

Understanding Clergy Taxes

or

Why are clergy taxes so confusing?

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THE EPISCOPAL CHURCH FOUNDATION (ECF) HAS RECEIVED A GRANT AS PART OF LILLY ENDOWMENT'S NATIONAL INITIATIVE TO ADDRESS THE ECONOMIC CHALLENGES FACING PASTORAL LEADERS. ECF'S GRANT ENTITLED "FROM ECONOMIC CHALLENGES TO TRANSFORMATIONAL OPPORTUNITIES" WILL PROVIDE LAY AND CLERGY LEADERS OF THE EPISCOPAL CHURCH WITH RESOURCES, TOOLS AND OTHER SUPPORT TO HELP ADDRESS THE FINANCIAL AND LEADERSHIP CHALLENGES OF CONGREGATIONAL MINISTRY IN THE 21ST CENTURY. THIS WEBINAR WAS MADE POSSIBLE BY THE LILLY ENDOWMENT GRANT. FOR MORE INFORMATION ON ECF'S LILLY ENDOWMENT INITIATIVE GO TO WWW.EPISCOPALFOUNDATION.ORG

The Two Headed Monster !



**Federal Income
Tax System**



**Social Security
Tax System**

Federal Income Tax System

Clergy are considered employees for Federal Income tax purposes

Social Security Tax System

Clergy are considered self employed (SE) for Social Security and Medicare tax purposes

Questions



Income to Include in W-2

- Salary, not including housing
- Bonuses
- Christmas and Special Occasion Offerings
- Retirement Gifts
- Social Security Tax Paid by the Church to the Cleric
- Non-Accountable Reimbursements
- Group Term Life Insurance more than \$50,000
- Sabbatical funds if not for reimbursable business expenses
- Moving Expenses paid or reimbursed

Items not Included in Wages for Income Tax Purposes

- Value of a Rectory and/or Housing Allowance
- Employer-Paid Medical Insurance Premiums
- Group Term Life Insurance less than \$50,000
- Lodging for interim assignments less than 1 year
- Contributions to a 403(b)



Contributions to a 403(b)

- **Excluded** for federal tax calculation
- **Excluded** for Self-Employment tax calculation
- Limits for 2019
 - \$19,000 for employee
 - \$6,000 catch-up provision if over the age of 50
 - \$56,000 limit for employee plus employer contributions (\$61,000 of over age 50)

Questions



Federal Income Tax System

Clergy are considered employees for Federal Income tax purposes

Social Security Tax System

Clergy are considered self employed (SE) for Social Security and Medicare tax purposes

Taxable Income for Social Security Tax

- Income reported as wages on the W-2
- Add Housing
- Deduct Unreimbursed Business Expense



Changes to Deduction of Unreimbursed Business Expenses



- No longer Deductible as Miscellaneous Itemized Deduction for federal income taxes
- Deductible for Self-Employment Tax

Questions





Housing Allowance Exclusion

Ministers Who Own or Rent Their Home

Amount Excluded for Federal Income Tax is the lower of:

1. The designated amount
2. Actual housing expenses
3. The fair rental value of the home, furnished, plus utilities

1. The Designated Amount

- The Amount – as requested by the cleric
 - reported on form W-2 in box 14 “Other”
- The Designation – by resolution
- In Advance – before payment and/or the beginning of a new year

A housing allowance is only effective forward, not retroactively

Sample Housing Allowance Resolution

Whereas, the Reverend Susan Smith is compensated by Christ Church exclusively for the services as a minister of the gospel, and

Whereas, Christ Church does not provide Rev. Smith with a rectory,

Therefore, it is hereby resolved, that the total compensation paid to Rev. Smith for calendar year 2019 shall be \$65,000 of which \$15,000 is hereby designated to be housing allowance, and it is further

Resolved, that the designation of \$15,000 as a housing allowance shall apply to calendar year 2019 and all future years unless otherwise provided.

2. Actual Housing Expenses

- Mortgage payments, both principal and interest
- Real estate taxes and special assessments
- Maintenance and upkeep of property including landscaping
- Fees paid for acquiring home titles, mortgages, etc.
- Improvements and repairs
- Costs of moving your home furnishings
- Utilities – electric, gas, oil, water, basic telephone, trash, cable television base rate (not including premium channels)
- Home furnishings which are primary and essential
- Fire and home liability insurance premiums
- Rent payments for home, garage, storage for household items, furnishings, etc.

3. Fair Rental Value Test

- Determining Fair Rental Value of Home
 - No Guidance from IRS
 - Suggested Ways -Opinion from Realtor, Appraisal, Zillow
- Furniture
 - Two ways to value
 - The fair rental of a furnished home.
 - The fair rental value of a home without furnishings plus the fair rental value of rented furniture.
- Utilities
 - Gas, electric, water, sewer
 - Basic cable, internet, phone

Ministers in Church-Provided Housing

- Church-Provided Housing (the Fair Rental Value of the Home)
 - Included for Self-Employment Tax
 - Cleric determines value
 - Not reported on W-2
- Utilities Provided by Church
 - Included for Self-Employment Tax
 - Church provides cleric with the amount
 - Not reported on W-2



Ministers in Church-Provided Housing

- Rectory Allowance (the Fair Rental Value of the Furnishings)
 - Included for Self-Employment Tax
 - Designated from salary
 - Subject to the 3-part test for exclusion from Federal Income Tax
 - Reported on W-2, box 14
- Utilities Allowance (for Utilities paid for by the cleric)
 - Included for Self-Employment Tax
 - Designated from salary
 - Subject to the 3-part test for exclusion from Federal Income Tax
 - Reported on W-2, box 14

Sample Rectory Allowance Resolution

Whereas, the Reverend John Smith is compensated by Grace Church exclusively for the services as a minister of the gospel; and

Whereas, Grace Church provides Rev. Smith with rent-free use of a church-owned rectory as compensation for services rendered to the church in the exercise of ministry; and

Whereas, Rev. Smith incurs expenses for living in church provided housing; therefore, it is hereby

Resolved, that the annual compensation paid to Rev. Smith for the calendar year 2019 shall be \$50,000 of which \$5,000 is hereby designated to be a housing allowance pursuant to Section 107 of the Internal Revenue Code; and it is further

Resolved, that the designation of \$5,000 as a housing allowance shall apply to calendar year 2019 and all future years unless otherwise provided by this governing board; and it is further

Resolved, that as additional compensation to Rev. Smith for calendar year 2019 and for all future years unless otherwise provided, Rev. Smith shall be permitted to live in the church-owned parsonage located at 123 Main Street, and that no rent or other fee shall be payable by Rev. Smith for such occupancy and use.

Questions



SPECIAL SITUATIONS

Sabbatical Leave

- Compensation is Taxable
- Expenses May be Deductible
- Grants



Hiring an Interim

- No difference from regular cleric for tax purposes
 - Housing allowance or rectory subject to SE tax but excluded from federal income tax
 - Must pay SE tax
 - Withholding is voluntary
- Interim contract for one year or less
 - Housing is a business expense whether provided or reimbursed
 - Travel from home to location is reimbursable
 - SE tax on wages only

Hiring a Retired Cleric

- Subject to same clergy tax rules
- Pension designated as housing allowance, so may not need to declare a housing allowance from salary
- Compensation is subject to SE tax, regardless of age
- Compensation may be limited by Pension Fund rules

Questions



Resources

Clergy Tax Line –

Nancy Fritschner 877-305-1414
Bill Geisler 877-305-1415
Dolly Rios 833-363-5751 (English
and Spanish)

- *Federal Reporting Requirements for Episcopal Churches*
 - *The Clergy Tax Preparation Guide*
- These publications are available at cpg.org*
- *Social Security and Other Information for Members of the Clergy and Other Religious Workers*

IRS publication 517





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