

## **THE PASTOR AND HIS TAXES**

The purpose of this paper is to help pastors understand the process of filing their personal income tax returns and identify some of the options available to them.

### **1. Remuneration from Church**

- a. All remuneration should be included on the pastor's T4 return which is required to be filed by the church by February 28 each year. The total included is usually comprised of the base salary and may include the following items:
  - Car allowance, if a flat rate is paid and not a per kilometre reimbursement.
  - Housing allowance.
  - Book allowance.
  - Life insurance, disability insurance where premiums are paid by the church.
  - Etc.
- b. The deductions made by the church (the employer) should be based on the total amount referred to in a. above.
- c. The church should complete the form "Declaration of Conditions of Employment" (Form T2200) and the pastor should have it on hand for submission if requested by Canada Revenue Agency (CRA). (Attached as Exhibit A)
- d. If the church owns and provides a home for the pastor and his family the rental value of the home will be added as a taxable benefit and included in his T4 return. (Note: The pastor will be able to claim the Clergy Housing Deduction as outlined in item 5 below.)
- e. Employment expenses that may be deducted, provided they are reflected as being not reimbursed on the "Declaration of Conditions of Employment (Form T2200), includes:
  - Office supplies
  - Resource materials
  - Vehicle expenses (See 3 below)

### **2. Self employed income**

Pastors may be engaged in services outside their own local church and will receive remuneration for such services as preaching, consulting, etc. If so, the pastor will complete form T2124, "Statement of Business Activities". (Exhibit F) Such income can be reduced for income tax purposes by declaring expenses used to earn that income. Expenses may include:

- Vehicle expenses (Suggested format is attached as Exhibit B.)
- "Office in home" expenses (Suggested format is attached as Exhibit C.)
- Supplies
- Resource material (Books and related magazine subscriptions)
- Etc.

### **3. Vehicle expenses (For a guide to calculation see Exhibit B.)**

- a. If the church pays a flat rate monthly allowance the amount should be included in his T-4 returns. The vehicle expenses may then be deducted on his income tax return.
- b. The pastor should keep a log book that records his odometer readings at the beginning and end of the year, together with kilometres travelled to earn:
  - Employment income from the church
  - Self Employment income
- c. If the Church does not pay mileage the portion of the kilometres that relate to the church activities can be deducted as “Employment Expenses”. Please note that kilometres incurred while driving from home to the church office and return, if an office is supplied at the church, is not deductible.
- d. Expenses relating to Self Employment Income are deductible as business expenses on the pastor’s tax return.
- e. If the church pays some, but not all of the costs by means of a per-kilometre calculation, it may be beneficial to add the amount paid during the year as income and then deduct the amount calculated as illustrated on Exhibit B.

### **4. “Office in Home” Expenses (For a guide to calculation see Exhibit C.)**

- a. The cost of running an office in your home is deductible under one of the following scenarios:
  - If the church does not provide an office and requires the pastor to work out of his home and has on file form T2200 – “Declaration of Conditions of Employment.”
  - If the pastor uses his home for pastoral work and the church indicates on Form T2200 that it is required to perform his duties, even though the church also provides an office for him.
  - If the pastor has self employed income and requires an office at home to earn Self Employed Income.
- b. The office must be a room set aside for the purpose. It cannot be a corner of the kitchen table. It should be used for:
  - Study
  - Writing
  - Storage of library
  - Etc.
- c. If the pastor only has “employment income” he can only deduct utilities and repairs and maintenance from his income.

### **5. Clergy Residence Deduction**

- a. The Income Tax act allows an employment deduction for pastors that amounts to:
  - The annual rent paid or

- the rental value of the home owned by him
  - Plus utilities
- b. The Pastor must have qualifying income (i.e. income from employment as a pastor as shown on his T4 return)
- c. The detailed calculation is on Form T1223. (Exhibit E)
- d. If his qualifying income is less than \$30,000 he is entitled to a deduction of \$10,000 but the deduction may not exceed the amount of the pastor's qualifying income for the year.
- e. If his qualifying income is greater than \$30,000 he is entitled to a deduction of the amount of the rental value plus utilities but not more than one third of his qualifying income.
- f. Please note that this deduction is available only if the pastor has qualifying employment income and receives a T4 return for such income. The deduction is not available for non-employment income, such as self employment or investment income.
- g. The pastor should supply the employer with documentation supporting the amounts claimed on Form T1223. Examples would be:
  - Letter from a realtor identifying the current rental value of the home owned by the pastor. (Sample attached as Exhibit D)
  - Copies of Utility Bills
- h. The employer must sign Form T1223 and keep it on hand.
- i. The employer should reduce the amount of Income Tax deductions at source by this "Clergy Residence Deduction". The church (employer) can only do so if Form T1223 is completed and on hand for review by the Canada Revenue Agency (CRA)
- j. Pensionable earnings for the purpose of calculating Canada Pension Plan should also be reduced by the amount of the Clergy Housing Deduction as calculated on form T1223. (Exhibit E)
- k. The administrative rules and policies for this deduction are covered in Interpretation Bulletin 141R published by The Canada Revenue Agency (CRA).

**6. Some Relevant Interpretation Bulletins and guidelines which can be downloaded from the Canada Revenue Agency Website are listed on EXHIBIT G.**

**Canada Revenue Agency Website: [www.cra-arc.gc.ca](http://www.cra-arc.gc.ca)**

**EXHIBIT A**  
**DECLARATION OF CONDITIONS OF EMPLOYMENT**  
**Canada Revenue Agency Form number T2200**

This exhibit can be downloaded from The Canada Revenue Agency website as follows:

Enter [www.cra-arc.gc.ca](http://www.cra-arc.gc.ca)  
Click on: "English" or "French"  
Click on: "Forms and Publications"  
Click on: "All Forms Listed by Form Number"  
Click on: "T"  
Click on: "T2"  
Scroll down to: "T2200"  
Download it as a ".pdf" file

Print out the form

**EXHIBIT B**  
**SCHEDULE OF AUTOMOBILE EXPENSES**  
**YEAR ENDED DECEMBER 31, \_\_\_\_\_**

Fuel	\$ 1,200
Service	600
Repairs	800
Washes	100
Insurance	1,100
Licenses	100
Capital cost allowance (see below)	3,000
Miscellaneous	<u>100</u>
 Total costs	 <u>\$ 7,000</u>

**Capital Cost allowance calculation**

Undepreciated balance beginning of year	\$ 10,000
Allowance for year – 30%	<u>3,000</u>
 Undepreciated balance, end of year	 <u>\$ 7,000</u>

Note: If the pastor has purchased a vehicle during the year special rules apply and he should get professional tax assistance before filing his return.

Odometer reading, beginning of year	45,000	
Odometer reading, end of year	<u>75,000</u>	
 Kilometres travelled during year	 <u>30,000</u>	
 Kilometres travelled for church per log book	 <u>10,000</u>	<u>33.3%</u>
Amount deductible from Employment Income 10,000/30,000 X \$7,000	<u>\$ 2,333</u>	
 Kilometres travelled to earn self employed income per log book	 <u>5,000</u>	<u>16.7%</u>
Amount deductible from Self Employment Income 5,000/30,000 X \$7,000	<u>\$ 1,169</u>	

**EXHIBIT C**  
**SCHEDULE OF “OFFICE IN HOME” EXPENSES**  
**YEAR ENDED DECEMBER 31, \_\_\_\_\_**

**COSTS FOR THE YEAR ENDED DECEMBER 31, \_\_\_\_\_**

Mortgage interest	\$ 3,000
Municipal taxes	2,450
Hydro	750*
Gas	1,200*
Repairs and maintenance	800*
Insurance	400
Miscellaneous	<u>600</u>
Total	<u>\$ 9,200</u>
Total square feet of office	<u>200</u>
Total square feet in house	<u>1,600</u>
Square foot of office as a percent of total square feet	<u>12.5%</u>
Amount deductible (\$ 9,200 X 12.5%)	<u>\$ 1,150</u>

Note: The above expenses are deductible from self-employed income. The expenses marked with an \* are the only expenses deductible from employment income provided that the “Declaration of Conditions of Employment” (Form T2200 – Exhibit A) allows the deduction.

**EXHIBIT D**  
**(Sample letter from Real Estate agency to Pastor**  
**regarding the rental value of his home.)**

**Real Estate Company Letterhead**

Date \_\_\_\_\_

Dear Mr. and Mrs. \_\_\_\_\_,

As requested, I am listing below the market rental value of your house based on our knowledge of rental homes in your area.

In our opinion your home has a rental value of \$ \_\_\_\_\_ per month (\$ \_\_\_\_\_ per year.) It is understood that this is a net amount and the tenant would be required to pay all utilities, taxes, insurance and other maintenance costs of the house.

Yours very truly,

Name (print) \_\_\_\_\_

Signature \_\_\_\_\_

\_\_\_\_\_ Real Estate Agency

**EXHIBIT E**  
**CLERGY RESIDENCE DEDUCTION**  
**Canada Revenue Agency Form number T1223**

This exhibit can be downloaded from The Canada Revenue Agency website as follows:

Enter [www.cra-arc.gc.ca](http://www.cra-arc.gc.ca)  
Click on: “English” or “French”  
Click on: “Forms and Publications”  
Click on: “All Forms Listed by Form Number”  
Click on: “T”  
Click on: “T1”  
Scroll down to: “T1223”  
Download it as a “.pdf” file  
Print out the form



**EXHIBIT F**  
**STATEMENT OF BUSINESS ACTIVITIES**  
**Canada Revenue Agency Form number T2124**

This exhibit can be downloaded from The Canada Revenue Agency website as follows:

Enter [www.cra-arc.gc.ca](http://www.cra-arc.gc.ca)  
Click on: "English" or "French"  
Click on: "Forms and Publications"  
Click on: "All Forms Listed by Form Number"  
Click on: "T"  
Click on: "T2"  
Scroll down to: "T214"  
Download it as a ".pdf" file

Print out the form

**EXHIBIT G**  
**Related Guides and Interpretation Bulletins published by**  
**The Canadian Revenue Agency (CRA)**

Guide T4404	Employment Expenses
IT Bulletin 352	Employment Expenses including Workspace in Home.
IT Bulletin 522	Vehicle Travel and Sales Expenses
IT Bulletin 141R	Clergy Residence Deduction
IT Bulletin T4130	Taxable Benefits