



---

## Pastors' Housing Allowances

**Pastors of churches and other religious organizations can save thousands of dollars annually in personal Federal income taxes by thoroughly understanding and implementing their legal rights to annual "housing allowances".** Leaders of churches and affiliated religious organizations should also understand how housing allowances "work" since they typically are involved in the process of documenting and designating annual housing allowance amounts.

### SOME BACKGROUND

Since 1921, ministers have been allowed to exclude from their taxable income the economic value of a church-owned parsonage. Although Congress has never explained the precise reason for this exemption, many believe that a pastor's housing value is tax-exempt since Federal tax law does exempt the value of lodging furnished rent-free on the employer's premises and "for the convenience of the employer" (such as an apartment complex manager/custodian who receives the use of an apartment rent-free in exchange for services). Regardless, Section 107 of the Internal Revenue Code provides that the rental value of a parsonage or rental allowance paid to a "minister of the Gospel" is exempt from Federal income tax to the extent that the allowance is actually used to rent or provide a home and to the extent the allowance does not exceed the fair rental value of the home, including furnishings, plus the cost of utilities.

### WHO QUALIFIES FOR HOUSING ALLOWANCE?

**Only "ministers" qualify for the housing allowance, and only with respect to a minister's income derived from "services performed in the exercise of ministry."** Services performed in the exercise of ministry include conducting religious worship, administering sacraments, and performing management functions for a church, denomination, or an integral agency of a church or denomination, such as a religious college).

Both the Tax Courts and the IRS have arrived at a "5 factor test" in defining "who is a minister" for the housing allowance and other unique tax matters pertaining to clergy. **The "5 factors" used in defining a minister are:**

- **Required Factor:** A person **must be "ordained, commissioned or licensed" by their church or denominational authorities;**
- The additional 4 factors are considered and "weighed" in determining whether a person is a minister for tax law purposes:

- Administers the sacraments;
- Conducts religious worship;
- Has management responsibility in a local church or religious denomination; and
- Is considered to be a religious leader by his/her church or denomination.

**All of the tax benefits associated with "clergy", including the housing allowance, are only available to "ministers" as they are defined above.**

## **DESIGNATING THE HOUSING ALLOWANCE**

**Housing allowances should be:**

- **Adopted by the church board** or other leadership of the organization;
- Should be **in writing**; and
- Should be **designated IN ADVANCE of the services being provided** (generally in advance of each new calendar year).

A housing allowance can be amended during the year but the revised amount will only apply prospectively and never retroactively.

**An template for a written "[Housing Allowance Designation](http://www.churchpaypros.com)" is illustrated at [www.churchpaypros.com](http://www.churchpaypros.com).**

## **CALCULATING THE HOUSING ALLOWANCE AMOUNT**

A minister should recalculate their estimated "housing expenses" at the end of each year for the following year, typically based on reviewing their household financial records along with anticipated additional housing costs for the following year. Since a pastor can not deduct actual housing expenses in excess of the designated housing allowance amount, **it is always best to estimate "on the high side" so that unanticipated housing costs can be deducted as part of each year's allowance** (estimating "on the high side" will provide a "cushion" if you decide to buy a new riding mower!)

See our "[Request for Housing Allowance Designation](#)" with its accompanying "[Housing Allowance Worksheet](#)" which will illustrate "best practices" as to calculating the annual housing allowance.

## **CONCLUSION**

**AccuPay has a division we call "ChurchPay Pros", which is totally focused on payroll, tax, HR and Quickbooks G/L services for our many church payroll clients.** ChurchPay Pros by AccuPay is led by Lisa Reed, SPHR and Larry Shaub, CPA, each of whom is intimately familiar with tax nuances associated with churches and pastors. You can reach Lisa or Larry at 317-885-7600. Also feel free to **"check us out" online at [www.churchpaypros.com](http://www.churchpaypros.com).**

*PayDay is an email communication of payroll news, legal updates and tax considerations intended to inform clients and colleagues of AccuPay about current payroll issues and planning techniques. You should consult with your CPA or tax advisor before implementing any ideas, comments or planning techniques.*