

CONTINUING LEGAL EDUCATION

FIRST NATION FISCAL & WEALTH MANAGEMENT COURSE

**FIRST NATIONS WEALTH MANAGEMENT
THROUGH GOOD GOVERNANCE**

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I. Introduction

Changes of historic proportions are taking place in aboriginal communities across Canada with the creation of Trusts resulting from Specific Claims Settlements, Economic Development, Impact Benefit Agreements and other resource sharing opportunities. From our existing relationships across Canada, we know that the resulting income and capital generated from within these Trusts have the potential to transform a community into an economically self-sustaining and self-governing entity, but only when managed effectively. We also recognize that the opportunity can easily be lost, especially if the community and its leadership are not equipped or prepared for the coming change. As a result, a Trust indenture should provide a Trustee with the opportunity to apply excellent stewardship through sound governance, while defining the division of power through established mechanisms to achieve accountability amongst stakeholders.

II. Changing History

Across Canada, the receipt of settlement proceeds in aboriginal communities is bringing with it opportunities, as well as challenges. As we have discovered, effective stewardship of this newfound wealth requires much more than prudent investment management. It requires specific provisions which address the investment of the Trust property. At a minimum these provisions should:

- require the Trustee and/or Council to obtain qualified, independent investment advice;
- require the development of an investment policy statement;
- clearly provide as to who can be retained to invest the Trust property; and
- in a very general way set out the type of investments in which the Trust property can be invested.

III. The Players - Investment Management

Generally, there are two types of firms that want to provide investment management services to First Nation and First Nation Trusts. The broad categories of registration are Dealer and Advisor. The dealers will include investment dealers and mutual fund dealers. Advisors are firms that actually manage the investment portfolios.

Dealers

Dealers

Investment Advisors

Dealers are distributors of investment products created and managed by others. They are the intermediary who is responsible for client contact and services. Individual circumstances will determine whether a fiduciary or contractual duty of care is owed to the client.

Advisors manage portfolios on a discretionary basis and report directly to clients. There is no intermediary involved. This type of advisor has a fiduciary duty of care to their clients.

Each First Nation must determine which type of firm is most appropriate to their needs. If it is determined that there is value in ensuring that the investment manager owes a fiduciary duty of care, then firms registered as Advisors will be preferred over firms registered as Dealers.

While Trustees do not absolve responsibility by using discretionary advisors, it can be suggested that by doing so, a degree of personal liability has been reduced. Not only does the use of discretionary advisors reduce the day to day involvement of the Trustees but utilizing discretionary advisors can be viewed as a prudent level of delegation under the definitions surrounding "*standard of care*" within the provincial *Trustees Acts*.

Of course, this is on the basis that you are putting the security selection process in the hands of a professional and proven investment management firm to use their experience and knowledge to make appropriate and reasonable decisions surrounding the management of the Trust mandate.

IV. Investment Consultants or Financial Advisors

These can go by many names; Asset Management Consultant, Financial Advisor, Investment Consultant and Investment Analyst. They typically have been awarded a CFA designation which is a globally recognized designation.

Their area of specialization and role is in evaluating investment managers' performance, developing investment policy statements and conducting manager

searches. Their primary purpose is to provide objectivity, independence and investment expertise.

“**Consulting**” is not a regulated industry so it is buyer beware and considerable due diligence should be completed before entertaining retaining a Consultant. These individuals and firms range from the one person show to large international firms.

V. Good Governance Documents - Investment Policy Statement

As previously stated, a Trust indenture should provide a Trustee with the opportunity to apply excellent stewardship through sound governance; while defining the division of power through established mechanisms to achieve accountability amongst stakeholders.

If we all agree that good governance is through an established structure used to effectively administer the Trust, and that the Trust Agreement is the key governance document, and then we should be able to agree it is not the only governance document you need to manage a Trust. It is simply not practical to have all of the governance structures incorporated into the body of a Trust agreement.

Within the Trust agreement, there should be a requirement to develop an Investment Policy Statement before any investing can take place. The standard practice is for authorized investments to be invested in accordance with the Prudent Investor Standard. This standard requires that consideration be given to the unique needs and objectives of the First Nation.

An effective Investment Policy Statement defines the overall Trust framework for investment. It provides details on who is responsible for which actions, the investments the Trust may undertake, the reporting process for Trust investments and the acceptable standards for performance. It should be a comprehensive document and provide substantial detail.

Since this is a key governance document for the investing function of the Trust it should always be a document of the Trust. It is not a document of the investment manager. Meaning, the first task of the Trustees is to translate the purposes of the Trust, as defined in the Trust agreement, into an Investment Policy Statement.

Today’s Investment Policy Statements are highly technical documents that should not be developed by the investment manager who has been retained as the discretionary manager. Time and effort should be applied to come up with a methodical method of establishing the following requirements:

- definitions
- overview

- responsibilities
- conflicts of interests
- fund objectives
- asset allocation
- fund investments
- investment risk
- voting rights
- **compliance & performance monitoring**
- repercussions

Like all good governance documents, there should be some level of review and oversight provisions. These two areas need to be covered not only in the Trust deed but in the Investment Policy Statement.

VI. Investment Advisors Searches

In today's economy of sophisticated investment options and investment management firms the selection, interviewing of investment management firms and monitoring of Trust property is a crucial part of good governance practices. If the Trust directs the First Nation to work in conjunction with the Trustee and an investment consultant to retain an investment manager it is highly likely that you can expect the Trustee to restrict the search for a manager to firms registered as Advisors rather than Dealers.

These firms are engaged in only one business: the management of client portfolios. There are a number of reasons for this but the primary one is that these firms have measurable track records from real accounts, they do not have conflicts of interests between the manufacturing and distribution of products, the execution of trades or the underwriting functions. Also, the client service representatives who deal with clients will normally hold the CFA designation.

The average size of Specific Claim settlements in Canada in the past year ranged from the low \$21 million to the high \$125 million. With this kind of wealth surfacing there are many purveyors of financial services, all of whom will have a good story to tell. It is an intensely competitive industry. The responsibility for sorting through the muddle is that of the Trustee. Hence, the need for qualified assistance coupled with an organized search that focuses on four key areas:

The four P's being:

- People
- Process
- Portfolio Construction

- Performance

VII. Custody of Trust Property

Ever heard of Bernie Made-Off?

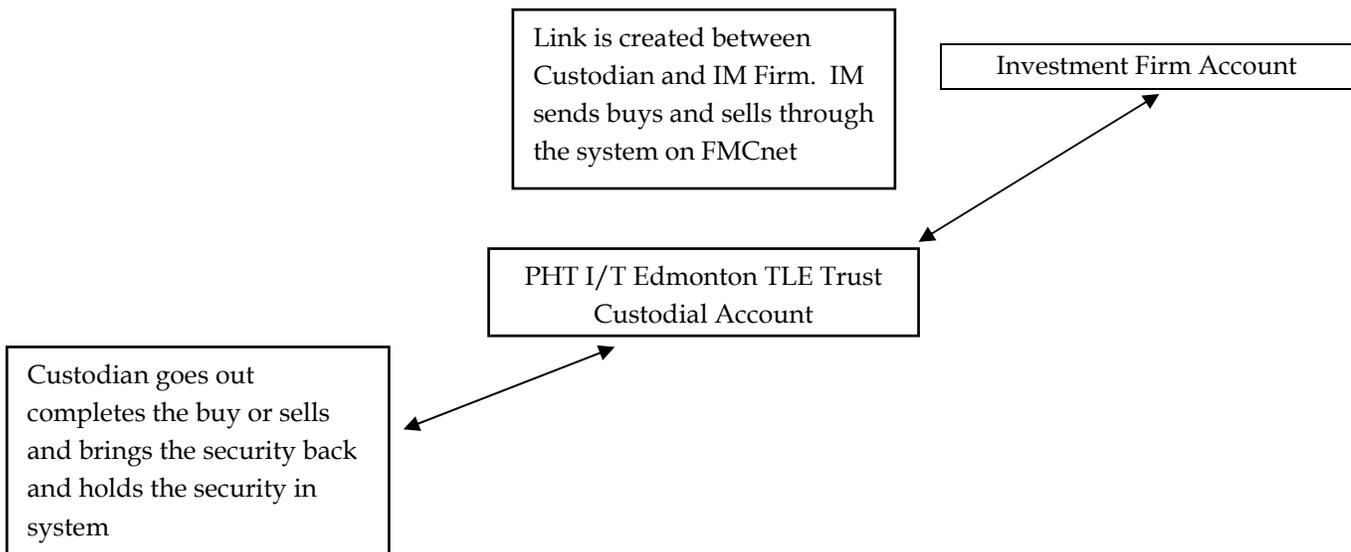
A bank cannot act as a custodian. To do so, the bank would literally have to place the physical assets in a vault. Only a trust company can act as a custodian in order to meet custodial requirements.

Legality

Waters Laws of Trust clearly defines the legality surrounding custody:

“The object of the Canadian federal and provincial legislation on this subject in addition to setting out a corporate framework, is to ensure that trust companies discharge their duties as laid down by the law of trusts in a strictly fiduciary manner, trust funds and trust management being disassociated by existence of the trust company concept from the creditor-debtor relationship and the conduct of banking operations. In particular, trust assets must be segregated and ear-marked”.

Custodial Structure



Currently, there are many incidents where Community Trustees are holding custody with external Investment Management firms. The challenge under this arrangement is the transfer of assets on termination of a particular manager. Over the past few years

there have been a number of cases where the Trustees have had to sue or involve the regulator industry to regain custody of Trust property.

VIII. Good Governance Documents – Leadership, Trustee(s), Advisors

The greatest challenge surrounding the administration of any Trust is the division of duties and clarity of decision makers. Then add to the equation potential conflicts of interest between advisors for the Nation and advisors for the Trust. Governance challenges can and do occur on a regular basis.

So the question is, how do we avoid these challenges and how do we apply excellent stewardship through sound governance, while defining the division of power through established mechanisms to achieve accountability amongst stakeholders?

I believe the solution is to address each party's role within the governance document in order to ensure that mechanisms are put in place to achieve accountability.

A clear example of this change in accountability over the past few years is in the area of who qualifies as the auditor. Recent Trusts define: "**Auditor**" means an auditor appointed by the Trustee, in consultation with Council, to prepare the audited financial statements of the Trust and who is independent of the Nation and the Trustee".

This definition clearly establishes who appoints the auditor, who is consulted and a mechanism to avoid conflicts.

Another area of challenge is associated with defining roles within the area of the investment of Trust property. If we all agree that the success or failure of the Trust is through the financial performance then are we not looking at clearly defined governance that will assist the Nation and the Trustee(s) in providing accountability to the stakeholders?

Recent governance documents clearly define who retains, who is consulted and a mechanism to avoid conflicts.

AUTHORIZED INVESTMENTS AND INVESTMENT MANAGERS (Actual Clauses in Use)

- a. Within ninety (90) days of the effective date of this Trust, the Trustee shall retain one or more Investment Managers selected by Council in consultation with the Trustee, and enter into Investment Management Agreements which are consistent with this Trust Agreement.

- b. The Trustee is authorized and empowered to delegate the ability to make decisions on the types and timing of the purchase and sale of Authorized Investments to the Investment Manager, provided the Investment Policy has been developed and the Investment Manager(s) enter into a Investment Management Agreement with the Trustee which are consistent with the Investment Policy and this Trust agreement.
- c. With the assistance of the Trustee and input from the Investment Manager, Council shall develop an Investment Policy that is consistent with this Trust agreement. Until the Investment Policy has been developed, the Trustee shall be permitted to purchase only those Authorized Investments listed in Part I of Schedule "A". Council may amend the Investment Policy from time to time with the assistance of the Trustee and with input from the Investment Manager.
- d. The Trustee shall review the terms of the Investment Management Agreement and Investment Policy and advise the Council and the Investment Manager of any conflict between the Investment Management Agreement and the Trust agreement.
- e. The Trustee shall obtain from the Investment Manager a quarterly report documenting the list of investments and the rate of return and confirming that the investments acquired with funds from each of the Trust Accounts comply with Schedule "A" or the Investment Policy and forward same to the Council.
- f. The Trustee shall satisfy itself that the investment of funds from the Trust Account by the Investment Manager complies with Schedule "A" or the Investment Policy and notify the Council and Investment Manager of any non-compliance.
- g. The Trustee, or any agent hired by the Trustee upon approval of Council, will hold Authorized Investments in accordance with industry standards.
- h. Upon receipt of a Council Resolution so directing, the Trustee shall cause to have evaluated the performance of the Investment Manager against industry

standards for portfolios with similar policies, objectives and investment guidelines and advise the Council of the results. If the Council does not issue a Council Resolution requiring the annual evaluation the Trustee shall ensure that such evaluation is conducted at least once every four years.

IX. Conclusion

There are many issues that a Nation needs to consider in developing a Trust agreement. Much thought and time needs to be taken in developing a sound governance structure in order to avoid unnecessary conflicts.

Appendix: Sample Clauses Good Governance

“Authorized Investment” means an investment in securities purchased with funds from the Trust Account, from those investments listed in Schedule “A” and in accordance with this Agreement.

“Beneficiary” means, for the purposes of this Agreement, _____, including all Members of _____ on a collective and undivided basis, as represented by its duly elected Council.

“Effective Date” means the date this Trust becomes effective, that being the date on which the first moneys are deposited to the Trust Account.

“Investment Manager” means a firm or individual that is a member in good standing, and has been in good standing for at least 5 years, with the Investment Industry Regulatory Organization of Canada or an equivalent body, that is a member of the Canadian Investor Protection Fund or an equivalent body and that has obtained registration with the Alberta Securities Commission as an advisor in the category of Investment Counsel Portfolio Manager in accordance with National Instrument 31-103 7.2(1)(a) as the term is amended from time to time, and whose revenue is derived from the discretionary management of investment portfolios.

“Investment Management Agreement” means an agreement between the Trustee and an Investment Managers which has been approved by Council, by which the investment management responsibility for funds in the Trust Account is vested with the Investment Managers, not the Trustee, and to be undertaken, pursuant to the terms of this Trust Agreement and the Investment Management Agreement.

“Investment Policy Statement” means the policy approved, from time to time by Council and the Trustee, which sets out the policy, objectives, and framework for the investment of funds in the Trust Account in Authorized Investments by the Investment Managers pursuant to the terms of this Trust Agreement in accordance with Schedule “A”.

“Investment Consultant” means a firm or individual whose primary business is providing independent advice on the development of the Investment Policy and selection of Investment Managers and evaluation of portfolio performance and whose staff have been awarded the Chartered Financial Analyst designation and the Investment Consultant, and all related companies, shall undertake in writing to not sell investment products to this Trust, nor to provide investment services to either the Trustee or the Investment Manager, such undertaking to be updated annually and upon any material change in corporate relationships of the Investment Consultant.

SCHEDULE “A”

AUTHORIZED INVESTMENTS

PART I

1. Debt instruments issued or guaranteed by the Government of Canada, a Province of Canada, or a Municipality of Canada, or mutual or pooled funds investing in these debt instruments, all of which shall have a term not exceeding three years.
2. Debt instruments issued or guaranteed by any Canadian Schedule 1 Chartered Bank or Canadian Trust Company including bankers' acceptances including mutual or pooled funds thereof investing in these debt instruments, all of which shall have a term not exceeding three years.
3. Mortgage backed securities guaranteed by the Government of Canada, an agency of the government of Canada, or one of the chartered banks or trust companies, including mutual or pooled funds thereof investing in these securities, all of which shall have a term not exceeding three years.
4. Commercial paper issued by corporations rated R-1 or A-1 by the Dominion Bond Rating Services or Standard and Poors Bond Rating Services including

mutual or pooled funds thereof investing in commercial paper, all of which shall have a term not exceeding three years.

5. Corporate Bonds rated A or better by the Dominion Bond Rating Services or Standard and Poors Bond Rating Services including mutual or pooled funds thereof investing in these corporate bonds, all of which shall have a term not exceeding three years.

PART II

Upon the development and implementation of an Investment Policy Statement, any investment that complies with the Prudent Investor / Prudent Portfolio Standard but not limited to common or preferred shares and any or all other debt or equity-like instruments, including derivatives, which take into consideration the following factors:

- 1) General economic conditions;
- 2) The possible effect of inflation or deflation on the investments;
- 3) The expected tax consequences of investment decisions or strategies;
- 4) The role that each investment or course of action plays within the overall Trust portfolio;
- 5) The expected total return from income and appreciation of capital;
- 6) The needs for liquidity, regularity of income, and preservation or appreciation of capital;
- 7) An asset's special relationship or special value, if any, to the purposes of the Trust or to one or more of the beneficiaries; and
- 8) Should the Investment Managers deem it in the best interests of the Nation and the Trust to purchase or retain shares in a financial institution or its affiliates, the Client hereby authorizes this purchase of, or retention of shares notwithstanding any connection between the financial institution or its affiliates and the Trustee. The Trustee, its successors and assigns, are hereby released, discharged and indemnified, from any liability to which the Trustee may become subject to as a result of such authorization and direction to retain or purchase shares in a related financial institution or its affiliates. It is acknowledged that the Trustee

shall not be held responsible for any loss resulting from the retention or purchase of such shares. The Trustee is authorized to charge fees as agreed in respect of these shares.