

Bluebonnet Baptist Association
CHURCH TAX SEMINAR

January 20, 2022

C. Dale Hendrix, CPA

832-524-0257
CDALEHENDRIX@ICLOUD.COM

Topics in this Session

Resources

Recent
Developments

Ministers
Taxation and
Reporting

The Church as
Employer

Charitable
Giving Essentials
for Churches

IRS Tax Helps

- IRS publications – Downloadable from www.irs.gov
 - Publ 15 Circular E, Employer's Tax Guide
 - Publ 15-A Employer's Supplemental Tax Guide
 - Publ 15-B Employer's Tax Guide to Fringe Benefits
 - Publ 463 Travel, Entertainment, and Car Expenses
 - Publ 517 Social Security and Other Information for Clergy
 - Publ 526 Charitable Contributions
 - Publ 969 HSA's and Other Tax-Favored Health Plans
 - Publ 557 Tax Exempt Status for Your Organization
 - Publ 561 Determining the Value of Donated Property
 - Publ 1771 Charitable Contributions – Substantiation and Disclosure
 - Publ 1828 Tax Guide for Churches and Religious Organizations

Filing Deadlines

2021 Information Returns

Form	Recipient	Paper Forms	Electronic Filing
W-2 – Copies B, C, and 2	Employees	January 31, 2022	January 31, 2022
W-2 – Copy A W-3	SSA	January 31, 2022	January 31, 2022
1099-NEC – Copy B	Contractors	January 31, 2022	January 31, 2022
1099-NEC – Copy A 1096	IRS	January 31, 2022	January 31, 2022

Recent Developments

- Charitable contribution deduction for non-itemizers
 - \$300 for single person filing status
 - \$600 for married couples filing jointly
- Revoking exemption from SE taxes
 - If application was made solely for economic considerations rather than religious opposition, exemption is null. (IRS Revenue Ruling 70-197)
 - See Internal Revenue Manual section 4.19.6.4.11.3
- Group tax exemptions
 - Pending IRS Notice 2020-36 would supersede current procedures
 - Subordinate organizations would be required to adopt a uniform governing instrument

Who is a Minister for Tax Purposes?

- Credentials test
 - **Must be** licensed, commissioned, or ordained
- Performance test
 - Conduct worship
 - Administer sacraments
 - Management responsibility in local church or denomination.
 - Considered a religious leader by church or denomination
- **Best practice – Obtain a copy of each minister's ordination certificate**

Dual Tax Status of Ministers

- Almost always an employee for income tax; however,
 - Exempt from payroll tax withholding
 - Pay taxes through quarterly estimated payments using Form 1040ES
 - May elect voluntary withholding
- **Always** self-employed for Social Security and Medicare (SS/Med) with respect to ministerial services
 - **Always** exempt from SS/Med withholding
 - May elect additional voluntary income tax withholding to cover SS/Med taxes
 - Church is not responsible for any portion of ministers SS/Med taxes
 - Minister responsible for 100% of SS/Med taxes
 - Social security 12.4%
 - Medicare 2.9%
 - Combined 15.3%
 - No SS due if max paid via secular employment earnings >
 - \$142,800 2021
 - \$147,000 2022

Minister's Form W-2

- Minister should receive a W-2 from the church in almost all cases
- Differences between a minister's W-2 and non-minister employee
 - There may not be any amount in Box 2, Federal income tax withheld
 - There will not be any amount in Boxes 3, 4, 5, and 6 relating to Social Security and Medicare
 - Housing allowance may be included in Box 14, Other
- Tip – FIT withheld can be applied against **any** type of tax assessed on a Form 1040

Minister Form W-2

Report if withholding was elected by the minister

22222		VOID <input type="checkbox"/>	Employee's social security number	For Official Use Only OMB No. 1545-0008	
Salaries and stipends			1 Wages, tips, other compensation	2 Federal income tax withheld	
Love offerings and other gifts			3 Social Security wages	4 Social Security tax withheld	
Nonaccountable allowances			5 Medicare wages and tips	6 Medicare tax withheld	
Church payment of personal expenses			7 Social Security taxes	8 Unreported tips	
Unrestricted discretionary funds			9	10 Dependent care benefits	
Personal use of church assets			11 Nonqualified plans	12a See instructions for box 12	
Wedding & funeral fees paid by church			13 Statutory employee <input type="checkbox"/> Retiree <input type="checkbox"/> Third-party sick pay <input type="checkbox"/>	12b	
Value of gift cards received from church			14 Other	12c	
Other taxable fringe benefits				12d	
Unsubstantiated purchases with a church-issued credit card					
16 State wages, tips, etc.		17 State income tax		18 Local wages, tips, etc.	
19 Local income tax		20 Locality name			

Optional reporting of housing allowance

Best Practice: Report FFCRA Employer Paid Leave in Box 14

Do Not Cut, Fold, or Staple Forms on This Page

Minister's Form W-2

Box 2 – Optional withholding

Boxes 3,4,5, and 6 – Always empty

Box 14 – Housing allowance optional

a Employee's social security number		Safe, accurate, FAST! Use		Visit the IRS website at www.irs.gov/efile	
OMB No. 1545-0008					
b Employer identification number (EIN)		1 Wages, tips, other compensation	2 Federal income tax withheld		
c Employer's name, address, and ZIP code		3 Social security wages	4 Social security tax withheld		
		5 Medicare wages and tips	6 Medicare tax withheld		
		7 Social security tips	8 Allocated tips		
d Control number		9	10 Dependent care benefits		
e Employee's first name and initial		Last name		Suff.	
f Employee's address and ZIP code		11 Nonqualified plans		12a See instructions for box 12	
		13 Statutory employee <input type="checkbox"/> Retirement plan <input type="checkbox"/> Third-party sick pay <input type="checkbox"/>		12b	
		14 Other		12c	
				12d	
15 State Employer's state ID number	16 State wages, tips, etc.	17 State income tax	18 Local wages, tips, etc.	19 Local income tax	20 Locality name

Form **W-2** Wage and Tax Statement **2022** Department of the Treasury—Internal Revenue Service
 Copy B—To Be Filed With Employee's FEDERAL Tax Return.
 This information is being furnished to the Internal Revenue Service.

Common W-2 Errors Affecting Ministers

- Reporting a housing allowance in Box 1
- Reporting any data in boxes 3, 4, 5, and 6 for a minister
- Failing to report certain non-salary payments as taxable comp
 - Nonaccountable expense reimbursements
 - Church “love offerings” or special occasion gifts
 - Personal use of a church vehicle
 - Social Security tax allowance for a pastor
 - Bargain purchase of church property
 - Moving expenses

Opting out of Social Security

File Form 4361 NLT second year earning ministerial income \leq \$400

Certify religious opposition to public insurance

Not approved before receipt of Form 4361 marked "Approved"

Opting out of Social Security

Election is
irrevocable if
based on religious
opposition

Forfeiture of Social
Security retirement
payments

Forfeiture of
Medicare benefits

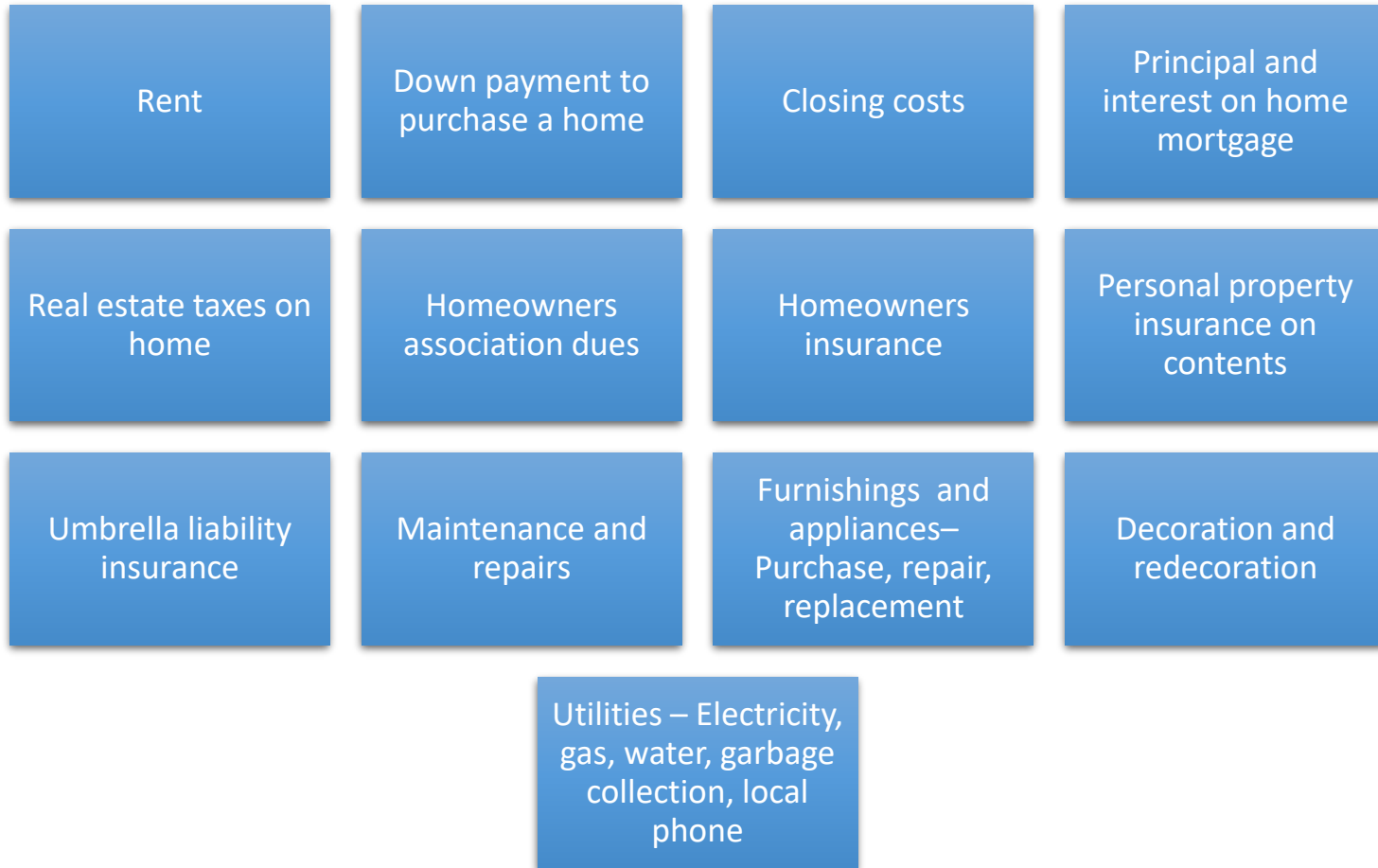
Housing Allowance Exclusion

- Excludable for federal income tax
- Includable for social security
- Designation requirement
 - In writing
 - Officially designated before the payment is made
 - Definite amount must be designated
- Excludable amount the smallest of
 - Amount designated as housing allowance
 - Amount actually used to provide a home
 - Fair rental value of the home, including
 - Furnishings
 - Utilities
- Excess housing allowance includable as income on Form 1040
 - Minister's responsibility, not the church's
- **Best practice – Include verbiage that designation of housing allowance remains effective until changed**

Other Housing Exclusion Information

- Double deduction of mortgage interest and real estate taxes
 - Excluded from income as part of housing allowance
 - Deductible as an itemized deduction
- Retired ministers
 - Eligible for housing allowance if paid from denominational retirement plan
 - Housing allowance not available to surviving spouse
- Evangelists
 - Portion of honorarium qualifies as housing allowance if so designated in advance by paying church.
 - If employed by nonprofit corporation for their ministry, the corporation may designate a housing allowance

Allowable Housing Expenses



Housing Allowance

Common Areas of Non-compliance

No documentation
of housing
allowance

Applied
retroactively

Non-ministers
given a housing
allowance

Incorrectly
reported on
minister's tax
return

Expense Reimbursement Arrangements



Unsubstantiated expense reimbursements must be included as income in employee's W-2



Implementing an accountable reimbursement plan can avoid this situation

Expense Reimbursement Arrangements

Accountable plan

- Cannot be reimbursed via salary reduction
- Must be in writing
- Expenses must have a business connection
- Must adequately account to employer within a reasonable time (60 days)
- Must return any excess reimbursement or allowance within a reasonable time (120 days)

Non-accountable plan

- A reimbursement arrangement that does not meet all rules listed above for an accountable plan.
- Payments deemed non-accountable even if made under an accountable plan
 - Excess reimbursements not returned to employer
 - Reimbursement of nondeductible expenses

Expense Reimbursement Arrangements

	Accountable Plan	Non-accountable Plan
Reported on W-2	No	Yes
Itemized deduction for unreimbursed expenses	No	No
Substantiation required	Yes	No

Accountable Reimbursement Plan Rules

Conditions for reimbursement or deductibility

- Ordinary – Common and accepted in your occupation
- Necessary – Helpful and appropriate

Elements to be substantiated

- The amount paid
- The date paid
- The business purpose for the expenditure
- The place traveled or a description of the item/service purchased
- For business meals
 - Business relationship of recipient, e.g. names, titles, or other designations
 - Proof that an officer or employee was present during the meal

Submit substantiation to employer within 60 days of payment

Return any excess advance to employer within 120 days after expense is paid

Ministers' Common Business Expenses



Transportation

2022 standard mileage rate - \$.585

2021 standard mileage rate - \$.560



Travel – Away from home overnight

Includes transportation, meals, lodging, cab fares, etc.

Does not include personal items, e.g. toothpaste, magazines



Books and subscriptions



Professional dues



Business meals, except when included in the cost of an entertainment event

Ideal Clergy Tax Reporting Arrangement

Employee status

Voluntary
withholding of
income tax and self-
employment tax

Housing allowance
properly designated

Accountable
reimbursement
plan adopted by
church

Church Tax Exemption

- Churches are automatically exempt from federal income taxes
 - Not required to file Form 1023 – Application for Exemption
 - A church may voluntarily file for exemption
 - Group exemption, e.g. Bluebonnet Baptist Association
 - Direct application to IRS, Form 1023
- Churches **are not** automatically exempt from State sales taxes and franchise taxes
 - Must file Form AP-209 with the Texas Comptroller for exemption from sales taxes and franchise taxes
 - Sales tax exemption applies to purchases but not to sales

Employer Responsibilities

- Churches are required to withhold, report, and pay employee
 - Income taxes
 - FICA taxes (Social Security and Medicare)
 - 50% paid by employee (Social Security 6.2%, Medicare 1.45%)
 - 50% paid by church (Social Security 6.2%, Medicare 1.45%)
- Churches not liable for federal unemployment taxes (FUTA)
- Special rules for ministers
 - Exempt from mandatory income tax withholding
 - Exempt from withholding for self-employment tax (Social Security/Medicare)
 - Eligible for voluntary FIT withholding to cover income tax and/or self-employment taxes

New Hires



Obtain Form I-9



Obtain Form W-4



Report new hire to State
within 20 days of
employment

Employer.oag.state.tx.us

Payroll Tax Deposits

- Must pay via Electronic Federal Tax Payment System (EFTPS), unless quarterly liability <\$2,500
- Enroll in EFTPS online – www.eftps.gov
- Basic rules
 - Liability <\$2,500 in a calendar quarter – Direct payment with quarterly Form 941 permitted
 - Liability >\$2,500 for quarter and <\$50,000 annually – Due monthly
 - Liability > \$50,000 annually – Semi-weekly depositor
 - Deposits for Saturday-Tuesday paydays are due the following Friday.
 - Deposits for Wednesday-Friday paydays are due the following Wednesday.

Payroll Tax Reporting

Churches that withhold P/R taxes must file Form 941 quarterly

- Due on last day of month succeeding quarter end (4/30, 7/31, 10/31, 1/31)
- Form 941 not required if no withholding is required
- Form 941 must be filed even if the only employee is a minister that has had voluntary income tax withheld

Form W-2 must be issued to each employee by January 31, 2022

Form W-3 must accompany a copy of all W-2's and submitted to the Social Security Administration by January 31, 2022

Payroll Filing

Common Areas of Non-compliance

Failure to include
value of gift cards
given to employees on
W-2

Giving monetary gifts
to volunteers

Reporting Social
Security and Medicare
withholding for
ministers

Taxable Compensation Examples

Personal Benefit to Employees

Salary	Bonuses	Social Security supplement	Love offerings
Retirement or farewell gifts from church	Dependent educational benefits	Premiums on individual life insurance policies	Premiums on group-term life insurance >\$50,000 coverage
Offerings and fees for marriages, funerals, etc.	Non accountable discretionary fund	Non accountable expense reimbursements	Bargain purchases of church property
	Church payment of employee's personal expense	Forgiveness of debt	

Tax-Free Benefits

- Accountable reimbursement plan expense reimbursements
- Premiums on group-term life insurance up to \$50,000 coverage
- Group health insurance paid or reimbursed by church
- Health savings account (HSA)
- Health care flexible spending account (FSA)
- Qualified Small Employer Health Reimbursement Arrangements
- Individual coverage HRA
- Long term care insurance paid or reimbursed by church
- Pension plan IRC section 403(b)

Employee vs Contractor Determination Reporting Requirements

- Employee – Form W-2
- Contractor – Form 1099-NEC
- Churches sometimes misclassify employees as contractors because
 - They don't know the rules
 - Non-compliance minimizes paperwork
 - They avoid payment of P/R taxes

Employee vs Contractor Determination

- Risk of reporting employee compensation on Form 1099
 - Church is responsible for 100% of uncollected P/R taxes
 - 100% penalty for failure to collect and remit P/R taxes
 - Intermediate sanctions up to \$10,000 can be assessed against responsible parties (Pastor, Business Administrator, Treasurer, etc.)

Employee vs Contractor Determination

- Service provider is an independent contractor if the customer
 - Only has the right to control the result of the work
 - Does not have the right to control the means and methods of accomplishing the result
- The more control your church exercises over an individual, the more likely the relationship is an employer/employee relationship.

Employee vs Contractor Determination Guidelines for Assessing Status

- **Behavioral control** – Whether right to direct or control how the worker performs a specific task
 - When and where to do the work
 - What tools or equipment to use
 - What order or sequence to follow
- **Financial control** – Whether right to direct or control business aspects of the worker's job
 - Extent to which worker has unreimbursed business expenses
 - Extent to which worker makes service available to others
 - Extent to which worker can realize a profit or loss
- **Type of relationship** – How the parties perceive their relationship
 - Written contracts describing relationship
 - Whether organization provides worker with employee-type benefits
 - Permanency of the relationship

Employee vs Contractor Determination

- Musicians – Trend is to treat musicians as employees
 - Treating musicians as independent contractors is not in line with IRS's stance
 - If you opt to treat musicians as contractors, prepare a document that supports your decision
- Common area of non-compliance – Treating employees that perform after-hours work as independent contractors for the extra work.

Form 1099-NEC

- Must be filed for every nonemployee (contractor) to whom the church makes aggregate payments for services of \$600 or more for the year.
 - Individuals
 - Partnerships
 - Estates
 - LLC's, unless taxed as an S-Corporation or C-Corporation
- 1099-NEC required for full value of both merchandise and services if both are provided.
- 1099-NEC not required
 - Corporations
 - Exempt organizations and government agencies
 - Payments for merchandise
 - Accountable travel expense reimbursements

Form 1099 - MISC

- Must be filed for each person to whom the church gives the following types of payments during the tax year
 - At least \$600 in the following
 - Rents
 - Payments to an attorney for legal services
 - Other payments not generally applicable to churches

IRS Charitable Gift Definition

- A donation or gift to, or for the use of, a qualified organization
 - To a 501 (c) (3) organization
- Voluntary and is made without getting, or expecting to get, anything of equal value

What can be Donated?

Nearly
anything of
value

Cash

Insurance
policies

Stocks and
bonds

IRA
distributions

Personal
property

Real estate

Unreimbursed
volunteer
expenses

14 cents per
mile for
volunteer work

Crypto
currency

Non-Deductible Transactions

Gifts to a non-qualified organization

Gifts to or for a specific individual

Value of donor's time or services

Rent-free use of property

Qualified charitable distributions

Exchange (Quid pro Quo) transactions

Qualified Charitable Distributions

- An otherwise taxable distribution from an IRA
- Excluded from taxable income
- Not tax deductible
- Conditions and restrictions
 - Donor must be 70 ½ or older on the date of transfer
 - Transfer must be directly from IRA trustee to donee organization
 - \$100,000 annual maximum
 - Donor may not receive any goods or services in exchange for any part of the gift
 - Recipient church must receipt separately from a donor's other contributions
 - Must meet all acknowledgement requirements of regular contributions, and
 - Acknowledge funds were received directly from IRA administrator
 - Should confirm it is a qualifying charity
 - Web search key words "sample qcd acknowledgement letter"

Exchange (Quid Pro Quo) Transactions

- Deduction limited to amount the payment exceeds the fair market value (FMV) of goods or services received
- FMV \neq cost to church
- Token benefits not deemed exchange transactions

Quid pro Quo Disclosure Statement

IF

- Payment is \$75 or more, and
- Goods or services are received by the donor in exchange

Then

- Church must inform donor of the limitation of the tax deductibility and provide good faith estimate of the FMV of the goods or services
- If the disclosure statement is furnished in connection with a particular solicitation, it is not necessary for the organization to provide another statement after it receives the contribution

Quid pro Quo Disclosure Statement Caveat

- If the church fails to disclose value of the benefit on the statement
 - IRS may impose a penalty of \$10 per statement
 - Maximum penalty of \$5,000 per event

Receipting Gifts of Cash

Single cash gifts of less than \$250

- Gifts of currency in any amount require a gift receipt
- Otherwise, donor may substantiate by bank record (cancelled check or bank/credit card statement), payroll deduction record, or proper gift acknowledgement

Single cash gifts of \$250 or more

- Donor must have a proper gift acknowledgement
- Burden is on donor to get receipt

Receipting Gifts of Cash

Must be written

Must include

- Church's name
- Donor's name
- The amount and date of each donation of \$250 or more.
- Description and good faith estimate of the value of any goods or services provided in return for the contribution
- If no goods or services were provided - A statement that no goods or services received (other than intangible religious benefits)

Recommended

- Include date receipt was issued on gift receipt
 - Donor must substantiate having receipt in hand before filing tax return

Receipting Non-Cash Gifts

- Donor must obtain a proper acknowledgement for deductions with FMV of \$250 or more
 - Additional IRS forms may be required depending on the value of the gift
- Provide a description of the property only
- Avoid reporting the value of donated property
 - You don't know if the donor qualifies for a FMV deduction
 - Your value may not be correct
- Out of pocket costs incurred by volunteers performing services are deductible
- Vehicles – Includes autos, boats, jet skis, aircraft, trailers, motorcycles, bicycles, and almost anything that moves people
 - File Form 1098-C within 30 days of receiving the donation

Timing for Deductibility

Which year for tax-deductible receipt purposes?

- Timing measured by unconditional delivery

“Delivery” date for checks

- Hand delivery – Date physically placed in offering or otherwise placed in control of the church
- Mail - Generally date of postmark
 - Exceptions
 - Post dated checks
 - NSF checks not deemed to be delivered

“Delivery” date for credit cards, text giving, and internet giving

- Delivery is when processor has received irrevocable instructions to pay the church

When Do Givers Need a Receipt?

- The earlier of
 - The date their tax return is filed
 - The due date of their tax return (including extensions)
- For good relations with givers, it's wise to provide gift receipts even though the burden for having the records is on the giver

Common Acknowledgment Mistakes

Failure to include the “no goods or services” disclaimer

Providing an acknowledgment indicating the gift is “to or for” an individual instead of “to and for” the church

Providing an acknowledgment for the gift of time

Providing an acknowledgment for the rent-free use of property

Including the valuation of property on a noncash acknowledgment

Failure to provide disclosure statement for qualifying “quid pro quo”

If church signed Form 8283 upon receipt of noncash gift

- Failure to file Form 8282 for certain gifts of property disposed of within 3 years of receiving the gift