

Ministers' Tax Guide for 2016 Returns



2017

**TAX RETURN
PREPARATION
GUIDE**

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GuideStone®

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This publication is intended to provide a timely, accurate, and authoritative discussion of tax reporting compliance and the impact of recent changes in the tax laws. It is not intended as a substitute for legal, accounting, or other professional advice. If legal, tax, or other expert assistance is required, the services of a competent professional should be sought. Although we believe this book provides accurate information, there may be changes resulting from IRS or judicial interpretations of the tax code, new tax regulations, or technical corrections that occurred after the printing of this edition that are not reflected in the text.



Welcome to the 2017 *Ministers' Tax Return Preparation Guide for 2016 Returns (Ministers' Tax Guide)*, written exclusively for ministers by noted CPA and attorney Richard Hammar.

One of our great joys is to serve as an advocate on behalf of our participants; as part of that commitment, we're privileged once again to provide you with this useful guide to help as you prepare your federal income tax forms.

We know that ministerial tax preparation can be complicated. While this book addresses the most commonly asked questions and most commonly used forms, you can find more extensive information on the IRS website, *IRS.gov*. For specific tax advice, you'll want to consult an accountant or an attorney who is familiar with the intricacies of ministerial taxes.

Additional copies of this free booklet may be obtained by visiting *GuideStone.org/TaxGuide* or by calling our Customer Solutions department at **1-888-98-GUIDE** (1-888-984-8433), weekdays from 7 a.m. to 6 p.m. CST.

Once again, we are thankful to serve you with this annual *Ministers' Tax Guide*, and we hope it will be a great resource for you. May God bless you in the ministry He has assigned to you!

Sincerely,

A handwritten signature in black ink, appearing to read "O.S. Hawkins". The signature is fluid and cursive, with a long horizontal stroke extending to the right.

O.S. Hawkins
President

GuideStone Financial Resources of the Southern Baptist Convention

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Special Supplement

CURRENT STATUS OF THE PARSONAGE AND HOUSING ALLOWANCE EXCLUSIONS

By Richard R. Hammar, J.D., LL.M., CPA

On November 22, 2013, federal district court judge Barbara Crabb of the District Court for the Western District of Wisconsin struck down the ministerial housing allowance as an unconstitutional preference for religion (*Freedom From Religion Foundation, Inc., v. Lew*, 983 F. Supp.2d 1051 (W.D. Wis. 2013)). The ruling was in response to a lawsuit brought by the Freedom From Religion Foundation (FFRF) and two of its officers challenging the constitutionality of the housing allowance and the parsonage exclusion. The federal government, which defended the housing allowance since it is a federal statute, asked the court to dismiss the lawsuit on the ground that the plaintiffs lacked standing to pursue their claim in federal court.

Standing is a constitutional requirement of any plaintiff in a federal case and generally means that a plaintiff must have suffered some direct injury as a result of a challenged law. The Wisconsin court concluded that the plaintiffs had standing on the ground that they would have been denied a housing allowance exclusion had they claimed one on their tax return. The government appealed this ruling to a federal appeals court — the Seventh Circuit Court of Appeals in Chicago.

On November 13, 2014, the appeals court issued its ruling reversing the Wisconsin court's decision (*Freedom From Religion Foundation, Inc., v. Lew*, 2014 WL 5861632 (7th Cir. 2014)). It concluded that the plaintiffs lacked standing to pursue their challenge to the housing allowance. The plaintiffs had asserted that they had standing due to their "injury" of being denied a tax-free housing allowance should they claim one on their tax returns. But the appeals court refused to base standing on theoretical injury. It concluded: "Only a person that has been denied such a benefit can be deemed to have suffered cognizable injury. The plaintiffs here have never been denied the parsonage exemption because they have never requested it; therefore, they have suffered no injury."

It suggested that this deficiency could be overcome if the FFRF's officers filed tax returns claiming a housing allowance that was later rejected by the IRS in an audit: "The plaintiffs could have sought the exemption by excluding their housing allowances from their reported income on their tax returns and then petitioning the Tax Court if the IRS were to disallow the exclusion. Alternatively, they could have paid income tax

on their housing allowance, claimed refunds from the IRS, and then sued if the IRS rejected or failed to act upon their claims."

The FFRF responded to the appeals court's ruling by designating a housing allowance for two of its officers. The officers reported their allowances as taxable income on their tax returns and thereafter filed amended tax returns seeking a refund of the income taxes paid on the amounts of their designated housing allowances. FFRF claims that in 2015 the IRS denied the refunds sought by its officers (one of whom had died and was represented by her executor).

Having endeavored to correct the standing problem, the FFRF renewed its legal challenge to the housing allowance in the federal district court in Wisconsin where the litigation began. Note the following considerations:

(1) Parsonages

The U.S. Department of Justice, which defends the constitutionality of federal legislation (such as the housing allowance), filed a brief with the Wisconsin federal district court asking it to dismiss FFRF's challenge to the constitutionality of the parsonage exclusion. The Department of Justice noted that section 107 of the tax code grants tax exclusions both for the rental value of parsonages provided to clergy as compensation for the performance of ministerial services and for housing allowances provided to clergy who own or rent their home. But, since none of FFRF's officers was living in housing owned by FFRF, they lacked standing to challenge the constitutionality of section 107's exclusion of the rental value of church-owned parsonages.

(2) Housing allowances

The Department of Justice brief states that "the United States does not contest plaintiffs' standing to sue under section 107(2)" (i.e., the housing allowance). This concession means that the federal appeals court will now have the opportunity to address the merits of FFRF's constitutional challenge to the housing allowance. The appeals court ultimately may rule that the housing allowance is constitutional. Or it may decide that it is not. Either way, the ruling likely will be appealed to the United States Supreme Court.

(3) Constitutionality

There are arguments that support the constitutionality of the parsonage exclusion and housing allowance. The validity and strength of these arguments will now be evaluated by the federal district court in Wisconsin and the Seventh Circuit Court of Appeals.

(4) Impact of the loss of the housing allowance exclusion

What would be the impact if the FFRF and its officers ultimately prevail in their quest to strike down the housing allowance as an unconstitutional preference for religion? A ruling by the Seventh Circuit Court of Appeals would apply to ministers in that circuit, which includes the states of Illinois, Indiana and Wisconsin. It would become a national precedent binding on ministers in all states if affirmed by the United States Supreme Court — an unlikely outcome because the Supreme Court accepts less than 1 percent of all appeals. Note, however, that the IRS would have the discretion to follow or not follow such a ruling in other circuits and might be inclined to follow it to promote consistency in tax administration.

In conclusion, ministers and churches should be aware that the housing allowance remains under attack and one day may be invalidated. Should that occur, two actions will need to be implemented quickly:

First, most ministers will experience an immediate increase in income taxes. As a result, they should be prepared to increase their quarterly estimated tax payments to reflect the increase in income taxes in order to avoid an underpayment penalty. Note that there will be no effect on self-employment taxes for which the housing allowance is not tax-exempt.

Second, many churches will want to increase ministers' compensation to offset the financial impact. Such an increase could be phased out over a period of years to minimize the impact on the church.

 **Key Point:** Ministers should address the continuing availability of the housing allowance with a tax professional.

All references in this publication to line numbers on IRS forms are for the draft versions of the 2016 forms; the final forms had not been released by the IRS as of the date of initial publication.

HOW TO USE THIS GUIDE

This book contains the basic information you need to complete your 2016 federal income tax return. It gives special attention to several forms and schedules and the sections of each form most relevant to ministers. The companion resource — *Federal Reporting Requirements for Churches* — helps churches comply with their federal tax reporting requirements and is available at GuideStone.org/FederalReportingRequirements as a downloadable document.

Key Point: In the closing days of 2015, Congress passed a massive spending bill (Consolidated Appropriations Act of 2016) to fund the federal government through the end of fiscal year 2016 and a tax bill (Protecting Americans from Tax Hikes Act of 2015, or the PATH Act) that, among other things, extended several expiring tax provisions, in some cases permanently. The key provisions are noted throughout this text.

This guide is divided into the following sections:

- **Part 1: Introduction** — This section reviews tax highlights for 2016 and presents several preliminary questions you should consider before preparing your tax return.
- **Part 2: Special Rules for Ministers** — In this section, you learn whether you are a Minister for Tax Purposes, an employee or self-employed for both income tax and Social Security purposes, and how you pay your taxes.
- **Part 3: Step-by-Step Tax Return Preparation** — This section explains how to complete the most common tax forms and schedules for ministers.
- **Part 4: Comprehensive Examples and Forms** — This section shows a sample tax return prepared for an active minister and spouse and for a retired minister and spouse.
- **Federal Reporting Requirements for Churches** — This resource provides assistance to churches (especially treasurers and bookkeepers) in filing federal tax forms.

TAX HIGHLIGHTS FOR 2016

1. Temporarily extend the American Opportunity Tax Credit

The American Opportunity Tax Credit is available for up to \$2,500 of the cost of tuition and related expenses paid during the taxable year. Under this provision, taxpayers receive a tax credit based on 100 percent of the first \$2,000 of tuition and related expenses (including course materials) paid during the taxable year and 25 percent of the next \$2,000 of tuition and related expenses paid during the taxable year. Forty percent of the credit is refundable. This tax credit is subject to a phase-out for taxpayers with adjusted gross income (AGI) in excess of \$80,000 (\$160,000 for married couples filing jointly).

In 2012, Congress extended the American Opportunity Tax Credit for five additional years, through 2017. The PATH Act of 2015 made this credit permanent.

2. Temporarily extend the “third-child” Earned Income Tax Credit (EITC)

In 2012, Congress extended for five additional years, through 2017, the 2009 enhancements that increased the EITC for families with three or more children and increased the phase-out range for all married couples filing a joint return. The PATH Act of 2015 made these enhancements permanent.

3. Deduction for certain expenses of elementary and secondary school teachers

In 2012, Congress extended for two years the \$250 above-the-line tax deduction for teachers and other school professionals for expenses paid or incurred for books, supplies (other than non-athletic supplies for courses of instruction in health or physical education), computer equipment (including related software and service), other equipment and supplementary materials used by the educator in the classroom.

This provision expired at the end of 2014, but was made permanent for 2015 and future years by the PATH Act of 2015. The Act also indexes the \$250 maximum deduction amount for inflation and provides that expenses for professional development are also eligible expenses for purposes of the deduction. However, the provisions pertaining to indexing the \$250 maximum deduction amount and qualifying professional development expenses apply to taxable years beginning after December 31, 2015.

4. Deduction for state and local general sales taxes

Congress enacted legislation in 2004 providing that, at the election of the taxpayer, an itemized deduction may be taken for state and local general sales taxes in lieu of the itemized deduction for state and local income taxes. This provision was added to address the unequal treatment of taxpayers in the nine states that assess no income tax. Taxpayers in these states cannot take advantage of the itemized deduction for state income taxes. Allowing them to deduct sales taxes helps offset this disadvantage.

This provision expired at the end of 2014 but was made permanent for 2015 and future years by the PATH Act.

5. Above-the-line deduction for qualified tuition-related expenses

In the past, taxpayers could claim an above-the-line tax deduction for qualified higher education expenses. The maximum deduction was \$4,000 for taxpayers with AGI of \$65,000 or less (\$130,000 for joint returns) or \$2,000 for taxpayers with AGI of \$80,000 or less (\$160,000 for joint returns).

This deduction expired at the end of 2014 but was reinstated by the PATH Act for 2015 and extended through 2016.

6. Tax-free distributions from individual retirement plans for charitable purposes

Congress enacted legislation in 2006 allowing tax-free qualified charitable distributions of up to \$100,000 from an Individual Retirement Account (IRA) to a church or other charity. Note the following rules and conditions:

- A qualified charitable distribution is any distribution from an IRA directly by the IRA trustee to a charitable organization, including a church, that is made on or after the date the IRA owner attains age 70½.
- A distribution will be treated as a qualified charitable distribution only to the extent that it would be includible in taxable income without regard to this provision.
- This provision applies only if a charitable contribution deduction for the entire distribution would be allowable under present law, determined without regard to the generally applicable percentage limitations. For example, if the deductible amount is reduced because the donor receives a benefit in exchange for the contribution of some or all of his or her IRA, or if a deduction is not allowable because the donor did not have sufficient substantiation, the exclusion is not available with respect to any part of the IRA distribution.

This provision expired at the end of 2014 but was made permanent for 2015 and future years by the PATH Act of 2015.

7. The Affordable Care Act

Those provisions of the Affordable Care Act that involve taxation, that have the greatest relevance to churches and church staff, and that affect tax reporting in 2016 or future years are summarized below.

- One of the most important and divisive provisions in the legislation is a requirement that, beginning in 2014, applicable individuals are required to maintain minimum essential health care coverage or pay a penalty. A requirement that persons failing to provide such coverage would be subject to imprisonment was dropped during final consideration. Failure to maintain minimum essential health care coverage will result in a penalty of the greater of 2.5 percent of household income, or \$695 per adult and \$347.50 per child, to a maximum of \$2,085 over a filing threshold for 2016. For tax year 2017, the penalty remains the same as 2016.
- The ACA imposed new health care reporting obligations on providers of health care coverage and applicable large employers (ALEs) (generally employers with 50 or more full-time employees, including full-time equivalent employees). These reporting obligations are summarized below.
 - (1) Providers of minimum essential coverage are required to file *Forms 1094-B* and *1095-B* for 2016. *Forms 1094-B* and *1095-B* are used to report certain information to the IRS and to employees about individuals who are covered by minimum essential coverage and therefore aren't liable for the individual shared responsibility payment.
 - (2) ALEs must provide each employee with *Form 1095-C* to evidence whether the employer has made offers of health coverage and/or enrollment in health coverage. Copies of *Forms 1095-C* are filed with the IRS through transmittal *Form 1094-C*.
 - (3) The employee retains *Forms 1095* for tax records.

These new reporting requirements are addressed further in the *Federal Reporting Requirements for Churches* located on the GuideStone website.

8. Other tax changes of interest to churches and church staff

There were several tax developments in 2016 that will affect tax reporting by both ministers and churches for 2016 and future years. Here is a rundown of some of the key provisions:

- You may be able to claim the earned income credit for 2016 if (1) you do not have a qualifying child and you earned less than \$14,880 (\$20,430 if married filing jointly); (2) a qualifying child lived with you and you earned less than \$39,296 (\$44,846 if married filing jointly); (3) two qualifying children lived with you and you earned less than \$44,648 (\$50,198 if married filing jointly); or (4) three or more qualifying children lived with you and you earned less than \$47,955 (\$53,505 if married filing jointly). The maximum earned income credit for 2016 is (1) \$506 with no qualifying child; (2) \$3,373 with one qualifying child; (3) \$5,572 with two qualifying children; and (4) \$6,269 with three or more qualifying children.
- For contributions to a Traditional IRA, the deduction phase-out range for an individual covered by a retirement plan at work begins at income of \$99,000 for joint filers and \$62,000 for a single person or head of household.
- The dollar limit on annual elective deferrals an individual may make to a 403(b) retirement plan is \$18,000 for 2016. It remains at \$18,000 for 2017.
- The catch-up contribution limit on elective deferrals to a 403(b) retirement plan for individuals who had attained age 50 by the end of the year was \$6,000 for 2016. It remains at \$6,000 for 2017.
- The IRS has announced that it will not issue private letter rulings addressing the question of “whether an individual is a minister of the gospel for federal tax purposes.” This means taxpayers will not be able to obtain clarification from the IRS in a letter ruling on their status as a minister for any one or more of the following matters: (1) eligibility for a parsonage exclusion or housing allowance; (2) eligibility for exemption from self-employment taxes; (3) self-employed status for Social Security; or (4) exemption of wages from income tax withholding. The IRS also has announced that it will not address “whether amounts distributed to a retired minister from a pension or annuity plan should be excludible from the minister’s gross income as a parsonage allowance.”
- The suggested business mileage reimbursement rate for 2016 was 54 cents per mile for business miles driven.
 - ✓ **New in 2017.** The standard business mileage rate for 2017 is 53.5 cents per mile.
- The IRS maintains that a minister’s housing allowance is earned income in determining eligibility for the earned income credit for ministers who have not opted out of Social Security by filing a timely *Form 4361*. For ministers who have opted out of Social Security, the law is less clear, and the IRS has not provided guidance.
- Be sure your estimated tax calculations or withholdings take into account the most recent tax law changes.
- For 2016, the following inflation adjustments took effect:
 - The amount of income needed to reach a higher tax rate was adjusted for inflation.
 - The value of each personal and dependency exemption, available to most taxpayers, increased to \$4,050.
 - The standard deduction is \$12,600 for married couples filing a joint return and \$6,300 for singles and married individuals filing separately. Nearly two out of three taxpayers take the standard deduction, rather than itemizing deductions, such as mortgage interest, charitable contributions, and state and local taxes.
 - Will Congress give ministers another opportunity to revoke an exemption from Social Security? It does not look likely, at least for now. No legislation is pending that would provide ministers with this option.

PRELIMINARY QUESTIONS

Below are several questions you should consider before preparing your 2016 federal tax return.

Q. Must ministers pay federal income taxes?

A. Yes. Ministers are not exempt from paying federal income taxes.

Q. How much income must I earn to be required to file a tax return?

A. Generally, ministers are required to file a federal income tax return if they have earnings of \$400 or more. Different rules apply to some ministers who are exempt from self-employment taxes.

Q. Can I use the simpler *Forms 1040A* or *1040EZ* rather than the standard *Form 1040*?

A. Most ministers must use the standard *Form 1040*.

Q. What records should I keep?

A. You should keep all receipts, canceled checks, and other evidence to prove amounts you claim as deductions, exclusions, or credits.

Q. What is the deadline for filing my federal income tax return?

A. The deadline for filing your 2016 federal income tax return is April 18, 2017.

Q. What if I am unable to file my tax return by the deadline?

A. You can obtain an automatic six-month extension (from April 18 to October 17, 2017) to file your 2016 *Form 1040* if you file *Form 4868* by April 18, 2017 with the IRS service center for your area. Your *Form 1040* can be filed at any time during the six-month extension period. An extension only relieves you from the obligation to **file your return; it is not an extension of the obligation to pay your taxes.** You must make an estimate of your tax for 2016 and pay the estimated tax with your *Form 4868*.

Q. Should I prepare my own tax return?

A. The answer depends on your ability and experience in working with financial information and in preparing tax returns. Keep in mind: Ministers' taxes present a number of unique rules, but these rules are not complex. Many ministers will be able to prepare their own tax returns if they understand the unique rules that apply. These rules are summarized in this document. On the other hand, if you experienced unusual events in 2016, such as the sale or purchase of a home or the sale of other capital assets, it may be prudent to obtain professional tax assistance. The IRS provides a service called Taxpayer Assistance, but it is not liable in any way if its agents provide you with incorrect answers to your questions. Free taxpayer

publications are available from the IRS, and many of these are helpful to ministers.

➤ **Recommendation.** If you need professional assistance, here are some tips that may help you find a competent tax professional:

- Ask other ministers in your community for their recommendations.
- If possible, use a CPA who specializes in tax law and who is familiar with the rules that apply to ministers.
- Ask local tax professionals if they work with ministers and, if so, with how many.
- Ask local tax professionals a few questions to test their familiarity with ministers' tax issues. For example, ask whether ministers are employees or self-employed for Social Security. Anyone familiar with ministers' taxes will know that ministers are self-employed for Social Security with respect to their ministerial duties. Or, ask a tax professional if a minister's church salary is subject to income tax withholding. The answer is no, and anyone familiar with ministers' taxes should be able to answer this question.

WHO IS A MINISTER FOR FEDERAL TAX PURPOSES?

Key Point: The IRS has its own criteria for determining who is a Minister for Tax Purposes.

The criteria the IRS uses to determine who is a minister are not necessarily the same as those used by churches and denominations. Whether or not one qualifies as a Minister for Tax Purposes is a very important question, since special tax and reporting rules apply to ministers under federal tax law. These rules include:

- Eligibility for housing allowances
- Self-employed status for Social Security
- Exemption of wages from income tax withholding (ministers use the quarterly estimated tax procedure to pay their taxes, unless they elect voluntary withholding)
- Eligibility under very limited circumstances to exempt themselves from self-employment taxes

These special rules only apply with respect to services performed in the exercise of ministry.

Example: Pastor J is an ordained minister at his church. In addition, he works a second job for a secular employer. Assume that Pastor J qualifies as a minister for federal tax purposes. Since his church duties constitute services performed in the exercise of ministry, the church can designate a portion of his compensation as a housing allowance. However, the secular employer cannot designate any portion of Pastor J's compensation as a housing allowance, since this work would not be service in the exercise of ministry.

According to the IRS, ministers are individuals who are duly ordained, commissioned, or licensed by a religious body constituting a church or church denomination. They are given the authority to conduct religious worship, perform sacerdotal functions, and administer ordinances according to the tenets and practices of that church or denomination. If a church or denomination ordains some ministers and licenses or commissions others, anyone licensed or commissioned must be able to perform substantially all the religious functions of an ordained minister to be treated as a minister for Social Security. See IRS *Publication 517*.

ARE MINISTERS EMPLOYEES OR SELF-EMPLOYED FOR FEDERAL TAX PURPOSES?

Key Point: Most ministers are considered employees for federal income tax purposes under the tests currently used by the IRS and the courts and should receive a *Form W-2* from their church reporting their taxable income. However, ministers are self-employed for Social Security (with respect to services they perform in the exercise of their ministry).

Ministers have a **dual** tax status. For federal income taxes they ordinarily are employees, but for Social Security they are self-employed with regard to services performed in the exercise of ministry. These two rules are summarized below.

Income taxes. For federal income tax reporting, most ministers are employees under the tests currently used by the IRS. This means that they should receive a *Form W-2* from their church at the end of each year (rather than a *Form 1099*). It also means that they report their employee business expenses on *Schedule A* rather than on *Schedule C*. A few ministers are self-employed, such as some traveling evangelists and interim pastors. Also, many ministers who are employees of a local church are self-employed for other purposes. For example, the minister of a local church almost always will be an employee, but will be self-employed with regard to guest speaking appearances in other churches and services performed directly for individual members (such as weddings and funerals).

Example: Pastor B is a minister at First Baptist Church. He is an employee for federal income tax reporting purposes with respect to his church salary. However, he is self-employed with respect to honoraria he receives for speaking in other churches and for compensation church members give him for performing personal services, such as weddings and funerals. The church issues Pastor B a *Form W-2* reporting his church salary. Pastor B reports this amount as wages on line 7 of *Form 1040*. He reports his compensation and expenses from self-employment activities on *Schedule C*.

Key Point: Most ministers will be better off financially being treated as employees, since the value of various fringe benefits will be tax-free, the risk of an IRS audit is substantially lower, and reporting as an employee avoids the additional taxes and penalties that often apply to self-employed ministers who are audited by the IRS and reclassified as employees.

§ Tax-savings tip. Ministers and other church staff members should carefully review their *Form W-2* to be sure that it does not report more income than was received. If an error was made, the church should issue a corrected tax form (*Form W-2c*).

The Tax Court test. The United States Tax Court has created a seven-factor test for determining whether a minister is an employee or self-employed for federal income tax reporting purposes. The test requires consideration of the following seven factors: (1) the degree of control exercised by the employer over the details of the work; (2) which party invests in the facilities used in the work; (3) the opportunity of the individual for profit or loss; (4) whether or not the employer has the right to discharge the individual; (5) whether the work is part of the employer's regular business; (6) the permanency of the relationship; and (7) the relationship the parties believe they are creating. Most ministers will be employees under this test.

Social Security. The tax code treats ministers as self-employed for Social Security with respect to services performed in the exercise of their ministry — even if they report their income taxes as an employee. This means that ministers must pay self-employment taxes (Social Security taxes for the self-employed) unless they have filed a timely exemption application (*Form 4361*) that has been approved by the IRS. As noted below, few ministers qualify for this exemption.

Key Point: While most ministers are employees for federal income tax reporting purposes, they are self-employed for Social Security with respect to services they perform in the exercise of their ministry. This means that ministers are not subject to the employee's share of Social Security and Medicare (FICA) taxes, even though they report their income taxes as employees and receive a *Form W-2* from their church. Rather, they pay the self-employment tax (SECA).

EXEMPTION FROM SOCIAL SECURITY (SELF-EMPLOYMENT) TAXES

If ministers meet several requirements, they may exempt themselves from self-employment taxes with respect to their ministerial earnings. Among other things, the exemption application (*Form 4361*) must be submitted to the IRS within a limited time period. The deadline is the due date of the federal tax return for the second year in which a minister has net earnings from self-employment of \$400 or more, any part of which comes from ministerial services. Further, the exemption is available only to ministers who are opposed on the basis of religious considerations to the acceptance of benefits under the Social Security program (or any other public insurance system that provides retirement or medical benefits). A minister who files the exemption application may still purchase life insurance

or participate in retirement programs administered by non-governmental institutions (such as a life insurance company).

A minister's opposition must be to accepting benefits under Social Security (or any other public insurance program). Economic, or any other non-religious considerations, are not a valid basis for the exemption, nor is opposition to paying the self-employment tax.

The exemption is only effective when it is approved by the IRS. Few ministers qualify for exemption. Many younger ministers opt out of Social Security without realizing that they do not qualify for the exemption. A decision to opt out of Social Security is irrevocable. Congress did provide ministers with a brief window of time to revoke an exemption by filing *Form 2031* with the IRS. This opportunity expired in 2002 and has not been renewed.

An exemption from self-employment taxes applies only to ministerial services. Ministers who have exempted themselves from self-employment taxes must pay Social Security taxes on any non-ministerial compensation they receive. And, they remain eligible for Social Security benefits based on their non-ministerial employment, assuming that they have worked enough quarters. Generally, 40 quarters are required. Also, the Social Security Administration (SSA) has informed the author of this text that ministers who exempt themselves from self-employment taxes may qualify for Social Security benefits (including retirement and Medicare) on the basis of their spouse's coverage, if the spouse had enough credits. However, the amount of these benefits will be reduced by the so-called "windfall elimination provision." Contact an SSA office for details.

Key Point: The amount of earnings required for a quarter of coverage in 2017 is \$1,300. A quarter of coverage is the basic unit for determining whether a worker is insured under the Social Security program.

Key Point: Ministers who work after they retire must pay Social Security tax on their wages (unless they exempted themselves from Social Security as a minister and they are employed in a ministerial capacity).

HOW DO MINISTERS PAY THEIR TAXES?

Key Point: Ministers must prepay their income taxes and self-employment taxes using the estimated tax procedure, unless they have entered into a voluntary withholding arrangement with their church with respect to federal income tax only.

As noted above, ministers' wages are exempt from federal income tax withholding. This means that a church does not have to withhold income taxes from a minister's paycheck. And, since ministers are self-employed for Social Security with respect

to their ministerial services, a church does not withhold the employee's share of FICA taxes from a minister's wages. Ministers must prepay their income taxes and self-employment taxes using the estimated tax procedure, unless they have entered into a voluntary withholding arrangement with their church. Estimated taxes must be paid in quarterly installments. If your estimated taxes for the current year are less than your actual taxes, you may have to pay an underpayment penalty. You can amend your estimated tax payments during the year if your circumstances change. For example, if your income or deductions increase unexpectedly, you should refigure your estimated tax liability for the year and amend your remaining quarterly payments accordingly.

You will need to make estimated tax payments for 2017 if you expect to owe at least \$1,000 in tax for 2017 after subtracting your withholding and credits and if you expect your withholding and credits to be less than the smaller of (1) 90 percent of the tax to be shown on your 2017 tax return or (2) 100 percent of the tax shown on your 2016 tax return (110 percent if AGI exceeds \$150,000 or, if married filing separately, more than \$75,000). Your 2016 tax return must cover all 12 months.

The four-step procedure for reporting and prepaying estimated taxes for 2017 is summarized below.

Step 1. Obtain a copy of IRS *Form 1040-ES* for 2017 before April 18, 2017. You can obtain forms by calling the **IRS toll-free forms hotline at 1-800-TAX-FORM (1-800-829-3676) or from the IRS website (IRS.gov)**. If you paid estimated taxes last year, you should receive a copy of your 2017 *Form 1040-ES* in the mail with payment vouchers preprinted with your name, address, and Social Security number.

Step 2. Compute your estimated tax for 2017 using the *Form 1040-ES* worksheet. Ministers' quarterly estimated tax payments should take into account both income taxes and self-employment taxes.

Step 3. Pay one-fourth of your total estimated taxes for 2017 in each of four installments as follows:

For the Period	Due Date
January 1–March 31	April 18, 2017
April 1–May 31	June 15, 2017
June 1–August 31	September 15, 2017
September 1–December 31	January 16, 2018

You must send each payment to the IRS, accompanied by one of the four payment vouchers contained in *Form 1040-ES*.

Step 4. After the close of 2016, compute your actual tax liability on *Form 1040*. Only then will you know your actual income, deductions, exclusions, and credits. If you overpaid your estimated taxes (that is, actual taxes computed on *Form 1040* are less than all of your estimated tax payments plus any withholding), you can elect to have the overpayment credited against your first 2017 quarterly estimated tax payment or spread it out in any way you choose among any or all of your next four quarterly installments. Alternatively, you can request a refund of the overpayment. If you underpaid your estimated taxes (that is, your actual tax liability exceeds the total of your estimated tax payments plus any withholding), you may have to pay a penalty.

Key Point: Ministers who report their income taxes as employees can request that their employing church voluntarily withhold income taxes from their wages. Simply furnish the church with a completed *Form W-4* (withholding allowance certificate). Since ministers are not employees for Social Security with respect to ministerial compensation, the church does not withhold the employee's share of FICA taxes. However, ministers can request on *Form W-4* (line 6) that an additional amount of income tax be withheld to cover their estimated self-employment tax liability for the year. The excess income tax withheld is a credit that is applied against the minister's self-employment tax liability. Many churches understandably withhold FICA taxes in addition to income taxes for a minister who requests voluntary withholding. Such withholding must be reported as income tax withheld.