



Minister & Ministry Finance FAQs

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Minister Finances FAQs

Is Form 1099-Misc or Form W-2 the correct form to report a minister's income?

The IRS indicates that form W-2 is the appropriate way to report a minister's taxable income paid as a regular salary by a church. (Rev. Ruling 80-11 and IRS Pub 517)

If the church provides the minister with Form 1099-Misc, **premiums paid by the church for medical coverage must be included as taxable income.** The chances of an IRS audit are increased if Form 1099-Misc is used.

What should the church do to enable the minister's housing allowance to be excluded from taxable income?

The housing allowance must be designated in advance, approved by the Board and be recorded in the ministries minutes. The amount which can be excluded is limited by IRS (Section 107) to the least of:

1. Amount submitted by the Minister and approved by the church.
2. Amount actually spent on housing for the year by the minister.
3. Fair rental value of house, furniture and utilities.

Are ministers covered by Social Security?

The Internal Revenue Service defines most ordained ministers as a hybrid employee, *common-law employees* for Federal income tax purposes, but *self-employed* for Social Security purposes (Treas. Reg. 31-3401 & IRS Pub. 517). Earnings from ministry services are subject to self-employment tax unless the minister has requested and received from IRS an exemption from self-employment tax for reason of conscience or religious principles.

Net earnings subject to Social Security tax are computed as the total of the following:

1. Income reported from W-2
2. (Plus), Housing Allowance
3. (Plus), Honoraria (weddings and funerals)
4. (Minus), any unreimbursed business expenses (automobile, office supplies and travel)

If total earnings exceed \$400 in a tax year, Schedule SE, Form 1040 must be filed by April 15 of the next year. Form 1040-ES with installments is paid by April 15, June 15, September 15 and January 15.

How does a minister apply for exemption from Social security tax?

An ordained (licensed or commissioned) minister can apply for exemption from Social Security



tax (Rev Ruling 80-59 & IRS Code 1402 c-4). Form 4361, Exemption Application, should be filed before April 15 of the second year from either the date of ordination or the date that net ministerial income exceeds \$400.

**Can a minister come back to Social Security plan after an exemption application is filed?
Does a minister filing for an exemption from Social Security lose benefits previously
accrued for non-ministerial service?**

At this time no is the answer to the question, “May a minister opt back into Social Security.” Benefits earned from non-ministerial service are not lost, yet, determining the social security distribution at retirement may be affected. It is advised that you have a sit down meeting with the Social Security Administration to ensure that your special earnings consideration from manse and opting out of the plan have been considered.

If you have further questions on this issue, please contact Bruce Verkruyse at the UWM office. Exemption from Social security covers only that compensation derived from service as a minister. Therefore, Social Security taxes will continue to be paid by any minister on any other self-employment income or covered wages after an approval of the exemption. Likewise, a minister does not lose any Social Security credit for earnings from prior non-ministerial services.

Does the church pay unemployment taxes for its minister and lay employees?

Not in most states. Ministers and lay employees generally are exempt from state unemployment taxes. Unity Worldwide Ministries (AUCI) is exempted both from federal unemployment tax and Missouri unemployment tax (FUTA & SUTA). Please check with the employment division of your state.

Must IRS Form 941 be submitted if our pastor is the church's only employee and there is no withholding of taxes?

Yes. With the addition, of Form 8822-B, Responsible Party and Address change form it is a requirement to have a (FEIN) Federal Tax Identification Number for each ministry. Please note that an FEI Number is not a non-profit number. It is instead an identification number only.

If a minister wishes to have income tax withheld voluntarily, what is the process?

Ministers may elect to have tax withheld under the voluntary provision of Section 3401 (a)(9) of I. R. C. if agreed to by the church. A W-4 withholding declaration must be filled out by the minister and given to the church. The reporting requirements and then the same as any other employee. It is recommended that this agreement be a part of a minister’s contract.



Is the expense reimbursement paid by a church taxable income to a minister?

No, it is not taxable. It is generally tax-free if it qualifies as an Accountable Plan. (i.e.) car allowance, office supplies. It is taxable if there is no requirement for the expenses to be verifiable or if this amount received is a flat amount each month.

What qualifies as an Accountable Plan for ministry-related expenses?

The church's reimbursement or allowance arrangement must meet all three of the following rules:

1. Expenses must have a business connection; expenses were paid or incurred while performing ministry services.
2. Adequate accounting to the church for expenses with documentary evidence, such as an accounting book, diary or equivalent to verify the amount, time, place and professional purpose of each expense.
3. Excess reimbursement not spent on ministry-related expenses must be returned to the church.

*Expenses must be substantiated within 60 days after expenses are paid or incurred and any excess reimbursement must be returned to the church within 120 days after the expenses are paid or incurred.

Can this Accountable Plan be funded through salary reduction?

No. Reimbursement for ministry-related expenses must be over and above the salary paid the minister. (IRS Pub 917, Pub 463).



Ministry Tax and Accounting Questions

Church's Tax

Is a church required to file an annual report or income tax return to the IRS?

No. As an affiliated church with Unity Worldwide Ministries (AUCI) hereafter noted as UWM, your ministry is automatically exempted from federal income tax under the provisions of section 501(c)(3) of the Internal Revenue Code and therefore your church is not required to file federal income tax returns (Form 990) so long as your church retains a tax-exempt status. And it has unrelated business taxable income of less than \$1,000. **However, your ministry needs to send an annual report including a Surplus and deficit financial statement to UWM by March 31 of each year for the previous year, so that UWM may file the required group tax umbrella annual report to the IRS.** Your church is not liable for federal unemployment taxes. The following outline illustrates the concept:

- **Church: Tax-Exemption Status**
 - Are churches required to apply for tax exempt status under IRS Code 501(c) 3?
 - Churches are not required to file -Application for exemption number (Form 1023) or Annual report (Form 990) (Treas. Reg. 1.6033-2)
 - **Key concept:** Churches do not have to apply for tax-exempt status to qualify as tax-exempt organizations. Churches are exempt from paying income tax simply by operating as a church (Treas. Reg. 1.511-2a)
- **Church: Tax-Exempt Number**
 - Churches affiliated with UWM are not required to file a separate application for exemption number for IRS Code 503(c)3 status (Form 1023)
 - Member churches may use UWM's group tax-exempt number, also called an umbrella number. Please contact the CFO's office (BVerkruyse@unity.org) for this information.
 - UWM is responsible for evaluating the tax status of its affiliated churches.
 - Ministries must opt into the UWM Annual Report to the IRS by submitting a completed Ministry Annual Report to UWM by January 31 each year.
- **Our Tax-Exempt Number**
 - UWM has applied for a tax exempt number by filing Form 1023, and has received IRS an approve tax determination letter granting UWM 501(c) 3 status.
 - UWM is not listed in Pub 78, Cumulative List of Organizations because UWM has not filed Form 990. We are exempt from the filing requirement, the same as churches are.
 - UWM is required to file an annual report (not a Form 990) on behalf of each opted in affiliated church and alternative ministry.
 - Therefore all member churches must submit a completed annual report each year.



Does a church need an Employer Identification Number (EIN) even if the church has no employees? How can we get an EIN?

Yes, your church needs an EIN regardless of the number of employees. You need to fill out Form SS-4 and submit it to the IRS. As a matter of fact, effective January 2014 and the requirement of Form 8822-B, a church with no employees is required to acquire an EIN.

Can we use Unity Worldwide Ministries (AUCI) EIN (44-0668175) for opening a bank account or to issue W-2 or Form 1099-Misc? When can we use UWM's EIN?

No. You need to have your own EIN for the purpose of W-2 and Form 1099-Misc reporting purposes. **The only time you can use UWM's EIN is as follows:**

1. **When you want to apply for a sales tax exemption to your state.**
2. **When you apply for a non-profit postal bulk permission.**
3. **When your minister applies for exemption from Social Security tax (Form 4361).**

- A) You will likely need a copy of the Annual Report by UWM to the IRS.
- B) A copy of the Association of Unity Churches, International original Tax Determination Letter.
- C) The Cover letter for the IRS Annual Report

What do I do if I have been using the AUC/UWM FEIN?

- **You need to stop immediately and file your own SS-4 requesting a new FEIN (EIN) for your church.**
- **Next File a Form 8822-B, showing the status change between the incorrect and the new FEIN.**

Is a church liable for tax on dividend, interest, annuities, royalties and rents from real property?

- Generally, those forms of income are exempted from tax on unrelated business taxable income (IRC Sec 512(b)). However, if the rental income is from Debt-Financed Property (not Mortgage-free) and less than 85 percent of the property is used for church's exempt purpose, then it constitutes unrelated business **taxable** income.
- Please note that a parking lot is not considered real property.

How does a ministry report unrelated business income to the IRS?

Unrelated business taxes are reported on IRS Form 990-T. Unrelated business income is income from a trade or business regularly carried on (*more often than twice a year as a general rule*) which is not substantially related to the charitable purpose of the church. If your church has \$1,000 or more gross income (less allowable deduction) from unrelated business, you must file Form 990-T and pay the necessary tax.



Our church bookstore carries many unrelated items. What should we do?

You need either to eliminate any unrelated items from your bookstore, form a separate entity as a bookstore (for-profit subsidiary), or maintain an accounting system that allows you to separated UBTI items and submit an annual Form 990-T reporting those unrelated items..

What is the major factor to consider to form a separate for-profit bookstore subsidiary?

1. When your bookstore carries many unrelated items.
2. Income from the bookstore may be too extensive to be conducted within the tax-exempt status of the church.
3. When your church board does not want to report the receipts of any unrelated income, and is enamored with the idea of use of a for-profit subsidiary.

*See IRS private letter Ruling 8706012 and Reg. & 1.501(c)(3)...1(e)

Is a church required to send an annual giving record to the donors at the end of each year?

Per IRS, your church should issue a statement of receipt either when a daily contribution exceeds \$250, or Quid Pro Quo a contribution exceeds \$75. Quid Pro Quo is defines as: something that is given to you or done for you in return for something you have given to or done for someone else.

However, for donor's convenience, it is best practice for your church to issue an annual giving statement at each year-end for all contributors that have given at a \$200 or greater level. It may be helpful for your fiscal financial planning and budget management.

To satisfy the IRS substantiation requirement your church needs to include the following paragraph at the end of the statement or something similar:

"No benefits were provided to you in return for your contribution other than intangible religious benefits. Please retain this letter for your tax records, since it fulfills the substantiation requirements that must be met in order to deduct your contribution." (Title XIII of OBRA '93 P.L. 103-66)

What other IRS Forms does a church need to issue?

- Form 8282: This is to be completed by the church only if non-cash donated items are sold by the church within two years of receiving the gift.
- Form 8283: This form is submitted to the IRS for donations of non-cash items in excess of \$500.
- Form 8300: If a church receives \$10,000 or more in cash (lump sum), it would need to be reported.
- Form 8822-B: Change of Address or Responsible Party — Business, within 60 days of a change in either area.



Is our church required to provide Workers' Compensation for our ministers and lay employees?

Most states require churches to provide Workers' Compensation for their ministers and lay employees. However, a very few states exempt churches from it. Please check with your state.

Church Accounting and Finance

Are there any national statistics or recommended amounts available regarding a proper percentage of a minister's salary compared to a church's income?

Setting a fair salary is the most difficult part of establishing an equitable pay rate.

Minister compensation is based on the combination of church income, church attendance, church's geographical setting, years of service, and minister's educational achievement. To say that the size of church's budget or attendance determines compensation is wrong and misleading. Hence, it must be determined in the context of all the factors, including theology.

*However, many congregations today make a big mistake in committing funds to building and programs rather than to people. Resources should be directed toward people first, then programs and facilities. (i.e.) For a service organization, total salary represents from 50 percent to 90 percent of the total budget.

UWM has a resource which we may share pertinent information around church employee compensation. Please contact the Minister Services Department.

Is it okay for a minister to be a church check signer?

As long as a church provides for an adequate separation of duties in order to ensure the accuracy of financial information and to protect the assets, it is acceptable for a minister to be a check signer. For adequate separation, no one person is allowed to perform more than one of these duties: authorization of transactions, recording of transactions, and custody of assets. It is recommended that two signatures are required on every check and that the two signers not represent the same area of the ministry. It is also best practice for the minister not to be one of the signers.

Our church has a building fund and the balance is \$50,000 now. Our building plan is not yet determined while our general fund has a deficit of \$10,000. Is it okay to use some of the building fund to make payments on the past due operating expenses?

If the building fund of \$50,000 is from funds earmarked by donors for a church building, it should be recorded as a temporary restricted fund until the building project is completed (per SFAS 117). It should be separated from unrestricted funds from which the annual operating expenses are paid.



However, if the building fund resulted from a decision of your church board or members when your annual fund had a surplus and your church wanted to set it aside for a future building project, then your church can use it if your board or membership meeting approves it. This is possible because these funds are not in a temporary restricted fund but rather an unrestricted fund (per SFAS 117).

*(Legal aspect: The Connecticut Supreme Court ruled that donors who give money and place restrictions on its use might not force institutions to comply with the restrictions. The court noted that while under the Uniform Management of Institutional Funds Act, the attorney general may bring a suit against an organization for violating grant restriction, the grant makers themselves may not. **The court also suggested that Treasury regulations provide that a donor may either place restrictions on the use of donated money, or take a tax deduction, but not both.**)*

Are there any guidelines for a church balanced budget system? We are under a deficit budget and we have some outstanding bills to pay now. What shall we do?

There are many different church budget systems such as a program budget system, a zero-base budget system, a traditionally known incremental budget system, a functional budget system, etc. An ideal budget system will be different dependent upon some factors such as the congregation size, the budget amount, number of programs, etc.

However, there are some basic components to consider for a balanced budget and the following is a step-by-step guideline to attain a balanced budget under a budgetary shortfall:

1. Are church's mission, goal, annual objectives clearly stated?
2. Do budget committee members know what is the minimum/essential expense amount needed to operate the church? (tithing, pastoral expense, minimum music, basic building expenses, basic education expenses)
3. What is the total variable expense amount? (pastoral raise, other salaries, outreach, other expenses over and above the basic expenses [music, building, education], new equipment and special program expenses)
4. What is an annual realistic income amount?
5. Is this projected income enough for the total amount of the expense items 2 and 3?
6. If the projected income is not enough for the total expense, then always go back to item 1 and adjust the annual objectives and accordingly adjust item 3 variable expenses.
 - NEVER jump to item 2 first and try to cut the pastoral expense!
 - If necessary, plan a stewardship drive by reviewing the existing stewardship campaign and amending the project income budget at the same time.
 - It is also ideal to consider that some expenses be reduced by means such as refinancing a loan, asking donation for office supplies and equipment, and a moratorium in hiring and purchasing.
7. Now, celebrate a balanced budget!



Is it okay for a church to pay the minister on a percentage of revenue as a part of his/her compensation?

The use of contingent compensation arrangements should be discouraged because of IRS scrutiny. Instead, the church can award a year-end bonus based on performance if incentive is necessary. (GCM 39674, PLR 8807081)

However, the following are recommendations by our counsel if a church really needs a contingent feature for minister compensation arrangement:

1. Document negotiations between the minister and the board.
2. Document the board's consideration of other alternative compensation arrangements.
3. Document discussions and reasons why the contingent payments serve the church well.
4. A *cap* should be inserted.
5. Seek ways to link it to minister's performance.
6. Document inquiries directed towards other churches to review and compare.
7. Document identification of any conflicts of interest.
8. Document discussions to explore available methods by church members.
9. Minister compensation should be both reasonable in amount and directly related to benefits by church members.
10. Identify minister's specific responsibilities, duties.

The Financial Accounting Standards Board (FASB) issued two accounting rules for non-profits organization including churches. What are the rules and how must a church comply?

A rule from FASB, known as SFAS-117, Financial Statements for Not-for-Profit Organizations, became effective for fiscal years beginning on or after 12/15/1995. This rule has had a profound impact on the presentation of the church financial statement.

SFAS-117 requires all non-profits to include the following in their financial statements:

1. Statement of Financial position. Formerly known as the balance sheet, this includes amounts for churches' total assets, liabilities, and **net assets** (a new term for fund balance). This net asset consists of permanently restricted, temporarily, and unrestricted net assets with donor's stipulation.
2. Statement of Activities. Formerly the statement of revenues and expenses, this includes the change in a churches' net assets. A church needs to indicate the change in permanently restricted, temporarily, and unrestricted net assets. This Statement of Activities also must include expense information reported by function (by major programs and major classes of supporting services). Alternatively, this functional report can be presented in the footnotes to the financial statements.



* Must your church comply? No. Your church is not bound by federal law or by the IRS to comply with accounting standards issued by the FASB. However, if your church issues financial statements, your church will not be able to have them certified as "prepared in accordance with generally accepted accounting principles". This could have very negative consequences when using the statements in fundraising efforts. Also banks may require a certified statement if your church applies for a loan.

*** How to change?**

Prior Fund Balance Description	New Net Asset Category
Current Unrestricted	Unrestricted
Current Unrestricted	Board Designated Unrestricted
Current Restricted	Temporarily Restricted
Endowment	Permanently Restricted
Term endowment	Temporarily Restricted
Fund functioning as endowment	Unrestricted
Quasi-endowment	Unrestricted
Annuity and life income funds	Temporarily Restricted
Unexpended capital funds-unrestricted	Unrestricted
Unexpended capital funds-restricted	Temporarily Restricted
Renewal & replacement funds	Unrestricted
Retirement of indebtedness funds	Unrestricted
Net investment in plant	Unrestricted

* Your church can continue to maintain internally the existing fund accounting in order to report to donors and agencies concerning restricted gifts and grants, and respective interest and earning allocations.