Building Indigenous Capital:
Removing obstacles to participation in the real economy

Drawing on the work of Peruvian economist, Hernando de Soto, this paper outlines the obstacles to Indigenous capital formation, the impact of this in Australia and the need for a solution. The solution is not about a uniform surrender of underlying title but about finding solutions that increase the fungibility of Indigenous-owned assets within the constraints of inalienability. These may take the form of simplifying the requirements for long-term leases or licences, exploring the potential of ILUAs, and addressing the most basic stumbling block: the problem of home ownership. Each of these require discrete attention, and will be a focus of research and policy development work by the Cape York Institute for Policy and Leadership. At a broad level, *Building Indigenous Capital* will address the administrative and legal structures required to facilitate the participation of Indigenous people in the mainstream economy.

1. Introduction

A key structural problem faced by many Indigenous people, particularly those living in remote communities, is the fact that they live in a welfare economy outside the mainstream Australian (real) economy.[1] The passivity bred by this welfare economy, and the adversarialism which pervades the native title system, are in themselves damaging incidents of an isolation from the real economy. This isolation is cemented, however, by specifically Indigenous landholding structures. These structures prevent many Indigenous people from leveraging their asset base in order to build capital: in remote Indigenous communities, you can't borrow against your own house because the land is either inalienable or the government owns it. Participation in the real economy is not, in practice, a choice available to many Indigenous people.

New and refreshing light has been cast on the mechanism of capital formation by Peruvian economist Hernando de Soto in relation to Third World and former communist countries, in his book, *The Mystery of Capital: Why Capitalism Triumphs in the West and Fails Everywhere Else* (Bantam, 2000). While de Soto's work does not deal with the specifically Indigenous situation, his insights are directly relevant: the reason that Indigenous Australians are unable to build capital is that they lack the necessary proprietary legal infrastructure to leverage the assets that they do have. What many Indigenous Australians have in common with the poor living in countries studied by de Soto is that the form of property they have is not conducive to participation in a transactional economy.

For the last 20 years, de Soto and his organization, the Institute for Liberty and Democracy (ILD), have been working with governments around the world to address the problem of capital formation. Yet the implications of his work for Indigenous Australians are yet to be thoroughly considered. This is a lacuna that needs to be addressed. Creative policy development and legal thinking are required to formulate

[1] The authors would like to thank Sean Brennan for his assistance in the preparation of this paper.

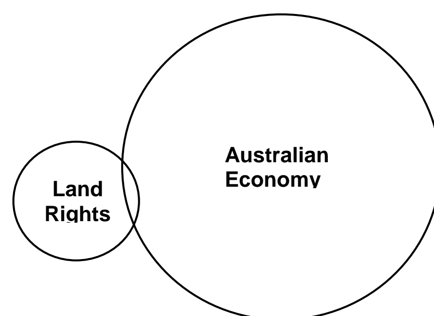
effective structures that can co-exist with inalienable Indigenous title to land. What is needed is an intelligent compromise, informed by an awareness that cultural preservation and integration into the mainstream economy are not immutably opposing forces.

Such a compromise will create a situation where individual effort has a chance of being rewarded: there is no real incentive for individuals to pursue economic growth, and no practical use for business and leadership skills, if the obstacles are so great as to make success virtually impossible. The structures that enable people to build assets, create capital and thereby gain financial security need to be in place. We need to create a pathway out of the welfare economy.

This paper elucidates a problem and suggests ways forward. *Building Indigenous Capital* is a critical part of the integrated research and policy program being pursued by the Cape York Institute for Policy and Leadership.

2. The problem of 'dead capital'

At the moment, the relationship between the Indigenous economy/asset base and the mainstream economy can be represented like this:



The majority of Indigenous assets exist outside the Australian economy. They are, in de Soto's words 'dead capital', because they cannot be leveraged to *create* capital.

Indigenous communities living on Indigenous lands (though we own 'property') are locked out of the Australian property system that enables capital formation. All of our assets, in the form of lands, housing, infrastructure, buildings, enterprises etc are inalienable and, as a result, have no *capital* value. They cost huge amounts of money to develop, to replace and to renovate – but they have no capital value. Billions of dollars transferred from government to Indigenous communities ends up in the form of dead capital. We end up in a dead capital trap – a poverty trap.

The insight to be drawn from de Soto's work is that while the inalienability of Indigenous title to land is an important factor in explaining this situation, it is not the only one. De Soto looks to mundane legal and regulatory mechanisms to explain why much of the world's poor are trapped in the 'extra-legal' economy. What he identified were barriers to entry into the real economy: the virtual impossibility of getting property and businesses registered, for example. These mundane legal structures (structures so taken for granted in the West that we have lost the memory of their evolution) are absolutely fundamental to economic life: they provide the **certainty and security of transaction** required to oil the wheels of a capital driven economy. These legal structures enable assets to be represented and transacted in

abstract forms – forms which can be leveraged, divided and combined to create capital. They become 'fungible'. A bank in Sydney, for example, can easily look up the Land Titles Register to ascertain the owner, bounds of, and any encumbrances on a property, allowing them to establish the value of the property. By holding the certificate of title – an abstract representation of the property – they can cover their lending risk. No such systems exist in the extra-legal economy.

a. The Indigenous Position

If we look at the situation of many Indigenous communities in Australia, we find a situation similar to the one de Soto identifies in Third world countries. The legal structures for Indigenous land and asset holding are so complex as to present an effective barrier to entry into the mainstream economy. The laws that govern our property and asset ownership (State lands legislation, native title legislation, Indigenous Land Corporation legislation, ATSIC legislation) make our assets un-fungible – beyond the protection of inalienability. Land title-holding structures are unnecessarily complex and inefficient so that they make it too difficult to leverage value out of our assets. Two owners for one area of land (say Land Trusts holding inalienable freehold title to land and Prescribed Body Corporates holding native title to the land) make the land un-amenable to capital formation. Inefficient property law unique to Indigenous people reduces valuable assets into valueless capital.

If, for example, the Cook Shire Council receives a government grant to construct a public building, that building is a capital asset that is fungible: it can be leveraged to create capital. It can be represented as property to secure mortgages or other means of capital raising. The Cooktown building has value beyond its use as a public building – it can perform other functions as capital. But if the Hope Vale Aboriginal Council constructs a similar building – the building is 'worthless' beyond its use as a public building. It cannot be used to secure a loan or otherwise raise capital.

b. An Individual Example

The problem faced by individuals can be elucidated by a hypothetical example. Say a resident of Hopevale wanted to set up a business within the township – a bakery. In addition to the ordinary legal and administrative steps required to set up a business, that person would have additional hurdles because of the multiple layers of law under which their community holds the land. The complexity of the legal structures and the number of ambiguous legal questions that arise out of these structures introduce uncertainty which is, in itself, a barrier to participation in a transactional economy.

In order to set up a business, and to be able to gain finance, the individual needs a most basic building block: security of tenure. They could not buy a piece of community owned land to set up a business on, so they would have to lease it from the trustees of the land, in the case of Hopevale, those appointed by the Minister under the DOGIT (Deed Of Grant In Trust).

i. Securing a lease

Under the *Land Act 1994* (Qld) which governs DOGIT land, the trustees would require 'in principle' approval from the Minister and then her endorsement of the lease. Once endorsement is given the lease must be registered under the Act (s 57, *Land Act*). If the lessee wants to mortgage the land in order to raise capital, they need

both trustee and ministerial approval (s 58, *Land Act*). This approval is given based on whether the transaction is consistent with, and would facilitate or enhance, the purpose of the trust (s 59, *Land Act 1994*). This creates the possibility of conflict between the aims of individuals and the communal purpose of the trust, or between Minister and the trustees. For example, Canadian courts have held leases to be invalid where Ministerial consent was given but the concerns of the band council were not adequately addressed by the Minister.[2] This is not to mention the fact that a mortgage on a lease, even a long-term lease, is less valuable than freehold and that the lessee may find it difficult in practice to secure a mortgage over the property.[3] Research in Canada has shown that Native Americans living on reserves have struggled to secure mortgages on leases within the reserve, even where the government has set up a bank 'of last resort'.[4] The situation in Australia is not entirely analogous – the legislative regimes are not identical – but there are sufficient similarities (underlying inalienable title, limited permitted dealings with land) to suggest that similar problems may be faced in Australia.

While DOGIT land was meant to be transferred to communities under the *Aboriginal Land Act 1991* (ALA), thirteen years later, this transfer has not occurred. The eventual transfer of the land could create further legal uncertainty for anyone attempting to set up a business today – while the requirements under the ALA are similar to those under the *Land Act*, they are not identical.

If the land is held by the community in trust under the ALA, a lease may be granted by the trustees, but what the lessee may do with that land is limited (ss 39, 76, *ALA*). In all cases, where a lease is granted by the trustees, the interests that may be created under that lease are limited. Crucially, a lessee cannot create an interest under that lease in favour of a non-Aboriginal person for a period over 10 years without Ministerial consent. That means, effectively, that if the lessee wants to get a mortgage, they need Ministerial consent. If the land is transferred as an Aboriginal lease under the ALA, further requirements are entailed: the trustees need Ministerial approval in order to mortgage or sublease the land, including approval of the specific terms and conditions (s 76(4), *ALA*).

ii. Native Title

Then the erstwhile Hopevale baker would have to consider the implications of native title over the land. Does native title exist over the land? If there has been no determination, might it exist? Even in Hopevale, where there has been a consent determination in relation to native title[5], the township area was excluded from that determination, and the question of whether native title exists is a live one. Thus, native title is an issue, and the lease must be valid under the *Native Title Act 1993-1998* (NTA) if it is an act 'affecting' native title (s 227, *NTA*). Given that a lease grants exclusive possession, it is likely to affect native title. If this is so, they would

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[2] *Tsartlip Indian Band v Canada* 1999 172 FTR 160, para 56. The case is discussed in Flanagan and Alcantara at 14-15.

[3] Cf Flanagan and Alcantara who discuss a similar problem in relation to First Nation peoples in Canada at 11-15.

[4] See discussion in Owens (2000) at 10-11, Flanagan and Alcantara at 7-9.

[5] Erica Deeral (On behalf of herself & the Gamaay Peoples) & Ors v Gordon Charlie & Ors [1997] 1408 FCA (8 December 1997)

then have to consider whether setting up the bakery is a past or future act under the terms of the NTA.

Although the lease of land for the bakery occurs well after 1 January 1994, it is possible that the lease, or the legislation enabling the lease, could be a past act within the definitions in the NTA (ss 228-232) – a negative check would have to be done in order to exclude this possibility. If it *is* a past act, compensation is most likely payable by the government (s 17, *NTA*), but the act will be valid (s 14, *NTA*).

It is more likely that, if the lease affects native title, it will be a future act, in which case the act provides different options to pursue (Part 2, Division 3, *NTA*). It may be, for example, that the act in question falls under the freehold test (s 24MA-MD, *NTA*), in which case the procedural requirements under the right to negotiate will be enlivened (s 25-44, *NTA*). The Minister may decide that the expedited procedures may be followed (s 32, *NTA*), but even these procedures require a 4 month notice period. If the regular procedure is followed, a far longer period of negotiations, including arbitration, may ensue (s 35, *NTA*).

In light of the above, or if none of the specific future act provisions of the NTA apply, the negotiation of an ILUA may be advantageous – or necessary. Assuming that there is no registered agreement in place outlining procedures to be followed (which in this case there is not), the process will depend on whether there has already been a finding of native title. If there has been a finding and a prescribed body corporate (PBC) created, the PBC can negotiate the agreement (under s 24BA-BI, *NTA*), following its own rules about consultation and consent with native title holders under the *Native Title (Prescribed Body Corporate) Regulations 1994*. Where there is no PBC, the burden on the individual in proving that the agreement was made with the correct parties before registration is permitted is onerous: they must meet the notification requirements (leaving 3 months for objection) (s 24CH, *NTA*) and either have the agreement certified by the relevant Land Council or provide a statement that authorization followed proper procedures under the act (s 24CG(3), *NTA*). The authorization procedures have themselves been the source of significant litigation over the past 5 years.[6] There are also significant administrative requirements under the *Native Title (Indigenous Land Use Agreements) Regulations 1999*, which contribute to the length of time required to prepare a registration application.

This outline is does not factor in a consideration of the politics or length of time that might be required to actually negotiate the agreement, the cost of legal advice, and the availability of legal advice for the community. Where a land council is overwhelmed with work on claims, they may not prioritise the negotiation of an ILUA – particularly where, as is likely, it falls outside the scope of its specific funding.

And Hopevale is in many senses a simple example. In an area where there is no claim underway, the native title group would first have to be identified – a process which typically takes 6 – 9 months of anthropological work and may involve legal challenges prior to engaging in the steps mentioned above.

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[6] See eg *Moran v Minister for Land and Water Conservation for the State of NSW* [1999] FCA 1637; *Strickland v Native Title Registrar* (1999) 168 ALR 242; *Daniel v State of Western Australia* (2002) 194 ALR 278; *Lawson on behalf of the 'Pooncari' Barkandji (Paakantyi) People v Minister for Land and Water Conservation for the State of NSW* [2002] FCA 1517; *Holborow v State of WA* [2002] FCA 1428.

Every step that causes delay or where there is ambiguity increases the associated legal costs and generates uncertainty in the transactions. This cost and uncertainty are effective barriers, keeping many Indigenous people outside the mainstream economy.

3. A lose-lose situation

At present, lawyers and Land Councils (and ATSIC[7] and the ILC[8]) create these inefficient and complex structures with little thought to how workable the ownership structures and decision-making and land use procedures might be for the purposes of economic development.

The result of this legal morass is a situation that is detrimental for everyone. Massive amounts of time and money being spent on Indigenous infrastructure and on the negotiation and litigation of native title claims are achieving minimal *practical* results for Indigenous people. The results do not create the conditions for economic growth. It is not only that there are no incentives for economic growth: within a welfare economy, it is *irrational* to improve land or assets over which you have no secure title. There is no reason to improve or even maintain a home that you do not own.

Beyond these immediate failings, the current system entrenches an antagonistic and adversarial approach between Indigenous and non-Indigenous Australians. Where a successful native title claim, or the allocation of resources to Indigenous infrastructure, in effect means that resources are being transferred out of the mainstream Australian economy, parties are understandably inclined see their interests as diametrically opposed: a win for the 'other side' is necessarily a 'loss' for themselves.

4. The way forward: moving Indigenous assets into the mainstream economy

The situation of Indigenous Australians, like that of the people de Soto has studied, is dire. There is a way forward.

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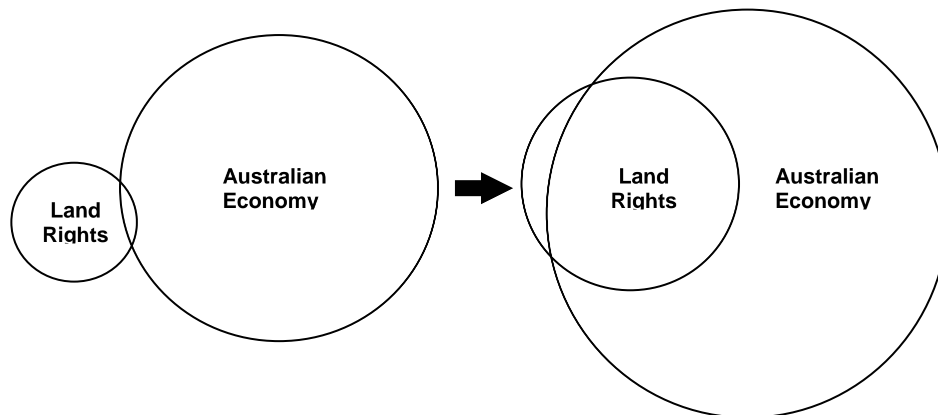
[7] Aboriginal and Torres Strait Islander Commission, whose administrative arm is now a separate organization, ATSIS, Aboriginal and Torres Strait Islander Services.
[8] Indigenous Land Corporation.

What we need to do is address the mundane legal processes which prevent indigenous people from using their assets to participate in the mainstream economy: to make their assets fungible. In terms of the location of their assets, we need to move them into the mainstream economy:



Invited by heads of State around the world, de Soto has been working on exactly this problem. For example, the ILD revamped Peru's property system, allowing its poor to acquire almost $10 billion in net benefits; an annual return of 142% on USAID initial investment.[9] A Canadian think-tank, the Frontier Centre for Public Policy, has also realized the potential of de Soto's work and is embarking on a similar investigation to the one we propose, although addressing a specifically Native Canadian situation.[10]

This is not to say that this process is a simple one or one that should be engaged in uncritically. Far from it – what is needed is an intelligent and well thought out solutions.

a. An intelligent compromise

There are legitimate concerns about moving Indigenous assets into the mainstream economy. With the alienability of indigenous title to land comes a real possibility of the surrender of land on unjust terms, as well as losing the capacity to protect environmentally sensitive or culturally significant areas. These concerns may dictate in particular cases that areas of land remain inalienable and therefore outside the mainstream economy. What is needed is creative policy and legal thinking to create maximum fungibility with minimum risks to Indigenous communities.

What we need to remember, however, when evaluating any compromise, is that we are not abandoning Indigenous culture with a movement towards the mainstream economy. Cultural protection and self-determination are not identical to, or co-extensive with, remaining outside of a real economy. De Soto has commented, specifically in relation to the situation of American Indigenous people, that while groups who desire to protect Indigenous property rights by keeping them outside the real economy may be informed by the best intentions, they 'do not realize that in

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[9] Facts on the achievements of the ILD are available on their website at <http://www.ild.org.pe/nutshell_01.htm>

[10] The project outline is available on the website of the Frontier Center for Public Policy at <http://www.fcpp.org/project_detail.php?ProjectID=53>.

many cases what they are talking about is protecting or promoting the sovereignty of a special ethnic group, not property rights. This results in a needless confrontation between the protection of sovereignty of an ethnic group and the property rights of individuals within such a group' (CIPE, 1996).

This comment directly addresses the Australian context. The current situation, where the majority of Indigenous lands and assets are outside the mainstream economy is, theoretically, the optimal situation for the protection and preservation of Indigenous culture. In practice, however, this is simply not the case. The problem is that, in a dual economy system, Indigenous people live in a passive welfare economy. Within this economy, Indigenous communities are dysfunctional and Indigenous culture is threatened with disintegration.

This cultural degradation is, in itself, a problem that needs to be addressed. But one that is better addressed in the context of economically vibrant communities.

b. Ways forward

The implications of de Soto's work should be kept firmly in mind when considering Indigenous policy generally and title transactions specifically. We need to keep it in the front of our minds in when creating Prescribed Bodies Corporate, and ensure that the structures we create are economically efficient. We need to keep it in the front of our minds in the context of land transfers, native title determinations, ILC title-holding structures and the negotiation of ILUAs. Driven by an awareness of the significance of de Soto's insights, we need to: address Indigenous home ownership (United States figures estimate that 90% of small businesses in North America are initially capitalized with a mortgage on a family home)[11]; simplify the multiple layers of Indigenous landholding structures; develop principles for internal community governance of individual enterprise; and provide for management of land and assets, including the development of sound investment strategies.

Certainly, these components must be explored with a view to complexities which de Soto's work does not specifically address. Environmental and cultural issues particular to the Australian Indigenous situation, in particular traditional structures of communal land ownership and the need to protect significant sites, demand a careful consideration of de Soto's work. De Soto is not dealing with countries where welfare has contributed to the problem it seeks to address.

Live to these challenges, *Building Indigenous Capital* seeks to promote the growth of Indigenous assets by building structures that will facilitate transactions in the real economy, enabling Indigenous people to build capital, as well as through intelligent negotiations in relation to native title. These structures are a part of challenging the passive welfare economy. The benefits extend further: by moving Indigenous assets into the mainstream economy, the interests of Indigenous and non-Indigenous Australians move towards alignment. It means that the growth of Indigenous property rights and assets generally contributes to the growth of the Australian economy as a whole. The creation of economically efficient structures reduces, over the long term, the amount of funding that needs to be poured into Indigenous infrastructure by creating the conditions for independently viable Indigenous communities. But it is also a possibility that is crucial for Indigenous communities: when communities look

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[11] Owens (2002)

to the future, there must be something on the horizon other than a passive welfare existence.

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