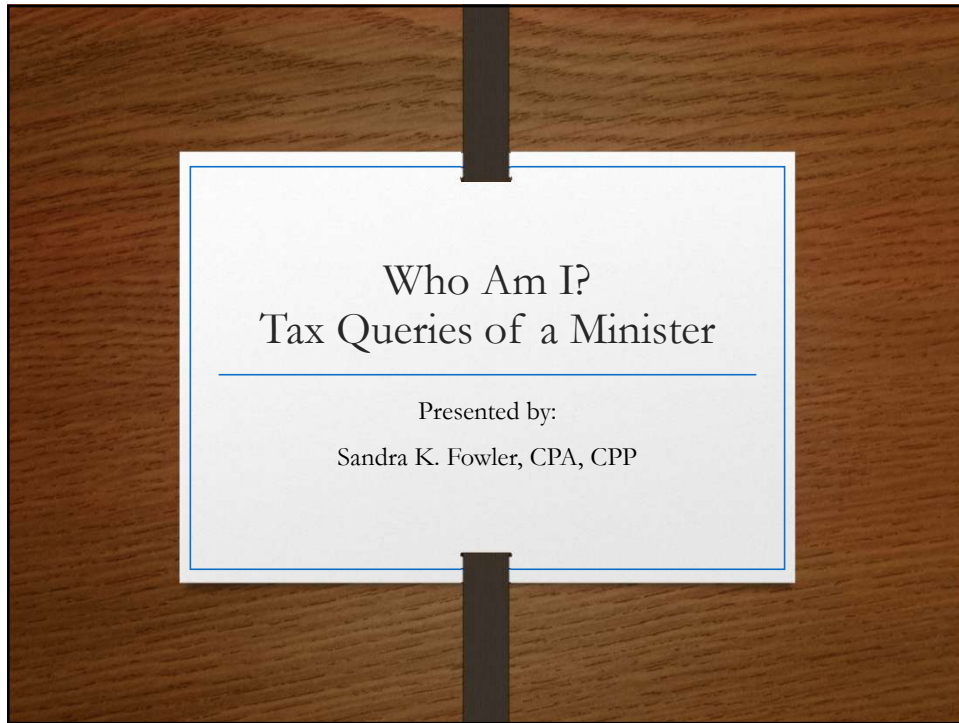




1

**Classifying
Ministers
for Payroll
Purposes**

- Step 1 - Must be commissioned, licensed or ordained by a church
- Step 2 – If Step 1 is met, then you must be performing ministerial duties*:
 - Performance of sacerdotal functions
 - Conduct religious worship services
 - Control, conduct or maintenance of religious organizations or
 - Teaching at theological seminaries
 - On assignment by a church

*If not working for a church, the list of duties is more restricted.

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Employees who meet the above two steps must be treated as ministers! This isn't optional, so if the above test is met, the rest of this course applies to you!

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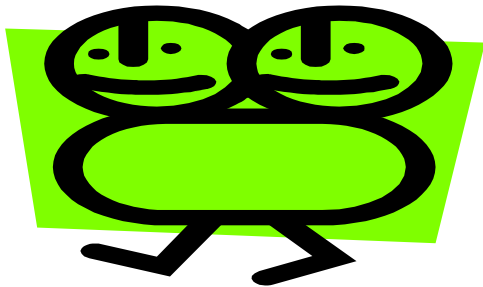
3

So, I am a Minister - What Now?

There are two main questions for tax purposes:

- How is a minister classified for federal income tax purposes?
- How is a minister classified for social security tax purposes?

TWO PEOPLE IN ONE



Because ministers can be classified differently for different tax purposes it is considered that they have "dual tax" status.

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Classification for Federal Income Tax

- There are two possible ways a minister can be classified for purposes of federal income tax
- A minister may be self-employed and file Schedule C
- A minister may be an employee and receive Form W-2

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When am I Self-Employed for Federal Income Tax?

- Income earned outside regular work for your primary church, i.e., honorariums for speaking, funerals, weddings, etc.
 - Income reported on Schedule C of your Form 1040
 - Any expenses related specifically to this work; i.e., mileage, hotels, etc., may be deducted on Schedule C.



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When Am I An Employee for Federal Income Tax?

- Income earned from one primary source is going classify you as an employee of that organization or church.
 - Classified as a common law employee
 - This determines:
 - Participation in Benefit Plans
 - The taxability of health insurance premiums
 - Form W-2 reporting of income not on a Form 1099-NEC
 - Income tax withholding optional. A minister must give the church specific permission to withholding tax.



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How Am I Classified for Paying into Social Security?

- There are two ways individuals to pay into the social security system
 - Self Employed Contributions Act (SECA) – Paid with Form 1040
 - Federal Insurance Contributions Act (FICA) – Paid through withholding and matching by your employer

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Ministers and Social Security

- The law says ministers must pay in through the self employment tax system for all their income earned from their ministry. Not an option to pay in through FICA.
- Therefore, **for social security only**, ministers are self-employed and required to file Schedule SE as a part of their Federal Form 1040 filing unless they have obtained an exemption from self-employment tax (to be discussed) even if they are considered an employee of the church.

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MINISTER'S FORM W-2

Optional withholding

22222		VOID ☐	a Employee's social security number		For Official Use Only OMB No. 1545-0008	
b Employer identification number (EIN)			1 Wages, tips, other compensation		2 Federal income tax withheld	
c Employer's name, address, and ZIP code			3 Social security wages		4 Social security tax withheld	
These boxes are always empty – A minister may never have FICA/Medicare withheld			5 Medicare wages and tips		6 Medicare tax withheld	
			7 Social security tips		8 Allocated tips	
d Control number			9		10 Dependent care benefits	
e Employee's first name and initial		Last name	Surf.	11 Nonqualified plans		12a See instructions for box 12
f Employee's address and ZIP code			13 Statutory employee ☐ Retirement plan ☐ Third-party sick pay ☐		12b	
			14 Other		12c	
15 State Employer's state ID number			16 State wages, tips, etc.		17 State income tax	
18 Local wages, tips, etc.			19 Local income tax		20 Locality name	

Housing allowance optional

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Isn't Self Employment Tax Optional?

- Ministers may opt out based on their theological beliefs against socialized insurance
- Form 4361
 - File by the due date of the Form 1040 for the 2nd year in which the minister had self employment income of \$400 or more of which any portion is attributable to ministry work
 - Filed in triplicate and **not** with your Form 1040
 - Not effective until it is approved by the IRS!
 - **DON'T LOSE THE APPROVED FORM!**

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4361 Form (Rev. January 2011) Department of the Treasury Internal Revenue Service		Application for Exemption From Self-Employment Tax for Use by Ministers, Members of Religious Orders and Christian Science Practitioners		OMB No. 1545-0074 File Original and Two Copies
File original and two copies and attach supporting documents. This exemption is granted only if the IRS returns a copy to you marked "approved."				
Please type or print	1 Name of taxpayer applying for exemption (as shown on Form 1040)		Social security number	
	Number and street (including apt. no.)		Telephone number (optional)	
	City or town, state, and ZIP code			
Please type or print	2 Check one box: ☐ Christian Science practitioner ☐ Ordained minister, priest, rabbi		3 Date ordained, licensed, etc. (Attach supporting document. See instructions.)	
	☐ Member of religious order not under a vow of poverty ☐ Commissioned or licensed minister (see line 6)			
	4 Legal name of ordaining, licensing, or commissioning body or religious order			
Please type or print	Number, street, and room or suite no.		Employer identification number	
	City or town, state, and ZIP code			
	5 Enter the first 2 years after the date shown on line 3 that you had net self-employment earnings of \$400 or more, any of which came from services as a minister, priest, rabbi, etc.; member of a religious order; or Christian Science practitioner			
6 If you apply for the exemption as a licensed or commissioned minister and your denomination also ordains ministers, please indicate how your ecclesiastical powers differ from those of an ordained minister of your denomination. Attach a copy of your denomination's bylaws relating to the powers of ordained, commissioned, and licensed ministers.				

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7 I certify that I am conscientiously opposed to, or because of my religious principles I am opposed to, the acceptance (for services I perform as a minister, member of a religious order not under a vow of poverty, or Christian Science practitioner) of any public insurance that makes payments in the event of death, disability, old age, or retirement; or that makes payments toward the cost of, or provides services for, medical care. (Public insurance includes insurance systems established by the Social Security Act.)

I certify that as a duly ordained, commissioned, or licensed minister of a church or a member of a religious order not under a vow of poverty, I have informed the ordaining, commissioning, or licensing body of my church or order that I am conscientiously opposed to, or because of religious principles I am opposed to, the acceptance (for services I perform as a minister or as a member of a religious order) of any public insurance that makes payments in the event of death, disability, old age, or retirement; or that makes payments toward the cost of, or provides services for, medical care, including the benefits of any insurance system established by the Social Security Act.

I certify that I have never filed Form 2031 to revoke a previous exemption from social security coverage on earnings as a minister, member of a religious order not under a vow of poverty, or Christian Science practitioner.

I request to be exempted from paying self-employment tax on my earnings from services as a minister, member of a religious order not under a vow of poverty, or Christian Science practitioner, under section 1402(e) of the Internal Revenue Code. I understand that the exemption, if granted, will apply only to these earnings. Under penalties of perjury, I declare that I have examined this application and to the best of my knowledge and belief, it is true and correct.

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Example

- Joe is credentialed as a minister in 2022.
- He earns \$5,000 in 2023 and \$20,000 in 2024 from being a minister.
- He decides to file Form 4361 to gain exemption from self-employment tax.
- The Form 4361 is due by the due date of his 2024 Form 1040 either April 15, 2025 or October 15, 2025, if Joe extends his 2024 Form 1040.

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The Minister & Income

JAIL TIME ANYONE?

- Rev. Ellis took his pay out of the offering plate on Sundays.
- Rev. Clark had the church pay his personal expenses such as auto payments & credit cards.
- Bishop Jinwright failed to report honorariums, personal expenses and employer provided autos to name a few.
- Rev. Springer failed to report love gifts that he had received.

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What is Considered as Income?



Salary



Housing Allowance



Auto Allowance



Love Gifts



Retirement Plan Contribution



Health and Other Benefit Plans



***The above are examples of both taxable and nontaxable forms of income ***

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General Rule of Thumb

- Everything that benefits you and is provided by your employer is taxable until you find the specific authority in the Internal Revenue Code that says it is not taxable.

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Special Income Considerations Love Gifts – including Special Occasion, Birthday & Retirement

- Taxable from the church
 - Goes in Box 1 on Form W-2
 - Church cannot be conduit for members
 - Church must control amount
 - Can be cash or noncash gifts
- Nontaxable if from a relative or a close friend
- Key for non-taxation: detached and disinterested generosity



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Special Income Considerations Housing Allowance

- A housing allowance is a portion of your compensation that is not taxable to the extent it does not exceed certain limits.
- It may apply where the minister owns his/her home or where the minister lives in a parsonage and has out of pocket expenses.

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Housing Allowance Organizational Issues

- Must be designated by the employer/payer, i.e., the church **and**
- Must be designated in advance of being paid **and**
- Must be designated in writing

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Housing Allowance More Organizational Issues

- Is not reported as taxable wages in Box 1 of W-2
- The church should not ask for an accounting of the housing expenses. However, a church may pay utilities and expenses directly for parsonages owned by the church.
- Only pay to those properly classified as a minister and performing ministerial duties
- Is not paid to anyone who is having FICA/Medicare taxes withheld & matched

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Is the Housing Allowance Taxable?

- Federal Income Tax – The amount that can be excluded is not taxable. Excess housing is claimed as additional income on Form 1040.
- Self Employment Tax – the full amount is taxable on Schedule SE.



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Housing Allowance & Federal Income Tax



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- A housing allowance is not taxable to the extent it does not exceed the lowest of:
 - Amount designated by the church;
 - Amount spent on housing expenses; or
 - The fair rental value of the home as furnished plus utilities.

23

What Are Valid Housing Expenses?

- Mortgage payments
- Utilities
- Base rate of phone – not cell phone
- Furniture & decorating items
- Cleaning supplies and cleaning services
- Repairs & maintenance
- Payments on home equity loans in limited instances
- Insurance
- Taxes

Tax Tip: Keep receipts and bills to prove these expenses. If you are audited, documentation of the expenses will be required. This may take planning in the world of electronic payments.

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What is the Fair Rental Value?

- Fair rental value is the value your home can be rented for as it is fully furnished. There is no specific guidance on how to arrive at this number. The following are some suggestions:
 - Real estate agent
 - Online systems for real estate valuations and rentals
 - Local ads for other properties in your area
 - Rental companies for furniture
- Should be determined every 3 to 5 years

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Housing Calculation

Housing Allowance Designated	\$25,000
Housing Expenses	\$30,000
Fair Rental Value of the Home	\$20,000

The lowest value, \$20,000, is excluded from federal taxable income leaving an excess of \$5,000 to be included in included in federal taxable income.

The \$25,000 paid is included in self-employment income.

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Tax Return Disclosure

- Some tax software includes the calculation of the taxable portion of the housing allowance.
- If no calculation is included, the following statement may be included:

The taxpayer receives a housing allowance pursuant to IRC Section 107. To the extent allowed by law, the allowance is excluded from taxable income. Any excess housing allowance has been included in taxable income. The full amount of the housing allowance is included in self-employment income on Schedule SE.

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The Parsonage

- Church Responsibility – Determine the fair rental value of the parsonage considering all the factors provided by the church and inform the minister of the value.
- Minister Responsibility – Include the fair rental value of the parsonage on Schedule SE unless exempt from self-employment tax.

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Housing Allowance & The Child Tax Credits

- There are times that lowering taxable income using the housing allowance can lower the amount of child tax credit available. Tax estimates should be done to determine the most beneficial balancing of reducing income and claiming these credits. It is most common where a minister has several children and a potentially large child tax credit and/or has a larger housing allowance.

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Tax Free Fringe Benefits – What's Left

- Qualified retirement plans such as 403(b)
- Autos utilized for business or mileage reimbursements
- Life insurance not to exceed \$50,000 of coverage under a group plan
- Qualified tuition assistance plans
- Qualified dependent care plans
- Qualified tuition reduction plans
- Group Medical insurance
- Nondiscriminatory health benefits including HRAs & HSAs (but there are lots of rules)

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Business Expenses

- The following may be considered as business expenses:
 - Books & magazines for study
 - Mileage to & from hospitals, member calls, meetings, etc.
 - Office supplies
 - Conference fees
 - Continuing education
 - Travel
 - Cell phones with caution

Check with the church's
Accountable Reimbursement
Plan to see what expenses are
eligible for reimbursement.

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Auto Expenses Different Payments – Different Tax

- Flat Allowances are taxable
- Reimburse mileage (70 cents per mile for 2025)
 - If a properly documented, then mileage is not taxable
- Employer Provided Autos
 - Add to taxable income the value for the personal use in Box 1 on Form W-2 – if no accounting, then it is 100% personal

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Cell Phones & Data Plans

A church may reimburse an employee's cell phone and/or data plan if:

- It determines that the employee needs the phone to perform their job duties
- The provision is not considered a part of the compensation plan
- The church obtains some documentation to prove it is paying a reasonable amount

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Accountable Expense Reimbursement Plans The Best Option Left

- Accountable Reimbursement Plans
 - Expenses documented as to the exempt purposes
 - Date of expense
 - Purpose of expense
 - Within a reasonable time-frame; i.e.; 60 days of the expense
 - Cash advances are fully documented with excess cash returned.
 - Receipts required for:
 - All lodging
 - Any other expense of \$75 or more but especially meals

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Nonaccountable Expense Reimbursement Plans The Worst Option



- Any sort of plan that does not require an accounting, i.e., a flat allowance for expenses, or a plan that is not “timely” carried out

WARNING: This can be a discretionary spending fund set up by the church, if not properly handled.

- Example

- Pastor Bob receives \$100 each week for expenses but the church does not require documentation.
- How much is taxable to Pastor Bob? - All \$100

Warning: All nonaccountable expense reimbursements are added into Box 1 on Form W-2 & no deductions are allowed on personal tax return

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Will Out-of-Pocket Business Expenses Be Fully Deductible?



For SE Tax = YES!



For Federal Income Tax = No!

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Making Your Tax Payments (This is very important!)

- Federal income tax withholding through employer. Take the amount on Line (O) and divide it by the number of pay periods you have and request it be withheld as federal income tax withholding from your paychecks
- Estimated tax payments
 - By mail – use Form 1040-ES paper voucher to send a check into the IRS (Please do not do this – the IRS is not processing paper well!)
 - Electronically
 - EFTPS – eftps.gov/eftps/ (Best method!!)
 - Credit card/debit card/ACH – irs.gov/payments

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37

Resources

- IRS Publication 517 - <https://www.irs.gov/forms-pubs/about-publication-517>
- Church Law and Tax – join for full member benefits and access to many resources for you and your church – www.churchlawandtax.com
- The Church Network – join for great access to other ministers and administrators working in churches – www.thechurchnetwork.com
- ECFA Minister's Tax & Financial Guide – Free download at <https://www.ecfa.org/TaxBooks/Default.aspx>
- The CO+OP Ministry Conference – each year in February in Houston – February 24th, 2026 <https://www.co-opministryconference.org/>

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38

THANK
YOU

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Sommerville & Associates encourage you to obtain Elaine Sommerville's compensation book for this topic and more. Go to the ChurchLawAndTaxStore.com to order the recently updated 2nd edition of **Church Compensation: From Strategic Plan to Compliance** by Elaine Sommerville, CPA.

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39