COMMISSION ON ACCOUNTABILITY

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POSITION PAPER

By: Rabbi David Saperstein, Rabbi Julie Schonfeld, Nathan Diament, Steven Woolf, Members

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A. Should the parsonage allowance be limited to a single primary residence?
B. Should the exclusion be limited to a specific dollar amount?
C. Should the exclusion be limited to a narrower group of individuals?

SHORT ANSWERS

A. Yes, this is supported by the recent decision in the 11th Circuit.
B. No, it is neither necessary nor appropriate to limit the exclusion to a dollar amount.
C. The exclusion should be made available to qualified individuals who meet the statutory requirements of Section 107 with deference paid to good-faith determinations made by the religious denomination.

Background: The Internal Revenue Code has historically provided ministers with an exclusion from income for their housing allowance. The origin of the housing or parsonage allowance dates back to 1921. As originally enacted, it provided an exclusion from income for the "rental value of a dwelling house and appurtenances thereof furnished to a minister of the gospel as part of his compensation." In 1954, Congress amended the provision to permit a minister to designate a portion of compensation as a housing allowance and to exclude that amount from income to the extent that it is actually used to provide a home. Internal Revenue Code Section 107 (hereinafter referred

to as "Code Section") now provides that in the case of a minister of the gospel, gross income does not include the rental value of a home furnished to him as part of his compensation; or the rental allowance paid to him as part of his compensation, to the extent used by him to rent or provide a home.

In order to qualify for the rental or "parsonage allowance," the amount paid to a minister to rent a home must be designated by the employing religious institution as rental allowance pursuant to official action taken in advance as evidenced in an employment contract, budget, minutes, or some other appropriate organizational instrument. The most recent amendments to Code Section 107, adopted as part of the Clergy Housing Allowance Clarification Act of 2002, codifies the Internal Revenue Service interpretation that the housing allowance is limited to the fair rental value of a minister's housing. As noted in the Senate Finance Committee Minority Staff memo to Senator Grassley on Media-Based Ministries, (hereinafter "Minority Staff memo"), the value of the parsonage allowance is separate from the issue of who is a "minister" eligible for the exclusion.

Conclusion: The parsonage allowance should be limited to a single primary residence. It should not be limited to a specific dollar amount nor should it be limited to a narrower group of individuals. The IRS should provide some additional reporting requirements and education related to the housing exclusion. Deference should be given to the good-faith determinations of religious organizations in defining the term "minister."

1. The housing allowance should be limited to a single residence following the recent 11th Circuit Court decision. The language of the decision makes it clear that the provisions of Code Section 107(2), when read in context of the Supreme Court decision in *Commissioner. v. Schleir,* 515 U.S. 323 (1995), that income exclusions such as those in Code Section 107(2) should be narrowly construed, and as such should apply to only one home.

The 11th Circuit Court of Appeals in *Commissioner v Philip A. Driscoll* (February 8, 2012), reversed the U.S. Tax Court (Driscoll v. Commissioner, 135 T.C. 557 (2010)) which had held that the parsonage allowance exclusion of Code Section 107(2) applied to more than one home. The Eleventh Circuit held that the legislative history of Code Section 107(2) does not support a plural application of the term "home" but continuously refers to the term "home" or similar words in the singular. The decision of the Eleventh Circuit is reasonable and should be supported in further interpretations of Code Section 107(2) by the courts and the IRS. There is no need for further legislative action by Congress at this time. Indeed, legislation in this area could open up the possibilities for further amendments which could prove to be counterproductive for the tax treatment of the income exclusion.

2. There should not be a dollar limit to the housing exclusion.

It is neither necessary nor advisable to impose any dollar limitation on the housing exclusion. A statutory limit already applies to Code Section 107(2) as it is limited to the fair market rental value of the residence. The amount excludable from gross income is the lesser of (1) the amount actually used to provide a home; (2) the amount officially designated as a housing allowance; or (3) the fair rental value of the home, including furnishing, utilities, and appurtenances.

Imposition of a dollar cap would be arbitrary and inequitable. It is clear from the legislative history of Code Section 107(2), both during the debate over the 1954 code and the 2002 amendments, that the housing allowance originated from a Congressional concern that clergy received modest compensation and often served denominations in rural communities. However, the parsonage allowance has been an integral part of the compensation agreements of ministers, rabbis and other clergy members for almost 100 years. Any attempt to set dollar limitations would undermine long-standing compensation arrangements and would add needless complexity for many, with little chance of stopping abuses that might be occurring among the few.

The cost of housing varies greatly throughout the country and a geographically-variable cap would add needless complexity to the tax code and would be difficult to administer. The housing exclusion should be considered as part of an overall compensation package for qualified individuals, discussed in more detail below. Such compensation packages are also subject to overall reasonable limits under other provisions of the tax code and in many cases are set within the guidelines of, or reviewed by compensation committees or within the specific religious denomination. As noted in the Minority Staff memo, the co-sponsor of the Senate version of the 2002 legislation stated that "the vast majority of clergy across America work very hard for very modest pay…and ministers are very dependent upon their churches providing or paying for their housing." The memo further notes that parsonage allowances provided by churches with denominational or similar oversight do not attract the attention of the media or the public. There is no need for the imposition of arbitrary dollar limits on compensation.

3. The IRS should provide some additional reporting requirements and education related to the housing exclusion.

The Internal Revenue Service could play an educational and information-providing role that would foster additional compliance in the area of the housing allowance. The Internal Revenue Service already provides several helpful publications for organizations and individuals in this area including Publication 1828, *Tax Guide for Churches and Religious Organizations,* Publication 517, *Social Security and Other Information for Members of the Clergy and Religious Workers,* Tax Topic 417, *Earnings for Clergy,* and the *Minister Audit Technique Guide,* among others. This information should be broadly disseminated by religious denominations in order to help assure improved compliance with existing statutes, rules, and regulations.

We also agree that the Internal Revenue Service should require that religious denominations require reporting on Form W-2 or Form 1099 of the amount of the housing allowance provided to qualified members of the clergy. Further, the IRS should provide clear, user-friendly forms and worksheets and instructions to the appropriate tax forms and schedules (Form 1040, Form 1040, Schedule A, Form 2106, Form 1040,

Schedule C or Schedule C-EZ, and Form 1040, Schedule SE, among others) to help qualified clergy properly report the excluded housing allowance amount, any excess housing allowance, as well as the amount taxable for self-employment purposes.

4. Deference should be given to the good-faith determinations of religious organizations in defining the term "minister."

Deference should be given by the Internal Revenue Service and the Treasury Department to religious organizations to make their own good-faith determinations of who qualifies for the housing allowance. However, we further believe that the existing Treasury regulations, as interpreted by judicial decisions for over 40 years provide sufficient guidance in this area. For example, Treasury Regulation section 1.107-1(a) incorporates the rules of Treasury Regulation section 1.1402(c)-5 in determining who is performing the duties of a "minister of the gospel." It requires that an individual be a "duly ordained, commissioned, or licensed minister of a church." The Tax Court has interpreted this phrase to be disjunctive, finding the purpose is not to limit benefits to the ordained, but is to prevent self appointed ministers from benefiting. *Salkov v. Commissioner*, 46 T.C. 190, 197 (1966) holding that a Jewish cantor was a minister eligible for the Code section 107 housing allowance because he was commissioned by, and was a duly qualified member of the Cantors Assembly of America, which functions as the official cantorial body for the Conservative branch of the Jewish religion in America, and because he was selected by a representative Conservative congregation to perform the functions of cantor. We also note parenthetically that the "ministerial exception" that was the subject of the recent Supreme Court decision in *Hosanna-Tabor Evangelical Lutheran Church and School v. Equal Employment Opportunity Commission, et al.*, (Case No. 10-553, January 11, 2012), is far broader than the narrow class of employees who qualify as ministers for tax purposes. Tax purposes ministers should be a subset of those who fall within the broader ministerial exception which was crafted in order to expand the flexibility of religious organizations to make critical personnel decisions.

Treasury Regulation section 1.1402(c)-5(b)(2) states that services performed by a minister in the exercise of the ministry includes:(1) ministration of sacerdotal functions; (2) conduct of religious worship; (3) control, conduct, and maintenance of religious organizations (including the religious boards, societies, and other integral agencies of such organizations), under the authority of a religious body constituting a church or denomination and that whether service performed by a minister constitutes conduct of religious worship or ministration of sacerdotal functions depends on the tenets and practices of the particular religious body constituting the church or denomination. Treasury Regulation section 1.107-1(a) also provides examples of specific services considered duties of a minister, including performance of sacerdotal functions, conduct of religious worship, administration and maintenance of religious organizations and their integral agencies, and performance of teaching and administrative duties at theological seminaries.