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# Tax Alert — Canada

## Bill C-2 receives Royal Assent, public company dividend restriction and amendment to executive compensation repayment rule introduced

EY Tax Alerts cover significant tax news, developments and changes in legislation that affect Canadian businesses. They act as technical summaries to keep you on top of the latest tax issues. For more information, please contact your EY advisor or EY Law advisor.

On Friday 17 December 2021, Bill C-2, *An Act to provide further support in response to COVID-19*, received Royal Assent. Among other measures, Bill C-2 provides for new targeted COVID-19 support measures in addition to an extension of the Canada Recovery Hiring Program. The new business support measures include wage and rent subsidies under the Tourism and Hospitality Recovery Program, the Hardest-Hit Business Recovery Program and the Public Health Lockdown Support (collectively, the Targeted Subsidy Programs). For further details about these measures, refer to Tax Alert 2021 Issue No. 30.

Notably, enacted Bill C-2 includes both a prohibition and a restriction on publicly traded companies and their subsidiaries in claiming the Canada Emergency Wage Subsidy (CEWS) or the wage subsidy component of the Targeted Subsidy Programs if they paid taxable dividends to individuals on common shares. These measures are discussed in more detail below.

### Amendments to the *Income Tax Act*

Bill C-2 contains two amendments to the *Income Tax Act* (the Act) that impose restrictions related to the payment of dividends. Those amendments were added to Bill C-2 by the House of Commons Standing Committee on Finance, and Bill C-2 was subsequently enacted without further amendments.

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The first amendment appears to provide that no CEWS or wage subsidy under the Targeted Subsidy Programs will be payable for a qualifying period if, in the qualifying period, a publicly traded company or its subsidiary paid "taxable dividends to an individual who is a holder of common shares" of the company or its subsidiary. It is not clear which qualifying periods could be covered, but it is clear from the Committee hearings that retroactivity was not intended.

The second amendment treats taxable dividends paid by a publicly traded company or its subsidiary to an individual who is a holder of common shares as part of the executive compensation repayment rule, thereby potentially increasing the amount of the repayment. Notably, however, this only applies in respect of pandemic support payments paid in respect of qualifying periods 24 and onward (i.e., under the Targeted Subsidy Programs).

The sections that follow outline the specific amendments to the Act referred to above and analysis and observations related to those amendments.

## Detailed discussion

*New subsection 125.7(2.01)*

Subsection 125.7(2) of the Act is the legislative authority for the CEWS and the wage subsidy component of the Targeted Subsidy Programs. The CEWS and the Targeted Subsidy Programs deem an overpayment on account of the qualifying entity's Part I income tax liability for the taxation year in which the particular qualifying period ends to arise during that qualifying period.

The first amendment added to enacted Bill C-2 is new subsection 125.7(2.01), which provides as follows:

- **125.7(2.01)** – Despite subsection (2), no overpayment on account of a qualifying entity's liability under this Part for the taxation year in which the qualifying period ends is deemed to have arisen with respect to a qualifying entity that is a publicly traded company or a subsidiary of such a company if, in the qualifying period, it paid taxable dividends to an individual who is a holder of common shares of the company or of the subsidiary of the company.

New subsection 125.7(2.01) raises certain questions that do not appear to have clear answers at this time. Examples of areas of uncertainty include, but are not limited to, the following:

- Does this new provision only apply to qualifying periods ending on or after the date Bill C-2 receives Royal Assent (i.e., qualifying period 24 (19 December 2021 to 15 January 2022)), or does it apply with respect to any qualifying period for which an eligible entity has yet to apply for a subsidy? For example, if an eligible entity that is a publicly traded company or its subsidiary has not yet applied for the CEWS for qualifying periods 17 through 21, does this new provision disqualify that entity from claiming the CEWS for those periods if it paid taxable dividends to an individual who is a common shareholder in those periods?

Based on what was said during the debate of the Standing Committee on Finance, this provision would likely not have received the support of the majority of the Committee if it were to apply retroactively. Further, the second amendment (discussed below) specifically applies only with respect to qualifying period 24 and subsequent periods. This may suggest that the intention of the Committee was that both amendments would only apply prospectively and not retroactively.

- Would only the taxable dividend-paying entity be restricted from claiming the CEWS and the wage subsidy component of the Targeted Subsidy Programs? To be a "qualifying entity", the entity must be the employer claiming the CEWS or Targeted Subsidy Programs in respect of its own employees. However, in the case of many publicly traded companies, employees are not employed by the public parent company, but rather are employed by an operating subsidiary or shared services corporation. Further, it is uncommon for operating subsidiaries and shared services corporations to have individuals as shareholders. It would therefore be rare for such an entity to pay taxable dividends to an individual.

*New subsection 125.7(14.1)*

Subsection 125.7(14) of the Act requires a publicly traded company to repay CEWS and wage subsidy amounts under the Targeted Subsidy Programs received for qualifying periods after 5 June 2021 (qualifying periods 17 to 23) if the company's aggregate executive remuneration for the 2021 calendar year exceeds aggregate executive remuneration for the 2019 calendar year. In the case of qualifying period 24 and subsequent qualifying periods, the repayment arises under subsection 125.7(14.1) if aggregate executive remuneration for the 2022 calendar year exceeds such remuneration for the 2019 calendar year. The "executive compensation repayment amount" is generally the lesser of the total of all CEWS and Targeted Subsidy Program wage subsidy amounts received in respect of active employees for qualifying periods beginning after 5 June 2021, and the amount by which the corporation's aggregate executive remuneration for 2021/2022 (as applicable) exceeds its aggregate executive remuneration for 2019.

The second amendment added to enacted Bill C-2 amends newly added subsection 125.7(14.1) to require an eligible entity that is a publicly traded company or a subsidiary of such a company to repay the greater of:

- The "executive compensation repayment amount" of the eligible entity; and

- The amount of taxable dividends paid by the company or its subsidiary to an individual who is a holder of common shares of the company or its subsidiary.

Amended subsection 125.7(14.1) only applies in respect of qualifying period 24 and subsequent qualifying periods. Since the CEWS expired after qualifying period 21, this new provision only applies in respect of wage subsidy amounts received under the Targeted Subsidy Programs.

New subsection 125.7(14.1) also raises certain questions that do not appear to have clear answers at this time.

It remains to be seen how the federal government will address the questions raised by these new provisions. The House of Commons Standing Committee on Finance seemed to have expected the Department of Finance to fix any deficiencies in these amendments and the Canada Revenue Agency to issue guidance on these matters, and we understand that the Agency is working hard to do so.

## Learn more

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