

DEDUCTIBLE EXPENSES FROM EMPLOYMENT



FEBRUARY 2024

**NOTHING IS DEDUCTIBLE
– UNLESS IT IS – EXCEPT WHEN IT ISN'T**

INTRODUCTION

“I have a quick question” is a common phrase heard during tax season. But let’s be honest, when it comes to Income Tax, even if the question is quick, the answers never are because they all start with: “Well that depends...”.

The thing to remember about employees in Canada and how the *Income Tax Act* is written for them can be summarize in two, very simple concepts:

- Everything an employee receives **is** taxable
 - unless we tell you it isn't;
- Everything an employee spends **is not** deductible
 - unless we tell you it is.

The Income Tax Act is written in such a way so as to cast a very broad net to include everything into income, and then list exceptions.

In this newsletter

Often the biggest roadblock to professional advice is misinformed discussions that then lead to comments like “I know someone who...” or “my friend said...”.

This newsletter hopes to get rid of many of the tax filing myths on employment related expenses and silence those that say: “I’ve always filed it this way”. That phrase just means they haven’t been caught - yet.

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THE GOLDEN RULE OF EMPLOYEE DEDUCTIONS

Only **specific** expenses can be deducted by an employee under section 8 of the *Income Tax Act*. It is important to not confuse what is written for employees with how it is worded for businesses.

For example, **businesses** fall under section 18 (not 8) of the *Income Tax Act*. In very layperson terms, section 18 says no deductions are allowed, unless it is incurred for income from business and then continues on to say “except for” and restricts specific deductions that are not allowed to be claimed.

Employee deductions are written differently. Instead of allowing all deductions, and then listing the restrictions on them - it only lists which specific deductions are allowed. If it is not listed, you cannot claim it.

The ‘Golden Rule’ of employee deductions is in *Income Tax Act* subsection 8(2) which basically says in layperson terms: unless we tell you otherwise, nothing is deductible, period.

TAX DEDUCTION VS TAX CREDIT

To clarify this, we must understand that there are other claims on a tax return that everyone can get to reduce their income tax amount. These are called **tax credits** (not tax deductions).

These credits include things like medical expense credits, charitable donation credits, disability tax credit, spousal credit, age credit, tuition credit, etc.

Most tax credits can be thought of like getting a store credit coupon at your local “Tax Store” to use against your bill.

It is only good for purchases while you are visiting the Tax Store, and there are no refunds or exchanges unless you have already given us a deposit on your bill first.

If you aren't shopping and won't have a bill anyway, then the Tax Store credit is useless.

The difference with **tax deductions** is that they are taken off the top before you figure out your bill at the tax store. They are not store credit, tax deductions are more like manufacturer coupons.

These manufacturer coupons will reduce the price you pay, but **only on specific items** that the coupon relates to. If you have a different coupon for a different item from a different manufacturer and that item isn't carried in the store, then the coupon is useless.

DECLARATION OF CONDITIONS OF EMPLOYMENT – FORM T2200

Subsection 8(10) simply states that no deduction can be claimed for expenses listed in various areas of section 8, unless this form has been provided and signed by the employer.

Form T2200 is used for the employer to confirm in writing that they required the employee to pay for these expenses as a condition of their employment.

It goes without saying that an employer providing false information on these prescribed government forms would put them at financial risk as well.

The form was recently updated for 2023 tax filings, so readers should confirm that they have the most recent form available, or it may cause tax filing issues for those relying on it.

DEDUCTIBLE EMPLOYMENT EXPENSES

By now, you should realize that employees issued a T4 slip can only deduct specific, itemized expenses that are listed in section 8 – that's it.

Below are details of the more common or less complicated expenses as of the date of this newsletter and what forms may be required for each.

Specific capped amounts are not listed as they may change frequently.

While, at the time of publication, this list may be considered correct, please make sure to verify the current list as it pertains to your specific circumstances.

LEGAL EXPENSES OF EMPLOYEES

Paragraph 8(1)(b) – no form required

Simply put, if you pay a lawyer to go after your employer for amounts payable to you – that, if successful in your lawsuit, would be taxable as income when received – then you can claim the legal costs incurred.

CLERGY RESIDENCE

Paragraph 8(1)(c) – Forms T2200 and T1223 required

A member of the clergy is able to deduct specific home costs against the income earned from full-time employment with a diocese, parish, congregation, or by appointment of a religious order or denomination.

TEACHERS' EXCHANGE FUND CONTRIBUTION

Paragraph 8(1)(d) – Teachers Exchange Fund Contribution – must be an employed teacher – no form required

A single contribution of an employed teacher up to a specified amount that is paid to a fund established by the Canadian Education Association for the benefit of teachers from Commonwealth countries present in Canada under a teachers' exchange agreement.

RAILWAY AND TRANSPORT EMPLOYEE EXPENSES

Paragraph 8(1)(e) or 8(1)(g) - Form TL2 required

These are subject to additional conditions about time away and length of trips, but are primarily for travel, meals, and accommodations expenses of railway or transport employees not receiving any reimbursement or allowance for these items.

SALES RELATED EXPENSES OF COMMISSION EMPLOYEES

Paragraph 8(1)(f) - Form T2200 and T4 Box 42 required

There are some additional expenses allowed under this particular paragraph for those earning commissions that regular employees are not entitled to.

This is a common area of error in filing as many are actually receiving bonuses or other performance target incentives and those are not considered to be commissions.

In order to qualify, employees must have a **T4 slip** (not a T4A) with an amount in **Box 42**. Box 42 is the amount of commissions earned by the employee. If there is no amount in Box 42, then these expenses cannot be claimed.

To claim any of these types of expenses the employee must meet **all** four of the below. The employee must be:

- *required to pay* their own expenses;^{8(1)(f)(i)}
- *required* to ordinarily carry on duties of employment *away from employer's* place of business;^{8(1)(f)(ii)}
- *remunerated* in whole or part *by commissions* fixed *by reference to* the volume of the *sales made or contracts negotiated*;^{8(1)(f)(iii)} and
- *not receiving* an amount from the employer for travel expenses incurred while selling items or negotiating sales contracts.^{8(1)(f)(iv)}

The amount claimed under this particular paragraph cannot exceed the amount in Box 42 (commissions earned).

While many (not all) similar expenses that a business can claim can be claimed here (subject to subsection 8(9) reasonability), they must be tied directly to the sale commission activity (sales of items or negotiation of contracts) – not the employment activity.

Even with these extra allowable expenses, claims cannot be made for capital expenditures. These are things like asset purchases: ex) new phone, computer, tablet, furniture, etc. It also does not allow deductions related to interest (yes, this considered a capital expenditure).

The confusion on the tax treatments for sales commissions earned by individuals commonly lies in how well the person understands the differences between the following:

- An employee earning sales related commissions receiving a T4 with Box 42 amounts, and
- An individual earning commissions from self-employment (ex: real estate agent) receiving a T4A slip with an amount in Box 020.

T4A self-employed commissions are considered business income and Section 8 does not apply.

DID YOU KNOW?

All amounts paid for services require a T4A slip with Box 048 to be issued?

This includes payments between businesses and corporations.

*However, as of the time of publication the CRA is **not** assessing penalties for this.*

*This means, **technically**, every client of our firm should issue a T4A with Box 048 to us for the amount they paid to us or risk a penalty.*

How many T4A slips would you need to issue?

TRAVEL EXPENSES

Paragraph 8(1)(h) – Form T2200 required

To claim any of these types of expenses the employee must meet **all** of the below. They must be:

- *required* to ordinarily carry on duties of employment away from employer's place of business or in different places,^{8(1)(h)(i)}
- *required* to pay their own travel expenses;^{8(1)(h)(ii)}
- be reasonable in amount⁸⁽⁹⁾
- *not related* to motor vehicle costs;
- *not in receipt* of a tax-free travel allowance;^{8(1)(h)(iii)}
- not claiming travel expenses under railway^{8(1)(e)} commission^{8(1)(f)} or transport^{8(1)(g)} expenses (*basically means do not double-claim*).^{8(1)(h)(iv)}

MOTOR VEHICLE TRAVEL EXPENSES

Paragraph 8(1)(h.1) – Form T2200 required

To claim any of these types of expenses the employee must meet **all** the below. They must be:

- *required* to ordinarily carry on duties of employment away from employer's place of business or in different places,^{8(1)(h.1)(i)}
- *required* to pay their own motor vehicle costs incurred in the performance of duties of employment;^{8(1)(h.1)(ii)}
- be reasonable in amount⁸⁽⁹⁾
- *not in receipt* of a tax-free motor-vehicle allowance (*example: per km prescribed rate*);^{8(1)(h.1)(iii)}
- not claiming travel expenses under railway^{8(1)(e)} commission^{8(1)(f)} or transport^{8(1)(g)} expenses (*basically means do not double-claim*).^{8(1)(h.1)(iv)}

DUES AND OTHER EXPENSES OF PERFORMING DUTIES

Paragraph 8(1)(i) – No form required unless specified below

Subject to some restrictions on dues for superannuation, annuities, or insurance under 8(5), amount paid for *any* of the below:

- annual professional membership dues the payment of which was *necessary* to maintain a professional status *recognized by statute*;⁸⁽¹⁾⁽ⁱ⁾⁽ⁱ⁾

- Please refer to Technical Interpretation 2014-0530691E5 to learn more on what **recognized by statute** means.

- office rent or salary to an assistant or substitute required under employment contract;⁸⁽¹⁾⁽ⁱ⁾⁽ⁱⁱ⁾ **Form T2200 required**
- cost of supplies consumed directly in the performance of duties of employment where employee required to supply and pay for;⁸⁽¹⁾⁽ⁱ⁾⁽ⁱⁱⁱ⁾ **Form T2200 required**
- annual trade union dues;^{8(1)(i)(iv)}
- annual dues pursuant to a collective agreement retained by the employer from employee's remuneration and paid to a trade union of which the employee is *not* a member;^{8(1)(i)(v)}
- dues to an advisory committee where payment is required under laws of a province in respect of employment; or ^{8(1)(i)(vi)}
- dues to a professions board where payment is required under laws of a province;^{8(1)(i)(vii)}

but only to the extent the employee was not reimbursed or not entitled to be reimbursed.

MOTOR VEHICLE AND AIRCRAFT COSTS

Paragraph 8(1)(j) – Form T2200 required

Capital Cost Allowance (ie: depreciation) and interest related to acquisition of a motor vehicle or aircraft related to employment.

PAYROLL TAXES FOR AN ASSISTANT

Paragraphs 8(1)(l.1) and 8(1)(l.2) – Form T2200 required

If you are able to hire an assistant mentioned above, you are also able to deduct the employer portion of Employment Insurance premiums, Canada Pension Plan contributions, and Quebec Parental Insurance Plan contributions you must pay as the assistant's employer.

VARIOUS PENSIONS AND BENEFITS

Paragraphs 8(1)(m) to 8(1)(o.2) – Form Varies

Other employment withholdings that are already taken off during the payroll process, like Group RRSPs

or RPPs; Salary Deferral Arrangements; Repayments to Employer for other Pension/Benefits listed, etc.

These are more complex and are maintained by an employer's payroll department beyond the high-level of discussion in this newsletter.

MUSICAL INSTRUMENT COSTS

Paragraph 8(1)(p) - No form required

Where employed as a musician, and in the terms of employment required to provide a musical instrument in the year, the amount of rental, insurance, and maintenance of the instrument as well as the Capital Cost Allowance (depreciation) as long as none of these expenses are already claimed elsewhere.

ARTIST'S EMPLOYMENT EXPENSES

Paragraph 8(1)(q) - No form required

Must be expenses that relate to income from any of:

- creation of physical art (not reproductions)
- composition of a dramatic, musical, or literary work;
- performance in a dramatic or musical work as an actor, dancer, singer, or musician; or
- artistic activity in respect of which the employee was a member of a professional artists' association that is certified by the Minister of Communications

The amount eligible to claim is subject to a capped amount. The capped amount is further reduced by amounts already claimed under:

- motor vehicle and aircraft interest and Capital Cost Allowance;⁸⁽¹⁾⁽ⁱ⁾ and
- musical instruments costs^{8(1)(p)}

APPRENTICE MECHANIC OR TRADESPERSON TOOLS

Paragraphs 8(1)(r), 8(1)(s) - Form T2200 required under 8(6)(b)(iii) and 8(6.1)(c) respectively as well as a specific tool list - cost is calculated under 8(7)

There is a complex formula related to the amount that can be claimed as well as what needs to occur if any tools are disposed of. Please refer to our April 2023 newsletter *Employee Costs of Tools* for specific details.

GST REBATE

Subsection 8(11) - Form GST370

Any amount of a rebate paid or payable to a taxpayer under the *Excise Tax Act* is not considered to be a reimbursement. This form allows the employee to get back GST paid on their eligible expenses, subject to the limitation that the employer certifies that they are not claiming any GST paid on amounts paid to their employees.

The amount received from the GST370 is to be included in income under 6(8) in the year it is received (so the next tax return) and is taxable.

So yes, it is taxable income, but getting back any percentage of GST paid on your expenses is still better than zero.

WORK SPACE IN HOME COSTS

Subsection 8(13) - Form T2200

Not the same meaning as "Business Use" of home as employment income is not business income.

This provision is actually restrictive, not permissive in that it caps the amount deductible to the income earned. In other words, you cannot use work space in home costs to create a loss.

There is common confusion on what can be claimed between:

- **Work space in** home for **T4** employee;
- **Work space in** home for **T4** employee earning Box 42 commissions; and
- **Business use of** home for **T4A** self-employed commissions

T4 Employee – can claim rent and cost of **supplies** – using power, heat, water, internet, maintenance, etc. ⁸⁽¹⁾⁽ⁱ⁾

T4 Employee with Box 42 Commissions – can claim **expenses** for things related to earning employment commissions. This includes rent and supplies above, but also includes others, but does not allow anything related to capital expenditures. ^{8(1)(f)}

Property tax and insurance are expenses but they are **not supplies**. They are only eligible against sales commission income.

Mortgage Interest is a capital expenditure listed in paragraph 20(1)(c). It is **not a expense, nor a supply**.

This is why neither an T4 employee, nor T4 employee with Box 42 commissions, can claim mortgage interest. Only someone in business, ex) T4A Self-Employed Commission agent would be able to claim a portion of mortgage interest related to the business use of home.

LABOUR MOBILITY DEDUCTION

Paragraph 8(1)(t) and subsection 8(14) – No form required

Fairly new legislation to assist with temporary relocations for tradespersons in the construction industry.

We have not seen much discussion of this yet or any filings in our firm, and so we will reserve detailed commentary at this time.

This provision is effective for 2022 and later years.

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Please refer to the 2022 Budget documents as well as the most recent information on it available.

PROPOSED ADDITION - TRADESPERSON TRAVEL EXPENSES

PROPOSED Paragraph 8(1)(q.1) – Form unknown

This is draft legislation that builds off of the Labour Mobility Deduction allowing for a simpler deduction of travel related expenses for tradespersons travelling greater than 120 kms for work.

At time of publication, this was still a proposed addition to the Income Tax Act and not yet enacted. We will reserve detailed commentary until this provision becomes law.

Please refer to the most recent information on this available.

SUMMARY

There are many situations where expenses may be eligible to be claimed against employment income.

If you take only one thing away from this newsletter, let it be this:

There is a difference between what a layperson may think they can claim, and the actual definitions and wording of what we know they can.