-vote. For instance, board members are elected by the membership on this basis. In contrast, the key decisions in a corporation are typically based on one-share, one-vote. While the one-member, one-vote process can slow decision-making, it can often result in a better alignment of decisions with member needs.

Traditional co-operatives emphasize open and voluntary membership, allowing anyone who wishes to use the co-op's services to join. Some co-ops, however, do allow restrictions on membership so that the capacity of the co-op is not exceeded. These co-operatives are referred to as New Generation Co-operatives and operate largely in the agricultural sector.

Co-op members receive a return on their investment through the payment of patronage payments. Patronage payments are made from the co-op's after-tax earnings. If the co-op members are consumers of final goods (as in a grocery co-op), the patronage payments are deemed to be a reduction in the price of the good and are thus not taxed. However, if the co-op members are businesses (as in a fishing co-op or an agricultural input supply co-op), then patronage payments are deemed to be an addition to profits and are taxed in the hands of the business receiving them. The combined rate of taxation is such that income earned through a corporation is taxed at the same rate as if the income had been earned directly. As in a corporation, members can be employed by the co-op. Table 4 summarizes the advantages and disadvantages of co-operatives.

Indigenous Nations have established co-operatives across Canada. In Northern Saskatchewan, the CCF government's development efforts in the 1950s and 1960s resulted in a substantial number of co-ops. Starting with a fishers' co-op in Kinoosao in 1945, by 1969 there were 57 co-ops, including fishing co-ops, retail co-ops, and credit unions, with 4,900 members.

Communities like Pinehouse, Ile-a-la-Crosse, and Stanley Mission continue to operate successful co-op stores, demonstrating co-ops' ability to support Indigenous economies in the region.[4]

Table 4. Advantages and disadvantages of co-operatives

Advantages	Disadvantages
Member-owned and controlled.	Risk of conflict among members.
Decisions better aligned with member needs.	Slower decision-making process.
Limited liability for members.	Member participation crucial for success.
Profits (surplus earnings) distributed to members in proportion to service usage.	Need for thorough record-keeping.

Conclusion

Choosing the right legal structure is crucial when starting a business, since each structure contributes in different ways to help the business achieve its goals and objectives. It is essential to understand and weigh the advantages and disadvantages of each business structure to determine which best aligns with the businesses' goals. As the business interests of Indigenous nations become larger and more complex, it is increasingly important to choose the right business structure.

Resources

Bachiu, V., M.E. Fulton, and K. Jackson. 2024. Limited Partnerships. Indigenous Business Toolkit Project. Johnson Shoyama Graduate School of Public Policy, University of Saskatchewan. https://www.schoolofpublicpolicy.sk.ca/research-ideas/projects-and-labs/indigenous-leadership-governance-and-development-project.php.

Beveridge, D. 2024. Co-operatives, Northern. Indigenous Saskatchewan Encyclopedia. Retrieved from https://teaching.usask.ca/indigenoussk/import/co-operatives_northern.php.

SK Startup. (2024). Choosing a business structure. Retrieved from https://skstartup.ca/guides/starting-up/choosing-a-business-structure/.

White, K. and M. Fulton. 2022. Ile-a-la-Crosse Co-op Case Study. Indigenous Leadership: Governance and Development Project. Retrieved from https://www.schoolofpublicpolicy.sk.ca/documents/research/case-studies/ile-a-la-crosse-case-study.pdf.

Wolf, P, V. Bachiu, and M. Fulton. 2023. Misty Ventures Case Study. Indigenous Leadership: Governance and Development Project. Retrieved from https://www.schoolofpublicpolicy.sk.ca/documents/research/case-studies/misty-ventures-case-study.pdf.

Notes

[1] See SK Startup (2024).
[2] See Wolf, Bachiu, and Fulton (2023).
[3] See Bachiu, Fulton, and Jackson (2024).
[4] See Beveridge (2024) and White and Fulton (2022).

Indigenous Business Toolkit Project

The Indigenous Business Toolkit Project is designed to provide Indigenous communities and individuals with the practical tools they and their advisors can use to undertake successful economic development. Indigenous economic development is more successful when everyone – community members, community leaders, consultants, business professionals, employees, and/or potential partners – understands its many aspects.

The Toolkit provides step-by-step instructions on selected aspects of economic development based on the best practices of leaders in the field. The modules in the Toolkit cover everything from the role of economic development in nation building, to the importance of business charters, to the various legal forms that can be used to pursue economic development, to the steps needed to identify and negotiate beneficial partnerships, to the governance challenges that economic development must address.

The modules are available for free and for use by anyone. The full set of Toolkit modules can be found at: https://www.schoolofpublicpolicy.sk.ca/research-ideas/projects-and-labs/indigenous-leadership-governance-and-development-project.php.

The Indigenous Business Toolkit Project is part of the larger Indigenous Leadership: Governance and Development project designed to support long-term Indigenous economic development. In addition to the toolkit, the larger project involves capturing the economic development experience of Saskatchewan Indigenous communities through a series of case studies. The case studies, along with a description of the larger project, can be found at the website listed above.

Disclaimer

The information contained in this document is designed to provide an overview of a particular topic and should not replace legal and other expert advice. Groups wishing to use the concepts discussed should receive the appropriate professional advice necessary to ensure their specific goals and circumstances are considered and recognized.

The Authors

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