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Envision: Implications for Canadian Corporations Contemplating a Merger

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On September 26, 2013 the Supreme Court released its decision in the *Envision*[1] case. The case deals with the amalgamation of two credit unions, but has broader implications for the tax treatment of amalgamations in Canada, and will be of interest to Canadian corporations contemplating a merger in the future.

In 2001, two BC credit unions amalgamated to form Envision. The transaction was undertaken for non-tax reasons, but structured to obtain a particular tax outcome. The amalgamation was carried out under the *Credit Union Incorporation Act* [2] ("CUIA"). Under the CUIA, an amalgamated credit union is the continuation of its predecessors, and deemed to be "seized of" all the property and liabilities of its predecessors.

The relevant provision of the *Income Tax Act* [3] ("ITA") dealing with amalgamations is section 87. Amalgamations which meet the criteria of section 87 of the ITA are known as "qualifying amalgamations". Those which do not are known as "non-qualifying". The distinction is important, because the tax results of a qualifying amalgamation are specified by section 87 of the ITA. The tax consequences of a non-qualifying amalgamation are not and, as confirmed by the Supreme Court, this means that a taxpayer must look to other provisions of the ITA, other statutes and to the common law to determine the outcome.

There are three requirements of a qualifying amalgamation:

1. All of the property of the predecessors must become property of the successor by virtue of the merger;

2. All of the liabilities of the predecessors must become property of the successor by virtue of the merger; and

3. All of the shareholders of the predecessors must receive shares of the successor because of the merger.

Generally, a taxpayer will look to complete a qualifying amalgamation because these are designed to occur on a tax-deferred basis. In the

[1] 2013 SCC 48
[2] RSBC 1996, c.82
[3] R.S.C. 1985, c. 1 (5th Supp.)

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Envision case, the predecessor corporations wanted to complete a non-qualifying amalgamation. They believed that this would result in two tax advantages, one of which is specific to credit unions, the other of which was an increase to the amount of capital cost allowance which the successor could take.

To achieve the desired result, the transaction was designed such that the beneficial interest in certain real property was intended to pass, at the precise moment of the amalgamation, to a subsidiary. The subsidiary issued shares in exchange for the beneficial interest in real property, which shares passed to the successor corporation by virtue of the amalgamation. Envision argued that it had created a non-qualifying amalgamation since not all of the property of the predecessors became property of the successor (breaching condition #1) – some of the property became property of a subsidiary.

The Supreme Court disagreed. It looked first to the CUIA, which deems the successor credit union to be seized of all the assets and liabilities of the predecessor. The court then concluded that this was a mandatory provision, which the predecessors of Envision could not contract out of by virtue of a provision in the amalgamation agreement. The court was clear: 'there is no independent common law power that permits credit unions to amalgamate in a manner that would contradict the terms of the CUIA.'[4] Accordingly, Envision was seized of the real property at the exact moment of the amalgamation, satisfying the condition of section 87 of the ITA. The property was successfully transferred to the subsidiary, but it was done so by Envision as their successor (which was specifically contemplated by the transfer agreement).

Canadian corporations considering a merger in the future should look first at the relevant corporate law statute, to see whether assets and liabilities pass automatically. If they do, section 87 may well provide certainty as to the tax consequences. Corporations may prefer to plan into that provision, since it provides a degree of certainty that non-qualifying amalgamations do not: the Supreme Court declined to comment on how tax attributes of a successor corporation should be calculated for a non-qualifying amalgamation. It is also open to the Ministry of Finance to supplement the ITA, by adding a comprehensive scheme for non-qualifying amalgamations.

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[4] *Envision* at paragraph 33.