PREPARING TAX RETURNS FOR CLERGY

Federal, state, and other reporting made easy.

by Dan Busby
Michael Martin
John Van Drunen
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John oversees the compliance process for ECFA including renewals, applications, compliance concerns, and site visits, in addition to serving as in-house general counsel.

John was extensively involved in the work of the Commission on Accountability and Policy for Religious Organizations and the Religious Organizations Accounting Committee.

Recent Developments ................................................................. 3
Key Federal Tax Limits, Rates, and Other Data ....................... 6
Introduction to Clergy Compensation
  The Tax System for Clergy ............................................................. 7
The Four Key Elements of Clergy Compensation
  The Housing Allowance .............................................................. 11
  Compensation and Fringe Benefits ............................................. 18
  Business and Professional Expenses ......................................... 24
  Income and Social Security Taxes ............................................. 30
Completing the Form 1040
  Form 1040 – Line by Line ......................................................... 32
Sample Income Tax Returns
  Example No. 1: Clergy-Employee for Income Tax Purposes
    (Accountable Plan) ................................................................. 36
  Example No. 2: Clergy-Employee for Income Tax Purposes
    (Nonaccountable Plan) ........................................................... 46
2016 Filing Dates ........................................................................ 64
Citations ..................................................................................... 65
Index .......................................................................................... 66
Appreciation — The authors express their sincere appreciation to Mr. Michael Batts, CPA and managing shareholder, Batts Morrison Wales & Lee, P.A., Orlando, FL, and the staff of the firm for their valued assistance in reviewing the two sample tax returns included in this guide.

This publication is designed to provide accurate and authoritative information regarding the subject matter covered. The text has been significantly excerpted from the Zondervan Minister’s Tax & Financial Guide, 2016 edition. It is distributed with the understanding that neither the publisher nor the authors are engaged in rendering legal, accounting, or other professional services. If legal advice or other expert assistance is required, the services of a competent professional person should be sought.

Every effort has been made to make the materials in this text current as of the date of publication. Federal tax law, however, is subject to change. Congress can modify the law as it has on numerous occasions over the years. Also, court decisions and IRS rulings can significantly affect the application of federal tax laws. Such changes may affect the accuracy of this publication.

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Clergy continue to be faced with a plethora of tax and finance developments. A summary of some of the more significant developments follow (see the “In the News” link at ECFA.org for current updates on these issues and much more):

Health care reform. The Patient Protection and Affordable Care Act (ACA), passed by Congress in 2010, overhauled the nation’s health care industry and has brought with it numerous changes to the tax code. The following is a summary of major ACA provisions directly impacting clergy:

- **Individual responsibility provision ("individual mandate").** As of January 1, 2014, most ministers were required to maintain “minimum essential” health care coverage as defined by the law or be subject to a penalty tax known as the individual shared responsibility payment. For 2016, this penalty is the greater of (1) a flat rate of $695 per adult and $347.50 per child (up to $2,085 for a family), or (2) 2.5% of household income, whichever is greater. The penalty is calculated based on the number of months in the year that the taxpayer is without the required coverage, and a taxpayer will not be penalized for a single gap in coverage less than three months. Individual shared responsibility payments are made along with the filing of federal income tax returns. Most ministers can avoid these penalties by obtaining health care coverage through their employer’s plan or purchasing “Bronze” level coverage through a government exchange (or equivalent coverage through a private insurer).

- **Health FSAs limits.** Health FSAs have traditionally been subject to a “use-or-lose” rule, under which employees must forfeit any remaining FSA amounts that are not used up during the plan year. Additionally, beginning in 2013, health FSAs became subject to a $2,500 annual limit indexed for inflation under changes brought by health care reform ($2,550 limit for 2015 and 2016). Employers sponsoring health FSAs have the option of amending their written plans to allow employees to carry over up to $500 of unused amounts remaining at the end of a plan year to the immediately following plan year, subject to certain limitations. The carryover does not otherwise affect the annual limit on FSAs.

Church payments or reimbursements of employee healthcare-related expenses. By now, most smaller churches across America are probably aware they are exempt from the employer mandate of the Affordable Care Act (ACA) because they have fewer than 50 full-time equivalent employees (FTEs).¹ That’s the good news.

The bad news: Without even knowing it, many churches may be subjecting themselves to penalties of up to $100 per employee, per day, per violation for making voluntary healthcare payments on behalf of employees (i.e., for individual policy premiums or for other out-of-pocket medical costs) that do not comply with ACA market reforms. These onerous penalties became effective for health plan years beginning on or after January 1, 2014, so care must be taken now to understand and follow the existing guidance.

- **Background.** For decades, it has been the common practice of many smaller churches and ministries that are unable to offer group health insurance coverage to assist employees with the cost of their individual health insurance coverage and/or other out-of-pocket medical expenses. Employers would pay these costs directly on behalf of employees or provide employees with reimbursements after incurring the expenses. If certain formalities were followed, generally these arrangements were blessed by the IRS and even allowed on a tax-free basis for employees.

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¹ Or less than 100 FTEs through 2015.
That all changed recently as the result of the issuance of certain guidance relating to the ACA market reforms. When the ACA guidance was initially issued related to reimbursements, it was clear that the tax-free reimbursement of individual healthcare insurance premiums would trigger an excise tax of $100 per employee, per day, per violation. However, many people interpreted the initial guidance as permitting the employer to avoid ACA excise tax problems if they reimbursed the individual healthcare insurance premiums on a post-tax basis.

A year later, the government issued additional guidance clarifying (changing its position) that an employer is not permitted to reimburse individual healthcare insurance premiums on either a pre- or post-tax basis. That means employers who adjusted their practices to align with the initial guidance by paying after-tax reimbursements should discontinue these payments or reimbursements on either a pre- or post-tax basis to avoid excise tax liability.

- **Excise tax liability.** Smaller churches are most likely to be impacted by these penalties. This is because churches with 100 or more full-time equivalent employees (FTEs) are subject to the ACA mandate to provide qualified group coverage to employees beginning with their 2015 health plan year. Similarly, churches with 50 or more FTEs who qualify for the employer mandate transition relief for 2015 must provide group health coverage beginning in 2016.

For more information, see the *5 Roads for Healthcare Reimbursement by Churches and Ministries* on the ECFA website.

- **Note on limited transition relief in 2015.** In February 2015, the IRS issued Notice 2015-17 providing limited transition relief to certain smaller employers from the ACA market reform excise tax penalties until June 30, 2015. The transition relief only applied to organizations with fewer than 50 FTEs. While payments or reimbursements for the cost of employees’ individual health insurance policy premiums were entitled to relief, other forms of noncompliant healthcare payments or reimbursements (e.g., out-of-pocket medical expense reimbursements under a stand-alone health reimbursement arrangement (HRA)) were still subject to excise tax penalties. Organizations that qualified for the transition relief rules in IRS Notice 2015-17 need not file Form 8928 to self-report violations for noncompliant payments or reimbursements made in 2014 or for the first half of 2015 (through June 30, 2015).

<table>
<thead>
<tr>
<th>Description of Payment/Reimbursement Arrangement:</th>
<th>Penalties waived until 6/30/15?</th>
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<tr>
<td>Employer with 50 or more FTEs</td>
<td>No</td>
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<tr>
<td>Employer with fewer than 50 FTEs that paid/reimbursed the cost of individual health insurance policy premiums for employees</td>
<td>Yes</td>
</tr>
<tr>
<td>Employer with fewer than 50 FTEs that paid/reimbursed health care expenses other than individual health insurance policy premiums</td>
<td>No</td>
</tr>
</tbody>
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2 IRS Notice 2013-54 published on September 13, 2013.
3 “FAQs about Affordable Care Act Implementation (Part XXII)” prepared jointly by the Departments of Labor (DOL), Health and Human Services (HHS), and the Treasury published on November 6, 2014.
Department of Labor’s proposed overtime regulations. The U.S. Department of Labor’s (DOL) proposed changes to its overtime regulations that could significantly impact employers across the country including thousands of churches.

Perhaps the most significant aspect of the proposed rules is the increase of the salary threshold for exempt workers from $23,660 to $50,440 per year (which equals the 40th percentile of wages for full-time salaried workers). This means that exemption from overtime rules would require salaried workers to earn at least $50,440, in addition to meeting one of the existing white collar duties tests (executive, administrative, professional, outside sales, and certain computer employers). This threshold would be adjusted annually, based on either a fixed percentile of wages or the consumer price index (the DOL has invited comment on which adjustment method would be the most appropriate). The salary threshold for exemption of highly compensated employees also increased, from $100,000 to $122,148.

According to church law expert Richard Hammar, the official position of the Department of Labor appears to be that “clergy are not subject to the minimum wage and overtime pay requirements of the FLSA no matter how little they earn.” Additionally, based on federal court precedent, the “ministerial exception” doctrine may bar application of the overtime rules to the employment relationship between churches and their ministers. Based on this analysis, these changes to the overtime rules have the greatest potential to impact the budgets of churches with non-ministerial employees who work more than 40 hours per week and are compensated below the new annual threshold of $50,440.

The DOL will prepare a final version of the regulations and determine an effective date—expected to be mid-2016. In the meantime, churches should contact their legal counsel for advice on how to prepare for the potential impact of these rules on their organizations.

Court challenge to clergy housing exclusion. The U.S. Court of Appeals for the Seventh Circuit issued an important decision in Freedom From Religion Foundation v. Lew, concluding that the federal tax code provision that treats church-provided housing allowances to ministers as income tax-free must stand.

In doing so, the appeals court overturned a previous decision by a lower district court in favor of the atheist group, Freedom From Religion Foundation (FFRF). The district court had found that the exclusion is an unconstitutional benefit in favor of religious groups.

Before the Seventh Circuit could even analyze the constitutionality of the law, it first decided it had to dismiss the case on the procedural ground of standing. The court determined that FFRF and its leaders were not proper parties to challenge the law in federal court because they had not suffered any concrete, personal injury—a critical element to establish standing.

It is unclear whether FFRF will mount another challenge on this issue.

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### Key Federal Tax Limits, Rates, and Other Data

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<thead>
<tr>
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<tbody>
<tr>
<td>Standard Deductions</td>
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<tr>
<td>Married-Joint Return</td>
<td>$12,400</td>
<td>$12,600</td>
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<tr>
<td>Head of Household</td>
<td>$9,100</td>
<td>$9,250</td>
<td>$9,300</td>
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<tr>
<td>Single</td>
<td>$6,200</td>
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<td>Married-Separate Returns</td>
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<tr>
<td>Personal &amp; dependent exemption amount</td>
<td>$3,950</td>
<td>$4,000</td>
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<tr>
<td>Foreign earned income exclusion</td>
<td>$99,200</td>
<td>$100,800</td>
<td>$101,300</td>
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<tr>
<td>Social security:</td>
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</tr>
<tr>
<td>SECA (OASDI &amp; Medicare) rate</td>
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<td></td>
</tr>
<tr>
<td>$175,000 married-joint, $250,000 all others</td>
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<tr>
<td>OASDI maximum compensation base</td>
<td>$117,000</td>
<td>$118,500</td>
<td>$118,500</td>
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<tr>
<td>Social security cost of living benefit increase</td>
<td>$1,500</td>
<td>$1,700</td>
<td>$0</td>
</tr>
<tr>
<td>Social security Full Retirement Age (FRA)</td>
<td>66 years</td>
<td>66 years</td>
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<tr>
<td>Medicare Part B Premiums - Basic</td>
<td>$104.90</td>
<td>$104.90</td>
<td>$104.90</td>
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<tr>
<td>Earnings ceiling for social security (for employment before FRA: special formula in FRA year)</td>
<td>Below FRA: $15,480</td>
<td>Below FRA: $15,720</td>
<td>Below FRA: $15,720</td>
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<tr>
<td>Earnings limit in year FRA attained</td>
<td>$41,400</td>
<td>$41,880</td>
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<td>Benefits and contributions:</td>
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<tr>
<td>Maximum annual contribution to defined contribution plan</td>
<td>$52,000</td>
<td>$53,000</td>
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<tr>
<td>Maximum salary deduction for 401(k)/403(b)</td>
<td>$17,500</td>
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<tr>
<td>401(k) &amp; 403(b) over 50 &quot;catch up&quot; limit</td>
<td>$5,500</td>
<td>$6,000</td>
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<tr>
<td>Maximum income exclusion for nonqualified plans in 501(c)(3) organizations (IRC 457)</td>
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<tr>
<td>IRA contribution limit -- age 49 and below</td>
<td>$5,500</td>
<td>$5,500</td>
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<tr>
<td>-- age 50 and above</td>
<td>$6,500</td>
<td>$6,500</td>
<td>$6,500</td>
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<tr>
<td>Highly compensated employee limit</td>
<td>$115,000</td>
<td>$120,000</td>
<td>$120,000</td>
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<tr>
<td>Maximum annual contribution to health flexible spending arrangements</td>
<td>$2,500</td>
<td>$2,550</td>
<td>$2,550</td>
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<tr>
<td>Per diem and mileage rates and other transportation:</td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Standard per diem: Lowest rates</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>in continental USA</td>
<td>$83</td>
<td>$83</td>
<td>$83</td>
</tr>
<tr>
<td>Meals &amp; Incidentsals</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Business auto mileage rate</td>
<td>$0.64 per mile</td>
<td>$0.57 per mile</td>
<td>$0.54 per mile</td>
</tr>
<tr>
<td>Moving &amp; medical auto mileage rate</td>
<td>$23.5¢ per mile</td>
<td>$23¢ per mile</td>
<td>$19¢ per mile</td>
</tr>
<tr>
<td>Charitable auto mileage rate</td>
<td>$14¢ per mile</td>
<td>$14¢ per mile</td>
<td>$14¢ per mile</td>
</tr>
<tr>
<td>Airplane mileage rate (1)</td>
<td>$1.31 per mile</td>
<td>$1.29 per mile</td>
<td></td>
</tr>
<tr>
<td>Motorcycle mileage rate (1)</td>
<td>$0.3¢ per mile</td>
<td>$0.54 per mile</td>
<td></td>
</tr>
<tr>
<td>Bicycle commuting rate</td>
<td>$20 per month</td>
<td>$20 per month</td>
<td></td>
</tr>
<tr>
<td>Maximum value of reimbursement of business expenses (other than lodging) without receipt</td>
<td>$75</td>
<td>$75</td>
<td>$75</td>
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<tr>
<td>Luxury automobile value (limit on use of cents-per-mile valuation of company automobile)</td>
<td>$16,000</td>
<td>$16,000</td>
<td></td>
</tr>
<tr>
<td>Monthly limit on free parking</td>
<td>$250</td>
<td>$250</td>
<td>$255</td>
</tr>
<tr>
<td>Transit passes/token -- monthly tax-free limit</td>
<td>$250</td>
<td>$250</td>
<td>$255</td>
</tr>
<tr>
<td>Other:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gift tax annual exclusion</td>
<td>$14,000</td>
<td>$14,000</td>
<td>$14,000</td>
</tr>
</tbody>
</table>

(1) Privately owned vehicle mileage rates set by the U.S. General Services Administration

Note: In some instances, the rate for a particular year may apply to a tax return filed in a subsequent year.
The Tax System for Clergy

Get the Big Picture

Six special tax provisions are available only to individuals who qualify as clergy under federal tax rules and who perform services that qualify in the exercise of ministry under federal tax rules.

Special Tax Provisions for Clergy

1. Exclusion of the housing allowance for income tax purposes and the fair rental value of a congregation-owned parsonage provided rent free to clergy.
2. Exemption of clergy from self-employment social security tax under very limited circumstances.
3. For social security tax purposes, treatment of clergy as self-employed as it relates to income from ministerial services.
4. Exemption of clergy compensation from mandatory income tax withholding.
5. Eligibility for a voluntary income tax withholding arrangement between clergy-employees and the congregation.
6. Potential “double deduction” of mortgage interest and real estate taxes as itemized deductions and as excludable housing expenses for housing allowance purposes for clergy living in clergy-provided housing.

Clergy Serving Local Congregations

You may believe you are classified as clergy, your congregation may consider you as clergy, your denomination may classify you as clergy, but what does the IRS consider you? For tax purposes, the opinion of the IRS is the one that counts.

Determining whether you are classified as clergy for tax purposes is very important. It determines how you prepare your tax return for income and social security tax purposes. Qualified clergy are eligible for the housing allowance. This alone can exclude thousands of dollars from income taxation. Clergy calculate self-employment social security tax on Schedule SE and pay the tax with Form 1040. Nonclergy have one-half of their social security tax (FICA) withheld from salary, and the congregation pays the other half.

How can I tell whether the IRS will treat me as clergy?

If you are employed by a congregation and are ordained, commissioned, or licensed and meet the following four tests, the IRS will generally consider you clergy. You

- administer the sacraments,
- are considered to be a religious leader by your church,
- conduct worship services, and

Remember

The major tax benefit for most clergy is the special housing allowance treatment.

Remember

There is some flexibility in applying certain clergy tax provisions. For example, clergy are exempt from mandatory income tax withholding but can enter into a voluntary income tax withholding arrangement. However, if clergy qualify for the housing allowance, self-employment social security tax (using Schedule SE) applies, not FICA—this is not optional.

Caution

Determination of clergy status is far from a precise matter. Only a review of all the pertinent facts and circumstances for particular clergy will assist in determining whether an individual will qualify for clergy tax status.
have management responsibility in the control, conduct, or maintenance of your congregation.

Based on guidelines issued by the IRS, some of the four tests, but not necessarily all, must be met in determining clergy status. This flexible approach is beneficial to many clergy because some positions relating to music, education, youth, or administration will not meet all four tests.

There is no requirement that you must be qualified to perform and actually perform every sacrament. If you are qualified to perform certain sacraments and actually perform or could perform some of the sacraments on occasion, you will generally meet this test. A similar test applies to conducting religious worship and providing management services. If you currently conduct religious worship and provide management services, have done it in the past, or could do it in the future, the test will generally be met.

Job titles have little significance for tax purposes. A licensed, commissioned, or ordained clergy may have a job title that implies a ministry function. However, the actual responsibilities of the position will determine if the four-factor test (see page 7) is met. Clergy performing services of a routine nature, such as those performed by secretaries, clerks, and janitors, generally do not qualify as clergy for tax purposes.

Because of the inconsistency of these rulings, clergy serving in a local congregation who do not clearly meet all four factors should review these matters with a qualified professional adviser before filing income tax returns.

- Clergy in Denominational, Administrative, and Teaching Positions

Ordained, commissioned, or licensed clergy not serving local churches may qualify as “clergy” for federal tax purposes in the following situations:

- Administration of religious denominations and their integral agencies, including teaching or administration in parochial schools, colleges, or universities that are under the authority of a denomination.

- Performing services for a parachurch organization based upon an assignment or designation by a congregation.

If a congregation does not assign or designate your services, you will qualify for the special tax treatments of clergy if your services substantially involve performing sacerdotal functions or conducting religious worship.

- Social Security Status of Clergy

Clergy engaged in the exercise of ministry are always treated as self-employed for social security tax purposes. Clergy pay social security...
under the Self-Employment Contributions Act (SECA) instead of the Federal Insurance Contributions Act (FICA). It is possible to become exempt from SECA only if you meet strict exemption requirements. The request for exemption must be filed using Form 4361 within a specified time from the beginning of your ministry. The request for exemption must be approved by the IRS (see page 31).

Your earnings that are not from the exercise of ministry are generally subject to social security tax under FICA or SECA as applied to all workers.

**Income Tax Status of Clergy**

Are clergy employees or self-employed (independent contractors) for income tax purposes? The IRS considers virtually all clergy to be employees for income tax purposes. The income tax filing status has many ramifications for what and how congregations and clergy report to the IRS.

The IRS often applies a common-law test to decide whether clergy are employees or self-employed for income tax purposes. Generally, you are an employee if your employer has the legal right to control both what you do and how you do it, even if you have considerable discretion and freedom of action. However, clergy who are employees of congregation for income tax purposes may also be self-employed for income tax purposes with respect to certain services (baptisms, marriages, and funerals).

Determining if you are an employee or self-employed for income tax purposes will determine several other tax-related issues:

- Clergy-employees must be given Form W-2 and report their compensation on page 1 of Form 1040. They are eligible to claim unreimbursed business expenses and expenses reimbursed under a nonaccountable plan on Schedule A (non-accountable plan reimbursements must be included in compensation on Form W-2). If you itemize deductions, business and professional expenses are deductible only to the extent that such expenses exceed 2% of adjusted gross income (AGI). Deductible business meals and entertainment expenses are limited to 50%.

- Accident, long-term care insurance, and qualified group health insurance premiums paid directly by a congregation or reimbursed by a congregation, after the cleric provides substantiation, are not reportable as income to the clergy-employee but must be reported as taxable income to the self-employed cleric.

Clergy-employees may deduct health, accident, and long-term care insurance premiums paid personally, and not reimbursed by the congregation, on Schedule A as a medical and dental expense, subject to a 10% limitation of adjusted gross income.
The impact of a minister being considered self-employed for income tax purposes is generally very significant even if only health insurance is considered. Reporting these premiums as taxable (minister-employee) versus tax-free (self-employed minister for income purposes) can impact the minister’s tax bill by thousands of dollars. If health insurance premiums are included in taxable income, a low-income minister might also have his or her earned income tax credit reduced or eliminated.

- Health savings accounts, health reimbursement arrangements, or flexible spending accounts are only available to clergy who are employees for income tax purposes.

- Group-term life insurance of $50,000 or less provided by a congregation is tax-free to clergy-employees but represents taxable income for self-employed clergy.

- A voluntary arrangement to withhold income tax may be used by clergy-employees but may not be used by the self-employed.

### Recommended Filing Status

Virtually all clergy serving local congregations qualify as employees for income tax purposes. It is wise to file as an employee for income tax purposes, unless you can clearly demonstrate that you qualify for self-employed status. Few clergy can substantiate filing as self-employed for income tax purposes.

Even though clergy may take exception to the reporting of the congregation, the congregation has a responsibility under the law to determine the proper filing method and to proceed accordingly.

### Evangelists and Missionaries

The qualifications of itinerant evangelists for the special clergy tax provisions are generally the same as for clergy serving local congregations.

Most evangelists are self-employed both for income tax and self-employment social security tax purposes. The only exception is the evangelist who has formed a corporation and is an employee of the corporation. In this instance, the evangelist is an employee for income tax purposes, but remains self-employed for social security tax purposes.

Missionaries are also subject to the same rules to qualify for clergy status for tax purposes. Qualifying for benefits such as a housing allowance is often not so important for clergy-missionaries because of the foreign earned income exclusion. However, the question of clergy tax status is vitally important to determine if clergy are subject to social security as employees or as self-employed persons. The foreign-earned income exclusion affects income tax but not social security tax.
Nearly all clergy should have a portion of salary designated as a housing allowance. Maximizing housing benefits requires careful planning. For clergy living in congregation-owned housing, a housing allowance that covers expenses such as furnishings, personal property insurance on contents, utilities, and so on could save several hundred dollars of income taxes annually. A properly designated housing allowance may be worth thousands of dollars in tax savings for clergy living in their own homes or rented quarters. For clergy without a housing allowance, every dollar of compensation is taxable for federal income tax purposes.

The housing allowance provides an opportunity to exclude dollars from gross income. The designated housing allowance should be subtracted from compensation before the congregation completes the data on Form W-2. The housing allowance designation is not entered on Form 1040 or related schedules, except Schedule SE, since it is not a deduction for income tax purposes. However, any unused portion of the housing designation must be reported as income on page 1, Form 1040.

If your congregation properly designates a portion of your cash salary for expenses of a home you provide, the exclusion is commonly referred to as a housing allowance. If the congregation properly designates a portion of your cash salary for expenses you incur in relation to congregation-provided housing, the exclusion is often called a parsonage allowance. In either instance, it is an exclusion from income tax, not self-employment tax.

Clergy are eligible to exclude the fair rental value of congregation-provided housing for income tax purposes without any official action by the congregation. However, a cash housing allowance related to congregation-provided or clergy-provided housing is only excludable under the following rules:

➤ The allowance must be officially designated by the congregation. The designation should be stated in writing, preferably by resolution of the top governing body, in an employment contract, or—at a minimum—in the congregation budget and payroll records. If the only reference to the housing allowance is in the congregation budget, the budget should be formally approved by the top governing body of the congregation.

Tax law does not specifically say an oral designation of the housing allowance is unacceptable. In certain instances, the IRS has accepted an oral housing designation. Still, the use of a written designation is preferable and highly recommended. The lack of a written designation significantly weakens the defense for the housing exclusion upon audit.

➤ The housing allowance must be designated prospectively by the congregation. Cash housing allowance payments made prior to a designation of the housing allowance are fully taxable for income tax purposes. Carefully word the resolution so that it will remain in effect until a subsequent resolution is adopted (see the examples on page 15).

➤ Only actual expenses can be excluded from income. The source of the funds used to pay clergy housing expenses must be compensation earned by clergy in the exercise of ministry in the current year.

➤ Only an annual comparison by clergy of housing expenses to the housing allowance is required. For example, if the housing allowance designation is stated in terms of a weekly or monthly amount, only a comparison of actual housing expenses to the annualized housing allowance is required.
The housing allowance exclusion cannot exceed the fair rental value of the housing, plus utilities.

**Types of Housing Arrangements**

**Clergy Living in a Parsonage Owned by or Rented by a Congregation**

If you live in a congregation-owned parsonage or housing rented by the congregation, the fair rental value of the housing is not reported for income tax purposes. The fair rental value is subject only to self-employment tax.

You may request a housing allowance to cover expenses incurred in maintaining the congregation-owned or rented housing. Examples of allowable expenses are utilities, repairs, furnishings, and appliances. If the actual expenses exceed the housing allowance designated by the congregation, the excess amount cannot be excluded from income.

It is appropriate for clergy’s out-of-pocket expenses for the maintenance of a congregation-owned parsonage to be reimbursed by the congregation if a full accounting is made. Such reimbursements do not relate to a housing allowance. If such expenses are not reimbursed, they could be excludable from income under a housing allowance.

If the congregation owns the parsonage, the congregation may wish to provide an equity allowance to help compensate clergy for equity not accumulated through home ownership. An equity allowance is taxable both for income and social security tax purposes, unless directed to a 403(b) tax-sheltered annuity or certain other retirement programs.

**Clergy Owning or Renting Own Home**

If you own or rent your own home, you may exclude, for income tax purposes, a cash housing allowance that is the lowest of (1) reasonable compensation, (2) the amount used to provide a home from current congregational income, (3) the amount prospectively and officially designated, or (4) the fair rental value of the furnished home, plus utilities.

Many clergy make the mistake of automatically excluding from income, for income tax purposes, the total designated housing allowance, even though the fair rental value of the furnished home or actual housing expenses are less than the designation. This practice may cause a significant underpayment of income taxes.

**Example:** A cleric lives in a personally owned home. The congregation prospectively designated $28,000 of the salary as housing allowance. The cleric spends $27,000 for housing-related items. The fair rental value of the home is $29,000. Since the amount spent is lower than the designated housing allowance or the fair rental value, the excludable housing is $27,000. Therefore, $1,000 ($28,000 less $27,000) must be added to taxable income on Form 1040, page 1, line 7. Unless the cleric has opted out of social security, the entire $28,000 is reportable for social security purposes on Schedule SE.
Designating the Housing Allowance

The following steps are often followed in designating and excluding the housing allowance:

1. Clergy estimates the housing-related expenses to be spent in the coming year and presents this information to the congregation.

2. The congregation then adopts a written housing allowance designation based on the estimate.

3. At the close of the tax year, the cleric who provides his or her own housing compares the amount designated for housing, the housing expenses substantiated, and the fair rental value of the home including furnishings and utilities. The lower of these amounts is excluded for income tax purposes. Clergy living in congregation-provided housing must compare the amount designated and actual housing expenses and exclude the lower of the two amounts.

Designation Limits

The IRS does not place a limit on how much of clergy compensation may be designated as a housing allowance by the employing congregation. But practical and reasonable limits usually apply.

Unless the amount is justified based on anticipated expenses and is within the fair rental value limit, it is generally inadvisable for the congregation to exclude 100% of compensation.

It is often best for the congregation to overdesignate your parsonage allowance by a reasonable amount, subject to the fair rental value test, to allow for unexpected expenses and increases in utility costs. Any excess housing allowance designated should be shown as income on line 7 of Form 1040.

Reporting the Housing Allowance to Clergy

The designated housing allowance may be reflected for clergy-employees on Form W-2 in Box 14 with the notation, “Housing Allowance.” Though not required, this reporting method is suggested by Publication 517. Or, congregations can report the designated housing allowance to clergy by providing a statement separate from Form W-2. This may be in a memo or letter. The statement should not be attached to your income tax returns.

Your congregation may erroneously include the housing allowance on Form W-2, Box 1. If this happens, the congregation should prepare a corrected Form W-2.

Accounting for the Housing Allowance

Determining Fair Rental Value

The determination of the fair rental value of congregation-provided housing for self-employment social security purposes is solely the responsibility of clergy. The congregation is not responsible to set the value. The fair rental value should be based on comparable rental values of other similar residences in the immediate neighborhood or community, comparably furnished.

One of the best methods to use in establishing fair rental value of your housing is to request a local realtor to estimate the value in writing. Place the estimate in your tax file and annually adjust the value for inflation and other local real estate valuation factors.
Housing Allowance in Excess of Actual Expenses or Fair Rental Value

Some clergy erroneously believe that they may exclude every dollar of the housing designation adopted by the congregation without limitation. The housing designation is merely the starting point. If reasonable compensation, actual expenses, or the fair rental value is lower, the lowest amount is eligible for exclusion from income.

Example: A cleric living in a personally owned home receives cash compensation of $60,000 from the congregation. The congregation prospectively designates $20,000 as a housing allowance. The fair rental value is $21,000. Actual housing expenses for the year are $14,000. The amount excludable from income is limited to the actual housing expenses of $14,000.

Actual Expenses in Excess of the Designated Housing Allowance or Fair Rental Value

Actual housing expenses that exceed the designated housing allowance are not excludable from income. There are no provisions to carry over “unused” housing expenses to the next year.

Example: A cleric living in a personally owned home receives cash compensation of $60,000 from the congregation. The congregation prospectively designates $20,000 of the $60,000 as a housing allowance. Actual housing expenses for the year are $50,000. The fair rental value is $21,000. The expenses were unusually high because of a down payment on that house. The amount excludable from income is the designated housing allowance of $20,000. There is no carryover of the $30,000 of actual expenses in excess of the designated housing allowance to the next tax year.

Housing Allowances for Retired Clergy

Pension payments, retirement allowances, or disability payments paid to retired clergy from an established plan are generally taxable as pension income. However, denominations often designate a housing allowance for retired clergy to compensate them for past services to local congregations of the denomination or in denominational administrative positions. The housing allowance designated relates only to payments from the denominationally sponsored retirement program.

Withdrawals from a denominationally sponsored 403(b), also called a tax-sheltered annuity (TSA), or 401(k) plan qualify for designation as a housing allowance. Withdrawals from a 403(b) or 401(k) plan not sponsored by a local congregation are not eligible for designation as a housing allowance. Retired clergy may also exclude the rental value of a home furnished by a congregation or a rental allowance paid by a congregation as compensation for past services.

If a denomination or organization reports the gross amount of pension or TSA payments on Form 1099-R and designates the housing allowance, the clergy may offset the housing expenses and reflect the net amount on page 1, Form 1040. A supplementary schedule such as the following example should be attached to the tax return:

- Pensions and annuity income (Form 1040, line 16a) $10,000
- Less housing exclusion $8,000
- Form 1040, line 16b $2,000
For retired clergy, the amount excluded for income tax purposes is limited to the lowest of (1) the amount used to provide a home, (2) the properly designated housing allowance, or (3) the fair rental value of the furnished home, plus utilities.

## Housing Allowance Resolutions

### Parsonage owned by or rented by a congregation

Whereas, the Internal Revenue Code permits clergy to exclude from gross income “the rental value of a home furnished as part of compensation” or a congregation-designated allowance paid as a part of compensation to the extent that actual expenses are paid from the allowance to maintain a parsonage owned or rented by the congregation;

Whereas, the congregation compensates (insert name) for services in the exercise of ministry; and

Whereas, the congregation provides (insert name) with rent-free use of a parsonage owned by (rented by) the congregation as a portion of the compensation for services rendered to the congregation in the exercise of ministry;

Resolved, That the compensation of (insert name) is $4,500 per month, of which $2,000 per month is a designated housing allowance; and

Resolved, That the designation of $2,000 per month as a housing allowance shall apply until otherwise provided.

### Home owned or rented by clergy

Whereas, the Internal Revenue Code permits clergy to exclude from gross income a church-designated allowance paid as part of compensation to the extent used for actual expenses in owning or renting a home; and

Whereas, the congregation compensates (insert name) for services in the exercise of ministry;

Resolved, That the compensation of (insert name) is $4,500 per month, of which $2,000 per month is a designated housing allowance; and

Resolved, That the designation of $2,000 per month as a housing allowance shall apply until otherwise provided.

### Evangelists

Whereas, the Internal Revenue Code permits clergy to exclude from gross income a congregation-designated allowance paid as part of compensation to the extent used in owning or renting a permanent home; and

Whereas, the congregation compensates (insert name) for services in the exercise of ministry as an evangelist;

Resolved, That the honorarium paid to (insert name) shall be $1,512, consisting of $312 for travel expenses (with documentation provided to the congregation), $500 for housing allowance, and a $700 honorarium.
Housing Allowance Worksheet
Clergy Living in Housing
Owned or Rented by the Congregation

Name: _________________________________________________________________________________

For the period ___________________, 20___ to __________________, 20___

Date designation approved _______________________, 20___

Allowable Housing Expenses (expenses paid from current income)

<table>
<thead>
<tr>
<th>Estimated Expenses</th>
<th>Actual</th>
</tr>
</thead>
<tbody>
<tr>
<td>Utilities (gas, electricity, water) and trash collection</td>
<td>$ _________</td>
</tr>
<tr>
<td>Local telephone expense (base charge)</td>
<td>_________</td>
</tr>
<tr>
<td>Decoration and redecoration</td>
<td>_________</td>
</tr>
<tr>
<td>Structural maintenance and repair</td>
<td>_________</td>
</tr>
<tr>
<td>Landscaping, gardening, and pest control</td>
<td>_________</td>
</tr>
<tr>
<td>Furnishings (purchase, repair, replacement)</td>
<td>_________</td>
</tr>
<tr>
<td>Personal property insurance on minister-owned contents</td>
<td>_________</td>
</tr>
<tr>
<td>Personal property taxes on contents</td>
<td>_________</td>
</tr>
<tr>
<td>Umbrella liability insurance</td>
<td>_________</td>
</tr>
</tbody>
</table>

Subtotal

$ _________  

10% allowance for unexpected expenses

$ _________

TOTAL $ _________  $ _________  (A)

Properly designated housing allowance $ _________  (B)

The amount excludable from income for federal income tax purposes is the lower of A or B.
### Housing Allowance Worksheet

**Clergy-Owned Housing**

Name: ________________________________________________________________________________

For the period __________________, 20___ to ___________________, 20___

Date designation approved _______________________, 20___

### Allowable Housing Expenses (expenses paid from current income)

<table>
<thead>
<tr>
<th>Estimated Expenses</th>
<th>Actual</th>
</tr>
</thead>
<tbody>
<tr>
<td>Down payment on purchase of housing</td>
<td>$ ________</td>
</tr>
<tr>
<td>Housing loan principal and interest payments (1)</td>
<td>________</td>
</tr>
<tr>
<td>Real estate commission, escrow fees</td>
<td>________</td>
</tr>
<tr>
<td>Real property taxes</td>
<td>________</td>
</tr>
<tr>
<td>Personal property taxes on contents</td>
<td>________</td>
</tr>
<tr>
<td>Homeowner’s insurance</td>
<td>________</td>
</tr>
<tr>
<td>Personal property insurance on contents</td>
<td>________</td>
</tr>
<tr>
<td>Umbrella liability insurance</td>
<td>________</td>
</tr>
<tr>
<td>Structural maintenance and repair</td>
<td>________</td>
</tr>
<tr>
<td>Landscaping, gardening, and pest control</td>
<td>________</td>
</tr>
<tr>
<td>Furnishings (purchase, repair, replacement)</td>
<td>________</td>
</tr>
<tr>
<td>Decoration and redecoration</td>
<td>________</td>
</tr>
<tr>
<td>Utilities (gas, electricity, water) and trash collection</td>
<td>________</td>
</tr>
<tr>
<td>Local telephone expense (base charge)</td>
<td>________</td>
</tr>
<tr>
<td>Homeowner’s association dues/condominium fees</td>
<td>________</td>
</tr>
</tbody>
</table>

**Subtotal**

_______

10% allowance for unexpected expenses

_______

**TOTAL**  

$ ________ $ ________ (A)

Properly designated housing allowance

$ ________ (B)

Fair rental value of home, including furnishings, plus utilities

$ ________ (C)

(1) Loan payments on home equity loans or second mortgages are includible only to the extent the loan proceeds were used for housing expenses.

The amount excludable from income for federal income tax purposes is the lowest of A, B, or C.
More Than Meets the Eye

Ask most clergy how much they are paid and the response will often be “My check from the church is $1,000 a week.” But that tells us very little. Not only is your salary subject to tax, but so are many fringe benefits that you may receive.

What are fringe benefits? A fringe benefit is any cash, property, or service that clergy receive from the congregation in addition to salary. The term “fringe benefits” is really a misnomer because clergy have come to depend on them as a part of the total compensation package. All fringe benefits are taxable income to clergy unless specifically exempted by the Internal Revenue Code.

Many fringe benefits can be provided by a congregation to a clergy without any dollar limitation (qualified health insurance is an example), while other fringe benefits are subject to annual limits (dependent care is an example). A brief discussion of some of the key fringe benefits follows.

- **Tax Treatment of Compensation Elements**

  - **Business and professional expenses reimbursed with adequate accounting.** If the congregation reimburses clergy under an *accountable* plan for employment-related professional or business expenses (for example, auto, other travel, subscriptions, and entertainment), the reimbursement is not taxable compensation and is not reported to the IRS by the congregation or clergy. Per diem reimbursements up to IRS-approved limits also qualify as excludable reimbursements.

  - **Business and professional expense payments without adequate accounting.** Many churches pay periodic allowances or reimbursements to ministers for business expenses with no requirement to account adequately for the expenses. These payments do not meet the requirements of an accountable expense reimbursement plan.

    Allowances or reimbursements under a *nonaccountable* plan must be included in a minister’s taxable income. For an employee, the expenses related to a nonaccountable reimbursement plan are deductible only if the minister itemizes expenses on Schedule A. Even then, the business expenses, combined with other miscellaneous deductions, must exceed 2% of adjusted gross income.

    A portion of unreimbursed expenses are subject to disallowance when they relate to a housing allowance according to the IRS.

  - **Club dues and memberships.** Dues for professional organizations (such as ministerial associations) or public service organizations (such as Kiwanis, Rotary, and Lions clubs) are generally deductible or reimbursable. Other club dues are generally not deductible or reimbursable (including any club organized for business, pleasure, recreation, or other social purposes). If the church pays the health, fitness, or athletic facility dues for a minister, the amounts paid are generally fully includible in the minister’s income as additional compensation.

  - **Disability insurance.** If the congregation pays the disability insurance premiums (and the cleric is named as the beneficiary) as a part of the compensation package, the premiums are excluded from income. However, any disability policy proceeds must be included in gross income. This is based on who paid the premiums for the policy covering the year when the disability started. If the premiums are shared between the congregation and clergy, then the benefits are taxable in the same proportion as the payment of the premiums.

Statistics suggest that clergy are seven times more likely to need disability insurance than life insurance before age 65. When a congregation provides the maximum disability insurance as a tax-free benefit, it could reduce the awkwardness of clergy transition relating to disability while serving the congregation.
Conversely, if you pay the disability insurance premiums or have the congregation withhold the premiums from your salary, you receive no current deduction and any disability benefits paid under the policy are not taxable to you.

A third option is for the congregation to pay the disability premiums. But instead of treating the premiums as tax-free, the congregation treats the premiums as additional clergy compensation. Benefits you receive under this option are tax-free.

- **Educational reimbursement plans.** If your congregation requires you to take educational courses or you take job-related courses, and your congregation either pays the expenses directly to the educational organization or reimburses you for the expenses after you make a full accounting, you may not have to include in income the amount paid by your church.

While there are no specific dollar limits on educational expenses paid under a nonqualified reimbursement plan, the general ordinary and necessary business expense rules do apply. These types of payments may be discriminatory.

Though the education may lead to a degree, expenses may be deductible or reimbursable if the education

- is required by your church to keep your salary, status, or job (and serves a business purpose of your church), or
- maintains or improves skills required in your present employment.

Even though the above requirements are met, expenses do not qualify if the education is

- required to meet the minimum educational requirements of your present work, or
- part of a program of study that will qualify you for a new occupation.

- **Entertainment expenses.** Clergy may deduct ministry-related entertainment expenses. Entertainment expenses must be directly related to or associated with the work of the congregation. Entertainment expenses are not deductible if they are lavish or extravagant.

If business meal and entertainment expenses are not reimbursed under an accountable plan, only 50% of the expenses are deductible. If the congregation reimburses the expenses, a 100% reimbursement may be made.

- **Flexible spending account (FSA).** “Cafeteria” or FSAs are plans used to reimburse the employee for certain personal expenses. They are provided by employers to pre-fund dependent care, medical, or dental expenses (often called a healthcare flexible spending account) in pre-tax dollars.

A cafeteria or flexible spending plan cannot discriminate in favor of highly compensated participants for contributions, benefits, or eligibility to participate in the plan. While only larger congregations generally offer cafeteria plans because of plan complexity and cost, many congregations could feasibly offer an FSA.

There is a $2,550 per person per year FSA contribution limit indexed for inflation for 2015 and 2016. The money is the account holder’s to use during the plan year. Ultimately the
employer owns the account and any unused balance at the end of the plan year or any administrative grace period is forfeited to the employer.

An administrative grace period may be adopted as a way to provide relief without running afoul of the prohibition on deferred compensation. Under this provision, employees are permitted a grace period of 2 1/2 months immediately following the end of the plan year. Expenses for qualified benefits incurred during the grace period may be paid or reimbursed from benefits or contributions remaining unused at the end of the plan year.

**Health insurance.** If the church pays a minister-employee’s qualified group health insurance premiums directly to the insurance carrier, the premiums are tax-free to the minister. However, if similar payments are made for a minister whom the church considers to be self-employed for income tax purposes, the payments represent additional taxable income.

Under health care reform, churches generally cannot discriminate in favor of more highly paid individuals when providing group health care coverage.

**Health reimbursement arrangement (HRA).** A properly designed, written HRA under which the church pays the medical expenses of the minister, spouse, and dependents may be non-taxable to the minister-employee.

HRAs must be integrated with the church’s group health insurance plan and only be funded by church-provided funds. Funding by a salary reduction election is not permitted. Excess money in a church-funded HRA can be carried over to a future year without any tax implications to the minister. Because benefits can be carried over indefinitely, the only danger of losing the balance in an HRA account is at retirement or other separation of employment.

Typical expenses covered by such a plan are deductibles, coinsurance, and noncovered amounts paid by the individual.

HRAs may not discriminate in favor of highly compensated employees with regard to either benefits or eligibility. HRAs are only available to employees.

**Health savings account (HSA).** HSAs are individual, portable, tax-free, interest-bearing accounts (typically held by a bank or insurance company) through which individuals with a high-deductible health plan (HDHP) save for medical expenses. The purpose of an HSA is to pay what basic coverage would ordinarily pay.

Within limits, HSA contributions made by employers are excludable from income tax and social security wages and do not affect the computation of the earned income credit. HSA contributions may not be funded through salary reduction. Earnings on amounts in an HSA are not currently taxable, and HSA distributions used to pay for medical expenses are not taxable.

HSAs can be funded up to $3,350 for individuals and $6,650 for families to cover health care costs (2015 limits). In addition to the maximum contribution amount, catch-up contributions may be made by or on behalf of individuals age 55 or older and younger than 65. Individuals who have reached age 55 by the end of the tax year are allowed to increase their annual contribution limit by $1,000.
Funding of an HSA by the employer may fluctuate from one month to the next. This is unlike a cafeteria or flexible spending account, under which changes in contributions are generally only available on each January 1.

Only employees who are enrolled in qualifying high-deductible plans may participate in an HSA. A HDHP has at least $1,300 annual deductible for self-only coverage and $2,600 deductible for family coverage (2015 limits). Additionally, annual out-of-pocket expenses for HSAs must be limited to $6,450 for self-covered and $12,900 (2015 limits) for families. A state high-risk health insurance plan (high-risk pool) qualifies as an HDHP if it does not pay benefits below the minimum annual deductible under the HSA rules.

HSA withdrawals do not qualify to cover over-the-counter medications (other than insulin or doctor-prescribed medicine). Additionally, the excise tax for nonqualified HSA withdrawals (withdrawals not used for qualified medical expenses) increased from 10 to 20%.

- **Life insurance/group-term.** If the group life coverage provided under a nondiscriminatory plan does not exceed $50,000 for clergy, the life insurance premiums are generally tax-free to clergy-employees. Group-term life insurance coverage of more than $50,000 provided to clergy by the congregation is taxable under somewhat favorable IRS tables.

- **Social security tax reimbursement.** Congregations commonly reimburse clergy for a portion or all of their self-employment social security (SECA) tax liability. Any social security reimbursement must be reported as taxable income.

Because of the deductibility of the self-employment tax in both the income tax and self-employment tax computations, a full reimbursement is effectively less than the gross 15.3% rate (the payroll tax “holiday” is ignored for this example):

<table>
<thead>
<tr>
<th>Your Marginal Tax Rate</th>
<th>Effective SECA Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>0%</td>
<td>14.13%</td>
</tr>
<tr>
<td>10</td>
<td>13.42</td>
</tr>
<tr>
<td>15</td>
<td>13.07</td>
</tr>
<tr>
<td>27</td>
<td>12.22</td>
</tr>
<tr>
<td>30</td>
<td>12.01</td>
</tr>
</tbody>
</table>

- **Tuition and fee discounts.** If you are an employee of a church-operated elementary, secondary, or undergraduate institution, certain tuition and fee discounts provided to a minister, spouse, or dependent children are generally tax-free. The discounts must be nondiscriminatory and relate to an educational program.

If you are employed by the church and not by the church-related or church-operated private school, any tuition and fee discounts that you receive are taxable income.

- **Vehicles/personal use of congregation-owned vehicle.** The personal use of a congregation-provided vehicle is considered a taxable fringe benefit. The fair market value of the personal use must be included in clergy gross income, unless the full value is reimbursed to the congregation.

---

**Caution**

An allowance to cover the minister’s self-employment social security tax provides absolutely no tax benefit since the amount is fully taxable. However, paying at least one-half of the minister’s social security tax is important so this amount can be properly shown as a fringe benefit for compensation analysis purposes.
<table>
<thead>
<tr>
<th>Explanation</th>
<th>Minister-Employee</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bonus or gift from the congregation</td>
<td>Taxable income/Form W-2</td>
</tr>
<tr>
<td>Business and professional expenses reimbursed with adequate accounting</td>
<td>Tax-free/excluded</td>
</tr>
<tr>
<td>Business and professional expense payments without adequate accounting</td>
<td>Deduction on Schedule A, Miscellaneous Deductions. Subject to 2% of AGI and 50% meals and entertainment limits</td>
</tr>
<tr>
<td>Club dues paid by the congregation</td>
<td>Taxable income/Form W-2 (exception for dues for civic and public service groups)</td>
</tr>
<tr>
<td>Compensation reported to clergy by the congregation</td>
<td>Form W-2</td>
</tr>
<tr>
<td>Dependent care assistance payments</td>
<td>Tax-free, subject to limitations</td>
</tr>
<tr>
<td>Earned income tax credit (EITC)</td>
<td>May be eligible for EITC</td>
</tr>
<tr>
<td>Educational assistance programs</td>
<td>May be eligible to exclude up to $5,250 of qualified assistance</td>
</tr>
<tr>
<td>401(k) plan</td>
<td>Eligible for 401(k)</td>
</tr>
<tr>
<td>403(b) tax-sheltered annuity</td>
<td>Eligible for 403(b)</td>
</tr>
<tr>
<td>Gifts/personal (not handled through the congregation)</td>
<td>Tax-free/excluded</td>
</tr>
<tr>
<td>Health reimbursement arrangement</td>
<td>Tax-free, if plan is properly established</td>
</tr>
<tr>
<td>Health Savings Account</td>
<td>Tax-free, if plan is properly established</td>
</tr>
<tr>
<td>Healthcare flexible spending account</td>
<td>Tax-free, if plan is properly established</td>
</tr>
<tr>
<td>Housing allowance</td>
<td>Taxable income/Form W-2, may be deducted on Form 1040, Line 25</td>
</tr>
<tr>
<td>IRA payments by congregation</td>
<td>Premiums are tax-free, but proceeds are taxable</td>
</tr>
<tr>
<td>Insurance, disability paid by congregation; clergy – beneficiary</td>
<td>Proceeds are tax-free</td>
</tr>
<tr>
<td>Insurance, group-term life paid by congregation</td>
<td>First 50,000 of coverage is tax-free, if plan properly established</td>
</tr>
</tbody>
</table>

* Many of these compensation elements are conditioned on plans being properly established and subject to annual limits.
<table>
<thead>
<tr>
<th><strong>Explanation</strong></th>
<th><strong>Minister-Employee</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>Insurance, health</td>
<td>Tax-free, if directly paid by congregation or reimbursed to clergy upon substantiation. If paid by clergy and not reimbursed by congregation, deduct on Schedule A</td>
</tr>
<tr>
<td>Insurance, life, whole or universal, congregation is beneficiary</td>
<td>Tax-free/excluded</td>
</tr>
<tr>
<td>Insurance, life, whole or universal, clergy designates beneficiary</td>
<td>Taxable income/Form W-2</td>
</tr>
<tr>
<td>Insurance, long-term care</td>
<td>Tax-free if directly paid by the congregation or reimbursed to clergy on substantiation. If paid by clergy and not reimbursed by congregation, deduct on Schedule A subject to limitations</td>
</tr>
<tr>
<td>Loans, certain low-interest or interest-free loans over $10,000 to clergy</td>
<td>Imputed (the difference between the IRS-established interest rate and the rate charged) interest is taxable income/Form W-2</td>
</tr>
<tr>
<td>Moving expenses paid by the congregation (only applies to certain qualified expenses)</td>
<td>Tax-free if directly paid by the congregation or reimbursed to clergy on substantiation. Reported on Form W-2, Box 12, using Code P</td>
</tr>
<tr>
<td>Pension payments by the congregation to a denominational plan for clergy</td>
<td>Tax-deferred. No reporting required until the funds are withdrawn by clergy or pension benefits are paid</td>
</tr>
<tr>
<td>Per diem payments for meals, lodging, and incidental expenses</td>
<td>May be used for travel away from home under an accountable reimbursement plan</td>
</tr>
<tr>
<td>Professional income (weddings, funerals)</td>
<td>Taxable income/Schedule C (C-EZ)</td>
</tr>
<tr>
<td>Property transferred to clergy at no cost or less than fair market value</td>
<td>Taxable income/Form W-2</td>
</tr>
<tr>
<td>Retirement or farewell gift to clergy from congregation</td>
<td>Taxable income/Form W-2</td>
</tr>
<tr>
<td>Salary from congregation</td>
<td>Report salary on page 1, Form 1040</td>
</tr>
<tr>
<td>Social security reimbursed by congregation to clergy</td>
<td>Taxable income/Form W-2</td>
</tr>
<tr>
<td>Travel paid for cleric’s spouse by the congregation</td>
<td>May be tax-free if there is a business purpose</td>
</tr>
<tr>
<td>Tuition and fee discounts</td>
<td>May be tax-free in certain situations</td>
</tr>
<tr>
<td>Value of home provided to clergy</td>
<td>Tax-free/excluded</td>
</tr>
<tr>
<td>Vehicles/personal use of congregation-owned auto</td>
<td>Taxable income/Form W-2</td>
</tr>
<tr>
<td>Voluntary withholding</td>
<td>Eligible for voluntary withholding agreement</td>
</tr>
</tbody>
</table>
Most clergy spend several thousands of dollars each year on congregation-related business expenses. For example, the ministry-related portion of auto expenses is often a major cost.

Business and professional expenses fall into three basic categories: expenses reimbursed under an accountable plan, expenses paid under a nonaccountable plan, and unreimbursed expenses. The last two categories are treated the same for tax purposes. You will almost always save tax dollars if your expenses are reimbursed.

The reimbursement of an expense never changes the character of the item from personal to business. Business expenses are business whether or not they are reimbursed. Personal expenses are always nondeductible and nonreimbursable. If a personal expense is inadvertently reimbursed by the congregation, clergy should immediately refund the money to the congregation.

To be deductible or reimbursable, a business expense must be both ordinary and necessary. An ordinary expense is one that is common and accepted in your field. A necessary expense is one that is helpful and appropriate for your field. An expense does not have to be indispensable to be considered necessary.

**Accountable and Nonaccountable Expense Reimbursement Plans**

An accountable plan is a reimbursement or expense allowance arrangement established by your congregation that requires (1) a business purpose for the expenses, (2) substantiation of the expenses to the congregation, and (3) the return of any excess reimbursements.

The substantiation of expenses and return of excess reimbursements must be handled within a reasonable time. The following methods meet the "reasonable time" definition:

- The fixed date method applies if:
  - an advance is made within 30 days of when an expense is paid or incurred;
  - an expense is substantiated to the congregation within 60 days after the expense is paid or incurred; and
  - any excess amount is returned to the congregation within 120 days after the expense is paid or incurred.

- The periodic statement method applies if:
  - the congregation provides employees with a periodic statement that sets forth the amount paid that is more than substantiated expenses under the arrangement;
  - the statements are provided at least quarterly;
  - the congregation requests that clergy provide substantiation for any additional expenses that have not yet been substantiated and/or return any amounts remaining unsubstantiated within 120 days of the statement.

If you substantiate your business expenses to the congregation and any unused payments are returned, expense reimbursements have no impact on your taxes. The expenses reimbursed are not included on Form W-2 or deducted on your tax return.
The IRS disallows deductions for a portion of unreimbursed business expenses on the premise that the expenses can be allocated to your tax-exempt housing allowance (see page 29). This is another reason that all clergy should comply with the accountable expense reimbursement rules. The goal should be to eliminate all unreimbursed business expenses.

**Nonaccountable Expense Reimbursement Plans**

If you do not substantiate your business expenses to the congregation, or if the amount of the reimbursement exceeds your actual expenses and the excess is not returned to the congregation within a reasonable period, your tax life becomes more complicated. Nonaccountable reimbursements and excess reimbursements over IRS mileage or per diem limits must be included in your gross income and reported as wages on Form W-2.

Unreimbursed expenses or expenses reimbursed under a nonaccountable plan can be deducted only as itemized miscellaneous deductions and only to the extent that they, with your other miscellaneous deductions, exceed 2% of your adjusted gross income. Unreimbursed expenses are not deductible if you are an employee for income tax purposes and do not itemize.

If your congregation pays you an “allowance” for business expenses, it represents taxable compensation. The term “allowance” implies that the payment is not based upon documented expenses, does not meet the adequate accounting requirements for an accountable plan, and must be included in your income.

**Documenting Business Expenses**

For expenses to be allowed as deductions, you must show that you spent the money and that you spent it for a legitimate business reason. To prove that you spent the money, you generally need to provide documentary evidence that can be confirmed by a third party. Canceled checks, credit card, or other receipts are an excellent starting point. To the IRS, third-party verification is important; if business expenses are paid in cash, be sure to get a receipt.

Documenting a business expense can be time-consuming. The IRS is satisfied if you note the five Ws on the back of your credit card slip or other receipt:

- **Why** (business purpose)
- **What** (description, including itemized accounting of cost)
- **When** (date)
- **Where** (location)
- **Who** (names of those for whom the expense was incurred; e.g., meals and entertainment)

The only exception to the documentation rules is if your individual outlays for business expenses, other than for lodging, come to less than $75. The IRS does not require receipts for such expenses, although the five Ws are still required. You always need a receipt for lodging expenses regardless of the amount. A congregation may apply a documentation threshold lower than $75.
**Auto Expense Deductions**

Clergy’s car expenses are deductible or reimbursable to the extent they are for business (or income producing) rather than personal use. Generally, only those expenses that are necessary to drive and maintain a car that is used to go from one workplace to another are deductible.

**Mileage and Actual Expense Methods**

In determining your deduction for the business use of a personal car, you can use one of two methods to figure your deduction: the standard mileage rate or the actual expense method. Generally, you can choose the method that gives you the greater deduction.

**Standard Mileage Rate Method**

If your congregation pays you a fixed mileage rate up to the IRS standard rate (see page 6 for rates) and you provide the congregation with the time, place, and business purpose of your driving, you have made an adequate accounting of your automobile expenses.

If the congregation does not reimburse you for auto expenses or reimburses you under a nonaccountable plan, you may deduct business miles on Form 2106 (2106-EZ). The total from Form 2106 (2106-EZ) is carried to Schedule A, Miscellaneous Deductions.

The standard mileage rate, which includes depreciation and maintenance costs, is based on the government’s estimate of the average cost of operating an automobile. Depending upon the make, age, and cost of the car, the mileage rate may be more or less than your actual auto expense. If you use the mileage rate, you also may deduct parking fees and tolls and the business portion of personal property tax. All auto-related taxes must be claimed on Schedule A for employees.

**Actual Expense Method**

If you keep accurate records, determining your deduction for most expenses should be straightforward. Generally, the amount of depreciation you may claim and the method you use to calculate it depend on when you purchased your auto and began to use it for ministerial purposes.

Under the actual expense method, you can use either accelerated depreciation or straight-line depreciation. As the names imply, the accelerated method front-loads the depreciation, giving you larger deductions sooner. The straight-line method gives you the same depreciation deduction every year.

Allowable expenses under the actual expense method include: gas and oil, interest on an auto loan, repairs, lease payments, tires, automobile club membership, batteries, car washes and waxes, insurance, license plates, parking fees and tolls, and supplies, such as antifreeze.

**Commuting**

Personal mileage is never deductible. Commuting expenses are non-deductible personal expenses.
Unless your home-office qualifies as a home-office under tax law, travel from home to the worship center (a regular work location) and return for worship services and other work at the worship center is commuting and is not deductible or reimbursable. The same rule applies to multiple trips made in the same day. The cost of traveling between your home and a temporary work location is generally deductible or reimbursable. Once you arrive at the first work location, temporary or regular, you may deduct trips between work locations.

A regular place of business is any location at which you work or perform services on a regular basis. These services may be performed every week, for example, or merely on a set schedule.

A temporary place of business is any location at which you perform services on an irregular or short-term (i.e., generally a matter of days or weeks) basis.

**Documentation of Auto Expense**

To support your automobile expense deduction or reimbursement, automobile expenses must be substantiated by adequate records. A weekly or monthly mileage log that identifies dates, destinations, business purposes, and odometer readings in order to allocate total mileage between business and personal use is a basic necessity if you use the mileage method. If you use the actual expense method, a mileage log and supporting documentation on expenses is required.

**Per diem allowance**

The IRS provides per diem allowances under which the amount of away-from-home meals and lodging expenses may be substantiated. These rates may not be used to claim deductions for unreimbursed expenses and may not be used to reimburse volunteers. Higher per diem rates apply to certain locations annually identified by the IRS. For more information on these rules, see IRS Publication 1542.

**Other Business and Professional Expenses**

**Business Gifts**

You can deduct up to $25 per donee for business gifts to any number of individuals every year. Incidental costs, such as for engraving, gift wrapping, insurance, and mailing do not need to be included in determining whether the $25 limit has been exceeded.

The gifts must be related to your ministry. Gifts to congregation staff or board members would generally be deductible, subject to the $25 limit. Wedding and graduation gifts generally do not qualify as business expenses.

**Entertainment**

Meal and entertainment expenses are deductible or reimbursable if they are ordinary and necessary and are either directly related to or associated with your ministerial responsibilities.

**Personal Computers**

Personal computers you own and use more than 50% for ministry may be depreciated (or reimbursed) as five-year recovery property or deducted (but not reimbursed). The business portion of
depreciation may be reimbursed under an accountable expense reimbursement plan if the 50% business “convenience of the congregation” and “condition of employment” tests are met.

If a computer is provided by the congregation in the congregation office but you prefer to work at home on your personal computer, it is not being used for the congregation’s convenience. If you meet the “convenience of the congregation” and “condition of employment” tests but do not use your computer (and related equipment) more than 50% of the time for your work, you must depreciate these items using the straight-line method and you cannot take the Section 179 write-off. If you qualify under the home-office rules, the 50% test does not apply to you.

Adequate records of the business use of your computer should be maintained to substantiate your deductions.

Subscriptions and Books

Subscriptions to clergy-related periodicals are deductible. If the information in a news magazine relates to your ministerial preparation, that periodical may qualify for a deduction.

The cost of books related to your ministry with a useful life of one year or less may be deducted. The cost of books with a useful life of more than one year may be depreciated over the useful life.

Telephone

You may not deduct, as a business expense, any of the basic local service charges (including taxes) for the first telephone line into your home. Ministry-related long distance calls, a second line, special equipment, and services used for business are deductible. If you are out of town on a business trip, the IRS generally will not challenge a reasonable number of calls home. Although your basic local telephone service (including taxes) for the first telephone line into your home is not deductible for tax purposes, it is includible as housing expense for housing allowance purposes.

Telephone/Cellular

The IRS treats the value of a church-provided cell phone, and similar telecommunications equipment, (including the value of any personal use by the employee) as excludible from the employee’s income, as long as the cell phone is provided to the employee primarily for a noncompensatory business reason (such as the employer’s need to contact the employee at all times for work-related emergencies). Providing a cell phone to promote morale or goodwill, to attract a prospective employee, or to furnish additional compensation to an employee is evidence that there is no noncompensatory business reason.

Church staff may be reimbursed for the business use of a cell phone but the church should probably require the employee to submit a copy of the monthly bill and evidence that the bill has been paid.

If a church does not have a substantial noncompensatory business reason for providing a cell phone to an employee, or reimbursing the employee for business use of his or her personal cell phone, the value of the use of the phone, or the amount of the reimbursement is

Warning

If clergy purchase a computer and use it primarily for congregation work and meet the “condition” and “convenience” tests, only the depreciation on the business portion of the computer can be reimbursed by the congregation, not the entire cost of the business portion, based on the Section 179 first-year write-off rules.

Remember

If a church provides a cell phone to an employee primarily for a noncompensatory business reason, the value of the cell phone is excludible from the employee’s income.
includible in gross income, reportable on Forms 941 and W-2, and for lay employees is subject to federal and state employment tax withholding.

● Allocation of Business Expenses

If you receive a rental or parsonage allowance that is tax-free, you must allocate the expenses of operating your ministry (this is commonly referred to as the “Deason Rule”). You cannot deduct expenses that are allocable to your tax-free rental or parsonage allowance. This rule does not apply to your deductions for home mortgage interest or real estate taxes. See examples on pages 43 and 61.

This limitation requires the following calculation:

1. Amount of tax-exempt income (the fair rental value of a congregation-provided parsonage and the housing allowance excluded from gross income; this may be less than the congregation-designated housing allowance) $____________

2. Total income from ministry:

   Salary (including the fair rental value of a congregation-provided parsonage and the housing allowance excluded from gross income) $ ______________
   Fees $ ______________
   Allowances (nonaccountable plan) $ ______________

3. Divide line 1 amount by line 2 amount = % of nontaxable income. ___________%

4. Total unreimbursed business and professional expenses, less 50% of meals and entertainment expenses. $____________

5. Multiply line 4 total by line 3 percentage (these are non-deductible expenses allocable to tax-exempt income). $____________

6. Subtract line 5 amount from line 4 amount (these are deductible expenses for federal income tax purposes on Form 2106 [2106-EZ] or Schedule C [C-EZ]). $____________
The federal income tax is a pay-as-you-go tax. You must pay the tax as you earn or receive income during the year. Employees usually have income tax withheld from their pay. However, the pay of qualified clergy is not subject to federal income tax withholding. Clergy who are employees for income tax purposes may enter into a voluntary withholding agreement with the congregation to cover any income tax and self-employment social security tax that are due. IRS Publication 505 provides additional information on tax withholding and estimated taxes.

**Tax Withholding**

Congregations are not required to withhold income taxes from wages paid to clergy for services performed in the exercise of their ministry. The exemption does not apply to nonministerial congregation employees such as a secretary, organist, or custodian.

Clergy-employees may have a voluntary withholding agreement with the employing congregation to cover income taxes (the amount may be set high enough to also cover the self-employment social security tax liability). Clergy need only file Form W-4 with the congregation to establish a voluntary withholding arrangement.

**Estimated Tax**

Estimated tax is the method used to pay income and self-employment taxes for income that is not subject to withholding. Your estimated tax is your expected tax for the year minus your expected withholding and credits.

If you are filing a declaration of estimated tax, complete the quarterly Forms 1040-ES. If 2015 estimated taxes are $1,000 or less, no declaration of estimated tax is required.

If your estimated tax payments for 2016 equal 90% of the 2015 tax liability, you will generally avoid underpayment penalties. An option is to make the 2016 estimated tax payments equal 100% of your 2015 federal and social security taxes (Form 1040, page 2, line 61). This method generally avoids underpayment penalties and is easier to calculate.

In estimating 2016 taxes, net earnings from self-employment should be reduced by 7.65% before calculating the self-employment tax of 15.3%. There also is an income tax deduction for one-half of your self-employment tax (Form 1040, page 1, line 27).

You pay one-fourth of your total estimated taxes in installments as follows:

<table>
<thead>
<tr>
<th>For the Period</th>
<th>Due Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>Jan. 1 - Mar. 31</td>
<td>April 15</td>
</tr>
<tr>
<td>April 1 - May 31</td>
<td>June 15</td>
</tr>
<tr>
<td>June 1 - Aug. 31</td>
<td>September 15</td>
</tr>
<tr>
<td>Sept. 1 - Dec. 31</td>
<td>January 15</td>
</tr>
</tbody>
</table>
Social Security Taxes

Social security taxes are collected under two systems. Under the Federal Insurance Contributions Act (FICA), the employer pays one-half of the tax and the employee pays the other half. Under the Self-Employment Contributions Act (SECA), the self-employed person pays all the tax (self-employment tax) as calculated on the taxpayer’s Schedule SE.

Compensation received by clergy for services performed in the exercise of ministry is self-employment income and is always subject to self-employment tax (SECA). Ministerial income is exempt from SECA only if you have opted out of social security. Federal Insurance Contributions Act (FICA) social security tax should never be withheld from the compensation of qualified clergy.

● Opting Out of Social Security Taxes

All clergy are automatically covered by social security (SECA) for services in the exercise of ministry, unless an exemption has been received based on the filing with and approval by the IRS of Form 4361. You must certify that you oppose, either conscientiously or because of religious principles, the acceptance of any public insurance (with respect to services performed as clergy), including social security coverage. This includes an opposition to insurance that helps pay for or provides services for medical care (such as Medicare) and social security benefits. Your opinion of the financial stability of the social security program is not a valid basis to file for exemption.

Deadline for Filing for an Exemption

The application for exemption from self-employment tax must be filed by the date your tax return is due, including extensions, for the second year in which you had net ministerial income of $400 or more. These do not have to be consecutive tax years.

● Computing the Self-Employment Tax

The following tax rates apply to net earnings from self-employment of $400 or more each year:

<table>
<thead>
<tr>
<th>Year</th>
<th>OASDI</th>
<th>Medicare</th>
<th>Maximum Earnings Base</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>OASDI</td>
<td>Medicare</td>
<td></td>
</tr>
<tr>
<td>2014</td>
<td>12.4%</td>
<td>2.9%</td>
<td>$117,000</td>
</tr>
<tr>
<td>2015</td>
<td>12.4%</td>
<td>2.9%</td>
<td>118,500</td>
</tr>
<tr>
<td>2016</td>
<td>12.4%</td>
<td>2.9%</td>
<td>118,500</td>
</tr>
</tbody>
</table>

OASDI = Old-age, survivors, and disability insurance, or social security

● Self-Employment Tax Deductions

You can take an income tax deduction equal to one-half of your self-employment tax liability. The deduction is claimed against gross income on line 27 of Form 1040, page 1. You may also deduct a portion of your self-employment tax liability in calculating your self-employment tax. This deduction is made on Schedule SE, Section A, line 4 or Section B, line 4a, by multiplying self-employment income by .9235. The purpose of these deductions is to equalize the social security (and income) taxes paid by (and for) employees and self-employed persons with equivalent income.
**Line by Line**

**Form 1040**

There are two short forms, the 51-line 1040A and the super-short, 14-line 1040EZ. Generally, ministers should use the 79-line Form 1040 instead. It accommodates every minister, and there’s no penalty for leaving some of the lines blank. Besides, going down the 1040 line by line may jog your memory about money you received or spent in 2015. (Line numbers noted refer to the 1040 and related schedules.)

- **Filing status (lines 1 to 5). Line 2:** If your spouse died in 2015, you can still file jointly and take advantage of tax rates that would be lower than if you file as a single person or as a head of household.

  **Line 3:** If you’re married and live in a separate-property state, compute your tax two ways—jointly and separately. Then, file the return resulting in the lower tax.

  **Line 4:** If you’re single, you may qualify as head of household if you provided a home for someone else—like your parent. Filing as head of household rather than as a single person can save you a bundle on taxes.

  **Line 5:** If your spouse died in 2013 or 2014 and you have a dependent child, you can also benefit from joint-return rates as a qualifying widow(er).

- **Exemptions (lines 6a to 6d).** Remember to include a social security number for any dependent who was at least one year old on December 31, 2015. If your child does not have one, obtain Form SS-5, Application for a Social Security Number, at http://www.ssa.gov/online/ssa-5.html. If you are unable to secure the social security number before the filing deadline, file for an extension of time to file.

- **Income (lines 7 to 22). Line 7:** If your employer considered you an employee for income tax purposes, you should receive Form W-2 from the employer. The total amount of your taxable wages is shown in Box 1 of Form W-2; attach Copy B of your W-2 to your Form 1040. Include the data from other W-2s you or your spouse received on this line. If the employer erroneously included your housing allowance in Box 1, Form W-2, ask the congregation to reissue a corrected Form W-2.

  If your cash housing allowance designated and paid by the employer exceeds the lowest of (1) reasonable compensation, (2) the amount used to provide a home from current ministerial income, (3) the amount properly designated by the employer, or (4) the fair rental value of the home including utilities and furnishings, enter the difference on line 7.

  **Line 8a:** Include as taxable-interest income the total amount of what you earned on savings accounts, certificates of deposit, credit union accounts, corporate bonds and corporate bond mutual funds, U.S. treasuries and U.S. government mutual funds, and interest paid to you for a belated federal or state tax refund (whether or not you have received a Form 1099-INT). If you haven’t yet received any of the statements due you, call

**Filing Tip**

**Form 1040, Line 7.** All compensation from Forms W-2 is reported on line 7. Be sure your congregation has not included the housing allowance amount in Box 1 of Form W-2.

**Filing Tip**

**Form 1040, Line 7.** If the housing allowance designated by the employer exceeds the housing allowance exclusion to which you are entitled, you must include the difference on line 7 with a description “Excess housing allowance.” Your exclusion is limited by the lower of the fair rental value of a minister-provided home or your actual housing expenses.
the issuer to get them. If you received more than $1,500 of taxable interest income in 2015, you must also complete Schedule B.

**Line 8b:** Here’s where you note any tax-exempt interest from municipal bond funds. Don’t worry—that income is not taxable. But social security recipients must count all their tax-exempt interest when computing how much of their social security benefits will be taxable.

**Line 9a:** Enter as dividend income only ordinary dividends, not capital-gains dividends paid by mutual funds, which are reported on Schedule D. Your Form 1099-DIV statements show the amount and type of ordinary dividends you received in 2015. If you received more than $1,500 in dividend income in 2015, you must also complete Schedule B. Remember: Earnings from a money-market mutual fund are considered dividend income, not interest income.

**Line 10:** If you received a refund of a state or local tax in 2015 that you deducted on Schedule A in a prior year, include the refund here.

**Line 12:** Even when you file as an employee for income tax purposes, you will probably have some honoraria or fee income from speaking engagements, weddings, funerals, and so on. This income, less related expenses (see pages 41 and 50), should be reported on Schedule C or C-EZ and entered on this line.

**Line 13:** Enter capital-gains dividends here if you had no other capital gains or losses in 2015.

**Line 15a:** Report as IRA distributions even amounts you rolled over tax-free in 2015 from one IRA into another. On line 15b, you will report as taxable the amount of any IRA distributions that you did not roll over minus any return of nondeductible contributions.

**Line 16a:** It’s likely that only a portion of the total pensions and annuities you received is taxable. Your Form 1099-R will show the taxable amount, which you enter on line 16b. If you received pensions and annuities from a denominationally sponsored plan, you may be eligible to exclude a portion or all of these payments as a housing allowance.

**Line 20a:** No more than 85% of your social security benefits can be taxed for 2015 and none at all if your provisional income is below $32,000 on a joint return, $25,000 for singles. If your income doesn’t exceed the threshold, leave this line blank. If it does, use the worksheet on Form 1099-SSA to compute taxes on your benefits.

- **Adjustments to income (lines 23 to 37).** **Line 25:** Health savings account deduction. Contributions made by a taxpayer to a health savings account (HSA) up to $3,350 for an individual plan and $6,650 for a family plan are deductible on this line. Individuals who have reached age 55 by the end of the tax year are allowed to increase their annual contribution for years after 2015.

**Line 26:** If your employer paid directly or reimbursed you for your qualified moving costs incurred in 2015, these amounts would not be included as compensation on your Form W-2. Therefore, you would have no moving expenses to deduct on line 26. However, if part or all of your moving costs were not paid directly or reimbursed, deduct these expenses here.
**Line 27:** One-half of your social security tax that is deductible for income tax purposes is reflected on this line. This number comes from Schedule SE, Section A, line 6 or Section B, line 13.

**Line 33:** Interest paid on a qualifying student loan may be deducted on this line.

**Line 36:** If you are employed as a chaplain or any other minister-employee of a nonreligious organization, use this line for your deduction of 403(b) contributions that you sent directly to the plan. On the dotted line next to line 36, enter the amount of your deduction and identify it as indicated.

- **Tax computation (lines 38 to 56). Line 40:** Claim the standard deduction only if the amount exceeds what you could write off in itemizing expenses on Schedule A. For 2015, the standard deduction is $12,600 joint, $9,250 head of household, and $6,300 single. The amounts are higher if you or your spouse is 65 or older or legally blind.

**Line 52:** Taxpayers with adjusted gross income of $50,000 or less may claim a credit on this line equal to a certain percentage of the employee contributions made to a retirement account or IRA (must complete Form 8880).

- **Other taxes (lines 57 to 63). Line 57:** If you are a qualified minister (see pages 7–8) and have not opted out of social security, you are self-employed for social security tax purposes. Your social security is not withheld by your church but is calculated on Schedule SE if you had net earnings of $400 or more and paid with Form 1040. The tax is 15.3% of the first $118,500 of 2015 self-employment income and 2.95% of income above $118,500. If your total wages and self-employment earnings were less than $118,500, you can probably save time and headaches by filing the Short Schedule SE on the front of the SE form.

**Line 59:** You will owe the tax on qualified plans plus the 10% penalty on the amount you withdrew from your IRA or another retirement plan if you were under 59%, unless you meet certain exceptions.

- **Payments (lines 64 to 74). Line 64:** Did you have a voluntary withholding arrangement whereby your employing congregation withheld federal income tax from your compensation? Then show the amount of federal income tax the church withheld (from your W-2, Box 2) along with other federal income tax withholding from other employment of you or your spouse here. Also include tax withheld on your W-2G and other Forms 1099 and W-2. The amount withheld should be shown in Box 2 of Form W-2G, in Box 6 of Form 1099-SSA, and Box 4 of other Forms 1099.

**Line 65:** Don’t get confused: Even though you made your fourth-quarter 2015 estimated tax payment in January 2016, it’s counted on your 2015 return.

**Line 66a:** Enter your earned income tax credit here or let the IRS calculate it for you. If you have a qualifying child, you must complete Schedule EIC.

- **Refund or amount you owe (lines 75 to 79). Line 79:** The IRS assumes you must pay the estimated tax penalty if you owe $1,000 or more beyond what you’ve paid through withholding or estimated tax and the amount due is more than 110% of your 2014 tax bill. You may qualify for one of several exceptions, however. Use Form 2210 to prove your case.
Schedule A (Itemized Deductions)
If you live in church-provided housing, you often cannot itemize. But run down Schedule A just to see whether you might have more write-offs than the standard deduction will permit.

- **Medical and dental expenses (lines 1 to 4).** Don’t overlook the cost of getting to and from the doctor or druggist. Write off 23 cents per mile plus the cost of parking. If you didn’t drive, deduct your bus, train, or taxi fares. The cost of trips to see out-of-town specialists and as much as $50 a day for the cost of lodging when you’re out of town to get medical care count toward the 7.5%. Include all your health insurance premiums, as well as Medicare Part B premiums for 2015.

- **Taxes you paid (lines 5 to 9).** Even though your real estate taxes are a housing expense excludable under the housing allowance, you may still deduct them (even for multiple properties if not deducted elsewhere on the return) on line 6 as an itemized deduction—one of the few “double deductions” allowed in the tax law.

- **Interest you paid (lines 10 to 15).** Line 10: If you bought a house during 2015, review your escrow or settlement papers for any mortgage interest you paid that was not shown on your lender’s year-end statement. If you paid interest on a second mortgage or line of credit secured by your home, include the interest expense here.

  As with real estate taxes, it is possible to deduct mortgage interest as an itemized deduction even if the interest is included in housing expenses subject to a housing allowance. Interest paid on a secured mortgage is deductible on Schedule A regardless of how the proceeds of the loan are used. However, the only mortgage interest properly includable as housing expense under a housing allowance is when the loan proceeds were used to provide housing. For example, interest on a second mortgage used to finance your child’s college education is deductible on Schedule A but does not qualify as a housing expense for housing allowance purposes.

  Don’t overlook points you paid to get the mortgage. All of the points are generally deductible as interest here. Points paid for a refinancing must be amortized over the life of the loan. But you can deduct on your 2015 return the portion of all points paid that correspond with the percentage of your refinancing used for home improvements.

- **Gifts to charity (lines 16 to 19).** Line 16: For gifts you made in 2015, you must have written acknowledgments from the charity of any single gifts of $250 or more and for all gifts of cash.

  Line 17: Deduct your charitable mileage for any volunteer work at the rate of 14 cents a mile.

- **Job expenses and other miscellaneous deductions (lines 21 to 27).** Don’t assume you can’t surmount the 2% AGI floor on these miscellaneous deductions. A wealth of employee business, investment, and tax-related expenses—from job-hunting costs to tax preparation fees—are deductible here. And if you bought business equipment required by your employer and you were not reimbursed, you can write off its entire cost up to the 2015 limit. (However, see the allocation of expense rules, page 29, and examples on pages 43 and 61.)
### Sample Return No. 1

- Accountable expense reimbursement plan
- Minister owns residence
- Pays federal taxes through voluntary withholding
- Congregation reimbursed nonqualifying moving expenses
- Housing fair rental value test applied
- 403(b) contribution by salary reduction and employer contributions
- Application of Deason Rule

#### Minister considered to be an employee for income tax purposes with an accountable business expense plan.

The Browns live in a home they are personally purchasing. Pastor Brown has entered into a voluntary withholding agreement with the church, and $12,000 of federal income taxes are withheld.

#### Income, Benefits, and Reimbursements:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Congregation salary</td>
<td>$64,850</td>
</tr>
<tr>
<td>Christmas and other special occasion gifts paid by the congregation based on designed member-gifts to the congregation</td>
<td>750</td>
</tr>
<tr>
<td>Honoraria for performing weddings, funerals, and baptisms</td>
<td>650</td>
</tr>
<tr>
<td>Honorarium for speaking as an evangelist at another church</td>
<td>1,000</td>
</tr>
<tr>
<td>Mutual fund dividend income:</td>
<td></td>
</tr>
<tr>
<td>Capital gain distributions</td>
<td>150</td>
</tr>
<tr>
<td>Ordinary</td>
<td>954</td>
</tr>
<tr>
<td>Interest income:</td>
<td></td>
</tr>
<tr>
<td>Taxable</td>
<td>675</td>
</tr>
<tr>
<td>Tax-exempt</td>
<td>1,200</td>
</tr>
<tr>
<td>Reimbursement of self-employment tax</td>
<td>12,000</td>
</tr>
</tbody>
</table>

#### Business Expenses, Itemized Deductions, Housing, and Other Data:

100% of church-related expenses (including 9,412 business miles) paid personally were reimbursed by the church under an accountable expense plan, based on timely substantiation of the expenses.

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Expenses related to honoraria income:</td>
<td></td>
</tr>
<tr>
<td>Parking</td>
<td>$ 25</td>
</tr>
<tr>
<td>Travel – 864 x 57.5¢ per mile</td>
<td>497</td>
</tr>
<tr>
<td>Meals and entertainment</td>
<td>50</td>
</tr>
<tr>
<td>Other</td>
<td>200</td>
</tr>
<tr>
<td>Potential itemized deductions:</td>
<td></td>
</tr>
<tr>
<td>Unreimbursed doctors, dentists, and drugs</td>
<td>1,500</td>
</tr>
<tr>
<td>State and local income taxes:</td>
<td></td>
</tr>
<tr>
<td>2014 taxes paid in 2015</td>
<td>400</td>
</tr>
<tr>
<td>Withheld from salary</td>
<td>1,600</td>
</tr>
<tr>
<td>Real estate taxes on home</td>
<td>1,000</td>
</tr>
<tr>
<td>Home mortgage interest</td>
<td>14,850</td>
</tr>
<tr>
<td>Cash contributions</td>
<td>8,200</td>
</tr>
<tr>
<td>Noncash contributions – household furniture/fair market value</td>
<td>266</td>
</tr>
<tr>
<td>Tax preparation fee</td>
<td>200</td>
</tr>
<tr>
<td>Student loan interest</td>
<td>1,906</td>
</tr>
<tr>
<td>Housing data:</td>
<td></td>
</tr>
<tr>
<td>Designation</td>
<td>26,000</td>
</tr>
<tr>
<td>Actual expenses</td>
<td>25,625</td>
</tr>
<tr>
<td>Fair rental value including utilities</td>
<td>25,000</td>
</tr>
</tbody>
</table>

#### 403(b) pre-tax contributions for Pastor Brown:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Voluntary employee contributions made under a salary reduction agreement</td>
<td>500</td>
</tr>
<tr>
<td>Nonvoluntary employer contributions</td>
<td>2,000</td>
</tr>
</tbody>
</table>

| Moving expenses reimbursed under a nonqualified plan (see page 45)         | 6,750    |
Line 7 – See page 44 for the calculation of the excess housing allowance.
Line 27 – See page 31 for the explanation of the self-employment tax deduction.
Line 64 – The minister had income tax withheld under a voluntary withholding agreement with the church. Notice that income tax was withheld relating to both the income and social security tax liability.
Lines 6 and 10 – The real estate taxes and home mortgage interest are deducted on this form plus excluded from income on line 7, Form 1040, page 1 as a housing allowance.

Line 21 – There are no unreimbursed employee expenses to deduct since the church reimbursed all the professional expenses under an accountable expense reimbursement plan.
### Interest and Ordinary Dividends

**Part I**

1. **Interest**
   - **State Highway Bonds**
   - **Ohio S&L**
   - **Subtotal**
   - **Less: Tax-Exempt Interest**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>State Highway Bonds</td>
<td>1,200</td>
</tr>
<tr>
<td>Ohio S&amp;L</td>
<td>675</td>
</tr>
<tr>
<td><strong>Subtotal</strong></td>
<td></td>
</tr>
<tr>
<td><strong>Less: Tax-Exempt Interest</strong></td>
<td></td>
</tr>
<tr>
<td></td>
<td>1,875</td>
</tr>
<tr>
<td></td>
<td>-1,200</td>
</tr>
</tbody>
</table>

**Note:** If line 6 is over $1,500, you must complete Part III.

**Part II**

5. **Ordinary Dividends**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Note:** If line 6 is over $1,500, you must complete Part III.

**Part III**

7a. **Foreign Accounts and Trusts**

<table>
<thead>
<tr>
<th>Description</th>
<th>Yes</th>
<th>No</th>
</tr>
</thead>
<tbody>
<tr>
<td>At any time during 2015, did you have a financial interest in or signature authority over a financial account (such as a bank account, securities account, or brokerage account) located in a foreign country?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>If &quot;Yes,&quot; are you required to file FinCEN Form 114, Report of Foreign Bank and Financial Accounts (FBAR), to report that financial interest or signature authority?</td>
<td></td>
<td>X</td>
</tr>
</tbody>
</table>

7b. **Foreign Accounts and Trusts**

<table>
<thead>
<tr>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>If you are required to file FinCEN Form 114, enter the name of the foreign country where the financial account is located</td>
</tr>
</tbody>
</table>

8. **Foreign Accounts and Trusts**

<table>
<thead>
<tr>
<th>Description</th>
<th>Yes</th>
<th>No</th>
</tr>
</thead>
<tbody>
<tr>
<td>During 2015, did you receive a distribution from, or were you the grantor of, or transferor to, a foreign trust?</td>
<td>X</td>
<td></td>
</tr>
</tbody>
</table>
Most clergy considered to be employees for income tax purposes (with that income reported on line 7, Form 1040, page 1) also have honoraria and fee income and related expenses that are reportable on Schedule C (C-EZ).
Sample Return No. 1 – Clergy-Employee for Income Tax Purposes (Accountable Plan)

Section B – Long Schedule SE

Part I Self-Employment Tax

Note. If your only income subject to self-employment tax is church employee income, see instructions. Also see instructions for the definition of church employee income.

A If you are a minister, member of a religious order, or Christian Science practitioner and you filed Form 4561, but you had $4,300 or more of other net earnings from self-employment, check here and continue with Part I. □

1a Net farm profit or loss from Schedule F, line 3d, and farm partnerships, Schedule K-1 (Form 1065), box 14, code A. Note. Skip lines 1a and 1b if you use the farm optional method (see instructions).

1b If you received social security retirement or disability benefits, enter the amount of Conservation Reserve Program payments included on Schedule F, line 4a, or listed on Schedule K-1 (Form 1065), box 22, code Z.

2 Net profit or loss from Schedule C, line 31; Schedule C-EZ, line 3; Schedule K-1 (Form 1065), box 14, code A (other than farming); and Schedule K-1 (Form 1065-B), box 9, code J1. Minsters and members of religious orders, see instructions for types of income to report on this line. See instructions for other income to report. Note. Skip this line if you use the nonfarm optional method (see instructions).

3 Combine lines 1a, 1b, and 2.

4a If line 3 is more than zero, multiply line 3 by 92.35% (0.9235). Otherwise, enter amount from line 3. Note. If line 4a is less than $100 due to Conservation Reserve Program payments on line 1b, see instructions.

4b If you elect one or both of the optional methods, enter the total of lines 15 and 17 here.

4c Combine lines 4a and 4b. If less than $400, stop; you do not owe self-employment tax. Exception. If less than $400 and you had church employee income, enter -20 and continue ▶

5a Enter your church employee income from Form W-2. See instructions for definition of church employee income.

5b Multiply line 5a by 92.35% (0.9235). If less than $100, enter -20.

6 Add lines 4c and 5b.

7 Maximum amount of combined wages and self-employment earnings subject to social security tax or the 6.2% portion of the 7.65% railroad retirement (tier 1) tax for 2016.

8a Total social security wages and tips (total of boxes 3 and 7 on Form(s) W-2) and railroad retirement (tier 1) compensation. If $118,500 or more, skip lines 8b through 10, and go to line 11.

8b Unreported tips subject to social security tax (from Form 4137, line 10).

8c Wages subject to social security tax (from Form W-2, line 10).

8d Subtract line 8d from line 7. If zero or less, enter -20 here and on line 10 and go to line 11.

10 Multiply the smaller of line 6 or line 9 by 12.4% (0.124).

11 Multiply 10 by 2.9% (0.029).

12 Self-employment tax. Add lines 10 and 11. Enter here and on Form 1040, line 37, or Form 1040NR, line 55.

13 Deduction for one-half of self-employment tax. Multiply line 12 by 50%. Enter the result here and on Form 1040, line 27, or Form 1040NR, line 27.

Part II Optional Methods To Figure Net Earnings (see instructions)

Farm Optional Method. You may use this method only if (a) your gross farm income was not more than $7,320, or (b) your net farm profits were less than $5,284.

14 Maximum income for optional methods.

15 Enter the smaller of: two-thirds (2/3) of gross farm income (not less than zero) or $4,380. Also include this amount on line 4b above.

Nonfarm Optional Method. You may use this method only if (a) your net nonfarm profits were less than $5,284 and also less than 72.18% of your gross nonfarm income, and (b) you had net earnings from self-employment of at least $400 in 2 of the prior 3 years. Caution. You may use this method no more than five times.

16 Subtract line 15 from line 14.

17 Enter the smaller of: two-thirds (2/3) of gross nonfarm income (not less than zero) or the amount on line 16. Also include this amount on line 4b above.

Line 2 – See Attachment 2 on page 43.

Line 4 – This line results in the deduction of a portion of the self-employment tax liability.

A minister must use Section B-Long Schedule if he or she received nonministerial wages (subject to FICA) and the total of these wages and net ministerial self-employment earnings (W-2 and Schedule C [C-EZ]-related) is more than $118,500.
Attachment 1.
Computation of expenses, allocatable to tax-free ministerial income, that are nondeductible.

<table>
<thead>
<tr>
<th>Description</th>
<th>Taxable</th>
<th>Tax-Free</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Salary as a minister</td>
<td>$ 57,850</td>
<td>$ 57,850</td>
<td></td>
</tr>
<tr>
<td>Housing allowance:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Amount designated and paid by church</td>
<td>$ 26,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Actual expenses</td>
<td>25,625</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fair rental value of home (including furnishings and utilities)</td>
<td>25,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Taxable portion of allowance</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(excess of amount designated &amp; paid over less of actual expenses or fair rental value)</td>
<td>$ 1,000</td>
<td>1,000</td>
<td>1,000</td>
</tr>
<tr>
<td>Tax-free portion of allowance (lesser of amount designated, actual expenses, or fair rental value)</td>
<td>25,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gross income from weddings, baptisms, and honoraria</td>
<td>1,650</td>
<td></td>
<td>1,650</td>
</tr>
<tr>
<td>Ministerial Income</td>
<td>$ 60,500</td>
<td>$ 25,000</td>
<td>$ 85,500</td>
</tr>
</tbody>
</table>

% of nondeductible expenses: $25,000/$85,500 = 29%

Schedule C-EZ Deduction Computation

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Parking</td>
<td>$ 25</td>
</tr>
<tr>
<td>Meals &amp; Entertainment ($50 x 50% deductible portion)</td>
<td>25</td>
</tr>
<tr>
<td>Other</td>
<td>200</td>
</tr>
<tr>
<td>Mileage (864 miles x 57.5 cents per mile)</td>
<td>497</td>
</tr>
<tr>
<td>Unadjusted Schedule C-EZ expenses</td>
<td>747</td>
</tr>
<tr>
<td>Minus:</td>
<td></td>
</tr>
<tr>
<td>Nondeductible part of Schedule C-EZ expenses (29% x $747)</td>
<td>(217)</td>
</tr>
<tr>
<td>Schedule C-EZ deductions (line 2) (See page 41)</td>
<td>$ 530</td>
</tr>
</tbody>
</table>

Attachment 2.
Net earnings from self-employment (attachment to Schedule SE, Form 1040)

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Congregation wages</td>
<td>$ 57,850</td>
</tr>
<tr>
<td>Housing allowance</td>
<td>26,000</td>
</tr>
<tr>
<td>Net profit from Schedule C-EZ</td>
<td>1,120</td>
</tr>
<tr>
<td>Less:</td>
<td></td>
</tr>
<tr>
<td>Schedule C-EZ expenses allocable to tax-free income</td>
<td>(217)</td>
</tr>
<tr>
<td>Net Self-Employed Income</td>
<td></td>
</tr>
<tr>
<td>Schedule SE, Section A, line 2 (See page 42)</td>
<td>$ 84,753</td>
</tr>
</tbody>
</table>
## Housing Allowance Worksheet

### Clergy-Owned Home

Name: ______________________________

For the period ______________ to ______________

Date designation approved ______________

### Allowable Housing Expenses (expenses paid from current income)

<table>
<thead>
<tr>
<th>Item</th>
<th>Estimated Expenses</th>
<th>Actual</th>
</tr>
</thead>
<tbody>
<tr>
<td>Down payment on purchase of housing</td>
<td>$ ______________</td>
<td>$ __________</td>
</tr>
<tr>
<td>Housing loan principal and interest payments</td>
<td>18,117</td>
<td>18,875</td>
</tr>
<tr>
<td>Real estate commission, escrow fees</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Real property taxes</td>
<td>900</td>
<td>1,000</td>
</tr>
<tr>
<td>Personal property taxes on contents</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Homeowner’s insurance</td>
<td>500</td>
<td>550</td>
</tr>
<tr>
<td>Personal property insurance on contents</td>
<td>150</td>
<td>200</td>
</tr>
<tr>
<td>Umbrella liability insurance</td>
<td>100</td>
<td></td>
</tr>
<tr>
<td>Structural maintenance and repair</td>
<td></td>
<td>550</td>
</tr>
<tr>
<td>Landscaping, gardening, and pest control</td>
<td></td>
<td>200</td>
</tr>
<tr>
<td>Furnishings <em>(purchase, repair, replacement)</em></td>
<td></td>
<td>400</td>
</tr>
<tr>
<td>Decoration and redecoration</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Utilities <em>(gas, electricity, water)</em> and trash collection</td>
<td>3,500</td>
<td>3,500</td>
</tr>
<tr>
<td>Local telephone expense <em>(base charge)</em></td>
<td>150</td>
<td>150</td>
</tr>
<tr>
<td>Homeowner’s association dues/condominium fees</td>
<td>219</td>
<td>200</td>
</tr>
</tbody>
</table>

**Subtotal** 23,636

10% allowance for unexpected expenses 2,364

**TOTAL** $ 26,000 $ 25,625 *(A)*

Properly designated housing allowance $ 26,000 *(B)*

Fair rental value of home, including furnishings, plus utilities $ 25,000 *(C)*

**Note:** The amount excludable from income for federal income tax purposes is the *lowest* of A, B, or C.

---

The $1,000 difference between the designation ($26,000) and the fair rental value ($25,000) is reported as additional income on Form 1040, line 7.
Pastor Brown received reimbursements of $7,593 under an accountable expense reimbursement plan. The reimbursements are not included on Form W-2 or deductible on Form 1040. There is no requirement to add the reimbursements to income taxable for social security purposes on Schedule SE.

Pastor Brown was also reimbursed for $6,750 of nonqualified moving expenses. He failed the distance test in that his new principal place of work was less than 50 miles farther from his old residence than the old residence was from his old place of work.
Sample Return No. 2

- Nonaccountable expense reimbursements
- Minister occupies a church-provided parsonage
- Pays federal taxes using Form 1040-ES
- Qualifies for the Earned Income Credit
- Congregation did not reimburse moving expenses
- Application of Deason Rule
- Tax Saver’s Credit

Minister considered to be an employee for income tax purposes with a nonaccountable business expense plan.

The Halls live in church-provided housing.

Income, Benefits, and Reimbursements:

- Church salary – Donald $11,000
- Salary – Julie (W-2 not shown)/Federal withholding of $250 13,350
- Christmas and other special occasion gifts paid by the church based on designated member-gifts to the church 500
- Honoraria for performing weddings, funerals, baptisms, and outside speaking engagements 5,200
- Interest income (taxable) 750
- Reimbursement of self-employment tax 2,100
- Business expense allowance (no accounting provided to church) 1,700

Business Expenses, Itemized Deductions, 403(b) Contributions, Housing Data, and Moving Expense Data:

Church-related expenses paid personally:
- Business use of personally-owned auto (W-2 related) 7,450 miles
- Personal nondeductible commuting 2,432 miles

Seminar expenses:
- Airfare $675
- Meals 233
- Lodging 167
- Subscriptions 200

Books (less than one-year life) 100
Supplies 250
Entertainment expenses 1,207
Continuing education tuition (related to church employment) 500
Travel expense related to honoraria (Schedule C-EZ):
- Airfare 2,042
- Business use of personally-owned auto 2,177 x 57.5¢ per mile 1,252
- Lodging 400
- Supplies 700

Potential itemized deductions:
- Unreimbursed doctors, dentists, and drugs 3,050
- State and local income taxes 460
- Personal property taxes 300
- Cash contributions 3,310

Housing data:
- Designation 2,000
- Actual expenses 1,000
- Fair rental value, including furnishings and utilities 11,150

403(b) pre-tax contributions for Pastor Hall: Voluntary employee contributions made under a salary reduction agreement 500

Moving expenses (deductible) 1,183

Estimated $24,000 in income for health insurance exchange subsidy at the beginning of year
Line 7 – Julie’s W-2, $9,150, Donald’s W-2, $12,800 (see page 63), plus $1,000 of excess housing allowance (see page 62).

Line 27 – See page 31 for explanation of the self-employment tax deduction.
**Sample Return No. 2 – Clergy-Employee for Income Tax Purposes (Nonaccountable Plan)**

<table>
<thead>
<tr>
<th>Line</th>
<th>Description</th>
<th>Amount($)</th>
</tr>
</thead>
<tbody>
<tr>
<td>38</td>
<td>Amount from line 37 (adjusted gross income)</td>
<td>27,834</td>
</tr>
<tr>
<td>39a</td>
<td>Check: You were born before January 2, 1921,</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Blind. Total boxes</td>
<td></td>
</tr>
<tr>
<td>40</td>
<td>If your spouse itemizes on separate return or you were a dual-status alien, check here</td>
<td>12,600</td>
</tr>
<tr>
<td>41</td>
<td>Subtract line 40 from line 38</td>
<td>15,234</td>
</tr>
<tr>
<td>42</td>
<td>Exemptions, if line 38 is $14,000 or less, multiply $4,000 by the number on line 63. Otherwise, see instructions.</td>
<td>16,000</td>
</tr>
<tr>
<td>43</td>
<td>Taxable income. Subtract line 42 from line 41. If line 42 is more than line 41, enter -0-</td>
<td>0</td>
</tr>
<tr>
<td>44</td>
<td>Tax (see instructions). Check if any tax: a) Form(s) 8814 b) Form 4972 c)</td>
<td></td>
</tr>
<tr>
<td>45</td>
<td>Alternative minimum tax (see instructions), Attach Form 6291</td>
<td>45</td>
</tr>
<tr>
<td>46</td>
<td>Excess advance premium tax credit repayment, Attach Form 6262</td>
<td>77</td>
</tr>
<tr>
<td>47</td>
<td>Add lines 44, 45, and 46</td>
<td>77</td>
</tr>
<tr>
<td>48</td>
<td>Foreign tax credit, Attach Form 1116 if required</td>
<td></td>
</tr>
<tr>
<td>49</td>
<td>Credit for care and dependent care expenses, Attach Form 2441</td>
<td></td>
</tr>
<tr>
<td>50</td>
<td>Education credits from Form 2290, line 19</td>
<td></td>
</tr>
<tr>
<td>51</td>
<td>Retirement savings contributions credit, Attach Form 8850</td>
<td></td>
</tr>
<tr>
<td>52</td>
<td>Child tax credit, Attach Schedule 8812, if required</td>
<td></td>
</tr>
<tr>
<td>53</td>
<td>Residential energy credit, Attach Form 8865</td>
<td></td>
</tr>
<tr>
<td>54</td>
<td>Add lines 48 through 54. These are your total credits</td>
<td>77</td>
</tr>
<tr>
<td>55</td>
<td>Subtract line 55 from line 47. If line 55 is more than line 47, enter -0-</td>
<td></td>
</tr>
<tr>
<td>56</td>
<td>Tax (see instructions). Check if any tax: a) Form(s) 8814 b) Form 4972 c)</td>
<td></td>
</tr>
<tr>
<td>57</td>
<td>Self-employment tax, Attach Schedule SE</td>
<td>2,806</td>
</tr>
<tr>
<td>58</td>
<td>Unemployment compensation and Medicare tax from Form: a) 4137 b) 8919</td>
<td>58</td>
</tr>
<tr>
<td>59</td>
<td>Additional tax on IRAs, other qualified retirement plans, etc, Attach Form 8329 if required.</td>
<td>59</td>
</tr>
<tr>
<td>60</td>
<td>Household employment taxes from Schedule H</td>
<td></td>
</tr>
<tr>
<td>61</td>
<td>First-time homebuyer credit repayment, Attach Form 8499 if required</td>
<td></td>
</tr>
<tr>
<td>62</td>
<td>Health care individual responsibility (see instructions), Full-year coverage</td>
<td></td>
</tr>
<tr>
<td>63</td>
<td>Add lines 48 through 62. This is your total tax</td>
<td>2,806</td>
</tr>
<tr>
<td>64</td>
<td>Federal income tax withheld from Forms W-2 and 1099</td>
<td></td>
</tr>
<tr>
<td>65</td>
<td>2015 estimated tax payments and amount applied from 2014 return</td>
<td></td>
</tr>
<tr>
<td>66</td>
<td>Earned income credit (EIC)</td>
<td>3,822</td>
</tr>
<tr>
<td>66a</td>
<td>Non-taxable combat pay election</td>
<td></td>
</tr>
<tr>
<td>67</td>
<td>Additional tax credit, Attach Schedule 8812</td>
<td></td>
</tr>
<tr>
<td>68</td>
<td>American opportunity credit, Attach Form 8863, line 8</td>
<td></td>
</tr>
<tr>
<td>69</td>
<td>Retired tax credit, Attach Form 8862</td>
<td></td>
</tr>
<tr>
<td>70</td>
<td>Amount paid with request for extension to the</td>
<td></td>
</tr>
<tr>
<td>71</td>
<td>Excise social security and tier 1 IRA tax withheld</td>
<td></td>
</tr>
<tr>
<td>72</td>
<td>Credit for federal tax on fuels, Attach Form 4150</td>
<td></td>
</tr>
<tr>
<td>73</td>
<td>Credit for Form: a) 8329 b) 8268 c) 8865</td>
<td></td>
</tr>
<tr>
<td>74</td>
<td>Add lines 64, 65, 66, 67 through 73. These are your total payments</td>
<td>74</td>
</tr>
<tr>
<td>75</td>
<td>If line 74 is more than line 69, subtract line 69 from line 74. This is the amount you overspent</td>
<td></td>
</tr>
<tr>
<td>76a</td>
<td>Amount of line 75 you want refunded to you. If Form 8858 is attached, check here</td>
<td>3,266</td>
</tr>
<tr>
<td>77</td>
<td>Amount you owe. Subtract line 74 from line 63. For details on how to pay, see instructions.</td>
<td>3,266</td>
</tr>
</tbody>
</table>

**Refund**

<table>
<thead>
<tr>
<th>Line</th>
<th>Description</th>
<th>Amount($)</th>
</tr>
</thead>
<tbody>
<tr>
<td>76a</td>
<td>Amount of line 75 you want refunded to you. If Form 8858 is attached, check here</td>
<td>3,266</td>
</tr>
</tbody>
</table>

**Payments**

**Payments**

- Federal income tax withheld from Forms W-2 and 1099
- 2015 estimated tax payments and amount applied from 2014 return
- Earned income credit (EIC)
- Non-taxable combat pay election
- Additional tax credit, Attach Schedule 8812
- American opportunity credit, Attach Form 8863, line 8
- Retired tax credit, Attach Form 8862
- Amount paid with request for extension to the
- Excise social security and tier 1 IRA tax withheld
- Credit for federal tax on fuels, Attach Form 4150
- Credit for Form: a) 8329 b) 8268 c) 8865
- Add lines 64, 65, 66, 67 through 73. These are your total payments

**Refund**

- If line 74 is more than line 69, subtract line 69 from line 74. This is the amount you overspent
- Amount of line 75 you want refunded to you. If Form 8858 is attached, check here
- Amount you owe. Subtract line 74 from line 63. For details on how to pay, see instructions

**Third Party Designee**

- Do you want to allow another person to discuss this return with the IRS? (see instructions)
- Yes. Complete below. No

**Sign Here**

- Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements and to the best of my knowledge and belief, they are true, correct, and complete. Declaration of preparer (other than taxpayer) is required on all returns on which preparer has any knowledge.

**Date**

- Signature: 4/15/16
- Date of signature: 4/15/16
- Signature of preparer: 4/15/16

**Print/Type preparer's name**

- Name: Hall
- Date: 4/15/16
- Signature: Hall

**Uses Only**

- Firm's name: Hall
- Phone: (555) 555-5555

**Preparer's EIN**

- EIN: 123456789

**Preparer's Signature**

- Signature: Hall
- Date: 4/15/16

**Preparer's Information**

- Date: 4/15/16
- Signature: Hall
- Phone: (555) 555-5555
(1) Expenses have been reduced by 39% as allocable to tax-free income (see page 61 for percentage). Most ministers are employees for income tax purposes (with that income reported on line 7, Form 1040, page 1) and also have honoraria and fee income and related expenses that are reportable on Schedule C (C-EZ). For an explanation of expenses related to the honoraria in this sample return, see page 58.
May I Use Short Schedule SE or Must I Use Long Schedule SE?

**Note.** Use this flowchart only if you must file Schedule SE. If unsure, see Who Must File Schedule SE in the instructions.

- **Did you receive wages or tips in 2015?**
  - **Yes:**
    - **Was the total of your wages and tips subject to social security or railroad retirement (tax line 1) plus your net earnings from self-employment more than $118,500?**
      - **Yes:**
        - **Did you report tips subject to social security or Medicare tax that you did not report to your employer?**
          - **Yes:**
            - **Did you report any wages on Form W-2, Unrelated Social Security and Medicare Tax on Wages?**
              - **Yes:**
                - **You may use Short Schedule SE below**
              - **No:**
                - **You must use Long Schedule SE on page 2**
          - **No:**
            - **You must use Long Schedule SE on page 2**
      - **No:**
        - **Did you receive church employee income (see instructions) reported on Form W-2 or 1099-DIV or other?**
          - **Yes:**
            - **You may use Short Schedule SE below**
          - **No:**
            - **You must use Long Schedule SE on page 2**

**Section A — Short Schedule SE. Caution.** Read above to see if you can use Short Schedule SE.

1a. Net farm profit or (loss) from Schedule F, line 34, and farm partnerships, Schedule K-1 (Form 1065), box 14, code A.
   - If you received social security retirement or disability benefits, enter the amount of Conservation Reserve Program payments included on Schedule F, line 4b, or listed on Schedule K-1 (Form 1065), box 21, code Z.

2. Net profit or (loss) from Schedule C, line 31; Schedule C-EZ, line 3; Schedule K-1 (Form 1065), box 14, code A (other than farming), and Schedule K-1 (Form 1065-B), box 9, code J. Ministers and members of religious orders, see instructions for types of income to report on this line. See instructions for other income to report.

3. Combine lines 1a, 1b, and 2.

4. Multiply line 3 by 0.92356 (%.235). If less than $400, do not owe self-employment tax; do not file this schedule unless you have an amount on line 1b.

**Self-employment tax.** If the amount on line 4 is:
- $118,500 or less, multiply line 4 by 15.3% (.153). Enter the result here and on Form 1040, line 57, or Form 1040NR, line 55.
- More than $118,600, multiply line 4 by 2.9% (.029). Then, add $14,464 to the result. Enter the total here and on Form 1040, line 57, or Form 1040NR, line 55.

5. Deduction for one-half of self-employment tax.
   - Multiply line 5 by 50% (.50). Enter the result here and on Form 1040, line 27, or Form 1040NR, line 27.

For Paperwork Reduction Act Notice, see your tax return instructions.

Line 2 — See the schedule on page 61 for the calculation of this amount.

Line 4 — This line results in the deduction of a portion of the self-employment tax liability.

A minister may use Section A-Short Schedule unless he received nonministerial wages (subject to FICA) and the total of these wages and net ministerial self-employment earnings (W-2 and Schedule C-related) is more than $118,500.
If you are eligible for the Earned Income Credit, you must file page 1 of Schedule EIC if you have a qualifying child. Compute your credit on Worksheet B found in the IRS instruction booklet.

There could have been a much larger Earned Income Credit if Donald Hall’s business expenses had been reimbursed and a lower salary prospectively established. The expenses claimed on Form 2106-EZ do not offset earned income for the EIC calculation.
### Part 1

<p>| | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Self-Employed, Members of the Clergy, and People With Church Employee Income Filing Schedule SE**

1. Enter the amount from Schedule SE, Section A, line 3, or Section B, line 3, whichever applies.
2. Enter any amount from Schedule SE, Section B, line 4b, and line 5a.
3. Combine lines 1a and 1b.
4. Enter the amount from Schedule SE, Section A, line 6, or Section B, line 13, whichever applies.
5. Subtract line 1d from 1c.

- **1a:** 33,210
- **1b:** 1,403
- **1c:** 31,807

**Part 2**

**Self-Employed NOT Required To File Schedule SE**

For example, your net earnings from self-employment were less than $400.

1. Enter any net farm profit or (loss) from Schedule F, line 34, and from firm partnerships, Schedule K-1 (Form 1065), box 14, code A.
2. Enter any net profit or (loss) from Schedule C, line 31, Schedule C-EZ, line 3; Schedule K-1 (Form 1065), box 14, code A (other than farming); and Schedule K-1 (Form 1065-B), box 9, code J.

- **2a:** 100
- **2b:** 200
- **2c:** 300

3. Enter the amount from Schedule C, line 1, or Schedule C-EZ, line 1, that you are filing as a statutory employee.

- **3:** 400

**Part 3**

**Statutory Employees Filing Schedule C or C-EZ**

4. Enter your earned income from Step 5.

- **4a:** 500
- **4b:** 600

5. If line 4b is zero or less, you cannot take the credit. Enter "No" on the dotted line next to line 6a.

**Part 4**

**All Filers Using Worksheet B**

Note: If line 4b includes income on which you should have paid self-employment tax but didn't, we may reduce your credit by the amount of self-employment tax not paid.

- **4a:** 500
- **4b:** 600

**Worksheet B**

1. Included on Line 1a: Julie Hall's salary $9,150
2. Schedule SE income 19,860
3. $29,010

*Worksheet B is found in the IRS instruction booklet. Complete this worksheet whether or not you have a qualifying child.*
### Part 5

#### All Filers Using Worksheet B

6. Enter your total earned income from Part 4, line 4b.

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>6</td>
<td>31,897</td>
</tr>
</tbody>
</table>

7. Look up the amount on line 6 above in the EIC Table to find the credit. Be sure you use the correct column for your filing status and the number of children you have. Enter the credit here.

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>7</td>
<td>3,822</td>
</tr>
</tbody>
</table>

If line 7 is zero, **X** You cannot take the credit. Enter “No” on the dotted line next to line 6b.

8. Enter the amount from Form 1040, line 38.

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>8</td>
<td>27,834</td>
</tr>
</tbody>
</table>

9. Are the amounts on lines 8 and 6 the same?

- [ ] Yes. Skip line 10; enter the amount from line 7 on line 11.
- **X** No. Go to line 10.

### Part 6

#### Filers Who Answered “No” on Line 8

10. If you have:

- No qualifying children, is the amount on line 8 less than $38,250 ($30,050 if married filing jointly)?
- 1 or more qualifying children, is the amount on line 8 less than $18,150 ($22,650 if married filing jointly)?

- [ ] Yes. Leave line 10 blank; enter the amount from line 7 on line 11.
- **X** No. Look up the amount on line 8 in the EIC Table to find the credit. Be sure you use the correct column for your filing status and the number of children you have. Enter the credit here.

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>10</td>
<td>4,665</td>
</tr>
</tbody>
</table>

Then, enter the smaller amount on line 11.

### Part 7

#### Your Earned Income Credit

11. This is your earned income credit.

**Reminder—**

- If you have a qualifying child, complete and attach Schedule EIC.

If your EIC for a year after 1996 was reduced or disallowed, see Form 8862, who must file earlier, to find out if you must file Form 8862 to take the credit for 2015.
### Child Tax Credit

**If your dependent is not a qualifying child for the credit, you cannot include that dependent in the calculation of this credit.**

Answer the following questions for each dependent listed on Form 1040, line 6c; Form 1040A, line 6c; or Form 1040NR, line 7c, who has an ITIN (Individual Taxpayer Identification Number) and who you indicated as a qualifying child for the child tax credit by checking column (A) for that dependent.

A. For the first dependent identified with an ITIN and listed as a qualifying child for the child tax credit, did this child meet the substantial presence test? See separate instructions.

   - [ ] Yes
   - [ ] No

B. For the second dependent identified with an ITIN and listed as a qualifying child for the child tax credit, did this child meet the substantial presence test? See separate instructions.

   - [ ] Yes
   - [ ] No

C. For the third dependent identified with an ITIN and listed as a qualifying child for the child tax credit, did this child meet the substantial presence test? See separate instructions.

   - [ ] Yes
   - [ ] No

D. For the fourth dependent identified with an ITIN and listed as a qualifying child for the child tax credit, did this child meet the substantial presence test? See separate instructions.

   - [ ] Yes
   - [ ] No

**Note:** If you have more than four dependents identified with an ITIN and listed as a qualifying child for the child tax credit, see separate instructions and check here.

---

### Part II Additional Child Tax Credit Filers

1. If you file Form 2555 or 2555-EZ, stop here, you cannot claim the additional child tax credit.

   If you are required to use the worksheet in Pub. 972, enter the amount from line 8 of the Child Tax Credit Worksheet in the box.

   **Filing status:**
   - 1040 filers: Enter the amount from line 6 of your Child Tax Credit Worksheet (see the instructions for Form 1040, line 52).
   - 1040A filers: Enter the amount from line 6 of your Child Tax Credit Worksheet (see the instructions for Form 1040A, line 35).
   - 1040NR filers: Enter the amount from line 6 of your Child Tax Credit Worksheet (see the instructions for Form 1040NR, line 49).

2. Enter the amount from Form 1040, line 52; Form 1040A, line 35; or Form 1040NR, line 49.

3. Subtract line 2 from line 1. If zero, stop; you cannot take this credit.

4a. Earned income (see separate instructions)...

   31,807 - 11,150 - 1,000 = 19,657

b. Nonrefundable combat pay (see separate instructions)...

5. Is the amount on line 4a more than $3,000?

   - [ ] No
   - [ ] Yes. Subtract $3,000 from the amount on line 4a. Enter the result...

6. Multiply the amount on line 5 by 15% (.15) and enter the result. Next. Do you have three or more qualifying children?

   - [ ] No
   - [ ] Yes. If line 6 is zero, stop; you cannot take this credit. Otherwise, skip Part III and enter the smaller of line 3 or line 6 on line 13.

   Otherwise, go to line 7.

---

For Paperwork Reduction Act Notice, see your tax return instructions.
### Part III Certain Filers Who Have Three or More Qualifying Children

7. Withheld social security, Medicare, and Additional Medicare taxes from Form(s) W-2, boxes 4 and 6. If married filing jointly, include your spouse's amounts with yours. If your employer withheld or you paid Additional Medicare Tax or Tier 1 RRTA taxes, see separate instructions. 

8. 1040 filers: Enter the total of the amounts from Form 1040, lines 27 and 58, plus any taxes that you identified using code "UT" and entered on line 62. Enter —.

1040NR filers: Enter the total of the amounts from Form 1040NR, lines 27 and 58, plus any taxes that you identified using code "UT" and entered on line 60.

9. Add lines 7 and 8. 

10. Enter the total of the amounts from Form 1040, lines 66a and 71.

11. Enter the amount from Form 1040A, line 42a, plus any excess social security and Tier 1 RRTA taxes withheld that you entered to the left of line 46 (see separate instructions).

12. Subtract line 10 from line 9. If zero or less, enter 0.

13. Enter the larger of line 6 or line 11. 

Next, enter the smaller of line 3 or line 12 on line 13.

### Part IV Additional Child Tax Credit

13. This is your additional child tax credit. 

14. Enter the amount on Form 1040, line 62. 

15. Enter the amount on Form 1040A, line 45. 

16. Enter the amount on Form 1040NR, line 64.
2015 Child Tax Credit Worksheet—Continued

Before you begin Part 2: \( \Box \) Figure the amount of any credits you are claiming on Form 8910, Form 8936, or Schedule R.

Part 2

7. Enter the amount from Form 1040, line 47.  
   \[ \Box \] 7  77

8. Add any amounts from:
   - Form 1040, line 48
   - Form 1040, line 49 +
   - Form 1040, line 50 +
   - Form 1040, line 51 +  77
   - Form 5695, line 39%+
   - Form 8910, line 15 +
   - Form 8936, line 23 +
   - Schedule R, line 22 +
   Enter the total: 8  77

9. Are the amounts on lines 7 and 8 the same?
   \( \Box \) Yes.  
   \( \Box \) No.
   You cannot take this credit because there is no tax to reduce. However, you may be able to take the additional child tax credit. See the TIP below.
   \[ \Box \] 9

10. Is the amount on line 6 more than the amount on line 9?
    \( \Box \) Yes. Enter the amount from line 9.
    \( \Box \) No. Enter the amount from line 8.
    This is your child tax credit.
    \[ \Box \] 10
    Enter this amount on Form 1040, line 52.

    **TIP**
    You may be able to take the additional child tax credit on Form 1040, line 67, if you answered "Yes" on line 9 or line 10 above.
    - First, complete your Form 1040 through lines 56a and 66b.
    - Then, use Schedule 8812 to figure any additional child tax credit.

    \( ^* \)See the Form 5695 Instructions to see if line 30 (nonbusiness energy property credit) applies for 2015.
**Form 2106-EZ**  
Unreimbursed Employee Business Expenses

**Information**
- Attach to Form 1040 or Form 1040NR.

**Your name**
Donald L. Hall

**Occupation in which you incurred expenses**
Minister

**Social security number**
482 11 6043

---

### Part I. Figure Your Expenses

<table>
<thead>
<tr>
<th>Line</th>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>2,613</td>
<td></td>
</tr>
<tr>
<td>2</td>
<td></td>
<td></td>
</tr>
<tr>
<td>3</td>
<td></td>
<td></td>
</tr>
<tr>
<td>4</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5</td>
<td>439</td>
<td></td>
</tr>
<tr>
<td>6</td>
<td>4,206</td>
<td></td>
</tr>
</tbody>
</table>

### Part II. Information on Your Vehicle

Complete this part only if you are claiming vehicle expense on line 1.

<table>
<thead>
<tr>
<th>Question</th>
<th>Notes</th>
</tr>
</thead>
<tbody>
<tr>
<td>7</td>
<td>When did you place your vehicle in service for business use? (month, day, year)</td>
</tr>
<tr>
<td>8</td>
<td>Of the total number of miles you drove your vehicle during 2015, enter the number of miles you used your vehicle for:</td>
</tr>
<tr>
<td>9</td>
<td>Was your vehicle available for personal use during off-duty hours?</td>
</tr>
<tr>
<td>10</td>
<td>Do you (or your spouse) have another vehicle available for personal use?</td>
</tr>
<tr>
<td>11a</td>
<td>Do you have evidence to support your deduction?</td>
</tr>
<tr>
<td>11b</td>
<td>If “Yes,” is the evidence written?</td>
</tr>
</tbody>
</table>

---

Lines 1, 3, 4, 5 – See allocations on page 61.

Line 6 – The total expenses on this line are carried forward to Form 1040, Schedule A, line 21.
### Computation of expenses related to honoraria on Sample Return No. 2/page 49

<table>
<thead>
<tr>
<th>Item</th>
<th>Deductible</th>
<th>Nondeductible</th>
</tr>
</thead>
<tbody>
<tr>
<td>Airfare</td>
<td>$2,042</td>
<td>$796</td>
</tr>
<tr>
<td>Auto</td>
<td>2,177 x 57.5¢</td>
<td>488</td>
</tr>
<tr>
<td>Lodging</td>
<td>400 x 61%</td>
<td>156</td>
</tr>
<tr>
<td>Supplies</td>
<td>700 x 61%</td>
<td>273</td>
</tr>
<tr>
<td></td>
<td>4,394 x 61%</td>
<td>1,714</td>
</tr>
</tbody>
</table>
### Credit for Qualified Retirement Savings Contributions

**Sample Return No. 2 – Clergy-Employee for Income Tax Purposes (Nonaccountable Plan)**

**Form 8880**

**Department of the Treasury**

**Internal Revenue Service**

[Image 63x120 to 548x700]

**Sample Return No. 2 – Clergy-Employee for Income Tax Purposes (Nonaccountable Plan) 59**

You cannot take this credit if either of the following applies:

- The amount on Form 1040, line 38; Form 1040A, line 22; or Form 1040NR, line 37 is more than $30,500 ($45,750 if head of household; $41,000 if married filing jointly).
- The person(s) who made the qualified contribution or elective deferral (a) was born after January 1, 1998, (b) is claimed as a dependent on someone else’s 2015 tax return, or (c) was a student (see instructions).

| **1** | Traditional and Roth IRA contributions for 2015. Do not include rollover contributions. |
| **2** | Elective deferrals to a 401(k) or other qualified employer plan, voluntary employee contributions, and 501(c)(18)(E) plan contributions for 2015 (see instructions). |
| **3** | Add lines 1 and 2. |
| **4** | Certain distributions received after 2012 and before the due date (including extensions) of your 2015 tax return (see instructions). If married filing jointly, include both spouses' amounts in both columns. See instructions for an exception. |
| **5** | Subtract line 4 from line 3. If zero or less, enter -0-. |
| **6** | In each column, enter the smaller of line 5 or $2,000. |
| **7** | Add the amounts on line 6. If zero, stop; you cannot take this credit. |
| **8** | Enter the amount from Form 1040, line 38; Form 1040A, line 22; or Form 1040NR, line 37. |
| **9** | Enter the applicable decimal amount shown below: |

<table>
<thead>
<tr>
<th><strong>If line 8 is</strong></th>
<th><strong>And your filing status is</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Over</strong></td>
<td><strong>But not over</strong></td>
</tr>
<tr>
<td>---</td>
<td>---</td>
</tr>
<tr>
<td>---</td>
<td>$19,750</td>
</tr>
<tr>
<td>$19,750</td>
<td>$19,750</td>
</tr>
<tr>
<td>$22,375</td>
<td>$22,375</td>
</tr>
<tr>
<td>$29,625</td>
<td>$29,625</td>
</tr>
<tr>
<td>$30,500</td>
<td>$30,500</td>
</tr>
<tr>
<td>$36,500</td>
<td>$36,500</td>
</tr>
<tr>
<td>$91,000</td>
<td>$91,000</td>
</tr>
<tr>
<td>$61,000</td>
<td>---</td>
</tr>
</tbody>
</table>

**Note:** If line 9 is zero, stop; you cannot take this credit.

**10** | Multiply line 7 by line 9. |
| **11** | Limitation based on tax liability. Enter the amount from the Credit Limit Worksheet in the instructions. |
| **12** | Credit for qualified retirement savings contributions. Enter the smaller of line 10 or line 11 here and on Form 1040, line 51; Form 1040A, line 34; or Form 1040NR, line 48. |

*See Pub. 590-A for the amount to enter if you are filing Form 2555, 2555-EZ, or 4563 or you are excluding income from Puerto Rico.

For Paperwork Reduction Act Notice, see your tax return instructions.

Cat. No. 33964D  Form 8880 (2015)
Form 8962

**Premium Tax Credit (PTC)**

2015

**Department of the Treasury**

**Internal Revenue Service**

**Sample Return No. 2 – Clergy-Employee for Income Tax Purposes (Nonaccountable Plan)**

**Name shown on your return:**

Donald L. Hall

**Social security number:**

482-11-6043

**You cannot claim the PTC if your filing status is married filing separately unless you are eligible for an exception (see instructions). If you qualify, check the box.**

**Part I Annual and Monthly Contribution Amount**

1 Tax family size. Enter the number of exemptions from Form 1040 or Form 1043A, line 6a, or Form 1404NR, line 7d.

<table>
<thead>
<tr>
<th>(a) Modified AGI</th>
<th>(b) Enter the total of your dependents modified AGI (see instructions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2a. Modified AGI</td>
<td>2b. Enter the total of your dependents modified AGI (see instructions)</td>
</tr>
<tr>
<td>Household income. Add the amounts on lines 2a and 2b.</td>
<td></td>
</tr>
<tr>
<td>Federal poverty line. Enter the federal poverty line amount from Table 1a, 1-2, or 1-3 (see instructions). Check the appropriate box for the federal poverty table used.</td>
<td></td>
</tr>
<tr>
<td>Other 48 states and DC</td>
<td></td>
</tr>
<tr>
<td>Household income as a percentage of federal poverty line (see instructions)</td>
<td></td>
</tr>
<tr>
<td>Did you enter 46% on line 5? (See instructions if you entered less than 100%)</td>
<td></td>
</tr>
</tbody>
</table>

**Part II Premium Tax Credit Claim and Reconciliation of Advance Payment of Premium Tax Credit**

<table>
<thead>
<tr>
<th>(b) Annual contribution amount</th>
<th>(b) Monthly contribution amount (divide line 6a by line 3)</th>
</tr>
</thead>
<tbody>
<tr>
<td>11. Annual Totals</td>
<td>559</td>
</tr>
<tr>
<td>12. January</td>
<td>559</td>
</tr>
<tr>
<td>13. February</td>
<td>559</td>
</tr>
<tr>
<td>14. March</td>
<td>559</td>
</tr>
<tr>
<td>15. April</td>
<td>559</td>
</tr>
<tr>
<td>16. May</td>
<td>559</td>
</tr>
<tr>
<td>17. June</td>
<td>559</td>
</tr>
<tr>
<td>18. July</td>
<td>559</td>
</tr>
<tr>
<td>19. August</td>
<td>559</td>
</tr>
<tr>
<td>20. September</td>
<td>559</td>
</tr>
<tr>
<td>21. October</td>
<td>559</td>
</tr>
<tr>
<td>22. November</td>
<td>559</td>
</tr>
<tr>
<td>23. December</td>
<td>559</td>
</tr>
<tr>
<td>Total annual premium</td>
<td>9,027</td>
</tr>
<tr>
<td>Monthly contribution amount</td>
<td>9,027</td>
</tr>
<tr>
<td>Monthly maximum premium assistance (minimum of all or 10)</td>
<td></td>
</tr>
<tr>
<td>Net premium tax credit. If line 24 is greater than line 25, subtract line 25 from line 24. Enter the difference here and on Form 1040, line 56; Form 1040A, line 15, or Form 1404NR, line 65. If you elected the alternative calculation for marriage, enter zero if line 24 equals line 25, enter [0]. Stop here if line 25 is greater than line 24, leave this line blank and continue to line 27.</td>
<td></td>
</tr>
</tbody>
</table>

**Part III Repayment of Excess Advance Payment of the Premium Tax Credit**

| Excess advance payment of PTC. If line 25 is greater than line 24, subtract line 24 from line 25. Enter the difference here |
| Repayment limitation (see instructions) |
| Excess advance premium tax credit repayment. Enter the smaller of line 27 or line 28 here and on Form 1040, line 48; Form 1040A, line 26; or Form 1404NR, line 44 |

For Paperwork Reduction Act Notice, see your tax return instructions.
Attachment 1.

**Computation of expenses, allocatable to tax-free ministerial income, that are nondeductible**

<table>
<thead>
<tr>
<th>Description</th>
<th>Taxable</th>
<th>Tax-Free</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Salary as a minister (less housing allowance designation and 403(b) contributions)</td>
<td>$ 8,500</td>
<td>$ 8,500</td>
<td></td>
</tr>
<tr>
<td>Special occasion gifts</td>
<td>500</td>
<td>500</td>
<td></td>
</tr>
<tr>
<td>Reimbursement of self-employment tax</td>
<td>2,100</td>
<td>2,100</td>
<td></td>
</tr>
<tr>
<td>Expense allowance under nonaccountable plan</td>
<td>1,700</td>
<td>1,700</td>
<td></td>
</tr>
<tr>
<td>Housing allowance:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Amount designated and paid by church</td>
<td>$ 2,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Actual expenses</td>
<td>1,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Taxable portion of allowance</td>
<td>$ 1,000</td>
<td>1,000</td>
<td>$ 1,000</td>
</tr>
<tr>
<td>Fair rental value of home (including furnishings and utilities)</td>
<td>11,150</td>
<td>11,150</td>
<td></td>
</tr>
<tr>
<td>Schedule C gross income from ministry</td>
<td>5,200</td>
<td></td>
<td>5,200</td>
</tr>
<tr>
<td>Ministerial income</td>
<td>$ 19,000</td>
<td>$ 12,150</td>
<td>$ 31,150</td>
</tr>
</tbody>
</table>

% of nondeductible expenses: $12,150/$31,150 = 39%

**Unreimbursed Employee Business Expenses**

<table>
<thead>
<tr>
<th>Description</th>
<th>61% Deductible</th>
<th>39% Not Deductible</th>
</tr>
</thead>
<tbody>
<tr>
<td>Business mileage:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>7,450 x 57.5¢ per mile</td>
<td>$ 2,613</td>
<td>$ 1,671</td>
</tr>
<tr>
<td>Travel expense:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Airfare</td>
<td>412</td>
<td>263</td>
</tr>
<tr>
<td>Lodging</td>
<td>102</td>
<td>65</td>
</tr>
<tr>
<td>Business expenses:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Subscriptions</td>
<td>122</td>
<td>78</td>
</tr>
<tr>
<td>Books and supplies</td>
<td>213</td>
<td>137</td>
</tr>
<tr>
<td>Continuing education tuition</td>
<td>305</td>
<td>195</td>
</tr>
<tr>
<td>Meals and entertainment expenses:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Meals</td>
<td>$ 233</td>
<td></td>
</tr>
<tr>
<td>Entertainment</td>
<td>1,207</td>
<td></td>
</tr>
<tr>
<td></td>
<td>$ 1,440 x 50% = $720</td>
<td>439  281</td>
</tr>
<tr>
<td>Form 2106-EZ</td>
<td>$ 4,206</td>
<td>$2,690</td>
</tr>
</tbody>
</table>

**Attachment 2.**

**Net earnings from self-employment (attachment to Schedule SE, Form 1040)**

<table>
<thead>
<tr>
<th>Description</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Salary paid by church as reflected on Form W-2, Box 1</td>
<td>$ 12,800</td>
</tr>
<tr>
<td>Net profit or loss as reflected on Schedule C or C-EZ (includes speaking honoraria, offerings you receive for weddings, baptisms, funerals, and other fees)</td>
<td>2,520</td>
</tr>
<tr>
<td>Housing allowance excluded from salary on Form W-2</td>
<td>2,000</td>
</tr>
<tr>
<td>Fair rental value of church-provided housing (including paid utilities)</td>
<td>11,150</td>
</tr>
<tr>
<td>Less:</td>
<td>28,470</td>
</tr>
<tr>
<td>Unreimbursed ministerial business and professional expenses or reimbursed expenses paid under a nonaccountable plan</td>
<td></td>
</tr>
<tr>
<td>A. Deductible on Schedule A before the 2% of AGI limitation</td>
<td>4,206</td>
</tr>
<tr>
<td>B. Not deductible on Form 2106/2106 EZ ($2,690) or Schedule C/C-EZ ($1,714) because expenses were allocated to taxable/nontaxable income</td>
<td>4,404</td>
</tr>
<tr>
<td><strong>Total deductions</strong></td>
<td>8,610</td>
</tr>
<tr>
<td>Net earnings from self-employment (to Schedule SE) (See page 50)</td>
<td>$ 19,860</td>
</tr>
</tbody>
</table>
### Housing Allowance Worksheet

**Clergy Living in Housing**  
**Owned or Rented by the Congregation**

**Name:** Donald L. Hall  
**For the period:** January 1, 2015 to December 31, 2015  
**Date designation approved:** December 20, 2014

#### Allowable Housing Expenses  
*expenses paid from current income*

<table>
<thead>
<tr>
<th>Estimated Expenses</th>
<th>Actual</th>
</tr>
</thead>
<tbody>
<tr>
<td>Utilities (gas, electricity, water) and trash collection</td>
<td>$ ____________</td>
</tr>
<tr>
<td>Local telephone expense <em>(base charge)</em></td>
<td>250</td>
</tr>
<tr>
<td>Decoration and redecoration</td>
<td>____________</td>
</tr>
<tr>
<td>Structural maintenance and repair</td>
<td>____________</td>
</tr>
<tr>
<td>Landscaping, gardening, and pest control</td>
<td>____________</td>
</tr>
<tr>
<td>Furnishings <em>(purchase, repair, replacement)</em></td>
<td>1,218</td>
</tr>
<tr>
<td>Personal property insurance on minister-owned contents</td>
<td>200</td>
</tr>
<tr>
<td>Personal property taxes on contents</td>
<td>150</td>
</tr>
<tr>
<td>Umbrella liability insurance</td>
<td>____________</td>
</tr>
<tr>
<td><strong>Subtotal</strong></td>
<td>1,818</td>
</tr>
<tr>
<td>10% allowance for unexpected expenses</td>
<td>182</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>$ 2,000</td>
</tr>
</tbody>
</table>

The amount excludable from income for federal income tax purposes is the lower of A or B.

---

Because actual housing expenses are less than the designated allowance, the housing exclusion is limited to $1,000. The $1,000 difference between the designation and the exclusion is reported as excess housing allowance on Form 1040, line 7 (see page 47).
Explanation of compensation reported on Form W-2, Box 1:
Salary ($11,000 less $2,000 housing allowance and
$500 403[b] contributions) $ 8,500
Special occasion gifts 500
Reimbursement of self-employment tax 2,100
Expense allowance under nonaccountable plan 1,700
$12,800
2016 Filing Dates

January
15 Quarterly Estimated Taxes (last payment for prior tax period)

February
18 W-4 (if claimed an exemption, to continue same exemption in current year)

April
15 Personal tax returns due
15 Quarterly Estimated Taxes, if not paid with return (first payment for current tax year)

June
15 Quarterly Estimated Taxes (2nd payment for current tax year)

September
15 Quarterly Estimated Taxes (3rd payment for current tax year)

October
15 If you had an automatic extension to file your individual income tax return, it is now due
The Tax System for Clergy

- Employees v. self-employed for income tax purposes
  Treas. Reg. 31.3401(c)-1(b)-(c)
  Shelley v. Commissioner, T.C.M. 432 (1994)
  Rev. Rul. 87-41
- Exempt from income tax withholding
  Code Sec. 3401(a)(9)
- Qualifying tests for ministerial status
  Treas. Reg. 1.1402(c)-5
  Ltr. Rul. 199910055
  Mosley v. Commissioner, T.C.M. 457 (1994)
- Voluntary withholding of income tax for clergy
  Rev. Rul. 68-507

The Housing Allowance

- Designation of housing allowance
  Treas. Reg. 1.107-1(b)
  Whittington v. Commissioner, T.C.M. 296 (2000)
  Mosley v. Commissioner, T.C.M. 457 (1994)
- Determination of housing exclusion amount
  Clergy Housing Allowance Clarification Act, Public Law 107-181
  Appeal to the Ninth Cir. Court of Appeals (Feb. 2000), case dismissed by Ninth Cir. Court of Appeals (Aug. 2002)
- Housing allowances for retired clergy
  Rev. Proc. 92-3
  Rev. Rul. 75-22

Compensation and Fringe Benefits

- 403(b) plans
  Code Sec. 403(b)
  Code Sec. 1402(a)
- Healthcare flexible spending account
  Code Sec. 105(b), (e)
- Health reimbursement arrangements
  Code Sec. 105(b), (e)
  Rev. Rul. 2002-41
  IRS Notice 2002-45
  IRS Policy 80,600
- Health savings accounts
  Code Sec. 233
  IRS Notice 2004-2
  IRS Notice 2004-23
  Rev. Rul. 2004-38
  IRS Notice 2004-50
- Highly compensated employees
  Code Sec. 414(q)
  Treas. Reg. 1.132-8(f)(1)
- Medical insurance premiums paid by the congregation
  Code Sec. 106(a)
  Code Sec. 4980B
- Nontaxable fringe benefits
  Code Sec. 132
- Property transfers
  Treas. Reg. 1.61-2(d)(2)
- Reimbursement payments excludable from recipient’s income
  Letter Ruling 9112022
- Sabbatical Pay
  Kant v. Commissioner,

Social Security Taxes

- Opting out of social security
  Code Sec. 1402(e)
  Treas. Reg. 1.1402(e)-3A
- Social security coverage for clergy
  Code Sec. 1402(c)(2) and (4)
  Code Sec. 3121(b)(8)(A)
  Code Sec. 3401(a)(9)
  Rev. Rul. 80-110

Business and Professional Expenses

- Accountable expense reimbursement plans
  Treas. Reg. 1.62-2
  Treas. Reg. 1.274-5T(f)
- Allocation of unreimbursed business expenses
  McFarland v. Commissioner, T.C.M. 440 (1992)
  Dalan v. Commissioner, T.C.M. 106 (1988)
  Deason v. Commissioner, 41 T.C. 465 (1964)
- Educational expenses
  Ltr. Rul. 9431024
  Burt v. Commissioner, 40 T.C.M. 1164 (1980)
- Personal computer expenses
  Code Sec. 280F
  Rev. Rul. 86-129
- Traveling/commuting
  Rev. Rul. 94-47
  Rev. Rul. 90-23
  Walker v. Commissioner, 101 T.C.M. 537 (1993)

Social Security Taxes

- Opting out of social security
  Code Sec. 1402(e)
  Treas. Reg. 1.1402(e)-3A
- Social security coverage for clergy
  Code Sec. 1402(c)(2) and (4)
  Code Sec. 3121(b)(8)(A)
  Code Sec. 3401(a)(9)
  Rev. Rul. 80-110

Social Security Taxes

- Opting out of social security
  Code Sec. 1402(e)
  Treas. Reg. 1.1402(e)-3A
- Social security coverage for clergy
  Code Sec. 1402(c)(2) and (4)
  Code Sec. 3121(b)(8)(A)
  Code Sec. 3401(a)(9)
  Rev. Rul. 80-110
Accountable plan, 18, 24-25, 36-45
Administrative positions, 8
Allocation of business expenses, 29, 43, 61
Automobiles,
   Actual expense method, 26
   Church-provided, 21
   Commuting, 26-27
   Depreciation, 26
   Documenting expenses, 27
   Mileage rate, 6, 26
Books, 27
Business and professional expenses,
   Accounting for, 18, 24-25, 36-45
   Allocation of, 29, 43, 61
   Automobile, 26-27
   Books, 28
   Business gifts, 27
   Cellular phones, 28-29
   Club dues, 18
   Commuting, 26-27
   Documenting, 25
   Educational expenses, 19
   Entertainment expenses, 19, 27
   Gifts, 27
   Mileage rate, 6, 26
   Moving expenses, 6, 46, 47
   Personal computers, 27-28
   Recordkeeping requirements, 25, 27
   Reimbursements, 18, 24-25
   Subscriptions and books, 28
   Telephone, 28-29
Cellular phones, 28-29
Child tax credit, 48, 54-55
Club dues, 18
Commuting expenses, 26-27
Computers, 28-29
Continuing education, 19
Denominational,
   Positions, 8
   Retirement plans, 14-15
Disability insurance, 18, 19
Dues and memberships, 18
Earned income credit, 51-53
Educational reimbursement plans,
   19
Employee v. self-employed, 8-10
Entertainment expenses, 19, 27
Estimated taxes, 30, 34
Evangelists, 10
Fair rental value, 12-14
Flexible spending account, 6, 19-20
Fringe benefits, 18-23
Gifts,
   Business, 27
Health care reform, 3-4
Health insurance, 3-4, 20
Health insurance deduction, 9
Health reimbursement arrangement,
   3-4, 20
Health Savings Accounts, 20-21, 33
Housing allowance,
   Accounting for, 12-13
   Designating, 13
   Equity allowance, 12
   Fair rental value, 12-14
   General, 5, 11-17
   Limitations, 11-12
   Reporting, 13, 32
   Resolutions, 15
   Retirees, 14-15
   Worksheets, 16-17
Income tax status of ministers, 9-10
Insurance,
   Disability, 18-19
   Group term life, 10, 21
   Health, 3-4, 20
Interest,
   Paid, 35
   Received, 32-33
Life insurance, 10, 21
Mileage rate, 6, 26
Missionaries, 10
Moving expenses, 6, 47
Nonaccountable plan, 25, 46-63
Overtime, 5
Pension distributions, 14-15
Per diem, 6, 27
Personal computers, 27-28
Reimbursements, 18, 24-25, 36-45
Retirement plans,
   Denominational plans, 14-15
Section 179 deductions, 28
Self-employment earnings, 31
Self-employment tax deductions, 31
Social security,
   Computation of tax, 31
   Deductions, 31
   Exemption of ministers, 31
   Opting out, 31
   Reimbursement, 21
   Services in which exemption applies,
      31
   Status of ministers, 8-9
   Tax rates, 31
Standard mileage rate, 6, 26
Substantiation,
   Business and professional expenses,
      24-25, 24-28
Tax rates
   Self-employment rates, 31
Tax withholding, 30
Teaching positions, 8
Telephone, 28-29
Transportation expenses, 27
Tuition discounts, 21
Unreimbursed business and professional expenses, 25, 46-63
Vehicles, personal use of church-owned, 21
Withholding,
   Voluntary, 10, 30

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1. Improperly treating congregation payments for out-of-pocket medical expenses as tax-free when the congregation has not established a proper plan.

2. Filing as self-employed for income tax purposes on your congregation salary, using tax benefits only available to employees, and leaving yourself vulnerable to reclassification by the IRS to employee status upon audit.

3. Failing to have at least a modest housing allowance designated when living in a congregation-provided housing.

4. Failure to understand and apply the fair rental test for the housing allowance relating to clergy-provided housing.

5. Confusing the fair rental value of a congregation-provided parsonage (only includible for social security purposes) with the designation of a portion of your salary as housing allowance (providing an exclusion for income tax purposes).

6. Failing to keep a log of miles driven for personal use v. congregation purposes.


8. Not documenting business expenses to reflect business purpose, business relationship, cost, time, and place.

9. Failure of clergy to use an accountable reimbursement plan.

10. Improperly opting out of social security because you don’t believe it is a good investment.
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