

TaxBrief

Keeping you informed

Tax Tips for the Clergy

Members of the clergy face a unique set of tax rules that differ significantly from those that apply to most other taxpayers. Understanding these complexities is essential for taking full advantage of the tax benefits available.

Who qualifies as clergy for tax purposes?

The tax code and IRS refer to clergy members as ministers and define them as individuals who are duly ordained, commissioned or licensed by a religious body constituting a church or church denomination.

To qualify as a minister, an individual must have the authority to conduct religious worship, perform sacerdotal functions and administer ordinances or sacraments according to the tenets and practices of their church or denomination. In certain cases, individuals who serve as ordained deacons, ministers of music or ministers of education may qualify if they perform a full range of ministerial duties.

Church employee or self-employed?

For tax purposes, it matters whether a minister is employed by a church or self-employed. Generally, those who perform services for a church that have the legal right to control what they do and how they do it are employees of the church, even if they have significant discretion and freedom of action. If the congregation pays the minister wages, those wages are subject to the federal income tax and withholding rules.

Ministers who receive funding directly from the congregation, such as fees for performing marriages or baptisms, are generally considered to have earned income from self-employment, even if they are a church employee. They are subject to the 15.3% self-employment tax, which covers their Social Security and Medicare obligations.

Individuals who are opposed to certain public insurance for religious or conscientious reasons can request an exemption from the self-employment tax for their earnings as a minister. To request an exemption, file Form 4361, *Application for Exemption From Self-Employment Tax for Use by Ministers, Members of Religious Orders and Christian Science Practitioners with the IRS*, by the date your income tax return is due for the second tax year in which you have net earnings from self-employment of at least \$400. If the IRS approves your application, you will be granted an exemption from the self-employment tax that can't be revoked.

What is the parsonage exclusion?

One of the primary benefits ministers have through the federal tax code is their right to exclude their parsonage allowance from their gross income. This means that ministers will not be taxed on the rental value of a home provided as part of their compensation from their church or a rental allowance.

The rental allowance can't exceed the fair rental value of the home, including furnishings and utilities. Fair rental value, according to the IRS, is the amount of rent you could reasonably expect to receive from an unrelated tenant for a property that is comparable to yours in the same market.

For a minister to claim the parsonage exclusion, the housing allowance must be officially designated in advance by the church employing the minister. This is usually done by including the amount in the minister's employment contract or the church budget. The minister must also use the designated amount to obtain or rent a home.

The parsonage exclusion is limited to the lesser of:

- The amount actually used to provide a home
- The amount officially designated as a housing allowance
- The fair rental value of the home (including furnishings and utilities)

In addition to claiming the parsonage allowance, ministers may claim payments for mortgage interest and property taxes as itemized deductions.

What expenses does the parsonage exclusion cover?

Ministers may apply the parsonage exclusion for amounts spent for:

- Mortgage payments
- Down payments
- Utilities
- Maintenance and repairs
- Furnishings
- Insurance
- Property taxes

The exclusion does not cover payments that exceed the amount used to provide a home, the official designated housing allowance or the home's fair rental value.

Deductible business expenses

Ministers are only allowed to deduct business expenses from their income if they receive income from self-employment. Most business expenses are not deductible for income tax purposes.

Items that may be deductible for self-employment tax purposes include:

- Vehicle expenses when driving on ministerial business (you must keep mileage logs)
- Cost of vestments, including laundering and dry cleaning
- Travel expenses if you are required to be away for longer than an ordinary day's work
- Meals directly related to business travel
- Costs of attending meetings and seminars related to your work as a minister

- Office supplies and equipment required for work
- Cell phone costs related to conducting church business
- Health insurance premiums up to the amount of your net self-employment income if neither you nor your spouse is eligible for employer-sponsored coverage

Special issues for members of religious orders and sects

Members of religious orders who have taken a vow of poverty and perform services as agents of their order are generally exempt from income and self-employment taxes because their income is considered to be that of the order. However, any income they receive for work outside of the order is subject to income tax.

Members of certain religious sects, such as the Amish or Mennonites, may apply for an exemption from Social Security and Medicare taxes if they are conscientiously opposed to public insurance and meet other requirements.

Still have questions? We can help.

If you have questions related to the tax issues faced by clergy members, we can help provide answers and ensure that you are receiving the tax benefits to which you are entitled and not paying more than you should.

