CHURCH PLANTER'S BRIEFING: TAXES

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What are the categories of taxation that affect ministers?

There are two categories of personal taxes: (1) Income Tax (federal and state) and (2) Payroll Tax, also called FICA/SECA. The acronym FICA stands for Federal Insurance Contributions Act (FICA) and SECA stands for Self-Employment Contribution Act. As of this publication, the payroll tax rate is 15.3%, allocating 12.4% to Social Security and 2.9% to Medicare.

What is a Minister's Housing Allowance (MHA)?

The MHA is an income tax deduction available to any "licensed or ordained minister." An MHA allows a minister to deduct housing expenses (mortgage, rent, utilities, furniture, improvements, etc.) from taxable income. For some ministers, the MHA reduces their income tax liability to zero.

Where did the Minister's Housing Allowance (MHA) come from?

The basis for tax-free housing allowance dates back to at least 1921, according to one history account in the federal government's court records. Congress decided that "ministers of the gospel" – as taxpayers who have little choice about personal living space, must reside where their employer requires, and often use their residence for business purposes – could receive tax benefit.[2] Therefore, this tax deduction for ministers derives out of the "convenience of employer" doctrine already available to seamen and hospital workers at that time.[3] The enactment of the Internal Revenue Code in 1954 expanded this tax law to include cash housing allowances. The rationale behind this change was that small churches and church plants should not be penalized if they cannot afford to provide housing or parsonages to ministers.

Will the Minister's Housing Allowance (MHA) ever change?

Recently, the Minister's Housing Allowance has come under fire as an unfair tax advantage given to clergy. There is always a chance that this allowance could go away, but it is a longstanding practice that government leaders have been resolute in supporting.

What is a minister's tax status?

Ministers have a dual tax status. They are considered employees for federal income tax purposes (they get a W-2), but they are considered self-employed for payroll tax purposes.

How does payroll tax (FICA/SECA) work for ministers?

For an ordinary employee (for example, at Home Depot), the employer will pay 7.65% (or half of the required 15.3%) of FICA and then deduct the other 7.65% from the employee's wages. But ministers, who are classified as "self-employed" by the IRS, are required to pay SECA (self-employment tax), which

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[1] This document is an informational summary only, and is not intended to provide official legal or financial advice. You are responsible for your own tax planning. Please consult an attorney or tax professional before making decisions that affect your tax withholding.

[2] http://www.forbes.com/sites/peterjreilly/2012/09/06/in-defense-of-special-tax-treatment-for-clergy/

[3] http://host.madison.com/news/local/with-court-ruling-clergy-housing-allowances-come-in-for-intense/article_aa394ca8-336d-57ab-8724-bd8d83361f74.html

means they are on the hook for the entire 15.3% (since a self-employed person is both employer and employee). At Coram Deo Church, we made the decision to functionally treat our employees like Home Depot would. Therefore, we increase our gross compensation for ministers to take into account the effect of SECA taxes. To say it another way: we give ministers a "7.65% raise" before deducting 15.3% from their payroll for FICA/SECA. Therefore, the net impact to the employee "feels like" 7.65%.

For self-employed ministers, how often does SECA have to be paid?
SECA taxes must be paid either as a monthly payroll deduction or in a quarterly estimated tax installments. If you expect to owe tax of $1,000 or more when you file your return, you must pay monthly or quarterly in order to not be subject to underpayment penalties.

Can a minister "opt out" of FICA/SECA?
Yes. Ministers can request an exemption from self-employment taxes if they are "conscientiously opposed to public insurance because of [their] individual religious considerations." In order to opt out, a minister must a) be "duly ordained, commissioned, or licensed by a religious body,"[4] and b) file Form 4361 with the IRS by the date their income tax return is due for the second year in which they have at least $400 of net earnings from services performed as a minister. If the IRS approves the exemption request, they will return an approved copy of Form 4361. File this form with your permanent records in a safe and secure place. Also be aware that once the exemption is approved, it is irrevocable.

If someone opts out of FICA/SECA, what should they do with the additional money earned?
Considering that Social Security and Medicare are means of income after Americans retire, a minister who has opted out of FICA/SECA should save or invest those funds. Good financial planners will encourage you to set aside every dime that would be going to FICA/SECA into a retirement account.

What is the theological basis for an objection of conscience to FICA/SECA?
A few passages in the New Testament to study are 1 Timothy 5, Romans 13, and Acts 6. The key question is: Who should be responsible to provide for Christian families at retirement age? Do I believe that is the federal government's responsibility? Or do I believe that is the responsibility of the individual Christian or church? The IRS specifies that exemptions must be based on a personal conviction of conscience, not on financial pragmatism.

Additional Resources:

- IRS Publication 517 – *Social Security and Other Information for Members of the Clergy and Religious Workers*
- IRS Form 4361 – *Application for Exemption From Self-Employment Tax for Use by Ministers*
- IRS Tax Topic 417 – *Earnings for Clergy*
- Top 10 Questions Pastors ask Tax Professionals from MinistryCPA
- Special Rules for Ministers in 2013 Tax Return Preparation and Federal Reporting Guide Prepared by Richard R. Hammar

[4] IRS Publication 517, http://www.irs.gov/pub/irs-prior/p517--2013.pdf