

There are various expense categories in Part 4 of CRA's form *T2125 Statement of Business or Professional Activities*, which self-employed people must complete. It can be difficult to categorize expenses, so the following is intended to provide some guidance on organizing your business' receipts and the placement of your expenses on this form.

Step 1: Organize your receipts

Organize your receipts into your own personal categories. Later you will group these personal categories into government categories so they can be easily listed in your tax return.

Example: A musician will have instruments. A painter will have brushes and paints. A landscaper will have gloves and tools. None of these categories show up on the T2125.

Step 2: Do you need to include GST/HST in your expenses?

If you are **not** registered to collect the GST/HST, then **include** the GST/HST in all your expenses.

If you **are** registered to collect the GST/HST, then **exclude** the GST/HST from your expenses.

(Please note: If you are registered with the CRA to use the quick method, **include** the GST/HST in all your expenses)

Step 3: Do you have any capital expenses?

Capital assets are not allowed to be written off entirely in the year of purchase; an annual depreciation amount is calculated. A capital expense is money you spend on an item that provides lasting value, beyond the current tax year. Non-capital items only have value for the current year.

To figure out if something is a capital expense, ask yourself: does the item purchased have a useful life greater than 1 year? If the answer is "yes", then it's a capital expense. Typically, current expenses are used up or expire regularly and need to be bought or renewed every year.

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| Example: | <u>Item</u> | <u>Is it a Capital Expense?</u> |
| | Computer | Yes – you keep using it year after year |
| | Postage stamp | No – once it's used, it's gone; need to buy more |
| | Furniture | Yes – you keep using it year after year |
| | Professional membership | No – you have to renew it every year |

Step 4: Group your categories into CRA categories listed on the T2125

Advertising (Line 8521)

Some common ones are business cards, brochures, posters, flyers, website hosting and domain names, and listings in directories such as the Yellow Pages.

Meals and entertainment (allowable part only) (Line 8523)

This category is for meals or events you attended as part of a business/client meeting. Also, for meals you have when travelling on a business trip. "Allowable part only" means 50% of your business meals and entertainment is included.

Bad debts (Line 8590)

Amounts that you billed clients and included in your income, however you never got paid.

Insurance (Line 8690)

Commercial insurance premiums you pay to cover buildings, machinery and equipment or for products you ship out.

Interest and bank charges (Line 8710)

Interest paid on loans, lines of credit and credit cards for business related expenses.

Business taxes, licenses and memberships (Line 8760)

Include fees such as trade licenses, professional memberships and business name registration.

(Note: Payments to medical plans are a medical expense)

Office expenses (Line 8810)

Use this category for small items such as office stationary, postage, courier fees, etc.

(Note: Computers, copiers, filing cabinets and furniture are capital expenses)

Office stationery and supplies (Line 8811)

Items purchased that are used in the product or service you provide. Example: A hairdresser would include shampoo, hairspray and gel. A florist would include vases, ribbons and packaging.

Professional fees (includes legal and accounting fees) (Line 8860)

Amounts paid to lawyers, bookkeepers, accountants and tax preparers for business advice and service.

Management and administration fees (Line 8871)

Include monthly bank fees for business account, payment processing fees or commissions paid to agents (actors).

Rent (Line 8910)

This line is for rent paid for workspaces or storage that is not part of your home.

(Note: If you work from home, you can write off a portion of rent paid under business-use-of-home).

Repairs and maintenance (Line 8960)

Amounts paid for labour and materials for maintenance and repairs of property, equipment or other items related to your business. (Note: **DO NOT** deduct the value of your own labour)

Salaries, wages and benefits (including employer's contributions) (Line 9060)

Payments to employees including insurance premiums; you can pay a spouse or a child if they do necessary work for your business. If you paid individuals with gifts or meals instead of (or in addition to) money, include the cost here.

Property taxes (Line 9180)

This line is for property tax paid for a workspace that is not part of your home.

(Note: If you work from home, you can write off a portion of property tax paid under business-use-of-home).

Travel expenses (Line 9200)

Costs incurred while on business or professional development trips such as bus/plane/train fare, hotel and rental car fees. Also, include cost of travelling by public transit, GO transit, VIA, taxis or Uber to get to business meetings.

Utilities (Line 9220)

For workspace that is not part of your home, you can include heat, electricity, water and phone expenses.

Fuel costs (except for motor vehicles) (Line 9224)

Fuel, motor oil and lubricants used in equipment and machinery.

(Note: Gas you put in a vehicle in order to get yourself from place to place is a motor vehicle expense)

Delivery, freight and express (Line 9275)

For businesses who ship out a product.

(Note: postage or courier charges on letters or small packages you send are office expenses)

Motor vehicle expenses (not including CCA) (Line 9281)

Include costs for gas, repairs and maintenance, insurance, lease or depreciation, license fees, car washes and CAA membership. The CRA requires a kilometer log of your business travel since personal travel is not deductible.

Capital cost allowance (CCA) (Line 9936)

Capital expenses are included in the business' assets and annual depreciation is calculated using a class structure.

Other expenses (Line 9270)

Category for business expenses that (i) doesn't fit anywhere else or (ii) you're not sure about. Some examples are: performance wardrobe, professional development courses, seminars, conferences (max. of two per year), books needed for research and promotional gifts.

Private Medical Insurance – Include on this line premiums paid for yourself, your spouse or common-law partner, or any member of your household, if you earn at least 50% of your income through your business. This expense qualifies as a medical expense, however, usually preferable to deduct them here.

Lastly, if you don't know where an expense goes . . . don't worry.

If an expense is not capital and not related to meals and entertainment, motor vehicles, or business-use-of-home, then the precise placement won't make any difference to your bottom line. If the CRA decides to do an audit, your task is to prove to the auditor that your expenses are "reasonable". If you've been honest and kept good records then you will be able to confidently prove the reasonableness of your expenses.