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# Memorandum

**To:** Clients

**From:** Kakkar CPA Professional Corporation

**Date:** May 22, 2020

**Re:** Canada and Quebec COVID-19 response plan – Emergency Measures related to the Canada Emergency Wage Subsidy (“CEWS”) and the National Research Council of Canada Industrial Research Assistance Program Innovation Assistance Program

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The Governments of Canada and Quebec announced a series of tax measures to help support those affected by the COVID-19 virus, some of which affect tax filing and payment deadlines.

This Memo details the Canada Emergency Wage Subsidy (i.e. the 75% Subsidy) and the National Research Council of Canada Industrial Research Assistance Program (NRC IRAP) Innovation Assistance Program (“IAP”).

We have issued a separate memo detailing the other emergency measures.

We have also issued a separate memo detailing the extensions available to tax filings and tax payments.

## **Canada Emergency Wage Subsidy (the “Wage Subsidy”)**

The Government has enacted a 75% wage subsidy to “eligible entities” for up to twelve weeks, retroactive to March 15, 2020. It is expected that this will allow businesses to prevent further job losses and re-hire workers previously laid off.

The amount of the Wage Subsidy would be the greater of:

- 75% of the amount of remuneration paid, up to a maximum of \$847 per week; and
- The lesser of the amount of actual remuneration paid, up to a maximum of \$847 per week or 75% of the employee’s “Baseline Remuneration”

“Baseline Remuneration” is the average weekly remuneration paid between January 1, 2020 and March 15, 2020, excluding any seven-day periods in respect of which the employee did not receive remuneration.

The Government has proposed that the definition of Baseline Remuneration be extended to include the average weekly remuneration paid to employees between March 1-May 31, 2019. This is meant to cover situations whereby employees are employed on a seasonal basis rather than a permanent basis.

Employers would be able to choose which period to use on an employee-by-employee basis. This change is to be retroactive so that it applies to the qualifying period beginning March 15, 2020. The Government has not announced any further specific details on this point.

Note that remuneration does not include severance pay or stock option benefits, nor does it include dividends.

There would be no overall limit on the subsidy amount that an eligible employer may claim. Eligible entities must make their best effort to top-up employees’ salaries to bring them to pre-crisis levels.

A special rule will apply to employees that do not deal at arm’s length with the employer. The Wage Subsidy for such employees will be limited to eligible remuneration paid, to a maximum of \$847 per week or 75% of the employee’s “Baseline Remuneration”. This prevents an employer from increasing a non-arm’s length subsidy post-COVID-19 and claiming an increased subsidy. The subsidy is only available in respect of non-arm’s length employees employed prior to March 15, 2020.

If an employee is employed by two employers that are not at arms’ length from each other, the subsidy must be calculated as if the employee earned the combined remuneration for one employer (ie the two employers cannot each claim a subsidy for the same employee).

Employers who have laid off employees and then hire them back retroactively may claim the subsidy once the employees are paid retroactively for the claim period.

CRA has confirmed that if a pay period does not align with the subsidy claim period, the employer must manually calculate how much remuneration is paid in respect of the claim period. This cannot be done on the basis of average daily wages paid. If employees are paid different amounts on each day (i.e. shift workers), the employer must use the actual amounts paid for each day and cannot use an average. An employer must have paid its workers for the entire claim period before it can claim the subsidy (e.g. if an employer pays its salaries monthly on the last day of each month, it must wait until April 30<sup>th</sup> to claim the subsidy for the claim period of March 15-April 11).

The Government has also expanded the Wage Subsidy by allowing a 100% refund for employer-paid contributions to EI, CPP, QPP and QPIP. The refund would be allowed for each week in which an employee is on leave with pay for that week. The refund would be determined on an employee by employee basis. The refund is over and above the weekly maximum of \$847 that is discussed earlier. Employers still need to collect and remit source deductions until such time as they apply for the refund, which is done concurrent with the application for Wage Subsidy.



Eligible entities that can apply for the Wage Subsidy include:

- Individuals
- Taxable corporations
- Partnerships consisting of at least 50% eligible entities
- Non-profit organizations
- Registered charities

The Wage Subsidy is available to eligible entities that incur a decrease of 15%-30% of their revenue from arm's length sources, from a business carried on in Canada, excluding extraordinary items and capital gains, on the following basis:

	<b>Qualifying Period</b>	<b>Required reduction in revenue</b>	<b>Reference Period for Eligibility</b>
<b>Period 1</b>	March 15 to April 11	15%	March 2020 over: <ul style="list-style-type: none"> <li>• March 2019 or</li> <li>• Average of January and February 2020</li> </ul>
<b>Period 2</b>	April 12 to May 9	30%	April 2020 over: <ul style="list-style-type: none"> <li>• April 2019 or</li> <li>• Average of January and February 2020</li> </ul>
<b>Period 3</b>	May 10 to June 6	30%	May 2020 over: <ul style="list-style-type: none"> <li>• May 2019 or</li> <li>• Average of January and February 2020</li> </ul>

The Federal Government has announced that the Wage Subsidy will extend the CEWS by an additional 12 weeks to August 29, 2020.

If the eligible entity was not carrying on business on March 1, 2019, it uses the average of January 2020 and February 2020 as its prior reference period. This is meant to allow “start-up” entities access to the Wage Subsidy.

If the eligible entity was carrying on business on March 1, 2019, it would use the corresponding month in the prior year as its prior reference period (i.e. March 2019 for Period 1, April 2019 for Period 2, etc) or it may elect to use January and February 2020 as its prior reference period. If the eligible entity so elects, it must use January and February 2020 as its prior reference period for all periods. This is meant to allow entities that have season fluctuations in their revenue access to the Wage Subsidy. The election is to be kept on file but is not required to be filed with CRA unless CRA specifically requests it.

The basis for the Wage Subsidy is “qualifying revenue,” which refers to the sale of goods, rendering of services, or use by others of resources, in the course of ordinary activities, to be determined in



accordance with “normal accounting practices” (the legislation does not define this term). Interest and dividends can form part of qualifying revenue if they are part of the entity’s ordinary activities.

Extraordinary items, amounts derived from non-arm’s length persons or partnerships and the subsidy itself are all excluded from the determination of qualifying revenue.

Extraordinary items are not a defined term, however CRA has offered the following guidance as to what an extraordinary item would be (note that all 3 conditions must be met):

- Not expected to occur regularly or frequently
- Not typical of the normal activities or risk inherent in the normal operations AND
- Primarily out of the control of owners or management

There are certain elective rules which expand the scope of qualifying revenue:

#### Groups Which Prepare Consolidated Financial Statements

- If a group of eligible entities normally prepares consolidated financial statements, each member of the group is permitted to determine its revenue on a “stand-alone” basis
- Consolidated is not a defined term. The accounting concept of consolidation refers only to a parent-subsidiary relationship. Therefore, if this is taken literally, “combined” financial statements may not meet this condition. CRA has not offered any guidance on this point.
- No election is required but every member of the group must use “stand-alone” revenue for this rule to apply.

#### Affiliated Groups

- An affiliated group of eligible entities is permitted to use qualifying revenue on a consolidated basis as a proxy for the “stand-alone” revenue for each member of the group.
- All members of the affiliated group must jointly elect in each period. The election is to be kept on file but is not required to be filed with CRA unless CRA specifically requests it.

#### Joint Ventures

- If all interests in an employer are owned by participants in a JV, and >90% of the qualifying revenue of the employer is in respect of the JV, the employer may use qualifying revenues of the JV as a proxy for its “stand-alone” revenue
- No election is required

#### Non-Arm’s Length Revenue

- If an eligible entity’s qualifying revenue is all or substantially all (generally, equal or greater than 90% but CRA will accept a lower percentage if the circumstances warrant) from non-arm’s length persons or partnerships, the eligible entity is permitted to calculate its qualifying revenue by a certain formula which incorporates qualifying revenue earned by the non-arm’s length sources,
- The eligible entity and all non-arm’s length sources must jointly elect. The election is to be kept on file but is not required to be filed with CRA unless CRA specifically requests it.



CRA has clarified that, for the above special rules, an eligible employer need not use the same special rule for each claim period, and may choose to apply a different approach in a subsequent period, provided that all requirements are met for the application of the different rule.

CRA has clarified verbally in French that WIP earned by professional firms may be considered part of qualifying revenue and this would depend on the method of accounting normally followed by the practitioner. CRA also commented that the treatment of WIP for income tax purposes has no bearing on whether or not it is qualifying revenue for the purposes of CEWS.

An employer may use the cash method (defined in ITA subsection 28(1)) to determine its revenues. The employer must elect to use the cash method and this election must apply for all qualifying periods. The election is to be kept on file but is not required to be filed with CRA unless CRA specifically requests it.

Eligible entities are responsible for keeping records substantiating the loss in revenue. An individual who has principal responsibility for the financial activities of the entity will be required to “attest” that these records are correct upon application of the Wage Subsidy. The attestation is performed on CRA form RC661, which should be signed and kept on file. Eligible entities should expect that CRA will ask to review them at a later date.

Eligibility for the Wage Subsidy of a particular employee’s remuneration will be limited to employees that have **not** been without remuneration for more than 14 consecutive days in the eligibility period. (i.e. only those employees who have been paid for 14 consecutive days can have their wages subsidized). This rule replaces the previously announced restriction that an employer could not claim the Wage Subsidy for the same period in which an employee is eligible for the Canada Emergency Response Benefit (“CERB”), presented in a separate memo detailing other measures.

The Government has proposed that corporations that have amalgamated in the past year be allowed to calculate Qualifying Revenue based on the combined revenues of the predecessor corporations that existed prior to the amalgamation. Previously, this was not allowed under on the enacted legislation. This change is to be retroactive so that it applies to the qualifying period beginning March 15, 2020. The Government has not announced any further specific details on this point.

For eligible entities and employees that are participating in a Work-Sharing program, EI benefits received by employees through the Work-Sharing program will reduce the benefit that their employer is entitled to receive under the CEWS.

The application for the Wage Subsidy will be managed through a new CRA portal. Starting Monday, April 27, 2020, eligible entities will be able to subscribe to the CEWS. **However, The Government also commented that it may take six weeks for the funds to be released and distributed to the eligible entities.** A calculator is available online to estimate the amounts to which the eligible entities might be entitled to at the following address: <https://www.canada.ca/en/revenue-agency/services/subsidy/emergency-wage-subsidy.html>

Eligible entities should create an online CRA account immediately if they do not already have one so that they can access the portal when it is available. **Eligible entities who qualify the Wage Subsidy**



**for a certain period automatically qualify for the immediate subsequent period. Otherwise, eligible entities will have to apply on a monthly basis.**

Beginning June 1, 2020, Eligible Entities will be able to request adjustments to claims they have submitted. The Government has not released any further details on this point.

The Wage Subsidy will be considered taxable income to the eligible entity.

For those eligible entities that qualify for both the Wage Subsidy and for the Federal 10 per cent Temporary Wage Subsidy (the “10% Subsidy”) announced on March 18, 2020, any benefit received from the 10% Subsidy would reduce the amount available to be claimed under the Wage Subsidy.

It is important to note that, for the purposes of calculating the Wage Subsidy, an entity is always deemed to have received the 10% Subsidy if that particular entity qualifies for it. However, the Government has announced that an entity may make its claim for the Wage Subsidy on the basis that it is forgoing the 10% Subsidy. This is a change from the Government’s previous position whereby entities were required to reduce their claim for Wage Subsidy by the notional amount of the 10% Subsidy to which they are entitled, even if they chose to forgo the 10% Subsidy.

If an entity opts to forgo the 10% Subsidy, it will be able to file a form with CRA to apply for a reinstatement of the above reduction in Wage Subsidy. Specific details on this point have not yet been released.

The following entities are eligible for the 10% Subsidy:

- Canadian-controlled private corporations (“CCPC”) with at least \$1 of business limit
- Individuals (excluding trusts)
- Partnerships, provided all partners are CCPC’s, individuals (other than trusts), other partnerships, or registered charities
- Non-profit entities
- Registered charities

The 10% Subsidy will be equal to 10% of remuneration paid during the period of March 18, 2020 and June 19, 2020 (the “Period”), up to a maximum subsidy of \$1,375 per employee and \$25,000 per employer.

The 10% Subsidy is further discussed in our “Other Emergency Measures” Memo.

If it is subsequently determined that an Employer applied for the subsidy where it was not entitled to do so, it will be required to repay the subsidy as well as continue to pay its employees accordingly. Penalties may apply. Further, “anti-abuse” rules will be proposed to ensure that the subsidy is not inappropriately obtained and to ensure that employees are paid the amounts they are owed. Eligible entities that engage in “artificial” transactions to reduce revenue so as to increase access to the Wage Subsidy could be subject to a penalty equal to 25% of the subsidy claimed, in addition to repayment



of the subsidy that was improperly claimed. CRA has further commented that a 50% gross negligence penalty could apply, based on the difference of the subsidy claimed vs the subsidy granted. The Government made a verbal comment that if an Employer applied for the subsidy where it was not entitled to do so, it could face a penalty of up to 225% of the subsidy. This was not written in any of the Government Backgrounders.

More details will follow once they are released by the Government.

The following example was published on the CRA website:

An employer has four full-time employees, each earning \$800 per week, and six part-time employees, each earning \$400 per week. The employer has closed its shop and is fulfilling online orders only. All 10 employees have been kept on payroll and paid their regular wages. During March 2020, their revenues have decreased by 30% from March 2019. Therefore, the employer is eligible for a weekly Wage Subsidy of \$4,200<sup>1</sup> for wages paid during the period of March 15-April 11, 2020. This is assuming the employees were not claiming the CERB during this time.

Furthermore, CRA has published a FAQ section on the CEWS, available at:

<https://www.canada.ca/en/revenue-agency/services/subsidy/emergency-wage-subsidy/cews-frequently-asked-questions.html>

Some of the important information that was released in these FAQs is as follows:

- The employer is under no obligation to prove to the CRA that the decline in revenue was in fact related to COVID-19;
- An employer can hire an employee back and pay them retroactively and if the employee has received the Canada Emergency response Benefit (“CERB”) from the CRA for a claim period there are ways by which the employee can return or repay the CERB amount.

It is the employees’ responsibility to determine their eligibility for the CERB for any given period, while it is the employers’ responsibility to ensure that the employee has not received eligible remuneration for more than 14 consecutive days in a claim period.

- Non-resident employees can be eligible employees, as an eligible employees’ status is determined based on where the individual is employer and not where the individual resides.
- For most complete applications (starting April 27<sup>th</sup>, 2020) that pass through CRA’s system validations, a payment will be issued automatically, though some applications

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<sup>1</sup> \$800 x 75% x 4 = \$2,400 for their full-time employees and \$400 x 75% x 6 = \$1,800 for their part-time employee = \$4,200 in aggregate



will be selected for a pre-claim review, in which case the CRA will contact you and you can generally expect to receive the payments within 10 business days;

- Employers will be expected to report the amount of the wage subsidy that was used to pay each of their employees' salaries by a special code in the "other information" area of the bottom of the employees T4 slip.
- The wage subsidy will not be automatically applied against any outstanding CRA debt, however, the legislation does provide CRA with that ability and the CRA does have the discretion to reduce the amount of the wage subsidy payment if an applicant owes or is about to owe a debt that the CRA determines that there is a risk of not collecting.
- To ensure compliance, the CRA will use a combination of automated queries, follow up phone calls to verify certain elements of the claim. This may also include a more comprehensive post payment audit or review.

The CRA's verification of these claims will change over time based on its experience with processing the verification of the claims.

The employer will be required to repay the amounts paid under the wage subsidy program if the CRA determines they do not meet the eligible requirements for the claim and as such the employer may also be subject to:

1. A penalty of 25% of the amount of the claim;
  2. A gross negligence penalty of up to 50% of the difference between the amount of the wage subsidy that it claimed in its application and the amount of the wage subsidy to which it is entitled to;
  3. If the claim is fraudulent the penalties may include fines up to 200% and even imprisonment.
- The CRA will expect all claimants to maintain adequate books and records to ensure that the claim is accurate and complete in accordance with section 125.7 of the Act; these books and records can include:
    - a. Ledgers;
    - b. Journals;
    - c. Financial statements;
    - d. Contracts;
    - e. Elections;
    - f. Calculations and
    - g. Other working papers as necessary





- h. An analysis of the nature of the eligible remuneration meaning dividends and other ineligible remuneration should be recognized and be clearly indicated as removed from the calculation.

Furthermore, to support the revenue decline, there should be adequate calculations and details of any assumptions made by the claimant available for the review of the CRA;

The attestation from the individual responsible for the financial information should also be retained in the records.

- If an accountant or tax preparer does file for the claim they themselves could be subject to third – party penalties under the Act, if they know, or would reasonably be expected to know that the application contains false statements or omissions of information.
- To apply for the wage subsidy representatives authorized at level 2 or 3 access can apply on behalf of their clients via the represent a client service or through a web forms application via: [www.canada.ca/taxes-iref](http://www.canada.ca/taxes-iref).

### **The National Research Council of Canada Industrial Research Assistance Program**

The National Research Council of Canada Industrial Research Assistance Program (“NRC IRAP”) provides advice, connections, and funding to help Canadian small and medium-sized businesses increase their innovation capacity and take ideas to market.

On April 17, 2020, the Government of Canada announced \$250 million in funding for the Innovation Assistance Program (“IAP”) to assist Canadian small and medium-sized enterprises (“SMEs”).

IRAP IAP provides a wage subsidy to eligible employers for up to 12 weeks.

SMEs pursuing technology-driven innovation who have been unable to secure funding under the CEWS are eligible and can apply for financial assistance under IRAP IAP.

Applications must be made between today and Wednesday, April 29, 2020 at 11:59 pm EDT.

More details about the specific measures taken by each government can be found at:

<https://www.canada.ca/en/department-finance/economic-response-plan/wage-subsidy.html>

[https://nrc.canada.ca/en/support-technology-innovation/nrc-irap-innovation-assistance-program-iap?utm\\_campaign=IRAP\\_funding\\_program&utm\\_medium=link\\_to\\_program\\_page\\_e&utm\\_source=home\\_page\\_e](https://nrc.canada.ca/en/support-technology-innovation/nrc-irap-innovation-assistance-program-iap?utm_campaign=IRAP_funding_program&utm_medium=link_to_program_page_e&utm_source=home_page_e)

