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CEWS Update: Review of New Rules and CRA Guidance

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Introduction

Earlier this year, Parliament enacted legislation adopting the Canada Emergency Wage Subsidy (CEWS) through amendments to the *Income Tax Act* (Canada) (Act). We previously reviewed the initial legislation in detail. Read our earlier [analysis](#).

In a press release issued on May 15, 2020, the federal government announced that the CEWS will be extended for an additional 12 weeks to August 29, 2020, and eligibility will be expanded to include a number of employer entities that may not have otherwise qualified for the CEWS.

The Canada Revenue Agency (CRA) has also released detailed guidance on its "Frequently Asked Questions" page addressing the expanded eligibility criteria and certain interpretive issues arising out of the initial CEWS-related amendments to the Act. We discuss some of the key takeaways from CRA's current guidance below.

Extension of the CEWS Program

The CEWS was initially put in place for the 12-week period running from March 15 to June 6, 2020. However, as noted above, the program has now been extended until at least August 29, 2020. The government also stated in its press release that it intends to consult with business and labour representatives in the coming weeks to consider potential adjustments to the CEWS program, including to the 30% revenue decline threshold required for eligible employers to qualify for the CEWS.

The initial legislation amending the Act to give effect to the CEWS allows the federal government to further extend the CEWS until September 30, 2020, should it choose to do so.

Expanded Eligibility

Prescribed Organizations

Under the CEWS legislation, the government may prescribe additional organizations to be eligible entities for CEWS purposes. In its May 15 press release, the government announced that it had made regulations prescribing the following types of organizations for these purposes:

- partnerships with one or more non-eligible members;
- certain Indigenous government-owned businesses;
- registered Canadian amateur athletic associations;
- registered journalism organizations; and
- non-public educational and training institutions.

These changes are retroactive to April 11, 2020 (when the legislation adopting CEWS was first enacted). Accordingly, prescribed organizations will be able to apply for the CEWS for the first qualifying period starting March 15, 2020, and any subsequent qualifying periods, provided that they are otherwise eligible.

The extended eligibility for partnerships should provide welcome relief for businesses that were previously ineligible for the CEWS due to having one or more non-eligible members, even if such non-eligible members held only nominal interests in the partnership. Under the new rules, partnerships that are not majority-owned by non-eligible entities may now qualify for the CEWS. This would include partnerships in which 50% or more of the interests (measured by fair market value) are held, directly or indirectly through upper-tier partnerships, by eligible entities throughout the qualifying period. Thus, a partnership that is at least 50% owned by a taxable corporation may qualify for the CEWS even if it has one or more members that is a non-eligible entity. Notably, eligible entities must maintain a 50% ownership stake in the partnership throughout the entire qualifying period for it to achieve eligible entity status.

The regulations also extend CEWS eligibility to certain Indigenous government-owned corporations that are carrying on a business. Under the initial legislation, these entities may not have been eligible for the CEWS if they were exempt from tax. Partnerships whose members are all either Indigenous governments or eligible entities are also prescribed organizations and thus eligible entities for purposes of the CEWS.

While public schools and colleges remain ineligible for purposes of the CEWS, private schools and private colleges have been prescribed as eligible entities. This change will permit for-profit and not-for-profit institutions such as arts schools, language schools, driving schools, flight schools and culinary schools to access the CEWS.

Amalgamations and Wind-Ups

The government also announced that it intends to make certain changes to the CEWS program by way of legislative amendment. Unlike the changes discussed above, which were made by way of regulation, the government will need to pass new legislation to implement these proposed amendments.

The first of such proposed amendments will permit a corporation formed by amalgamation, or a corporation into which another has been wound up, to include the qualifying revenues of the predecessor corporations for purposes of calculating its pre-pandemic revenue "benchmark." Thus, for example, in determining whether an amalgamated corporation has experienced the requisite revenue decline in a current reference period, its qualifying revenues for that period would be compared with the combined qualifying revenues of the predecessor corporations for the relevant prior reference period. Absent this rule, an amalgamated corporation could be required to determine its CEWS eligibility by comparing the qualifying revenue of the recently combined business of the amalgamated corporation with the qualifying revenue of a single predecessor corporation.

While this proposed amendment should provide welcome relief to corporations that may have otherwise failed to qualify for the CEWS owing to a recent merger transaction, it is notable that the amendment does not provide relief in the case of asset purchase transactions. For example, if a corporation purchased business assets directly, instead of acquiring the shares of the owner of the business followed by an amalgamation with or a wind-up of the target, the proposed amendment would not permit the acquirer to combine its qualifying revenues with those of the pre-acquisition business to determine its revenue benchmark.

The government intends to supplement this new relieving provision with an anti-avoidance rule that will apply where it is reasonable to consider that one of the main purposes for the amalgamation or winding-up was to qualify for the CEWS. Presumably, amalgamations and wind-ups undertaken prior to the announcement of the CEWS will not be affected by this anti-avoidance rule.

The government proposes to enact this legislative amendment with retroactive effect to April 11, 2020. Thus, corporations that qualify for the CEWS by virtue of these new rules should be eligible to claim the wage subsidy for the initial qualifying period and any subsequent qualifying periods, provided that the requisite revenue declines continue to be experienced.

Additional Flexibility in Determining Baseline Remuneration

The government has also proposed a legislative amendment affecting the determination of an eligible employee's "baseline remuneration." An employee's baseline remuneration serves two critical purposes in determining the amount of the subsidy an employer is entitled to under the CEWS. For arm's length employees, there is an effective eligible remuneration "floor" equal to 75% of an employee's baseline remuneration, up to the weekly cap of \$847, as the CEWS will cover 100% of the employee's eligible remuneration

paid up this amount. The CEWS will then cover 75% of the employee's eligible remuneration exceeding such baseline remuneration (again, subject to the \$847 weekly cap).

For non-arm's length employees, there is an effective eligible remuneration "ceiling" equal to an employee's baseline remuneration, provided that such baseline remuneration does not exceed the \$847 weekly cap. Any eligible remuneration paid above this amount is ineligible for the wage subsidy. Thus, in respect of both arm's length and non-arm's length employees, higher baseline remuneration figures can result in a greater subsidy received.

Under the current CEWS legislation, an employee's baseline remuneration is calculated for the period beginning January 1 and ending March 15, 2020, excluding any period of seven or more consecutive days without remuneration. As a result, employers could receive lower than intended subsidies in respect of seasonal employees or employees who were on unpaid leave during this time. The proposed amendment seeks to address this issue by permitting employers to determine an employee's baseline remuneration using either the January 1 to March 15, 2020 period or, alternatively, the period beginning March 1 and ending May 31, 2019, excluding in either case any period of seven or more consecutive days without remuneration.

The government announced that this proposed amendment will be retroactive to the first qualifying period and thus employers should be permitted to use the new determination period for all qualifying periods. The choice of period can be made on an employee-by-employee basis in respect of both arm's length and non-arm's length employees. As discussed above, it will generally be favourable for an employer to select the period that results in a higher baseline remuneration figure.

Restricted CEWS Eligibility for Certain Trusts

Effective for the May 10 to June 6, 2020 qualifying period and subsequent qualifying periods, the government is also proposing to amend the Act to restrict the CEWS eligibility of certain trusts. Specifically, the government proposes to limit the availability of the CEWS in the following circumstances:

- where a trust is a tax-exempt entity (other than a public institution), it will qualify for the CEWS only if it is a registered charity or one of the other types of eligible tax-exempt entities; and
- where a trust is a public institution, it will qualify for the CEWS only if it is a prescribed organization.

Relevant CRA Guidance

Consolidation by Affiliated Groups

In our initial review of the CEWS legislation, we discussed the rules permitting affiliated entities to determine their eligibility for the wage subsidy on a consolidated basis. In particular, we noted that the legislation is ambiguous with respect to whether a smaller affiliated group within a larger affiliated group can elect to consolidate for CEWS purposes. The CRA has addressed this ambiguity in its administrative guidance, stating that the consolidation election must be made by the broadest affiliated group of eligible entities possible and not a subset of that group. Thus, a smaller affiliated group cannot elect to consolidate to the exclusion of other members within the larger affiliated group. However, as noted in our previous analysis, only the Canadian revenue of the affiliated group is counted, and thus revenue fluctuations among foreign affiliates within a corporate group generally are not considered in determining CEWS eligibility.

The CRA also provided some favourable administrative guidance regarding affiliated groups by affirming that a prior decision to make the consolidation election for a qualifying period is not binding on subsequent qualifying periods. Consequently, an affiliated group can determine for each qualifying period whether to report its revenues on a consolidated basis or individually and elect accordingly. Given that provincial COVID-19 quarantine measures are expected to be lifted in stages, certain members within an affiliated group may be permitted to resume normal operations before other group members. In those cases, this election optionality should provide affiliated groups with the flexibility to select the optimal revenue computation method for their particular circumstances.

CEWS Eligibility of Non-Residents

Canadian residency is not a prerequisite for CEWS eligibility. Thus, a non-resident entity that qualifies as an eligible entity can access the CEWS if it satisfies the other program requirements – namely, employing eligible employees in Canada and experiencing the requisite decline in qualifying revenue. In addition, the CRA has confirmed that a non-resident that is exempt from Canadian income tax by virtue of one of Canada's tax treaties should not be prevented from obtaining eligible entity status on that basis alone.

Likewise, the CRA has confirmed that a non-resident individual employed in Canada during a qualifying period can be an eligible employee so long as all of the other conditions under that definition are met.

Retroactive Pay

The CRA has confirmed that an eligible entity may claim the wage subsidy in respect of retroactive eligible remuneration paid to eligible employees that were previously laid off. To access the subsidy in respect of such retroactive pay, an eligible entity must retroactively rehire the employee in respect of a particular qualifying period and ensure that the employee is not without eligible remuneration for a period of 14 or more consecutive days in the qualifying period.

New Hires

The CRA has also indicated that eligible entities may claim the CEWS in respect of eligible remuneration paid to arm's length employees hired after March 15, 2020. However, the CEWS will not be available in respect of eligible remuneration paid to non-arm's length employees who are hired after this date.

Cause of Revenue Decline

Consistent with the government's prior announcements regarding the CEWS, the CRA has confirmed that an applicant is not required to demonstrate that its revenue decline occurred as a result of the COVID-19 pandemic. The mere existence of the requisite decline in qualifying revenue (15% for the first qualifying period and 30% for the two subsequent qualifying periods) is sufficient to meet the revenue reduction requirement.

Amending CEWS Applications

The CRA has indicated that it will be possible to file amendments to previously submitted CEWS applications as of June. Presumably, this will permit applicants to revise applications in light of the proposed retroactive amendments, such as those affecting the computation of baseline remuneration, though the CRA has not yet commented on the scope of permitted amendments.

Continued Privacy Concerns

As discussed in our initial review of the CEWS legislation, wage subsidy applicants do not benefit from the usual confidential treatment of taxpayer information collected under the Act. On the contrary, the CEWS legislation provides that the name of any applicant for relief may be publicized in any manner the government considers appropriate.

The CRA has confirmed in its guidance that, indeed, it intends to publish a list or registry of CEWS applicants.

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