

# Tax Issues

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From Volume 2005, Issue 5 - 5 2005

## Proper treatment of fringe benefits

by: Dan Busby, CPA

Church employees enjoy many tax-free reimbursements, tax-free or tax-deferred fringe benefits, and perhaps even exclusions from income and/or social security tax. However, in many instances there is a fine line between tax-free, tax-deferred or an exclusion. This fine line can be the difference between good stewardship and illegal reporting of compensation!

Every church employee should receive the maximum benefits that the law provides - this is simply legal and ethical tax avoidance. Too often, perhaps out of naivety, churches treat certain fringe benefits as tax-free or tax-deferred when they are actually taxable - this may make the minister guilty of tax evasion!

What is a fringe benefit? It is a form of payment for the performance of services, and it includes property, services, cash or cash equivalent. Fringe benefits are taxable to an employee even if the benefit is received by or for another person such as a spouse or a child, for example.

The general rule is that all resources provided to a church employee is taxable for income and social security tax purposes unless the tax laws specifically provide tax-free or tax-deferred treatment.

Allowances paid to a church employee without adequate substantiation results in taxable income. Whether the allowance is provided for auto, entertainment, education, supplies, dues and subscriptions, or medical expenses, the result is the same - fully taxable income.

In this article, we will walk through some of the fringe benefits often provided by churches and clarify the taxability of each of them. You may also find the new Taxable Fringe Benefit Guide issued by the IRS in January 2005 to be a helpful tool ([www.irs.gov/pub/irs-tege/fringe\\_bnft\\_flgsg.pdf](http://www.irs.gov/pub/irs-tege/fringe_bnft_flgsg.pdf)).

**Health insurance** - If the church reimburses (based on substantiation of the expense) the employee (or directly pays the premiums) for an individual or group health insurance policy issued by a licensed insurance company, the payment is tax-free (IRC 105). The health insurance payments may be discriminatory; for example, the health insurance fringe benefits do not have to be equal for every employee.

**Life insurance** - If the church pays group-term life premium for coverage up to \$50,000, the payments are tax-free (IRC 79). If coverage over \$50,000 is provided, the value of the additional coverage is fully taxable. Group-term-life benefits must be offered on a non-discriminatory basis unless the arrangement qualifies under the church plan rules.

**Employee-owned vehicle** - Employees often use their personal automobiles on church business. A church's reimbursement of an employee's business auto expenses is excludable from the employee's income, if it is made under an accountable plan. Otherwise, it is a taxable fringe benefit.

Reimbursements for allowable business travel are excludable from the wages of the employee if made at or less than the standard federal mileage rate (40.5 cents per mile for 2005). A reimbursement of actual automobile expenses is another option - although rarely used by churches because of its complexity.

Substantiation rules require the employee to record the date, business purpose, and place of each trip. Mileage should be recorded "at or near the time" incurred. Monthly expense reports generally qualify as "at or near the time."

Rolling advances are often a problem for churches. This is where the church advances the same amount to the employee every month. Even if the employee fully substantiates the auto mileage, if any excess advances are not returned within a certain time period (150 days under the fixed date method and 210 days under the periodic statement method), the timeliness safe harbors of an

accountable plan are not met and the reimbursements become taxable.

**Church-owned vehicle** - When a church-owned vehicle is used partly for church work and partly for personal purposes, the verified business use is not taxable to the employee but the personal use is taxable as wages. The employee can pay the employer for personal use rather than having it treated as wages.

If records are not provided by the employee to the church, the value of all use of the vehicle is wages to the employee. The value of the vehicle use is generally determined by using lease valuation tables provided by the IRS.

**Cell phones, electronic devices, computer** - Churches often provide employees with cell phones and other electronic equipment for use outside of the church's premises in the performance of their duties. The tax law requires employees to account for business and personal use (IRC 274(d)).

Business use of this equipment is excludable from the wages of the employee as a working condition fringe benefit. Personal use is included in the wages of the employee. If substantiation requirements are not met, all use is included in the wages of the employee. Example: A church provides an employee with a cell phone and pays the monthly charges. The church requires the employee to highlight personal calls on the monthly bill. The church includes the direct charges for personal use and a pro rata share of monthly fees and services in the wages of the employee. The business use is not taxable to the employee.

**Medical expenses** - There are only four ways a church can provide for the tax-free treatment of out-of-pocket medical expenses. If your church is reimbursing medical expenses under some other arrangement the amounts are fully taxable.

The four medical plans under which out-of-pocket medical expenses may be covered are subject to the discrimination rules and must be in proper written form:

Cafeteria plan - Only large churches can typically justify the administrative effort and cost for a cafeteria plan (IRC 125) under which an employee may choose from a menu of different medical insurance and healthcare reimbursement options and "pay" for them with before-tax dollars by taking a reduced salary.

**Health reimbursement arrangement (HRA)** - Under an HRA (IRC 105), a church may reimburse medical expenses up to a maximum dollar amount established by the church. HRAs do not provide a salary reduction election.

**Flexible spending account (FSA)** - An FSA (IRC 125) may be established by providing one option - the reimbursement of out-of-pocket medical expenses. It allows an employee to pre-fund medical and dental expenses in pre-tax dollars using a salary reduction election.

**Health Savings Account (HSA)** - Churches can provide high-deductible health insurance and make tax-excludable contributions to an employee's HSA (\$5,250 in 2005 for family coverage and \$2,650 for individual coverage) (IRC 223). The HSA funds provide the money to cover the employee's out-of-pocket medical expenses.

**De minimis fringe benefits** - A property or service provided by a church for an employee that has a small value, and accounting for it is unreasonable or administratively impractical, may be a de minimis fringe benefit and tax-free (IRC 132). The value of the benefit is determined by the frequency provided to each individual employee or by the frequency provided to the whole staff. A benefit of \$100 does not qualify as de minimis.

Examples of de minimis fringe benefits that are tax-free include the infrequent, not routine, personal use of photocopier; group meals or employee picnics; theater or sporting event tickets; coffee, doughnuts, and/or soft drinks; flowers, fruit for special circumstances; local tele-phone calls; gift certificates limited to specific non-cash items, such as holiday turkey, coffee or drinks.

Examples of benefits not qualifying as tax-free de minimis fringe benefits are cash, except for occasional and infrequent meal money to allow overtime work; cash equivalent, such as a gift certificate for a department store or allowing "cash back;" use of an apartment, vacation home or boat owned by the church; commuting use of church's vehicle more than once a month.

The proper and adequate understanding of these and other fringe benefits is a fundamental prerequisite in order for a church to properly steward God's money.

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## **Freedom of religion does not allow for discrimination**    << [BACK](#)

From Volume 2007, Issue 11 - 11 2007

### **The First Amendment protects churches in regards to employment decisions but parameters still apply.**

*by: Kathleen J. Turpin*

"Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof ..." — The First Amendment to the U.S. Constitution

The First Amendment to the U.S. Constitution gives religious organizations a lot of freedom from government regulation. It gives them so much freedom, in fact, that church and ministry leaders may assume that it protects them from employment discrimination complaints as well. This is a dangerous and misleading assumption. While the First Amendment protects religious organizations from some claims, its protection extends only to a portion of the employment discrimination claims possible.

The First Amendment protects churches from legal challenges to employment decisions in two primary areas: discrimination based on religion and decisions involving ministerial employees. In addition, it provides some protection in legal cases that might cause a court to get "excessively entangled" in church issues.

### **Religious discrimination**

Federal law bars employment discrimination based on race, color, religion, sex, or national origin. Such discrimination isn't limited to hiring and firing. It also could apply to promotions, transfers, training, pay, fringe benefits, and other terms and conditions of employment.

However, the law makes an exception for churches in the area of religious discrimination. This exception is found in Section 702 of Title VII of the Civil Rights Act of 1964. The Supreme Court has found that religious institutions may discriminate on the basis of religion when making employment decisions about any and all employees. A Christian college can discriminate against Muslims, for example.

The Section 702 exemption is limited to religious discrimination, however. It does not apply to claims of discrimination based on sex, race, color, age, or national origin. The courts have also found that the First Amendment precludes them from intruding into the employment relationship between a church and its ministerial employees. This means that the courts usually won't interfere with an employment decision involving a minister, even if the minister claims discrimination based on race, age, or sex.

There are a few exceptions. One is sexual harassment. Most courts have found that religious institutions don't encourage sexual harassment as part of their religious foundation. Consequently, courts can make a determination on the case by applying secular principles that won't infringe on religious issues.

## **Ministerial employee**

The greatest debate is what constitutes a ministerial employee. Courts differ significantly in defining how broadly this exception should apply. Furthermore, the Supreme Court has rarely officially addressed the “ministerial exception,” so this issue has been handled by the various federal districts. This, of course, has led to different interpretations.

One test various courts have applied seeks to determine the primary duties of the plaintiff. If the employee’s primary duties consist of one of the following options, the courts have considered the person to be a minister:

**Teaching**

**Spreading the faith**

**Church governance**

**Supervision of a religious order**

**Supervision or participation in religious ritual or worship**

Courts have also looked at whether the employment decision involved selecting an employee who would serve as a liaison between the church and those whom it would touch with its message. A church that treats all of its employees as if they qualify for the ministerial exception may wish to consider the courts’ rulings in this area.

The courts have often tried to determine if a religious employment issue would cause excessive entanglement of church and state because it involves evaluating subjective religious factors. Many times, this argument follows a determination that someone is not a ministerial employee.

While the “excessive entanglement” argument has not always been successful, courts have sometimes refused to get involved in a matter if a church connects its basis for discrimination to a religious tenet.

For example, if a Christian college held a religious belief that women should not hold positions of authority over men, and it failed to promote a woman on that basis, it may be able to successfully defend its case based on a First Amendment argument.

Because the grounds for termination arguably concerned a theological principle of the college, a court might dismiss the case to avoid getting entangled in determining the propriety or application of religious doctrine.

In another example, let’s say that you fired the church secretary because she became pregnant outside of marriage. She could likely claim sex discrimination under Title VII of the Civil Rights Act.

Your church would presumably explain that she was terminated not because she became pregnant but because she had sex outside of marriage, which violates the tenets of the church. Most courts have held that as long as the termination was applied equally to women and men (a male employee also could be terminated for having extramarital sex), the issue isn’t sex discrimination, and the termination was legal.

## **When does the First Amendment not apply?**

In most other cases, the First Amendment does not provide legal protection for churches in the area of employment discrimination. Small churches may consider themselves exempt from employment discrimination laws because Title VII of the Civil Rights Act applies only to organizations with 15 or more employees. This, too, is a dangerous assumption. Although Title VII may not apply, nearly every state has human rights statutes that mirror federal discrimination statutes, and their requirements vary. Laws in a few states apply to businesses with more than one employee.

In addition, some federal employment laws, such as the Fair Labor Standards Act, apply to all organizations that employ more than one person. The safest course of action is to consult with a local attorney who is familiar with employment law. Your attorney can help you to follow state and federal employment laws, even if they don’t currently apply to your religious organization.

As your ministry grows, you may not realize when you cross the line from being exempt to being affected by state or federal laws. For example, your church might employ only five people. However, it operates a preschool or day care center that employs 30. Although you consider the childcare operation to be separate from the church, a court may view it differently.

It's best to assume that all employment discrimination laws apply to you. Learn the parameters for hiring, firing, or disciplining church staffers. If you don't, a legal challenge could catch you off guard, and the First Amendment won't be there to protect you.

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### **Classification of workers other than ministers**

Before starting to fill out Form W-2, it is important to determine which individuals receiving compensation as workers are employees vs. independent contractors. The decision determines a church's responsibility under the Federal Insurance Contributions Act (FICA) for social security purposes, income tax withholding responsibilities, potential coverage under the Fair Labor Standards Act, and coverage under certain employee benefit plans. In some instances, misclassification can lead to significant penalties.

The IRS generally relies on 20 common law factors to determine whether workers are employees or independent contractors. Generally, employees:

- Comply with instructions.
- Have a continuous relationship.
- Perform work personally.
- Work full-time or part-time.
- Are subject to dismissal.
- Can quit without incurring liability.
- Often are reimbursed for expenses.
- Must submit reports.

Independent contractors normally:

- Set the order and sequence of work.
- Set their hours of work.
- Work for others at the same time.
- Are paid by the job.
- Offer their services to the public.
- Have an opportunity for profit or loss.

- Furnish their tools.
- May do work on another's premises.
- Often there is substantial investment by the worker. Frequently questions arise about the classification of certain church workers. Part-time workers such as secretaries, custodians and musicians require special attention for classification purposes. If a part-time worker receives pay at an hourly rate, it will be difficult to justify independent contractor status.

### **Classification of ministers**

In addition to determining whether all workers are employees or independent contractors, it is important that your church decides if the services of a minister employed by the church qualify for special tax treatment as ministerial services. Nearly all ordained, commissioned or licensed ministers serving local churches will qualify for the special tax treatments with respect to services performed in the exercise of ministry. The IRS and courts apply certain tests to ministers serving local churches. These tests may include determining whether the minister administers the sacraments, conducts worship services, is considered to be a spiritual leader by the church, and performs management services in the "control, conduct or maintenance of a religious organization." The term "salary reduction" is a proper phrase for ministers only in connection with 403(b) tax-sheltered annuities, 401(k) plans, flexible spending plans, and employee-funded qualified medical expense reimbursement plans.

### **Business expense reimbursements**

Business reimbursements must be included on Form W-2 as taxable income, unless paid through an accountable reimbursement plan that has been formally adopted by the church board. If the church establishes a dollar limit on the expense plan (instead of reimbursing 100 percent of expenses), any balance remaining in the expense plan at year-end should remain with the church to avoid nullifying the entire plan.

Be sure that the data reflected on Forms W-2, W-3, and 941 are reconciled before distributing Form W-2s to employees. There is one exception: If the minister is the only employee of the church and no federal or state income tax is withheld from the minister's compensation, there is no requirement to file Form 941 quarterly.

Make all entries without a dollar sign or comma but with a decimal point and cents. For example, enter 4000.00, not \$4,000. If you enter 4000, the IRS scanning equipment will read it as 40.00. Magnetic filing is required only if you are filing 250 or more Form W-2s.

### **Key data to include**

Box 1-Wages, tips and other compensation. Before considering any payroll deductions, include the following in Box 1:

- Total wages paid during the year (including love offerings paid by the church).
- The value of non-cash payments, including taxable fringe benefits.
- Business expense payments under a non-accountable plan, including "allowance" for automobile usage, entertainment, books, continuing education, and so on.
- Payments made by a church to an employee's Individual Retirement Plan.
- Nonqualified moving expense reimbursements and payments for either ministerial or lay employees.
- The value of personal use of a church-owned or leased automobile.
- Severance pay and settlements for back wages.

Exclude the following: The fair rental value of a church-provided parsonage or a properly designated

housing allowance for ministers; auto or business expense reimbursements paid through an accountable expense plan; contributions to 403(b) tax sheltered annuities or 401(k) plans.

**Box 2**-Enter the total federal income tax withheld. A qualified minister may enter into a voluntary withholding arrangement with the employing church. The minister may request that an additional amount of income tax be withheld to cover self-employment tax. The additional amount withheld is reported as income tax withheld on the quarterly Form 941 and in Box 2 of Form W-2. If the church reimburses part or all of the self-employment tax liability, the church reports the reimbursement as additional compensation on Form 941 and in Box 1 of Form W-2.

**Box 3**-Show the total wages paid (before payroll deductions) subject to employee social security tax (FICA). This amount must not exceed \$87,900 in 2004 (the maximum social security tax wage base). Generally, all cash and non-cash payments reported in Box 1 also must be shown in Boxes 3 and 5. For qualified ministers, Boxes 3 and 5 are left blank since ministers are not subject to FICA tax. Nonqualified moving expense reimbursements and payments for lay employees are included in Box 3.

**Box 4**-Show the total FICA social security tax (not including the church's share) withheld or paid for the employee. The amount shown must equal 6.2 percent of the amount in Box 3 and must not exceed \$5,449.80 for 2004. Do not include the matching employer ICA tax.

A few churches pay the employee's share of the FICA tax for some or all non-minister employees instead of deducting it from the employee's wages. These amounts paid by the church must be included in Boxes 1, 3, and 5 as wages, and proportionately in Boxes 4 and 6 as social security and Medicare tax withheld. Box 4 should be blank for qualified ministers. Any amounts of withholding to meet the minister's SECA tax liability must be reported in Box 2, not in Box 4 or Box 6.

**Box 5**-The wages subject to Medicare tax are the same as those subject to social security tax (Box 3), except there is no wage limit for the Medicare tax. Box 5 should be blank for ministers. Nonqualified moving expense reimbursements and payments for lay employees are included in Box 5. For example, a non-minister employee is paid wages of \$88,000. The amount shown in Box 3 (social security wages) should be \$87,000, but the amount shown in Box 5 (Medicare wages) should be \$88,000. If the wages are less than \$87,000, the amounts entered in Boxes 3 and 5 will be the same.

**Box 6**-Enter the total employee Medicare tax (not your share) withheld or paid by you for your employee. The amount shown must equal 1.45 percent of the amount in Box 5. Box 6 should be blank for ministers.

**Box 12**-The following items are most frequently inserted in Box 12 by churches:

C - Group-term life insurance. If you provided an employee more than \$50,000 of group-term life insurance, show the cost of the coverage over \$50,000. Also include the amount in Box 1 (also in Boxes 3 and 5 if a lay employee).

E - Section 403(b) voluntary salary reduction agreement to purchase an annuity contract. This amount would not be included in Box 1 for either ministerial or lay employees. This amount would be included in Boxes 3 and 5 for a lay employee.

P - Qualified moving expenses paid directly to an employee must be reported on Form W-2, only in Box 12, using code P. Qualified moving expenses paid for an employee directly to a vendor are not reportable on Form W-2.

**Box 14**-You may use this box for any other information you want to give your employee. Label each item and include information such as health insurance premiums deducted or educational assistance payments. The minister's housing allowance could be included with the words "Housing Allowance."

If the church owns or leases a vehicle for an employee's use, the value of the personal use of the vehicle is taxable income. The value of the use of the vehicle is established by using one of the methods prescribed by the IRS. The amount of personal use must be included in Box 1 (and in Boxes 3 and 5 if a lay employee). The employee is required to maintain a mileage log or similar records to

substantiate business and personal use of the vehicle and submit this to the church. If the employee fully reimburses the church for the value of the personal use of the vehicle, then no value would be reported in either Box 1 or in Box 14.

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## Tax Issues

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### Catch a break on health care costs

*by: Frank Sommerville, JD, CPA*

The tax code is frequently used by Congress to manage the U.S. economy. Since health care costs have increased dramatically, Congress has enacted several tax breaks to help health care consumers. All these tax breaks work the same way: If you pay health care costs with money that is not subject to tax, it costs less. For example, to pay a \$100 health care expense with wages after taxes were deducted, the individual would typically need to earn \$140. On the other hand, if the taxpayer could pay this expense with untaxed wages, the individual would only need \$100.

Since Congress wants employers to fund health care expenses, all these methods involve the employer working with the employee to minimize the employee's tax burden. This is why the church must take the steps to create health care benefits that allow health care expenses to be paid with untaxed wages.

### Health insurance

The church may provide health insurance to its employees with untaxed compensation. Further, federal law allows employers to discriminate in how they provide health insurance. This means that the church could pay the full premiums for the minister and his family, while agreeing to pay the premium that covers only the secretary. Please note that some state laws and insurance companies prohibit discrimination and require all employees to be enrolled. You should check with your tax advisor and insurance agent to see if you are in one of those states.

### Health care reimbursement plans

Sections 105 and 106 of the Internal Revenue Code (IRS) allow employers to adopt a plan to reimburse employees their qualifying health care expenses. The reimbursement is tax-free to the employee. The plan must be in writing and must not discriminate in favor of the highly compensated employees. The church is free to select the health care expenses it will reimburse and set any limits that it desires.

This plan may include reimbursement for all medical expenses that would qualify for a tax deduction, including prescription medicines. Recently, the IRS approved a plan that included nonprescription medicines on the approved reimbursement list.

### Health care savings accounts

In December 2003, Congress passed the Medicare reforms that included allowing certain employees to set up a personal health care savings account. These accounts are patterned after the Individual Retirement Accounts (IRAs). To participate in the health savings account, the individual must be covered by a high-deductible health insurance policy. A high-deductible policy is one with a deductible in the amount of \$1,000, or up to \$5,000 under certain circumstances.

Employees may submit qualifying health care expenses to the account administrator for reimbursement. The reimbursement is tax-free.



## **Cafeteria plans**

All the above methods involve only church-funded benefits. For a variety of reasons, this may not always be possible. That is where cafeteria plans come in. A cafeteria plan provides a convenient way for employees to fund their own fringe benefits. The health insurance premiums and the Section 105/106 plans can be funded with employee salary reductions. In addition to these health care expenses, the cafeteria plan can reimburse other qualified expenses, such as child care expenses. The church saves money because the amounts paid into the cafeteria plan by lay employees are not subject to payroll taxes. However, some important things need to be considered before setting up a cafeteria plan.

First, the church must adopt a cafeteria plan that meets all the technical requirements. Second, the employees must sign a form authorizing the salary reduction. The amounts that go into the cafeteria plan are not taxed. This method achieves the same goal as providing the health expense benefits described in the prior paragraphs.

In 2002, the IRS made it even easier for churches to adopt a "premium-only cafeteria plan." The IRS removed all filing requirements for premium-only cafeteria plans. This means that the church can adopt a qualifying plan that reduces taxes without requiring a third-party administrator.

However, none of the tools can be implemented without expert advice. They all have technical requirements. Also, they have continuing requirements that must be met. A church cannot adopt any of these plans and simply forget it.

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## **Tax Issues**

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From Volume 2004, Issue 3 - 3 2004

### **Prepare error-free tax returns**

*by: Frank Sommerville, JD, CPA*

February is the time when many ministers begin gathering their tax information. Many ministers overlook critical items, creating costly errors when their tax return is prepared. This article will highlight some of the more common errors in the following areas:

#### **Income**

Everything of benefit received because of ministerial services is taxable, unless the minister can find a specific code section that excludes that type of income from tax. Ministers should review their Form W-2 to determine whether all forms of compensation are reported properly. For example, the church must add to taxable income non-cash compensation given to the minister. Common forms of non-cash compensation would include the provision for the use of a car, life insurance and gifts received from the church or parishioners. Taxable income would include non-payroll items such as love gifts and anniversary and birthday gifts from the church. Finally, the minister must remember to include in taxable income any payments received from individuals for services. Typical ministerial services generating this type of income would include funerals, weddings and special services.

The minister should consider whether certain fringe benefits meet the requirements to be excluded from income. These items would include housing allowance (discussed below), tuition discounts, health insurance, life insurance, disability insurance, travel, entertainment, childcare, educational expenses, and business expenses.

#### **Housing allowance**

To be eligible to receive a housing allowance, the individual must hold current recognition as a minister from a recognized church and be performing the duties of a minister. While a detailed

discussion of this definition is beyond the scope of this article, it is still important for the minister to provide proof of their ministerial status to their church. Annually, each minister should submit proof of their recognition as a minister (license, ordination or commission) to the employing body and confirm that they are currently in good standing with the issuing body.

Performing the duties of a minister gets complicated in today's entrepreneurial church world. The minister is clearly performing the duties of a minister if they are leading worship services and performing other sacerdotal functions. If the individual's primary job is to sweep the floors, then that person is not performing the duties of a minister. Outside these two extremes, the church and the minister should consult with a clergy tax professional to determine whether the individual is performing the duties of a minister.

If the minister is receiving a cash housing allowance, then the church must designate the amount of the housing allowance before paying it to the minister. The minister may exclude for income tax purposes the lowest of three amounts: (1) the amount properly designated by the church, (2) the amount in cash that the minister spent owning, occupying or maintaining a home, or (3) the fair rental value of the home, as furnished and including appurtenance, plus utilities. If the amount designated by the church exceeds the other two factors, then the minister must report the excess amount as miscellaneous income on their tax return. Unless the minister has elected to exempt their ministerial income from self-employment taxes, the minister must report the full amount of housing allowance designated by the church on Schedule SE.

The most common mistake is not correctly classifying the cash expenses related to owning, occupying or maintaining the residence. For example, many ministers overlook yard upkeep and furnishings as allowable housing expenses. The rent or mortgage payment and down payment also count.

If the church provides a home to the minister and the minister pays self-employment tax on their income, then the church must report to the minister the fair rental value of the home provided, as furnished, plus utilities. This amount is usually reported in a letter addressed to the minister and never included as taxable income on the minister's W-2 Form.

### **Deductions**

While I strongly recommend that all churches adopt an accountable expense reimbursement plan, many have not done so. Besides, the minister will likely have expenses related to their other sources of income (funerals, weddings and special services). With an accountable expense reimbursement plan, the minister does not count any reimbursements as income and does not deduct any business expenses on their tax return.

Many ministers overlook the Deason Rule when claiming ministerial expenses. This rule basically requires the minister to reduce the amount of expenses claim by the ratio of the tax exempt income (allowable housing allowance) to the total income. For example, if a minister received \$30,000 in salary, plus \$10,000 in housing allowance, the minister would only be allowed 75 percent of their business expenses.

Many ministers suffer from record keeping deficiencies; that is, they are poor record keepers. Travel and entertainment expenses require special records. For entertainment, the record must show who was entertained, the business purpose for the entertainment, the place, amount, and date(s). For travel, the record must show the persons traveling, the business purpose for the trip, activities during the trip, cost, and dates.

Trips also create record keeping problems. The minister must show the destination, the purpose of the trip, miles driven, and date for each claimed trip. Usually a calendar showing the appointments of the day is very useful in creating this record. Except for special circumstances, the minister cannot count the trip to and from their residence to the church as business miles, though they drive it several times a day.

This article contains just a few common mistakes. Every minister is responsible to file an error-free tax return. I suggest that they review it very carefully before submitting it to the IRS. By the way, the return should always be sent to the IRS via certified mail, return receipt requested.

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