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2019 Overview of Tax Issues
for Synagogues and other
Religious Congregations

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2019 OVERVIEW OF TAX ISSUES FOR SYNAGOGUES

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Remember: Synagogues are exempt from income tax, but nonetheless must comply with many tax laws, particularly payroll taxes for non-clergy employees. They must also comply with other applicable federal and state laws, particularly state corporate laws applicable to nonprofit religious organizations and state property and sales tax laws.

1. Exempt Status

A. Exemption and Reporting

Synagogues are not required to file an application with the IRS to be exempt under section 501(c)(3), but many do file Form 1023, the application for exemption, in order to be on the published IRS list of section 501(c)(3) charities eligible to receive tax-deductible contributions. Synagogues do not need to file the annual federal information returns (Form 990) or the e-postcard (Form 990-N) required of other kinds of charities. State filing laws, however, may differ. Moreover, because of recent changes to the tax laws, some may need to file Form 990-T for unrelated business income tax owed on parking and other benefits provided to employees.

B. Compensation and Intermediate Sanctions

A law designed to reduce the risk of revocation of exempt status requires that, in setting compensation for clergy and others, particular care be taken in obtaining comparables and in recording the basis for the compensation package. See *Attachment A*.

C. Political Activities and Lobbying.

Synagogues cannot intervene in candidates' campaigns for elected office and are limited in the amount of lobbying they can do. See *Attachment B*.

2. Contributions, Fundraising

A. Dues and Fees

Synagogues must acknowledge contributions of \$250 or more (including dues); they must inform members of the value of goods or services (other than intangible religious benefits) received in exchange for contributions. Difficult issues arise in connection with Hebrew/religious school education and with donations of automobiles. See *Attachment C*.

B. Fundraising

Care must be taken so that various fundraising activities, such as advertising in tribute books or newsletters, do not subject synagogues to the federal tax on unrelated business income. That is, exempt organizations including synagogues are not taxed on income related to their exempt purposes, but are subject to income tax on income from unrelated activities. Moreover, because of a law enacted at the end of 2017, some synagogues may have to pay unrelated business income tax on parking and other transportation benefits provided to employees. Being subject to unrelated business tax will not jeopardize exempt status, unless such unrelated activities come to dominate the organization. Fundraising activities may also be subject to state and local regulation. *See Attachment D.*

Many congregations encourage their members to consider sophisticated estate planning techniques, such as charitable lead trusts or charitable remainder trusts, to benefit the synagogue. Special care must be taken to ensure that such plans comply with all applicable tax rules and that the members consult their own tax advisors to understand the consequences.

3. Issues for Clergy and Other Staff

A. Income Tax Withholding, Social Security, Medicare

Clergy are subject to a unique set of tax rules regarding their compensation. Those regularly employed by a congregation are almost always considered to be employees, but withholding of income tax is not required and they are subject to self-employment rather than employee payroll taxes. Their compensation should be reported on Form W-2, with no social security or Medicare tax withheld or paid, not on Form 1099. *See Attachment E.*

B. Parsonage or housing allowance

Clergy may exclude from income for purposes of income tax the fair rental value of their housing, if certain requirements, including formal action by the synagogues board, are met. The amount of this housing allowance, along with clergy salary, is, subject to self-employment tax. *See Attachment F.*

C. Discretionary Funds

An official statement of the synagogue about the purpose and use of discretionary funds will help protect clergy from any assertion that these funds represent additional income to them. *See Attachment G.*

D. Other employee issues

For both clergy and non-clergy employees, some benefits are subject to income tax and payroll taxes and some are not. In many cases, the tax consequences of benefits, such as medical benefits and tuition discounts, will depend on how they are structured and to whom they are offered. For non-clergy employees, failure to comply with withholding and payroll tax laws risks particularly stringent penalties on those who had the responsibility to deposit these funds.

Compensation and “Intermediate Sanction” Provisions Applicable to Tax-Exempt Organizations

While obtaining comparable data is part of a Board's fiduciary duty in setting compensation, tax laws make doing so even more important. Some years ago Congress passed legislation, known as intermediate sanctions, requiring that nonprofit organizations pay reasonable compensation. Violation of these rules can lead to imposition of sizable excise taxes on senior staff and organization managers (who include directors and trustees) of the organization.

IRS regulations regarding this legislation give a presumption of reasonableness for compensation (and other transactions, such as sales and contracts) if and only if the organization follows very specific procedures. The procedures include the organization obtaining and relying upon appropriate data as to comparability for compensation of those who have substantial influence over the organization and who receive total economic benefits above a specified amount (\$125,000 in 2019; this amount is adjusted for inflation annually). These procedures require that the organization concurrently record the compensation package, the basis for the compensation package (including the comparables), and those who voted on the compensation package. Under the applicable regulations, even small organizations (defined as those with gross receipts under \$1 million) must obtain three comparables to have the benefit of the presumption or reasonable compensation.

This law does not exempt religious organizations, although the regulations state that the IRS will comply with the Church Audit Act. Under the Church Audit Act, the IRS could seek to impose these taxes only if it has a reasonable basis for believing that such taxes are due.

Attachment A

Tax Rules Regarding Lobbying and Political Activities by Section 501(c)(3) Organizations

The tax code distinguishes campaigns for elective public office from attempts to influence legislation.

All section 501(c)(3) organizations, including synagogues, are prohibited, at risk of losing exemption, from participating in political campaigns. In general, political campaigns are defined for this purpose as campaigns by candidates for elective office. (This prohibition was introduced by Lyndon Johnson in 1954, supposedly because he was annoyed about some newspaper ads that charities had run against him in his last campaign.) In a case called *Branch Ministries*, decided in May, 2000, a federal appellate court upheld revocation of a church's exemption for running anti-Clinton newspaper ads. (The Church had claimed that the political campaign prohibition violates the First Amendment.) Despite attempts to repeal or amend the so-called Johnson Amendment, it is still good law.

Tax-exempt charities cannot, whether directly or indirectly, endorse or oppose any candidate for elective public office, including, for example, elected state judges. They cannot contribute any money or resources to any candidate's campaign, political action committee, or political party or rank candidates, even if the ranking is the result of neutral process. Particular care should be taken to avoid statements that name candidates or that comment on their positions from the bimah (pulpit) or at any official synagogue function - including activities of the social action committee - because they are likely to be treated as being the position of the organization.

Not all activities involving campaigns for elective office are considered prohibited political activity. Charities can register voters, conduct candidate debates, distribute general voter education information or run get-out-the vote operation on election day - but only if these activities are conducted in a nonpartisan manner. A debate will not be considered nonpartisan unless all qualified candidates are invited to attend.

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While any involvement in a political campaign for elective office is prohibited, synagogues, like other charities, can participate in lobbying to a limited degree. For tax purposes, lobbying is distinguished from intervening in electoral politics. Lobbying is defined as an attempt to influence legislation, either directly through legislators or indirectly through grass root campaigns which ask citizens to contact their legislators. (Taking such positions on initiatives or propositions as well as confirmation of federal judges, is considered lobbying, not political campaign activity). Under the tax code, lobbying by charitable organizations is permitted to a limited extent; it cannot be more than an insubstantial part of the organization's activities. The meaning of insubstantial is not clear, but it is clear that it means more than dollars spent. (Organizations other than religious congregations can choose to have their lobbying activities subject to specified dollar limits, but this option is not available to religious congregations.) The Supreme Court has upheld the constitutionality of the lobbying limits, although the case did not involve a religious organization.

Attachment B

Substantiation and Quid Pro Quo Requirements

Charitable contributions of \$250 or more must be substantiated by a contemporaneous written acknowledgment from the donee organization and the charitable contribution consequences of quid pro quo contributions that exceed \$75 must be disclosed. Failure to satisfy this latter rule subjects the charity to penalties of \$10 per contribution, with a maximum of \$5,000 per event or mailing. The burden is on the taxpayer to show that all or part of a payment to a charitable organization is a contribution or gift. A charitable deduction is not allowed for a payment to charity for goods or services (other than for intangible religious benefits) unless (a) the amount paid exceeds the fair market of the goods or services and (b) the taxpayer intends to make a payment in excess of such fair market value. In determining this excess, if any, the taxpayer may rely on the value of the goods and services as provided by the donee organization, unless the taxpayer knows the donee's stated value or good faith estimate of value is unreasonable. Synagogue dues are deductible; what is received in return for dues is deemed to be entirely intangible religious benefit. Synagogues should note that, with the standard deduction for married couples now at \$24,000, fewer congregants may be itemizing. Some congregants over 70-1/2 may wish to take advantage of special rules permitting contributions directly from IRAs to a charity because they satisfy required minimum distribution rules without being included in income.

Decisions by the Ninth Circuit Court of Appeals and the Tax Court, which involved suits by a family named Sklar against the IRS Commissioner, concluded that the part of the payments by parents to a Jewish religious day school for religious education are NOT deductible as charitable contributions. There is no IRS or judicial authority permitting deduction for costs of religious education; these costs are seen as payment for education, not a contribution that results in an intangible religious benefit.

In the case of donations of automobiles, applicable rules generally limit any deduction above \$500 to the amount for which the charity sells the car.

An organization may use any reasonable methodology in making a good faith estimate of the value of goods and services it provides. For goods or services that are not generally available in a commercial market, the good faith estimate may use goods or services that are similar or comparable even if they do not have the unique qualities of those offered by the organization.

Substantiation requirements for deductible contributions of \$250 or more may be satisfied for several such contributions with one or more contemporaneous acknowledgments. Since each payment is considered separately, a contribution of less than \$250 is not subject to the substantiation requirement, even if contributions exceed \$250 in the aggregate. An acknowledgment must provide (1) the amount of cash paid and a description of any property transferred, (2) a statement of whether goods or services were provided for consideration, in whole or part, for such cash or property, (3) a description and good faith estimate of the value of any goods or services so provided, and (4) a statement by organizations providing intangible religious benefits that they do so. The written acknowledgment is contemporaneous if the taxpayer obtains it on or before the earlier of the taxpayer's filing date for the original return for the taxable year in which the contribution was made or the due date, including extensions, for such return. Goods or services are provided for consideration if the "the taxpayer receives or expects to receive goods or services in exchange for payment." Goods and services received in connection with fundraising may be disregarded and thus need not be acknowledged if either they have value of not more than 2% of the amount contributed, up to a maximum (for 2019) of \$110.00, or if the goods received are only token items with the charity's name and logo or low-cost items worth no more than \$11.50 when the taxpayer makes at least a minimum payment of \$55.50. (These numbers are adjusted for inflation annually.) Newsletters of less than commercial quality and low-cost items provided for free without advanced orders also are deemed to have insubstantial value.

Acknowledgment for unreimbursed out-of-pocket expenses is satisfied if the taxpayer has records of the expenditures and obtains a timely statement from the organization describing the services provided by the taxpayer and whether the organization provided any goods or services in consideration for them.

Attachment C

Laws Regarding Charitable Fundraising

Charitable fundraising, including that conducted by religious organizations, is subject to federal, state and local laws. The rules most likely to be applicable to synagogue fundraising activities are summarized briefly below.

1. Charitable contributions are deductible for income tax purposes only to the extent that they exceed the fair market value of what is received. NOTE: The deductible contribution must be reduced by the fair market value of what is received, **not** the cost to the synagogue. Thus, having the goods or services donated to a synagogue does not prevent reduction of the deductible amount. Additional federal disclosure laws apply to payments above \$75 that involve both a charitable donation and a receipt of goods or services. Any fundraising event that costs more than \$75 and involves the provision of a meal, such as a dinner dance or the typical "rubber chicken" dinner, will be subject to these rules. In such cases, the reduction in deductible contribution must be disclosed on the solicitation/invitation or receipt for the event.

A sample disclosure might look like this:

The estimated value of the goods or services received for each ticket [to the dinner/lunch/gala] is [\$XX]. Only the amount of your contribution in excess of this value is tax deductible.

2. Auctions require particular care. Fair market value of what is received needs to be established. In many cases, the amount paid is below fair market value and thus there is no charitable contribution deduction. In other cases, the amount bid will be the only indication of fair market value and thus, again, there will be no charitable contribution deduction. Also, states differ considerably in the extent of sales tax exemptions, and in a few states, such as California, the synagogue must charge - and pay - sales tax on auction items.

3. Raffles and lotteries require particular care and state laws, including state gambling law, must be consulted.

4. Under federal law, if someone wins \$600 or more gambling (and gambling includes raffles), the synagogue must issue a form W-2G, the form for reporting gambling winnings, and if winnings amount to more than \$5,000 the synagogue must withhold.

5. Sales of advertising, scrip, magazines, candy, etc. will be exempt from income tax on unrelated income if they meet some of the special exceptions to that tax. The most likely exceptions are (1) having substantially all the work conducted solely by volunteers or (2) having the sales activities not be regularly carried on - that is, sales activities conducted only a few weeks a year are not subject to tax. Special rules regarding "qualified sponsorship payments" generally exempt from the unrelated business income tax the kinds of congratulatory notices in tribute books for fundraising events.

6. Religious organizations need to determine whether they are subject to state and local solicitation or disclosure requirements.

7. Passive income received by synagogues in the form of dividends, interest, rent for real property and royalties is not subject to income tax. It is important, however, that the rent must be charged for space not for services. If anywhere between 10% and 50% of rent received is attributable to personal property, the amount attributable to rental of personal property is taxable. If more than 50% of the rent received is for personal property, all of the rental received is taxable. Thus, synagogues that rent out not only social halls but also tables and chairs, etc. for non-religious purposes need to take great care. Also, debt-financed income, even if passive, will be subject to income tax.

Attachment D

Payroll Taxes and Withholding for Clergy

1. Although clergy who work regularly part or full-time are, with only rare exceptions, employees of their synagogues, they are subject to a special set of rules when it comes to income tax withholding and liability for social security and Medicare taxes. (Note that, while there is a limit to the amount of wages to which social security taxes apply, there is no longer any limit on the taxes for Medicare.)

2. Income tax withholding is not required for clergy, although they may elect to have income tax withheld.

3. There is a special rule in the tax code requiring that clergy be treated as self-employed for purpose of **social security and Medicare** taxes (but please note, only for this purpose). That is, they are subject to self-employment tax, under SECA (the Self-Employment Contribution Act), rather than taxed as employees under FICA (Federal Insurance Contribution Act) on the amounts they are paid. In essence, this means that they are liable for both halves of this tax, where in the case of employees, the employee pays half and the employer pays half.

For clergy, because they are treated as self-employed, Social Security tax is 12.4% of wages up to up to \$132,900 in 2019. (This amount is adjusted for inflation annually.) Medicare tax is 2.9% of all wages. (For clergy, these taxes apply to net self-employment earnings; that is, based on an algebraic formula, 1/2 of the tax is deducted on their personal tax return in calculating the amount on which they pay self-employment tax.)

4. While parsonage/housing allowances are excluded from income tax, they do constitute wages for purposes of social security and Medicare tax. Clergy are subject to SECA (meaning they must pay both halves of the payroll tax) on **all** the wages they receive as clergy – **that is, on both their salary and their parsonage/housing allowance.**

5. In the vast, vast majority of situations, synagogues should report the income of clergy who work regularly for the synagogue on Form W-2, NOT Form 1099. That is, the law treating clergy as self-employed for purposes of Medicare and Social Security does NOT make them independent contractors rather than employees for purposes of reporting income. The amount of income reported is reduced by the amount of parsonage/housing allowance properly claimed by the clergyperson, although it can be listed in the "other" box on the W-2. If the synagogue withholds amounts equal to the usual employer's share of payroll taxes in order to help the rabbi or cantor satisfy payroll tax obligations, as some do, such amounts are reported as additional income tax withheld and not as social security or Medicare tax withheld.

6. If synagogues reimburse their clergy for half of the payroll taxes, this reimbursement must be reported as additional income and is itself subject to payroll taxes (subject to the rules that permit certain payroll tax deductions for people subject to self-employment tax, per #3 above.)

7. Clergy employed by synagogues remain employees for other purposes of the tax code and for state law purposes. Thus, for example, they may not deduct unreimbursed employee expenses. As employees, they are also eligible for employee fringe benefits, such as cafeteria plans, medical plans, etc. and for coverage as employees under the synagogue's insurance plans.

8. Erroneously treating clergy as self-employed independent contractors poses several kinds of risks and disadvantages for the clergy. Many tax-free fringe benefits, such as cafeteria plans, are available only to employees. Audit risk is much lower for employees. If clergy are audited, the IRS in almost all cases will reclassify them as employees, and the clergy/taxpayer may then be liable for taxes, interest and penalties for deductions improperly taken on Schedule C instead of as unreimbursed employee expenses. Generally, health plans and insurance contracts cover only employees.

Attachment E

Overview of Rules Regarding Clergy's Parsonage or Housing Allowance

1. The clergy housing allowance was recently held to be constitutional by a federal appellate court. Clergy are defined by the tax law for this purpose as those who are ordained, commissioned, or licensed. It includes invested cantors. It is uncertain whether a cantorial soloist who is named as a cantor by the congregation and function as a cantor by fulfilling the full all cantorial functions on a full-time basis would be considered clergy by the IRS or not. Clergy who are hired to fill administrative or other similar positions and who do not function as clergy are not entitled to tax-free parsonage. The IRS requires that clergy be hired to function as clergy on a substantial basis to be entitled to this allowance.

2. Clergy **who function as such in the congregation** are entitled to exclude from income the **lowest** of the following three numbers: (1) the portion of their income designated in advance by their employer as a housing/parsonage allowance; (2) the amount the clergy in fact used to pay for housing-related expenses; or (3) the fair rental value of the home (furnished) plus utilities. Thus, particularly in the year a clergy person buys a house and pays a down payment, all actual housing expenses may not be excludible from income. Legislation passed in May 2002 makes clear that housing allowances are limited to fair market rental value.

3. For any amounts to be excluded, there must be a housing/parsonage allowance adopted (1) by official action and (2) **in advance** of the time the amounts to be excluded are earned by services. Applicable IRS regulations list the following as examples of official action: employment contract, board minutes, board resolution, and congregational budget.

Some congregations follow the practice of having the clergyperson estimate, before the year begins, the housing expenses for the coming year and use that estimate as the basis of a board resolution. Such practice is perfectly acceptable.

As noted, it is also permissible to set the allowance in the clergy's employment contract, because the contract is in writing, approved by the board and adopted prior to the time when the amounts are earned.

4. Amounts that come within parsonage/housing allowance include: down payment, mortgage payments on loan to purchase or improve home (both principal and interest); real estate taxes, property insurance; utilities (electricity, gas, water, trash pickup, local telephone charges, furnishings and appliances (purchase and repair); structural repairs and remodeling; yard maintenance and improvements; maintenance items (household cleaners, light bulbs, pest control), **subject, however, to the limits described in #2 above.**

5. The amount of parsonage reduces the amount reported as compensation on the clergyperson's W-2 (or Form 1099, in those rare cases where the clergyperson is operating as an independent contractor); thus clergy need to supply these amounts to the synagogue in time to prepare the required form. Best practices call for the congregation to require that the clergyperson substantiate the amount claimed as parsonage.

6. With the possible exception of cantorial soloists functioning as cantors, clergy do not need to work full-time to be eligible for parsonage. As noted above, whether cantorial soloists are eligible for parsonage/housing allowance is uncertain.

7. Remember that anyone receiving parsonage/housing allowance **MUST** be treated as self-employed **for purposes of** social security and Medicare (payroll) taxes.(SECA, not FICA).

8. Clergy are permitted both to exclude parsonage/housing allowance from income and to deduct mortgage interest.

Attachment F

Clergy Discretionary Funds

1. Synagogues must exercise oversight of discretionary funds to protect both the clergy and the members who contribute. Clergy discretionary funds raise two different kinds of issues: income to clergy and deductibility for donors.

2. To avoid the former, the clergy cannot use the funds for personal purposes. (If they can, all monies in their discretionary fund could be deemed taxable income to them.) Examples of inappropriate personal purposes include such uses as professional dues, tickets for the clergy or their family to attend to events and dinners, gifts to others from the rabbi, satisfaction of personal pledges by the rabbi.

3. To accomplish the latter, the clergy must be acting as an agent of the synagogue. That is, the funds do not come from the clergy personally; they come from the congregation through the discretionary fund. The money is the property of the synagogue, and the synagogue board must retain oversight over the funds to ensure that they are spent for religious, educational, and charitable (i.e. tax deductible) purposes. Charitable for these purposes means relief of the poor, distressed, and needy. The IRS defines "needy" for these purposes to include not only financial impoverishment but also "a person who is temporarily not self-sufficient as a result of a sudden and severe personal or family crisis." (Moreover, these funds cannot be used for political purposes, which here means participating on behalf or in opposition to any candidate for public office, at risk of losing the synagogue's exemption.)

4. The bank account for the discretionary fund should be an account of the congregation, albeit one for which the clergy has signing authority.

5. A sample resolution to accomplish these goals might look like the following:

The rabbis and cantors act as agents of the synagogue in disbursing funds from their discretionary funds. These funds remain the property of the synagogue.

The rabbis and cantor of the synagogue are authorized to use the monies contributed to their discretionary funds for needs and projects consistent with the religious, educational, and charitable purposes of the synagogue. No monies from these discretionary funds shall be used or distributed for personal purposes of the rabbis and cantor or their family. The purposes for which discretionary funds have been used shall be reviewed annually by the then-President and or any delegates appointed by the then-President, including, should the President so choose, outside auditors.

6. Oversight by the synagogue should not violate the purpose of these funds – which is to allow the clergy to decide how to use these funds through exercise of their discretion within the broad permitted categories. Use of discretionary funds need not require prior approval, but all distributions must be reviewed for consistency with permitted uses. Thus, even use of discretionary funds for particular individuals must satisfy charitable purposes and be subject to review, but review should not violate confidentiality or expose any recipients of funds to embarrassment. The necessary oversight must be done with care and sensitivity. It can be accomplished by having the clergy report by category of the kind of uses to which they had put the funds and the amounts expended in each category, along with more detailed review annually of each distribution by one or two officers or outside auditors who are under an obligation to keep details about any individual recipient confidential. The purpose of such review is not to second guess or direct the clergy's use of the funds, but only to ensure that each use of the fund is within the permitted purposes.

Attachment G

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While any involvement in a political campaign for elective office is prohibited, religious congregations, like other charities, can participate in lobbying to a limited degree. For tax purposes, lobbying is distinguished from intervening in electoral politics. Lobbying is defined as an attempt to influence legislation, either directly through legislators or indirectly through grass root campaigns which ask citizens to contact their legislators. (Taking such positions on initiatives or propositions as well as confirmation of federal judges, is considered lobbying, not political campaign activity). Under the tax code, lobbying by charitable organizations is permitted to a limited extent; it cannot be more than an insubstantial part of the organization's activities. The meaning of insubstantial is not clear, but it is clear that it means more than dollars spent. (Organizations other than religious congregation can choose to have their lobbying activities subject to specified dollar limits, but this option is not available to religious congregations.) The Supreme Court has upheld the constitutionality of the lobbying limits, although the case did not involve a religious organization.

Attachment B

Substantiation and Quid Pro Quo Requirements

Charitable contributions of \$250 or more must be substantiated by a contemporaneous written acknowledgment from the donee organization and the charitable contribution consequences of quid pro quo contributions that exceed \$75 must be disclosed. Failure to satisfy the latter rule subjects the charity to penalties of \$10 per contribution, with a maximum of \$5,000 per event or mailing. The burden is on the taxpayer to show that all or part of a payment to a charitable organization is a contribution or gift. A charitable deduction is not allowed for a payment to charity for goods or services (other than for intangible religious benefits) unless (a) the amount paid exceeds the fair market of the goods or services and (b) the taxpayer intends to make a payment in excess of such fair market value. In determining this excess, if any, the taxpayer may rely on the value of the goods and services as provided by the donee organization, unless the taxpayer knows the donee's stated value or good faith estimate of value is unreasonable. Dues to religious congregations are deductible; what is received in return for dues is deemed to be entirely intangible religious benefit. Religious congregations should note that, with the standard deduction for married couples now at \$24,000, fewer congregants may be itemizing. Some congregants over 70-1/2 may wish to take advantage of special rules permitting contributions directly from IRAs to a charity because they satisfy required minimum distribution rules without being included in income.

Decisions by the Ninth Circuit Court of Appeals and the Tax Court, which involved suits by a family named Sklar against the IRS Commissioner, concluded that the part of the payments by parents to a Jewish religious day school for religious education are NOT deductible as charitable contributions. There is no IRS or judicial authority permitting deduction for costs of religious education; these costs are seen as payment for education, not a contribution that results in an intangible religious benefit.

In the case of donations of automobiles, applicable rules generally limit any deduction above \$500 to the amount for which the charity sells the car.

An organization may use any reasonable methodology in making a good faith estimate of the value of goods and services it provides. For goods or services that are not generally available in a commercial market, the good faith estimate may use goods or services that are similar or comparable even if they do not have the unique qualities of those offered by the organization.

Substantiation requirement for deductible contributions of \$250 or more may be satisfied for several such contributions with one or more contemporaneous acknowledgments. Since each payment is considered separately, a contribution of less than \$250 is not subject to the substantiation requirement, even if contributions exceed \$250 in the aggregate. An acknowledgment must provide (1) the amount of cash paid and a description of any property transferred, (2) a statement of whether goods or services were provided for consideration, in whole or part, for such cash or property, (3) a description and good faith estimate of the value of any goods or services so provided, and (4) a statement by organizations providing intangible religious benefits that they do so. The written acknowledgment is contemporaneous if the taxpayer obtains it on or before the earlier of the taxpayer's filing date for the original return for the taxable year in which the contribution was made or the due date, including extensions, for such return. Goods or services are provided for consideration if the "the taxpayer receives or expects to receive goods or services in exchange for payment." Goods and services received in connection with fundraising may be disregarded and thus need not be acknowledged if either they have value of not more than 2% of the amount contributed, up to a maximum (for 2019) of \$110.00, or if the goods received are only token items with the charity's name and logo or low-cost items worth no more than \$11.50 when the taxpayer makes at least a minimum payment of \$55.50. (These numbers are adjusted for inflation annually.) Newsletters of less than commercial quality and low-cost items provided for free without advanced orders also are deemed to have insubstantial value.

Acknowledgment for unreimbursed out-of-pocket expenses is satisfied if the taxpayer has records of the expenditures and obtains a timely statement from the organization describing the services provided by the taxpayer and whether the organization provided any goods or services in consideration for them.

Attachment C

Laws Regarding Charitable Fundraising

Charitable fundraising, including that conducted by religious organizations, is subject to federal, state and local laws. The rules most likely to be applicable to religious congregation fundraising activities are summarized briefly below.

1. Charitable contributions are deductible for income tax purposes only to the extent that they exceed the fair market value of what is received. NOTE: The deductible contribution must be reduced by the fair market value of what is received, not the cost to the religious congregation. Thus, having the goods or services donated to a religious congregation does not prevent reduction of the deductible amount. Additional federal disclosure laws apply to payments above \$75 that involve both a charitable donation and a receipt of goods or services. Any fundraising event that costs more than \$75 and involves the provision of a meal, such as a dinner dance or the typical "rubber chicken" dinner, will be subject to these rules. In such cases, the reduction in deductible contribution must be disclosed on the solicitation/invitation or receipt for the event.

A sample disclosure might look like this:

The estimated value of the goods or services received for each ticket [to the dinner/lunch/gala] is [\$XX]. Only the amount of your contribution in excess of this value is tax deductible.

2. Auctions require particular care. Fair market value of what is received needs to be established. In many cases, the amount paid is below fair market value and thus there is no charitable contribution deduction. In other cases, the amount bid will be the only indication of fair market value and thus, again, there will be no charitable contribution deduction. Also, states differ considerably in the extent of sales tax exemptions, and in a few states, such as California, the congregation must charge - and pay - sales tax on auction items.

3. Raffles and lotteries require particular care and state laws, including state gambling law, must be consulted.

4. Under federal law, if someone wins \$600 or more gambling (and gambling includes raffles), the religious congregation must issue a form W-2G, the form for reporting gambling winnings, and if winnings amount to more than \$5,000 the congregation must withhold.

5. Sales of advertising, scrip, magazines, candy, etc. will be exempt from income tax on unrelated income if they meet some of the special exceptions to that tax. The most likely exceptions are (1) having substantially all the work conducted solely by volunteers or (2) having the sales activities not be regularly carried on - that is, sales activities conducted only a few weeks a year are not subject to tax. Special rules regarding "qualified sponsorship payments" generally exempt from the unrelated business income tax the kinds of congratulatory notices in tribute books for fundraising events.

6. Religious organizations need to determine whether they are subject to state and local solicitation or disclosure requirements.

7. Passive income received by religious congregations in the form of dividends, interest, rent for real property and royalties is not subject to income tax. It is important, however, that the rent must be charged for space not for services. If anywhere between 10% and 50% of rent received is attributable to personal property, the amount attributable to rental of personal property is taxable. If more than 50% of the rent received is for personal property, all of the rental received is taxable. Thus, religious congregation that rent out not only social halls but also tables and chairs, etc. for non-religious purposes need to take great care. Also, debt-financed income, even if passive, will be subject to income tax.

Attachment D

Payroll Taxes and Withholding for Clergy

1. Although clergy who work regularly part or full-time are, with only rare exceptions, employees of their religious congregations, they are subject to a special set of rules when it comes to income tax withholding and liability for social security and Medicare taxes. (Note that, while there is a limit to the amount of wages to which social security taxes apply, there is no longer any limit on the taxes for Medicare.)

2. Income tax withholding is not required for clergy, although they may elect to have income tax withheld.

3. There is a special rule in the tax code requiring that clergy be treated as self-employed for purpose of **social security and Medicare** taxes (but please note, only for this purpose). That is, they are subject to self-employment tax, under SECA (the Self-Employment Contribution Act), rather than taxed as employees under FICA (Federal Insurance Contribution Act) on the amounts they are paid. In essence, this means that they are liable for both halves of this tax, where in the case of employees, the employee pays half and the employer pays half.

For clergy, because they are treated as self-employed, Social Security tax is 12.4% of wages up to up to \$132,900 in 2019. (This amount is adjusted for inflation annually.) Medicare tax is 2.9% of all wages. (For clergy, these taxes apply to net self-employment earnings; that is, based on an algebraic formula, 1/2 of the tax is deducted on their personal tax return in calculating the amount on which they pay self-employment tax.)

4. While parsonage/housing allowances are excluded from income tax, they do constitute wages for purposes of social security and Medicare tax. Clergy are subject to SECA (meaning they must pay both halves of the payroll tax) on **all** the wages they receive as clergy – **that is, on both their salary and their parsonage/housing allowance.**

5. In the vast, vast majority of situations, congregations should report the income of clergy who work regularly for the religious congregation on Form W-2, NOT Form 1099. That is, the law treating clergy as self-employed for purposes of Medicare and Social Security does NOT make them independent contractors rather than employees for purposes of reporting income. The amount of income reported is reduced by the amount of parsonage/housing allowance properly claimed by the clergyperson, although it can be listed in the “other” box on the W-2. If the religious congregation withholds amounts equal to the usual employer’s share of payroll taxes in order to help the rabbi or cantor satisfy payroll tax obligations, as some do, such amounts are reported as additional income tax withheld and not as social security or Medicare tax withheld.

6. If congregations reimburse their clergy for half of the payroll taxes, this reimbursement must be reported as additional income and is itself subject to payroll taxes (subject to the rules that permit certain payroll tax deductions for people subject to self-employment tax, per #3 above.)

7. Clergy employed by their congregations remain employees for other tax purposes and for state law purposes. Thus, for example, they may not deduct unreimbursed employee expenses. As employees, they are also eligible for employee fringe benefits, such as cafeteria plans, medical plans, etc. and for coverage as employees under the congregation’s insurance plans.

8. Erroneously treating clergy as self-employed independent contractors poses several kinds of risks and disadvantages for the clergy. Many tax-free fringe benefits, such as cafeteria plans, are available only to employees. Audit risk is much lower for employees. If clergy are audited, the IRS in almost all cases will reclassify them as employees, and the clergy/taxpayer may then be liable for taxes, interest and penalties for deductions improperly taken on Schedule C instead of as unreimbursed employee expenses. Generally, health plans and insurance contracts cover only employees.

Attachment E

Overview of Rules Regarding Clergy's Parsonage or Housing Allowance

1. The clergy housing allowance was recently held to be constitutional by a federal appellate court. Clergy are defined by the tax law for this purpose as those who are ordained, commissioned, or licensed. Clergy who are hired to fill administrative or other similar positions and who do not function as clergy are not entitled to tax-free parsonage. The IRS requires that clergy be hired to function as clergy on a substantial basis to be entitled to this allowance.
 2. Clergy **who function as such in the congregation** are entitled to exclude from income the **lowest** of the following three numbers: (1) the portion of their income designated in advance by their employer as a housing/parsonage allowance; (2) the amount the clergy in fact used to pay for housing-related expenses; or (3) the fair rental value of the home (furnished) plus utilities. Thus, particularly in the year a clergy person buys a house and pays a down payment, all actual housing expenses may not be excludible from income. Legislation passed in May 2002 makes clear that housing allowances are limited to fair market rental value.
 3. For any amounts to be excluded, there must be a housing/parsonage allowance adopted (1) by official action and (2) **in advance** of the time the amounts to be excluded are earned by services. Applicable IRS regulations list the following as examples of official action: employment contract, board minutes, board resolution, and congregational budget.

Some congregations follow the practice of having the clergyperson estimate, before the year begins, the housing expenses for the coming year and use that estimate as the basis of a board resolution. Such practice is perfectly acceptable.
- Note that the allowance can be set in the clergy's employment contract, because the contract is in writing, approved by the board and adopted prior to the time when the amounts are earned.
4. Amounts that come within parsonage/housing allowance include: down payment, mortgage payments on loan to purchase or improve home (both principal and interest); real estate taxes, property insurance; utilities (electricity, gas, water, trash pickup, local telephone charges, furnishings and appliances (purchase and repair); structural repairs and remodeling; yard maintenance and improvements; maintenance items (household cleaners, light bulbs, pest control), **subject, however, to the limits described in #2 above.**
 5. The amount of parsonage reduces the amount reported as compensation on the clergyperson's W-2 (or Form 1099, in those rare cases where the clergyperson is operating as an independent contractor); thus clergy need to supply these amounts to the congregation in time to prepare the required form. Best practices call for the congregation to require that the clergyperson substantiate the amount claimed as parsonage.
 6. In general, clergy do not need to work full-time to be eligible for parsonage.
 7. Remember that anyone receiving parsonage/housing allowance **MUST** be treated as self-employed **for purposes of** social security and Medicare (payroll) taxes (SECA, not FICA)..
 8. Clergy are permitted both to exclude parsonage/housing allowance from income and to deduct mortgage interest.

Attachment F

Clergy Discretionary Funds

1. Religious congregations must exercise oversight of discretionary funds to protect both the clergy and the members who contribute. Clergy discretionary funds raise two different kinds of issues: income to clergy and deductibility for donors.
2. To avoid the former, the clergy cannot use the funds for personal purposes. (If they can, all monies in their discretionary fund could be deemed taxable income to them.) Examples of inappropriate personal purposes include such uses as professional dues, tickets for the clergy or their family to attend to events and dinners, gifts to others from the rabbi, satisfaction of personal pledges by the rabbi.
3. To accomplish the latter, the clergy must be acting as an agent of the congregation. That is, the funds do not come from the clergy personally; they come from the congregation through the discretionary fund. The money is the property of the congregation, and the congregation's board must retain oversight over the funds to ensure that they are spent for religious, educational, and charitable (i.e. tax deductible) purposes. Charitable for these purposes means relief of the poor, distressed, and needy. The IRS defines "needy" for these purposes to include not only financial impoverishment but also "a person who is temporarily not self-sufficient as a result of a sudden and severe personal or family crisis." (Moreover, these funds cannot be used for political purposes, which here means participating on behalf or in opposition to any candidate for public office, at risk of losing the congregation's tax exemption.)
4. The bank account for the discretionary fund should be an account of the congregation, albeit one for which the clergy has signing authority.
5. A sample resolution to accomplish these goals might look like the following:

Clergy act as agents of the congregation in disbursing funds from their discretionary funds. These funds remain the property of the congregation. The clergy of the congregation are authorized to use the monies contributed to their discretionary funds for needs and projects consistent with the religious, educational, and charitable purposes of the congregation. No monies from these discretionary funds shall be used or distributed for personal purposes of the clergy or their family. The purposes for which discretionary funds have been used shall be reviewed annually by the then-President and or any delegates appointed by the then-President, including, should the President so choose, outside auditors.

6. Oversight by the congregation should not violate the purpose of these funds – which is to allow the clergy to decide how to use these funds through exercise of their discretion within the broad permitted categories. Use of discretionary funds need not require prior approval, but all distributions must be reviewed for consistency with permitted uses. Thus, even use of discretionary funds for particular individuals must satisfy charitable purposes and be subject to review, but review should not violate confidentiality or expose any recipients of funds to embarrassment. The necessary oversight must be done with care and sensitivity. It can be accomplished by having the clergy report by category of the kind of uses to which they had put the funds and the amounts expended in each category, along with more detailed review annually of each distribution by one or two officers or outside auditors who are under an obligation to keep details about any individual recipient confidential. The purpose of such review is not to second guess or direct the clergy's use of the funds, but only to ensure that each use of the fund is within the permitted purposes.

Attachment G