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Tax & Money
S E R I E S

E D I T I O N

PREPARING TAX RETURNS FOR CLERGY

Federal, state, and other reporting made easy.



by Dan Busby, CPA
John Van Drunen, JD, CPA

The federal tax laws offer you special treatment for both income taxes and social security taxes. Most congregations will gladly help you maximize the tax advantages.

This booklet includes a seven-page section on the line-by-line preparation of the Form 1040 and related key forms and schedules. There are a number of changes related to 2010 and 2011 taxes including:

- **Mileage rates.** The IRS increased the standard business mileage rate beginning January 1, 2011 from 50 cents to 51 cents per mile. On July 2, 2011, the rate was raised to 55.5 cents per mile. This rate is the same for 2012. This is the maximum rate that clergy may be reimbursed for business mileage on a tax-free basis or deduct on Form 2106, if the business miles are not reimbursed. The medical and moving mileage rate is 23 cents per mile effective January 1, 2012.
- **Retirement contribution limits.** The maximum salary reduction for 401(k) or 403(b) plans remains at \$16,500 for 2011. The annual catch-up limit for individuals age 50 or over remains at \$5,500 for 2011.
- **Social security.** The social security tax rates are in flux as Congress only extended the payroll tax “holiday” for the first two months of 2012 (there is a 2% reduction in the employee FICA rate and the SECA rate for self-employed—see page 28). It is likely they will extend this reduction through the entire year of 2012.
- **Unreimbursed expenses.** In the most recent Minister Audit Technique Guide, the IRS reinforces their position that a minister’s unreimbursed business expenses must be allocated (see page 26) based on the portion of a minister’s compensation that is taxable and nontaxable (related to a housing allowance).




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Dan Busby is a CPA with a master’s degree in business from Emporia State University, Emporia, Kansas. He served as controller at the University of Kansas Medical Center in Kansas City and later founded the CPA firm of Busby, Keller & Co. in suburban Kansas City. Formerly the chief financial officer of a religious denomination, he currently serves as president of the Evangelical Council for Financial Accountability (ECFA) in Winchester, VA. Forty-four volumes of his books have been published since 1990. *The Zondervan Minister’s Tax & Financial Guide* and *The Zondervan Church and Nonprofit Tax & Financial Guide* are published annually. He authored *Donor-Restricted Gifts Simplified* (updated in 2012 with a new title: *When Givers Designate Gifts*) and coauthored *The Christian’s Guide to Worry-free Money Management*.

John Van Drunen has a bachelor of arts in accounting, magna cum laude, from Anderson University and a juris doctor from Regent University School of Law. He is also a CPA. John has received many awards, including The Virginia Bar Association recognition for his pro bono work during his tenure as a law student. This work included working with nonprofit organizations and assisting low-income individuals by preparing their taxes. John is a member of the Christian Legal Society, American Bar Association, Virginia Bar Association, and the AICPA. He is also a member of the Alpha Chi and Delta Mu Delta Honor Societies. With Dan Busby, he co-authored *The Zondervan Minister’s Tax & Financial Guide* and *The Zondervan Church and Nonprofit Tax & Financial Guide* for 2011 and 2012. He also co-authored *When Givers Designate Gifts* in 2012 with Dan Busby. John is the vice president and in-house counsel of the Evangelical Council for Financial Accountability (ECFA) in Winchester, VA.

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Recent Developments

The year 2011 only brought modest tax and finance changes impacting ministers in preparing their 2011 tax returns. However, the health care reform legislation passed in 2010 provides a series of issues ministers must face as the law is implemented through 2018. This law continues to be challenged in the courts. A discussion of significant recent developments follows (see the “In the News” link at ECFA.org for current updates on issues affecting ministers):

Grassley requests assistance from ECFA on church tax policy issues. In 2011, Senator Charles Grassley, then the ranking member of the Senate Finance Committee, requested ECFA (Evangelical Council for Financial Accountability) facilitate response to 61-pages of church and other nonprofit tax policy issues raised by his staff. The issues relates to topics such as the minister’s housing exclusion (should the exclusion be limited, should the exclusion only apply to one house at a time and related issues), the potential of requiring churches to annually file Form 990 with the IRS, as is required for most non-church organizations, the possible clarification of the rules relating to clergy “love” offerings, compensation setting matters and whether the clergy should be allowed to speak their conscience with respect to candidates for public office.

In response to this request from Grassley, ECFA formed a national commission: the Commission on Accountability and Policy for Religious Organizations. The Commission is expected to release an initial report on its findings in 2012 and a second report in 2013.

Congress extends payroll tax “holiday.” Congress approved an extension of the FICA and SECA payroll tax “holiday,” in effect for 2011, through February 28, 2012. The extension allows employers to withhold employee payroll taxes at 4.2% (instead of 6.2%) on all wages paid during the two-month extension period, subject only to the full 2012 wage base (\$110,100) and without regard to the \$18,350 cap (two-twelfths of the wage base of \$110,100) on wages earned through the end of February 2012. The 2% holiday also applies to self-employment income, with the OASDI tax rate at 10.4%.

Minister’s housing allowance constitutional challenge dropped—new lawsuit filed. On June 17, 2011, the Freedom From Religion Foundation (FFRF) and related parties agreed to a dismissal of their lawsuit challenging the constitutionality of the housing allowance exclusion for ministers in the Internal Revenue Code.

On September 13, 2011, FFRF filed a new case seeking a declaration that the clergy housing allowance violates the First Amendment. In this lawsuit, the foundation argues that the allowance “... violates the Establishment Clause of the First Amendment to the Constitution ... by providing preferential tax benefits to ministers of the gospel.”

Tax Court allows multiple houses to be excluded under the housing allowance rules. In a split decision, the Tax Court held that a Phil Driscoll, an ordained minister and his wife, were entitled to exclude from gross income a parsonage allowance that was paid by the ministry to the minister as compensation and used to provide a second home.

The requirements for exclusion from income were satisfied because the minister used the allowance to provide a home or dwelling for himself and did not use the second home for any business purpose. The Court concluded that nothing in Code Section 107, its legislative history or the relevant regulations limited the phrase “a home” in Code Sec. 107 to only one home for purposes of the excludible parsonage allowance. The U.S. Department of Justice appealed the Tax Court decision on May 24, 2011.

Impact of health care reform on ministers. Health care reform will affect nearly all ministers. Here are the main issues impacting ministers:

- **Flexible spending account (FSA), health reimbursement account (HRA), and Health Savings Account (HSA) changes.** The law will require the following changes to these types of accounts:
 1. In 2011, ministers (and other church staff members) were no longer able to receive pre-tax reimbursements from their FSA, HRA or HSA for non-prescribed over-the-counter medications. Thus, the cost of over-the-counter medicine (other than insulin or doctor prescribed medicine) cannot be reimbursed on a tax-free basis through an HSA or Archer MSA. Medical supplies and equipment continue to qualify for reimbursement (contact lens solutions, bandages, crutches, etc.).
 2. In 2013, ministers' (and other staff members') contributions to FSAs will be capped at \$2,500 annually, with the cap adjusted annually to the Consumer Price Index.
- **Supreme Court to rule on health care law.** The U.S. Supreme Court will review the 2010 health care law in 2012.

The court accepted appeals from a decision by the U.S. Court of Appeals for the 11th Circuit in Atlanta, which is the only appellate court to date to say the law is unconstitutional. The suit was filed by the National Federation of Independent Business and 26 states, who claimed that Congress overstepped its authority by passing a law requiring most Americans to purchase health insurance or pay a steep fine. The Atlanta appellate court found in favor of the plaintiffs, calling the law's individual mandate provision "a wholly novel and potentially unbounded assertion of congressional authority."

The Supreme Court is expected to hear oral arguments in the case next March, which would be roughly two years after the law's passage. A ruling in the case will come before the court recesses in late June.

IRS provides guidance on employer-provided cell phones. For 2010 and succeeding years, the IRS will treat the value of church-provided cell phone, and similar telecommunications equipment, (including the value of any personal use by the employee) as excludible from the employee's income, as long as the cell phone is provided to the employee primarily for a noncompensatory business reason (such as the employer's need to contact the employee at all times for work-related emergencies). Providing a cell phone to promote morale or goodwill, to attract a prospective employee, or to furnish additional compensation to an employee is evidence that there is no non-compensatory business reason.

Church staff may be reimbursed for the business use of a cell phone but the church should probably require the employee to submit a copy of the monthly bill and evidence that the bill has been paid.

If a church does not have a substantial noncompensatory business reason for providing a cell phone to an employee, or reimbursing the employee for business use of his or her personal cell phone, the value of the use of the phone, or the amount of the reimbursement is includible in gross income, reportable on Forms 941 and W-2, and for lay employees is subject to federal and state employment tax withholding.

IRS announces 2012 business mileage rate. Effective January 1, 2012, the standard business mileage rate is 55.5 cents per mile—no change from the rate in effect at the close of 2011.

Key Federal Tax Limits, Rates, and Other Data			
	2010	2011	2012
Standard deductions, exemptions, and exclusions:			
Standard Deductions	Married-Joint Return \$11,400 Head of Household 8,400 Single 5,700 Married-Separate Returns 5,700	Married-Joint Return \$11,600 Head of Household 8,500 Single 5,800 Married-Separate Returns 5,800	Married-Joint Return \$11,900 Head of Household 8,700 Single 5,950 Married-Separate Returns 5,950
Personal & dependent exemption amount	\$3,650	\$3,700	\$3,800
Foreign earned income exclusion	\$91,500	\$91,900	\$95,100
Social security:			
SECA (OASDI & Medicare) rate	15.3%	13.3%	15.3%
FICA (OASDI & Medicare) rate – employee	7.65%	5.65%	5.65% ⁽¹⁾
FICA (OASDI & Medicare) rate – employer	7.65%	7.65%	7.65%
OASDI maximum compensation base	\$106,800	\$106,800	\$110,100
Social security cost of living benefit increase	0%	0%	3.6%
Social security Full Retirement Age (FRA)	66 years	66 years	66 years
Medicare Part B premiums - Basic ⁽²⁾	\$110.50	\$115.40	\$99.90
Earnings ceiling for social security (for employment before FRA; special formula in FRA year)	Below FRA: \$14,160 Over FRA: None	Below FRA: \$14,160 Over FRA: None	Below FRA: \$14,640 Over FRA: None
Earnings limit in year FRA attained	\$37,680	\$37,680	\$38,880
Benefits and contributions:			
Maximum annual contribution to defined contribution plan	\$49,000	\$49,000	\$50,000
Maximum salary deduction for 401(k)/403(b)	\$16,500	\$16,500	\$17,000
401(k) & 403(b) over 50 "catch up" limit	\$5,500	\$5,500	\$5,500
Maximum income exclusion for nonqualified plans in 501(c)(3) organizations (IRC 457)	\$16,500	\$16,500	\$17,000
IRA contribution limit – age 49 and below	\$5,000	\$5,000	\$5,000
– age 50 and above	\$1,000	\$1,000	\$1,000
Highly compensated employee limit	\$110,000	\$110,000	\$115,000
Per diem and mileage rates and other transportation:			
Standard per diem: Lowest rates in continental USA	Lodging \$70 Meals & Incidentals \$46	Lodging \$70 Meals & Incidentals \$46	Lodging \$77 Meals & Incidentals \$46
Business auto mileage rate:	50¢ per mile	1/1 – 51¢ per mile 7/1 – 55.5¢ per mile	55.5¢ per mile
Moving & medical auto mileage rate	16.5¢ per mile	1/1 – 19¢ per mile 7/1 – 23.5¢ per mile	23¢ per mile
Charitable auto mileage rate	14¢ per mile	14¢ per mile	14¢ per mile
Airplane mileage rate ⁽³⁾	\$1.29 per mile	\$1.29 per mile	
Motorcycle mileage rate	47¢ per mile	48¢ per mile	
Bicycle commuting rate	\$20 per month	\$20 per month	
Maximum value of reimbursement of business expenses (other than lodging) without receipt	\$75	\$75	\$75
Luxury automobile value (limit on use of cents-per-mile valuation of company automobile)	\$15,000	\$15,300	
Monthly limit on free parking	\$230	\$230	\$240
Transit passes/token – monthly tax-free limit	\$230	\$230	\$125
Other:			
Sec. 179 expensing limit	\$500,000	\$500,000	\$500,000
Gift tax annual exclusion	\$13,000	\$13,000	\$13,000
<p>⁽¹⁾ The 5.65% FICA employee rate reverts to 7.65% on March 1, 2012, unless Congress extends the payroll tax "holiday." ⁽²⁾ Premium for single taxpayers making \$85,000 or less and couples making \$170,000 or less ⁽³⁾ Privately owned vehicle mileage rates set by the U.S. General Services Administration. Note: In some instances, the rate for a particular year may apply to a tax return filed in a subsequent year.</p>			

Get the Big Picture

Six special tax provisions are available only to individuals who qualify as clergy under federal tax rules and who perform services that qualify in the exercise of ministry under federal tax rules.

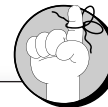
Special Tax Provisions for Clergy

- Exclusion of the housing allowance for income tax purposes and the fair rental value of a congregation-owned parsonage provided rent free to clergy.
- Exemption of clergy from self-employment tax under very limited circumstances.
- For social security tax purposes, treatment of clergy as self-employed as it relates to income from ministerial services.
- Exemption of clergy compensation from mandatory income tax withholding.
- Eligibility for a voluntary income tax withholding arrangement between clergy-employees and the congregation.
- Potential “double deduction” of mortgage interest and real estate taxes as itemized deductions and as excludable housing expenses for housing allowance purposes for clergy living in clergy-provided housing.



Remember

The major tax benefit for most clergy is the special housing allowance treatment.



Remember

There is some flexibility in applying certain clergy tax provisions. For example, clergy are exempt from mandatory income tax withholding but can enter into a voluntary income tax withholding arrangement. However, if clergy qualify for the housing allowance, self-employment social security tax (using Schedule SE) applies, not FICA—this is not optional.

● **Clergy Serving Local Congregations**

You may believe you are classified as clergy, your congregation may consider you as clergy, your denomination may classify you as clergy, but what does the IRS consider you? For tax purposes, the opinion of the IRS is the one that counts.

Determining whether you are classified as clergy for tax purposes is very important. It determines how you prepare your tax return for income and social security tax purposes. Qualified clergy are eligible for the housing allowance. This alone can exclude thousands of dollars from income taxation. Clergy calculate self-employment social security tax on Schedule SE and pay the tax with Form 1040. Nonclergy have one-half of their social security tax (FICA) withheld from salary, and the congregation pays the other half.

How can I tell whether the IRS will treat me as clergy?

If you are serving a congregation and ordained, commissioned, or licensed and meet the following four tests, the IRS will generally consider you clergy. You

- administer the sacraments,
- are considered to be a religious leader by your church,
- conduct worship services, and
- have management responsibility in the “control, conduct, or maintenance” of a congregation.



Caution

Determination of clergy status is far from a precise matter. Only a review of all the pertinent facts and circumstances for particular clergy will assist in determining whether an individual will qualify for clergy tax status.

Based on guidelines issued by the IRS, some of the four tests, but not necessarily all, must be met in determining clergy status. This flexible approach is beneficial to many clergy, because some positions relating to music, education, youth, or administration will not meet all four tests.

There is no requirement that you must be qualified to perform and actually perform every sacrament. If you are qualified to perform certain sacraments and actually perform or could perform some of the sacraments on occasion, you will generally meet this test. A similar test applies to conducting religious worship and providing management services. If you currently conduct religious worship and provide management services, have done it in the past, or could do it in the future, the test will generally be met.

Job titles have little significance for tax purposes. A licensed, commissioned, or ordained clergy may have a job title that implies a ministry function. However, the actual responsibilities of the position will determine if the four-factor test (see page 5) is met. Clergy performing services of a routine nature, such as those performed by secretaries, clerks, and janitors, generally do not qualify as clergy for tax purposes.

Because of the inconsistency of these rulings, clergy serving in a local congregation who do not clearly meet all four factors should review these matters with a qualified professional adviser before filing income tax returns.



Warning

Individuals serving local congregations must meet certain tests to qualify as a minister in the eyes of the IRS. The individual must always be ordained, licensed, or commissioned.

● Clergy in Denominational, Administrative, and Teaching Positions

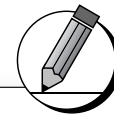
Ordained, commissioned, or licensed clergy not serving local churches may qualify as “clergy” for federal tax purposes in the following situations:

- Administration of religious denominations and their integral agencies, including teaching or administration in parochial schools, colleges, or universities that are under the authority of a denomination.
- Performing services for a parachurch organization based upon an assignment or designation by a congregation.

If a congregation does not assign or designate your services, you will qualify for the special tax treatments of clergy if your services substantially involve performing sacerdotal functions or conducting religious worship.

● Social Security Status of Clergy

Clergy engaged in the exercise of ministry are always treated as self-employed for social security purposes. Clergy pay social security under the Self-Employment Contributions Act (SECA) instead of the Federal Insurance Contributions Act (FICA). It is possible to become exempt from SECA only if you meet strict exemption



Tip

Clergy employed by institutions that are an “integral agency” of a religious denomination are subject to special tax treatment if their position is in a teaching or administrative area.



Caution

Social security is one of the most confusing issues for many clergy. FICA-type social security never applies to an individual who qualifies as clergy for tax purposes. Stated another way, if a housing allowance has been designated for you, FICA tax should not be deducted from your pay—you are responsible to determine your social security tax by completing Schedule SE each year.

requirements. The request for exemption must be filed using Form 4361 within a specified time from the beginning of your ministry. The request for exemption must be approved by the IRS (see page 28).

Your earnings that are not from the exercise of ministry are generally subject to social security tax under FICA or SECA as applied to all workers.

● Income Tax Status of Clergy

Are clergy employees or self-employed (independent contractors) for income tax purposes? The IRS considers virtually all clergy to be employees for income tax purposes. The income tax filing decision has many ramifications for what and how congregations and clergy report to the IRS.

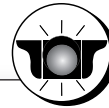
The IRS generally applies a common-law test to decide whether clergy are employees or self-employed for income tax purposes. You are an employee if your employer has the legal right to control both what you do and how you do it, even if you have considerable discretion and freedom of action. However, clergy who are employees of congregation for income tax purposes may also be self-employed for income tax purposes with respect to certain services (baptisms, marriages, and funerals).

Determining if you are an employee or self-employed for income tax purposes will determine several other tax-related issues:

- ❑ Clergy-employees must be given Form W-2 and report their compensation on page 1 of Form 1040. They are eligible to claim unreimbursed business expenses and expenses reimbursed under a nonaccountable plan on Form 2106 (2106-EZ) with the amount carried forward to Schedule A as an itemized deduction (nonaccountable plan reimbursements must be included in compensation on Form W-2). If you itemize deductions, business and professional expenses are deductible only to the extent that such expenses exceed 2% of adjusted gross income (AGI). Deductible business meals and entertainment expenses are limited to 50%.
- ❑ Health and accident insurance premiums paid directly by a congregation or reimbursed by a congregation, after the cleric provides substantiation, are not reportable as income to the clergy-employee but must be reported as taxable income to the self-employed cleric.

Clergy-employees may deduct health, accident, and long-term care insurance premiums paid personally, and not reimbursed by the congregation, on Schedule A, subject to a 7.5% limitation of adjusted gross income.

The impact of a minister being considered self-employed for income tax purposes is generally very significant even if only health insurance is considered. With health insurance premiums often running \$10,000 to \$15,000 per year, reporting these premiums as taxable (minister-employee) versus tax-free



Caution

The IRS considers virtually all clergy as employees for income tax purposes. Employee income tax status actually is very beneficial to most clergy. Many fringe benefits are tax-free only to employees.



Key Issue

The defining court case on the topic of income tax status for clergy was a case in which a United Methodist cleric (Weber) took the position he was self-employed for income tax purposes. The Tax Court held that he was an employee for income tax purposes. The decision was elevated when a federal appeals court upheld the decision.

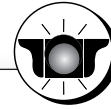


Caution

With rare exceptions, clergy should receive Form W-2 from their congregation or other employer. Few clergy qualify as independent contractors for income tax purposes (even though considered self-employed for social security tax purposes). A congregation or other employer generally has sufficient control over the cleric to qualify for W-2 treatment.

(self-employed minister for income purposes) can impact the minister's tax bill by thousands of dollars. If health insurance premiums are included in taxable income, a low-income minister might also have his or her earned income tax credit reduced or eliminated.

- Health savings accounts, health reimbursement arrangements, or flexible spending accounts are only available to clergy who are employees for income tax purposes.
- Group-term life insurance of \$50,000 or less provided by a congregation is tax-free to clergy-employees but represents taxable income for self-employed clergy.
- A voluntary arrangement to withhold income tax may be used by clergy-employees but may not be used by the self-employed.



Caution

When a church directly pays or reimburses health insurance premiums for a minister considered to be self-employed for income tax purposes, the payments are fully taxable.

● Recommended Filing Status

Virtually all clergy serving local congregations qualify as employees for income tax purposes. It is wise to file as an employee for income tax purposes, unless you can clearly demonstrate that you qualify for self-employed status. Few clergy can substantiate filing as self-employed for income tax purposes.

Congregations must provide a Form W-2 to clergy it considers to be employees. Clergy may take exception to the reporting of the congregation. For example, if the congregation gives the cleric a Form 1099-MISC or provides no W-2, the cleric may report as an employee on line 7, page 1 of Form 1040 and attach a statement to explain that the congregation did not provide a W-2.

Even though clergy may take exception to the reporting of the congregation, the congregation has a responsibility under the law to determine the proper filing method and to proceed accordingly.



Key Issue

It is vital for congregations to treat clergy as employees (Form W-2) for income tax purposes in nearly every instance. If clergy are not considered employees for income tax purposes, it jeopardizes the tax-free treatment of fringe benefits like health, accident, and long-term care insurance premiums, group-term life premiums, and certain other fringe benefits.

● Evangelists and Missionaries

The qualifications of itinerant evangelists for the special clergy tax provisions are generally the same as for clergy serving local congregations.

Most evangelists are self-employed both for income tax and self-employment social security tax purposes. The only exception is the evangelist who has formed a corporation and is an employee of the corporation. In this instance, the evangelist is an employee for income tax purposes, but remains self-employed for social security tax purposes.

Missionaries are also subject to the same rules to qualify for clergy status for tax purposes. Qualifying for benefits such as a housing allowance is often not so important for clergy-missionaries because of the foreign earned income exclusion. However, the question of clergy tax status is vitally important to determine if clergy are subject to social security as employees or as self-employed persons. The foreign-earned income exclusion affects income tax but not social security tax.

The Best Friend of Clergy

Nearly all clergy should have a portion of salary designated as a housing allowance. Maximizing housing benefits requires careful planning. For clergy living in congregation-owned housing, a housing allowance that covers expenses such as furnishings, personal property insurance on contents, utilities, and so on could save several hundred dollars of income taxes annually. A properly designated housing allowance may be worth thousands of dollars in tax savings for clergy living in their own homes or rented quarters. For clergy without a housing allowance, every dollar of compensation is taxable for federal income tax purposes.

The housing allowance provides an opportunity to *exclude* dollars from gross income. The designated housing allowance should be subtracted from compensation before the congregation completes the data on Form W-2. The housing allowance designation is not entered on Form 1040 or related schedules, except Schedule SE since it is not a deduction for income tax purposes. However, any unused portion of the housing designation must be reported as income on page 1, Form 1040.

If your congregation properly designates a portion of your cash salary for expenses of a home you provide, the exclusion is commonly referred to as a *housing* allowance. If the congregation properly designates a portion of your cash salary for expenses you incur in relation to congregation-provided housing, the exclusion is often called a *parsonage* allowance. In either instance, it is an exclusion from income tax, not self-employment tax.

Clergy are eligible to exclude the fair rental value of congregation-provided housing for income tax purposes without any official action by the congregation. However, a cash housing allowance related to congregation-provided or clergy-provided housing is only excludable under the following rules:

- The allowance must be officially designated by the congregation. The designation should be stated in writing, preferably by resolution of the top governing body, in an employment contract, or—at a minimum—in the congregation budget and payroll records. If the only reference to the housing allowance is in the congregation budget, the budget should be formally approved by the top governing body of the congregation.

Tax law does not specifically say an oral designation of the housing allowance is unacceptable. In certain instances, the IRS has accepted an oral housing designation. Still, the use of a written designation is preferable and highly recommended. The lack of a written designation significantly weakens the defense for the housing exclusion upon audit.

- The housing allowance must be designated prospectively by the congregation. Cash housing allowance payments made prior to a designation of the housing allowance are fully taxable for income tax purposes. Carefully word the resolution so that it will remain in effect until a subsequent resolution is adopted (see the examples on page 13).
- Only actual expenses can be excluded from income. The source of the funds used to pay clergy housing expenses must relate to compensation earned by clergy in the exercise of ministry in the current year.
- Only an annual comparison by clergy of housing expenses to the housing allowance is required. For example, if the housing allowance designation is stated in terms of a weekly or monthly amount, only a comparison of actual housing expenses to the annualized housing allowance is required.



Key Issue

Understanding the distinction between a housing allowance designation and the housing exclusion is fundamental. The designation is officially made by the congregation. The exclusion is the amount clergy actually exclude for income tax purposes after applying the limitations outlined here.

- The housing allowance exclusion cannot exceed the fair rental value of the furnished housing, plus utilities.

● Types of Housing Arrangements

Clergy Living in a Parsonage Owned by or Rented by a Congregation

If you live in a congregation-owned parsonage or housing rented by the congregation, the fair rental value of the housing is not reported for income tax purposes. The fair rental value is subject only to self-employment tax.

You may request a housing allowance to cover expenses incurred in maintaining the congregation-owned or rented housing. Examples of allowable expenses are utilities, repairs, furnishings, and appliances. If the actual expenses exceed the housing allowance designated by the congregation, the excess amount cannot be excluded from income.

It is appropriate for out-of-pocket expenses for the minister's out-of-pocket expenses for the maintenance of a congregation-owned parsonage to be reimbursed by the congregation if a full accounting is made. Such reimbursements do not relate to a housing allowance. If such expenses are not reimbursed, they could be excludable from income under a housing allowance.

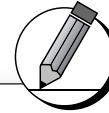
If the congregation owns the parsonage, the congregation may wish to provide an equity allowance to help compensate clergy for equity not accumulated through home ownership. An equity allowance is taxable both for income and social security tax purposes, unless directed to a 403(b) tax-sheltered annuity or certain other retirement programs.

Clergy Owning or Renting Own Home

If you own or rent your own home, you may exclude, for income tax purposes, a cash housing allowance that is the *lowest* of (1) reasonable compensation, (2) the amount used to provide a home from current congregational income, (3) the amount prospectively and officially designated, or (4) the fair rental value of the furnished home, plus utilities.

Many clergy make the mistake of automatically excluding from income, for income tax purposes, the total designated housing allowance, even though the fair rental value of the furnished home or actual housing expenses are less than the designation. This practice may cause a significant underpayment of income taxes.

Example: A cleric lives in a personally owned home. The congregation prospectively designated \$18,000 of the salary as housing allowance. The cleric spends \$17,000 for housing-related items. The fair rental value of the home is \$19,000. Since the amount spent is lower than the designated housing allowance or the fair rental value, the excludable housing is \$17,000. Therefore, \$1,000 (\$18,000 less \$17,000) must be added to taxable income on page 1, Form 1040, line 7. Unless the cleric has opted out of social security, the entire \$18,000 is reportable for social security purposes on Schedule SE.



Tip

The designation of a housing allowance for clergy living in congregation-provided housing is often overlooked. While the largest housing allowance benefits go to clergy with mortgage payments on their own homes, a housing allowance of a few thousand dollars is often beneficial to clergy in a congregation-provided home.

● Designating the Housing Allowance

The following steps are often followed in designating and excluding the housing allowance:

1. Clergy estimates the housing-related expenses to be spent in the coming year and presents this information to the congregation.
2. The congregation then adopts a written housing allowance designation based on the estimate.
3. At the close of the tax year, the cleric who provides his or her own housing compares the amount designated for housing, the housing expenses substantiated, and the fair rental value of the home including furnishings and utilities. The *lower* of these amounts is excluded for income tax purposes. Clergy living in congregation-provided housing must compare the amount designated and actual housing expenses and exclude the lower of the two amounts.



Remember

The housing allowance designation may be prospectively amended at any time during the year, regardless of whether the congregation uses a calendar or fiscal year. Changing the designation to cover expenses that have already been paid (almost all clergy use the cash basis for tax purposes) is not acceptable.

Designation Limits

The IRS does not place a limit on how much of clergy compensation may be designated as a housing allowance by the employing congregation. But practical and reasonable limits usually apply.

Unless the amount is justified based on anticipated expenses and is within the fair rental value limit, it is generally inadvisable for the congregation to exclude 100% of compensation.

It is often best for the congregation to overdesignate your parsonage allowance by a reasonable amount, subject to the fair rental value test, to allow for unexpected expenses and increases in utility costs. Any excess housing allowance designated should be shown as income on line 7 of Form 1040.

● Reporting the Housing Allowance to Clergy

The designated housing allowance may be reflected for clergy-employees on Form W-2 in Box 14 with the notation, "Housing Allowance." Though not required, this reporting method is suggested by Publication 517. Or, congregations can report the designated housing allowance to clergy by providing a statement separate from Form W-2. This may be in a memo or letter. The statement should not be attached to your income tax returns.

Your congregation may erroneously include the housing allowance on Form W-2, Box 1. If this happens, the congregation should prepare a corrected Form W-2.

● Accounting for the Housing Allowance

Determining Fair Rental Value

The determination of the fair rental value of congregation-provided housing for self-employment social security purposes is solely the responsibility of clergy. The congregation is not responsible to set the value. The fair rental value should be based on comparable rental values of other similar residences in the immediate neighborhood or community, comparably furnished.

One of the best methods to use in establishing fair rental value of your housing is to request a local realtor to estimate the value in writing. Place the estimate in your tax file and annually adjust the value for inflation and other local real estate valuation factors.

Housing Allowance in Excess of Actual Expenses or Fair Rental Value

Some clergy erroneously believe that they may exclude every dollar of the housing *designation* adopted by the congregation without limitation. The housing designation is merely the starting point. If actual expenses or the fair rental value is lower, the lowest amount is eligible for exclusion from income.

Example: A cleric living in a personally owned home receives cash compensation of \$75,000 from the congregation. The congregation prospectively designates \$20,000 as a housing allowance. The fair rental value is \$21,000. Actual housing expenses for the year are \$14,000. The amount excludable from income is limited to the actual housing expenses of \$14,000.

Actual Expenses in Excess of the Designated Housing Allowance or Fair Rental Value

Actual housing expenses that exceed the designated housing allowance are not deductible. There are no provisions to carry over “unused” housing expenses to the next year.

Example: A cleric living in a personally owned home receives cash compensation of \$60,000 from the congregation. The congregation prospectively designates \$20,000 of the \$60,000 as a housing allowance. Actual housing expenses for the year are \$50,000. The fair rental value is \$21,000. The expenses were unusually high because of a down payment on that house. The amount excludable from income is the designated housing allowance of \$20,000. There is no carryover of the \$30,000 of actual expenses in excess of the designated housing allowance to the next tax year.

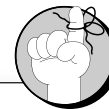
● Housing Allowances for Retired Clergy

Pension payments, retirement allowances, or disability payments paid to retired clergy from an established plan are generally taxable as pension income. However, denominations often designate a housing allowance for retired clergy to compensate them for past services to local congregations of the denomination or in denominational administrative positions. The housing allowance designated relates only to payments from the denominationally sponsored retirement program.

Withdrawals from a denominationally sponsored 403(b), also called a tax-sheltered annuity (TSA), or 401(k) plan qualify for designation as a housing allowance. Withdrawals from a 403(b) or 401(k) plan not sponsored by a local congregation are not eligible for designation as a housing allowance. Retired clergy may also exclude the rental value of a home furnished by a congregation or a rental allowance paid by a congregation as compensation for past services.

If a denomination reports the gross amount of pension or 403(b) payments on Form 1099-R and designates the housing allowance, the clergy may offset the housing expenses and reflect the net amount on page 1, Form 1040. A supplementary schedule such as the following example should be attached to the tax return:

Pensions and annuity income (Form 1040, line 16a)	\$ 10,000
Less housing exclusion	<u>8,000</u>
Form 1040, line 16b	<u>\$ 2,000</u>



Remember

Payments from denominational retirement plans are generally subject to a housing allowance designation. This means the money going into the plan is generally tax-deferred for income tax purposes and not subject to social security tax. The money coming out of the plan qualifies for exclusion for income tax purposes (subject to the actual expense limitation) and is not subject to social security tax.

For a retired minister, the amount excluded is limited to the lowest of (1) the amount used to provide a home, (2) the properly designated housing allowance, or (3) the fair rental value of the furnished home, plus utilities.

Housing Allowance Resolutions

Parsonage owned by or rented by a congregation

Whereas, the Internal Revenue Code permits clergy to exclude from gross income “the rental value of a home furnished as part of compensation” or a congregation-designated allowance paid as a part of compensation to the extent that actual expenses are paid from the allowance to maintain a parsonage owned or rented by the congregation;

Whereas, the congregation compensates (insert name) for services in the exercise of ministry; and

Whereas, the congregation provides (insert name) with rent-free use of a parsonage owned by (rented by) the congregation as a portion of the compensation for services rendered to the congregation in the exercise of ministry;

Resolved, That the compensation of (insert name) is \$4,500 per month, of which \$2,000 per month is a designated housing allowance; and

Resolved, That the designation of \$2,000 per month as a housing allowance shall apply until otherwise provided.

Home owned or rented by clergy

Whereas, the Internal Revenue Code permits clergy to exclude from gross income a church-designated allowance paid as part of compensation to the extent used for actual expenses in owning or renting a home; and

Whereas, the congregation compensates (insert name) for services in the exercise of ministry;

Resolved, That the compensation of (insert name) is \$4,500 per month, of which \$2,000 per month is a designated housing allowance; and

Resolved, That the designation of \$2,000 per month as a housing allowance shall apply until otherwise provided.

Evangelists

Whereas, the Internal Revenue Code permits clergy to exclude from gross income a congregation-designated allowance paid as part of compensation to the extent used in owning or renting a permanent home; and

Whereas, the congregation compensates (insert name) for services in the exercise of ministry as an evangelist;

Resolved, That the honorarium paid to (insert name) shall be \$1,512, consisting of \$312 for travel expenses (with documentation provided to the congregation), \$500 for housing allowance, and a \$700 honorarium.

Housing Allowance Worksheet

Clergy Living in Housing Owned or Rented by the Congregation

Name: _____

For the period _____, 20__ to _____, 20__

Date designation approved _____, 20__

Allowable Housing Expenses *(expenses paid from current income)*

	<u>Estimated Expenses</u>	<u>Actual</u>	
Utilities (<i>gas, electricity, water</i>) and trash collection	\$ _____	\$ _____	
Local telephone expense (<i>base charge</i>)	_____	_____	
Decoration and redecoration	_____	_____	
Structural maintenance and repair	_____	_____	
Landscaping, gardening, and pest control	_____	_____	
Furnishings (<i>purchase, repair, replacement</i>)	_____	_____	
Personal property insurance on minister-owned contents	_____	_____	
Personal property taxes on contents	_____	_____	
Umbrella liability insurance	_____	_____	
Subtotal	_____	_____	
10% allowance for unexpected expenses	_____	_____	
TOTAL	\$ _____	\$ _____	(A)
Properly designated housing allowance		\$ _____	(B)

The amount excludable from income for federal income tax purposes is the *lower* of A or B.

Housing Allowance Worksheet

Clergy-Owned Housing

Name: _____

For the period _____, 20__ to _____, 20__

Date designation approved _____, 20__

Allowable Housing Expenses (*expenses paid from current income*)

	<u>Estimated Expenses</u>	<u>Actual</u>
Down payment on purchase of housing	\$ _____	\$ _____
Housing loan principal and interest payments ⁽¹⁾	_____	_____
Real estate commission, escrow fees	_____	_____
Real property taxes	_____	_____
Personal property taxes on contents	_____	_____
Homeowner's insurance	_____	_____
Personal property insurance on contents	_____	_____
Umbrella liability insurance	_____	_____
Structural maintenance and repair	_____	_____
Landscaping, gardening, and pest control	_____	_____
Furnishings (<i>purchase, repair, replacement</i>)	_____	_____
Decoration and redecoration	_____	_____
Utilities (<i>gas, electricity, water</i>) and trash collection	_____	_____
Local telephone expense (<i>base charge</i>)	_____	_____
Homeowner's association dues/condominium fees	_____	_____
Subtotal	_____	
10% allowance for unexpected expenses	_____	
TOTAL	\$ _____	\$ _____ (A)
Properly designated housing allowance		\$ _____ (B)
Fair rental value of furnished home, plus utilities		\$ _____ (C)

⁽¹⁾ Loan payments on home equity loans or second mortgages are includible only to the extent the loan proceeds were used for housing expenses.

The amount excludable from income for federal income tax purposes is the *lowest* of A, B, or C.

More Than Meets the Eye

Ask most clergy how much he or she is paid and the response will often be: “My check from the church is \$1,000 a week.” But that tells us very little. Not only is your salary subject to tax, but so are many fringe benefits that you may receive.

What are fringe benefits? A fringe benefit is any cash, property, or service that clergy receives from the congregation in addition to salary. The term “fringe benefits” is really a misnomer because clergy have come to depend on them as a part of the total compensation package. All fringe benefits are taxable income to clergy unless specifically exempted by the Internal Revenue Code.

Many fringe benefits can be provided by a congregation to a clergy without any dollar limitation (health insurance is an example), while other fringe benefits are subject to annual limits (dependent care is an example). A brief discussion of some of the key fringe benefits follows.

● Tax Treatment of Compensation Elements

- **Business and professional expenses reimbursed with adequate accounting.** If the congregation reimburses clergy under an *accountable* plan for employment-related professional or business expenses (for example, auto, other travel, subscriptions, and entertainment), the reimbursement is not taxable compensation and is not reported to the IRS by the congregation or clergy. Per diem reimbursements up to IRS-approved limits also qualify as excludable reimbursements. Allowances or reimbursements under a nonaccountable plan must be included in clergy taxable income.
- **Club dues and memberships.** Club dues are not deductible or reimbursable. This includes dues for any club organized for business, pleasure, recreation, or other social purposes. The disallowance provision for club dues does not extend to dues for professional organizations (such as a ministerial association) or public service organizations (such as Kiwanis, Rotary, and Lions Clubs). If the congregation pays the health, fitness, or athletic facility dues for clergy, the amounts paid are generally fully includible in clergy income as additional compensation.
- **Disability insurance.** If the congregation pays the disability insurance premiums (and the cleric is named as the beneficiary) as a part of the compensation package, the premiums are excluded from income. However, any disability policy proceeds must be included in gross income. This is based on who paid the premiums for the policy covering the year when the disability started. If the premiums are shared between the congregation and clergy, then the benefits are taxable in the same proportion as the payment of the premiums.

Conversely, if you pay the disability insurance premiums or have the congregation withhold the premiums from your salary, you receive no current deduction and any disability benefits paid under the policy are not taxable to you.

A third option is for the congregation to pay the disability premiums. But instead of treating the premiums as tax-free, the congregation treats the premiums as additional clergy compensation. Benefits you receive under this option are tax-free.

- **Educational reimbursement plans.** If your congregation requires you to take educational courses or you take job-related courses, and your congregation either pays the expenses directly to the educational organization or reimburses you for the expenses after you make a full accounting, you may not have to include in your income the amount paid by your church.



Idea

Statistics suggest that clergy are seven times more likely to need disability insurance than life insurance before age 65. When a congregation provides the maximum disability insurance as a tax-free benefit, it could reduce the awkwardness of clergy transition relating to disability while serving the congregation.

While there are no specific dollar limits on educational expenses paid under a nonqualified reimbursement plan, the general ordinary and necessary business expense rules do apply. These types of payments may be discriminatory.

Though the education may lead to a degree, expenses may be deductible or reimbursable if the education

- is required by your church to keep your salary, status, or job (and serves a business purpose of your church), or
- maintains or improves skills required in your present employment.

Even though the above requirements are met, expenses do not qualify if the education is

- required to meet the minimum educational requirements of your present work, or
- part of a program of study that will qualify you for a new occupation.

- **Entertainment expenses.** Clergy may deduct ministry-related entertainment expenses. Entertainment expenses must be directly related to or associated with the work of the congregation. Entertainment expenses are not deductible if they are lavish or extravagant.

If business meal and entertainment expenses are not reimbursed under an accountable plan, only 50% of the expenses are deductible. If the congregation reimburses the expenses, a 100% reimbursement may be made.

- **Flexible spending account (FSA).** “Cafeteria” or FSAs are plans used to reimburse the employee for certain personal expenses. They are provided by employers to pre-fund dependent care, medical, or dental expenses (often called a healthcare flexible spending account) in pre-tax dollars.

A cafeteria or flexible spending plan cannot discriminate in favor of highly compensated participants for contributions, benefits, or eligibility to participate in the plan. While only larger churches generally offer cafeteria plans because of plan complexity and cost, many churches could feasibly offer an FSA.

The IRS has approved an administrative grace period as a way to provide relief without running afoul of the prohibition on deferred compensation. Under this provision, employees are permitted a grace period of 2½ months immediately following the end of the plan year. Expenses for qualified benefits incurred during the grace period may be paid or reimbursed from benefits or contributions remaining unused at the end of the plan year.

- **Health insurance.** If the congregation pays the medical insurance premiums directly to the insurance carrier or reimburses clergy-employees for the premiums based on substantiation, the premiums are tax-free to clergy. However, if similar payments are made for clergy who the congregation considers to be self-employed for income tax purposes, the payments represent taxable income.

Congregations are *exempt* from the requirements imposed on other employers to refrain from discriminating in favor of more highly paid individuals for health insurance programs handled through an insurance carrier.

- **Health reimbursement arrangement (HRA).** A properly designed, *written* employee HRA under which the congregation pays the medical expenses of the cleric, spouse, and dependents, not



Idea

A college costs deduction for itemizers and non-itemizers alike is available up to \$4,000. To take this deduction, the education need not be necessary for you to keep your position. The education can even qualify you for a new occupation.

covered by health insurance, may be nontaxable to clergy-employees. Typical expenses covered by such a plan are deductibles, co-insurance, and non-covered amounts paid by the individual.

HRAs may *only* be funded by congregation-provided funds. Funding by a salary reduction election is not permitted. Excess money in an HRA can be carried over to a future year without any tax implications to clergy. HRAs may not discriminate in favor of highly compensated clergy, with regard to either benefits or eligibility. HRAs may not discriminate in favor of highly compensated employees with respect to either benefit or eligibility.

- **Health savings account (HSA).** HSAs are individual, portable, tax-free, interest-bearing accounts (typically held by a bank or insurance company) through which individuals with a high-deductible health plan (HDHP) save for medical expenses.

Within limits, HSA contributions made by employers are excludable from income tax and social security wages and do not affect the computation of the earned income credit. HSA contributions may not be funded through salary reduction. Earnings on amounts in an HSA are not currently taxable and HSA distributions used to pay for medical expenses are not taxable.

- **Insurance/group-term life.** If the group life coverage provided under a nondiscriminatory plan does not exceed \$50,000 for clergy, the life insurance premiums are generally tax-free to clergy-employees. For a clergy-employees, group-term life insurance coverage of more than \$50,000 provided to clergy by the congregation is taxable under somewhat favorable IRS tables.
- **Social security tax reimbursement.** Congregations commonly reimburse clergy for a portion or all of their self-employment social security (SECA) tax liability. Any social security reimbursement must be reported as taxable income.

Because the self-employment tax is deductible in both the income tax and self-employment tax computations, a full reimbursement is effectively less than the gross 15.3% rate (the payroll tax “holiday” is ignored for this example):

<u>Your Marginal Tax Rate</u>	<u>Effective SECA Rate</u>
0%	14.13%
10	13.42
15	13.07
27	12.22
30	12.01

- **Tuition and fee discounts.** If you are an employee of a church-operated elementary, secondary, or undergraduate institution, certain tuition and fee discounts provided to a minister, spouse, or dependent children are generally tax-free. The discounts must be nondiscriminatory and relate to an educational program.

If you are employed by the church and not by the church-related or church-operated private school, any tuition and fee discounts that you receive are taxable income.

- **Vehicles/personal use of church-owned vehicle.** The personal use of a congregation-provided vehicle is considered a taxable fringe benefit. The fair market value of the personal use must be included in clergy gross income, unless the full value is reimbursed to the congregation.



Caution

An allowance to cover the minister's self-employment social security tax provides absolutely no tax benefit since the amount is fully taxable. However, paying at least one-half of the minister's social security tax is important so this amount can be properly shown as a fringe benefit for compensation analysis purposes.

**Compensation, Fringe Benefit, and Reimbursement
Reporting for Income Tax Purposes**

Explanation	Clergy-Employee
Bonus or gift from the congregation	Taxable income/Form W-2
Business and professional expenses reimbursed with adequate accounting	Tax-free/excluded
Business and professional expense payments without adequate accounting	Deduction on Schedule A, Miscellaneous Deductions. Subject to 2% of AGI and 50% meals and entertainment limits
Club dues paid by the congregation	Taxable income/Form W-2 (exception for dues for civic and public service groups)
Compensation reported to clergy by the congregation	Form W-2
Dependent care assistance payments	Tax-free, subject to limitations
Educational assistance programs	May be eligible to exclude up to \$5,250 of qualified assistance
Earned income tax credit (EITC)	May be eligible for EITC
401(k) plan	Eligible for 401(k)
403(b) tax-sheltered annuity	Eligible for 403(b)
Gifts/personal (not handled through the congregation)	Tax-free/excluded
Health savings account	Tax-free, if plan is properly established
Healthcare flexible spending account	Tax-free, if plan is properly established
Health reimbursement arrangement	Tax-free, if plan is properly established
Housing allowance	Excludable, subject to limitations
IRA payments by congregation	Taxable income/Form W-2, may be deducted on Form 1040, Line 25
Insurance, disability paid by congregation; clergy – beneficiary	Premiums are tax-free, but proceeds are taxable
Insurance, disability paid by clergy; clergy – beneficiary	Proceeds are tax-free
Insurance, group-term life paid by congregation	First \$50,000 of coverage is tax-free
Insurance, health	Tax-free, if directly paid by congregation or reimbursed to clergy upon substantiation (“newsletter” plan payments do not qualify). If paid by clergy and not reimbursed by congregation, report on Schedule A

**Compensation, Fringe Benefit, and Reimbursement
Reporting for Income Tax Purposes**

Explanation	Minister-Employee
Insurance, life, whole or universal, congregation is beneficiary	Tax-free/excluded
Insurance, life, whole or universal, clergy designates beneficiary	Taxable income/Form W-2
Insurance, long-term care	Tax-free if directly paid by the congregation or reimbursed to clergy on substantiation. If paid by clergy and not reimbursed by congregation, deduct on Schedule A subject to limitations
Loans, certain low-interest or interest-free loans over \$10,000 to clergy	Imputed (the difference between the IRS-established interest rate and the rate charged) interest is taxable income/Form W-2
Moving expenses paid by the congregation (only applies to certain qualified expenses)	Tax-free if directly paid by the congregation or reimbursed to clergy on substantiation. Reported on Form W-2, Box 12, using Code P
Pension payments by the congregation to a denominational plan for clergy	Tax-deferred. No reporting required until the funds are withdrawn by clergy or pension benefits are paid
Per diem payments for meals, lodging, and incidental expenses	May be used for travel away from home under an accountable reimbursement plan
Professional income (weddings, funerals)	Taxable income/Schedule C (C-EZ)
Property transferred to clergy at no cost or less than fair market value	Taxable income/Form W-2
Retirement or farewell gift to clergy from congregation	Taxable income/Form W-2
Salary from congregation	Report salary on page 1, Form 1040
Social security reimbursed by congregation to clergy	Taxable income/Form W-2
Travel paid for cleric's spouse by the congregation	May be tax-free if there is a business purpose
Tuition and fee discounts	May be tax-free in certain situations
Value of home provided to clergy	Tax-free/excluded
Vehicles/personal use of congregation-owned auto	Taxable income/Form W-2
Voluntary withholding	Eligible for voluntary withholding agreement

How Much Are They Worth?

Most clergy spend several thousands of dollars each year on congregation-related business expenses. For example, the ministry-related portion of auto expenses is often a major cost.

Business and professional expenses fall into three basic categories: expenses reimbursed under an accountable plan, expenses reimbursed under a nonaccountable plan, and unreimbursed expenses. The last two categories are treated the same for tax purposes. You will almost always save tax dollars if your expenses are reimbursed.

The reimbursement of an expense never changes the character of the item from personal to business. Business expenses are business whether or not they are reimbursed. Personal expenses are always nondeductible and nonreimbursable. If a personal expense is inadvertently reimbursed by the congregation, clergy should immediately refund the money to the congregation.

To be deductible or reimbursable, a business expense must be both ordinary and necessary. An *ordinary* expense is one that is common and accepted in your field. A *necessary* expense is one that is helpful and appropriate for your field. An expense does not have to be indispensable to be considered necessary.



Key Issue

Combining an accountable expense reimbursement plan with a housing allowance or health reimbursement arrangement (or any other fringe benefit plan) is not permissible. These concepts are each covered under separate sections of the tax law and cannot be commingled.

● Accountable and Nonaccountable Expense Reimbursement Plans

An accountable plan is a reimbursement or expense allowance arrangement established by your congregation that requires (1) a business purpose for the expenses, (2) substantiation of the expenses to the congregation, and (3) the return of any excess reimbursements.

The substantiation of expenses and return of excess reimbursements must be handled within a reasonable time. The following methods meet the “reasonable time” definition:

➤ The fixed date method applies if:

- an advance is made within 30 days of when an expense is paid or incurred;
- an expense is substantiated to the congregation within 60 days after the expense is paid or incurred; and
- an excess amount is returned to the congregation within 120 days after the expense is paid or incurred.

➤ The periodic statement method applies if:

- the congregation provides employees with a periodic statement that sets forth the amount paid that is more than substantiated expenses under the arrangement;
- the statements are provided at least quarterly;
- the congregation requests that clergy provide substantiation for any additional expenses that have not yet been substantiated and/or return any amounts remaining unsubstantiated within 120 days of the statement.

If you substantiate your business expenses to the congregation and any unused payments are returned, expense reimbursements have no impact on your taxes. The expenses reimbursed are not included on Form W-2 or deducted on your tax return.

The IRS disallows deductions for unreimbursed business expenses on the premise that the expenses can be allocated to a tax-exempt housing allowance (see page 26). This is another reason that all clergy should comply with the accountable expense reimbursement rules. The goal should be to eliminate all unreimbursed business expenses.

Nonaccountable Expense Reimbursement Plans

If you do not substantiate your business expenses to the congregation, or if the amount of the reimbursement exceeds your actual expenses and the excess is not returned to the congregation within a reasonable period, your tax life becomes more complicated. Nonaccountable reimbursements and excess reimbursements over IRS mileage or per diem limits must be included in your gross income and reported as wages on Form W-2.

Unreimbursed expenses or expenses reimbursed under a nonaccountable plan can be deducted only as itemized miscellaneous deductions and only to the extent that they, with your other miscellaneous deductions, exceed 2% of your adjusted gross income. Unreimbursed expenses are not deductible if you are an employee for income tax purposes and do not itemize.

If your congregation pays you an “allowance” for business expenses, it represents taxable compensation. The term “allowance” implies that the payment is not based upon documented expenses, does not meet the adequate accounting requirements for an accountable plan, and must be included in your income.



Warning

Many clergy are paid expense “allowances.” These payments accomplish nothing in terms of good stewardship. “Allowances” are fully taxable for income and social security tax purposes. Clergy must then resort to trying to deduct their expenses—much of which will be limited by the tax law—instead of receiving a full reimbursement.

● Documenting Business Expenses

For expenses to be allowed as deductions, you must show that you spent the money and that you spent it for a legitimate business reason. To prove that you spent the money, you generally need to provide documentary evidence that can be confirmed by a third party. Canceled checks, credit card or other receipts are excellent evidence. To the IRS, third-party verification is important; if business expenses are paid in cash, be sure to get a receipt.

Documenting a business expense can be time-consuming. The IRS is satisfied if you note the five Ws on the back of your credit card slip or other receipt:

- Why (business purpose)
- What (description, including itemized accounting of cost)
- When (date)
- Where (location)
- Who (names of those for whom the expense was incurred; *e.g.*, meals and entertainment)

The only exception to the documentation rules is if your individual outlays for business expenses, other than for lodging, come to less than \$75. The IRS does not require receipts for such expenses, although the five Ws are still required. You always need a receipt for lodging expenses. A congregation may apply a documentation threshold lower than \$75.



Remember

When clergy provide a listing of business expenses to the congregation or other employer—this is only a report, not documentation. Documentary evidence is much more than a report. It involves a hard-copy support of the five Ws (why, what, when, where, and who).

● Auto Expense Deductions

A minister's car expenses are deductible or reimbursable to the extent they are for business (or income producing) rather than personal use. Generally, only those expenses that are necessary to drive and maintain a car that is used to go from one workplace to another are deductible.

Mileage and Actual Expense Methods

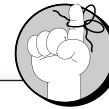
In determining your deduction for the business use of a personal car, you can use one of two methods to figure your deduction: the standard mileage rate or the actual expense method. Generally, you can choose the method that gives you the greater deduction.

Standard Mileage Rate Method

If your congregation pays you a fixed mileage rate up to the IRS standard rate (see page 4 for rates) and you provide the congregation with the time, place, and business purpose of your driving, you have made an adequate accounting of your automobile expenses.

If the congregation does not reimburse you for auto expenses or reimburses you under a nonaccountable plan, you may deduct business miles on Form 2106 (2106-EZ). The total from Form 2106 (2106-EZ) is carried to Schedule A, Miscellaneous Deductions.

The standard mileage rate, which includes depreciation and maintenance costs, is based on the government's estimate of the average cost of operating an automobile. Depending upon the make, age, and cost of the car, the mileage rate may be more or less than your actual auto expense. If you use the mileage rate, you also may deduct parking fees and tolls and the business portion of personal property tax. All auto-related taxes must be claimed on Schedule A for employees.



Remember

The standard mileage rate may generate a lower deduction than using actual expenses in some instances. But the simplicity of the standard mileage method is a very compelling feature.

Actual Expense Method

If you keep accurate records, determining your deduction for most expenses should be straightforward. Generally, the amount of depreciation you may claim and the method you use to calculate it depend on when you purchased your auto and began to use it for ministerial purposes.

Under the actual expense method, you can use either accelerated depreciation or straight-line depreciation. As the names imply, the accelerated method front-loads the depreciation, giving you larger deductions sooner. The straight-line method gives you the same depreciation deduction every year.

Allowable expenses under the actual expense method include: gas and oil, interest on an auto loan, repairs, lease payments, tires, automobile club membership, batteries, car washes and waxes, insurance, license plates, parking fees and tolls, and supplies, such as antifreeze.



Warning

You have an important decision to make the first year you put a car into service. You will generally want to use the standard mileage rate in that first year. If you do not use the standard mileage rate in the first year, you may not use it for that car in any year.

Commuting

Personal mileage is never deductible. Commuting expenses are nondeductible personal expenses.

Unless your home-office qualifies as a home-office under tax law, travel from home to the worship center (a regular work location) and return for worship services and other work at the worship center is commuting and is not deductible or reimbursable. The same rule applies to multiple trips made in the same day. The cost of traveling between your home and a temporary work location is generally deductible or reimbursable. Once you arrive at the first work location, temporary or regular, you may deduct trips between work locations.

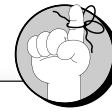
A regular place of business is any location at which you work or perform services on a regular basis. These services may be performed every week, for example, or merely on a set schedule. A temporary place of business is any location at which you perform services on an irregular or short-term (i.e., generally a matter of days or weeks) basis.

Documentation of Auto Expense

To support your automobile expense deduction or reimbursement, automobile expenses must be substantiated by adequate records. A weekly or monthly mileage log that identifies dates, destinations, business purposes, and odometer readings in order to allocate total mileage between business and personal use is a basic necessity if you use the mileage method. If you use the actual expense method, a mileage log and supporting documentation on expenses is required.

Per diem allowance

The IRS provides per diem allowances under which the amount of away-from-home meals and lodging expenses may be substantiated. These rates may not be used to claim deductions for unreimbursed expenses and may not be used to reimburse volunteers. The standard 2011-12 per diem rates for travel inside the continental United States are: lodging, \$77; meals and incidentals \$46. Higher per diem rates apply to certain locations annually identified by the IRS.



Remember

For your records to withstand an IRS audit, use a daily mileage log to document business vs. personal mileage. Whether you keep a notepad in the car or track the data in a PDA, some type of a log is the best approach to submitting data for reimbursement from your congregation or taking a tax deduction.

● Other Business and Professional Expenses

Business Gifts

You can deduct up to \$25 per donee for business gifts to any number of individuals every year. Incidental costs, such as for engraving, gift wrapping, insurance, and mailing do not need to be included in determining whether the \$25 limit has been exceeded.

The gifts must be related to your ministry. Gifts to congregation staff or board members would generally be deductible, subject to the \$25 limit. Wedding and graduation gifts generally do not qualify as business expenses.

Entertainment

Meal and entertainment expenses are deductible or reimbursable if they are ordinary and necessary and are either directly related to or associated with your ministerial responsibilities.

Personal Computers

Personal computers you own and use more than 50% for ministry may be depreciated (or reimbursed) as five-year recovery property or deducted (but not reimbursed) under Section 179 up to \$500,000 in 2011 on a joint return. The business portion of depreciation may be reimbursed under an accountable expense reimbursement plan if the 50% business “convenience of the congregation” and “condition of employment” tests are met.

If a computer is provided by the congregation in the congregation office but you prefer to work at home on your personal computer, it is not being used for the congregation’s convenience. If you meet the “convenience of the congregation” and “condition of employment” tests but do not use your computer (and related equipment) more than 50% of the time for your work, you must depreciate these items using the straight-line method and you cannot use the Section 179 write-off. If you qualify under the office-in-the-home rules, the 50% test does not apply to you.

Adequate records of the business use of your computer should be maintained to substantiate your deductions. Similar rules apply to cellular telephones.

Subscriptions and Books

Subscriptions to ministry-related periodicals are deductible. If the information in a news magazine relates to your ministerial preparation, that periodical may qualify for a deduction.

The cost of books related to your ministry with a useful life of one year or less may be deducted. The cost of books with a useful life of more than one year may be depreciated over the useful life.

Telephone

You may not deduct, as a business expense, any of the basic local service charges (including taxes) for the first telephone line into your home. Ministry-related long distance calls, a second line, special equipment, and services used for business such as call-waiting are deductible. If you are out of town on a business trip, the IRS generally will not challenge a reasonable number of calls home. Although your basic local telephone service for the first telephone line into your home is not deductible for tax purposes, it is includible as housing expense for housing allowance purposes.

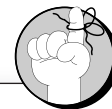
Telephone/Cellular

For 2010 and succeeding years, the IRS will treat the value of church-provided cell phone, and similar telecommunications equipment, (including the value of any personal use by the employee) as excludible from the employee’s income, as long as the cell phone is provided to the employee primarily for a noncompensatory business reason (such as the employer’s need to contact the employee at all times for work-related emergencies). Providing a cell phone to promote morale or goodwill, to attract a prospective employee, or



Warning

If clergy purchase a computer and uses it primarily for congregation work and meets the “condition” and “convenience” tests, only the depreciation on the business portion of the computer can be reimbursed by the congregation, not the entire cost of the business portion, based on the Section 179 first-year write-off rules.



Remember

If a church provides a cell phone to an employee primarily for a noncompensatory business reason, the value of the cell phone is excludible from the employee’s income.

to furnish additional compensation to an employee is evidence that there is no noncompensatory business reason.

Church staff may be reimbursed for the business use of a cell phone but the church should probably require the employee to submit a copy of the monthly bill and evidence that the bill has been paid.

If a church does not have a substantial noncompensatory business reason for providing a cell phone to an employee, or reimbursing the employee for business use of his or her personal cell phone, the value of the use of the phone, or the amount of the reimbursement is includible in gross income, reportable on Forms 941 and W-2, and for lay employees is subject to federal and state employment tax withholding.

● Allocation of Business Expenses

If you receive a rental or parsonage allowance that is tax-free, you must allocate the expenses of operating your ministry (this is commonly referred to as the “Deason Rule”). You cannot deduct expenses that are allocable to your tax-free rental or parsonage allowance. This rule does not apply to your deductions for home mortgage interest or real estate taxes. See examples on pages 40 and 58.

This limitation requires the following calculation:

1. Amount of tax-exempt income (the fair rental value of a congregation-provided parsonage and the housing allowance excluded from gross income; this may be less than the congregation-designated housing allowance) \$ _____

2. Total income from ministry:

Salary (including the fair rental value of a congregation-provided parsonage and the housing allowance excluded from gross income)	\$ _____	
Fees	_____	
Allowances (nonaccountable plan)	_____	\$ _____

3. Divide line 1 amount by line 2 amount = % of nontaxable income. _____ %

4. Total unreimbursed business and professional expenses, less 50% of meals and entertainment expenses. \$ _____

5. Multiply line 4 total by line 3 percentage (these are non-deductible expenses allocable to tax-exempt income). \$ _____

6. Subtract line 5 amount from line 4 amount (these are deductible expenses for federal income tax purposes on Form 2106 [2106-EZ] or Schedule C [C-EZ]). \$ _____

Income Taxes

The federal income tax is a pay-as-you-go tax. You must pay the tax as you earn or receive income during the year. Employees usually have income tax withheld from their pay. However, the pay of qualified clergy is not subject to mandatory federal income tax withholding. Clergy who are employees for income tax purposes may enter into a voluntary withholding agreement with the congregation to cover any income tax and self-employment social security tax that are due. IRS Publication 505 provides additional information on tax withholding and estimated taxes.

● **Tax Withholding**

Congregations are not required to withhold income taxes from wages paid to clergy for services performed in the exercise of their ministry. The exemption does not apply to nonministerial congregation employees such as a secretary, organist, or custodian.

Clergy-employees may have a voluntary withholding agreement with the employing congregation to cover income taxes (the amount may be set high enough to also cover the self-employment tax liability). Clergy need only file Form W-4 with the congregation to establish a voluntary withholding arrangement.



Idea

Though not required, congregations should offer to withhold federal (and state and local, where applicable) income taxes (never FICA taxes!) from clergy pay. Filing Forms 1040-ES often means saving up money for the 4/15, 6/15, 9/15, and 1/15 deadlines. Withholding the proper amount each week or payday is so much more efficient.

● **Estimated Tax**

Estimated tax is the method used to pay income and self-employment taxes for income that is not covered by income tax withholding. Your estimated tax is your expected tax for the year minus your projected withholding and credits.

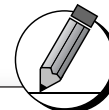
If you are filing a declaration of estimated tax, complete the quarterly Forms 1040-ES. If 2012 estimated taxes are \$1,000 or less, no declaration of estimated tax is required.

If your estimated tax payments for 2012 equal 90% of the 2011 tax liability, you will generally avoid underpayment penalties. An option is to make the 2012 estimated tax payments equal 100% of your 2011 federal and social security taxes (Form 1040, page 2, line 60). This method generally avoids underpayment penalties and is easier to calculate.

In estimating 2012 taxes, net earnings from self-employment should be reduced before calculating the self-employment tax. There also is an income tax deduction for one-half of your self-employment tax (Form 1040, page 1, line 27).

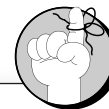
You pay one-fourth of your total estimated taxes in installments as follows:

<u>For the Period</u>	<u>Due Date</u>
Jan. 1 - Mar. 31	April 15
April 1 - May 31	June 15
June 1 - Aug. 31	September 15
Sept. 1 - Dec. 31	January 15



Filing Tip

When using the estimated tax method of submitting income and social security tax money to the IRS, pay at least as much as your previous year's total taxes (before offsetting withholding, estimated tax payments, etc.). Spread the payments equally over the four Forms 1040-ES. This will generally avoid underpayment penalties.



Remember

State income tax payment requirements may also be met by making estimated state tax payments.

Social Security Taxes

Social security taxes are collected under two systems. Under the Federal Insurance Contributions Act (FICA), the employer pays one-half of the tax and the employee pays the other half. Under the Self-Employment Contributions Act (SECA), the self-employed person pays all the tax (self-employment tax) as calculated on the taxpayer's Schedule SE.

Compensation received by clergy for services performed in the exercise of ministry is self-employment income and is always subject to self-employment tax (SECA). Ministerial income is exempt from SECA only if you have opted out of social security. Federal Insurance Contributions Act (FICA) social security tax should *never* be withheld from the compensation of qualified clergy.

● Opting Out of Social Security Taxes

All clergy are automatically covered by social security (SECA) for services in the exercise of ministry, unless an exemption has been received based on the filing with and approval by the IRS of Form 4361. You must certify that you oppose, either conscientiously or because of religious principles, the *acceptance* of any public insurance (with respect to services performed as clergy), including social security coverage. This includes an opposition to insurance that helps pay for or provides services for medical care (such as Medicare) and social security benefits. Your opinion of the financial stability of the social security program is not a valid basis to file for exemption.

Deadline for Filing for an Exemption

The application for exemption from self-employment tax must be filed by the date your tax return is due, including extensions, for the second year in which you had ministerial income of \$400 or more. These do not have to be consecutive tax years.

● Computing the Self-Employment Tax

The following tax rates apply to net earnings from self-employment:

Year	Tax Rate		Maximum Earnings Base	
	OASDI	Medicare	OASDI	Medicare
2010	12.4%	2.9%	\$106,800	no limit
2011	10.4%	2.9%	106,800	no limit
2012	10.4%*	2.9%	110,100	no limit

* The 10.4% rate for 2012 only applies to January and February unless Congress extends the payroll tax "holiday."

OASDI = Old-age, survivors, and disability insurance, or social security

● Self-Employment Tax Deductions

You can take an income tax deduction equal to one-half of your self-employment tax liability. The deduction is claimed against gross income on line 27 of Form 1040, page 1. You may also deduct a portion of your self-employment tax liability in calculating your self-employment tax. This deduction is made on Schedule SE, Section A, line 4 or Section B, line 4a, by multiplying self-employment income by .9235. The purpose of these deductions is to equalize the social security (and income) taxes paid by (and for) employees and self-employed persons with equivalent income.



Warning

Opting out of social security is relatively simple. Form 4361 must be filed by the due date of the tax return for the second year with \$400 or more of clergy income. But the simplicity of opting out should not be confused with the significant difficulty of complying with the requirements for opting out.



Key Issue

Unless clergy have opted out of social security, the net ministerial income plus the excluded housing allowance and the fair rental value of church-provided housing is subject to self-employment social security tax. This is true even if clergy are retired and receiving social security benefits. There is no age limit on paying social security tax.

Line by Line

Form 1040

There are two short forms, the 49-line 1040A and the super-short, 13-line 1040EZ. Generally, ministers should use the 77-line Form 1040 instead. It accommodates every minister, and there's no penalty for leaving some of the lines blank. Besides, going down the 1040 line by line may jog your memory about money you received or spent in 2011. (Line numbers noted refer to the 1040 and then to Schedule A.)

- **Filing status (lines 1 to 5).** **Line 2:** If your spouse died in 2011, you can still file jointly and take advantage of tax rates that would be lower than if you file as a single person or as a head of household.

Line 3: If you're married and live in a separate-property state, compute your tax two ways—jointly and separately. Then, file the return resulting in the lower tax.

Line 4: If you're single, you may qualify as head of household if you provided a home for someone else—like your parent. Filing as head of household rather than as a single person can save you a bundle on taxes.

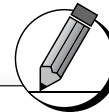
Line 5: If your spouse died in 2009 or 2010 and you have a dependent child, you can also benefit from joint-return rates as a qualifying widow(er).

- **Exemptions (lines 6a to 6d).** Remember to include a social security number for any dependent who was at least one year old on December 31, 2011. If your child does not have one, obtain Form SS-5, Application for a Social Security Number, at <http://www.ssa.gov/online/ssa-5.html>. If you are unable to secure the social security number before the filing deadline, file for an extension of time to file.

- **Income (lines 7 to 22).** **Line 7:** If your employer considered you an employee for income tax purposes, you should receive Form W-2 from the employer. The total amount of your taxable wages is shown in Box 1 of Form W-2; attach Copy B of your W-2 to your Form 1040. Include the data from other W-2s you or your spouse received on this line. If the employer erroneously included your housing allowance in Box 1, Form W-2, deduct the designated housing allowance, show the net amount on line 7, and attach an explanatory schedule.

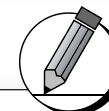
If your cash housing allowance designated and paid by the employer exceeds the lowest of (1) reasonable compensation, (2) the amount used to provide a home from current ministerial income, (3) the amount properly designated by the employer, or (4) the fair rental value of the home including utilities and furnishings, enter the difference on line 7.

Line 8a: Include as taxable-interest income the total amount of what you earned on savings accounts, certificates of deposit, credit union accounts, corporate bonds and corporate bond mutual funds, U.S. treasuries and U.S. government mutual funds, and interest paid to you for a belated federal or state tax refund (whether or not you have received a Form 1099-INT). If you haven't yet received any of the statements due you, call



Filing Tip

Form 1040, Line 7. All compensation from Forms W-2 is reported on line 7. Be sure your church has not included a formally and prospectively designated housing allowance in Box 1 of Form W-2. If so, deduct the housing allowance included in Box 1 and attach a schedule to explain the adjustment.



Filing Tip

Form 1040, Line 7. If the housing allowance designated by the employer exceeds the housing allowance exclusion to which you are entitled, you must include the difference on line 7. Your exclusion should be limited by the lower of the fair rental value of a minister-provided home or your actual housing expenses.

the issuer to get them. If you received more than \$1,500 of taxable interest income in 2011, you must also complete Schedule B.

Line 8b: Here's where you note any tax-exempt interest from municipal bonds or municipal bond funds. Don't worry—that income is not taxable. But social security recipients must count all their tax-exempt interest when computing how much of their social security benefits will be taxable.

Line 9a: Enter as dividend income only ordinary dividends, not capital-gains dividends paid by mutual funds, which are reported on Schedule D. Your Form 1099-DIV statements show the amount and type of ordinary dividends you received during 2011. If you received more than \$1,500 in dividend income in 2011, you must also complete Schedule B. Remember: Earnings from a money-market mutual fund are considered dividend income, not interest income.

Line 10: If you received a refund of a state or local tax in 2011 that you deducted on Schedule A in a prior year, include the refund here.

Line 12: Even when you file as an employee for income tax purposes, you will probably have some honoraria or fee income from speaking engagements, weddings, funerals, and so on. This income, less related expenses (see pages 38 and 47), should be reported on Schedule C or C-EZ and entered on this line.

Line 13: Enter capital-gains dividends here if you had no other capital gains or losses in 2011.

Line 15a: Report as IRA distributions even amounts you rolled over tax-free in 2011 from one IRA into another. On line 15b, you will report as taxable the amount of any IRA distributions that you did not roll over minus any return of nondeductible contributions.

Line 16a: It's likely that only a portion of the total pensions and annuities you received is taxable. Your Form 1099-R will show the taxable amount, which you enter on line 16b. If you received pensions and annuities from a denominationally sponsored plan, you may be eligible to exclude a portion or all of these payments as a housing allowance.

Line 20a: No more than 85% of your social security benefits can be taxed for 2011 and none at all if your provisional income is below \$32,000 on a joint return, \$25,000 for singles. If your income doesn't exceed the threshold, leave this line blank. If it does, use the worksheet on Form 1099-SSA to compute taxes on your benefits.

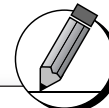
- **Adjustments to income (lines 23 to 37).** **Line 25:** Health savings account deduction. Contributions made by a taxpayer to a health savings account (HSA) up to \$3,050 for an individual plan and \$6,150 for a family plan are deductible on this line. Individuals who have reached age 55 by the end of the tax year are allowed to increase their annual contribution for years after 2011.

Line 26: If your employer paid directly or reimbursed you for your qualified moving costs incurred in 2011, these amounts would not be included as compensation on your Form W-2. Therefore, you would have no moving expenses to deduct on line 26. However, if part or all of your moving costs were not paid directly or reimbursed, deduct these expenses here.



Remember

Most ministers do not have to file a separate schedule if interest or dividend income is \$1,500 or less, only the totals need to be reported on Form 1040.



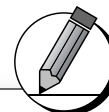
Filing Tip

Form 1040, Line 12. The only ministerial income that should be reported on line 12 is: fees from weddings, funerals, speaking engagements, and similar income. Unreimbursed expenses related to this income should be deducted on Schedule C or Schedule C-EZ.

Line 27: One-half of your social security tax that is deductible for income tax purposes is reflected on this line.

Line 33: Interest paid on a qualifying student loan may be deducted on this line.

Line 36: If you are employed as a chaplain or any other minister-employee of a nonreligious organization, use this line for your deduction of 403(b) contributions that you sent directly to the plan. On the dotted line next to line 36, enter the amount of your deduction and identify it as indicated.



Filing Tip

Form 1040, Line 53. If you made contributions to a 403(b) or 401(k) plan, and your adjusted gross income was \$50,000 or less, you may be eligible for this credit. The credit is also available for contributions to either a traditional or a Roth IRA. The excluded portion of minister's housing does not reduce this credit.

- **Tax computation (lines 38 to 55).** **Line 40:** Claim the standard deduction only if the amount exceeds what you could write off in itemizing expenses on Schedule A. For 2011, the standard deduction is \$11,600 joint, \$8,500 head of household, and \$5,800 single. The amounts are higher if you or your spouse is 65 or older or legally blind.

Line 50: Taxpayers with adjusted gross income of \$50,000 or less may claim a credit on this line equal to a certain percentage of the employee contributions made to a retirement account or IRA.

- **Other taxes (lines 56 to 60).** **Line 56:** If you are a qualified minister (see pages 5-6) and have not opted out of social security, you are self-employed for social security tax purposes. Your social security is not withheld by your church but is calculated on Schedule SE if you had net earnings of \$400 or more and paid with Form 1040. The tax is 15.3% of the first \$106,800 of 2011 self-employment income and 2.9% of income above \$106,800. If your total wages and self-employment earnings were less than \$106,800, you can probably save time and headaches by filing the Short Schedule SE on the front of the SE form.

Line 58: You will owe the tax on qualified plans plus the 10% penalty on the amount you withdrew from your IRA or another retirement plan if you were under 59½, unless you meet certain exceptions.

- **Payments (lines 61 to 72).** **Line 61:** Did you have a voluntary withholding arrangement whereby your employing church withheld federal income tax from your compensation? Then show the amount of federal income tax the church withheld (from your W-2) along with other federal income tax withholding from other employment of you or your spouse here. Also include tax withheld on your W-2G and other Forms 1099. The amount withheld should be shown in Box 2 of Form W-2G, in Box 6 of Form 1099-SSA, and Box 4 of other Forms 1099.

Line 62: Don't get confused: Even though you made your fourth-quarter 2011 estimated tax payment in January 2012, it's counted on your 2011 return.

Line 64a: Enter your earned income tax credit here or let the IRS calculate it for you. If you have a qualifying child, you must complete Schedule EIC.

- **Refund or amount you owe (lines 73 to 77).** **Line 77:** The IRS assumes you must pay the estimated tax penalty if you owe \$1,000 or more beyond what you've paid through withholding or estimated tax and the amount due is more than 110% of your 2010 tax bill. You may qualify for one of several exceptions, however. Use Form 2210 to prove your case.

Schedule A (Itemized Deductions)

If you live in church-provided housing, you often cannot itemize. But run down Schedule A just to see whether you might have more write-offs than the standard deduction will permit.

- **Medical and dental expenses (lines 1 to 4).** Don't overlook the cost of getting to and from the doctor or druggist. Write off 19 cents a mile for the first half of 2011 and 23.5 cents per miles from July 1 through the end of the year, plus the cost of parking. If you didn't drive, deduct your bus, train, or taxi fares. The cost of trips to see out-of-town specialists and as much as \$50 a day for the cost of lodging when you're out of town to get medical care count toward the 7.5%. Include all your health insurance premiums, as well as Medicare Part B premiums for 2011.
- **Taxes you paid (lines 5 to 9).** Even though your real estate taxes are a housing expense excludable under the housing allowance, you may still deduct them (even for multiple properties if not deducted elsewhere on the return) on line 6 as an itemized deduction—one of the few “double deductions” allowed in the tax law.
- **Interest you paid (lines 10 to 15).** **Line 10:** If you bought a house during 2011, review your escrow or settlement papers for any mortgage interest you paid that was not shown on your lender's year-end statement. If you paid interest on a second mortgage or line of credit secured by your home, include the interest expense here.

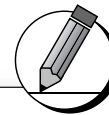
As with real estate taxes, it is possible to deduct mortgage interest as an itemized deduction even if the interest is included in housing expenses subject to a housing allowance. Interest paid on a secured mortgage is deductible on Schedule A regardless of how the proceeds of the loan are used. However, the only mortgage interest properly includible as housing expense under a housing allowance is when the loan proceeds were used to provide housing. For example, interest on a second mortgage used to finance your child's college education is deductible on Schedule A but does not qualify as a housing expense for housing allowance purposes.

Don't overlook points you paid to get the mortgage. All of the points are generally deductible as interest here. Points paid for a refinancing must be amortized over the life of the loan. But you can deduct on your 2011 return the portion of all points paid that correspond with the percentage of your refinancing used for home improvements.

- **Gifts to charity (lines 16 to 19).** **Line 16:** For gifts you made in 2011, you must have written acknowledgments from the charity of any single gifts of \$250 or more and for all gifts of cash.

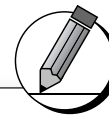
Line 17: Deduct your charitable mileage for any volunteer work at the rate of 14 cents a mile.

- **Job expenses and other miscellaneous deductions (lines 21 to 27).** Don't assume you can't surmount the 2% AGI floor on these miscellaneous deductions. A wealth of employee business, investment, and tax-related expenses—from job-hunting costs to tax preparation fees—are deductible here. And if you bought business equipment required by your employer and you were not reimbursed, you can write off its entire cost in 2011, as much as \$500,000. (However, see the allocation of expense rules, page 26, and an example on pages 40 and 58.)



Filing Tip

Schedule A, Lines 6, 10-12. These lines relate to the most significant tax break available to ministers who own their own homes. Even though real estate taxes, mortgage interest, and points are excludable under the housing allowance, subject to certain limits, the same amounts are deductible as itemized deductions.



Filing Tip

Schedule A, Line 21. Since the deduction for meal and entertainment expense is limited on Form 2106, expenses claimed on lines 21 to 23 are reduced by 2% of your adjusted gross income, and the standard deduction may be advantageous for you, using an accountable expense reimbursement plan to reduce or eliminate unreimbursed expenses is generally a wise move.

Sample Return No. 1

- Accountable expense reimbursement plan
- Minister owns residence
- Pays federal taxes through voluntary withholding
- Church reimbursed nonqualifying moving expenses
- Housing fair rental value test applied
- 403(b) contribution by salary reduction and employer contributions
- Application of Deason Rule

Minister considered to be an employee for income tax purposes with an accountable business expense plan.

The Browns live in a home they are personally purchasing. Pastor Brown has entered into a voluntary withholding agreement with the church and \$12,000 of federal income taxes are withheld.

Income, Benefits, and Reimbursements:

Church salary	\$64,850
Christmas and other special occasion gifts paid by the church based on designed member-gifts to the church	750
Honoraria for performing weddings, funerals, and baptisms	650
Honorarium for speaking as an evangelist at another church	1,000
Mutual fund dividend income:	
Capital gain distributions	150
Ordinary	954
Interest income:	
Taxable	675
Tax-exempt	1,200
Reimbursement of self-employment tax	12,000

Business Expenses, Itemized Deductions, Housing, and Other Data:

100% of church-related expenses (including 9,412 business miles) paid personally (\$7,593) were reimbursed by the church under an accountable expense plan, based on timely substantiation of the expenses.

Expenses related to honoraria income:

Parking		\$ 25
Mileage –		
1/1–6/30/11	420 x 51¢ per mile	214
7/1–12/31/11	509 x 55.5¢ per mile	283
Meals and entertainment		50
Other		200

Potential itemized deductions:

Unreimbursed doctors, dentists, and drugs	1,500
State and local income taxes:	
2010 taxes paid in 2011	400
Withheld from salary	1,600
Real estate taxes on home	1,000
Home mortgage interest	14,850
Cash contributions	8,200
Noncash contributions – household furniture/fair market value	266
Tax preparation fee	200

Student loan interest 1,908

Housing data:

Designation	26,000
Actual expenses	25,625
Fair rental value including utilities	25,000

403(b) pre-tax contributions for Pastor Brown:

Voluntary employee contributions made under a salary reduction agreement	500
Nonvoluntary employer contributions	2,000

Moving expenses reimbursed under a nonqualified plan (see page 42) 6,750

Form	1040	Department of the Treasury—Internal Revenue Service (99)	2011	OMB No. 1545-0074	IRS Use Only—Do not write or staple in this space.
For the year Jan. 1–Dec. 31, 2011, or other tax year beginning			, 2011, ending	, 20	See separate instructions.
Your first name and initial Milton L.		Last name Brown		Your social security number 541 16 8194	
If a joint return, spouse's first name and initial Alessia S.		Last name Brown		Spouse's social security number 238 49 7249	
Home address (number and street). If you have a P.O. box, see instructions. 418 Trenton Street				Apt. no.	
City, town or post office, state, and ZIP code. If you have a foreign address, also complete spaces below (see instructions). Springfield, OH 45504				Presidential Election Campaign Check here if you, or your spouse if filing jointly, want \$3 to go to this fund. Checking a box below will not change your tax or refund. <input type="checkbox"/> You <input type="checkbox"/> Spouse	
Foreign country name		Foreign province/county			
Filing Status 1 <input type="checkbox"/> Single 4 <input type="checkbox"/> Head of household (with qualifying person). (See instructions.) If the qualifying person is a child but not your dependent, enter this child's name here. ▶ 2 <input checked="" type="checkbox"/> Married filing jointly (even if only one had income) 3 <input type="checkbox"/> Married filing separately. Enter spouse's SSN above and full name here. ▶ 5 <input type="checkbox"/> Qualifying widow(er) with dependent child Check only one box.					
Exemptions 6a <input checked="" type="checkbox"/> Yourself. If someone can claim you as a dependent, do not check box 6a b <input checked="" type="checkbox"/> Spouse c Dependents:					
		(2) Dependent's social security number	(3) Dependent's relationship to you	(4) <input checked="" type="checkbox"/> if child under age 17 qualifying for child tax credit (see instructions)	Boxes checked on 6a and 6b No. of children on 6c who: • lived with you • did not live with you due to divorce or separation (see instructions) Dependents on 6c not entered above Add numbers on lines above ▶
(1) First name	Last name	514 43 9196	Son	<input checked="" type="checkbox"/>	2
Charles Brown					1
If more than four dependents, see instructions and check here ▶ <input type="checkbox"/>					
d Total number of exemptions claimed					3
Income 7 Wages, salaries, tips, etc. Attach Form(s) W-2 (Incl. excess housing allow. \$1,000) 7 58,850 8a Taxable interest. Attach Schedule B if required 8a 675 b Tax-exempt interest. Do not include on line 8a 8b 1,200 9a Ordinary dividends. Attach Schedule B if required 9a 954 b Qualified dividends 9b 10 Taxable refunds, credits, or offsets of state and local income taxes 10 11 Alimony received 11 12 Business income or (loss). Attach Schedule C or C-EZ 12 1,120 13 Capital gain or (loss). Attach Schedule D if required. If not required, check here ▶ <input type="checkbox"/> 13 150 14 Other gains or (losses). Attach Form 4797 14 15a IRA distributions 15a b Taxable amount 15b 16a Pensions and annuities 16a b Taxable amount 16b 17 Rental real estate, royalties, partnerships, S corporations, trusts, etc. Attach Schedule E 17 18 Farm income or (loss). Attach Schedule F 18 19 Unemployment compensation 19 20a Social security benefits 20a b Taxable amount 20b 21 Other income. List type and amount 21 22 Combine the amounts in the far right column for lines 7 through 21. This is your total income ▶ 22 61,749					
Adjusted Gross Income 23 Educator expenses 23 24 Certain business expenses of reservists, performing artists, and fee-basis government officials. Attach Form 2106 or 2106-EZ 24 25 Health savings account deduction. Attach Form 8889 25 26 Moving expenses. Attach Form 3903 26 27 Deductible part of self-employment tax. Attach Schedule SE 27 5,986 28 Self-employed SEP, SIMPLE, and qualified plans 28 29 Self-employed health insurance deduction 29 30 Penalty on early withdrawal of savings 30 31a Alimony paid b Recipient's SSN ▶ 31a 32 IRA deduction 32 33 Student loan interest deduction 33 1,908 34 Tuition and fees. Attach Form 8917 34 35 Domestic production activities deduction. Attach Form 8903 35 36 Add lines 23 through 35 36 7,894 37 Subtract line 36 from line 22. This is your adjusted gross income ▶ 37 53,855					

Line 21 – See page 41 for the calculation of the excess housing allowance.
 Line 27 – See page 40 for the explanation of the self-employment tax deduction.

Form 1040 (2011)

Page **2**

Tax and Credits	38	Amount from line 37 (adjusted gross income)	38	53,855
	39a	Check <input type="checkbox"/> You were born before January 2, 1947, <input type="checkbox"/> Blind. <input type="checkbox"/> Spouse was born before January 2, 1947, <input type="checkbox"/> Blind. Total boxes checked ▶ 39a		
	b	If your spouse itemizes on a separate return or you were a dual-status alien, check here ▶ 39b <input type="checkbox"/>		
Standard Deduction for—	40	Itemized deductions (from Schedule A) or your standard deduction (see left margin)	40	26,316
• People who check any box on line 39a or 39b or who can be claimed as a dependent, see instructions.	41	Subtract line 40 from line 38	41	27,539
• All others: Single or Married filing separately, \$5,800	42	Exemptions. Multiply \$3,700 by the number on line 6d.	42	11,100
Married filing jointly or Qualifying widow(er), \$11,600	43	Taxable income. Subtract line 42 from line 41. If line 42 is more than line 41, enter -0-	43	16,439
Head of household, \$8,500	44	Tax (see instructions). Check if any from: a <input type="checkbox"/> Form(s) 8814 b <input type="checkbox"/> Form 4972 c <input type="checkbox"/> 962 election	44	1,643
	45	Alternative minimum tax (see instructions). Attach Form 6251	45	
	46	Add lines 44 and 45	46	1,643
	47	Foreign tax credit. Attach Form 1116 if required	47	
	48	Credit for child and dependent care expenses. Attach Form 2441	48	
	49	Education credits from Form 8863, line 23	49	
	50	Retirement savings contributions credit. Attach Form 8880	50	
	51	Child tax credit (see instructions)	51	1,000
	52	Residential energy credits. Attach Form 5695	52	
	53	Other credits from Form: a <input type="checkbox"/> 3800 b <input type="checkbox"/> 8801 c <input type="checkbox"/>	53	
	54	Add lines 47 through 53. These are your total credits	54	1,000
	55	Subtract line 54 from line 46. If line 54 is more than line 46, enter -0-	55	643
Other Taxes	56	Self-employment tax. Attach Schedule SE	56	10,410
	57	Unreported social security and Medicare tax from Form: a <input type="checkbox"/> 4137 b <input type="checkbox"/> 8919	57	
	58	Additional tax on IRAs, other qualified retirement plans, etc. Attach Form 5329 if required	58	
	59a	Household employment taxes from Schedule H	59a	
	b	First-time homebuyer credit repayment. Attach Form 5405 if required	59b	
	60	Other taxes. Enter code(s) from instructions	60	
	61	Add lines 55 through 60. This is your total tax	61	11,053
Payments	62	Federal income tax withheld from Forms W-2 and 1099	62	12,000
	63	2011 estimated tax payments and amount applied from 2010 return	63	
	64a	Earned income credit (EIC)	64a	
	b	Nontaxable combat pay election 64b		
	65	Additional child tax credit. Attach Form 8812	65	
	66	American opportunity credit from Form 8863, line 14	66	
	67	First-time homebuyer credit from Form 5405, line 10	67	
	68	Amount paid with request for extension to file	68	
	69	Excess social security and tier 1 RRTA tax withheld	69	
	70	Credit for federal tax on fuels. Attach Form 4136	70	
	71	Credits from Form: a <input type="checkbox"/> 2439 b <input type="checkbox"/> 8839 c <input type="checkbox"/> 8801 d <input type="checkbox"/> 8885	71	
	72	Add lines 62, 63, 64a, and 65 through 71. These are your total payments	72	12,000
Refund	73	If line 72 is more than line 61, subtract line 61 from line 72. This is the amount you overpaid	73	947
	74a	Amount of line 73 you want refunded to you . If Form 8888 is attached, check here ▶ <input type="checkbox"/>	74a	947
Direct deposit? See instructions.	b	Routing number	c	Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings
	d	Account number		
	75	Amount of line 73 you want applied to your 2012 estimated tax ▶	75	
Amount You Owe	76	Amount you owe. Subtract line 72 from line 61. For details on how to pay, see instructions ▶	76	
	77	Estimated tax penalty (see instructions)	77	

Third Party Designee Do you want to allow another person to discuss this return with the IRS (see instructions)? Yes. Complete below. No

Designee's name Phone no. Personal identification number (PIN)

Sign Here Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

Your signature *Milton A. Brown* Date **4/15/12** Your occupation **Minister** Daytime phone number

Spouse's signature. If a joint return, both must sign. *Alessia S. Brown* Date **4/15/12** Spouse's occupation **Housewife** Identity Protection PIN (see inst.)

Paid Preparer Use Only

Print/Type preparer's name Preparer's signature Date Check if self-employed PTIN

Firm's name Firm's EIN

Firm's address Phone no.

Line 62 – The minister had income tax withheld under a voluntary withholding agreement with the church. Notice that income tax was withheld relating to both the income and social security tax liability.

SCHEDULE A (Form 1040) <small>Department of the Treasury Internal Revenue Service (99)</small>	Itemized Deductions ▶ Attach to Form 1040. ▶ See Instructions for Schedule A (Form 1040).	<small>OMB No. 1545-0074</small> 2011 <small>Attachment Sequence No. 07</small>
Name(s) shown on Form 1040 Milton L. and Alessia S. Brown		Your social security number 541-16-8194
Medical and Dental Expenses	Caution. Do not include expenses reimbursed or paid by others. 1 Medical and dental expenses (see instructions) 1 1,500 2 Enter amount from Form 1040, line 38 2 53,855 3 Multiply line 2 by 7.5% (.075) 3 4,039 4 Subtract line 3 from line 1. If line 3 is more than line 1, enter -0- 4 0	0
Taxes You Paid	5 State and local (check only one box): a <input checked="" type="checkbox"/> Income taxes, or b <input type="checkbox"/> General sales taxes 6 Real estate taxes (see instructions) 6 1,000 7 Personal property taxes 7 8 Other taxes. List type and amount ▶ 9 Add lines 5 through 8 9 3,000	3,000
Interest You Paid <small>Note. Your mortgage interest deduction may be limited (see instructions).</small>	10 Home mortgage interest and points reported to you on Form 1098 10 14,850 11 Home mortgage interest not reported to you on Form 1098. If paid to the person from whom you bought the home, see instructions and show that person's name, identifying no., and address ▶ 12 Points not reported to you on Form 1098. See instructions for special rules 12 13 Mortgage insurance premiums (see instructions) 13 14 Investment interest. Attach Form 4952 if required. (See instructions.) 14 15 Add lines 10 through 14 15 14,850	14,850
Gifts to Charity <small>If you made a gift and got a benefit for it, see instructions.</small>	16 Gifts by cash or check. If you made any gift of \$250 or more, see instructions 16 8,200 17 Other than by cash or check. If any gift of \$250 or more, see instructions. You must attach Form 8283 if over \$500 17 266 18 Carryover from prior year 18 19 Add lines 16 through 18 19 8,466	8,466
Casualty and Theft Losses	20 Casualty or theft loss(es). Attach Form 4684. (See instructions.) 20	
Job Expenses and Certain Miscellaneous Deductions	21 Unreimbursed employee expenses—job travel, union dues, job education, etc. Attach Form 2106 or 2106-EZ if required. (See instructions.) ▶ 22 Tax preparation fees 22 200 23 Other expenses—investment, safe deposit box, etc. List type and amount ▶ 24 Add lines 21 through 23 24 200 25 Enter amount from Form 1040, line 38 25 53,855 26 Multiply line 25 by 2% (.02) 26 1,077 27 Subtract line 26 from line 24. If line 26 is more than line 24, enter -0- 27 0	0
Other Miscellaneous Deductions	28 Other—from list in instructions. List type and amount ▶	
Total Itemized Deductions	29 Add the amounts in the far right column for lines 4 through 28. Also, enter this amount on Form 1040, line 40 29 26,316	26,316
Deductions	30 If you elect to itemize deductions even though they are less than your standard deduction, check here <input type="checkbox"/>	

Lines 6 and 10 – The real estate taxes and home mortgage interest are deducted on this form plus excluded from income on line 7, Form 1040, page 1 as a housing allowance.

Line 21 – There are no unreimbursed employee expenses to deduct since the church reimbursed all the professional expenses under an accountable expense reimbursement plan.

SCHEDULE B
(Form 1040A or 1040)

Department of the Treasury
Internal Revenue Service (99)

Interest and Ordinary Dividends

▶ Attach to Form 1040A or 1040. ▶ See instructions on back.

OMB No. 1545-0074

2011
Attachment
Sequence No. **08**

Name(s) shown on return

Milton L. and Alessia S. Brown

Your social security number

540-16-8194

Part I
Interest

1 List name of payer. If any interest is from a seller-financed mortgage and the buyer used the property as a personal residence, see instructions on back and list this interest first. Also, show that buyer's social security number and address ▶

State Highway Bonds

Ohio S&L

(See instructions on back and the instructions for Form 1040A, or Form 1040, line 8a.)

Note. If you received a Form 1099-INT, Form 1099-OID, or substitute statement from a brokerage firm, list the firm's name as the payer and enter the total interest shown on that form.

Subtotal

Less: Tax-Exempt Interest

2 Add the amounts on line 1

3 Excludable interest on series EE and I U.S. savings bonds issued after 1989. Attach Form 8815

4 Subtract line 3 from line 2. Enter the result here and on Form 1040A, or Form 1040, line 8a ▶

Note. If line 4 is over \$1,500, you must complete Part III.

Amount

1,200

675

1,875

-1,200

675

675

Part II

5 List name of payer ▶

Vanguard

Ordinary Dividends

(See instructions on back and the instructions for Form 1040A, or Form 1040, line 9a.)

Note. If you received a Form 1099-DIV or substitute statement from a brokerage firm, list the firm's name as the payer and enter the ordinary dividends shown on that form.

6 Add the amounts on line 5. Enter the total here and on Form 1040A, or Form 1040, line 9a ▶

Note. If line 6 is over \$1,500, you must complete Part III.

Amount

954

954

Part III
Foreign Accounts and Trusts

(See instructions on back.)

You must complete this part if you (a) had over \$1,500 of taxable interest or ordinary dividends; (b) had a foreign account; or (c) received a distribution from, or were a grantor of, or a transferor to, a foreign trust.

7a At any time during 2011, did you have a financial interest in or signature authority over a financial account, such as a bank account, securities account, or brokerage account located in a foreign country? See instructions

If "Yes," are you required to file Form TD F 90-22.1 to report that financial interest or signature authority? See Form TD F 90-22.1 and its instructions for filing requirements and exceptions to those requirements

b If you are required to file Form TD F 90-22.1, enter the name of the foreign country where the financial account is located ▶

Yes	No
	X

**SCHEDULE C-EZ
(Form 1040)**

Department of the Treasury
Internal Revenue Service (99)

Net Profit From Business

(Sole Proprietorship)

▶ Partnerships, joint ventures, etc., generally must file Form 1065 or 1065-B.
▶ Attach to Form 1040, 1040NR, or 1041. ▶ See instructions on page 2.

OMB No. 1545-0074

2011

Attachment
Sequence No. **09A**

Name of proprietor

Milton L. Brown

Social security number (SSN)

541-16-8194

Part I General Information

You May Use
Schedule C-EZ
Instead of
Schedule C
Only If You:

- Had business expenses of \$5,000 or less.
- Use the cash method of accounting.
- Did not have an inventory at any time during the year.
- Did not have a net loss from your business.
- Had only one business as either a sole proprietor, qualified joint venture, or statutory employee.
- Did not receive any credit card or similar payments that included amounts that are not includible in your income (see instructions for line 1a).

And You:

- Had no employees during the year.
- Are not required to file Form 4562, Depreciation and Amortization, for this business. See the instructions for Schedule C, line 13, to find out if you must file.
- Do not deduct expenses for business use of your home.
- Do not have prior year unallowed passive activity losses from this business.

A Principal business or profession, including product or service
Minister

B Enter business code (see page 2)
8 1 3 0 0 0

C Business name. If no separate business name, leave blank.

D Enter your EIN (see page 2)

E Business address (including suite or room no.). Address not required if same as on page 1 of your tax return.
City, town or post office, state, and ZIP code

F Did you make any payments in 2011 that would require you to file Form(s) 1099 (see the Schedule C instructions) Yes No

G If "Yes," did you or will you file all required Forms 1099? Yes No

Part II Figure Your Net Profit

1a Gross merchant card and third party network receipts and sales (see instructions)	1a		
b Gross receipts or sales not entered on line 1a (see instructions)	1b	1,650	
c Income reported to you on Form W-2 if the "Statutory Employee" box on that form was checked. Caution. See Schedule C instructions before completing this line	1c		
d Total of lines 1a, 1b, and 1c. If any adjustments to line 1a, you must use Schedule C (see instructions)	1d	1,650	
2 Total expenses (see page 2). If more than \$5,000, you must use Schedule C	2	530	
3 Net profit. Subtract line 2 from line 1d. If less than zero, you must use Schedule C. Enter on both Form 1040, line 12, and Schedule SE, line 2, or on Form 1040NR, line 13 and Schedule SE, line 2 (see instructions). (If you entered an amount on line 1c, do not report the amount from line 1c on Schedule SE, line 2.) Estates and trusts, enter on Form 1041, line 3	3	1,120	

Part III Information on Your Vehicle. Complete this part **only** if you are claiming car or truck expenses on line 2.

4 When did you place your vehicle in service for business purposes? (month, day, year) ▶ 1/1/06

5 Of the total number of miles you drove your vehicle during 2011, enter the number of miles you used your vehicle for:
Schedule C **929**

a Business **9,412** **b** Commuting (see page 2) **1,216** **c** Other

6 Was your vehicle available for personal use during off-duty hours? Yes No

7 Do you (or your spouse) have another vehicle available for personal use? Yes No

8a Do you have evidence to support your deduction? Yes No

b If "Yes," is the evidence written? Yes No

For Paperwork Reduction Act Notice, see your tax return instructions.

Cat. No. 14374D

Schedule C-EZ (Form 1040) 2011

Gross receipts:

Honoraria (weddings, etc.) \$650
Speaking honorarium 1,000
\$1,650

Expenses:

See Attachment 1 on page 40

Most ministers considered to be employees for income tax purposes (with that income reported on line 7, Form 1040, page 1) also have honoraria and fee income and related expenses that are reportable on Schedule C (C-EZ).

Schedule SE (Form 1040) 2011

Attachment Sequence No. **17**

Page **2**

Name of person with self-employment income (as shown on Form 1040)
Milton L. Brown

Social security number of person with self-employment income ▶ **541-16-8194**

Section B—Long Schedule SE

Part I Self-Employment Tax

Note. If your only income subject to self-employment tax is church employee income, see instructions. Also see instructions for the definition of church employee income.

A If you are a minister, member of a religious order, or Christian Science practitioner and you filed Form 4361, but you had \$400 or more of other net earnings from self-employment, check here and continue with Part I

1a Net farm profit or (loss) from Schedule F, line 34, and farm partnerships, Schedule K-1 (Form 1065), box 14, code A. **Note.** Skip lines 1a and 1b if you use the farm optional method (see instructions) **1a**

b If you received social security retirement or disability benefits, enter the amount of Conservation Reserve Program payments included on Schedule F, line 4b, or listed on Schedule K-1 (Form 1065), box 20, code Y **1b** ()

2 Net profit or (loss) from Schedule C, line 31; Schedule K-1 (Form 1065), box 14, code A (other than farming); and Schedule K-1 (Form 1065-B), box 9, code J1. Ministers and members of religious orders, see instructions for types of income to report on this line. See instructions for other income to report. **Note.** Skip this line if you use the nonfarm optional method (see instructions) **2** **84,753**

3 Combine lines 1a, 1b, and 2 **3** **84,753**

4a If line 3 is more than zero, multiply line 3 by 92.35% (.9235). Otherwise, enter amount from line 3 **Note.** If line 4a is less than \$400 due to Conservation Reserve Program payments on line 1b, see instructions. **4a** **78,269**

b If you elect one or both of the optional methods, enter the total of lines 15 and 17 here **4b**

c Combine lines 4a and 4b. If less than \$400, **stop**; you do not owe self-employment tax. **Exception.** If less than \$400 and you had church employee income, enter -0- and continue ▶ **4c** **78,269**

5a Enter your church employee income from Form W-2. See instructions for definition of church employee income **5a**

b Multiply line 5a by 92.35% (.9235). If less than \$100, enter -0- **5b**

6 Add lines 4c and 5b **6** **78,269**

7 Maximum amount of combined wages and self-employment earnings subject to social security tax or the 4.2% portion of the 5.65% railroad retirement (tier 1) tax for 2011 **7** **106,800** **00**

8a Total social security wages and tips (total of boxes 3 and 7 on Form(s) W-2) and railroad retirement (tier 1) compensation. If \$106,800 or more, skip lines 8b through 10, and go to line 11 **8a**

b Unreported tips subject to social security tax (from Form 4137, line 10) **8b**

c Wages subject to social security tax (from Form 8919, line 10) **8c**

d Add lines 8a, 8b, and 8c **8d**

9 Subtract line 8d from line 7. If zero or less, enter -0- here and on line 10 and go to line 11 ▶ **9** **106,800**

10 Multiply the smaller of line 6 or line 9 by 10.4% (.104) **10** **8,140**

11 Multiply line 6 by 2.9% (.029) **11** **2,270**

12 Self-employment tax. Add lines 10 and 11. Enter here and on Form 1040, line 56, or Form 1040NR, line 54 **12** **10,410**

13 Deduction for employer-equivalent portion of self-employment tax. Add the two following amounts.
• 59.6% (.596) of line 10.
• One-half of line 11.
Enter the result here and on Form 1040, line 27, or Form 1040NR, line 27 **13** **5,986**

Part II Optional Methods To Figure Net Earnings (see instructions)

Farm Optional Method. You may use this method **only** if (a) your gross farm income¹ was not more than \$6,720, or (b) your net farm profits² were less than \$4,851.

14 Maximum income for optional methods **14** **4,480** **00**

15 Enter the smaller of: two-thirds (2/3) of gross farm income¹ (not less than zero) or \$4,480. Also include this amount on line 4b above **15**

Nonfarm Optional Method. You may use this method **only** if (a) your net nonfarm profits³ were less than \$4,851 and also less than 72.189% of your gross nonfarm income,⁴ and (b) you had net earnings from self-employment of at least \$400 in 2 of the prior 3 years. **Caution.** You may use this method no more than five times.

16 Subtract line 15 from line 14 **16**

17 Enter the smaller of: two-thirds (2/3) of gross nonfarm income⁴ (not less than zero) or the amount on line 16. Also include this amount on line 4b above **17**

¹ From Sch. F, line 9, and Sch. K-1 (Form 1065), box 14, code B.

² From Sch. F, line 34, and Sch. K-1 (Form 1065), box 14, code A—minus the amount you would have entered on line 1b had you not used the optional method.

³ From Sch. C, line 31; Sch. K-1 (Form 1065), box 14, code A; and Sch. K-1 (Form 1065-B), box 9, code J1.

⁴ From Sch. C, line 7; Sch. K-1 (Form 1065), box 14, code C; and Sch. K-1 (Form 1065-B), box 9, code J2.

Line 2 – See Attachment 2 on page 40.

Line 4 – This line results in the deduction of a portion of the self-employment tax liability.

A minister must use Section B-Long Schedule if he or she received nonministerial wages (subject to FICA) and the total of these wages and net ministerial self-employment earnings (W-2 and Schedule C [C-EZ]-related) is more than \$106,800.

Attachment 1.**Computation of expenses, allocatable to tax-free ministerial income, that are nondeductible.**

	<u>Taxable</u>	<u>Tax-Free</u>	<u>Total</u>
Salary as a minister	\$ 57,880		\$ 57,850
Housing allowance:			
Amount designated and paid by church	\$ 26,000		
Actual expenses	25,625		
Fair rental value of home (including furnishings and utilities)	25,000		
Taxable portion of allowance (excess of amount designated & paid over lesser of actual expenses or fair rental value)	<u>\$ 1,000</u>		1,000
Tax-free portion of allowance (lesser of amount designated, actual expenses, or fair rental value)		25,000	
Gross income from weddings, baptisms, and honoraria	<u>1,650</u>		<u>1,650</u>
Ministerial Income	<u>\$ 60,500</u>	<u>\$ 25,000</u>	<u>\$ 85,500</u>
% of nondeductible expenses: \$25,000/\$85,500 = 29%			

Schedule C-EZ Deduction Computation

Parking	\$ 25
Meals & Entertainment (\$50 x 50% deductible portion)	25
Other	200
Mileage (420 miles x 51 cents per mile + 509 miles x 55.5 cents per mile)	<u>497</u>
Unadjusted Schedule C-EZ expenses	747
Minus:	
Nondeductible part of Schedule C-EZ expenses (29% x \$747)	<u>(217)</u>
Schedule C-EZ deductions (line 2) (See page 38)	<u>\$ 530</u>

Attachment 2.**Net earnings from self-employment (attachment to Schedule SE, Form 1040)**

Church wages	\$ 57,850
Housing allowance	26,000
Net profit from Schedule C-EZ	<u>1,230</u>
	84,970
Less:	
Schedule C-EZ expenses allocable to tax-free income	(217)
Net Self-Employed Income	<u>84,753</u>
Schedule SE, Section A, line 2 (See page 39)	<u>\$ 84,753</u>

Housing Allowance Worksheet

Clergy-Owned Home

Name: Milton L. BrownFor the period January 1, 2011 to December 31, 2011Date designation approved December 20, 2010**Allowable Housing Expenses** (*expenses paid from current income*)

	<u>Estimated Expenses</u>	<u>Actual</u>
Down payment on purchase of housing	\$ _____	\$ _____
Housing loan principal and interest payments	<u>18,117</u>	<u>18,875</u>
Real estate commission, escrow fees	_____	_____
Real property taxes	<u>900</u>	<u>1,000</u>
Personal property taxes on contents	_____	_____
Homeowner's insurance	<u>500</u>	<u>550</u>
Personal property insurance on contents	<u>150</u>	<u>200</u>
Umbrella liability insurance	<u>100</u>	_____
Structural maintenance and repair	_____	<u>550</u>
Landscaping, gardening, and pest control	_____	<u>200</u>
Furnishings (<i>purchase, repair, replacement</i>)	_____	<u>400</u>
Decoration and redecoration	_____	_____
Utilities (<i>gas, electricity, water</i>) and trash collection	<u>3,500</u>	<u>3,500</u>
Local telephone expense (<i>base charge</i>)	<u>150</u>	<u>150</u>
Homeowner's association dues/condominium fees	<u>219</u>	<u>200</u>
Subtotal	<u>23,636</u>	
10% allowance for unexpected expenses	<u>2,364</u>	
TOTAL	\$ <u>26,000</u>	\$ <u>25,625</u> (A)
Properly designated housing allowance		\$ <u>26,000</u> (B)
Fair rental value of home, including furnishings, plus utilities		\$ <u>25,000</u> (C)

Note: The amount excludable from income for federal income tax purposes is the *lowest* of A, B, or C.

The \$1,000 difference between the designation (\$26,000) and the fair rental value (\$25,000) is reported as additional income on Form 1040, line 7.

22222		Void <input type="checkbox"/>	a Employee's social security number 541-16-8194		For Official Use Only ▶ OMB No. 1545-0008					
b Employer identification number (EIN) 38-9417217			1 Wages, tips, other compensation 57850.00		2 Federal income tax withheld 12000.00					
c Employer's name, address, and ZIP code Magnolia Springs Church 4805 Douglas Road Springfield, OH 45504			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 Milton L.		Last name Brown		Suff.		11 Nonqualified plans				
f Employee's address and ZIP code 418 Trenton Street Springfield, OH 5504			12a See instructions for box 12 E 500		12b		12c			
			12d		13 Statutory employee <input type="checkbox"/> Retirement plan <input type="checkbox"/> Third-party sick pay <input type="checkbox"/>		14 Other			
			15 State Employer's state ID number OH 627803		16 State wages, tips, etc. 57850.00		17 State income tax 1600.00		18 Local wages, tips, etc.	
			19 Local income tax		20 Locality name					

Form **W-2 Wage and Tax Statement** **2011** Department of the Treasury—Internal Revenue Service
Copy A For Social Security Administration — Send this entire page with Form W-3 to the Social Security Administration; photocopies are **not** acceptable. **For Privacy Act and Paperwork Reduction Act Notice, see back of Copy D.**
 Cat. No. 10134D
Do Not Cut, Fold, or Staple Forms on This Page — Do Not Cut, Fold, or Staple Forms on This Page

Explanation of compensation reported on Form W-2, Box 1:

Salary (\$64,850 less \$26,000 housing allowance and \$500 403[b] contributions)	\$ 38,350
Special occasion gifts	750
Reimbursement of self-employment tax	12,000
Moving expense reimbursement of nonqualified expenses	<u>6,750</u>
	<u>\$ 57,850</u>

Pastor Brown received reimbursements of \$7,593 under an accountable expense reimbursement plan. The reimbursements are not included on Form W-2 or deductible on Form 1040. There is no requirement to add the reimbursements to income taxable for social security purposes on Schedule SE.

Pastor Brown was also reimbursed for \$6,750 of nonqualified moving expenses. He failed the distance test in that his new principal place of work was less than 50 miles farther from his old residence than the old residence was from his old place of work.

Sample Return No. 2

- | | |
|---|--|
| <ul style="list-style-type: none"> ■ Nonaccountable expense reimbursements ■ Minister occupies a church-provided parsonage ■ Pays federal taxes using Form 1040-ES | <ul style="list-style-type: none"> ■ Qualifies for the Earned Income Credit ■ Church did not reimburse moving expenses ■ Application of Deason Rule ■ Tax Saver’s Credit |
|---|--|

Minister considered to be an employee for income tax purposes with a nonaccountable business expense plan.

The Halls live in church-provided housing.

Income, Benefits, and Reimbursements:

Church salary – Donald	\$ 11,000
Salary – Julie (W-2 not shown)/ Federal withholding of \$250	9,150
Christmas and other special occasion gifts paid by the church based on designated member-gifts to the church	500
Honoraria for performing weddings, funerals, baptisms, and outside speaking engagements	5,200
Interest income (taxable)	4,950
Reimbursement of self-employment tax	2,100
Business expense allowance (no accounting provided to church)	1,700

Business Expenses, Itemized Deductions, 403(b) Contributions, Housing Data, and Moving Expense Data:

Church-related expenses paid personally:	
Business use of personally-owned auto (W-2 related)	
1/1–6/30	4,212 x 51¢ per mile 2,148
7/1–12/31	3,849 x 55.5¢ per mile 2,136
Personal nondeductible commuting	2,432 miles
Seminar expenses:	
Airfare	\$675
Meals	233
Lodging	167

Subscriptions	200
Books (less than one-year life)	100
Supplies	250
Entertainment expenses	1,207
Continuing education tuition (related to church employment)	500
Travel expense related to honoraria (Schedule C-EZ):	
Airfare	2,042
Mileage	
1/1–6/30	1,253 x 51¢ per mile 639
7/1–12/31	1,105 x 55.5¢ per mile 613
Lodging	400
Supplies	700
Potential itemized deductions:	
Unreimbursed doctors, dentists, and drugs	3,050
State and local income taxes	460
Personal property taxes	300
Cash contributions	3,310
Housing data:	
Designation	2,000
Actual expenses	1,000
Fair rental value, including furnishings and utilities	11,150
403(b) pre-tax contributions for Pastor Hall: Voluntary employee contributions made under a salary reduction agreement	
	500
Moving expenses (deductible)	1,183

Form **1040** Department of the Treasury—Internal Revenue Service (99) **2011** U.S. Individual Income Tax Return OMB No. 1545-0074 IRS Use Only—Do not write or staple in this space.

For the year Jan. 1–Dec. 31, 2011, or other tax year beginning , 2011, ending , 20 See separate instructions.

Your first name and initial **Donald L.** Last name **Hall** Your social security number **482 | 11 | 6043**

If a joint return, spouse's first name and initial **Julie M.** Last name **Hall** Spouse's social security number **720 | 92 | 1327**

Home address (number and street). If you have a P.O. box, see instructions. **804 Linden Avenue** Apt. no. **▲ Make sure the SSN(s) above and on line 6c are correct.**

City, town or post office, state, and ZIP code. If you have a foreign address, also complete spaces below (see instructions). **Wabash, IN 46992**

Foreign country name Foreign province/county Foreign postal code

Filing Status 1 Single 4 Head of household (with qualifying person). (See instructions.) If the qualifying person is a child but not your dependent, enter this child's name here. ▶
 2 Married filing jointly (even if only one had income)
 3 Married filing separately. Enter spouse's SSN above and full name here. ▶ 5 Qualifying widow(er) with dependent child

Check only one box.

Exemptions 6a Yourself. If someone can claim you as a dependent, do not check box 6a } Boxes checked on 6a and 6b **2**
 b Spouse } No. of children on 6c who:
 • lived with you **2**
 • did not live with you due to divorce or separation (see instructions) _____
 (1) First name Last name (2) Dependent's social security number (3) Dependent's relationship to you (4) if child under age 17 qualifying for child tax credit (see instructions)
 If more than four dependents, see instructions and check here ▶
 David K. Hall 514 42 7465 Son
 Sarah E. Hall 416 49 0125 Daughter
 d Total number of exemptions claimed **4**

Income 7 Wages, salaries, tips, etc. Attach Form(s) W-2 (Incl. excess housing allow. \$1,000) **7 22,950**
 8a Taxable interest. Attach Schedule B if required **8a 4,950**
 b Tax-exempt interest. Do not include on line 8a **8b**
 9a Ordinary dividends. Attach Schedule B if required **9a**
 b Qualified dividends **9b**
 10 Taxable refunds, credits, or offsets of state and local income taxes **10**
 11 Alimony received **11**
 12 Business income or (loss). Attach Schedule C or C-EZ **12 2,520**
 13 Capital gain or (loss). Attach Schedule D if required. If not required, check here ▶ **13**
 14 Other gains or (losses). Attach Form 4797 **14**
 15a IRA distributions **15a** b Taxable amount **15b**
 16a Pensions and annuities **16a** b Taxable amount **16b**
 17 Rental real estate, royalties, partnerships, S corporations, trusts, etc. Attach Schedule E **17**
 18 Farm income or (loss). Attach Schedule F **18**
 19 Unemployment compensation **19**
 20a Social security benefits **20a** b Taxable amount **20b**
 21 Other income. List type and amount **21**
 22 Combine the amounts in the far right column for lines 7 through 21. This is your total income ▶ **22 30,420**

Attach Form(s) W-2 here. Also attach Forms W-2G and 1099-R if tax was withheld.
 If you did not get a W-2, see instructions.
 Enclose, but do not attach, any payment. Also, please use Form 1040-V.

Adjusted Gross Income 23 Educator expenses **23**
 24 Certain business expenses of reservists, performing artists, and fee-basis government officials. Attach Form 2106 or 2106-EZ **24**
 25 Health savings account deduction. Attach Form 8889 **25**
 26 Moving expenses. Attach Form 3903 **26 1,183**
 27 Deductible part of self-employment tax. Attach Schedule SE **27 1,403**
 28 Self-employed SEP, SIMPLE, and qualified plans **28**
 29 Self-employed health insurance deduction **29**
 30 Penalty on early withdrawal of savings **30**
 31a Alimony paid b Recipient's SSN ▶ **31a**
 32 IRA deduction **32**
 33 Student loan interest deduction **33**
 34 Tuition and fees. Attach Form 8917 **34**
 35 Domestic production activities deduction. Attach Form 8903 **35**
 36 Add lines 23 through 35 **36 2,586**
 37 Subtract line 36 from line 22. This is your adjusted gross income ▶ **37 27,834**

For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see separate instructions. Cat. No. 11320B Form **1040** (2011)

Line 7 – Julie's W-2, \$9,150, Donald's W-2, \$12,800 (see page 60), plus \$1,000 of excess housing allowance (see page 59).

Line 27 – See pages 28 for explanation of the self-employment tax deduction.

Form 1040 (2011)

Page **2**

Tax and Credits	38 Amount from line 37 (adjusted gross income)	38	27,834
	39a Check <input type="checkbox"/> You were born before January 2, 1947, <input type="checkbox"/> Blind. } Total boxes if: <input type="checkbox"/> Spouse was born before January 2, 1947, <input type="checkbox"/> Blind. } checked ▶ 39a		
	b If your spouse itemizes on a separate return or you were a dual-status alien, check here ▶ 39b <input type="checkbox"/>		
Standard Deduction for— • People who check any box on line 39a or 39b or who can be claimed as a dependent, see instructions. • All others: Single or Married filing separately, \$5,800 Married filing jointly or Qualifying widow(er), \$11,600 Head of household, \$8,500	40 Itemized deductions (from Schedule A) or your standard deduction (see left margin)	40	11,600
	41 Subtract line 40 from line 38	41	16,234
	42 Exemptions. Multiply \$3,700 by the number on line 6d	42	14,800
	43 Taxable income. Subtract line 42 from line 41. If line 42 is more than line 41, enter -0-	43	1,434
	44 Tax (see instructions). Check if any from: a <input type="checkbox"/> Form(s) 8814 b <input type="checkbox"/> Form 4972 c <input type="checkbox"/> 962 election	44	144
	45 Alternative minimum tax (see instructions). Attach Form 6251	45	
	46 Add lines 44 and 45 ▶	46	144
	47 Foreign tax credit. Attach Form 1116 if required	47	
	48 Credit for child and dependent care expenses. Attach Form 2441	48	
	49 Education credits from Form 8863, line 23	49	
50 Retirement savings contributions credit. Attach Form 8880	50		
51 Child tax credit (see instructions)	51	144	
52 Residential energy credits. Attach Form 5695	52		
53 Other credits from Form: a <input type="checkbox"/> 3800 b <input type="checkbox"/> 8801 c <input type="checkbox"/>	53		
54 Add lines 47 through 53. These are your total credits	54	144	
55 Subtract line 54 from line 46. If line 54 is more than line 46, enter -0- ▶	55	0	
Other Taxes	56 Self-employment tax. Attach Schedule SE	56	2,439
	57 Unreported social security and Medicare tax from Form: a <input type="checkbox"/> 4137 b <input type="checkbox"/> 8919	57	
	58 Additional tax on IRAs, other qualified retirement plans, etc. Attach Form 5329 if required	58	
	59a Household employment taxes from Schedule H	59a	
	b First-time homebuyer credit repayment. Attach Form 5405 if required	59b	
	60 Other taxes. Enter code(s) from instructions	60	
	61 Add lines 55 through 60. This is your total tax ▶	61	2,439
Payments	62 Federal income tax withheld from Forms W-2 and 1099	62	250
	63 2011 estimated tax payments and amount applied from 2010 return	63	
If you have a qualifying child, attach Schedule EIC.	64a Earned income credit (EIC)	64a	3,837
	b Nontaxable combat pay election <input type="checkbox"/> 64b		
	65 Additional child tax credit. Attach Form 8812	65	1,856
	66 American opportunity credit from Form 8863, line 14	66	
	67 First-time homebuyer credit from Form 5405, line 10	67	
	68 Amount paid with request for extension to file	68	
	69 Excess social security and tier 1 RRTA tax withheld	69	
	70 Credit for federal tax on fuels. Attach Form 4136	70	
	71 Credits from Form: a <input type="checkbox"/> 2439 b <input type="checkbox"/> 8839 c <input type="checkbox"/> 8801 d <input type="checkbox"/> 8885	71	
	72 Add lines 62, 63, 64a, and 65 through 71. These are your total payments ▶	72	5,943
Refund	73 If line 72 is more than line 61, subtract line 61 from line 72. This is the amount you overpaid	73	3,504
	74a Amount of line 73 you want refunded to you. If Form 8888 is attached, check here <input type="checkbox"/>	74a	3,504
Direct deposit? ▶ See instructions.	b Routing number <input type="text"/> ▶ c Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings		
	d Account number <input type="text"/>		
	75 Amount of line 73 you want applied to your 2012 estimated tax ▶ 75	75	
Amount You Owe	76 Amount you owe. Subtract line 72 from line 61. For details on how to pay, see instructions ▶	76	
	77 Estimated tax penalty (see instructions)	77	
Third Party Designee	Do you want to allow another person to discuss this return with the IRS (see instructions)? <input type="checkbox"/> Yes. Complete below. <input type="checkbox"/> No		
	Designee's name ▶	Phone no. ▶	Personal identification number (PIN) ▶ <input type="text"/>
Sign Here	Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.		
Joint return? See instructions. Keep a copy for your records.	Your signature <i>Ronald J. Hall</i>	Date 4/15/12	Your occupation Minister
	Spouse's signature. If a joint return, both must sign. <i>Julie M. Hall</i>	Date 4/15/12	Spouse's occupation Secretary
	Print/Type preparer's name	Preparer's signature	Date
	Firm's name ▶	Firm's EIN ▶	Check <input type="checkbox"/> if self-employed PTIN
	Firm's address ▶	Phone no.	

**SCHEDULE A
(Form 1040)**

Department of the Treasury
Internal Revenue Service (99)

Itemized Deductions

▶ **Attach to Form 1040.** ▶ **See Instructions for Schedule A (Form 1040).**

OMB No. 1545-0074

2011

Attachment
Sequence No. **07**

Name(s) shown on Form 1040

Donald L. and Julie M. Hall

Your social security number

482-11-6043

		1	2	3	4	
Medical and Dental Expenses	Caution. Do not include expenses reimbursed or paid by others.					
	1 Medical and dental expenses (see instructions)	1	3,050			
	2 Enter amount from Form 1040, line 38	2	27,834			
	3 Multiply line 2 by 7.5% (.075)	3	2,088			
4 Subtract line 3 from line 1. If line 3 is more than line 1, enter -0-				4	962	
Taxes You Paid	5 State and local (check only one box):	5	460			
	a <input checked="" type="checkbox"/> Income taxes, or					
	b <input type="checkbox"/> General sales taxes					
	6 Real estate taxes (see instructions)	6				
	7 Personal property taxes	7	300			
8 Other taxes. List type and amount ▶	8					
9 Add lines 5 through 8				9	760	
Interest You Paid	10 Home mortgage interest and points reported to you on Form 1098	10				
	11 Home mortgage interest not reported to you on Form 1098. If paid to the person from whom you bought the home, see instructions and show that person's name, identifying no., and address ▶	11				
	12 Points not reported to you on Form 1098. See instructions for special rules	12				
	13 Mortgage insurance premiums (see instructions)	13				
	14 Investment interest. Attach Form 4952 if required. (See instructions.)	14				
15 Add lines 10 through 14				15	0	
Gifts to Charity	16 Gifts by cash or check. If you made any gift of \$250 or more, see instructions.	16	3,310			
	17 Other than by cash or check. If any gift of \$250 or more, see instructions. You must attach Form 8283 if over \$500	17				
	18 Carryover from prior year	18				
19 Add lines 16 through 18				19	3,310	
Casualty and Theft Losses	20 Casualty or theft loss(es). Attach Form 4684. (See instructions.)	20			20	0
Job Expenses and Certain Miscellaneous Deductions	21 Unreimbursed employee expenses—job travel, union dues, job education, etc. Attach Form 2106 or 2106-EZ if required. (See instructions.) ▶	21	4,206			
	22 Tax preparation fees	22				
	23 Other expenses—investment, safe deposit box, etc. List type and amount ▶	23				
	24 Add lines 21 through 23	24	4,206			
	25 Enter amount from Form 1040, line 38	25	27,834			
26 Multiply line 25 by 2% (.02)	26	557				
27 Subtract line 26 from line 24. If line 26 is more than line 24, enter -0-				27	3,649	
Other Miscellaneous Deductions	28 Other—from list in instructions. List type and amount ▶	28			28	0
Total Itemized Deductions	29 Add the amounts in the far right column for lines 4 through 28. Also, enter this amount on Form 1040, line 40	29			29	8,681
	30 If you elect to itemize deductions even though they are less than your standard deduction, check here <input type="checkbox"/>					

For Paperwork Reduction Act Notice, see Form 1040 instructions.

Cat. No. 17145C

Schedule A (Form 1040) 2011

Line 21 – Because the minister did not have an accountable expense reimbursement plan, the unreimbursed expenses appear on this line. One of the disadvantages of this approach is the 2% deduction (line 26), which costs the minister \$557 of deductions.

**SCHEDULE C-EZ
(Form 1040)**

Department of the Treasury
Internal Revenue Service (99)

Net Profit From Business

(Sole Proprietorship)

▶ Partnerships, joint ventures, etc., generally must file Form 1065 or 1065-B.
▶ Attach to Form 1040, 1040NR, or 1041. ▶ See instructions on page 2.

OMB No. 1545-0074

2011

Attachment
Sequence No. **09A**

Name of proprietor
Donald L. Hall

Social security number (SSN)
482-11-6043

Part I General Information

**You May Use
Schedule C-EZ
Instead of
Schedule C
Only If You:**

- Had business expenses of \$5,000 or less.
- Use the cash method of accounting.
- Did not have an inventory at any time during the year.
- Did not have a net loss from your business.
- Had only one business as either a sole proprietor, qualified joint venture, or statutory employee.
- Did not receive any credit card or similar payments that included amounts that are not includible in your income (see instructions for line 1a).

And You:

- Had no employees during the year.
- Are not required to file **Form 4562**, Depreciation and Amortization, for this business. See the instructions for Schedule C, line 13, to find out if you must file.
- Do not deduct expenses for business use of your home.
- Do not have prior year unallowed passive activity losses from this business.

A Principal business or profession, including product or service Minister	B Enter business code (see page 2) ▶ 8 1 3 0 0 0
C Business name. If no separate business name, leave blank.	D Enter your EIN (see page 2)
E Business address (including suite or room no.). Address not required if same as on page 1 of your tax return. City, town or post office, state, and ZIP code	
F Did you make any payments in 2011 that would require you to file Form(s) 1099 (see the Schedule C instructions) <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No	
G If "Yes," did you or will you file all required Forms 1099? <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No	

Part II Figure Your Net Profit

1a Gross merchant card and third party network receipts and sales (see instructions)	1a			
b Gross receipts or sales not entered on line 1a (see instructions)	1b	5,200		
c Income reported to you on Form W-2 if the "Statutory Employee" box on that form was checked. Caution. See Schedule C instructions before completing this line	1c			
d Total of lines 1a, 1b, and 1c. If any adjustments to line 1a, you must use Schedule C (see instructions)	1d	5,200		
2 Total expenses (see page 2). If more than \$5,000, you must use Schedule C	2	2,680	(1)	
3 Net profit. Subtract line 2 from line 1d. If less than zero, you must use Schedule C. Enter on both Form 1040, line 12 , and Schedule SE, line 2 , or on Form 1040NR, line 13 and Schedule SE, line 2 (see instructions). (If you entered an amount on line 1c, do not report the amount from line 1c on Schedule SE, line 2.) Estates and trusts, enter on Form 1041, line 3	3	2,520		

Part III Information on Your Vehicle. Complete this part **only** if you are claiming car or truck expenses on line 2.

4 When did you place your vehicle in service for business purposes? (month, day, year) ▶ 1/01/06

5 Of the total number of miles you drove your vehicle during 2011, enter the number of miles you used your vehicle for:

a Business 2,358 **b** Commuting (see page 2) _____ **c** Other _____
1/1-6/30 – 1,253 miles @ 51¢ per mile and 7/1-12/31 – 1,105 miles @ 55.5¢ per mile

6 Was your vehicle available for personal use during off-duty hours? Yes No

7 Do you (or your spouse) have another vehicle available for personal use? Yes No

8a Do you have evidence to support your deduction? Yes No

b If "Yes," is the evidence written? Yes No

(1) Expenses have been reduced by 39% as allocable to tax-free income (see calculation on page 58). Most ministers are employees for income tax purposes (with that income reported on line 7, Form 1040, page 1) and also have honoraria and fee income and related expenses that are reportable on Schedule C (C-EZ).

**SCHEDULE SE
(Form 1040)**

Department of the Treasury
Internal Revenue Service (99)

Self-Employment Tax

▶ **Attach to Form 1040 or Form 1040NR.** ▶ **See separate instructions.**

OMB No. 1545-0074

2011

Attachment
Sequence No. **17**

Name of person with **self-employment** income (as shown on Form 1040)
Donald L. Hall

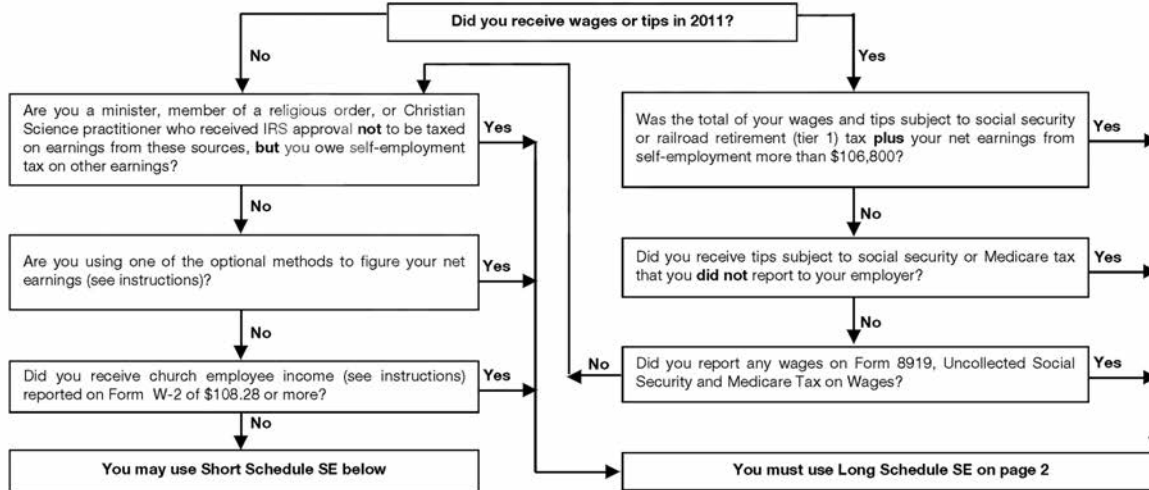
Social security number of person
with **self-employment** income ▶

482-11-6043

Before you begin: To determine if you must file Schedule SE, see the instructions.

May I Use Short Schedule SE or Must I Use Long Schedule SE?

Note. Use this flowchart **only** if you must file Schedule SE. If unsure, see *Who Must File Schedule SE* in the instructions.



Section A—Short Schedule SE. Caution. Read above to see if you can use Short Schedule SE.

1a Net farm profit or (loss) from Schedule F, line 34, and farm partnerships, Schedule K-1 (Form 1065), box 14, code A	1a	
b If you received social security retirement or disability benefits, enter the amount of Conservation Reserve Program payments included on Schedule F, line 4b, or listed on Schedule K-1 (Form 1065), box 20, code Y	1b	()
2 Net profit or (loss) from Schedule C, line 31; Schedule K-1 (Form 1065), box 14, code A (other than farming); and Schedule K-1 (Form 1065-B), box 9, code J1. Ministers and members of religious orders, see instructions for types of income to report on this line. See instructions for other income to report	2	19,860
3 Combine lines 1a, 1b, and 2	3	19,860
4 Multiply line 3 by 92.35% (.9235). If less than \$400, you do not owe self-employment tax; do not file this schedule unless you have an amount on line 1b ▶	4	18,341
Note. If line 4 is less than \$400 due to Conservation Reserve Program payments on line 1b, see instructions.		
5 Self-employment tax. If the amount on line 4 is: • \$106,800 or less, multiply line 4 by 13.3% (.133). Enter the result here and on Form 1040, line 56, or Form 1040NR, line 54 • More than \$106,800, multiply line 4 by 2.9% (.029). Then, add \$11,107.20 to the result. Enter the total here and on Form 1040, line 56, or Form 1040NR, line 54	5	2,439
6 Deduction for employer-equivalent portion of self-employment tax. If the amount on line 5 is: • \$14,204.40 or less, multiply line 5 by 57.51% (.5751) • More than \$14,204.40, multiply line 5 by 50% (.50) and add \$1,067 to the result. Enter the result here and on Form 1040, line 27, or Form 1040NR, line 27	6	1,403

Line 2 – See the schedule on page 58 for the calculation of this amount.

Line 4 – This line results in the deduction of a portion of the self-employment tax liability.

A minister may use Section A-Short Schedule unless he received nonministerial wages (subject to FICA) and the total of these wages and net ministerial self-employment earnings (W-2 and Schedule C-related) is more than \$106,800.

SCHEDULE EIC
(Form 1040A or 1040)

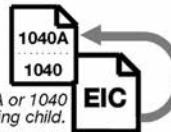
Department of the Treasury
Internal Revenue Service (99)

Name(s) shown on return
Donald L. Hall

Earned Income Credit

Qualifying Child Information

Complete and attach to Form 1040A or 1040
only if you have a qualifying child.



OMB No. 1545-0074

2011

Attachment
Sequence No. **43**

Your social security number
482-11-6043

Before you begin:

- See the instructions for Form 1040A, lines 38a and 38b, or Form 1040, lines 64a and 64b, to make sure that (a) you can take the EIC, and (b) you have a qualifying child.
- Be sure the child's name on line 1 and social security number (SSN) on line 2 agree with the child's social security card. Otherwise, at the time we process your return, we may reduce or disallow your EIC. If the name or SSN on the child's social security card is not correct, call the Social Security Administration at 1-800-772-1213.



- If you take the EIC even though you are not eligible, you may not be allowed to take the credit for up to 10 years. See page 2 of schedule for details.
- It will take us longer to process your return and issue your refund if you do not fill in all lines that apply for each qualifying child.

Qualifying Child Information

Child 1

Child 2

Child 3

	Child 1	Child 2	Child 3
1 Child's name If you have more than three qualifying children, you only have to list three to get the maximum credit.	First name: David K. Last name: Hall	First name: Sarah E. Last name: Hall	First name: Last name:
2 Child's SSN The child must have an SSN as defined in the instructions for Form 1040A, lines 38a and 38b, or Form 1040, lines 64a and 64b, unless the child was born and died in 2011. If your child was born and died in 2011 and did not have an SSN, enter "Died" on this line and attach a copy of the child's birth certificate, death certificate, or hospital medical records.	514-42-7465	416-49-0125	
3 Child's year of birth	Year <u>2</u> <u>0</u> <u>0</u> <u>3</u> <i>If born after 1992 and the child was younger than you (or your spouse, if filing jointly), skip lines 4a and 4b; go to line 5.</i>	Year <u>2</u> <u>0</u> <u>0</u> <u>7</u> <i>If born after 1992 and the child was younger than you (or your spouse, if filing jointly), skip lines 4a and 4b; go to line 5.</i>	Year _____ <i>If born after 1992 and the child was younger than you (or your spouse, if filing jointly), skip lines 4a and 4b; go to line 5.</i>
4a Was the child under age 24 at the end of 2011, a student, and younger than you (or your spouse, if filing jointly)?	<input checked="" type="checkbox"/> Yes. <input type="checkbox"/> No. <i>Go to line 5. Go to line 4b.</i>	<input checked="" type="checkbox"/> Yes. <input type="checkbox"/> No. <i>Go to line 5. Go to line 4b.</i>	<input type="checkbox"/> Yes. <input type="checkbox"/> No. <i>Go to line 5. Go to line 4b.</i>
b Was the child permanently and totally disabled during any part of 2011?	<input type="checkbox"/> Yes. <input type="checkbox"/> No. <i>Go to line 5. The child is not a qualifying child.</i>	<input type="checkbox"/> Yes. <input type="checkbox"/> No. <i>Go to line 5. The child is not a qualifying child.</i>	<input type="checkbox"/> Yes. <input type="checkbox"/> No. <i>Go to line 5. The child is not a qualifying child.</i>
5 Child's relationship to you (for example, son, daughter, grandchild, niece, nephew, foster child, etc.)	Son	Daughter	
6 Number of months child lived with you in the United States during 2011 • If the child lived with you for more than half of 2011 but less than 7 months, enter "7." • If the child was born or died in 2011 and your home was the child's home for the entire time he or she was alive during 2011, enter "12."	<u>12</u> months <i>Do not enter more than 12 months.</i>	<u>12</u> months <i>Do not enter more than 12 months.</i>	<u> </u> months <i>Do not enter more than 12 months.</i>

For Paperwork Reduction Act Notice, see your tax return instructions.

Cat. No. 13339M

Schedule EIC (Form 1040A or 1040) 2011

If you are eligible for the Earned Income Credit, you must file page 1 of Schedule EIC if you have a qualifying child. Compute your credit on Worksheet B found in the IRS instruction booklet.

There could have been a much larger Earned Income Credit if Donald Hall's business expenses had been reimbursed and a lower salary prospectively established. The expenses claimed on Form 2106-EZ do not offset earned income for the EIC calculation.

Worksheet B—Earned Income Credit (EIC)—Lines 64a and 64b

Keep for Your Records



Use this worksheet if you answered “Yes” to Step 5, question 3, on page 47.

- ✓ Complete the parts below (Parts 1 through 3) that apply to you. Then, continue to Part 4.
- ✓ If you are married filing a joint return, include your spouse’s amounts, if any, with yours to figure the amounts to enter in Parts 1 through 3.

Part 1	1a. Enter the amount from Schedule SE, Section A, line 3, or Section B, line 3, whichever applies.		1a	29,010 ¹
Self-Employed, Members of the Clergy, and People With Church Employee Income Filing Schedule SE	b. Enter any amount from Form 1040, line 29.	+	1b	
	c. Enter any amount from Schedule SE, Section B, line 4b, and line 5a.	+	1c	
	d. Combine lines 1a, 1b, and 1c.	=	1d	29,010
	e. Enter the amount from Schedule SE, Section A, line 6, or Section B, line 13, whichever applies.	-	1e	1,403
	f. Subtract line 1e from 1d.	=	1f	27,607

Part 2	2. Do not include on these lines any statutory employee income, any net profit from services performed as a notary public, any amount exempt from self-employment tax as the result of the filing and approval of Form 4029 or Form 4361, any income or loss from a qualified joint venture reporting only rental real estate income not subject to self-employment tax, or any other amounts exempt from self-employment tax.			
Self-Employed NOT Required To File Schedule SE <small>For example, your net earnings from self-employment were less than \$400.</small>	a. Enter any net farm profit or (loss) from Schedule F, line 36, and from farm partnerships, Schedule K-1 (Form 1065), box 14, code A*.		2a	
	b. Enter any net profit or (loss) from Schedule C, line 31; Schedule C-EZ, line 3; Schedule K-1 (Form 1065), box 14, code A (other than farming); and Schedule K-1 (Form 1065-B), box 9, code J1*.	+	2b	
	c. Combine lines 2a and 2b.	=	2c	

*If you have any Schedule K-1 amounts, complete the appropriate line(s) of Schedule SE, Section A. Reduce the Schedule K-1 amounts as described in the Partner’s Instructions for Schedule K-1. Enter your name and social security number on Schedule SE and attach it to your return.

Part 3	3. Enter the amount from Schedule C, line 1, or Schedule C-EZ, line 1, that you are filing as a statutory employee.		3	
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Part 4	4a. Enter your earned income from Step 5 on page 47.		4a	
All Filers Using Worksheet B <small>Note. If line 4b includes income on which you should have paid self-employment tax but did not, we may reduce your credit by the amount of self-employment tax not paid.</small>	b. Combine lines 1f, 2c, 3, and 4a. This is your total earned income.		4b	27,607
	5. If you have:			
	<ul style="list-style-type: none"> • 3 or more qualifying children, is line 4b less than \$43,352 (\$48,362 if married filing jointly)? • 2 qualifying children, is line 4b less than \$40,363 (\$45,373 if married filing jointly)? • 1 qualifying child, is line 4b less than \$35,535 (\$40,545 if married filing jointly)? • No qualifying children, is line 4b less than \$13,460 (\$18,470 if married filing jointly)? <input type="checkbox"/> Yes. If you want the IRS to figure your credit, see page 47. If you want to figure the credit yourself, enter the amount from line 4b on line 6 (page 51). <input type="checkbox"/> No. You cannot take the credit. Enter “No” on the dotted line next to line 64a.			

¹Included on Line 1a:
 Julie Hall’s salary \$ 9,150
 Schedule SE income 19,860
 \$29,010

Worksheet **B**—Continued from page 50

Keep for Your Records



Part 5

All Filers Using Worksheet B

6. Enter your total earned income from Part 4, line 4b, on page 50.

6	27,607
---	--------

7. Look up the amount on line 6 above in the EIC Table on pages 52–68 to find the credit. Be sure you use the correct column for your filing status and the number of children you have. Enter the credit here.

7	3,879
---	-------

If line 7 is zero, You cannot take the credit. Enter “No” on the dotted line next to line 64a.

8. Enter the amount from Form 1040, line 38.

8	27,834
---	--------

9. Are the amounts on lines 8 and 6 the same?
 Yes. Skip line 10; enter the amount from line 7 on line 11.
 No. Go to line 10.

Part 6

Filers Who Answered “No” on Line 9

10. If you have:
• No qualifying children, is the amount on line 8 less than \$7,500 (\$12,500 if married filing jointly)?
• 1 or more qualifying children, is the amount on line 8 less than \$16,450 (\$21,500 if married filing jointly)?
 Yes. Leave line 10 blank; enter the amount from line 7 on line 11.
 No. Look up the amount on line 8 in the EIC Table on pages 52–68 to find the credit. Be sure you use the correct column for your filing status and the number of children you have. Enter the credit here. Look at the amounts on lines 10 and 7. Then, enter the **smaller** amount on line 11.

10	3,837
----	-------

Part 7

Your Earned Income Credit

11. **This is your earned income credit.**

11	3,837
----	-------

Reminder—

✓ If you have a qualifying child, complete and attach Schedule EIC.



Enter this amount on Form 1040, line 64a.



If your EIC for a year after 1996 was reduced or disallowed, see page 48 to find out if you must file Form 8862 to take the credit for 2010.

Form **8812**

Additional Child Tax Credit



OMB No. 1545-0074

2011

Attachment
Sequence No. **47**

Department of the Treasury
Internal Revenue Service (99)

Complete and attach to Form 1040, Form 1040A, or Form 1040NR.

Name(s) shown on return

Donald L. and Julie M. Hall

Your social security number

482-11-6043

Part I All Filers

1	1040 filers: Enter the amount from line 6 of your Child Tax Credit Worksheet (see the Instructions for Form 1040, line 51).				
	1040A filers: Enter the amount from line 6 of your Child Tax Credit Worksheet (see the Instructions for Form 1040A, line 33).				
	1040NR filers: Enter the amount from line 6 of your Child Tax Credit Worksheet (see the Instructions for Form 1040NR, line 48).				
If you used Pub. 972, enter the amount from line 8 of the Child Tax Credit Worksheet in the publication.					
2	Enter the amount from Form 1040, line 51, Form 1040A, line 33, or Form 1040NR, line 48	2			144
3	Subtract line 2 from line 1. If zero, stop ; you cannot take this credit	3			1,856
4a	Earned income (see instructions on back) (27,607 - 1,000)	4a		26,607	
b	Nontaxable combat pay (see instructions on back)	4b			
5	Is the amount on line 4a more than \$3,000? <input type="checkbox"/> No. Leave line 5 blank and enter -0- on line 6. <input checked="" type="checkbox"/> Yes. Subtract \$3,000 from the amount on line 4a. Enter the result	5		23,607	
6	Multiply the amount on line 5 by 15% (.15) and enter the result Next. Do you have three or more qualifying children? <input checked="" type="checkbox"/> No. If line 6 is zero, stop; you cannot take this credit. Otherwise, skip Part II and enter the smaller of line 3 or line 6 on line 13. <input type="checkbox"/> Yes. If line 6 is equal to or more than line 3, skip Part II and enter the amount from line 3 on line 13. Otherwise, go to line 7.	6			3,541

Part II Certain Filers Who Have Three or More Qualifying Children

7	Withheld social security and Medicare taxes from Form(s) W-2, boxes 4 and 6. If married filing jointly, include your spouse's amounts with yours. If you worked for a railroad, see instructions on back	7			
8	1040 filers: Enter the total of the amounts from Form 1040, lines 27 and 57, plus any taxes that you identified using code "UT" and entered on line 60. 1040A filers: Enter -0-. 1040NR filers: Enter the total of the amounts from Form 1040NR, lines 27 and 55, plus any taxes that you identified using code "UT" and entered on line 59.	8			
9	Add lines 7 and 8	9			
10	1040 filers: Enter the total of the amounts from Form 1040, lines 64a and 69. 1040A filers: Enter the total of the amount from Form 1040A, line 38a, plus any excess social security and tier 1 RRTA taxes withheld that you entered to the left of line 41 (see instructions on back). 1040NR filers: Enter the amount from Form 1040NR, line 65.	10			
11	Subtract line 10 from line 9. If zero or less, enter -0-	11			
12	Enter the larger of line 6 or line 11 Next, enter the smaller of line 3 or line 12 on line 13.	12			

Part III Additional Child Tax Credit

13	This is your additional child tax credit	13			1,856
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Enter this amount on
Form 1040, line 65,
Form 1040A, line 39, or
Form 1040NR, line 63.

Child Tax Credit Worksheet

Keep for Your Records

Before you begin: ✓ Figure the amount of any credits you are claiming on Form 5695, Part I; Form 8834, Part I; Form 8910; Form 8936; or Schedule R.



To be a qualifying child for the child tax credit, the child must be **under age 17** at the end of 2011 and meet the other requirements listed earlier, under Qualifying Child.



Part 1

1. Number of qualifying children: 2 × \$1,000. Enter the result.

1	2,000
---	-------

2. Enter the amount from Form 1040, line 38; Form 1040A, line 22; or Form 1040NR, line 37.

2	27,834
---	--------

3. **1040 Filers.** Enter the total of any—
 • Exclusion of income from Puerto Rico, and
 • Amounts from Form 2555, lines 45 and 50; Form 2555-EZ, line 18; and Form 4563, line 15.
1040A and 1040NR Filers. Enter -0-.

3	0
---	---

4. Add lines 2 and 3. Enter the total.

4	27,834
---	--------

5. Enter the amount shown below for your filing status.
 • Married filing jointly - \$110,000
 • Single, head of household, or qualifying widow(er) - \$75,000
 • Married filing separately - \$55,000

5	110,000
---	---------

6. Is the amount on line 4 more than the amount on line 5?
 No. Leave line 6 blank. Enter -0- on line 7.
 Yes. Subtract line 5 from line 4.
 If the result is not a multiple of \$1,000, increase it to the next multiple of \$1,000.
 For example, increase \$425 to \$1,000, increase \$1,025 to \$2,000, etc.

6	
---	--

7. Multiply the amount on line 6 by 5% (.05). Enter the result.

7	0
---	---

8. Is the amount on line 1 more than the amount on line 7?
 No. You cannot take the child tax credit on Form 1040, line 51; Form 1040A, line 33; or Form 1040NR, line 48. You also cannot take the additional child tax credit on Form 1040, line 65; Form 1040A, line 39; or Form 1040NR, line 63. Complete the rest of your Form 1040, Form 1040A, or Form 1040NR.
 Yes. Subtract line 7 from line 1. Enter the result.
Go to Part 2 on the next page.

8	2,000
---	-------

Child Tax Credit Worksheet—Continued

Keep for Your Records

Part 2

9. Enter the amount from Form 1040, line 46; Form 1040A, line 28; or Form 1040NR, line 44. 9 144

10. Add the following amounts from:

Form 1040 or Form 1040A or Form 1040NR

Line 47	Line 45	+ _____
Line 48	Line 46	+ _____
Line 49	Line 47	+ _____
Line 50	Line 47	+ _____

Form 5695, line 14	+ _____
Form 8834, line 23	+ _____
Form 8910, line 22	+ _____
Form 8936, line 15	+ _____
Schedule R, line 22	+ _____

Enter the total. 10 0

11. Are you claiming any of the following credits?

- Mortgage interest credit, Form 8396.
- Residential energy efficient property credit, Form 5695, Part II.
- District of Columbia first-time homebuyer credit, Form 8859.

No. Enter the amount from line 10. 11 0

Yes. Complete the Line 11 Worksheet on the next page to figure the amount to enter here.

12. Subtract line 11 from line 9. Enter the result. 12 144

13. Is the amount on line 8 of this worksheet more than the amount on line 12?

No. Enter the amount from line 8.

Yes. Enter the amount from line 12. See the **TIP** below. 13 144

This is your child tax credit.

Enter this amount on Form 1040, line 51; Form 1040A, line 33; or Form 1040NR, line 48.



You may be able to take the **additional child tax credit** on Form 1040, line 65; Form 1040A, line 39; or Form 1040NR, line 63, only if you answered “Yes” on line 13.

- First, complete your Form 1040 through line 64a (also complete line 69), Form 1040A through line 38a, or Form 1040NR through line 62 (also complete line 65).
- Then, use Form 8812 to figure any additional child tax credit.

Form **2106-EZ**

Unreimbursed Employee Business Expenses

OMB No. 1545-0074

2011

Department of the Treasury
Internal Revenue Service (99)

▶ Attach to Form 1040 or Form 1040NR.

Attachment
Sequence No. **129A**

Your name Donald L. Hall	Occupation in which you incurred expenses Minister	Social security number 482 11 6043		
------------------------------------	--	--	--	--

You Can Use This Form Only if All of the Following Apply.

- You are an employee deducting ordinary and necessary expenses attributable to your job. An ordinary expense is one that is common and accepted in your field of trade, business, or profession. A necessary expense is one that is helpful and appropriate for your business. An expense does not have to be required to be considered necessary.
- You **do not** get reimbursed by your employer for any expenses (amounts your employer included in box 1 of your Form W-2 are not considered reimbursements for this purpose).
- If you are claiming vehicle expense, you are using the standard mileage rate for 2011.

Caution: You can use the standard mileage rate for 2011 **only if:** (a) you owned the vehicle and used the standard mileage rate for the first year you placed the vehicle in service, or (b) you leased the vehicle and used the standard mileage rate for the portion of the lease period after 1997.

Part I Figure Your Expenses

1	Complete Part II. Multiply line 8a by 51¢ (.51) for miles driven before July 1, 2011, and by 55.5¢ (.555) for miles driven after June 30, 2011. Add the amounts, then enter the result here	1	2,613
2	Parking fees, tolls, and transportation, including train, bus, etc., that did not involve overnight travel or commuting to and from work	2	
3	Travel expense while away from home overnight, including lodging, airplane, car rental, etc. Do not include meals and entertainment	3	514
4	Business expenses not included on lines 1 through 3. Do not include meals and entertainment	4	640
5	Meals and entertainment expenses: \$ <u>878</u> × 50% (.50). (Employees subject to Department of Transportation (DOT) hours of service limits: Multiply meal expenses incurred while away from home on business by 80% (.80) instead of 50%. For details, see instructions.)	5	439
6	Total expenses. Add lines 1 through 5. Enter here and on Schedule A (Form 1040), line 21 (or on Schedule A (Form 1040NR), line 7). (Armed Forces reservists, fee-basis state or local government officials, qualified performing artists, and individuals with disabilities: See the instructions for special rules on where to enter this amount.)	6	4,206

Part II Information on Your Vehicle. Complete this part **only** if you are claiming vehicle expense on line 1.

- 7 When did you place your vehicle in service for business use? (month, day, year) ▶ 1 / 1 / 06
- 8 Of the total number of miles you drove your vehicle during 2011, enter the number of miles you used your vehicle for:
- a Business 8,061 b Commuting (see instructions) 2,432 c Other 2,358 (Sch. C Related)
- 9 Was your vehicle available for personal use during off-duty hours? Yes No
- 10 Do you (or your spouse) have another vehicle available for personal use? Yes No
- 11a Do you have evidence to support your deduction? Yes No
- b If "Yes," is the evidence written? Yes No

For Paperwork Reduction Act Notice, see your tax return instructions. Cat. No. 20604Q Form **2106-EZ** (2011)

Lines 1, 3, 4, 5 – See allocations on page 58.
Line 6 – The total expenses on this line are carried forward to Form 1040, Schedule A, line 21.

Form **3903**
 Department of the Treasury
 Internal Revenue Service (99)

Moving Expenses

▶ Attach to Form 1040 or Form 1040NR.

OMB No. 1545-0074

2011
 Attachment
 Sequence No. **170**

Name(s) shown on return

Donald L. Hall

Your social security number

482-11-6043

Before you begin: ✓ See the **Distance Test** and **Time Test** in the instructions to find out if you can deduct your moving expenses.
 ✓ See **Members of the Armed Forces** in the instructions, if applicable.

1 Transportation and storage of household goods and personal effects (see instructions)	1	1,183	
2 Travel (including lodging) from your old home to your new home (see instructions). Do not include the cost of meals	2		
3 Add lines 1 and 2	3	1,183	
4 Enter the total amount your employer paid you for the expenses listed on lines 1 and 2 that is not included in box 1 of your Form W-2 (wages). This amount should be shown in box 12 of your Form W-2 with code P	4		
5 Is line 3 more than line 4? <input type="checkbox"/> No. You cannot deduct your moving expenses. If line 3 is less than line 4, subtract line 3 from line 4 and include the result on Form 1040, line 7, or Form 1040NR, line 8. <input checked="" type="checkbox"/> Yes. Subtract line 4 from line 3. Enter the result here and on Form 1040, line 26, or Form 1040NR, line 26. This is your moving expense deduction	5	1,183	

For Paperwork Reduction Act Notice, see your tax return instructions.

Cat. No. 12490K

Form **3903** (2011)

Form **8880**
Department of the Treasury
Internal Revenue Service

Credit for Qualified Retirement Savings Contributions

▶ Attach to Form 1040, Form 1040A, or Form 1040NR.
▶ See instructions on back.

OMB No. 1545-0074
2011
Attachment
Sequence No. **54**

Name(s) shown on return
Donald L. Hall

Your social security number
482-11-6043

You **cannot** take this credit if **either** of the following applies.



- The amount on Form 1040, line 38; Form 1040A, line 22; or Form 1040NR, line 37 is more than \$28,250 (\$42,375 if head of household; \$56,500 if married filing jointly).
- The person(s) who made the qualified contribution or elective deferral **(a)** was born after January 1, 1994, **(b)** is claimed as a dependent on someone else's 2011 tax return, or **(c)** was a **student** (see instructions).

	(a) You	(b) Your spouse
1 Traditional and Roth IRA contributions for 2011. Do not include rollover contributions		
2 Elective deferrals to a 401(k) or other qualified employer plan, voluntary employee contributions, and 501(c)(18)(D) plan contributions for 2011 (see instructions)	500	
3 Add lines 1 and 2	500	
4 Certain distributions received after 2008 and before the due date (including extensions) of your 2011 tax return (see instructions). If married filing jointly, include both spouses' amounts in both columns. See instructions for an exception		
5 Subtract line 4 from line 3. If zero or less, enter -0-	500	
6 In each column, enter the smaller of line 5 or \$2,000	500	
7 Add the amounts on line 6. If zero, stop ; you cannot take this credit		500
8 Enter the amount from Form 1040, line 38*; Form 1040A, line 22; or Form 1040NR, line 37		
9 Enter the applicable decimal amount shown below:		

If line 8 is—		And your filing status is—		
Over—	But not over—	Married filing jointly	Head of household	Single, Married filing separately, or Qualifying widow(er)
Enter on line 9—				
---	\$17,000	.5	.5	.5
\$17,000	\$18,250	.5	.5	.2
\$18,250	\$25,500	.5	.5	.1
\$25,500	\$27,375	.5	.2	.1
\$27,375	\$28,250	.5	.1	.1
\$28,250	\$34,000	.5	.1	.0
\$34,000	\$36,500	.2	.1	.0
\$36,500	\$42,375	.1	.1	.0
\$42,375	\$56,500	.1	.0	.0
\$56,500	---	.0	.0	.0

Note: If line 9 is zero, **stop**; you cannot take this credit.

10 Multiply line 7 by line 9		250
11 Enter the amount from Form 1040, line 46; Form 1040A, line 28; or Form 1040NR, line 44	0	
12 1040 filers: Enter the total of your credits from lines 47 through 49, and Schedule R, line 22. } 1040A filers: Enter the total of your credits from lines 29 through 31. } 1040NR filers: Enter the total of your credits from lines 45 and 46. }	0	
13 Subtract line 12 from line 11. If zero, stop ; you cannot take this credit		0
14 Credit for qualified retirement savings contributions. Enter the smaller of line 10 or line 13 here and on Form 1040, line 50; Form 1040A, line 32; or Form 1040NR, line 47		

*See Pub. 590 for the amount to enter if you are filing Form 2555, 2555-EZ, or 4563 or you are excluding income from Puerto Rico.

Attachment 1.**Computation of expenses, allocatable to tax-free ministerial income, that are nondeductible**

	<u>Taxable</u>	<u>Tax-Free</u>	<u>Total</u>
Salary as a minister (less housing allowance designation)	\$ 8,500		\$ 8,500
Special occasion gifts	500		500
Reimbursement of self-employment tax	2,100		2,100
Expense allowance under nonaccountable plan	1,700		1,700
Housing allowance:			
Amount designated and paid by church	\$ 2,000		
Actual expenses	<u>1,000</u>		
Taxable portion of allowance	<u>\$ 1,000</u>	1,000	2,000
Fair rental value of home (including furnishings and utilities)		11,150	11,150
Schedule C gross income from ministry	<u>5,200</u>		<u>5,200</u>
Ministerial income	<u>\$ 19,000</u>	<u>\$ 12,150</u>	<u>\$ 31,150</u>
% of nondeductible expenses: \$12,150/\$31,150 = 39%			

Unreimbursed Employee Business Expenses

	<u>61%</u> <u>Deductible</u>	<u>39%</u> <u>Not Deductible</u>
Business mileage:		
1/1 – 6/30 — 4,212 x 51¢ per mile		
7/1 – 12/31 — 3,849 x 55.5¢ per mile	\$ 2,613	\$ 1,671
Travel expense:		
Airfare	412	263
Lodging	102	65
Business expenses:		
Subscriptions	122	78
Books and supplies	213	137
Continuing education tuition	305	195
Meals and entertainment expenses:		
Meals	\$ 233	
Entertainment	<u>1,207</u>	
	<u>\$ 1,440</u> x 50% = \$720	
	<u>439</u>	<u>281</u>
Form 2106-EZ	<u>\$ 4,206</u>	<u>\$ 2,690</u>

Attachment 2.**Net earnings from self-employment (attachment to Schedule SE, Form 1040)**

Salary paid by church as reflected on Form W-2, Box 1	\$ 12,800
Net profit or loss as reflected on Schedule C or C-EZ (includes speaking honoraria, offerings you receive for weddings, baptisms, funerals, and other fees)	2,520
Housing allowance excluded from salary on Form W-2	2,000
Fair rental value of church-provided housing (including paid utilities)	<u>11,150</u>
	<u>28,470</u>
Less:	
Unreimbursed ministerial business and professional expenses or reimbursed expenses paid under a nonaccountable plan	
A. Deductible on Schedule A before the 2% of AGI limitation	4,206
B. Not deductible on Form 2106/2106 EZ (\$2,690) or Schedule C/C-EZ (\$1,714) because expenses were allocated to taxable/nontaxable income	<u>4,404</u>
Total deductions	<u>8,610</u>
Net earnings from self-employment (to Schedule SE) (See page 48)	<u>\$ 19,860</u>

Housing Allowance Worksheet

Clergy Living in Housing

Owned or Rented by the Congregation

Name: Donald L. Hall

For the period January 1, 2011 to December 31, 2011

Date designation approved December 20, 2010

Allowable Housing Expenses (*expenses paid from current income*)

	<u>Estimated Expenses</u>	<u>Actual</u>
Utilities (<i>gas, electricity, water</i>) and trash collection	\$ _____	\$ _____
Local telephone expense (<i>base charge</i>)	<u>250</u>	<u>275</u>
Decoration and redecoration	_____	_____
Structural maintenance and repair	_____	_____
Landscaping, gardening, and pest control	_____	_____
Furnishings (<i>purchase, repair, replacement</i>)	<u>1,218</u>	<u>460</u>
Personal property insurance on minister-owned contents	<u>200</u>	<u>190</u>
Personal property taxes on contents	<u>150</u>	<u>75</u>
Umbrella liability insurance	_____	_____
Subtotal	<u>1,818</u>	
10% allowance for unexpected expenses	<u>182</u>	
TOTAL	\$ <u><u>2,000</u></u>	\$ <u><u>1,000</u></u> (A)
Properly designated housing allowance		\$ <u><u>2,000</u></u> (B)

The amount excludable from income for federal income tax purposes is the lower of A or B.

Because actual housing expenses are less than the designated allowance, the housing exclusion is limited to \$1,000. The \$1,000 difference between the designation and the exclusion is reported as excess housing allowance on Form 1040, line 7 (see page 44).

22222		Void <input type="checkbox"/>	a Employee's social security number 482-11-6043		For Official Use Only ▶ OMB No. 1545-0008		
b Employer identification number (EIN) 25-7921873			1 Wages, tips, other compensation 12800.00		2 Federal income tax withheld		
c Employer's name, address, and ZIP code Lancaster Community Church 1425 Spencer Avenue Wabash, IN 46992			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 Donald L.		Last name Hall	Suff.	11 Nonqualified plans		12a See instructions for box 12 E 500	
f Employee's address and ZIP code 804 Linden Avenue Wabash, IN 46992			13 Statutory employee <input type="checkbox"/>	Retirement plan <input checked="" type="checkbox"/>	Third-party sick pay <input type="checkbox"/>	12b	
			14 Other			12c	
						12d	
15 State Employer's state ID number IN		16 State wages, tips, etc. 12800.00	17 State income tax 750	18 Local wages, tips, etc.	19 Local income tax	20 Locality name	

Form **W-2** Wage and Tax Statement **2011** Department of the Treasury—Internal Revenue Service
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Explanation of compensation reported on Form W-2, Box 1:

Salary (\$11,000 less \$2,000 housing allowance and \$500 403[b] contributions)	\$ 8,500
Special occasion gifts	500
Reimbursement of self-employment tax	2,100
Expense allowance under nonaccountable plan	<u>1,700</u>
	<u>\$12,800</u>

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- Healthcare flexible spending account
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- Health reimbursement arrangements
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Rev. Rul. 2002-41

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40 T.C.M. 1164 (1980)
- Personal computer expenses
Code Sec. 280F

Rev. Rul. 86-129
- Traveling/commuting
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Walker v. Commissioner,
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- Opting out of social security
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10

Biggest Tax Mistakes Made By Clergy

- 1.** Improperly treating congregation payments for out-of-pocket medical expenses as tax-free when the congregation has not established a proper plan.
- 2.** Filing as self-employed for income tax purposes on your congregation salary, using tax benefits only available to employees, and leaving yourself vulnerable to reclassification by the IRS to employee status upon audit.
- 3.** Failing to have at least a modest housing allowance designated when living in a congregation-provided housing.
- 4.** Failure to understand and apply the fair rental test for the housing allowance relating to clergy-provided housing.
- 5.** Confusing the fair rental value of a congregation-provided parsonage (only includible for social security purposes) with the designation of a portion of your salary as housing allowance (providing an exclusion for income tax purposes).
- 6.** Failing to keep a log of miles driven for personal use v. congregation purposes.
- 7.** Claiming office-in-the-home treatment — rarely justified under present law.
- 8.** Not documenting business expenses to reflect business purpose, business relationship, cost, time, and place.
- 9.** Failure of clergy to use an accountable reimbursement plan.
- 10.** Improperly opting out of social security because you don't believe it is a good investment.



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