

Frequent Tax Questions and Answers For Active Ministers

1. What's the most important thing an ordained minister should know when preparing taxes?

The single most important thing an ordained minister should know is that he or she has a “dual status” when filing a tax return. Ordained Presbyterian clergy are — in most cases — considered:

- *employees* for federal income tax purposes
- *self-employed* for Social Security tax purposes, meaning the minister must pay the full Self-Employment Contributions Act (SECA) tax amount

Given that most clergy are considered employees for federal income tax purposes, their churches must report clergy income to the IRS on form W-2, not form 1099. Form 1099 is used only for consultants and independent contractors.

Clergy serving in non-parish situations and those in interim, stated supply, or tent-making ministries may have unique circumstances that require consultation with a tax adviser familiar with clergy tax matters.

Remember the following with regard to the clergy housing allowance:

- Only an employer may designate housing allowance, and it must be done in advance.
- It is excluded from federal income tax calculation only.
- It must be included when calculating Social Security taxes.
- Ministers who are independent contractors *may not* exclude 1099 income under tax code section 107.

The employment status of clergy is further detailed on [irs.gov](https://www.irs.gov), the IRS website. You may read more about this in the annual *Tax Guide for Ministers*, published by the Board of Pensions in January and available on Pensions.org.

2. Is there any danger pastors will lose the clergy housing allowance? Also, is it available to me when I retire?

It is impossible to know what Congress, the courts, or the IRS might do in the future. Under current federal law, the clergy housing allowance is also available to retired ministers *if* a church pension board (such as the Board of Pensions) annually designates retirement income as housing allowance subject to the IRS rules. Currently, the Board designates retirement pension payments, disability payments, and/or distributions from the Board-sponsored Retirement Savings Plan as 100 percent clergy housing allowance, to the extent the recipient can justify that designation.

3. How do I determine the fair market rental value of my residence and furnishings? Are interims and non-parish clergy treated differently from called and installed pastors?

To date, the IRS has not given specific guidance on how to determine fair market rental value. Tax expert Richard R. Hammar, co-author of the Board's annual *Tax Guide for Ministers and Federal Reporting Requirements for Churches*, says that one way to get a determination is to consult real estate experts.

For example, talk with a local Realtor or someone in the residential rental business about obtaining the fair market rental value of your home (or manse), furnished, plus any appurtenances — such as a garage — in writing. This can be a drive-by estimate given to you in a signed letter from the Realtor. At a minimum, find and keep comparable rental listings in your neighborhood from the newspaper, Craig's List, or another independent source of reference.

In terms of how clergy are treated for purposes of the housing allowance based on their particular call, a key requirement is that the work be ministry-related, i.e., either a call approved by the presbytery or a validated ministry. Who the employer is may also play a role as well as the job function. **Consult a tax professional to determine your status.**

4. What items can be considered for “furnishing” and “maintaining” a residence for the housing allowance? (Manse vs. own residence)

The IRS has never provided detailed guidelines for what expenditures qualify for exclusion under the clergy housing allowance. However, the Board's annual *Tax Guide for Ministers* lists items that Mr. Hammar advises should be included in computing a housing allowance exclusion.

5. What are the tax advantages of the Board's Retirement Savings Plan (RSP) for clergy?

a) Contributions, via salary deferral, save both federal income and Social Security taxes for clergy. (Lay church workers save on federal income taxes only.) A contribution to the RSP could mean a tax deferral of 10 percent to 25 percent or more.

b) The Board's RSP has no setup fees, all investments are “no-load” (no sales charges), and there is a \$3.75 per quarter fee deducted by Fidelity Investments from each participant's account to offset administration and recordkeeping.

c) Investments grow tax-deferred while in your account.

d) Investment options include a variety of mutual funds (and two proprietary funds), and thus reduce your investment risk versus investing in individual stocks or bonds. Remember, *all* investments carry some level of risk.

e) A church or employing organization can also put money into your RSP. To the extent that it is a “match” under rules adopted by the Board of Pensions, it is *not* included in your effective salary and thus not subject to plan dues.

f) Distributions to clergy may be considered housing allowance to the extent that the funds are used in compliance with the IRS rules for the clergy housing allowance.

g) The RSP account is easy for the church or employing organization to set up. Once set up, the employer or church pays a monthly invoice.

h) There is 24/7 account access via the Internet or phone through Fidelity Investments. Your account information is confidential.

6. What are the IRS implications for honoraria, “love offerings,” and fees received separately from compensation?

For the most part, any income received in exchange for services rendered is taxable for both federal income and Social Security taxes, regardless of how it was received. The only exceptions are income paid for certain employer-provided benefits and housing allowances.

If income comes through a source other than your employing organization, and it is more than \$600 from one source in a calendar year, it needs to be reported at year-end on a Form 1099-MISC by the organization that paid it to you. Any additional income that you received from your church or employer must be reported on your W-2.

Regarding “love offerings,” there are several tax decisions to draw upon regarding special occasion gifts, according to Mr. Hammar.

One criterion for determining whether a gift is taxable or nontaxable is *the intent with which the money is given*. If the donor wants to provide additional compensation to his or her minister in recognition of services rendered, similar to a bonus, then the contribution ordinarily will be taxable compensation rather than a tax-free gift. If the contribution “proceeds from a detached and disinterested generosity” and is offered out of sincere affection, respect, and admiration, not out of a desire to compensate the pastor more fully for services rendered, it *might* qualify as a gift.

In all cases, the contribution must be made directly to the pastor, not the church, and the donor must *not* take a tax deduction for the gift.

One example is a Christmas gift offering. The offering is announced, and members are told to make their gifts by check payable directly to the pastor. They are told contributions will not be receipted through the church and will not be tax-deductible. Because the church collected the offering and gave it to the pastor, he or she would report it as taxable income. The church would include the total amount on his or her W-2 for that year.

In any of these examples, the pastor would be liable in an audit because the church is not required to withhold payroll taxes for clergy and ***misrepresenting income on a W-2 Form could jeopardize the church’s own tax status.***

7. What are the tax implications when the church designates a portion of compensation as a Self-Employment Contributions Act (SECA) tax offset? If the church does so, why do I need to pay Social Security and federal tax on it, too? How does this affect my effective salary reporting to the Board of Pensions?

By law, clergy are considered self-employed for Social Security tax purposes, and therefore *cannot* have any of their SECA tax paid for them on a tax-favored basis. If you receive any allowance or SECA “offset,” unfortunately it will be subject to federal income tax and added to your SECA tax base.

To the extent that any such SECA allowance is $\frac{1}{2}$ or less of the estimated amount due in any given year, the employer does not need to include the allowance in calculating the minister's effective salary reported to the Board or pay plan dues on that amount.

Amounts greater than $\frac{1}{2}$ of the estimated SECA amount are reportable and subject to plan dues. This dues adjustment is designed to treat clergy and lay church workers — who have $\frac{1}{2}$ of their Social Security tax (FICA) paid by the employer on a non-dues-bearing basis — equally.

8. How can I use the clergy housing allowance to maximum benefit when purchasing a home? What are the basic rules related to the clergy housing allowance?

It is possible to exclude the down payment and other home-purchase costs in calculating the amount of your allowable clergy housing allowance. However, you cannot exceed the total amount of such an allowance the IRS will allow in any given year. The maximum amount you can exclude for housing allowance in any year is the *smallest* of the following:

- the fair rental value of your primary residence, furnished, including appurtenances such as a garage, plus the actual annual cost of utilities
- the amount designated in advance by your church or session
- the amount you actually spent

With regard to clergy entering a retirement facility, admission fees to retirement communities may be included in your calculation of the housing allowance. However, they can be claimed only in the year you moved into the facility and cannot be pro-rated over a longer period of time.

In addition, the monthly “maintenance fees” in such communities often include housing costs, which may be broken out for you by the facility's administration.

Important note: The admission and maintenance fees cannot be excluded unless your employer designated the amount as a housing allowance in advance of your earning the income, i.e., entering the retirement community in January versus December.

9. Does the Board offer a list of qualified tax preparers familiar with clergy tax issues?

The Board of Pensions does not maintain any such list because we are not tax advisers, nor are we an accrediting institution for them. Active members have access to [Enhanced Financial Services](#) through the Employee Assistance Program. You may wish to check with Enhanced Financial Services about qualified tax professionals in your area who specialize in clergy taxes.

You may obtain copies of the Board's tax-related resources, including the annual guides, at [Pensions.org](https://www.pensions.org) or by calling 800-773-7752 (800-PRESPLAN).

Disclaimer: *The Board of Pensions does not provide individual tax advice to individuals or employers. The preceding information is provided as a part of the Board's education program. For updated forms, guidance, and instructions, individuals and employers should go to the IRS website at [irs.gov](https://www.irs.gov) or consult with their individual tax or financial advisers.*