Design Flaws in the Covid-19 Wage and Rent Subsidy Programs in Canada

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Abstract

While the central criterion of the Canada Emergency Wage Subsidy (CEWS) and the Canada Emergency Rent Subsidy (CERS) during Covid-19 was a requisite Revenue Reduction Percentage (RRP), we illustrate how a business with modest *increases* in revenue can be eligible for, and receive CEWS and CERS. These outcomes are feasible because rules under both programs allowed applicants the choice to demonstrate their revenue reductions under a cash accounting method, plus an additional choice that allowed applicants to assess their revenue reductions in relation to a baseline determined by an average of two months immediately prior to the pandemic (January and February 2020). Using the CEWS and CERS calculators on the Canada Revenue Agency (CRA) portal, we show how a firm that earns a vast majority of its revenues from annual subscriptions collected in the first two months of the calendar year can report sufficient reductions in revenue determined under cash method of accounting to be eligible for CEWS and CERS during all the months in which these two programs were in effect. Such a firm could receive CEWS and CERS despite enjoying modestly higher revenues during the Covid-19 pandemic. It also appears that these design flaws have not been fixed in the new Tourism and Hospitality Recovery Program (THRP) and the Hardest-Hit Business Recovery Program (HHBRP) launched in November 2021. These design flaws could be fixed by requiring firms that reported revenue reductions using the cash accounting method to use only the baseline of the same period in 2019 (e.g., May 2020 vs. May 2019), or to not allow the cash accounting method for assessing monthly revenue reductions, or both.

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Introduction

The Canada Emergency Wage Subsidy (CEWS) was rolled out by the Canadian federal government as a wage subsidy for businesses experiencing a prespecified decline in revenues during the Covid-19 pandemic. Businesses that retained their employees could apply for and receive CEWS on behalf of their employees. Businesses were strictly intended to be the conduit for the employees, and CEWS was only available for employees retained. While there was no requirement to renounce layoffs, firms did not receive CEWS for employees that were not retained.

In the absence of vaccinations and antivirals, CEWS was a necessary program as the economy slowed down driven by an insufficient demand for activities requiring close physical interactions (such as restaurant dining, airline flights and retail shopping), and deficient supply of things compatible with social distancing (such as communications technology and deliveries or supply chain logistics). With schools closed, parents were often not able to fully return to work, nor did they want to venture out for nonessential trips. The significant decline in demand and supply of non-essential goods reflected consumers' and employees' focus on their well-being instead of their normal consumption and production activities. CEWS enabled businesses to retain their employees and remain prepared when things returned to normal. CEWS could also be viewed as part of an organization's corporate social responsibility. Managing employees by viewing them as internal customers could contribute to their job satisfaction, retention and productivity. Keeping employees productive and healthy maintained their interests aligned with those of the shareholders (Mawani 2020a and Mawani and Hajee, 2020). Gosselin, Godbout, Gagné-Dubé and St-Cerny (2020) favourably describe the Canadian government's initial and rapid launch of subsidy programs, and how it tried to help just about everyone. Li, Bao, Hu and

Zerbino (2020) describe the Canadian government's reliance on tax policy and fiscal instruments to support workers and business during Covid-19.

The eligible wage subsidy was the greater of 75% of pre-crisis weekly wage and the actual weekly wage paid to the employee during the Covid-19 pandemic, up to a dollar limit per week per employee.[1] Employers satisfying the requisite Revenue Reduction Percentage (RRP) criterion for CEWS eligibility were often reimbursed 100% of wages paid if they offered reduced wages during the Covid-19 pandemic. For example, if the pre-crisis weekly wage was $1,000 and the weekly wage paid during the pandemic was $750 (presumably for less work during the pandemic), then the employer would be reimbursed 100% of the $750 weekly wage paid since it was not greater than 75% of the pre-crisis wage, and as long as it was not greater than the weekly dollar limit.

The Canada Emergency Rent Subsidy (CERS) was also implemented during Covid-19 and shared the RRP as the central requisite criterion. Both the CEWS and CERS programs were delivered via the "tax pipeline" administered by the Canada Revenue Agency (CRA). This channel was expeditious since all businesses already had an account with the CRA, and subsidy amounts – once approved – could be deposited into the bank accounts linked with the taxpayers' accounts in a manner similar to any income tax refunds.

Since its launch in May 2020, the federal government has paid out $98.6 billion in CEWS subsidies for 4,840,590 approved applications (a 99.3% acceptance rate) from 457,630 unique applicants.[2] This program was offered for 21 periods of four weeks each. The high approval rate

[1] The dollar limit of weekly CEWS support varied over time and approximated 75% of the $52,600 average annual wage of Canadians in 2019. CEWS, therefore, was targeted towards average wage earners who would experience economic hardship without a subsidy, and who likely spent all of their earnings on the necessities of life.
[2] As of December 5, 2021 – accessed at https://www.canada.ca/en/revenue-agency/services/subsidy/emergency-wage-subsidy/cews-statistics.html

is not surprising since it was reasonably easy for applicant businesses to demonstrate the central criterion, namely a RRP of varying amounts over time compared to the baseline period of the same month in the year before the pandemic (e.g., April 2020 versus April 2019) or compared to the (average of the two month) period immediately preceding the pandemic (i.e., January and February 2020).

The government intended the subsidy to flow through to the employees to ensure they had sufficient cash flows during the Covid-19 lockdown when supply was curtailed for public health reasons. CEWS was one of several programs intended to help 'freeze' the economy and businesses until the health shock had been contained, and then allow the economy and businesses to resume their normal activities. It was designed to prevent job and income losses while the pandemic prevailed.

However, the CEWS program has garnered much criticism since its initial launch within weeks of the Covid-19 onset. Mawani (2020b), for example, describes CEWS as a payroll or business subsidy rather than a conduit for a wage subsidy to employees since businesses received CEWS even if they continued operating without interruptions, and their employees continued working the same number of hours (remotely or in person) as before the pandemic. This is because the CEWS benefits were not restricted to hours missed working by employees due to lower demand for the employers' products and services.[3] As a result, some CEWS recipients ended up reporting higher profits in 2020 compared to 2019.[4] Monpetit, Nakonechny and Hétu

[3] For example, journalists at many Canadian news media companies continued writing and submitting their stories remotely and submitting them electronically at full pay during the pandemic, while their employers received a business subsidy for up to 75% of the wages paid (up to a weekly maximum) if they could show the RRP decline in monthly revenues (which materialized because advertising revenues as well as delivery and circulation of hard copies declined during the pandemic).
[4] Examples of firms reporting higher profits include Leon's (which received $32 million in CEWS benefits) and Extendicare (which received $82.2 million in CEWS benefits).

(2020) detected 213 public corporations listed on the TSX that received CEWS. These authors analyzed 53 of such CEWS recipients, of which 19 (or 36%) reported higher profits during the Covid-19 year compared to the previous non-pandemic year. CEWS made labour artificially cheap, perhaps discouraging new investments in technology.

In contrast, Germany's successful *Kurzarbeit* ("short work") scheme paid employees (via their employers, like CEWS) only for missing work hours.[5] If the employees missed no working hours (as with the hypothetical newspaper example described above), then the *Kurzarbeit* would have paid out nothing.

While CEWS offered support to all businesses that suffered the requisite RRP decline, the lack of targeting meant that most jobs subsidized were not necessarily at risk of being lost. CEWS recipients did not have to demonstrate the need for cash, and therefore the subsidy often flowed through to higher reported income, dividends, share repurchases or executive compensation.[6] Firms receiving CEWS could use their subsidy to increase payouts to employees (e.g., by increasing their hourly wage), customers (e.g., reducing prices), suppliers (e.g., accelerating payments), or shareholders (e.g., increasing dividends or share buybacks). For example, Air Canada received $492 million in CEWS subsidies (one of the highest of any company) while holding $2.3 billion in unearned revenues from unused ticket sales to customers. Gatehouse (2020) describes the example of Royal Ottawa Golf Club that reported a surplus of $825,000 during the first year of the pandemic compared to $43,000 reported in 2019 fiscal year.

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[5] *Kurzarbeit* subsidized 60% of employees after-tax wages for up to 12 months (International Monetary Fund News 2020). It is approximately equivalent in generosity to the CEWS since the 60% subsidy in Germany was not taxable while CEWS in Canada was taxable. These two subsidies are equivalent at an average tax rate on wages of 20%, or 75% (1-0.20) = 60%.

[6] The federal government later introduced a rule requiring businesses to repay CEWS if they also increased their executive compensation from the pre-pandemic levels. Even if firms were restricted from increasing dividends during the year of CEWS receipt, they would unlikely be restricted or even monitored from increasing dividends in subsequent post-pandemic years.

Corak (2021, p. 4) describes this overkill as part of the government's dilemma of "supporting too few or supporting too many Canadians."

The level of wage subsidies may explain why the number of companies filing for bankruptcy or restructuring proposal declined in 2021 compared to both 2019 and 2020, and was the lowest in the third quarter of 2021 since at least 1987.[7] Statistics from Office of the Superintendent of Bankruptcy Canada show that bankruptcies across Canada were 15 percent lower in the third quarter of 2021 compared to the same period in 2020, and 35 percent lower compared to the same period in 2019. The generous support from CEWS may also have allowed zombie firms to survive longer than otherwise, thereby tying up government resources that could be reallocated to more profitable ventures.

Analysis by Smart (2020) and Smart and Eisen (2021) show that 4,170 companies (about 1% of all CEWS recipients) were part of corporate groups with assets of $600 million or more, and included subsidiaries of multinationals. As a result of this lack of targeting, Smart (2020) estimates that the cost to save one job for one month as of September 2020 was about $14,500 – an amount likely to be significantly higher if his estimation was to be done a year later.

The experience was similar for the U.S. Paycheck Protection Program (PPP), a U.S. $800 billion wage subsidy program enacted and delivered in the first phase of Covid-19. Autor et al (2022) estimate the cost of saving a job for one year to be $169,300, an amount much greater than the $58,200 average compensation. This analysis estimates that the PPP handed out $3.13 to businesses for every $1 in wages it prevented from being lost. Similar to the Canadian

[7]Innovation, Science and Economic Development Canada, Office of the Superintendent of Bankruptcy Canada at https://www.ic.gc.ca/eic/site/bsf-osb.nsf/vwapj/Insolvency-Statistics-Q3-2021-EN.pdf/$file/Insolvency-Statistics-Q3-2021-EN.pdf

experience, the money did not primarily go to workers who would have lost jobs. Instead, it went to shareholders and creditors.

This article focuses on a novel critique of the CEWS rules in a setting that has yet not been exposed in this literature. It illustrates how firms not only did not need to show missing hours for their employees or cash flow needs for employers, but they also did not have to experience an actual decline in revenue or even a decline in revenue compared to the same month in the previous year (however fleeting the decline may be) to be eligible for CEWS. The article focuses on the choice applicant firms had in using accrual accounting or cash accounting to benchmark their monthly revenues with the baseline period of the same month in the year before the pandemic (e.g., April 2020 versus April 2019) or the baseline of the period immediately preceding the pandemic (i.e., the average revenue for January and February 2020).

Revenues measured according to "normal accounting practices"

Subsection 125.7(4) of the Canadian Income Tax Act allows entities to determine revenues in accordance with its "normal accounting practices" – an expression not defined in the Act nor clarified with any guidance from the CRA. For purposes of applying for CEWS, normal accounting practices does not have to conform to Generally Accepted Accounting Principles (GAAP).[8] Instead, CRA Document 2020-0855831E5 (September 21, 2020) requires "revenue" to satisfy "certain performance obligations [by the reporting entity] such as the sale of goods or the performance of services that would typically result in a corresponding inflow of cash, accounts receivable, or other consideration" (Bersenas and Weinrauch 2022). This CRA

[8] GAAP includes accounting standards for private enterprises (ASPE) or international financial reporting standards (IFRS).

definition does not preclude the use of cash basis of accounting by CEWS applicants as long as they were using it as part of their "normal accounting practice" or if they changed their normal accounting practice to cash basis of accounting just prior to their first CEWS application. Furthermore, the CEWS calculator on the CRA portal specifically allowed for revenues to be measured according to the cash basis of accounting.

General Implications of CEWS legislation

The baseline of average revenue for January and February 2020 (the two months immediately prior to the pandemic) may have been initially justified for new businesses that were not in existence for much of 2019, and therefore did not have sufficient history of past revenues to have a 2019 comparator. However, when the CEWS legislation was rolled out, this baseline option was available to all firms – old and new – presumably in the interest of equity. To the extent that CEWS and CERS can be viewed as negative income taxes (since they were arguably business subsidies and not wage subsidies, and delivered via the tax pipeline), it seems inequitable for such negative income taxes to be different across firms with different lengths of histories. There is no sound public policy reason to subsidize or tax one firm more than another just because they have been in existence for a different period of time.

Similarly, initial discussions to allow the cash method of accounting to assess RRPs for CEWS may have been limited only to the few firms that use cash method of accounting for their regular reporting, but later extended to all firms presumably on equity grounds. To the extent that CEWS and CERS can be viewed as negative income taxes (since they were more appropriately business subsidies and not wage subsidies delivered via the tax pipeline), it seems inequitable for such negative income taxes to be based on the choice of accounting methods. There is no sound public policy reason to subsidize or tax one firm more than another just because they use a different method of accounting.

One other reason to consider CEWS as a negative income tax is that businesses could (and did) argue that they felt obliged to apply for CEWS for competitive reasons if other firms in their industry were also applying for CEWS, and if they were eligible based on the strict interpretation of the rules. In response to whether CEWS recipients were justified in paying higher dividends, Corcoran (2021) argues that firms owe their allegiance to shareholders who are mobile and seek competitive returns on their investments. These are the same arguments that firms (and their tax advisors) use to operationally justify why they take every advantage of income tax legislation to legally minimize their income taxes, since otherwise they would face an uncompetitive cost disadvantage against their competitors. The legality of tax avoidance was reaffirmed in a 1998 Supreme Court of Canada decision where Justice Iacobucci ruled that "taxpayers can arrange their affairs in a particular way for the sole purpose of deliberately availing themselves of tax reduction devices in the Income Tax Act."[9] Unlike tax evasion, tax avoidance does not require taxpayers to question whether they need or deserve the tax deduction, or conversely, whether they need or deserve a tax subsidy like CEWS.

The accrual accounting and the comparison baseline of the same period in 2019 were the default methods, while the cash method of accounting and the comparison baseline of the average revenues in January and February of 2019 were the alternate methods. Firms had a clear choice of using the cash method or accrual method of accounting, and the pre-pandemic months

[9] *Melville Neuman v. Her Majesty the Queen*, 98 DTC, p. 6302.

of January and February 2020 or the same month in 2019 as a baseline for determining RRP. However, deviating from the default methods required applicants to file formal elections specified under provisions of the Income Tax Act (ITA) and signed by business officers.[10]

The choice to measure revenue decline on accrual basis or cash basis as well as the short baseline period (January and February 2020) immediately prior to the pandemic was extended to the Canada Emergency Rent Subsidy (CERS) program with similar effects.[11]

Allowing these two choices suggests that those who drafted the CEWS rules may not have quite appreciated the shortcoming of cash accounting over accrual accounting in the context where a short window (average of January and February 2020) is used as a baseline against which RRP declines are assessed. Unfortunately, these design flaws from CEWS and CERS continue in the recently launched Tourism and Hospitality Recovery Program (THRP) and the Hardest-Hit Business Recovery Program (HHBRP) subsidy programs as discussed later.

One major implication of the CEWS rules described above is that firms with identical annual aggregate revenues that are unchanged from the previous non-pandemic year could receive different amounts of CEWS support. Using the online CEWS calculator[12], Table 1 shows how firms with identical payroll costs, identical unchanged annual revenues, and identical unchanged annual net incomes received CEWS support ranging from $0 to $155,889.60 depending on the distribution of monthly revenues.[13] Firms with relatively higher revenues in the

[10]Paragraph 125.7(4)(e) of the Canadian Income Tax Act (ITA) required firms to make an election to choose between the cash method or accrual method of accounting, while Clauses 125.7(1)(b)(i)(A) and 125.7(1)(b)(i)(B) elections required firms to choose the appropriate “prior reference period” as a baseline for determining RRP. See CEWS legislation at Parliament of Canada at https://www.parl.ca/DocumentViewer/en/43-1/bill/C-14/royal-assent
[11] The similar definition of the requisite RRP for the new CERS program was designed to maintain consistency and simplicity, and the use of a common foundation for the online calculator.
[12] CEWS calculator at https://www.canada.ca/en/revenue-agency/services/wage-rent-subsidies/covid-wage-hiring-support-businesses/wage-calculate-amount.html#cal-calc
[13] This covers CEWS Period 01 to Period 10 from March 15, 2020 to December 19, 2020.

baseline comparator period of January and February 2020 could demonstrate a higher RRP in subsequent months, and therefore receive higher CEWS. The amount of CEWS support was directly and nonlinearly associated with the decline in monthly revenues compared to the baseline period of January and February 2020. The CEWS rules focused on monthly revenues declines instead of annual net income levels as the basis for "entitlement to receive subsidy."[14]

The negative income tax perspective is based on CEWS being a business subsidy rather than a wage subsidy, and therefore akin to a negative income tax – albeit based on revenue declines rather than net income levels. After all, firms pay (often equal) monthly income tax installments based on the current year's estimated annual level of income taxes payable, or prior year's actual annual level of income taxes payable. This may explain the concern by the public and the media about the inequity in CEWS received by applicant firms on the basis of need or reported net income.[15]

Nelson (2021) discusses CRA's role in delivery of social benefits in general. He points out favourably how subsidies like CEWS adopted four-week periods rather than being based on the full taxation year, allowing pandemic assistance to be delivered more rapidly. Robson and Schwartz (2021) review the arguments for and against the CRA taking on a much larger role as a social benefits agency to deliver benefits not directly tied to the tax system. They conclude that, on balance, an expanded role for the CRA may not be warranted. Instead, they propose that CRA share its collected information about taxpayers with other agencies who may be more effective at administering benefits.

[14] The criterion symmetric to an "ability to pay taxes" could be considered an "entitlement to receive subsidy."
[15] Firms that did not apply for cost or political reasons are not considered to be treated inequitably since they had an opportunity to apply for CEWS and CERS.

The Setting

Consider a payroll software developer that employs five people (including the owner-manager) to update its single tax and pension software product, and launches a new version of the software in late December each year in time for the new calendar / taxation year. It invoices customers in late December, and they all pay their invoices in January of each year, with a few late stragglers paying in February. In the remaining 10 months of each year, the business earns some revenues doing customized consulting work for its customers. During the pandemic, the number of subscribers renewing their software at the beginning of the year remains constant. The online consulting services sold during the pandemic months (March 2020 – December 2021) enjoyed a slight price increase during 2020, as well as an additional price increase in 2021. Since this slightly higher online revenue resulted from a price increase and not additional labour, the firm had sufficient labour capacity within the existing five personnel and did not have to hire more employees. Table 2 describes this company's revenues during the pre-pandemic and pandemic years.

Given that the central criterion for CEWS was demonstrating revenue decline, this company – at first glance – does not seem eligible for CEWS or CERS since monthly *accrued* revenues did not decline during the pandemic. However, the CEWS and CERS rules allowed businesses to report revenues using either accrual or cash method of accounting as long as they were reported consistently using a single method.[16]

[16] Consistent measurement over time is considered a major safeguard in accounting since it often allows disclosure of an accurate trendline despite some measurement errors made consistently over time.

Businesses were eligible for CEWS if they could demonstrate a RRP decline ranging from 15% in the first period to 30% in Periods 2-4.[17] The maximum amount of CEWS benefits were available for firms demonstrating a RRP of at least 70%.[18] In later periods, subsidies were reduced for smaller revenue declines but maintained for larger revenue declines.[19] Importantly, firms did not have to demonstrate that their revenue loss was related to Covid-19 since it would be difficult to conclusively establish that loss of revenues was due to Covid-19.

In the interest of offering businesses some certainty during the pandemic, the rules allowed a business applicant to qualify for CEWS in a period if it also qualified for CEWS in the immediately preceding period. This "safe harbour" outcome resulted from lobbying by the small business community which successfully reframed the discourse from helping employees via the business conduit to helping the businesses themselves during an uncertain period.[20] The lobbying was aided by highlighting a survey of small business owners expressing pessimism about recovery from the pandemic lockdown. The safe harbour provision meant that this particular payroll software firm profiled would qualify for CEWS in January 2021 even though its consistently reported revenues under cash method of accounting were not lower than the baseline period of January / February 2020.

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[17] The minimum RRP for Periods 01 -04 are in Table 1, and for Periods 05 - 21 in Table 2A of Frequently Asked Questions for CEWS at https://www.canada.ca/en/revenue-agency/services/wage-rent-subsidies/cews-frequently-asked-questions.html

[18] The RRP at which maximum CEWS is available is described on Page 86 of Frequently Asked Questions for CEWS at https://www.canada.ca/en/revenue-agency/services/wage-rent-subsidies/cews-frequently-asked-questions.html

[19] Some firms may have found that the advisory or accounting cost of obtaining CEWS support plus the potential political costs of public disclosure in the CEWS Registry may not exceed the benefits of small subsidies available for small RRPs.

[20] See for example, Bill Curry and Chris Hannay (2021) "Ottawa in discussions to extend pandemic aid beyond Oct. 23 deadline" *The Globe and Mail*. October 6th at https://www.theglobeandmail.com/politics/article-freeland-signals-openness-to-extending-some-pandemic-support-programs/

Table 3 describes how the firm can be eligible for CEWS in all the 20 months of 2020 and 2021 during which the CEWS was offered despite enjoying same or higher actual annual revenues in every month compared to 2019. Minimum RRP required to be eligible for CEWS range from greater than 0% to greater than 30%.[21] In the case of our profiled company, the RRPs in Columns 2 and 5 of Table 3 exceed 70% in every period, except in January 2021. An applicant firm is eligible for *maximum* CEWS in a given period if it can demonstrate a RRP of at least 70% in Column 2 ***or*** have a 'Yes' response in Column 6 of Table 3 under either the accrual method or the cash method of accounting.

This is a surprising and egregious result given that the firm enjoyed higher (or same) revenues compared to the same month in the previous year for all the CEWS periods. It illustrates an example of how a firm could benefit from the CEWS rules when its skewed annual revenues under the cash accounting method are earned almost entirely in the first two months of the year prior to the pandemic. While not in the mainstream, such businesses can exist in the software licensing industry, in seasonal business such as ski resorts, and in some businesses selling annual subscriptions on a calendar year basis.

Design flaws like the one illustrated above can be expected for new subsidy programs designed in the rush of a pandemic lockdown. However, such design flaws should have been detected and corrected for subsequent periods when many other features of the program were fine-tuned. The government did make many design changes during the course of the pandemic. For example, the subsidy rate as a function of the RRP changed several times. The subsidy rate increased with RRPs in order to target businesses that were the hardest-hit. However, the design

[21] The *minimum* RRP are listed in Table 1 for Periods 01 -04 and in Table 2A for Periods 05 - 21 of Frequently Asked Questions for CEWS at https://www.canada.ca/en/revenue-agency/services/wage-rent-subsidies/cews-frequently-asked-questions.html

flaws described in this paper continued to potentially allow businesses that did not suffer any decline in (annual or monthly) revenues to qualify for and receive subsidies.

In their analysis of 389 CEWS recipients, Brethour, Cardoso, Milstead and Subramaniam (2021) show that "more than a third [of the CEWS recipients] posted revenue increases. That doesn't mean those companies didn't play by the rules, but it indicates the decline in their business was fleeting." In the example of our payroll software company, there was no actual or expected revenue decline – however fleeting.

The amount of CEWS and CERS subsidies received by this payroll software business was not immaterial. Table 4 documents the bi-weekly and annual payroll costs of this small business, while Table 5 highlights summary income statements to illustrate the magnitude of subsidies in relation to net incomes. Net income as a percentage of revenue increased from 16% before the pandemic to 49% and 50% in the pandemic years of 2020 and 2021, respectively. This "excess profit" could be paid out in dividends, debt repayment[22] or executive compensation,[23] establishing that the legal incidence of subsidies does not always reflect the economic incidence of the subsidies.[24] CEWS subsidized 43% of annual payroll[25] in 2020 and 40% in 2021, while CERS subsidized 13% of annual rent in 2020 and 42% in 2021. As a result, net income (after subsidies) increased by 233% in 2020 and 258% in 2021 compared to the pre-pandemic net income of 2019. This firm netted more cash inflows from CEWS ($155,889.60 in 2020 and

[22] Deleveraging could make the business less risky, and perhaps a target for a takeover by a larger player in the industry.
[23] The business could wait until after the pandemic to pay out higher executive compensation to escape scrutiny of CEWS recipients during the pandemic.
[24] Recipients of the Canada Emergency Response Benefit (CERB) could also be considered temporary holders of the subsidy before the incidence was redirected to grocery stores and existing home-owners in the form of higher prices.
[25] Payroll included employer portion of statutory deductions for Employment Insurance and Canada Pension Plan.

$144,288.40 in 2021) than it did from earnings on selling software ($98,768.58 in 2020 and $121,873.83 in 2021).

While the amount of CEWS support is proportional to the amount of payroll, it is important to note that CEWS is triggered entirely and solely by a reduction in *monthly* revenues that could be imposed externally by Covid-19 circumstances, or engineered opportunistically to attain some "down time" for the employees over the duration of the various subsidy programs, or to work on new product developments that could generate future revenues. Net income (and its labour productivity determinant) during Covid-19 periods did not feature into CEWS eligibility and support, thereby allowing many CEWS recipients to report higher net incomes during the pandemic. While accounting principles[26] require labour costs incurred for new product development to be capitalized instead of being expensed, the CEWS calculator did not differentiate between expensed and capitalized labour outlays. Ignoring net income in determining CEWS support allowed labour productivity to remain obscured.[27] As an unintended consequence, CEWS may have incentivized and subsidized new product development and generation of future revenues instead of subsidizing the opportunity cost of losing current revenues during a pandemic.[28]

This example of our profiled firm is more egregious than the Royal Ottawa Golf Club example reported at the beginning of this article. While the Golf Club enjoyed higher cash

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[26] Accounting principles as set out in International Financial Reporting Standards (IFRS) for Canadian publicly traded companies and Accounting Standards for Private Enterprises (ASPE) for private entities.

[27] Furthermore, several companies such as BCE, Canadian Natural Resources, Suncor and Telus did not disclose CEWS support in their financial statements on grounds of materiality even though they were on the government's CEWS registry as having received the wage subsidy (Ferreira, 2020).

[28] While linkages to wages supported (or reimbursed) under the Scientific Research & Experimental Development (SR&ED) program is beyond the scope of this paper on CEWS, a cursory review of ineligible wages does not include subsidized wages - https://www.canada.ca/en/revenue-agency/services/scientific-research-experimental-development-tax-incentive-program/eligibility-work-investment-tax-credits/eligibility-work-investment-tax-credits-2015.html

inflows and profits despite suffering decline in revenue during the Covid-19 lockdown, the payroll software developer in this example never suffered any actual revenue decline nor anticipated a revenue decline in any month (when compared to the same month in previous year), and instead enjoyed higher revenues. CEWS and CERS just constituted a “general business subsidy” once the applicant became familiar with the rules of the subsidy programs.

Table 6 provides details on CEWS and CERS claims for each 4-week period during 2020 and 2021, while Table 6A summarizes the annual subsidies. Figure 1 depicts the downloaded spreadsheet-based CEWS application for Period 1, while Figure 2 depicts the web-based CERS application for Period 1.

Fixing the Flaws

These design flaws could be fixed by requiring firms that report RRPs using the cash method of accounting to use only the baseline of the same period in 2019 (e.g., May 2020 vs. May 2019), or to not allow cash method of accounting for reporting RRPs, or both. Table 7 summarizes these options and the subsidies available under the different options. If our profiled company were to report monthly revenues on an annual accrual basis (Option A), it would report no decline in revenues and therefore not be eligible for any CEWS or CERS.

Alternatively, the CEWS and CERS rules could insist that applicants only have one choice for comparing monthly revenues with the same month in the previous non-pandemic year (Option B in Table 7). Under Option B, our profiled company would not be able to show any reduction in revenues during the pandemic, and thereby not be eligible for CEWS and / or CERS.

The New Subsidies: THRP and HHBRP

The Canadian government launched two new subsidy programs in November 2021: the Tourism and Hospitality Recovery Program (THRP) and the Hardest-Hit Business Recovery Program (HHBRP). Both these programs are based on the CEWS calculator and infrastructure, and both programs require firms to now demonstrate the following major requisite conditions:[29]

(1) An average monthly revenue reduction of at least 40% for THRP and at least 50% for HHBRP over a 12-month period; *and*

(2) A current month revenue loss of at least 40% for THRP and at least 50% for HHBRP.

As shown in Table 3, our profiled firm would qualify under both these new programs (assuming it satisfied industry classification and other minor conditions) for 11 out of the 12 months in 2021 since it can demonstrate (1) an average monthly RRP of greater than 50% over the corresponding 12-month period[30]; and (2) a current month RRP of at least 50% in 11 out of the 12 months. This establishes that the design flaws highlighted in this paper have not been fixed, and firms enjoying higher revenues (as shown with the firm profiled in the setting of this paper) could still qualify for subsidies under HHBRP and THRP.

Concluding Remarks

This article has illustrated how a firm that enjoyed higher revenues during the pandemic could be eligible for both CEWS and CERS subsidies. It points to common design flaws in both programs. While design flaws can be tolerated initially when programs are launched in a very

[29] https://www.canada.ca/en/department-finance/news/2021/10/targeting-covid-19-support-measures.html
[30] The 12-month baseline period for these two new programs is March 2020 - February 2021. In our specific case, the average 12-month RRP from Table 3 is [(78% x 10 Months) + (-72% x 1 month) + (72% x 1 month)] = 780 / 12 = 65%. This exceeds 50%, and therefore satisfies the first criterion for both programs.

short period of time during a lockdown, it is not excusable for the design flaws to remain uncorrected over the 21-month life of the programs, nor for such design flaws to continue in the new programs that were launched in November 2021.

Firms in seasonal industries such as ski resorts may also earn their cash revenues in a few concentrated winter months, and could demonstrate significant decline in revenue for the remaining calendar months under a cash method of accounting. Snow removal businesses could also demonstrate negative RRPs for many months of the year under the cash method of accounting.

At a time of declining tax revenues and higher public healthcare commitments, CEWS and CERS programs have cost the federal treasury in excess of $100 billion over their life. Future subsidy programs should avoid determining the baseline as an average of a short horizon, except for firms that have no history beyond the months immediately prior to the pandemic. Instead, a 12-month rolling average of revenues for firms with sufficient history would serve as a more appropriate benchmark against which RRPs are determined. Firms with only six months of history (for example) could be asked to base their comparator over the six months. A longer horizon baseline would reduce the unintended consequences illustrated in this article.

Corak (2021, p.2) aptly summarizes how "The Canada Emergency Wage Subsidy may reasonably be thought of as an experiment not to be repeated." In planning to arm ourselves with fiscal antibodies for the next pandemic, we should be more determined to detect structural flaws and design future subsidy programs on a more solid foundation. An appropriate design would ensure that the subsidies flow through to firms in actual need and at a lower cost to the taxpayers.

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Table 1: CEWS Receivable in 2020 across different variations in monthly revenues for firms with identical payroll costs, identical and unchanged annual revenues and identical and unchanged annual net incomes

	Identical Cash Revenue in 2020 and 2019	Identical Cash Revenue in 2020 and 2019	Identical Cash Revenue in 2020 and 2019	Identical Cash Revenue in 2020 and 2019	Identical Cash Revenue in 2020 and 2019	Identical Cash Revenue in 2020 and 2019
January	$200,000	25,000	30,000	70,000	$50,000	$41,667
February	50,000	25,000	30,000	70,000	$50,000	$41,667
March	25,000	200,000	30,000	60,000	$40,000	$41,667
April	25,000	50,000	30,000	0	$40,000	$41,667
May	25,000	25,000	30,000	0	$40,000	$41,667
June	25,000	25,000	30,000	0	$40,000	$41,667
July	25,000	25,000	30,000	0	$40,000	$41,667
August	25,000	25,000	30,000	60,000	$40,000	$41,667
September	25,000	25,000	30,000	60,000	$40,000	$41,667
October	25,000	25,000	30,000	60,000	$40,000	$41,667
November	25,000	25,000	30,000	60,000	$40,000	$41,667
December	25,000	25,000	170,000	60,000	$40,000	$41,667
Total Annual Revenue	$500,000	$500,000	$500,000	$500,000	$500,000	$500,000
Total Annual Payroll[31]	$359,736.42	$359,736.42	$359,736.42	$359,736.42	$359,736.42	$359,736.42
Annual Net Income Before Subsidies	$75,643.58	$75,643.58	$75,643.58	$75,643.58	$75,643.58	$75,643.58
CEWS Receivable under most *favourable* method[32]	$155,889.60	$0	$0	$98,713.48	$56,038.24	$0
CEWS Received as a % of Payroll	43.3%	0%	0%	27.4%	15.6%	0%

[31]Including employer contributions for CPP and EI.
[32]The two methods available are accrual accounting and cash method of accounting. Based on the CEWS calculator at https://www.canada.ca/en/revenue-agency/services/wage-rent-subsidies/covid-wage-hiring-support-businesses/wage-calculate-amount.html#cal-calc

Table 2: Annual Revenues 2019-2021

	2019	2020	2021
January	$215,000	$215,000	$215,000
February	$35,000	$35,000	$35,000
March	$25,000	$27,500	$30,000
April	$25,000	$27,500	$30,000
May	$25,000	$27,500	$30,000
June	$25,000	$27,500	$30,000
July	$25,000	$27,500	$30,000
August	$25,000	$27,500	$30,000
September	$25,000	$27,500	$30,000
October	$25,000	$27,500	$30,000
November	$25,000	$27,500	$30,000
December	$25,000	$27,500	$30,000
Total Annual Revenue	$500,000	$525,000	$550,000

Table 3: Reductions in monthly revenues during 2020 and 2021 under cash method of accounting compared to baseline of average of January and February 2020

Panel A: 2020			Panel B: 2021		
Month	**2020 Revenues**	**RRP% compared to average of January / February 2020?**[33]	**2021 Revenues**	**RRP% compared to average of January / February 2020?**	**Did Applicant qualify for CEWS in immediately preceding period?**
January	$215,000	N/A since pandemic not started and CEWS not offered	$215,000	RRP = -72%	Yes (since applicant qualified for CEWS in December 2020)
February	$35,000	N/A since pandemic not started and CEWS not offered	$35,000	RRP = 72%	
March	$27,500	RRP = 78%	$30,000	RRP = 76%	
April	$27,500	RRP = 78%	$30,000	RRP = 76%	
May	$27,500	RRP = 78%	$30,000	RRP = 76%	
June	$27,500	RRP = 78%	$30,000	RRP = 76%	
July	$27,500	RRP = 78%	$30,000	RRP = 76%	
August	$27,500	RRP = 78%	$30,000	RRP = 76%	
September	$27,500	RRP = 78%	$30,000	RRP = 76%	
October	$27,500	RRP = 78%	$30,000	RRP = 76%	
November	$27,500	RRP = 78%	$30,000	N/A since CEWS ended	
December	$27,500	RRP = 78%	$30,000	N/A since CEWS ended	

[33] Since the RRP exceeds 70% in each of the 20 months of 2020 and 2021, the firm receives the maximum amount of CEWS in all months. Under the "safe harbour" provision, the firm remains eligible for CEWS in January 2021 because it was eligible for CEWS in the immediately preceding month (December 2020).

Table 4: Bi-weekly and annual compensation by employee during 2019-2021

	Bi-weekly payroll	2019 Annual Payroll	2020 Annual Payroll	2021 Annual Payroll
Owner-Manager	$ 3,500.00	$ 91,350.00	$ 91,700.00	$ 91,350.00
Accountant	$ 3,000.00	$ 78,300.00	$ 78,600.00	$ 78,300.00
Programmer 1	$ 2,500.00	$ 65,250.00	$ 65,500.00	$ 65,250.00
Programmer 2	$ 2,500.00	$ 65,250.00	$ 65,500.00	$ 65,250.00
Administrator	$ 1,500.00	$ 39,150.00	$ 39,300.00	$ 39,150.00
Total	$13,000.00	$339,300.00	$340,600.00	$339,300.00

Table 5: Summary Income Statements 2019-2021

	2019	**2020**	**2021**
Revenues	$500,000.00	$525,000.00	$550,000.00
Payroll	(339,300.00)	(340,600.00)	(339,300.00)
Employer Cost of CPP and EI Premiums	(18,518.91)	(19,136.42)	(20,456.17)
Rent	(24,000.00)	(24,000.00)	(24,000.00)
HST on Rent	(3,120.00)	(3,120.00)	(3,120.00)
Other Costs 7.5% of Revenues	(37,500.00)	(39,375.00)	(41,250.00)
Income before Government Subsidies	77,561.09	98,768.58	121,873.83
Wage Subsidy from CEWS	-	155,889.60	144,288.40
Rent Subsidy from CERS	-	3,570.11	11,343.00
Pretax Income after Subsidies	77,561.09	258,228.29	277,505.23
Net Income as % of Revenues	16%	49%	50%
Wage Subsidy as % of Payroll	0%	43%	40%
Rent Subsidy as % of Rent Cost	0%	13%	42%

Table 6: CEWS and CERS Subsidies by Periods

Year	Period	Start Date	End Date	CEWS Received	CERS Received	Total CEWS + CERS
2020	1	2020-Mar-15	2020-Apr-11	15,802.00	-	15,802.00
2020	2	2020-Apr-12	2020-May-09	15,802.00	-	15,802.00
2020	3	2020-May-10	2020-Jun-06	15,802.00	-	15,802.00
2020	4	2020-Jun-07	2020-Jul-04	15,802.00	-	15,802.00
2020	5	2020-Jul-05	2020-Aug-01	17,904.40	-	17,904.40
2020	6	2020-Aug-02	2020-Aug-29	17,904.40	-	17,904.40
2020	7	2020-Aug-30	2020-Sep-26	15,798.00	-	15,798.00
2020	8	2020-Sep-27	2020-Oct-24	13,691.60	1,179.78	14,871.38
2020	9	2020-Oct-25	2020-Nov-21	13,691.60	1,203.55	14,895.15
2020	10	2020-Nov-22	2020-Dec-19	13,691.60	1,186.78	14,878.38
2021	11	2020-Dec-20	2021-Jan-16	15,798.00	1,174.19	16,972.19
2021	12	2021-Jan-17	2021-Feb-13	15,798.00	1,232.60	17,030.60
2021	13	2021-Feb-14	2021-Mar-13	15,798.00	1,241.59	17,039.59
2021	14	2021-Mar-14	2021-Apr-10	15,798.00	1,188.17	16,986.17
2021	15	2021-Apr-11	2021-May-08	15,798.00	1,202.15	17,000.15
2021	16	2021-May-09	2021-Jun-05	15,798.00	1,181.18	16,979.18
2021	17	2021-Jun-06	2021-Jul-03	15,798.00	1,209.14	17,007.14
2021	18	2021-Jul-04	2021-Jul-31	12,638.40	1,083.87	13,722.27
2021	19	2021-Aug-01	2021-Aug-28	8,425.60	722.58	9,148.18
2021	20	2021-Aug-29	2021-Sep-25	8,425.60	744.09	9,169.69
2021	21	2021-Sep-26	2021-Oct-23	4,212.80	363.44	4,576.24
Total				$300,178.00	$14,913.11	$315,091.11

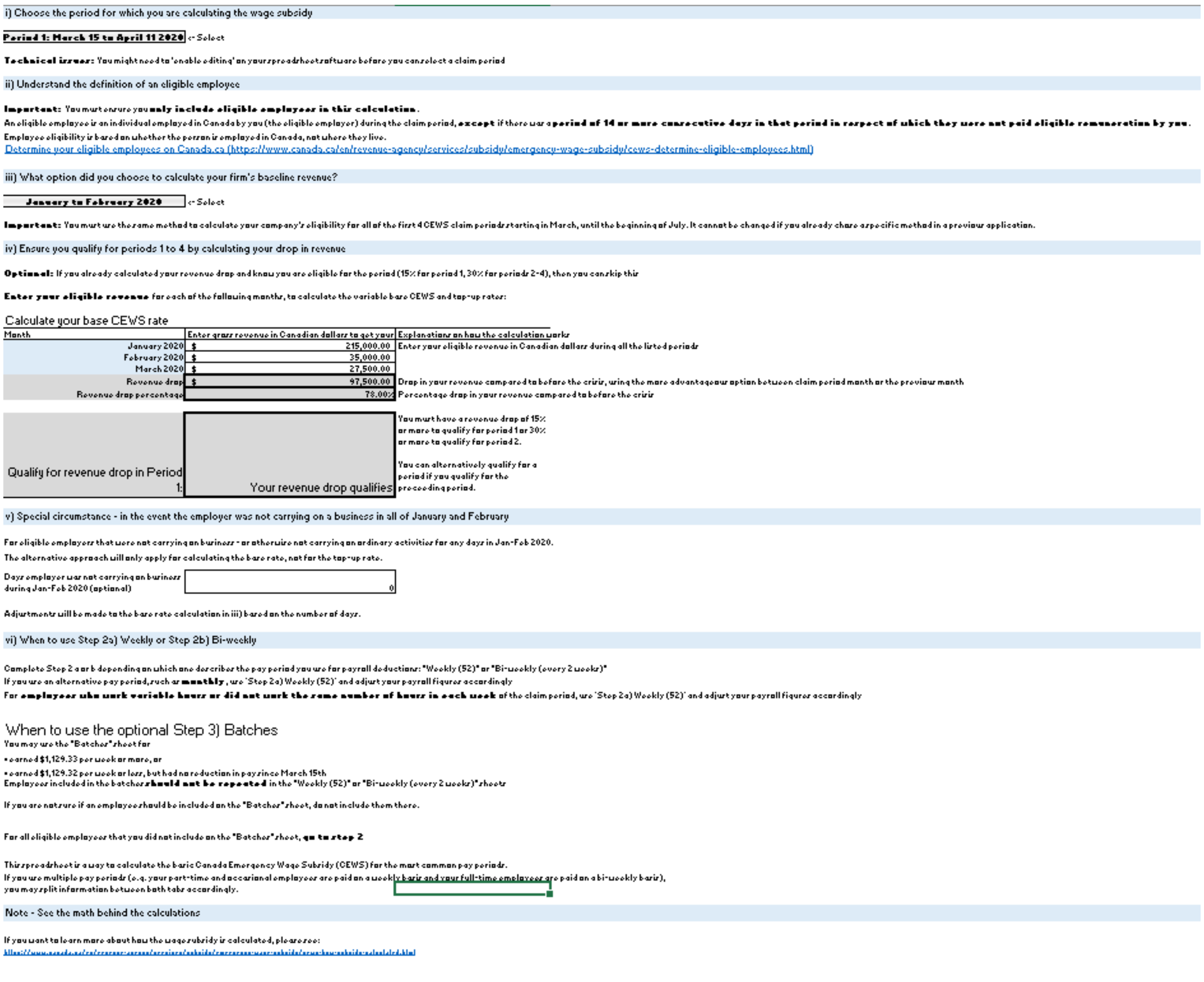
Table 6A: CEWS and CERS Subsidies 2020-21

	Total CEWS Subsidy	Total CERS Subsidy	Total Subsidies
2020	155,889.60	3,570.11	159,459.71
2021	144,288.40	11,343.00	155,631.40
Total	300,178.00	14,913.11	315,091.11

Table 7: Subsidy amounts available under different rules for CEWS and CERS

	Under CEWS and CERS rules as legislated	Option A: Comparison with baseline of monthly revenue computed under accrual accounting	Option B: Comparison with baseline of same month in 2019
Actual Revenue Reduction	None	None	None
Reported RRP Satisfied?	Yes, in every month that CEWS was offered	No	No
CEWS Receivable	$300,178.00 over duration of CEWS program	$0	$0
CERS Receivable	$14,913.11 over duration of CERS program	$0	$0

Figure 1: CEWS application forms for Period 1



i) Choose the period for which you are calculating the wage subsidy

Period 1: March 15 to April 11 2020 <- Select

Technical issues: You might need to 'enable editing' on your spreadsheet software before you can select a claim period

ii) Understand the definition of an eligible employee

Important: You must ensure you **only include eligible employees in this calculation**.
An eligible employee is an individual employed in Canada by you (the eligible employer) during the claim period, **except** if there was a **period of 14 or more consecutive days in that period in respect of which they were not paid eligible remuneration by you.**
Employee eligibility is based on whether the person is employed in Canada, not where they live.
Determine your eligible employees on Canada.ca (https://www.canada.ca/en/revenue-agency/services/subsidy/emergency-wage-subsidy/cews-determine-eligible-employees.html)

iii) What option did you choose to calculate your firm's baseline revenue?

January to February 2020 <- Select

Important: You must use the same method to calculate your company's eligibility for all of the first 4 CEWS claim periods starting in March, until the beginning of July. It cannot be changed if you already chose a specific method in a previous application.

iv) Ensure you qualify for periods 1 to 4 by calculating your drop in revenue

Optional: If you already calculated your revenue drop and know you are eligible for the period (15% for period 1, 30% for periods 2-4), then you can skip this

Enter your eligible revenue for each of the following months, to calculate the variable base CEWS and top-up rates:

Calculate your base CEWS rate

Month	Enter gross revenue in Canadian dollars to get your	Explanations on how the calculation works
January 2020	$ 215,000.00	Enter your eligible revenue in Canadian dollars during all the listed periods
February 2020	$ 35,000.00	
March 2020	$ 27,500.00	
Revenue drop	$ 97,500.00	Drop in your revenue compared to before the crisis, using the more advantageous option between claim period month or the previous month
Revenue drop percentage	78.00%	Percentage drop in your revenue compared to before the crisis
Qualify for revenue drop in Period 1:	Your revenue drop qualifies	You must have a revenue drop of 15% or more to qualify for period 1 or 30% or more to qualify for period 2. You can alternatively qualify for a period if you qualify for the preceding period.

v) Special circumstance - in the event the employer was not carrying on a business in all of January and February

For eligible employers that were not carrying on business - or otherwise not carrying on ordinary activities for any days in Jan-Feb 2020.
The alternative approach will only apply for calculating the base rate, not for the top-up rate.

Days employer was not carrying on business during Jan-Feb 2020 (optional)	0

Adjustments will be made to the base rate calculation in iii) based on the number of days.

vi) When to use Step 2a) Weekly or Step 2b) Bi-weekly

Complete Step 2 a or b depending on which one describes the pay period you use for payroll deductions: "Weekly (52)" or "Bi-weekly (every 2 weeks)"
If you use an alternative pay period, such as **monthly**, use 'Step 2a) Weekly (52)' and adjust your payroll figures accordingly
For **employees who work variable hours or did not work the same number of hours in each week** of the claim period, use 'Step 2a) Weekly (52)' and adjust your payroll figures accordingly

When to use the optional Step 3) Batches
You may use the "Batches" sheet for
• earned $1,129.33 per week or more, or
• earned $1,129.32 per week or less, but had no reduction in pay since March 15th
Employees included in the batches **should not be repeated** in the "Weekly (52)" or "Bi-weekly (every 2 weeks)" sheets

If you are not sure if an employee should be included on the "Batches" sheet, do not include them there.

For all eligible employees that you did not include on the "Batches" sheet, **go to step 2**

This spreadsheet is a way to calculate the basic Canada Emergency Wage Subsidy (CEWS) for the most common pay periods.
If you use multiple pay periods (e.g. your part-time and occasional employees are paid on a weekly basis and your full-time employees are paid on a bi-weekly basis),
you may split information between both tabs accordingly.

Note - See the math behind the calculations

If you want to learn more about how the wage subsidy is calculated, please see:
[illegible]

Totals: Final values to input on Canada.ca are displayed on the "Step 4) Amounts to use" sheet

*Figure 1 continued:

Totals: Final values to input on Canada.ca are displayed on the "Step 4) Amounts to use" sheet after you finish this step

			Weekly gross pay in respect of the claim period				Employee amount (calculated)						
Eligible employe	Employee at arm's length: Yes - arm's length/No - non-arm's length	Average weekly gross pay - January 1 to March 15, 2020 or - March 1 to May 31, 2019	Week 1	Week 2	Week 3	Week 4	Week 1	Week 2	Week 3	Week 4	Claim period total for employee (75%)		
An eligible employee is an individual employed in Canada by you (the eligible employer) during the claim period, except if there was a period of 14 or more consecutive days in that period in respect of which they were not paid eligible remuneration by you. Do not include ineligible employees in this spreadsheet.	Arm's-length: Generally, an arm's-length employee includes any employee who does not own the business (or in the case of a corporation, have a controlling interest in the corporation) and is not a member of that person's immediate family. Non-arm's length (not at arm's length): A non-arm's-length employee is someone who owns the business (or in the case of a corporation, have a controlling interest in the corporation) or is part of that person's immediate family.	Any period of 7 or more consecutive days for which an employee was not paid between January 1 and March 15, 2020, such as unpaid leave from work, should be omitted from the average baseline pay.	March 15 to March 21	March 22 to March 28	March 29 to April 4	April 5 to April 11	March 15 to March 21	March 22 to March 28	March 29 to April 4	April 5 to April 11	Columns B through G must be completed before this field calculates. The basic CEWS calculated in this spreadsheet does not include all deductions. Continue through the rest of the steps at the Canada.ca calculator for the actual CEWS amount.	Chk: Gross Pay for Period	Chk: EE Amount for Period
Owner-Manager	No - non-arm's length	1,731.33	1,750.00	1,750.00	1,750.00	1,750.00	$847.00	$847.00	$847.00	$847.00	$3,388.00	7,000.00	3,388.00
Accountant	Yes - arm's-length	1,484.00	1,500.00	1,500.00	1,500.00	1,500.00	$847.00	$847.00	$847.00	$847.00	$3,388.00	6,000.00	3,388.00
Programmer_1	Yes - arm's-length	1,236.67	1,250.00	1,250.00	1,250.00	1,250.00	$847.00	$847.00	$847.00	$847.00	$3,388.00	5,000.00	3,388.00
Programmer_1	Yes - arm's-length	1,236.67	1,250.00	1,250.00	1,250.00	1,250.00	$847.00	$847.00	$847.00	$847.00	$3,388.00	5,000.00	3,388.00
Admin_1	Yes - arm's-length	742.00	750.00	750.00	750.00	750.00	$562.50	$562.50	$562.50	$562.50	$2,250.00	3,000.00	2,250.00
							$0.00	$0.00	$0.00	$0.00	$0.00	26,000.00	15,802.00

Complete your calculation on Canada.ca with these amounts

i) After you've completed the weekly and/or bi-weekly calculation tab(s), the "Values to use in step 2b" will appear below.

Use these amounts to complete section 2 on the Canada.ca calculator and continue through the rest of the steps to determine your actual CEWS amour

Three values to use in step 2b on Canada.ca:
[Calculate your subsidy amount at Canada.ca/calculate-wage-subsidy]

Total number of eligible employees Period 1: March 15 to April 11 2020	Total eligible remuneration Period 1: March 15 to April 11 2020	Total basic CEWS Period 1: March 15 to April 11 2020
5	$26,000.00	$15,802.00

The basic CEWS calculated in this spreadsheet does not include all deductions. Continue through the rest of the steps at the Canada.ca calculator for the actual CEWS amount.

ii) Save or print a copy of this spreadsheet for your records.

Figure 2: Web-based CERS application forms for Period 1

Canada Emergency Rent Subsidy (CERS)

Print preview for CERS statement

Print and keep this record using the print preview button below.

The line amounts you will need to complete your application for **Period 1: September 27, 2020, to October 24, 2020** of the CERS in your online CRA account:

- **Line 110:** Number of eligible properties: 1
- **Line 120:** Total eligible rent[1]: $1,815.05
- **Line 130:** Total eligible property taxes: $0.00
- **Line 140:** Total eligible property insurance: $0.00
- **Line 150:** Total eligible interest on commercial mortgages: $0.00
- **Line 160:** Total qualifying rent expenses: $1,815.05
- **Line 200:** Revenue drop for the current period: 95.00%
- **Line 210:** Revenue drop for the previous period: 95.00%
- **Line 310:** Lockdown support: $0.00

1. **Net lease:** Lines 130, 140, and 150 are only used for owned properties. Any amounts paid for rented properties under a net lease are included in line 120.

Period 1: Summary of CERS calculation

Affiliated entity percentage	N/A
Maximum expenses that can be claimed for the base subsidy (Line 170: Lesser of line 160 or $300,000 or $300,000 x Affiliated entity percentage)	$1,815.05
Rent subsidy rate	x (multipled by) 65.00%
Base Canada Emergency Rent Subsidy (Line 300)	= $1,179.78
Lockdown support amount (Line 310)	+ $0.00
Total Canada Emergency Rent Subsidy (Line 300 + Line 310)	$1,179.78

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