Canadian tax alert

COVID-19 – Update on the Canada Emergency Wage Subsidy (CEWS)

April 13, 2020

On April 11, 2020, the federal government convened the House of Commons and Senate in order to enact the CEWS. The legislation contains a landmark stimulus program focused on retaining jobs across Canada in all economic sectors. This enacted version of the CEWS includes several changes to the originally announced program, that provide guidance surrounding a number of previously ambiguous program mechanics. This alert summarizes the CEWS program, highlighting areas where additional guidance has been provided, as well as identifying areas where further clarity may still be required.

Our Tax and Legal team is closely monitoring all government announcements and will remain available to support you during this unprecedented and uncertain time.

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Political context

According to Deloitte's Future of Canada Centre, the final wage subsidy– the second piece of emergency legislation of the COVID-19 pandemic – represents the consensus of a divided House of Commons, after days of talks between the government and opposition parties.

While the government had advocated for use of a virtual Parliamentary sitting to pass the bill, the opposition insisted that the physical legislature meet – albeit with a reduced quorum of only 20 Members of Parliament – so that opposition parties could question the government's general handling of the pandemic. In addition, several negotiated changes were agreed upon for the final version of the legislation. The government has signaled that businesses should expect to wait up to a month before wage subsidy payments will be delivered.

Simultaneously, the federal government considered invocation of the Emergencies Act, a never-before-used law that gives the federal government extraordinary sweeping enforcement authorities, including the ability to streamline health delivery across the country. On Thursday, the federal government sent a letter to provincial and territorial governments consulting on the potential use of the Act. On a subsequent call with premiers across the country, Canada's premiers came to a quick consensus on a key message to the federal government: now is not the time for the federal Emergencies Act.

Summary of the CEWS program

Eligible employer

In order to qualify for the CEWS, an applicant must be an eligible employer, which is one of the following:

a) a corporation (other than one exempt from tax or a public institution);
b) an individual;
c) a registered charity, a non-profit organization or certain other not-for-profit entities (other than a public institution);
d) a partnership whose members are described above; or
e) a prescribed organization.

Public institutions are those described in paragraphs 149(1)(a) to (d.6) of the Income Tax Act, as well as schools, school boards, hospitals, health authorities, and public universities or colleges.

NEW Prescribed organizations are currently not defined, but this provision affords the government future flexibility.

Revenue test and calculation

In order to qualify for the CEWS, eligible employers must be able to demonstrate that their revenues have declined (when compared to a reference period) by more than the requisite percentage during the months in question, as noted in the table below.

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Month	Required revenue percentage reduction	Reference period
March 2020	15%	Same month in 2019 or Average of January and February 2020
April 2020	30%	
May 2020	30%	

Eligible employers will be able to elect whether to use the same month of the prior year or to use the average of their January and February 2020 revenues as their reference period. This election would apply for the duration of the CEWS program.

NEW If an eligible employer satisfies the revenue reduction criterion for its first month of applying for the CEWS, it will be deemed to satisfy the test for the subsequent month. For instance, an employer that meets the 15% test in March will automatically qualify for April, even if it does not meet the 30% test for April. That employer would then be required to re-test its revenues for May, and to satisfy the revenue reduction criterion for that month.

Revenue has been defined as the inflow of cash, receivables or other consideration arising in the course of the ordinary activities of the eligible employer. Revenue from persons or partnerships not dealing at arm's length with the eligible employer will not be considered for purposes of this revenue test. In other words, only revenue from arm's length parties will be considered for purposes of assessing revenue for the CEWS program.

NEW In instances where all or substantially all of an eligible employer's revenues originate from non-arm's length sources, new revenue rules have been introduced. They are outlined below.

Charities and non-profit organizations would have the choice to elect whether or not to include revenues from government sources. This election will apply for the duration of the CEWS program.

Eligible employers have the option to elect to use either a cash or accrual basis for calculating revenue. This election will apply for the duration of the CEWS program.

NEW *Corporate groups and non-arm's length revenues*

Corporate groups will have the option to jointly elect to have their Canadian revenues calculated on a consolidated or stand-alone entity basis. This election would be filed jointly for each eligibility period and would apply to all potential eligible members of the corporate group.

If all or substantially all of an eligible employer's revenue originates from a person with which it does not deal at arm's length, it may still qualify for the program. Such employer will be subject to a modified revenue calculation, whereby if the revenue generated by the non-arm's length person has declined by the requisite percentage, during the relevant reference period, then the eligible employer will qualify. In other words, the revenue percentage reduction test would instead look at the revenues of the non-arm's length person, rather than testing the eligible employer's revenues.

Claiming periods

If an eligible employer satisfies the revenue percentage reduction requirement outlined above, it will be able to access the CEWS for eligible remuneration paid to eligible employees (discussed below) during the following claiming periods:

Revenue month	Claiming period
March 2020	March 15 to April 11
April 2020	April 12 to May 9
May 2020	May 10 to June 6

NEW The legislation provides the government with the ability to extend the program through September 2020.

Eligible employees

Eligible employees are all those employed by the eligible employer, other than those who have gone without pay for 14 or more consecutive days during the claiming period in question. Note that new hires or re-hires can equally qualify for the CEWS program, as long as they meet this definition.

In other words, remuneration paid to employees who received the Canada Emergency Response Benefit (CERB) would not qualify for the CEWS. That said, where employers re-hire previously laid off employees, and retroactively pay them, such remuneration paid can qualify for the CEWS. This would result in the requirement to repay any CERB payments received by employees. Employers should carefully review their employee calculations on a case-by-case basis to determine what may the best outcome for their employees.

Non-arm's length employees

Employees who do not deal at arm's length with the eligible employer can qualify for the CEWS. However, the subsidy would only be available in respect of non-arm's length employees employed prior to March 15, 2020. In other words, an employer cannot begin paying a non-arm's length employee during the claiming periods and access the CEWS program on that remuneration. Subject to the weekly maximum of $847 per week (detailed below), the subsidy wages paid to a non-arm's length employee would be calculated on the least of the pre-crisis (i.e., before March 15, 2020) remuneration and the amount actually paid to the employee during the week for which the CEWS is claimed.

Computation of subsidy

Eligible remuneration

Eligible remuneration may include salary, wages and other remuneration such as taxable benefits. However, it does not include severance pay (or retirement allowances) or stock option benefits.

NEW Remuneration that is expected to be repaid by an employee to the employer (or to a person or partnership not dealing at arm's length with the employer) would not qualify for the CEWS. In addition, the employer would not be able to claim the CEWS on any excess remuneration paid to employees above their baseline remuneration, where employees are being paid more than they were pre-crisis, and where these same employees' salaries would be reduced following the claiming periods. In short, these examples would be seen as attempts to inflate the amount of CEWS receivable by the employer and would therefore not qualify for purposes of the subsidy calculation.

For purposes of the wage subsidy calculation, baseline remuneration (pre-crisis) is defined as the average weekly remuneration paid between January 1, 2020 and March 15, 2020 inclusively, excluding any seven-day periods in respect of which the employee did not receive remuneration.

Wage subsidy

The subsidy amount for a given employee will be calculated as the greater of:

- 75% of the amount of remuneration paid, up to a maximum benefit of $847 per week; and
- The lesser of:
    - the amount of remuneration paid, up to a maximum benefit of $847 per week, or
    - 75% of the employee's baseline remuneration.

Interaction with 10% wage subsidy program

Eligible employers may also qualify for the previously announced 10% wage subsidy. For employers that are eligible for both programs, any benefits received from the 10% wage subsidy program will reduce the 75% subsidy as calculated above.

Interaction with Work-Sharing program

For employers and employees that are participating in a Work-Sharing program, Employment Insurance (EI) benefits received by employees through the Work-Sharing program will also reduce the subsidy as calculated above.

Additional refund of certain payroll contributions

This additional refund will cover 100% of employer-paid payroll contributions (to EI, Canada Pension Plan, Quebec Pension Plan and Quebec Parental Insurance Plan) in respect of eligible employees for each week throughout which those employees are on leave with pay and for which the employer is eligible to claim the CEWS. In general, an employee will be considered to be on leave with pay throughout a week if the employee is remunerated by the employer for that week but does not perform any work for the employer during that week. This refund will not be available for eligible employees who are on leave with pay for only a portion of a week. However, and subject to confirmation from the government, the refund may apply to contributions paid for employees who are on leave and being paid via accrued vacation during the particular week.

This refund would not be subject to the $847 weekly cap per eligible employee.

Application deadline

Eligible employers must file their application, using the prescribed forms, no later than September 30, 2020. The application portal has not yet been opened, but is expected to be launched in the coming weeks. Applications will be made through the Canada Revenue Agency (CRA) *My Business Account* portal as well as through a web-based application. Eligible Employers are encouraged to ensure that they have access to their *My Business Account* so as to minimize any delays receiving the CEWS.

The individual who has principal responsibility for the financial activities of the eligible employer will be required to attest that the application is complete and accurate in all material respects.

Overpayments and penalties

**__NEW__* Mechanics of the refund*

The mechanism by which the CEWS program will entitle eligible employers to refunds is by deeming the employers to have made overpayments of corporate tax. This approach is similar to that used for other refundable tax credits available through the Income Tax Act.

In addition, the legislation provides the CRA with explicit authority to issue immediate refunds of these deemed overpayments, as opposed to only issuing refunds through standard corporate tax compliance processes.

Penalties

Employers that are found to have engaged in artificial transactions in order to qualify for the program, or who are otherwise found to have abused the program, will be required to fully repay the amounts received, as well as pay a penalty equal to 25% of the value of the subsidy claimed. Additional penalties and fines, including imprisonment, as already contemplated by other provisions of the Income Tax Act, may also apply.

Tax treatment of the CEWS

Government assistance

The usual Income Tax Act treatment of tax credits will apply to the CEWS. As a consequence, the wage subsidy received by an employer will be considered government assistance and be included in the employer's taxable income. For clarity, any CEWS amounts expected to be received would not be considered revenue for purposes of the revenue tests outlined above.

Some outstanding issues

In our opinion, the following issues remain unclear and additional guidance would be welcome:

1. Will employers will be required to substantiate that they could not top up the 25% of salaries not covered by CEWS?

2. Will there be any consideration given to entities that have multiple divisions under the same legal entity, where only certain divisions are facing severe revenue declines?
3. When will details around the specific information required in order to complete the application be made available?

For more information on COVID-19, see our [Canadian COVID-19 information hub](#) and our [global COVID-19 information hub](#)

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