Canadian tax alert

COVID-19 – Extension of the Canada Emergency Wage Subsidy (CEWS)

July 29, 2020

The CEWS program was initially enacted on April 11, 2020 and focused on retaining jobs in Canada across all economic sectors. The original program was designed to end on June 6, 2020. However, on July 17, 2020, the Department of Finance (Finance) introduced draft legislative proposals which extended the CEWS program until November 21, 2020, with a potential additional extension through to December 19, 2020, with significant changes to the original program mechanics.

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As highlighted by the consultation process, the proposed legislation addresses the inadequacy of the CEWS program due to the 30% revenue decline threshold required to qualify and the insufficient details provided for future periods.

The proposed legislation received Royal Assent on July 27, 2020.

This tax alert, following last week's alert which gave an overview of the proposed measures, provides more detailed information on the changes to the CEWS legislation.

Key changes to the CEWS program

At a high level, the most significant changes to the CEWS program are as follows:

- the elimination of the revenue threshold effective July 5, 2020, **such that a business with any revenue decline,** irrespective of revenue decline percentage, will be eligible to participate going forward;
- modifying the subsidy such that the amount of subsidy for each employee will **be directly proportional to the revenue decline**;
- increasing the maximum amount of subsidy available for each employee **(from $847 to $960)** for businesses with higher revenue declines (for Periods 5 and 6);
- gradually decreasing the maximum subsidy amount available in **Period 7 through 9** for all businesses; and
- **extending the program** by an additional 12 weeks, through to November 21, 2020, with a new submission deadline of January 31, 2021 for all periods.

The changes are intended to assist businesses in qualifying, albeit the proposed changes fundamentally modify how businesses will compute their CEWS subsidy. With a few exceptions, the changes are effective July 5, 2020 (i.e., for Period 5 and subsequent periods).

To learn more about the initial CEWS program, please refer to our previous tax alert dated April 13, 2020. Broadly, the original program provides qualified employers who have experienced at least a 30% decline in their revenues with a 75% wage subsidy of up to $847/week per eligible employee.

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Summary of modifications

Overall program

The CEWS program now includes the following additional qualifying periods.

Additional period	Qualifying period for wages	Calendar month period to determine revenue declines
Period 4	June 7 – July 4, 2020	June 2020
Period 5	July 5 – August 1, 2020	July 2020
Period 6	August 2 – August 29, 2020	August 2020
Period 7	August 30 – September 26, 2020	September 2020
Period 8	September 27 – October 24, 2020	October 2020
Period 9	October 25 – November 21, 2020	November 2020

Although the program runs until November 21, 2020, the legislation could allow for another one-month extension, as Finance's Backgrounder released on July 17, 2020 indicates a potential Period 10 that begins on November 22, 2020 and ends on December 19, 2020.

Qualifying period refers to the period for which an eligible employer can claim the wage subsidy for wages paid to eligible employees during such period. The corresponding revenue reference periods continue to be calendar-month based.

To qualify for a subsidy in a particular qualifying period, an entity will be required to compute its revenue decline for the particular 2020 calendar month (i.e., the current reference period) that corresponds to the particular qualifying period. Further detail on the computation of revenue decline is discussed below.

The original program mechanics continue to apply for Period 4, with no further changes.

For Period 5 and subsequent periods, the wage subsidy percentage (which remains 75% for the previous periods) will be equal to the sum of:

A. the base rate and
B. the top-up rate, where applicable.

The aim of the amended legislation is to provide enhanced support for businesses with greater revenue declines and, therefore, the top-up rate is only available to businesses with a revenue decline in excess of 50%.

It should be noted that although the maximum wage subsidy for Periods 5 and 6 is $960/week per employee (provided that the maximum top-up rate is achieved), the maximum wage subsidy will be $847/week per employee in Period 7, $734/week per employee in Period 8, and $508/week per employee in Period 9. Effectively, Finance is seeking to broaden the number of employers that qualify, while also reducing the CEWS subsidy available per employee in future periods.

A. Base rate

For Period 5 and subsequent periods, all eligible employers that experience any level of reduction to revenues should, at a minimum, qualify for the base subsidy. The base subsidy is calculated proportionally to the employer's revenue decline, and the amount of the subsidy maximizes when the revenue decline reaches 50%.

The Finance Backgrounder included the table below to outline how the base rate is determined and the related maximum base subsidy available.

Base rate for purposes of the base component of the CEWS					
	Period 5	**Period 6**	**Period 7**	**Period 8**	**Period 9**
Maximum per week per employee	$677	$677	$565	$452	$226
Revenue decline	**Wage subsidy %**				
50% or more	60%	60%	50%	40%	20%
Less than 50%	1.2 x revenue decline	1.2 x revenue decline	1.0 x revenue decline	0.8 x revenue decline	0.4 x revenue decline

Source: Department of Finance.

For example, if an employer experiences a 20% revenue decline in Period 5, their base rate for the subsidy will be 1.2 x 20% = 24%. That is, the employer will be eligible for a base subsidy equal to 24% of eligible remuneration paid to an eligible employee (Example 1). The base rate applies to remuneration of up to $1,129 per week.

For Periods 5 to 9, Finance has continued the automatic qualification deeming rule, with a modification. An employer can use the greater of its percentage revenue decline in the current period or that of the preceding period solely for purposes of determining the base CEWS rate. Therefore, if in Period 4, an employer experienced a decline of greater than 24%, it should be deemed to use the greater percentage revenue decline for its base CEWS rate for Period 5. More details on the automatic qualification are discussed below.

It should be noted that for businesses with revenue declines of less than 50%, this modified scale system significantly increases the burden on businesses to determine their precise revenue decrease, as the revenue decline percentage directly impacts the base rate to be applied.

B. Top-up rate

Employers who experience a revenue decline of more than 50% for their three-month rolling average of qualifying revenue will be entitled to an additional top-up rate of up to 25%.

The top-up rate is computed based on the following formula: 1.25 x (3-month average revenue decline less 50%), with such amount not less than 0% and up to a maximum top-up CEWS rate of 25%. Consistent with the base CEWS rate, the top-up CEWS rate applies to remuneration of up to $1,129 per week.

Businesses with a revenue decline of less than 50% in a period will not be eligible for the top-up rate for that period, rather they would only be entitled to the base rate. Businesses with a revenue decline of at least 70% will be eligible for the maximum top-up of 25% (bringing their aggregate wage subsidy percentage to a maximum of 85% for Periods 5 and 6).

Below is a summary of the maximum CEWS rate and wage subsidy available for each period.

Claim Period	Monthly reference period	Maximum base rate (revenue decline of 50% or more)	Maximum top-up rate (revenue decline of 70% or more)	CEWS rate	Maximum weekly subsidy per employee
Period 5	July	60%	25%	85%	$960
Period 6	August	60%	25%	85%	$960
Period 7	September	50%	25%	75%	$847 (i.e., same as Periods 1 to 4)
Period 8	October	40%	25%	65%	$734
Period 9	November	20%	25%	45%	$508

Source: Deloitte.

Continuing Example 1 described above, if the employer is recovering in Period 5 with a revenue drop of 20%, however, over the preceding three months had an average revenue drop of 60%, the employer would have a base CEWS rate of 24% (being 1.2 x 20%, as mentioned above) and a top-up CEWS rate of 12.5% (being 1.25 x (60% - 50%)), which would result in a combined CEWS rate of 36.5% for Period 5.

Computation of decline in qualifying revenues

The change in an eligible employer's monthly revenues, for the applicable calendar month, must be computed to determine eligibility for the CEWS. Very broadly, with respect to claim Periods 1 to 4, an eligible employer:

(i) is able to compute its revenue decline for each period based on a comparison of the current period revenue against either:
   a. revenue of the same month in 2019 (i.e., a "year-over-year approach"); or
   b. the average of January and February 2020 revenues (an "alternative approach"), or

(ii) that meets the revenue test in the preceding period automatically qualifies for the wage subsidy in the immediately following period.

Base CEWS rate – Period 5 and onwards

Elections for purposes of computing decline in qualifying revenues

For Period 5 and subsequent periods, the following should be noted with respect to the available elections for purposes of computing a decline in an employer's qualifying revenues:

- Regardless of whether an employer chose the year-over-year approach or the alternative approach in Periods 1 to 4, an employer would be able to choose an approach to apply to Period 5 and subsequent periods. For greater clarity, if an employer had elected to use the alternative approach with respect to Periods 1 to 4, it would be able to either continue with the same approach or revert to the year-over-year approach. The same approach must be applied to Period 5 and all subsequent periods.
- If an employer has elected to compute qualifying revenues under the cash method in Periods 1 to 4, the same method must be applied to all subsequent periods (i.e., Periods 5 to 9).
- If an employer that is a charity or a not-for-profit organization has elected to exclude funding received from government sources in determination of its qualifying revenues for Periods 1 to 4, it must continue to apply that election to all its subsequent periods (i.e., Periods 5 to 9).

Accordingly, for Period 5 and subsequent periods, an employer is only provided with a choice with respect to the prior reference period.

Automatic qualification

Irrespective of the approach selected (the year-over-year approach or the alternative approach) in Periods 5 to 9, an employer can use the greater of its percentage revenue decline in the current period or that of the preceding period for the purpose of determining the base CEWS rate. This is intended to be a continuation of the automatic qualification deeming rule that is available to eligible employers during Periods 1 to 4, except now the deeming provision specifically deems the particular revenue reduction percentage, which only impacts the base CEWS rate (and <u>not</u> the top-up CEWS rate, discussed below).

For example, if an employer experiences a 50% decline in its revenues in July and a 30% decline in its revenues in August, the employer would be deemed to have a 50% decline in its revenues for August. Accordingly, the calculation of the base CEWS rate for August would be based on a 50% decline in revenues, even if revenues actually increased in August.

For greater clarity, where an employer has a decline in revenues of 30% in July or August, it should be eligible for a subsidy equal to their entitlement if calculated under the CEWS rules that were in place for Periods 1 to 4 (see further discussion below on the grandfathering of the 75% wage subsidy rate).

Top-up CEWS rate – Period 5 and onwards

An eligible employer's top-up rate is determined based on the revenue decline when comparing revenues in the preceding three months to either:

(i) the revenue in the same three months of the preceding year (i.e., 2019), if the business selects the year-over-year approach; or
(ii) the average of January and February 2020, if the business selects the alternative approach.

As previously outlined, once the revenue comparison approach is determined, it cannot be modified and must be used for both the base and top-up rates for Period 5 and all subsequent periods.

Although a business will be able to utilize the revenue decline percentage for the preceding period for purposes of determining their base CEWS rate, no such flexibility is available for the top-up CEWS rate (i.e., the top-up CEWS is only available for businesses with revenue declines of greater than 50% in that specific period based on their previous 3-month rolling average).

For illustrative purposes, a business would determine its top-up CEWS rate for Period 5 by comparing its April to June 2020 revenue decline against, either:

(i) April to June 2019 under the general approach; or
(ii) January to February 2020 average under the alternative approach.

The Finance Backgrounder included the table below to outline how the top-up rate is determined.

Top-up rate for purposes of the top-up component of the CEWS		
3-month average revenue drop	**Top-up CEWS rate**	**Top-up calculation =** 1.25 x (3-month average revenue decline – 50%)
70% and over	25%	1.25 x (70% - 50%)
65%	18.75%	1.25 x (65% - 50%)
60%	12.5%	1.25 x (60% - 50%)
55%	6.25%	1.25 x (55% - 50%)
50% and under	0.0%	1.25 x (50% - 50%)

Source: Department of Finance.

Grandfathering of 75% wage subsidy rate (safe harbour rule) – Periods 5 and 6

Finance acknowledges that businesses may have made business decisions based on how the CEWS was computed for Periods 1 to 4. Accordingly, for Periods 5 and 6, businesses that would be disadvantaged by the proposed modifications will be eligible for a 75% wage subsidy if such businesses have a revenue decline of at least 30%.

For example, if an eligible employer has a revenue decline of 30% in Period 5, absent this safe harbour rule, the employer would be eligible for a base CEWS subsidy of $406/week per employee. In such a circumstance, the employer is permitted to qualify for a subsidy equal to the amount that they would have been entitled to under the CEWS rules for Periods 1 to 4. One point to consider is that the definition of eligible employee for Periods 1 to 4 is different than that for Periods 5 to 9 (see further discussion below). The grandfathering provision would only impact the calculation of the subsidy amount; it would not circumvent the new definition of eligible employee (or any new elections that may be made that relate to Periods 5 to 9).

For greater clarity, this grandfathering rule will be beneficial for businesses which have a revenue decline of between 30% and 61.9% for the period, as without this grandfathering rule, the wage subsidy percentage would otherwise be between 36% and 74.9% (i.e., less than the 75% subsidy that applied for Periods 1 to 4). See the table below for an illustration.

	Maximum subsidy available per week per employee				
Reference period	June	July	July	August	August
Salary start	7-Jun-20	5-Jul-20	5-Jul-20	2-Aug-20	2-Aug-20
Salary end	4-Jul-20	1-Aug-20	1-Aug-20	29-Aug-20	29-Aug-20
Revenue decline		**No safe harbour**	**Safe harbour**	**No safe harbour**	**Safe harbour**
5%		$68	N/A	$68	N/A
10%		$135	N/A	$135	N/A
15%		$203	N/A	$203	N/A
20%		$271	N/A	$271	N/A
25%		$339	N/A	$339	N/A
30%	$847	$406	$847	$406	$847
35%	$847	$474	$847	$474	$847
40%	$847	$542	$847	$542	$847
45%	$847	$610	$847	$610	$847
50%	$847	$677	$847	$677	$847
55%	$847	$745	$847	$745	$847
60%	$847	$813	$847	$813	$847
65%	$847	$889	N/A	$889	N/A

Source: Deloitte.

It should be further noted that where Period 4 (i.e., June) had a revenue decline of 30% or more, July should be eligible for a subsidy that is equal to at least 75% of remuneration. This is due to the combination of the automatic qualification provision, coupled with the safe harbour rule. Therefore, if July's revenue decline is less than 30%, the automatic qualification provision would deem July's revenue decline to be that of the preceding period (i.e., 30%), thereby triggering the safe harbour rule to allow the employer to be eligible for a 75% wage subsidy. However, the deeming provision does not extend the safe harbour through to August. In August, an employer would calculate its revenue reduction percentage based either on deeming July's actual decline to August or calculating August's actual decline.

Summary of maximum subsidy available per week per employee

Below is an illustration of the maximum subsidy that is available per week per employee, based on the following:

- current month decline in revenues and the average preceding 3-month decline in revenues are identical;
- where an eligible entity's revenues have recovered in a current period, it uses the greater of its percentage revenue decline in the current period or that of the preceding period; and
- the safe harbour rule applies for Periods 5 and 6.

It should be noted that the actual subsidy may vary based on the following:

- Base CEWS and top-up CEWS percentages scale independently based on revenue decline in current month (compared to elected reference period) and average decline in preceding 3-months (compared to elected reference period).
- The potential subsidy for furloughed employees (currently receiving Canada Emergency Response Benefit (CERB)/Employment Insurance (EI)) may vary.

Maximum subsidy per employee per week									
Revenue reference	March	April	May	June	July	August	September	October	November
Start of period	15-Mar-20	12-Apr-20	10-May-20	7-Jun-20	5-Jul-20	2-Aug-20	30-Aug-20	27-Sep-20	25-Oct-20
End of period	11-Apr-20	9-May-20	6-Jun-20	4-Jul-20	1-Aug-20	29-Aug-20	26-Sep-20	24-Oct-20	21-Nov-20
% revenue decline									
5%	$ -	$ -	$ -	$ -	$68	$68	$56	$45	$23
10%	$ -	$ -	$ -	$ -	$135	$135	$113	$90	$45
15%	$847	$ -	$ -	$ -	$203	$203	$169	$135	$68
20%	$847	$ -	$ -	$ -	$271	$271	$226	$181	$90
25%	$847	$ -	$ -	$ -	$339	$339	$282	$226	$113
30%	$847	$847	$847	$847	$847	$847	$339	$271	$135
35%	$847	$847	$847	$847	$847	$847	$395	$316	$158
40%	$847	$847	$847	$847	$847	$847	$452	$361	$181
45%	$847	$847	$847	$847	$847	$847	$508	$406	$203
50%	$847	$847	$847	$847	$847	$847	$565	$452	$226
55%	$847	$847	$847	$847	$847	$847	$635	$522	$296
60%	$847	$847	$847	$847	$847	$847	$706	$593	$367
65%	$847	$847	$847	$847	$889	$889	$776	$663	$437
70% or more	$847	$847	$847	$847	$960	$960	$847	$734	$508

Source: Deloitte.

Other modifications

Amalgamations and asset acquisitions

Legislation has been introduced allowing entities that have made acquisitions during the CEWS program period to have access to modified qualifying revenue determinations. In short, where an entity has amalgamated with an acquired company, or where an entity has acquired assets representing all or substantially all of the fair market value of the seller, the CEWS definition of qualifying revenue will allow for the revenue sources of both entities (acquirer and acquired) to be added together for purposes of calculating revenue reduction percentages. This change applies retroactively to the beginning of the program.

Note that this only applies to asset purchases that meet the "all or substantially all" test. Where an entity only acquires or disposes of some (but not all or substantially all) assets, the legislation, and the administrative policy as expressed in the Canada Revenue Agency's current Frequently Asked Questions, do not allow for any modifications to qualifying revenue when deriving revenue reduction percentages.

CEWS for furloughed employees

The subsidy calculation for furloughed employees in Periods 5 and 6 remains the same as the previous periods. This represents a separation of the mechanics between furloughed employees (e.g., those on leave with pay) and active employees. In short, furloughed employees may still qualify for a 100% subsidy of current period eligible remuneration, whereas active employees may not.

Furthermore, beginning in Period 7, the computation of the CEWS subsidy for furloughed employees may include adjustments to account for benefits provided through the CERB and/or EI programs. The stated intention would be for the maximum subsidy amount to not be less than the amount the individual would otherwise be entitled to under CERB or EI. These specific provisions have not yet been tabled. Additional regulations in this regard are expected.

The employer portion of contributions in respect of the Canada Pension Plan, EI, the Quebec Pension Plan, and the Quebec Parental Insurance Plan in respect of furloughed employees would continue to be refunded to the employer. Note that this refund would not be subject to any form of base or top-up CEWS rates, but would continue to be a full refund, irrespective of the actual percentage revenue decline of the employer.

Baseline remuneration

In Periods 5 and 6, baseline remuneration remains relevant for the following employee scenarios:

(i) employees on leave with pay (i.e., furloughed employees), as the mechanics of the subsidy for these individuals continues to point to the Periods 1 to 4 mechanics; and
(ii) employers relying on the safe harbour provisions, as the mechanics of the subsidy for all active employees points to the Periods 1 to 4 mechanics.

Beginning in Period 7, the CEWS amount will no longer be tied to baseline remuneration other than in the case of non-arm's length employees.

The charts below summarize the baseline remuneration (average paid weekly remuneration) date ranges for each qualifying period, for both arm's length and non-arm's length employees. **Note that the "greater of" mechanics are achieved through an election, which can be made on an employee-by-employee basis.**

Arm’s Length Employees

GREATER OF:	Baseline period	Baseline period	Baseline Period
Periods 1-3	Jan 1 – Mar 15, 2020	Mar 1 – May 31, 2019	N/A
Period 4	Jan 1 – Mar 15, 2020	Mar 1 – May 31, 2019	Mar 1 – June 30, 2019
Periods 5-6	Jan 1 – Mar 15, 2020	Jul 1 – Dec 31, 2019	N/A
Periods 7-9	N/A		

Note that the baseline remuneration for arm’s length employees is only relevant in Periods 5 and 6 if the employer is relying on the safe harbour provisions. Where an employer is instead relying on the new mechanics (e.g., where its declines are less than 30% or more than 62%), then baseline remuneration would no longer be relevant for those employees.

Beginning in Period 7, the concept of baseline remuneration is no longer relevant, as it appears that the subsidy is calculated by multiplying the remuneration by the base CEWS rate and the top-up CEWS rate. That is, there is no tie to the baseline remuneration of arm’s length employees. As a consequence, employers may no longer be able to subsidize 100% of the wages paid to their employees where current wages represent reduced amounts relative to baseline periods.

In prior periods, the CEWS amount was generally the greater of eligible remuneration paid to the employee with respect to the current week, $847, and 75% of baseline remuneration. This allowed an employer to potentially subsidize more than 75% (and in some cases 100%) of their current wages by reducing the wages of their employees post-crisis. However, the mechanics now proposed for Periods 5 to 9 (absent the safe harbour rules) seem to remove this mechanism and instead subsidy amounts for active employees will always be determined as a percentage of current remuneration.

Non-arm’s length employees

GREATER OF:	Baseline period	Baseline period	Baseline Period
Periods 1-3	Jan 1 – Mar 15, 2020	Mar 1 – May 31, 2019	N/A
Period 4	Jan 1 – Mar 15, 2020	Mar 1 – May 31, 2019	Mar 1 – June 30, 2019
Periods 5-9	Jan 1 – Mar 15, 2020	Jul 1 – Dec 31, 2019	N/A

Consistent with the mechanics for Periods 1 to 4, non-arm’s length employees would only be eligible for the subsidy for Periods 5 to 9 where they actually have a calculated baseline remuneration amount. In other words, you cannot receive a subsidy for a non-arm’s length employee, unless that individual was already being paid a salary during the appropriate baseline periods outlined above.

Definition of eligible employee

Effective Period 5, the definition of eligible employee:

(i) refers to any individual employed in Canada, and
(ii) removes the exclusion that previously applied for employees who were without remuneration for 14 or more consecutive days during the period.

This change is a welcome expansion to the CEWS program eligibility, particularly for industries where employees are employed on a rotational basis (for example, 2 weeks on and 2 weeks off). This change to the definition of eligible employee will allow such employers to benefit from the CEWS program on a prospective basis only (i.e., effective Period 5).

Election to use accrual based accounting

Previously, an employer could only elect to use the cash basis to measure revenues. If the employer's normal accounting practices were on a cash method, an employer could not elect to measure revenues on an accrual basis. However, the legislation is amended to allow an eligible employer to measure their revenues either on an accrual basis or cash basis for purposes of computing their revenue decline. Once chosen, the same accounting method would have to be used by the employer throughout all periods of the CEWS program.

Filing deadline

The filing deadline has been extended and an entity must file an application prior to February 2021 (i.e., must be filed by January 31, 2021) in order to be eligible for the wage subsidy.

How can Deloitte help?

If you have questions, please contact your Deloitte representative or any of the individuals noted in this document.

For more information on COVID-19, see our Canadian COVID-19 information hub and our global COVID-19 information hub

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