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Get the keys to the clergy housing allowance

MIMBB understands how important it is to maximize the value of the housing allowance for the benefit of the clergy. Many ministers either fail to claim the allowance or simply do not claim enough. Keep in mind that the clergy housing allowance applies only to amounts paid on federal income taxes.

Pastors can take one of the three common types of clergy housing allowance, depending on their living situation.

- Those who live in a church-provided parsonage do not pay federal income taxes on the amount of their compensation that their church designates in advance as a parsonage allowance.
- If the pastor rents a home or apartment, the pastor does not pay federal income taxes on the amount of compensation the church designates in advance as a housing allowance.
- The same applies if a minister owns their home.

The clergy housing allowance includes housing-related expenses such as mortgage and rental payments, utilities, repairs, furnishings, insurance, property taxes, additions and maintenance. The housing allowance is also subject to limits, according to the IRS code.

“The limits for the housing allowance are really based on what you claim and what is designated by the church and then what is actually spent,” as Rev. Dr. Perry Hopper, Associate Executive Director explains. “So, for example, the Internal Revenue Service applies a three-part test to determine how much of the income you can actually claim. First, how much did your church or employer designate as your housing allowance? Second, what is the fair rental value of your home furnished, plus utilities? That requires some assessment of how much that home is worth, maybe even an appraisal. And the third is what is actually spent. When you total up all your expenses for the year, how much did you actually spend? Under the IRS code the limit is the lowest amount of those three that you’re eligible to claim as the housing amount for the year.”

So, the bottom line is clergy are limited to the lesser of the three:

- What did the church designate?
- What did the pastor actually spend for the year?
- What is the fair market value of the home?

Keep these considerations in mind when determining your clergy housing allowance:

- The housing allowance is considered compensation for ministerial services, and the church must designate the value of the clergy housing allowance in advance. It's important to know that a minister cannot exclude more than the church designates. Any amount a minister spends on housing that exceeds what the church designates must be reported as taxable income. If audited by the IRS, it is the responsibility of the minister to document actual housing expenses and keep all receipts.
- Pastors must pay close attention to structuring their compensation package to take advantage of every tax benefit available. Hopper points out, "If you structure certain elements of a clergy person's compensation in ways that are tax-advantaged and paid on their behalf instead of directly to them, it becomes a favorable strategy."
- Some parts of compensation should be paid directly to the clergy, but other parts should be paid on their behalf. MMBB recommends structuring compensation so that cash and the Social Security allowance (also known as a Social Security/Medicare tax offset) are paid directly to the clergy, and the rest paid on their behalf, so it doesn't become taxable income to the pastor. Ministers should also take note that they must pay Social Security/Medicare taxes on the dollar amount designated as clergy housing allowance.
- During budget season, churches must consider the clergy housing allowance as part of their spending plan for the year. "As we're in this budget season, and as pastors consider where they're headed in 2023, this would be the time to begin making those kinds of estimates," Dr. Hopper explains. "And I say 'estimate' because it's not always an exact science, but you estimate to the best of your ability how much of your income will be declared as housing. And so, you set it up in consultation with the church, you declare how much it is, or is going to be, and then you put that on file with the employer or with the church."
- Under certain circumstances, pastors can make changes in their housing allowance. "It can be changed for things like a major expense that requires you to change your housing allowance, such as a roof replacement, or if you're going to add on a room to the house for various reasons," Hopper says. "If there's some major change that requires you to change your housing allowance,

that is fine. If you change in the middle of the year, in July, for example, that can only be for expenses going from July forward. You cannot change retroactively. Pastors and other church workers often get confused as to whether they can change and include retroactive expenses: you cannot. Changes can only be for those expenses that are paid forward."

Hopper also adds one helpful caveat. "If you move from one ministry to another, or you go to another church during the middle of the year, of course, you are able to change your housing allowance from that point on."

MMBB recommends that clergy work with accountants who are acquainted with how the housing allowance works when it comes to preparing their taxes. For more information on the housing allowance visit our website. [f i](#)

Portions of this article appeared in the December 2020 issue of Charisma Digital, a publication of Charisma magazine.

