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Mergers and Amalgamations within the Canadian non-profit and charity sector

by Mark Blumberg (February 8, 2009)

There are 160,000 non-profits in Canada, of which 82,000 are registered charities. The non-profit and charitable sectors are increasingly competitive in terms of fundraising and service delivery. There is a debate about whether we have too many charities in Canada.[1] Quite frequently I am approached by charities or non-profits that wish to either partner/cooperate with other charities or non-profits or wish to merge or amalgamate some or all of their operations. There are different options in terms of mergers, some have greater autonomy while others have greater integration. In this article, I will discuss some of the many issues when Canadian non-profit organizations and charities wish to work together in the most integrated form of cooperation: amalgamation, merger or consolidations, which in this article I will generally refer to as "merger".

Why consider Merger?

What necessitates the discussion of merger? In some cases, it is a strategic process in which it is discovered that there could be some benefits of merging the two operations. In other cases, an organization has gone through some sort of catastrophic event or is concerned for its future and sees the merger as a lifeline. In other circumstances, one organization sees an opportunity to essentially take over another organization by merger. Sometimes mergers are forced on two entities such as the case of Women's College Hospital and Sunnybrook (although that merger did not work out and the hospitals subsequently split). In other cases, having a funder "suggest" that you merge does achieve positive results.

Merger can be everything from collaboration on certain areas to joint programming to more structured joint ventures and to ultimately amalgamations. Although generally

[1] In my article "Should We Establish another Canadian Charity?", I discusses the issue of whether a fewer or greater number of Canadian registered charities would be beneficial to the charitable sector http://www.globalphilanthropy.ca/images/uploads/Should_We_Set_Up_Another_Canadian_Charity_-_for_Canadian_Association_of_Paralegals_CAP.pdf

when people talk about merger, they are referring to something more substantial like one organization being subsumed by another or an amalgamation. Some other options to an amalgamation include an asset transfer or interlocking boards.

Some of the challenges that non-profits face that may make them consider merger in addition to the highly competitive marketplace include the following:

1. There is increasing competition in a number of areas like home health care and daycare, etc. with for-profit entities or other non-profits.

2. Funders are increasingly requesting that non-profits and charities work together in some fashion, whether it is joint programming, partnership or merger in order to avoid duplication, increase efficiency and improve service delivery. In some cases, having a merged organization may result in more funds from funders compared to the amounts received by the individual organizations prior to merger.

3. Merger may also result in cost savings because of the ability to share resources, have greater purchasing power, consolidate duplicate governance structures for 2 or 3 organizations.

4. Many funders are requiring more complicated types of reporting and making greater demands on non-profits and charities for accountability, transparency, measurement and evaluation, which a smaller non-profit may have more difficulty meeting.

5. The world is changing quite rapidly. In some cases, by merging two organizations, one organization may benefit significantly from the technical, financial, fundraising, and other resources of the other organization. As well a larger staff will allow for greater specialization of staff people.

6. The public may feel that a particular area is overcrowded with organizations and public opinion may favour a merger. The merger may also result in greater public profile and credibility and greater resources for fundraising and development and less confusion in the public's mind about what your organization does.

7. Provide broader and better services rather than trying to be a small organization that is a jack of all trades and master of none.

8. You are having trouble attracting necessary human resources including staff and volunteers because of limited opportunities or profile in the community. Your thinly stretched staff may be close to exhaustion and burnout.

9. Sometimes a merger is the natural progression of a successful partnership between two entities.

Problems with Mergers

The topic of mergers can be fraught with pitfalls and difficulties. Here are some of the issues:

1) Mergers often bring a tremendous amount of emotional baggage and egos to the table. Whether it is the notion of the charity being a "person" and its individuality is about to be subsumed by another organization or whether it is the potential loss of employment or a position within a charity, there can be many emotional concerns.

2) The organizational culture of one organization may be very different from others. Culture includes attitude to taking on risk, decision making and management style, beneficiary participation, and flexibility to change. The merger of two organizations is like a marriage: it can take a long time to find the right person; and then a long time to prepare the wedding; and if the marriage is rocky or there is a divorce, the results can be disastrous for all concerned. Just like a marriage, sometime the relatives are more aware of the lack of fit and the couple is oblivious!

3) Although funders often encourage mergers, there is sometimes a "merger penalty" in that good intentions aside after the merger the funder may be providing the merged entity with less than what it provided the individual organizations prior to the merger. If a funder is encouraging mergers, try to get the funder to provide some funds to explore whether a merger proposal makes sense and to obtain necessary professional advice. Funders are usually prepared to do so if they think in the long term there will be benefits.

4) Boards of directors, or board members, often have concerns with respect to mergers including whether the discussion of merger will result in a distraction for the organization as well as if a merger were to take place how it could affect the mission of the organization, its board and its officers.

5) It is extremely difficult to select a partner and to build trust between organizations. In many cases, organizations that would come together in a merger are "competitors" of each other and they may have had a history.

6) There will be jockeying for positions within the merger. One obstacle could be if you have two permanent CEO's or ED's who have a long history with their organization, then who will be the remaining CEO at the end of the merger. It is very important that there be trust built up between the two parties. Often that trust is developed by charities working together when there is no pressure to merge.

7) Bigger is not necessarily better. It often results in larger costs, loss of efficiency, and more bureaucratic organization that is less able to adjust to changing times. Bigger organizations tend to use more staff and less volunteers. Often the boards are moved further to a policy making role and not active involvement with the charity, which for some is considered a loss. Systems that worked adequately for each organization may not be adequate for the larger organization. Most non-profits spend little on administration/IT (they lack capacity in this area) and there is little room for savings. For most non-profits there are no easy savings and human resources are their biggest expense and a reduction in employees is the only way that significant savings will ever be realized at least in the short term.

8) Are there assets or agreements which pose particular difficulties such as restrictions placed on the use of property, special purpose trust, funder agreements with rigid requirements which may no longer be met by the merged entity? This may not prevent a merger, but care needs to be taken that these assets are not just mixed in with other assets in the new merged charity. Well-intentioned merger agreements between parties that may not fully trust each other may put the merged into a straightjacket, which is cumbersome and unhealthy for the merged entity.

9) Mergers are expensive – time, professional fees, creating common technology, rebranding, relocation, training staff on new systems, changes in HR including terminations in some cases. Perhaps the biggest cost is the distraction caused by the merger may result in lost opportunities and inferior provision of service. Goodwill and public recognition may be lost with new branding. Often the merged entity is not equal to the sum of the parts and may take years to adjust to the new situation and the distraction caused by the merger. This is especially the case when two organizations that are struggling are getting together. The merger is another burden to deal with, over and above the regular operations, which are overwhelming the organization.

10) Charities often are not good at making decisions. If it can take 6 months to decide whether to buy a new computer, how long will it take and how stressful will it be for a charity to make a merger happen?

Unfortunately most merger discussions are not handled well and charities often do not obtain necessary professional advice and expertise which results in the merger discussions being more costly, frustrating and less likely to succeed. Most merger discussions that are started never result in a merger taking place. Furthermore, after most mergers there is not an impartial evaluation of the results, and I am guessing if an impartial assessment a few years after the merger was to made it might find in many cases find that the costs of the merger were far greater than expected; the benefits far less than expected; and that the dislocation, protracted distraction from mission of a merger far exceed any value created by the merger.

Continuum

Although mergers are often discussed, they are far more infrequently implemented. Merger is by no means the only way for non-profits to work together. There is a continuum when you have non-profits working together. It can be everything from informal networking to amalgamation. Below are some relationships from least integrated to merged.

Informal networking, membership organizations, umbrella groups, and collaboration
Endorsement/Sponsorship
Sharing Premises, facilities, buying groups
Joint Ventures, Joint Research, Joint Training, Joint Programming
Partnership
Agency
Merger/Amalgamation/Consolidation.

For a discussion of various types of structured arrangements such as agency, joint venture, partnerships and coalitions, you might find my article "Canadian Charities and Foreign Activities"[2] interesting. Although it is geared toward Canadian charities working with foreign charities, many of the considerations apply to two non-profits in Canada working together when one is a qualified donee (eg. Charity) and the other is a non-qualified donee.

Merger issues

Some of the issues that will have to be dealt with in terms of a merger are:

1. What are the drivers for merger?
2. What are short, medium and long term goals of merger?
3. Have you indentified a number of possible merger possibilities and if not, why not?
4. Is this the right time to merge?
5. Are the merger organizations unincorporated associations, trusts or incorporated?
6. What are the legal objects of each merger partner? Are they acting currently within objects?
7. Do the organizations have the legal powers necessary to effect the proposed merger? Does either organization need to modify their governing documents?
8. Have you retained necessary professional advisors including a lawyer who is knowledgeable about mergers to assist and give advice on a merger? Is the lawyer knowledgeable about charity law if one of the parties is a charity?

[2] http://www.globalphilanthropy.ca/images/uploads/Canadian_Charities_and_Foreign_Activities_-_The_Philanthropist_-_by_Mark_Blumberg.pdf

9. How many voting members are there for each organizations? Who are members?
10. Who are the stakeholders of each organization?
11. What does the statute and by-laws provide in terms of quorum for a meeting, majority required for various options?
12. Who is going to the dominant party or will there be equality at the end?
13. How many board members are there for each party to the merger? How many will there be with the merged entity? What skills, resources, diversity, connections do each board member bring?
14. Is the merger in the best interest of both organizations? The directors of an organization must be satisfied that the merger is beneficial.
15. How much time will be spent on the merger discussions and how long will it take for the merger to take place?
16. Employment issues – How many employees are there? Will all employees move to merged entity? How many years have each employee worked for the organization and review 20 or so other factors relevant to termination and severance? What was last year's total payroll. If one organization is paying a greater amount to its employees than the other, will the more "efficient" organization have to raise the amount that it is paying its employees? Will there be employment law issues, pension liability issues etc.? Will there be at some point redundancies and will they be handled appropriately by attrition or proper notice or termination and severance payments? If one organization is unionized, will the other one become unionized? If each has a union, which union will represent the employees or will both remain?
17. Are there any liabilities with respect to either of the parties?
18. Identify all assets owned by each organization, restrictions on the asset, and the ease with which that asset can be transferred to another entity. Assets could include real estate, intellectual property etc.
19. Identify all liabilities and ongoing obligations including service agreements, leases, employment as discussed above, funding agreements, partnership agreements with domestic and foreign partners.
20. Have you been provided with a list of all actual and threatened litigation over the last five years?
21. Has each party reviewed the financial statements and information of the other?
22. Does one or both charities have any special purpose trusts, endowments, and what donor restrictions need to be complied with?
23. If a trust or association, ensure compliance with the trust agreement or constitution, or the trustee or member could be liable for breach of trust or reimbursement of funds.
24. With corporate entities, ensure that directors are meeting their fiduciary duties in managing the merger, being prudent and only acting in an authorized manner?
25. What name will the merged entity have and has it been reserved?
26. Have debts been appropriately identified and dealt with?

27. Conduct a comprehensive due diligence process on your potential partner to identify any concerns or impediments to merger. This due diligence should be proportional.
28. What are sources of revenue for each organization? Will donors, funders, earned income be able to continue and be assigned or transferred to the merged entity?
29. Are the organizational cultures compatible and is there a fit? Has work been successfully worked on between the merger parties?
30. Do you have a communication strategy in place to consult with and communicate with each stakeholder?
31. Do you have a plan for implementing the merger?
32. What will the post-merger structure look like?
33. What obligations will the merged entity take on in terms of continuing programs of one or the other organization, if any?
34. Are there any particular consents required for the merger? Are their provincial or federal acts or regulations that could affect the merger such as the Public Hospitals Act with a hospital merger?

Some of these issues above would help to decide whether in fact some sort of form or cooperation or joint-venture partnership would be appropriate rather than a full scale merger of the organizations. In some cases, with international mergers it is easier when a Canadian charity and foreign charity are interested in merging to have each organization remain, with its attendant liabilities and assets and tax status, but have them work together, often with interlocking or identical boards. It is vital that the relationship between the two organizations be scrupulously maintained and that the Canadian charity retain direction and control over its resources.

Mechanics of merger

How a merger takes place depends on the way the various parties are set up and which entities will survive the merger.[3] In terms of trusts, look to the terms of the trust deed as to whether an amendment is possible. With unincorporated associations look to the agreement between the members – usually called the constitution and if it does not provide for mergers you should obtain consent of all members. With corporations you look to corporate law, letters patent and by-laws of the corporation.

Federal

Federal corporations under the *Canada Corporations Act* are not allowed to amalgamate. Therefore, two federal corporations cannot amalgamate and also a federal corporation and a provincial corporation cannot amalgamate. In order then to create a "union" one needs to either create a new charity and transfer assets from both into it or take the assets of one and transfer them into the other. If a Federal Special Act corporation wants to

[3] For an excellent discussion of mergers see *Issues Arising from Mergers and Fusions of Charitable Organizations* by Louise J.A. Greig and M. Elena Hoffstein 40 The Philanthropist, Volume 15, No. 1

amalgamate with another it can do so by having a statute passed. However, this is a time consuming, expensive and uncertain path.

Ontario

Ontario non-share capital corporations under the Ontario Corporations Act can amalgamate under section 113 of the Act. Section 113 sets out some limitations and requirements including the following:

Amalgamation

113. (1) Any two or more companies, including a holding and subsidiary company, *having the same or similar objects* may amalgamate and continue as one company. R.S.O. 1990, c. C.38, s. 113 (1).

Agreement

(2) The companies proposing to amalgamate may enter into an *agreement* for the amalgamation prescribing the terms and conditions of the amalgamation, the mode of carrying the amalgamation into effect and stating the name of the amalgamated company, the names and address for service of each of the first directors of the company and how and when the subsequent directors are to be elected with such other details as may be necessary to perfect the amalgamation and to provide for the subsequent management and working of the amalgamated company, the authorized capital of the amalgamated company and the manner of converting the authorized capital of each of the companies into that of the amalgamated company. R.S.O. 1990, c. C.38, s. 113 (2); 2001, c. 9, Sched. D, s. 5 (4).

Adoption by shareholders

(3) The *agreement shall be submitted* to the shareholders of each of the amalgamating companies at general meetings thereof called for the purpose of considering the agreement, and, if two-thirds of the votes cast at each such meeting are in favour of the adoption of the agreement, that fact shall be certified upon the agreement by the secretary of each of the amalgamating companies. R.S.O. 1990, c. C.38, s. 113 (3); 1998, c. 18, Sched. E, s. 64.

Joint application for letters patent

(4) If the agreement is adopted in accordance with subsection (3), the amalgamating companies may *apply jointly to the Lieutenant Governor for letters paten*t confirming the agreement and amalgamating the companies so applying, and on and from the date of the letters patent such companies are amalgamated and are continued as one company by the name in the letters patent provided, and the amalgamated company possesses all the property, rights, privileges and franchises and is subject to all liabilities, contracts, disabilities and debts of each of the amalgamating companies. R.S.O. 1990, c. C.38, s. 113 (4).

When two or more Ontario non-profit corporations wish to amalgamate, as long as they have similar objects, they can amalgamate and continue as one corporation under s.113 of the Ontario Corporations Act. They need to have an amalgamation agreement. They would need to prepare an Application for Letters Patent of Amalgamation, which is Form 11 prescribed under the Regulations, in duplicate which will be filed later with the Companies Branch of the Ontario Government. They will either need to use a by-law from one of the existing corporations or create a new general by-law. They will need a board resolution of each organization to approve the amalgamation agreement and Letters Patent of Amalgamation. They will also need a members meeting to approve the same. The name of one of the amalgamating corporations may be used or if there will be a change of name, at which point an Ontario-based NUANS name search report needs to be obtained. You will need a solvency certificate of each organization prepared by an officer as well as a certificate from the secretary of each corporation attesting to the adoption of the amalgamation agreement. A Form 1 – Initial Return needs to be filed within sixty days of the amalgamation.

Public Guardian and Trustee in Ontario

If the non-profit is a charity, but not necessarily a registered charity with CRA, then the Public Guardian and Trustee will review the application for Letters Patent of Amalgamation.

After the amalgamation, a copy of the Letters Patent of Amalgamation should be provided to the PGT.

In Ontario, the Not-For-Profit Incorporators Handbook of the Attorney General provides in section 6.6.4 that:

> **6.6.4 Amalgamation**
>
> Subject to certain conditions, the *Corporations Act* allows two or more corporations under that Act to amalgamate as one corporation. If one of the amalgamating corporations is charitable or if the amalgamated corporation is to be charitable, the request to amalgamate must be submitted to the Public Guardian and Trustee for its review and pre-approval.
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> **What to send**
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> The following should be submitted to the Public Guardian and Trustee:
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> - Duplicate original signed copies of the application for Letters Patent of Amalgamation.
> - A signed copy of the Amalgamation Agreement.

- A covering letter setting out the name, address and telephone number of the person or firm to whom the Letters Patent of Amalgamation and any correspondence regarding the application should be mailed.
- A cheque or money order payable to the Public Guardian and Trustee. The fees as of the date of the Not-For-Profit Incorporator's Handbook are set out in **Appendix "J"** . *[Currently Amalgamation - $150 for each amalgamating corporation plus $155. This includes the Public Guardian and Trustee fee for reviewing the application ($150 for each amalgamating corporation) and the Companies Branch fee for reviewing the application and issuing Letters Patent of Amalgamation ($155).]*
- If the name of the amalgamated corporation will not be the same as the name of one of the amalgamating corporations, you may send a NUANS search report (described in section 2.13 of the Not-For-Profit Incorporator's Handbook) with your application, but remember that a NUANS search is only valid for 90 days. You may choose not to enclose a NUANS report with the application. You will be contacted when the NUANS report is required.
- The annual audited financial statements for each of the amalgamating corporations for the last three years (or since incorporation, if incorporated less than three years ago). Generally, a corporation (whether charitable or not) whose liabilities exceed its assets will not be permitted to amalgamate with a charitable corporation.
- A copy of the Letters Patent and any Supplementary Letters Patent for each amalgamating corporation unless they have already been filed with our Office.
- The current names and addresses of the directors and officers.

If the objects of the amalgamated corporation will be significantly different from those of one of the amalgamating corporations you may be required to amend the amalgamation agreement to include a clause similar to the following:

"All funds and other property held by the amalgamating corporations immediately before the Letters Patent of Amalgamation become effective or at any time thereafter received by the amalgamated corporation pursuant to any Will, deed or other instrument made before the Letters Patent of Amalgamation become effective, together with all income thereon and accretions thereto shall be applied only to the objects of the respective amalgamating corporation as they are immediately before the Letters Patent of Amalgamation become effective."

If the application for Letters Patent of Amalgamation is accepted, the Public Guardian and Trustee will forward it to Companies Branch. The Public Guardian and Trustee's review portion of the fee is non-refundable even if the applicant discontinues the application.

Charities Directorate of the Canada Revenue Agency

After the amalgamation, a copy of the Letters Patent of Amalgamation should be provided to the CRA. As well, when writing to the CRA indicate which charitable registration number will be kept for the amalgamating entity. Ensure that all official donation receipts reflect the name of the amalgamated entity.

Agreements

It is a good idea to have a preliminary agreement to cover off various issues related to any discussion of merger including confidentiality and non-solicitation of employees. During a merger discussion it is important that there be appropriate disclosure, and it is best if there has been some collaborative or joint work between the organizations which can form the basis of the trust. Later a merger agreement should be prepared whether or not there is an amalgamation to cover off many issues.

Some Thoughts

Here are some thoughts in terms of merger:

1) Ideally start preparing six months to a year before you engage in any serious discussion.
2) Clean up your organization if you are serious about a merger. Your documents, processes, assets etc. will be scrutinized like never before. If you think that you are going to be taken over then this is less important, but if you are going to argue that your charity should be subsuming another charity, it is harder to do when your charity is a mess.
3) If you are going to merge do so from a position of some strength and preferably do not wait till you are about to go under.
4) Do your due diligence on the other organization.
5) Consult with stakeholders extensively.
6) Obtain consents from funders to the merger and obtain commitments with respect to funding. Funding after a merger can be less, the same or more from a funder, and it is important to know what the effect of the merger will be on a major funder.
7) Be honest and conservative in terms of the benefits of a merger and realistic about the costs.
8) Carefully identify a suitable partner or partners.
9) Have a confidentiality and non-solicitation agreement with any prospective merger partner.

10) Establish a committee or representative from each organization to deal with merger.
11) Establish terms of reference for the committee.
12) Have board approval for any negotiations.
13) Work together with the other organization to discuss feasibility.
14) Be prepared to walk away from a merger.
15) If you are the bigger party to the merger, this does not mean that you have to compromise less. Often it means you have to compromise more.
16) Work hard to develop trust. Usually you need to work together on something before some trust can be developed. Having trust in place between two parties that have worked together can dramatically reduce the time required for merger. Be honest with each other or you will kill any trust that may have developed.
17) If the merger is going to go through, try to do it as quickly as possible because multi-year merger discussions are extremely costly on many fronts.
18) It is more cost effective to obtain some legal advice up front with respect to a merger. In some cases, lawyers are contacted at the end, to ostensibly finalize the details of a merger agreement and the parties then find out that their plan they had been working on for one and a half years is not going to work. Furthermore, if you are planning on having a committed lawyer who is on your board and who is not very knowledgeable about non-profits do the legal work on a pro bono basis, you should have a plan B. Otherwise you will probably burn out or alienate the lawyer. Keep in mind that you want to get impartial advice from a third party – a lawyer on the board may be in favour or opposed to a merger and that could colour their view of the merger. For non-profits, especially charities, it is vital to get relevant and accurate advice.
19) If you are merging a charity and non-profit ensure that the activities of the non-profit are charitable and the non-profit will have to cease any activities that a registered charity cannot conduct.
20) Communicate effectively with all stakeholders and involve stakeholders in the discussion or expect that there will be greater concern, anxiety and opposition.
21) A legal merger is a legal merger. If you want a real merger, have a well thought through integration plan.

CRA's Views on Mergers, Amalgamations and Consolidations

CRA Registered Charity Newsletter 21

In registered charity newsletter #21 (2005), the CRA discusses amalgamations, mergers and consolidations. Below are some excerpts from Newsletter 21.

> **"When is an amalgamation not an amalgamation?**

In a previous issue, we explained how the Charities Directorate differentiates between amalgamations, mergers and consolidations for the purpose of determining whether the originating organizations will continue to exist (and thus can keep their BN) or cease to exist (and need to apply for charitable registration as the new entity).

Amalgamations When two or more charities amalgamate, they bring their membership, assets, and liabilities into the entity that emerges. However, the original charities do not cease to exist or dissolve. While they no longer have separate identities, they continue their existence within a single entity—the amalgamated charity.
Mergers In mergers, one entity winds up its affairs and transfers its assets to another.
Consolidations In consolidations, all the original bodies dissolve and transfer their assets to a new entity.

We recognize that for other purposes these words are sometimes used interchangeably or given a completely different meaning than we ascribe to them. These meanings are not consistent even within provinces, and it is not unusual for legislation that affects charities to use conflicting meanings for each term.

In particular, some legislation uses the word "amalgamation" when referring to what the Charities Directorate considers to be a merger or a consolidation.

Charities may distinguish between these situations by examining the language used in the legislation in each case.

For example, with respect to amalgamations, one should look for the words "continue" or "continuance" as in "any two or more companies may amalgamate and continue as one company". The amalgamated body may be said to "possess" all the assets and rights of the original bodies.

On the other hand, if the legislation refers to assets being "transferred," "transmitted," or "conveyed," this indicates that there has not been an amalgamation.

Letters patent of amalgamation are issued that "confirm the agreement" between the corporations.

If, however, Letters Patent of incorporation are issued which create a corporation and make reference to the "new" corporation or the corporation "so incorporated," this indicates that there has not been an amalgamation.

For example, based on our last review, **the following pieces of legislation do <u>not</u> allow for amalgamations**:

Canada Corporations Act
Northwest Territories Societies Act
Nova Scotia Societies Act
Prince Edward Island Companies Act
Yukon Societies Act
British Columbia Societies Act

Some pieces of legislation that **<u>do allow</u>** for amalgamations include:

Alberta Companies Act
Alberta Society Act
Manitoba Corporations Act
New Brunswick Companies Act
Newfoundland Corporations Act
*Ontario Corporations Act (*Request to amalgamate under this statute must first be submitted to the Public Guardian and Trustee for their review and approval.*)*
Quebec Companies Act
Saskatchewan Corporations Act

CRA Registered Charity Newsletter 16

The CRA's Newsletter 16 notes:

> **How do such organizational structures affect the use of Business Numbers (BNs)?**
>
> Each of these organizational structures affects the use of BNs differently. In the case of **amalgamations**, one BN is retained and used by the amalgamated body. The other BN(s) will be terminated. The charity will usually be able to choose which BN it retains. With **mergers**, the body proposing to dissolve undergoes voluntary revocation of its registration. The BN of the other remaining organization is not affected. The assets are all transferred to the remaining organization. In the case of **consolidations**, all original bodies are considered to undergo voluntary revocation. The new consolidated body needs to submit an application for registration and, if accepted, will typically be given a new BN

If you are changing the charities legal name, you must ensure that official donation receipts reflect the new name.

CRA Information Letters

The information letter CIL - 1998 – 029 dated October 16, 1998 deals with three health care institutions who were all charities and amalgamated. When CRA was advised of this, they cancelled two of the charitable registrations and transferred the third to the new entity. However, CRA took a while to let the charity know the details. It appears that the three health care institutions were not getting good legal advice because they were under the impression that the new entity could be a non-profit and not a charity because charitable registration was not required by them since almost all the funding came from the government and there was no need to issue official donation receipts for gifts.

The hospital believed that "amalgamation on XXXXXXXXXX, created a new corporate entity that is distinct from the previously registered charities. You also advise that since 1995, XXXXXXXXXX has operated as if it were a non-profit organization for the purposes of the GST and the XXXXXXXXXX and has been treated as such by XXXXXXXXXX. ... We have carefully considered your arguments; however, it is our position that when the amalgamation took place, XXXXXXXXXX inherited the rights and obligations of the formerly registered charities. Therefore, it was appropriate to assign a charitable registration number to the amalgamated entity. We regret the unfortunate delay in sending out the official notice in 1997.

> XXXXXXXXXX is constituted for charitable purposes and is carrying on charitable health care services. For these reasons, we are not prepared to revoke its charitable registration. Also, as explained previously, if XXXXXXXXXX decides to request voluntary revocation of its charitable registration, there are serious consequences under the *Income Tax Act*.
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> Because XXXXXXXXXX has been registered as a charity, it is a qualified donee for the purposes of the *Income Tax Act*. Had it not been a qualified donee, XXXXXXXXXX, XXXXXXXXXX and XXXXXXXXXX would not have been able to transfer their assets to it upon amalgamation. Instead, these assets would have been subject to tax under Part V of the *Income Tax Act*. XXXXXXXXXX can also receive gifts from other qualified donees like XXXXXXXXXX. If XXXXXXXXXX's charitable registration is revoked, it may not longer receive such gifts.
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> Subsection 188(1) in Part V of the *Income Tax Act* imposes a tax on charities whose registration has been revoked by the Minister of National Revenue. This tax is equal to the total of the value of the assets of the charity on the day that is 120 days before the day notice of the Minister's intention to revoke its registration is mailed. The amount of this tax is reduced by the value of assets transferred to qualified donees, amounts expended on charitable activities and amounts used to pay outstanding debts and reasonable expenses within the winding up period. The Minister does not have the discretion to not impose this tax on revoked charities. Therefore, if XXXXXXXXXX gives up its registration number, it will be subject to this tax.

> We understand that one of the principal reasons why XXXXXXXXXX would like to give up its charitable registration is that it is involved in research contracts with private businesses. Because XXXXXXXXXX is a registered charity, most of the services it provides are not taxable under the GST and the XXXXXXXXXX. This means it is not entitled to claim input tax credits to the same extent as would organizations making taxable goods and services in the course of a commercial activity.
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> If XXXXXXXXXX wishes to enter into agreements to conduct private research activities and claim input tax credits to an extent not allowed registered charities, then we recommend that it establish a separate organization whose purpose is to carry on research activities with the commercial sector.
>
> Under this proposal, the charity (XXXXXXXXXX), would devote its resources exclusively to its charitable activities. Most of the goods and services it provides, including its health care services and teaching services would be exempt for the purposes of the GST and XXXXXXXXXX. XXXXXXXXXX would continue to be exempt of Part I income tax; it could issue tax receipts for gifts; it would remain a qualified donee and therefore, could attract gifts from similar organizations. A corollary benefit would be the fact that XXXXXXXXXX would not be required to change its objectives or give up its own charitable registration. Finally, by remaining a registered charity, XXXXXXXXXX would not have to face the consequences of deregistration, including the revocation tax under Part V of the *Income Tax Act*.
>
> A separately constituted organization could explore commercial opportunities and carry on taxable research activities with private businesses. It could register for the purposes of the GST and claim input tax credits on purchases related to the taxable goods and services it provides in the course of its commercial activity. In addition, proceeds from this separate non-profit organization could be used to subsidize the charitable activities carried on by XXXXXXXXXX. If the organization falls under the definition of non-profit organization in subsection 149(1)(*l*), it would be exempt of Part I income tax but would not be bound by the restrictions of the *Income Tax Act* concerning registered charities.
>
> We appreciate that this recommendation may be complicated and take some time to implement. However, it is in our view, the only solution to the situation faced by XXXXXXXXXX that is consistent with the requirements of the *Income Tax Act*.

As well, the CRA information letter CIL - 1999 – 005 dated February 2, 1999 deals with the merger of two charities:

> Dear XXXXXX:

I refer to our telephone conversation of XXXXXXXXXX and your letter of XXXXXXXXXX concerning the integration of the XXXXXXXXXX and XXXXXXXXXX.

I understand that the XXXXXXXXXX is proposing to surrender its charitable registration and have XXXXXXXXXX (a non-charity) take over its operations, liabilities and assets. A revoked charity must normally pay off *bona fide* debts and distribute its remaining assets to another charity or "qualified donee" within one year of its revocation. Any remaining assets are owed to the Government in the form of a 100% revocation tax. The charity and its directors are responsible for assets that are improperly disposed.

You expressed concerns about the tax implications for XXXXXXXXXX of letting XXXXXXXXXX acquire the XXXXXXXXXX assets and liabilities. In my view, the proposal to have XXXXXXXXXX assume control of the XXXXXXXXXX assets and liabilities would be acceptable provided that the liabilities clearly exceed the assets. You should also note that we can only technically sanction this approach once revocation is effected. In view of the fact that the XXXXXXXXXX liabilities are in excess of its assets, once XXXXXXXXXX assumes control of the XXXXXXXXXX assets and liabilities, its net assets would essentially be nil. Consequently, the revocation tax on any remaining assets would not apply in this circumstance.

Should you proceed with the above proposal, I would suggest that you provide the Department with a written request to voluntarily revoke the charitable registration of the XXXXXXXXXX.

Likely Opponents of Merger

Some of the groups that may oppose the merger could include:

1) board members who may be concerned about the mission of the organization being compromised;
2) board members who may be concerned that their numbers will be reduced and that some of them will not be serving on the consolidated board;
3) employees who may be worried about their position in the new organization. In the case of one of the entities being unionized, the union may have concerns with respect to a merger. A merger can sometimes cause both organizations to adopt the salary and benefits of the more expensive organization which increases the costs of the merged entity and makes it less "competitive", albeit perhaps with happier employees.
4) Another concern could be from donors and funding agencies. The merged entity may not be attractive to funders or even eligible for certain funding.

5) Professional advisors, afraid that they will lose a client, rather than gain a bigger client may oppose the notion of a merger.

If you want to ensure that a merger is successful then it is useful to anticipate likely opposition, consider modifications or responses to the issues raised. This may make the merger more likely to succeed and less bumpy.

Red Flags

Some red flags in a merger situation include:

- the records of an organization are in disarray;
- an organization has recently lost a major donor or revenue source;
- an organization has recently lost its charitable status or has been audited for non-payment or withholding taxes or other obligation;
- unwillingness of one party to provide full disclosure;
- litigation that was not mentioned upfront in the merger talks.

For many reasons mergers of two or more organizations may become more common. They are a major undertaking and should be carefully planned and thought through to increase the likelihood of success.

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