

**FINANCE AND ADMINISTRATION TEAM
EVANGELICAL FRIENDS CHURCH EASTERN REGION**

CHURCH GUIDELINES FOR PASTOR/CLERGY COMPENSATION

This document is not meant to be legal advice but merely as a guideline to our local churches. Please consult the resources listed or a church/clergy tax professional for additional information.

- 1) A pastor/clergy is considered a dual status employee. They are self employed for social security purposes and an employee for income tax purposes. The church can withhold income taxes (voluntary) but cannot withhold or match social security or medicare. The clergy must pay this him/her self by quarterly deposits or have the church increase the amount of federal income tax withheld. See no. 7. If the church reimburses any portion of their social security tax it must be included in the wage/income portion on Form W01

- 2) The churches issues a W-2 at the end of the year reporting salary amount but not housing allowance in the wage box. Housing Allowance may be reported in the other box. The church also only reports the salary amounts on quarterly 941s. **The church is considered an employer for income tax purposes and should not issue a 1099 to pastor/clergy.**

- 3) *A housing allowance amount/portion must be designated and minuted by the congregational meeting in advance of the calendar year but need not be a separate line item in the budget. This should include all allowable expenses in maintaining a home. This amount can be revised during the year but must be designated and minuted.*

IRS PUBLICATION 517 -Designation requirement. The church or organization that employs you must officially designate the payment as a housing allowance before it makes the payment. It must designate a definite amount. It can't determine the amount of the housing allowance at a later date. If the church or organization doesn't officially designate a definite amount as a housing allowance, you must include your total salary in your income. If you are employed and paid by a local congregation, a resolution by a national church agency of your denomination doesn't effectively designate a housing allowance for you. The local congregation must officially designate the part of your salary that is a housing allowance. However, a resolution of a national church agency can designate your housing allowance if you are directly employed by the national agency. An official designation of an amount as a housing or rental allowance may be shown in an employment contract, in the minutes of a church or qualified organization, in a budget, or in any official action taken in advance of payment of the allowance. A designation is sufficient if it permits a payment to be identified as a payment of a rental or housing allowance as distinguished from salary or other remuneration. Informal discussions don't amount to an official designation. However, the facts and circumstances of a designation may demonstrate that the designation was official.

Churches are not required to receive documentation/verification of expenses from the pastor. This is the pastor's responsibility on their individual income tax return.

4) The church should adopt an accountable reimbursement plan with the amount declared in advance of the calendar year and should be a separate line item apart from the salary and housing. Professional expenses that are allowed include tuition, books, subscriptions, gifts, mileage, etc. Mileage to and from the church is not allowed because of the Pastor's dual stats. Expenses must be documented and submitted for reimbursement within 60 days or any excess advance/lump sum be returned in 120 days to be accountable and non taxable. Accountable professional expenses are not included or reported on the W-2 do not have to be calculated at tax time.

IRS PUBLICATION 517 Accountable plans. To be an accountable plan, your employer's reimbursement arrangement must include all three of the following rules. • Your expenses must have a business connection—that is, you must have paid or incurred deductible expenses while performing services as an employee of your employer. • You must adequately account to your employer for these expenses within a reasonable period of time. • You must return any excess reimbursement or allowance within a reasonable period of time. The reimbursement isn't reported on your Form W-2. Generally, if your expenses equal your reimbursement, you have no deduction. If your expenses are more than your reimbursement, you can deduct your excess expenses for SE tax and income tax purposes.

Health Reimbursement Plans may be available for pastors/clergy On June 20, 2019, the Internal Revenue Service, the Department of the Treasury, the Department of Labor and the [Department of Health and Human Services](#) issued final rules regarding health reimbursement arrangements (HRAs) and other account-based group health plans. Specifically, the final rules allow HRAs and other account-based group health plans to be integrated with individual health insurance coverage or Medicare, if certain conditions are satisfied (an individual coverage HRA). The final rules also set forth conditions under which certain HRAs and other account-based group health plans will be recognized as limited excepted benefits (an excepted benefit HRA).

5) Monetary pastor appreciation, Christmas gifts/church bonuses, etc, should be recorded as income and included on the W-2 wages.

6) If the pastor receives other income directly from congregants or other sources such as honorariums for weddings, etc. this should be included as "Other income" on Schedule C on the pastor's personal tax return. The church has no responsibility in tracking these. Only associated expenses can be deducted on Sch C.

7) The social security base includes salary amount from W-2, housing allowance and net profit (if any) from Schedule C. If the housing allowance exceeds actual housing expenses, this is reported as additional income on the income tax return as "excess parsonage allowance. The pastor may report mortgage interest deduction on Schedule A even though it is part of the Housing allowance. This "double deduction" is allowed to offset the full Social Security self employed tax rate.

8) The church must comply with state and local tax laws regarding withholding and paying taxes on the salary and housing amounts. For example, in Ohio Workers Compensation is paid on both salary and housing and clergy must be named under Elective Coverage.

Additional information can be found in
IRS Publication 517

2022 Church and Clergy Tax Guide – Richard Hammar (Church Law and Tax)
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