



Indigenous economic development in Canada: Confronting principal-agent and principal–principal problems to reduce resource rent dissipation



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ABSTRACT

In Canada, indigenous communities have strengthened de jure and de facto rights over the last generation, thereby enabling them to realize substantial resource rents and other economic development income. Canadian First Nations (the preferred name for most indigenous communities) have in recent years established over 200 economic development corporations, many of them hybrid organizations partnering with non-Aboriginal resource corporations. We analyze the challenges of institutional design of such hybrids, employing the concept of fractionalized ownership. We discuss principal-agent problems at two levels: First Nation members relative to their leaders, and leaders relative to managers of economic development corporations. We also analyze principal-to-principal problems that arise with multiple owners. Using a sample of Ontario First Nation communities, the empirical section analyzes the impact of own-source revenue (much of it derived from resource projects) on a socio-economic index. The main conclusion is that incremental own-source revenue improves community socio-economic conditions, but only modestly.

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1. Introduction

The Canadian government forecasts that over \$700 billion worth of natural resource projects will occur in Canada in the 2016–2026 decade (Natural Resources Canada, 2016). Indigenous Canadians¹ are now acquiring significant, although not yet clearly specified, property rights to a significant share of the potential resource rents that should arise from these projects. But, much global evidence shows that governments and related institutions find it difficult to avoid at least partial resource rent dissipation: the “resource curse” (Collier, 2010; Frankel, 2010; Corrigan, 2014).

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¹ The Canadian indigenous population consists of three groups. First Nations are those who identify as members of an indigenous tribe, such as Cree, Ojibwa or Algonquin. Most of these individuals are registered as Indians pursuant to the Indian Act, an oft-amended Canadian law dating from 1876. Métis are those who identify as descendants of intermarriage in the 18th and 19th centuries between indigenous women and European men, most of them fur traders or early settlers. The third group is Inuit; most still reside in Arctic Canada. “Aboriginal” is generically used to designate members of any of these peoples in constitutional law (*The Constitution Act 1982*, s.35). “Indigenous” is increasingly used as equivalent to aboriginal. The term aboriginal or indigenous can also designate communities of First Nation or Métis residing on designated reserves.

Even if indigenous groups do avoid or contain dissipation, most find it extremely difficult to ensure that the income captured, either as rent accruing to the indigenous government or to some indigenous members as employment income, benefits the indigenous community residents overall, rather than their various “agents” and a select few (Allard, 2002; Altman, 2004; Graham, 2012).

The process of indigenous resource rent capture often requires the creation and management of indigenous-controlled economic development vehicles: economic development corporations (EDCs). In turn, EDCs or their subsidiaries frequently partner with non-indigenous corporations, which can provide valuable human resources, expertise and capital (Anderson, 1997; Anderson and Parker, 2009). The potential benefit to indigenous community residents of resource rents could be substantial if indigenous and non-indigenous governmental institutions and their economic organizations can avoid or minimize the various institutional problems that can contribute to rent dissipation (Grossman and Hart, 1983; Krepps and Caves, 1994; Dixit, 2002; Young et al., 2008; Ross, 2015).

After reviewing some contextual history relating to the evolution of indigenous property rights and economic development, the paper presents both a theoretical framework and empirical

evidence germane to indigenous resource rents. The theoretical framework categorizes, specifies and discusses many of the institutional principal-agent and principal-principal problems that indigenous groups must confront in order to avoid or reduce rent dissipation (Duncan, 2003). The empirical multivariate analysis examines some aspects of these institutional challenges in the context of a sample of 64 First Nation communities in the province of Ontario. This empirical evidence focuses on the relationship between perceptions of well being in these communities and aspects of their fiscal situation arising from resource rents and other own-source revenue.

2. Indigenous property rights and resource rents

2.1. Indigenous property rights

As “settler” societies occupied indigenous lands and established new institutions, indigenous peoples in some countries retained some *de jure* property rights and management of local government. However, in almost all countries, *de facto* indigenous rights suffered continuous erosion, at least until the second half of the 20th century. In Canada, Australia, the United States, Scandinavia, New Zealand, Latin America and elsewhere this erosion is to an extent being reversed (Cairns, 2000; Wilkins and Lomawaima, 2001; MacKay, 2004; Ortiga, 2004; Söderholm and Svahn, 2015).

In Australia, for example, governments have instituted indigenous resource rent payment regimes (“royalties”) without necessarily addressing or altering formal property rights (Martin and Tran-Nam, 2012). In Canada, the judiciary has played a crucial role in mandating, enforcing, specifying and enhancing these rights, though the legal scope of these enhanced rights remains unclear and contested. More effective property rights have enabled members of Canadian indigenous communities to participate in economic development, primarily through the exploitation of both renewable and non-renewable natural resources situated on their lands or traditional territories. The potential for significant resource-based development was enhanced by the post-2000 rise in mineral and petroleum prices. Recent resource price declines have obviously reduced expectations, in First Nation communities as elsewhere (Söderholm and Svahn, 2015). A more sympathetic view of indigenous treaty claims by the broader society and an increase in the indigenous population's demographic weight, particularly in western Canada, have also contributed to a greater willingness to share resource rents with indigenous communities. But much evidence demonstrates that resource rents are a mixed blessing; they may degenerate into the iconic “resource curse” (Cornell and Kalt, 2007; Parlee, 2015).²

Enhanced property rights to natural resources require difficult decisions and present institutional challenges (Duncan, 2003). Many indigenous communities are interested in these commercial ventures only if they involve active indigenous participation in equity ownership and local employment. Even then, indigenous communities are often ambivalent about resource development on their lands because it involves tradeoffs between income and traditional cultural values. Despite ambivalence, many indigenous communities in Canada have decided to participate in at least some natural resource projects within their traditional territories,

if they can “get their price”. If they do undertake resource development, how should they organize it? If they partner with non-indigenous corporate owners in “hybrid” organizations, which they often must do, how should it be done? For example, what are the likely consequences of the goal conflicts that arise between owners? More specifically, what should be the institutional structure of agreements with non-indigenous property right holders, as well as with those agents who provide complementary managerial and technical skills? There also arise questions pertaining to relations between and within indigenous communities. Accountability issues arise between indigenous community members and their elected governments or appointed managers.

2.2. Indigenous economic development and economic development corporations

Indigenous economic development corporations (EDCs) are not typical private corporations maximizing income on behalf of owners. The Canadian Council for Aboriginal Business (CCAB) provides a broad definition of EDCs as: “community-owned corporations [that] invest in, own and/or manage subsidiary businesses with the goal of benefiting the Aboriginal citizens that they represent” (Canadian Council for Aboriginal Business CCAB, 2015: 3). The definition appropriately (in our view) focuses on the collective ownership aspect of EDCs and their investment in subsidiary businesses, which may in turn invest in hybrid firms having multiple equity owners.

There is very limited empirical evidence on the behavior or performance of indigenous EDCs that partner with non-indigenous entities. In these hybrid ventures, ownership is formally shared with non-indigenous actors. Recently, a government-appointed group of indigenous leaders released a report that summarized these challenges as follows:

... even with revenues flowing to communities, agreements between Aboriginal groups and the private sector or other levels of government are no guarantee that a community will reach economic prosperity and self-sufficiency. There are many reasons for this, including: resource opportunities creating dependence on a single, and often volatile, revenue stream; management systems being overwhelmed by a large influx of revenues; and chronic underfunding of many services and programs placing pressure on Aboriginal governments and their decision-making processes (National Aboriginal Economic Development Board (NAEDB), 2015: 4).

Below we shed some empirical light on the issues by analyzing the financial reports of 64 First Nation communities in the province of Ontario, Canada. Our premise is that both efficient institutional and organizational design and the effective structuring of organizational governance mechanisms are likely to be as important to efficient and equitable resource rent extraction as are cost-effective technology, incentive-compatible taxation and effective national legal and political governance (McGinnis, 2016).

3. Fractionalized property rights and hybrid organizations

3.1. Hybrids

When indigenous communities partner with other corporate entities, public or private, they create a “hybrid” organization. Hybrids typically have characteristics of both private sector organizations that pursue profit and public or quasi-public organizations that pursue some broader collective goal. Over the last two decades, hybrids as an organizational class have experienced explosive growth around the world (Hodge et al., 2011). Hybrids include “social entrepreneurship” organizations (formally “for-

² Provided it is not actually inaccurate, we use the term “indigenous” communities until the empirical section. Although practice varies and some prefer “aboriginal”, indigenous now appears to be the preferred term of most of these communities. However, where a different terminology is clearly more informative and/or more accurate we change to the more appropriate terminology. In the empirical part of the article, we use the term First Nations because none of these Ontario communities are Métis or Inuit.

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