

April 13, 2020

## The Canada Emergency Wage Subsidy: Increased Assistance on the Horizon

On April 11, 2020, the Federal Government enacted the previously announced (and now enhanced) "Canada Emergency Wage Subsidy" program (the "**CEWS**").

The CEWS is designed to encourage employers that have been grappling with financial challenges to recall employees from layoff, or to keep employees on payroll, while the COVID-19 crisis continues. Wage subsidies under the CEWS may be available for up to 12 weeks, retroactive to March 15, 2020.

For employers that are struggling to meet their payroll obligations, the CEWS provides some relief, but it is important for employers to understand the eligibility and reporting requirements set out below to ensure that they do not run afoul of the restrictions that limit CEWS eligibility.

### Basic Parameters of the CEWS

When available, the CEWS will generally provide eligible employers with a per week subsidy equal to the greater of (i) 75% of the "eligible remuneration" paid to most employees in respect of the week, and (ii) 75% of the average weekly "eligible remuneration" paid to most employees during the period that begins on January 1, 2020 and ends on March 15, 2020, provided that, in either case, the subsidy per employee cannot exceed the lesser of \$847 per week and the amount of eligible remuneration paid to such employees in respect of the week.<sup>1</sup>

"Eligible remuneration" includes most salary, wages and other remuneration payable to an employee, including most fees, commissions or other amounts payable in respect of services. Certain notable exclusions from the definition of "eligible remuneration" include "retiring

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<sup>1</sup> Special computational rules apply in respect of remuneration paid to employees that do not deal at "arm's length" with their employer (such as family members).

allowances" (e.g., certain non-statutory severance payments) and most equity-based compensation, including most amounts in respect of stock options.

Employers may seek wage subsidies in respect of "eligible remuneration" paid during one or more of three separate "qualifying periods": (i) March 15, 2020 to April 11, 2020, (ii) April 12, 2020 to May 9, 2020, and (iii) May 10, 2020 to June 6, 2020. (The Government may add further "qualifying periods" by regulation, so long as no period extends beyond September 30, 2020.)

Wage subsidies will be based on the salary or wages paid by an eligible employer to its "eligible employees". "Eligible employees" are defined as individuals employed in Canada in a qualifying period (other than individuals who are without remuneration in respect of 14 or more consecutive days in the qualifying period).

The amount of the wage subsidies claimed by an employer is technically deemed to represent an overpayment of the employer's income tax under Part I of the *Income Tax Act* (Canada) (the "**Tax Act**"). Employers will be entitled to claim an immediate refund of any such deemed "overpayments".

The amount of any wage subsidies claimed under the CEWS will be characterized as government assistance and, therefore, will be required to be included in computing the employer's taxable income for the year.

## Eligibility for the Subsidy

To be eligible to claim a wage subsidy under the CEWS, an employer must satisfy a number of conditions, including the following:

First, the employer must be an "eligible entity". "Eligible entities" are defined to include (i) corporations (other than tax-exempt corporations and certain "public institutions"), (ii) individuals, (iii) registered charities (other than "public institutions"), (iv) certain non-profit and tax-exempt organizations (other than certain "public institutions") and (v) partnerships, all of the members of which would qualify as "eligible entities"<sup>2,3</sup>.

Second, the employer must generally establish that its "qualifying revenue" for the relevant "current reference period" was equal to or less than 70% of its "qualifying revenue" for the corresponding "prior reference period" (i.e., there must have been a reduction in qualifying

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<sup>2</sup> The definition also accommodates certain "stacked partnership" structures.

<sup>3</sup> The Government has reserved the right to designate further entities as "eligible entities" by regulation.

revenue of at least 30% compared to the qualifying revenue earned during the relevant prior reference period). (However, with respect to the first qualifying "current reference period" (i.e., March 2020), the required reduction in qualifying revenue is less onerous and must only equal or exceed 15%.)

To determine whether an employer has sustained the necessary decrease in qualifying revenue in respect of a particular period, the employer must separately compare its revenue in March, April or May 2020 (each, a "current reference period") to the revenue it earned in the corresponding month of 2019 (each, a corresponding "prior reference period").

Alternatively, an employer may elect instead to compare its revenue earned in a "current reference period" to an average of its monthly revenue earned in January and February 2020. For employers that did not carry on any business on March 1, 2019, the monthly average of the employer's revenue earned in January and February 2020 must be used as the "prior reference period" for comparison purposes.

**Table 1. Relevant Time Periods for the CEWS Program.**

<b>Current Reference Period</b>	<b>Default Prior Reference Period</b>	<b>Elective Prior Reference Period (or for employers that were not carrying on business as of March 1, 2019)</b>	<b>Minimum Reduction in Qualifying Revenue</b>	<b>Qualifying Period</b>
March 2020	March 2019	Average of January and February 2020	15%	March 15, 2020 – April 11, 2020
April 2020	April 2019	Average of January and February 2020	30%	April 12, 2020 – May 9, 2020
May 2020	May 2019	Average of January and February 2020	30%	May 10, 2020 – June 6, 2020

For the purposes of the CEWS, "qualifying revenue" is generally defined as "the inflow of cash, receivables or other consideration arising in the course of the ordinary activities of the eligible entity - generally from the sale of goods, the rendering of services and the use by others of resources of the eligible entity - in Canada in the particular period". The definition of "qualifying revenue" notably excludes extraordinary items and amounts derived from persons or partnerships not dealing at "arm's length" with the eligible entity.

In measuring revenues, an employer may choose to use either the accrual method or cash method<sup>4</sup> of accounting; however, once a computational method is chosen, an employer must continue to use the same method consistently when measuring revenue in respect of subsequent periods.

In response to concerns raised by the business community, the legislation enacting the CEWS also provides some accommodation for enterprises that conduct activities through multiple entities. The new legislation contains additional, permissive computational rules, including the following:

- If a group of eligible entities normally prepares consolidated financial statements, each member of the group may determine its qualifying revenue separately, provided every member of the group determines its qualifying revenue on that basis;
- If an eligible entity and each member of an "affiliated group" of eligible entities (of which the eligible entity is a member) jointly elect, the qualifying revenue of the group determined on a consolidated basis in accordance with relevant accounting principles is to be used for each member of the group.

(This elective provision is aimed at correcting a technical issue that would arise if one member of a corporate group employs staff and its goods or services are provided to entities with which it is affiliated. Under such circumstances, the member might not otherwise have been entitled to claim a wage subsidy under the CEWS because revenue derived from non-arm's length parties is not accounted for in computing qualifying revenues. It is important to note that this relieving rule applies in the context of "affiliated groups", which are specifically defined in section 251.1 of the Tax Act.);

- If all of the interests in an eligible entity are owned by participants of a joint venture and "all or substantially all"<sup>5</sup> of the qualifying revenue of the eligible entity for a qualifying period is in respect of the joint venture, the eligible entity may use the qualifying revenue of the joint venture (determined as if the joint venture were an eligible entity) instead of its qualifying revenue for the purposes of performing the necessary revenue reduction comparison; and
- If "all or substantially all" of an eligible entity's qualifying revenue for a qualifying period - determined without reference to the exclusion of revenue derived from non-arm's length

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<sup>4</sup> As defined in subsection 28(1) of the Tax Act.

<sup>5</sup> The Canada Revenue Agency generally considers "all or substantially all" of an amount to represent 90% or more of the amount.

counterparties - is from persons with which the entity does not deal at arm's length, and each of the non-arm's length counterparties and the eligible entity jointly elect, special computational rules will apply that address certain issues that arise from revenues from non-arm's length parties generally being excluded when computing eligibility under the CEWS.

## Deemed Carryover Rule

To provide greater planning certainty to employers, the CEWS provides that once an eligible entity meets the applicable revenue reduction threshold for a qualifying period, it will be deemed to meet the threshold for the immediately following qualifying period. (For instance, if an employer qualifies for subsidies under the CEWS in respect of the first qualifying period, it will automatically be deemed to have sustained the required revenue loss in respect of the second qualifying period.)

## Anti-Avoidance Rules and Penalties

In an effort to discourage claims for artificially enhanced subsidies, certain anti-avoidance rules have been introduced, which, if applicable, will require an employer to repay amounts received under the CEWS, along with a penalty equal to 25% of the amounts received as subsidies under the CEWS.

## Other Points of Note

Certain other subtle facets of the CEWS warrant special consideration, including the following:

1. It is especially important to submit accurate applications for the CEWS. The CEWS legislation appears to limit an employer's entitlement to subsidies under the CEWS to the amount claimed by the employer in its subsidy application, even if the legislation, properly applied, would have granted the employer a larger subsidy.
2. When submitting an application for subsidies under the CEWS, "the individual who has principal responsibility for the financial activities of the eligible entity [must attest] that the application is complete and accurate in all material respects". The attesting individual will potentially be personally liable for material penalties if the application for subsidies under the CEWS is inaccurate. Individuals that are required to attest to the accuracy of a CEWS application should carefully consider the contents of the application before the application is submitted.
3. Applications for subsidies under the CEWS must be made no later than September 30, 2020.

4. **The name of any employer applying for subsidies under the CEWS may be made public by the Government.** Businesses that are sensitive to the publication of information surrounding revenue losses should carefully consider the prudence of applying for the CEWS.
5. The CEWS contains a number of elective provisions that govern how an employer's revenue is to be computed and the determination of the baselines for revenue comparisons. Once an election is made, the elected rules must be applied consistently across all qualifying periods. As a consequence, care should be taken, and sensitivity analyses should be performed, before any elections are made under the CEWS.
6. Only qualifying entities with employer remittance numbers on March 15, 2020 are entitled to claim subsidies under the CEWS. Accordingly, certain owner-managed enterprises that have historically paid compensation by way of dividends/draws, rather than salary, may be precluded from claiming subsidies under the CEWS.
7. The CEWS requires employers to carefully calculate and report eligible remuneration. Businesses must be mindful that the CEWS applies in respect of eligible remuneration payable to employees, so businesses that use a high number of independent contractors will not be permitted to include such payments in the calculation of eligible remuneration.

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#### [a cautionary note](#)

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