Claiming a Deduction for Child Care Expenses

Wolters Kluwer

CLAIMING A DEDUCTION FOR CHILD CARE EXPENSES

Millions of Canadian families incur substantial costs each year for child care, and many of those families are entitled to deduct such costs for tax purposes. While that deduction would seem, in principle, to be relatively straightforward, the rules which govern many aspects of the child care expense deduction, including the kinds of expenses which are deductible, the amount of such expenses which qualify for deduction, and even which parent can make the claim, are very detailed and often complex.

The basic general rule is that a taxpayer can deduct child care expenses where those expenses are incurred in order to allow that taxpayer to go to work or to attend school.

More specifically, a deduction can be available where a taxpayer incurs qualifying child care expenses in order to carry out the following specific kinds of activities:

- employment duties:
- carrying on a business, either alone or as a partner who is actively engaged in the business;
- conducting research for which the taxpayer or a supporting person receives a grant; or
- attending a secondary or post-education institution on either a part-time or a full-time basis.

Essentially, an individual who pays qualifying child care expenses in order to work, either in employment or self-employment, or to carry out research for which a research grant is received (with some restrictions) or to attend school, at either a secondary or post-secondary level, can claim a deduction for some or all of those expenses.

What kinds of child care expenses are deductible?

The child care obtained by Canadian families can range from care provided at licensed and day care facilities operated on either a for-profit or a non-profit basis to more informal and frequently unlicensed in-home day care arrangements.

Generally speaking, it doesn't matter, for purposes of the child care expense deduction, whether child care is provided in a licensed day care facility or in a more informal home setting. The Canada Revenue Agency (CRA) identifies the following types of arrangements as qualifying for a child care expense deduction:

- caregivers providing child care services;
- day nursery schools and daycare centres;
- educational institutions, for the part of the fees that relate to child care services (e.g., programs providing after-school care at a child's school);
- day camps and day sports schools where the primary goal of the camp is to care for children (an institution offering a sports study program is not a sports school); or
- boarding schools, overnight sports schools, or camps where lodging is involved.

While the range of child care situations in which fees eligible for a deduction are paid is obviously very broad, there are restrictions, particularly where child care is provided by a single individual. Generally speaking, those restrictions prevent a claim being made for

child care expenses where the fees for child care are paid to a family member or a supporting person. Consequently, it's not possible to claim any deduction for child care amounts paid to a stay-at-home parent of the child, or to certain relatives who are related by blood or marriage and are 18 years of age or less, or to a spouse or common-law partner of the parent of the child who lives with that parent. Identifying who is or isn't related to the child for this purpose is somewhat confusing and not necessarily intuitive. For instance, child care expenses aren't deductible if paid to a sister-in-law or brother-in-law but are deductible if paid to an aunt, uncle, niece, or nephew. A more complete list of the individuals who can provide paid child care services for which a deduction is allowed can be found on the CRA website at www.cra-arc.gc.ca/tx/ndvdls/tpcs/ncm-tx/rtrn/cmpltng/ddctns/lns206-236/214/pymnts-eng.html.

Who is an eligible child?

The question of who is an eligible child for purposes of the child care expense deduction may seem an obvious one, but, once again, there are specific rules which govern the availability of the deduction in this area.

The first, and most obvious definition of an eligible child for purposes of the child care expense deduction is a child of the taxpayer or of the taxpayer's spouse or common-law partner.

A deduction is also, however, available with respect to any children who are dependent on the taxpayer or his or her spouse or common-law partner (with no requirement that they be related by blood or adoption) during the taxation year and whose income for that year is less than $11,635 (for 2017).

Regardless of the relationship between the payor of child care expenses and the child for whom those expenses are paid, there is an age restriction imposed, in that such expenses may be claimed only for a child who is aged 16 or under at some point during the year (i.e., no more than 16 years of age at the end of the year). That age restriction does not apply where the child is dependent on the taxpayer or the taxpayer's spouse because of a physical or mental infirmity.

Who makes the claim?

Where child care expenses can be claimed for tax purposes, that claim is made as a deduction from income, rather than as a credit, and the difference is significant one for tax purposes.

Any deduction claimed reduces taxable income, meaning that no tax is payable on income used to pay the deductible amount. By contrast, a credit reduces the amount of tax payable by the person claiming the credit, usually by a specified percentage of the amount of the expenditure.

Canada's tax system is a progressive one, in which the tax rate levied rises as income increases. Consequently, the same deduction is worth more, in tax terms, to a higher income individual than to a lower income one. When it comes to making a claim for a deduction for child care expenses, the greatest benefit would consequently be realized if that deduction claim were made by the spouse with the higher income. Unfortunately, in most instances, the rules don't allow that.

Where child care expenses are incurred by a two-parent family, the rules specify that the deduction claim must be made by the spouse who has the lower net income. That rule includes situations in which one spouse has no income at all, since the definition of net income, for this purpose, includes a net income of zero. In such cases, of course, the deduction is valueless, since the zero income spouse has no income which will be reduced by the child care expense claim.

In the very unusual circumstances that both spouses have exactly the same net income for the year, they must decide which of them will make the claim for child care expenses.

There are some exceptions to the general rule that child care expenses must be claimed by the lower income spouse. Those situations include circumstances in which the second parent is unable to care for the child for any of the following reasons.

- He or she was attending school full-time or part-time. Whether attendance is full-time or part-time, the program enrolled in must last at least three consecutive weeks.
- He or she was unable, because of physical or mental infirmity, to care for the children. For this circumstance to apply, the second parent must have been in hospital or confined to a wheelchair or bed for a period of at least two weeks. Such circumstances must be certified by a statement from that person's doctor.
- He or she was not capable of caring for the children because of a mental or physical infirmity and such infirmity is likely to continue for an indefinite period. Once again, a statement from the person's doctor certifying such infirmity and its ongoing nature must be provided.
- He or she was confined to a prison for a period of at least two weeks.

Finally, where there has been a marriage breakdown and reconciliation, such circumstances can give rise to a claim by the higher income spouse. In order for that to happen, the following must be true:

- the spouses lived together at some time during the year;
- the spouses were living apart as the result of a breakdown in their marriage at the end of the calendar year;
- the spouses lived apart for at least 90 days; and
- the spouses reconciled and resumed living together by March 1 of the following year.

In such circumstances, however, the higher income spouse can make the claim only where he or she actually paid the child care expenses.

How much can be claimed?

Child care, especially care provided in licensed facilities in larger urban areas, or care provided for infants, can be very expensive – sometimes prohibitively so. Unfortunately, no matter how much a family actually spends on child care in a year, the amount which they can claim for tax purposes is limited both by specific dollar figure limits and by the amount of income earned by the person making the claim.

The specific dollar limits imposed depend on the age of the child for whom care is provided, as well as whether he or she has a severe mental or physical disability. The following limits are currently imposed:

- $8,000 per year for a child who was 6 years of age or under at the end of the year:
- $5,000 per year for a child who was older than 6 years of age at the end of the year but under 16 years of age at any time during the year;
- $5,000 per year for a child who was over the age of 15 throughout the year and who has a physical or mental infirmity which makes him or her dependent on the parent, but who does not qualify for the disability amount; and
- $11,000 per year for a child of any age, for whom the federal disability amount can be claimed. In order to claim such disability amount, the child must have a mental or physical impairment severe enough to limit his or her ability to perform the normal activities of daily life.

How to calculate the actual amount eligible for deduction

The amount of child care expenses which can be deducted (regardless of the amount of the actual expenditure) is the least of the following three amounts:

- the amount of child care expenses actually incurred for a child during the year:
- the statutory limit on such expenses for a child of that age and disability status ($5,000, $8,000, or $11,000); and
- two-thirds of the net income (from line 236 on the tax return) of the taxpayer claiming the deduction.

While that computation sounds complex, it's actually relatively simple in application, as in the following example.

A couple incur $9,600 in eligible child care expenses during the year for their two-year-old daughter. One spouse's net income for the year is $35,000, while the other earns $42,000.

The spouse with the lower net income of $35,000 is required to make the claim for the child care expense deduction, and the amount of that claim is calculated as follows:

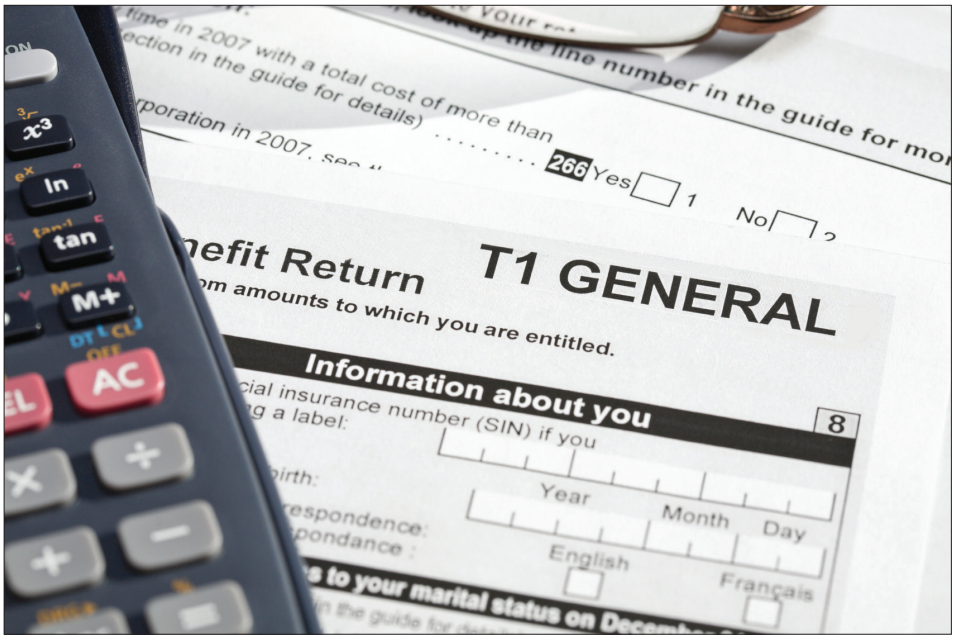
$9,600 – actual child care expenses incurred

$8,000 – statutory limit on expenses claimable for a child under 7 years of age

$23,310 – two-thirds of the claimant's net income for the year ($35,000 × 66.6%)

Since the least of these figures is the $8,000 statutory deduction limit, that is the amount which can be claimed as a deduction for the year. Although the actual cost of child care expenses for the year was $9,600, no deduction is available for the "excess" $1,600 in expenditures incurred.

For some types of tax deductions (e.g., moving expenses), any amounts not able to be deducted during a year can be carried forward and claimed in the next or subsequent years. That's not the case for the child care expense deduction – any costs which are incurred in a particular year but cannot be carried forward and deducted in a subsequent taxation year.



What documentation is required?

As is the case with all claims for tax deductions, it's the taxpayer's responsibility to obtain and keep receipts for all amounts paid for child care. Taxpayers aren't required to file those receipts with paper-filed returns (and, of course, no receipts are filed where a return is filed online), but the CRA can ask to see those receipts in order to verify the claim made and the amount of that claim. And, as is also the case with all claims for tax deductions, the taxpayer must substantiate the claim made with receipts containing the required information, failing which the CRA will deny the claim on assessment.

Where child care is obtained through a licensed child care facility, obtaining receipts which will satisfy the CRA's requirements is generally not an issue. Where, however, child care is provided through more informal, often home-based arrangements, the issue of receipts can be problematic.

Where child care is provided by an individual, receipts provided must include the social insurance number of that individual, as amounts received are income to that person. It is sometimes the case that informal child care arrangements are provided at a lower cost, on the understanding that payments will be made in cash and no receipts will be issued. Parents who agree to such an arrangement must understand, however, that where no receipts are provided (or where receipts provided do not include the provider's social insurance number), no deduction will be claimable on that year's return for any child care expenses paid.

All claims for child care expenses are made using Form T778 E, on which the amount of eligible child care expenses claimable are calculated. That form is filed as part of the annual return, whether that return is filed on line or paper-filed. Form T778 E can be found on the CRA website at www.cra-arc.gc.ca/E/pbg/tf/t778/README.html.

The cost of summer camps

During the school year, parents of school-aged children usually need to be concerned only with arranging and paying for after-school care for those children. During July and August, however, it's often necessary to obtain all-day care and sometimes that means summer camps for school-aged children.

As a general rule, amounts paid (within the statutory and income limits set out above)

for summer camps, whether day camps or overnight camps, qualify as child care expenses for purposes of the deduction. However, where those camps are overnight camps, a per-week limit is placed on the amount which will qualify for the deduction, regardless of the actual cost. Those limits are as follows:

- $200 per week for a child who was 6 years of age or under at the end of the year:
- $125 per week for a child who was older than 6 but under 16 years of age at any time during the year;
- $125 per week for a child who was over the age of 15 throughout the year and who has a physical or mental infirmity which makes him or her dependent on the parent, but who does not qualify for the disability amount; and
- $275 per week for a child of any age, for whom the federal disability amount can be claimed.

Amounts paid for attendance at overnight summer camps (up to these limits) are added to other child care expenses incurred during the year, and the deduction is then calculated as follows:

A couple send their 10-year-old son to overnight camp for one week in the summer, at a cost of $400 per week. They also incur $4,600 in child care expenses for their son throughout the rest of the year. One spouse's net income for the year is $42,000, while the other earns $56,000.

The spouse with the lower net income of $42,000 is required to make the claim for the child care expense deduction, and the amount of that claim is calculated as follows:

$4,725 ($4,600 + $125) – actual child care expenses incurred (since their son is 10 years of age, the weekly limit on overnight camp costs for purposes of the deduction is $125)

$5,000 – statutory limit on expenses claimable for a child over 7 years of age who is not disabled

$27,972 – two-thirds of the claimant's net income for the year ($42,000 × 66.6%)

Since the least of these figures is the $4,725 in allowable child care expenses, that is the amount which can be claimed as a deduction for the year. Although the actual cost of the camp was $400, only $125 of that amount is eligible to be claimed as a child care expense, owing to the dollar figure limit on such costs. No deduction is available for the other $275 in camp costs.

Other available credit claims

For several years, parents could claim a tax credit for the cost of enrolling their children in arts-related or sports-related activities, and there were rules governing how such claims could be integrated with the child care expense deduction claim.

However, both the children's art credit and the children's physical activities credit were eliminated as of December 31, 2016, so no such considerations arise (and no such credits are claimable) for the 2017 and subsequent tax years.

The various limits, qualifications, and restrictions which govern the child care expense deduction can make calculating and claiming that deduction on the annual return a challenge. Current information on the rules that govern the deduction is, however, available on the CRA website, and that information can be found at www.cra-arc.gc.ca/tx/ndvdls/tpcs/ncm-tx/rtrn/cmpltng/ddctns/lns206-236/214/menu-eng.html.