MERGERS AND AMALGAMATIONS IN THE CANADIAN NONPROFIT AND CHARITABLE SECTOR

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ABSTRACT Difficult times and an increasingly competitive charitable sector are forcing some nonprofits and charities to consider organizational changes and collaborations. For some, a merger, the most integrated form of cooperation, is the most appropriate option. Unfortunately, many nonprofit mergers are handled poorly and the costs of the merger are far greater than expected; the benefits far less than expected; and the dislocation and protracted distraction from the organizations' mission far exceed any value created by the merger. This article discusses in a straightforward and practical manner some of the many issues that arise when Canadian nonprofit organizations and charities wish to merge. It also examines: the many reasons to consider merger; problems and pitfalls of merger; red flags and tips for managing a merger; likely opponents of merger; issues and steps in completing a successful merger; the mechanics of merger for Ontario and federal non-share capital corporations; as well as the views of the Charities Directorate and the Ontario Public Guardian and Trustee on mergers.

RÉSUMÉ Les temps durs et un secteur caritatif de plus en plus compétitif obligent certains organismes sans but lucratif et de bienfaisance à envisager des changements et des collaborations organisationnels. Pour certains, la fusion—qui est la plus intégrée des formes de coopération—est l'option la plus appropriée. Malheureusement, plusieurs fusions dans le secteur non lucratif sont mal gérées et leurs coûts sont souvent au-delà des attentes, les bénéfices ne sont pas à la hauteur des espoirs, et les bouleversements et distractions par rapport à la mission de l'organisme dépassent de loin toute valeur engendrée par la fusion. Cet article discute de manière directe et pratique certaines des questions soulevées quand les organismes sans but lucratif et de bienfaisance songent à fusionner. Il examine : les nombreuses raisons de fusionner; les problèmes relatifs aux fusions; des indices et avertissements pour gérer une fusion; les opposants probables aux fusions; les étapes à suivre pour réussir une fusion; le processus de fusion dans le cas de sociétés sans capital-actions ontariennes et fédérales; et les points de vue sur les fusions de la Direction des organismes de bienfaisance et du Bureau du Tuteur et curateur public en Ontario.

KEYWORDS Charitable sector, Mergers, Ontario Public Guardian and Trustee

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THE NONPROFIT AND CHARITABLE SECTOR IS INCREASINGLY COMPETITIVE IN terms of revenue generation and program activities. The global economic crisis and its uncertain and multifaceted effect on the Canadian nonprofit sector has led to more openness to considering change in many areas, including organizational structure.

Quite frequently I am approached by charities or nonprofits that wish to either partner and/or cooperate with other charities or nonprofits, or to merge or amalgamate some or all of their operations.

There are different options available to organizations that are interested in cooperating, coordinating, or collaborating with one another. Some options provide for greater autonomy while others lead to greater integration. Collaboration can be everything from informal networking to participation in membership organizations to the creation of umbrella groups or coalitions. It can mean even closer arrangements such as sharing premises and facilities by buying product or services together as well as joint ventures, joint research, joint training, joint programming,[1] and joint fundraising.[2] These are more often than not sufficient collaboration for most organizations. However, in this article, I will discuss some of the many issues that arise when Canadian nonprofit organizations and charities wish to work together in the most integrated form of cooperation: amalgamation, merger, or consolidation, which in this article I will generally refer to as "merger."

WHY CONSIDER A MERGER?

There are an estimated 160,000 nonprofits in Canada, of which 83,000 are registered charities. There is a debate about whether we have too many charities in Canada,[3] which I will not discuss here, but certainly in some regions of the country the multiplicity of organizations dealing with the same issues may work against all of these organizations.

What leads to discussion of a merger? In some cases, it is a strategic process in which two or more organizations discover that there could be some benefits to merging their 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 still other circumstances, one organization sees an opportunity to take over another organization and its assets. Sometimes mergers are forced on two entities, such as the case of Toronto's Women's College and Sunnybrook Hospitals (although that merger was not successful and the hospitals subsequently split). Sometimes a funder may "suggest" a merger that leads to positive results. In some cases, talk of a merger is a face-saving way of avoiding discussion of winding up an organization and transferring its assets to another organization. There is nothing wrong with a successful charity that has had many years of serving the community paying off its debts and winding down after it has achieved its objective or when it no longer has the financial or volunteer resources needed to continue; however, some people see this as a failure. Finally, sometimes a merger is the natural progression of a successful partnership between two entities.

Some of the challenges that nonprofits face that may make them consider merger include the following:

1. There is increasing competition in a number of areas such as home health care and daycare with for-profit entities or other nonprofits.

2. Funders are increasingly requesting that nonprofits and charities work together in some fashion, whether through joint programming, partnership or merger, in order to avoid duplication, increase efficiency and improve service delivery. In some cases, the merged organization may receive more funds from funders than the individual organizations did prior to merger.
3. Many organizations are squeezed for resources. A merger can result in cost savings because of the ability to share resources, exercise greater purchasing power and consolidate duplicate governance structures.
4. An organization may need to make dramatic changes but, for a variety of reasons, may not be up to the task. A merger can shake up the organization and give it the political will and strategic thinking to effect changes that would not otherwise have been welcomed or palatable.
5. Many funders are requiring more complicated forms of reporting and making greater demands on nonprofits and charities for accountability, transparency, measurement and evaluation. Some smaller nonprofits may have difficulty meeting.
6. The world is changing quite rapidly. In some cases, a merger allows one organization to benefit significantly from the technical, financial, fundraising, and other resources of another organization. As well, a larger staff resulting from a merger can allow for greater specialization.
7. The public may feel that a particular area is overcrowded with organizations, and public opinion may favour a merger. This can also result in greater public profile and credibility, greater resources for fundraising and development, and less confusion in the public's mind about what the organization does.
8. Many small organizations try to be jacks-of-all-trades and end up being masters of none. A merger with another organization may provide the opportunity to offer broader and better services.
9. Some organizations have trouble attracting human resources, including staff and volunteers, because of limited opportunities or low profile in the community. Existing, thinly stretched staff may be close to exhaustion and burnout. A merger can alleviate this pressure.

PROBLEMS WITH MERGERS

Mergers can be fraught with pitfalls and difficulties. Here are some examples:

1. Organizations seeking to merge often bring a tremendous amount of emotional baggage and ego to the table. This can include everything from one charity worrying about its individuality being subsumed by the other organization to staff concerns about the potential loss of employment or position within the merged charity.
2. The organizational culture of one organization may be very different from another. Culture includes attitude to taking on risk, decision-making processes and management style, beneficiary participation, flexibility to change, and theories of change. The merger of two organizations is like a marriage: it can take a long time to find the right person; then the wedding must be planned; and if the marriage is rocky or if there is a divorce, the results can be disastrous for all concerned.
3. Although funders often encourage mergers, there is sometimes a “merger

penalty" in that, good intentions aside, after the merger the funder may provide the merged entity with less funding than it provided to the individual organizations prior to the merger.

4. Boards of directors or board members, often have concerns with respect to mergers, including whether the discussion of merger will be a distraction for the organization. They may also have concerns about how a merger might affect the mission of the organization and its board and officers.

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

6. There may be jockeying for positions within the merged organization. One potential obstacle could arise if there are two permanent CEOs or executive directors who have a long history with their respective organizations; in this case, an important question is who will be the remaining CEO at the end of the merger. It is also very important to build trust between the two parties. Often this happens when charities work together when there is no pressure to merge.

7. Bigger is not necessarily better. Larger organizations often result in higher costs, loss of efficiency, and more bureaucracy, which can reduce the ability to adjust to changing times. Bigger organizations tend to use more staff and fewer volunteers. Often the boards of larger organizations are moved further to a policy-making role and are less actively involved with the charity, which for some is considered a loss. Systems that worked well for each organization individually may not be adequate for the larger merged organization. Most nonprofits spend little on administration/information technology (they lack capacity in this area), and there is less room for savings compared to the for-profit sector. This remains true after a merger. For most nonprofits, 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. In many cases, a merger is not needed in order to realize savings.

8. There may be financial matters that have to be taken into account before a merger. For example, do one or more parties have assets or agreements that may pose particular difficulties, such as restrictions placed on the use of property, special purpose trusts, or funder agreements with rigid requirements that may no longer be met by the merged entity? Keep in mind that many bequest provisions state that the bequest is to a named charity if it still exists on the death of the testator and the type of merger used could affect what happens to the bequest. These matters 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.

9. Well-intentioned merger agreements between parties that may not fully trust each other can result in the merger agreement trying to micromanage the merged organization and put the merged entity into a straightjacket, which is cumbersome and unhealthy for the merged entity.

10. Mergers are expensive, involving time, professional fees, the need to create common technology as well as the need to rebrand the new organization, relocate, train staff on new systems, and make changes in human resources, including, in some cases, terminations. Perhaps the biggest cost is that 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 its 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 struggling organizations get together. A merger may add a burden over and above regular operations, which are already overwhelming the organizations.

11. Some charities are not good at making decisions. If it can take them six months to decide whether to buy a new computer, then how long will it take and how stressful will it be to make a merger happen?

MERGER ISSUES AND STEPS

There are many issues that need to be analyzed before the organizations involved understand whether a merger is appropriate and what steps must be taken to successfully accomplish a merger. There are a few very informative American and Canadian publications on the subject.[4]

The prospective partners to a merger should be clear on the answers to a series of questions and should take certain specific steps.

Questions to answer are:

1. What are the drivers for merger?
2. What are short, medium and long-term goals of merger?
3. Have you carefully indentified a number of possible merger partners and if not, why not?
4. Is this the right time to merge?
5. Are the merger organizations unincorporated, trusts or incorporated?
6. What are the legal objects of each merger partner? Are they acting currently within objects? Will objects need to be changed?
7. Do the organizations have the legal powers necessary to effect the proposed merger? Do either organization need to modify their governing documents?
8. Have the necessary professional advisors, including a lawyer who is knowledgeable about mergers, been retained to assist and give advice on a merger? Is the lawyer knowledgeable about charity law if one of the parties is a charity?
9. How many voting members are there for each organization? Who are the members and will they support merger? What do the statute and by-laws provide in terms of quorum for a members' meeting and can this be achieved?
10. Who are the stakeholders of each organization and will they support merger?
11. Who is going to be the dominant party or will there be equality?
12. 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, and connections does each board member bring?
13. Is the merger in the best interest of both organizations? The directors of an organization must be satisfied that the merger is beneficial.
14. How much time will be spent on the merger discussions, and how long will it take for the merger to take place?
15. How many employees are there? Will all employees move to the merged entity? How many years has each employee worked for the organization? Is a review of factors relevant to termination and severance required? What was last year's total payroll? If one organization is paying its employees more 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, et cetera? Will there be redundancies at some point, 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?

16. Are there any liabilities with respect to either of the parties?
17. Have both organizations been provided with a list of all actual and threatened litigation over the last five years?
18. Has each party reviewed the financial statements and information of the other?
19. Does one or both charities have any special purpose trusts or endowments, and what donor restrictions need to be complied with?
20. What name will the merged entity have, and has it been reserved?
21. Have debts been appropriately identified and dealt with?
22. What are sources of revenue for each organization? Will donors, funders, and earned income be able to continue and be assigned or transferred to the merged entity?
23. Are the organizations' cultures compatible, and is there a fit? Have both parties to the merger successfully completed work together?
24. Is there a communication strategy in place to consult with and communicate with each stakeholder?
25. Is there a plan for implementing the merger?
26. What will the post-merger structure look like?
27. What obligations will the merged entity take on in terms of continuing programs of one or the other organization, if any?
28. Are there any particular consents required for the merger? Are there provincial or federal acts or regulations that could affect the merger such as the Public Hospitals Act (Ontario)[5] for a hospital merger? It is important to 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 or funders.

Steps to take are:

1. Obtain board approval for any negotiations.
2. Have a confidentiality and non-solicitation agreement with any prospective merger partner.
3. Establish a committee or representative from each organization to deal with the merger and establish terms of reference for the committee or representatives.
4. Work together with the other organization to discuss feasibility.
5. 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, valuable equipment, et cetera.
6. Identify all liabilities and ongoing obligations including service agreements, leases, employment, funding agreements, and partnership agreements with domestic and foreign partners.

7. Conduct a comprehensive due diligence process on your potential partner to identify any concerns or impediments to merger.

If a charity and nonprofit are merging, ensure that the activities of the nonprofit are charitable. Also, the nonprofit will have to cease any activities that a registered charity cannot conduct.

Some of the issues arising from these questions and steps can help organizations decide whether, in fact, some sort of cooperation or joint-venture partnership would be more appropriate than a full-scale merger. In some cases, for example, when a Canadian charity and foreign charity are interested in merging, it is easier to retain the two organizations, with their attendant liabilities, assets, and tax status, and to have them work together, with or without interlocking boards or similar memberships. It is vital that the relationship between the two organizations be scrupulously maintained and that the Canadian charity retains direction and control over its resources.

THE MECHANICS OF A MERGER

How a merger takes place depends on the way the various parties are set up and on which entities will survive the merger.[6] For example, if there are three charities—Charity A, Charity B, and Charity C—it is easy to see that there may be many merger possibilities.

A, B, and C could amalgamate. This is often the first thought but sometimes, because of liabilities facing one or more of the partners, it is not the best idea. A could survive, and B and C could transfer their assets to A. B could survive, and A and C could transfer their assets to B. C could survive, and A and B could transfer their assets to C. Or two of the corporations can be amalgamated, and the assets of the third one could be transferred into the amalgamated entity. Or a new corporation (D) could be set up, and the assets of A, B and C could be transferred into D. Alternatively, one of the merger partners could decide it is prepared to merge with only one of the others and not the third. Or all three could decide that merger is not right for them at this time. During the process, one or more of the parties could realize that another party might provide better synergies for a merger.

Different types of organizations will have to look at the feasibility of a merger. In the case of trusts, this means looking at the terms of the trust deed to see whether an amendment is possible. Unincorporated associations should look at the agreement between the members—usually called the constitution. If it does not provide for mergers, consent must be obtained from all members. For corporate mergers, references must be made to corporate law and the letters patent and by-laws of the corporation.

FEDERAL NON-SHARE CORPORATIONS

Federal corporations under the Canada Corporations Act[7] are not allowed to amalgamate. Similarly, a federal corporation and a provincial corporation cannot amalgamate. In order for a merger to take place, either a new corporation must be created and the assets from both transferred into it, or the assets of one corporation must be transferred into the other. If a Federal Special Act corporation wants to amalgamate with another, it

can do so by having a statute passed. However, this is a time consuming, expensive, and uncertain endeavour.

Ontario

Non-share capital corporations of Ontario, under the Corporations Act (Ontario), can amalgamate under section 113 of the Corporations Act (Ontario).[8] This section 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 patent 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 nonprofit corporations wish to amalgamate, as long as they have similar objects, they can amalgamate and continue as one corporation under s.113 of the Corporations Act (Ontario). The organizations will need:

1. to have an amalgamation agreement.
2. to prepare an Application for Letters Patent of Amalgamation (Form 11, prescribed under the Regulations) in duplicate, which will be filed later with the Companies Branch of the Ontario Government.

3. to use a by-law from one of the existing corporations or create a new general by-law.
4. a board resolution of each organization to approve the amalgamation agreement and Letters Patent of Amalgamation.
5. to hold a members' meeting to approve the amalgamation agreement and Letters Patent of Amalgamation.
6. a name. The name of one of the amalgamating corporations may be used or if, there will be a change of name, an Ontario-biased NUANS name search report needs to be obtained.
7. a solvency certificate for 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.
8. to file a Form 1—Initial Return—within sixty days of the amalgamation.

PUBLIC GUARDIAN AND TRUSTEE IN ONTARIO

If the nonprofit is an Ontario non-share capital corporation and a charity, but not necessarily a registered charity with the Canada Revenue Agency, then the Ontario 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 Public Guardian and Trustee.

In Ontario, the Not-For-Profit Incorporators Handbook[9] 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.
>
> *What to send*
>
> The following should be submitted to the Public Guardian and Trustee:
>
> - 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". [They are currently $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.

VIEW OF THE CHARITIES DIRECTORATE OF CANADA REVENUE AGENCY (CRA) ON MERGERS, AMALGAMATIONS AND CONSOLIDATIONS

When Canadian registered charities have relationships with organizations that are not qualified donees under the Income Tax Act (Canada) that are short of amalgamation (e.g., an agency, joint venture, partnership or contractor relationship), the charity needs to be careful that there is no gifting of resources from the charity to the non-qualified donee. For a discussion of various types of relationships between Canadian charities and structured arrangements, you might find my article Canadian Charities and Foreign Activities[10] useful. Although it is geared to Canadian charities working with foreign charities, many of the considerations apply to two nonprofits in Canada working together when one is a qualified donee (e.g., a registered charity) and the other is a non-qualified donee.

When it comes to a merger, CRA wants registered charities to comply with their obligations under the Income Tax Act (Canada).[11]

CRA REGISTERED CHARITY NEWSLETTER 21

In Registered Charity Newsletter #21[12] released in 2005, 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 not 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 **do allow** 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

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.

Registered charities that are changing their charity's legal name must ensure that official donation receipts reflect the new name or they could face substantial penalties.

Other CRA information and concerns

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

If you are planning to modify the objects of one or more charities, you may wish to confirm with CRA that the revised objects are appropriate for a registered charity.

If one of the registered charity corporations is to be dissolved, remember that under the Income Tax Act, a registered charity can only transfer its remaining assets to a qualified donee upon its dissolution.[13] The registered charity cannot transfer its assets to a non-qualified donee, but a non-qualified donee can transfer its assets to a qualified donee. In the case where a Notice of Intention to Revoke a Charity's Registration has been issued, a registered charity can only transfer assets to an eligible donee, rather than qualified donee, during the winding-up period.

For example, if three health-care institutions that are all charities[14] (or if some are charities) amalgamate, the amalgamated entity would need to be a registered charity whether or not they want to have charitable status. Otherwise, if a charity's registration is revoked, the charity must either pay off its legitimate debts and distribute its remaining assets to an eligible donee within one year of the publication of the Notice of Intent to Revoke in the

Canada Gazette or pay a revocation tax in the amount of 100% of the assets. The charity and its directors are responsible for assets that are improperly disposed of.

Another example is the merger of a registered charity and a nonprofit in which the registered charity has liabilities that are greater than its assets and these are being assumed by the nonprofit that is not a registered charity.[15] Since the charity does not then really have any remaining assets after it pays off outstanding liabilities, the net assets that are the subject of the revocation tax are nil.

In some cases a registered charity has a disbursement quota excess while another registered charity has a disbursement quota shortfall. How will CRA deal with such a situation? Like in the case of a merger where one charity has an excess and another one has a shortfall, it would depend on which one is dissolved, the one with excess or shortfall. CRA would take the position that a merged entity cannot use disbursement excesses created by the original charity (i.e., because it has been dissolved). Based on CRA`s definition of "mergers," this also means that if the entity that dissolved had the shortfall the entity with the excess can retain its excess. The same principal holds true for consolidations, because where a new charity is registered and the previous charities are revoked, excesses or shortfalls from the old registered charities will not be transferred to the new entity.

However, for an amalgamation, where two or more registered charities will continue to exist within the BN of another the excesses and shortfalls will probably be netted out.

AGREEMENTS

It is a good idea to have a preliminary agreement to cover 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 that can form the basis of the trust. Later, a merger agreement should be prepared, whether or not there is a formal amalgamation, to cover issues such as the objects and mission and governance of the merged organization, the time lines for merger, the mechanics of how the merger will take place, the governance of the new entity, and other matters. The merger agreement should cover important issues while being flexible enough to allow the new merged entity to respond to events.

LIKELY OPPONENTS OF MERGER

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

1. Board members. Some may be concerned that the mission of the organization could be compromised; others may worry that their numbers will be reduced and that some of them will not be serving on the consolidated board.
2. Employees. They 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.

3. Donors and funding agencies. The merged entity may not be attractive to funders or even eligible for certain funding.
4. Professional advisors. They may be afraid that they will lose a client rather than gain a bigger client and may oppose the notion of a merger.

If you want to ensure that a merger is successful, it is useful to anticipate likely opposition and 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 following situations:

- 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 obligations.
- One party is unwilling to provide full disclosure to the other party.
- One party finds out about litigation that was not mentioned upfront in the merger talks.

TIPS

Here are some tips for managing a merger:

1. Ideally start preparing six months to a year before engaging in any serious discussion with a partner.
2. If you are serious about a merger, clean up the organization. The organization's documents, processes, assets, etc. will be scrutinized like never before. If the organization thinks it will be taken over, this is less important. But it will be difficult for an organization to argue that it should subsume another charity if its governance and documents are a mess.
3. If your organization is going to merge, do it from a position of some strength. Do not wait until your organization is about to go under.
4. Do due diligence on the other organization.
5. Consult extensively with your stakeholders.
6. Be honest and conservative about the benefits of a merger, and be realistic about the costs.
7. Be prepared to walk away from a merger.
8. If your organization is the bigger party to the merger, this does not mean that you have to compromise less. Often it means you have to compromise more.
9. Work hard to develop trust. Usually you need to work together with your prospective merger partner on something before some trust can be developed. Trust can dramatically reduce the time required for merger. Be honest with each other or you will kill any trust that may have developed.
10. 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.
11. Communicate effectively with all stakeholders and involve them in the discussion or expect that there will be greater concern, anxiety and opposition.

12. A legal merger is only a legal merger. For a real merger, you need a well-thought-through integration plan and be prepared for a lot of hard work.

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.

It is more cost effective, both in terms of legal fees and organizational resources, to obtain some legal advice many months prior to the merger. In some cases, lawyers are retained at the end of the process, ostensibly to finalize the details of the merger agreement and then the parties find out that the plan they had been working on for a year and a half is not going to work. Each merger partner should have independent legal advice. Furthermore, if you are planning to have a committed volunteer lawyer or lawyer board member, who do the legal work on a pro bono basis, you should have a plan B. Otherwise, you will probably burn out or alienate the volunteer or board member lawyer. Also keep in mind that you need to get impartial legal 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 nonprofits, especially charities, it is vital to get relevant, accurate, practical, impartial, and timely advice.

Unfortunately, most merger discussions are not handled well, and charities often do not obtain necessary consulting and professional advice and expertise, which results in the merger discussions being more costly, frustrating and less likely to succeed. Most merger discussions never result in a merger. Furthermore, there is rarely an impartial evaluation of the results following a merger. I am guessing if an impartial assessment were made a few years after the merger, it would find that in many cases the costs of the merger were far greater than expected; the benefits far less than expected; and the dislocation and protracted distraction from the organizations' mission far exceeded any value created by the merger. Because of the huge investment made in the merger, many merged entities would not want to publicly or privately admit this.

ACKNOWLEDGEMENT
The author would like to thank Julie Waldman for assisting with this article.

NOTES

[1] An example of joint programming is Uniterra, a Canadian international voluntary program operated by two independent entities, CECI and WUSC, which work together on the volunteer cooperation part of their mandate.

[2] An example of joint fundraising is The Humanitarian Coalition between Care Canada, Save the Children Canada, Oxfam Quebec, and Oxfam Canada, which make joint emergency appeals in major humanitarian disasters.

[3] In my article "Should We Establish another Canadian Charity?" I discuss 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.

[4] David La Piana, *The Nonprofit Mergers Workbook, Part I: The Leader's Guide to Considering, Negotiating, and Executing a Merger*; La Piana Associates' *The Nonprofit Mergers Workbook Part II Unifying the Organization after a Merger* are both excellent resources. For a very helpful guide see "The M Word: A Board Member's Guide to

Mergers" by Alfredo Vergara-Lobo, Jan Masaoka & Sabrina L. Smith. As well, in the Canadian context here is an excellent discussion of mergers in the article "Issues Arising from Mergers and Fusions of Charitable Organizations" by Louise J.A. Greig and M. Elena Hoffstein, *The Philanthropist*, Volume 15, No. 1.

[5] *Public Hospitals* Act R.S.O. 1990, c. P.40.

[6] "Issues Arising from Mergers and Fusions of Charitable Organizations" by Louise J.A. Greig and M. Elena Hoffstein, *The Philanthropist,* Volume 15, No. 1.

[7] *Canada Corporations Act* (1970, c. C-32).

[8] Corporations Act R.S.O. 1990, c. C.38.

[9] The *Not-For-Profit Incorporators Handbook* can be found at: http://www.attorneygeneral.jus.gov.on.ca/english/family/pgt/nfpinc.

[10] See *Canadian Charities and Foreign Activities* http://www.globalphilanthropy.ca/images/uploads/Canadian_Charities_and_Foreign_Activities_-_The_Philanthropist_-_by_Mark_Blumberg.pdf.

[11] *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.).

[12] See CRA Summary Policy CSP-D15 revised March 09, 2009 at http://www.cra-arc.gc.ca/tx/chrts/plcy/csp/csp-d15-eng.html.

[13] See CRA Summary Policy CSP-D15 revised March 09, 2009 at http://www.cra-arc.gc.ca/tx/chrts/plcy/csp/csp-d15-eng.html.

[14] See CRA information letter CIL-1998–029 dated October 16, 1998 at http://www.cra-arc.gc.ca/tx/chrts/plcy/cl/1998/cl-029-eng.html.

[15] See CRA information letter CIL-1999-005 dated February 2, 1999.