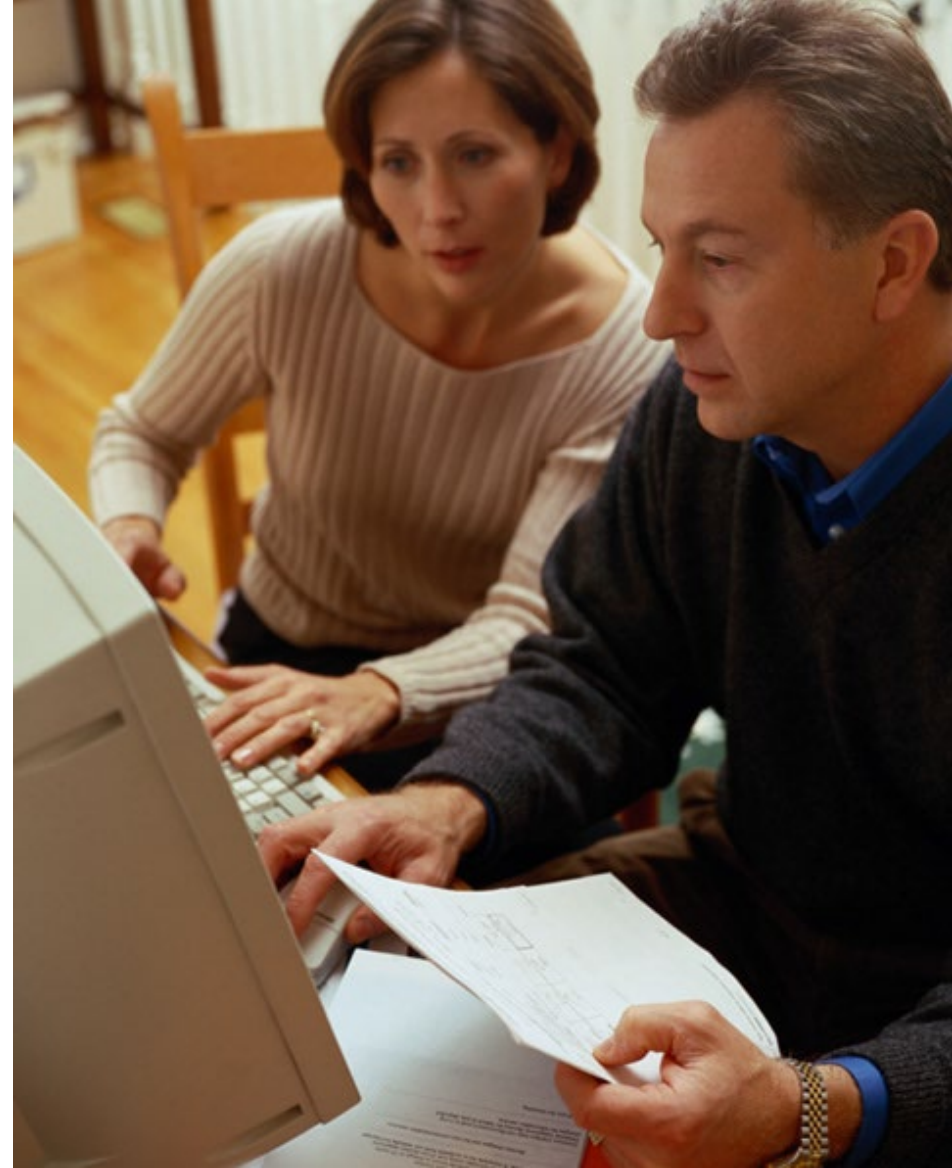


# **THE ESSENTIALS OF CLERGY TAXES**

**February 16, 2022**



# “Minister” Defined.....

*Knight v. Commissioner* – 2 part test:

1. Must be ordained, commissioned, or licensed!
2. Must then meet at least one of these:
  - ✓ Perform religious worship
  - ✓ Administer the sacraments
  - ✓ Management responsibilities in church or denomination
  - ✓ Considered to be a religious leader

# Employee or Self-employed?

- Ministers have “**DUAL TAX STATUS**”
- Federal Income Taxes – an **EMPLOYEE** of “Who”? (1995)
- Should receive a W-2 – not a 1099 form
- W-2 should, at a minimum, show income numbers in boxes 1 & 16

a Employee's social security number 22222 031-04-8264		MB No. 1545-0008			
b Employer identification number (EIN) 02-0514387		1 Wages, tips, other compensation <b>\$18000.00</b>		2 Federal income tax withheld <b>\$3600.00</b>	
c Employer's name, address, and ZIP code <b>Salem United Methodist Church</b> <b>29 Cottage Court Gorham, ME 04038</b>		3 Social security wages		4 Social security tax withheld	
		5 Medicare wages and tips		6 Medicare tax withheld	
		7 Social security tips		8 Allocated tips	
d Control number		9		10 Dependent care benefits	
e Employee's first name and initial <b>Fred G</b>  <b>123 Main St.</b> <b>Merrimack, NH 03054</b>		Last name <b>Smith</b>		Suff.	
		11 Nonqualified plans		12a f g d	
		13 Department of the Treasury-Internal Revenue Service		12b c	
		14 Other <b>Housing Allowance -</b> <b>\$2000</b>		12c c d g c	
f Employee's address and ZIP code		12d d		c	
15 State Employer's state ID number <b>NH 1</b> _____ <b>02-</b> <b>0514387</b> _____ _____ _____ _____		16 State wages, tips, etc. <b>\$20000.00</b>		17 State income tax	
		18 Local wages, tips, etc.		19 Local income tax	
				20 Locality name	

# Employee or Self-employed?

- Must pay quarterly “Estimated Tax” payments or request voluntary withholding from paycheck – Form W-4 (beware of withholding tables)
- Thus, box 2 on W-2 might have numbers...
- Should never be numbers in boxes 3-4-5-6
- Box 14 – can disclose housing allowance amount here

<small>a Employee's social security number</small> <b>22222 031-04-8264</b>		<small>MB No. 1545-0008</small>				
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		<b>7 Social security tips</b>	<b>8 Allocated tips</b>			
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<small>e Employee's first name and initial</small> <small>Last name</small> <small>Suff.</small> <b>Fred G</b> <b>Smith</b>  <b>123 Main St.</b> <b>Merrimack, NH 03054</b>		<b>11 Nonqualified plans</b>	<b>12a</b> <small>f</small> <small>g</small> <small>d</small>			
		<small>13</small> <b>6</b> <small>Department of the Treasury-Internal Revenue Service</small>	<b>12b</b> <small>c</small> <small>c</small>			
		<b>14 Other</b> <b>Housing Allowance -</b> <b>\$2000</b>	<b>12c</b> <small>c</small> <small>d</small> <small>d</small> <small>c</small>			
			<b>12d</b> <small>d</small> <small>c</small>			
<b>15 State</b> <small>Employer's state ID number</small> <b>NH 1</b> <b>02-</b> <b>0514387</b>		<b>16 State wages, tips, etc.</b> <b>\$20000.00</b>	<b>17 State income tax</b>	<b>18 Local wages, tips, etc.</b>	<b>19 Local income tax</b>	<b>20 Locality name</b>

# Employee or Self-employed?

- Different story for Social Security & Medicare taxes – **SELF-EMPLOYED**
- Must pay Self-Employed Contributions Act (SECA) tax of 15.3% of “self-employment” income!!!
- Church can provide a “social security supplement” to help – However, such a payment is taxable income!

# Employee or Self-employed?

- **CAUTION:** Fair Market Rental value of parsonage & church-paid utilities or utilities allowance & housing allowance (if any) are taxable for SECA tax purposes!!!
- Current fair-market rental value appraisal for parsonage/home ...
- Contributions made to UM Pension plan or Medical Reimbursement/Dependent Care Account are not counted here...

# What is “Income”?

- Salaries & wages
- Honoraria for weddings, etc.  
(“constructive receipt” concept)
- Fringe benefits (Christmas gifts...)
- Discretionary Account Funds – wise to have a written policy

# **Business & Professional Expenses – Not Deductible**

Solution: an accountable reimbursement plan established and funded by your church!

- Agreement re: which expenses are considered “business” and reimbursable
- Requires documentation of miles driven or payment actually made (written receipt)
- These payments are reimbursements, not taxable income

# Business & Professional Expenses Options

- transportation & travel (lodging & meals)  
Note: Federal mileage rate is \$ .58.5/mile
- Meals, etc.
- Books & publications
- Educational expenses
- Office equipment (laptop, etc.)

**Every Minister  
Should Consider  
Using a Housing  
Allowance  
Agreement!**



# Basis for Housing Allowance

IRS Code Section 107 (1968) permits “minister of the gospel” to exclude from gross income the “value of home furnished or allowance paid to rent or provide a home”.

- Exclusion from Federal income taxes
- Subject to Social Security/Medicare (SECA) taxes

# Let's Define Some Terms

- **Housing Allowance:** Funds provided by a local church that you use to help pay for housing and utilities
- **Housing Allowance Exclusion:** An amount you elect each year to have “excluded” from your taxable income (Federal taxes) in recognition of housing or parsonage related expenses you pay in a given year

# Church Provided Housing Payments

If your church provides you funds to buy or rent housing – you must have a housing allowance agreement in place in advance to provide any exclusion of these dollars from Federal income taxes!!!

# Housing Allowance Exclusion

“Cost to provide a home” includes:

- Rent or mortgage payments (PMI)
- Down payment
- Real estate taxes
- Insurance (homeowner’s or renter’s)
- Furnishings & accessories & utilities
- Key question: Do you pay significant dollars for housing expenses above what your church currently covers?

# Housing Allowance Exclusion

- Exclusion agreement needs official action taken in advance by Church Council/Admin. Board
- Retroactive designation not allowed, but mid-year corrections can be done.
- Can have a housing allowance exclusion for only one house which must be your primary residence

# Housing Allowance Exclusion

At end of each year, you can deduct from taxable income (Federal taxes) the lowest of three amounts:

- a) designated housing allowance exclusion amount;
- b) actual housing & utilities expenses;
- c) fair market rental value & utilities.

# Church Provides Dollars to Pay for Housing

- Housing allowance: \$18,000
- Actual rent & expenses: 16,550
- Fair market rental value: 19,800
  
- Can exclude \$16,550 from taxable income
  - pastor must report \$1450 (\$18,000 minus \$16,550) as taxable income

# **Future of Housing Allowance Exclusion**

October 2017: Wisconsin U.S. District Court again struck down ministerial housing allowance exclusion as unconstitutional preference for religion!

Spring 2019: Federal Appeals Court upheld the constitutionality of the ministerial housing allowance exclusion

# Avoiding IRS Problems!

- Find a CPA who understands the tax code as it applies to pastors
- [www.gcfa.org](http://www.gcfa.org) – “Services” in top menu; then “Legal Services” and “GCFA Tax Packet”
- <https://www.guidestone.org/Updates/Ministers-Tax-Guide>

# **For More Information.....**

**Rev. James (Jim) Mentzer  
(cell) 910-214-2914  
revmen949@comcast.net**