

# Publication 1828

## Tax Guide for Churches & Religious Organizations

501(c)(3)

Volume 2 of 2



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# **Business Activity**

The question of whether an activity constitutes participation or intervention in a political campaign may also arise in the context of a business activity of the church or religious organization, such as the selling or renting of mailing lists, the leasing of office space or the acceptance of paid political advertising. (The tax treatment of income from unrelated business activities follows.) In this context, some of the factors to be considered in determining whether the church or religious organization has engaged in prohibited political campaign activity include:

- whether the good, service or facility is available to the candidates equally;
- whether the good, service or facility is available only to candidates and not to the general public;

- whether the fees charged are at the organization's customary and usual rates; and
- whether the activity is an ongoing activity of the organization or is conducted only for the candidate.

## **EXAMPLE 1**

Church K is a Section 501(c)(3) organization. It owns a building that has a large basement hall suitable for hosting dinners and receptions. For several years, Church K has made the hall available for rent to the public. It has standard fees for renting the hall based on the number of people in attendance. A number of different organizations have rented the hall. Church K rents the hall on a first come, first served basis. Candidate P's campaign pays the standard fee for the dinner. Church K isn't involved in political campaign intervention as a result of renting

the hall to Candidate P for use as the site of a campaign fundraising dinner.

## **EXAMPLE 2**

Church L is a Section 501(c)(3) organization. It maintains a mailing list of all its members. Church L has never rented the mailing list to a third party. The campaign committee of Candidate A, who supports funding for faith-based programs, approaches Church L and offers to rent Church L's mailing list for a fee that is comparable to fees charged by similar organizations. Church L rents the list to Candidate A's campaign committee, but declines similar requests from campaign committees of other candidates. Church L has intervened in a political campaign.

**Websites.** The Internet has become a widely used communications tool. Section 501(c)(3) organizations use their own websites to disseminate statements and information. They also routinely link their websites to

websites maintained by other organizations as a way of providing additional information that the organizations believe is relevant to the public.

A website is a form of communication. If an organization posts something on its website that favors or opposes a candidate for public office, the organization will be treated the same as if it distributed printed material, oral statements or broadcasts that favored or opposed a candidate.

An organization has control over whether it establishes a link to another site. When an organization establishes a link to another website, the organization is responsible for the consequences of establishing and maintaining that link, even if the organization doesn't have control over the content of the linked site. Because the linked content may change over time, an organization may reduce the risk of political campaign

intervention by monitoring the linked content and adjusting the links accordingly.

Links to candidate-related material, by themselves, do not necessarily constitute political campaign intervention. All the facts and circumstances must be taken into account when assessing whether a link produces that result. The facts and circumstances to be considered include, but are not limited to, the context for the link on the organization's website, whether all candidates are represented, any exempt purpose served by offering the link and the directness of the links between the organization's website and the Web page that contains material favoring or opposing a candidate for public office.

## **EXAMPLE 1**

Church P, a Section 501(c)(3) organization, maintains a website that includes biographies of its ministers, times of services, details of

community outreach programs and activities of members of its congregation. B, a member of Church P's congregation, is running for a seat on the town council. Shortly before the election, Church P posts the following message on its website, "Lend your support to B, your fellow parishioner, in Tuesday's election for town council." Church P has intervened in a political campaign.

## **EXAMPLE 2**

Church N, a Section 501(c)(3) organization, maintains a website that includes staff listings, directions to the church and descriptions of its community outreach programs, schedules of services and school activities. On one page of the website, Church N describes a particular type of treatment program for homeless veterans. This section includes a link to an article on the website of O, a major national newspaper, praising Church N's treatment program for homeless veterans. The page containing the article on



O's website doesn't refer to any candidate or election and has no direct links to candidate or election information. Elsewhere on O's website, there is a page displaying editorials that O has published. Several of the editorials endorse candidates in an election that hasn't yet occurred. Church N has not intervened in a political campaign by maintaining a link on O's website because the link is provided for the exempt purpose of educating the public about its programs; the context for the link, the relationship between Church N and O and the arrangement of the links going from Church N's website to the endorsement on O's website don't indicate that Church N was favoring or opposing any candidate.

### **EXAMPLE 3**

Church M, a Section 501(c)(3) organization, maintains a website and posts an unbiased, nonpartisan voter guide. For each candidate covered in the voter guide, Church M includes a link to that candidate's official campaign

website. The links to the candidate websites are presented on a consistent neutral basis for each candidate, with text saying “For more information on Candidate X, you may consult [URL].” Church M has not intervened in a political campaign because the links are provided for the exempt purpose of educating voters and are presented in a neutral, unbiased manner that includes all candidates for a particular office.

## **Consequences of Political Campaign Activity**

When it participates in political campaign activity, a church or religious organization jeopardizes both its tax-exempt status under IRC Section 501(c)(3) and its eligibility to receive tax-deductible contributions. In addition, it may become subject to an excise tax on its political expenditures. This excise tax may be imposed in addition to revocation, or it may be imposed instead of revocation.

Also, the church or religious organization should correct the violation.

***Excise tax.*** An initial tax is imposed on an organization at the rate of 10 percent of the political expenditures. Also, a tax at the rate of 2.5 percent of the expenditures is imposed against the organization managers (jointly and severally) who, without reasonable cause, agreed to the expenditures knowing they were political expenditures. The tax on management may not exceed \$5,000 with respect to any one

expenditure. In any case in which an initial tax is imposed against an organization, and the expenditures are not corrected within the period allowed by law, an additional tax equal to 100 percent of the expenditures is imposed against the organization. In that case, an additional tax is also imposed against the organization managers (jointly and severally) who refused to agree to make the correction. The additional tax on management is equal to

50 percent of the expenditures and may not exceed \$10,000 with respect to any one expenditure.

***Correction.*** Correction of a political expenditure requires the recovery of the expenditure, to the extent possible, and establishment of safeguards to prevent future political expenditures.

Please note that a church or religious organization that engages in any political campaign activity also needs to determine whether it complies with the appropriate federal, state or local election laws, as these may differ from the requirements under IRC Section 501(c)(3).

# **Unrelated Business Income Tax (UBIT)**

## **Net Income Subject to the UBIT**

Churches and religious organizations, like other tax-exempt organizations, may engage in income-producing activities unrelated to their tax-exempt purposes, as long as the unrelated activities aren't a substantial part of the organization's activities. However, the net income from these activities will be subject to the UBIT if the following three conditions are met:

- the activity constitutes a trade or business,
- the trade or business is regularly carried on, and
- the trade or business is not substantially related to the organization's exempt purpose. (The fact that the organization uses the

income to further its charitable or religious purposes does not make the activity substantially related to its exempt purposes.)

## **Exceptions to UBIT**

Even if an activity meets the above criteria, the income may not be subject to tax if it meets one of the following exceptions: (a) substantially all the work in operating the trade or business is performed by volunteers, (b) the activity is conducted by the organization primarily for the convenience of its members or (c) the trade or business involves the selling of merchandise substantially all of which was donated.

In general, rents from real property, royalties, capital gains, and interest and dividends aren't subject to the unrelated business income tax unless financed with borrowed money.

# **Examples of Unrelated Trade or Business Activities**

Unrelated trade or business activities vary depending on types of activities.

## **Advertising**

Many tax-exempt organizations sell advertising in their publications or other forms of public communication. Generally, income from the sale of advertising is unrelated trade or business income. This may include the sale of advertising space in weekly bulletins, magazines or journals, or on church or religious organization websites.

## **Gaming**

Most forms of gaming, if regularly carried on, may be considered the conduct of an unrelated trade or business. This can include the sale of pull-tabs and raffles. Income derived from bingo games may be eligible for a special tax exception (in addition to the

exception regarding uncompensated volunteer labor), if: (a) the bingo game is the traditional type of bingo (as opposed to instant bingo, a variation of pull-tabs), (b) the conduct of the bingo game is not an activity carried out by for-profit organizations in the local area and (c) the operation of the bingo game does not violate any state or local law.

## **Sale of merchandise and publications**

The sale of merchandise and publications (including the actual publication of materials) can be considered the conduct of an unrelated trade or business if the items involved do not have a substantial relationship to the exempt purposes of the organization.

## **Rental income**

Generally, income derived from the rental of real property and incidental personal property is excluded from unrelated business income. However, there are certain situations in which



rental income may be unrelated business taxable income:

- if a church rents out property on which there is debt outstanding (for example, a mortgage note), the rental income may constitute unrelated debt-financed income subject to UBIT. (However, if a church or convention or association of churches acquires debt-financed land and intends to use it for exempt purposes within 15 years of the time of acquisition, then income from the rental of the land may not constitute unrelated business income.)
- if personal services are rendered in connection with the rental, then the income may be unrelated business taxable income.

## **Parking lots**

If a church owns a parking lot that is used by church members and visitors while attending

church services, any parking fee paid to the church would not be subject to UBIT.

However, if a church operates a parking lot that is used by members of the general public, parking fees would be taxable, as this activity would not be substantially related to the church's exempt purpose, and parking fees are not treated as rent from real property. If the church enters into a lease with a third party who operates the church's parking lot and pays rent to the church, these payments would not be subject to tax, as they would constitute rent from real property.

Whether an income-producing activity is an unrelated trade or business activity depends on all the facts and circumstances. For more information, see IRS [Publication 598](#), *Tax on Unrelated Business Income of Exempt Organizations*.

# **Tax on Income-Producing Activities**

If a church, or other exempt organization, has gross income of \$1,000 or more for any taxable year from the conduct of any unrelated trade or business, it must file IRS Form 990-T, Exempt Organization Business Income Tax Return, for that year.

If the church is part of a larger entity (such as a diocese), it must file a separate Form 990-T if it has a separate EIN. Form 990-T is due the 15th day of the 5th month following the end of the church's tax year. (IRC Section 512(b)(12) provides a special rule for parishes and similar local units of a church. A specific deduction is provided, which is equal to the lower of \$1,000 or the gross income derived from any unrelated trade or business regularly carried on by the parish or local unit of a church.) See Filing Requirements.

# Employment Tax

Generally, churches and religious organizations are required to withhold, report and pay income and Federal Insurance Contributions Act (FICA) taxes for their employees. Employment tax includes income tax and FICA taxes withheld and paid for an employee. Substantial penalties may be imposed against an organization that fails to withhold and pay the proper employment tax. Whether a church or religious organization must withhold and pay employment tax depends upon whether the church's workers are employees. Determination of worker status is important. Several facts determine whether a worker is an employee. For an in-depth explanation and examples of the common law employer-employee relationship, see IRS [Publication 15-A](#), *Employer's Supplemental Tax Guide*. If a church or a worker wants the IRS to determine whether the worker is an employee, the church or

worker should file IRS Form SS-8, *Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding*, with the IRS.

## **Social Security and Medicare Taxes — Federal Insurance Contributions Act (FICA)**

FICA taxes consist of Social Security and Medicare taxes. Wages paid to employees of churches or religious organizations are subject to FICA taxes unless one of the following applies:

- wages are paid for services performed by a duly ordained, commissioned or licensed minister of a church in the exercise of his or her ministry, or by a member of a religious order in the exercise of duties required by such order; or

- a church that is opposed to the payment of Social Security and Medicare taxes for religious reasons files IRS [Form 8274](#), *Certification by Churches and Qualified Church-Controlled Organizations Electing Exemption From Employer Social Security and Medicare Taxes*. Very specific timing rules apply to filing Form 8274. It must be filed before the first date on which the electing entity is required to file its first quarterly employment tax return. This election does not relieve the organization of its obligation to withhold income tax on wages paid to its employees. In addition, if an employee makes such an election and earns more than \$108.28 in wages in a calendar year, he or she must pay Self-Employment Contributions Act (SECA) tax. For more information, see [Publication 517](#), *Social Security and Other Information*

*for Members of the Clergy and Religious Workers.*

Withheld employee income tax and FICA taxes are reported on IRS [Form 941](#), *Employer's Quarterly Federal Tax Return*. Some small employers are eligible to file an annual Form 944 instead of quarterly returns. For more information about employment tax, see;

- [Publication 15](#), *Circular E, Employer's Tax Guide*
- [Publication 15-A](#), *Employer's Supplemental Tax Guide*
- [Publication 517](#), *Social Security and Other Information for Members of the Clergy and Religious Workers*
- [Form 944 Instructions](#)

# **Federal Unemployment Tax Act (FUTA)**

Churches and religious organizations are not liable for FUTA tax. For further information on FUTA, see IRS Publication 15, *Circular E, Employer's Tax Guide*, IRS Publication 15-A, *Employer's Supplemental Tax Guide*, and IRS Publication 517, *Social Security and Other Information for Members of the Clergy and Religious Workers*.



# **Special Rules for Compensation of Ministers**

## **Withholding Income Tax for Ministers**

Unlike other exempt organizations or businesses, a church isn't required to withhold income tax from the compensation it pays to its duly ordained, commissioned or licensed ministers for performing services in the exercise of their ministry. An employee minister may, however, enter into a voluntary withholding agreement with the church by completing IRS [Form W-4, Employee's Withholding Allowance Certificate](#). A church should report compensation paid to a minister on [Form W-2, Wage and Tax Statement](#), if the minister is an employee, or on IRS [Form 1099-MISC, Miscellaneous Income](#), if the minister is an independent contractor.

## **Parsonage or Housing Allowances**

Generally, a minister's gross income does not include the fair rental value of a home (parsonage) provided, or a housing allowance paid, as part of the minister's compensation for services performed that are ordinarily the duties of a minister.

A minister who is furnished a parsonage may exclude from income the fair rental value of the parsonage, including utilities. However, the amount excluded can't be more than the reasonable pay for the minister's services.

A minister who receives a housing allowance may exclude the allowance from gross income to the extent it's used to pay expenses in providing a home. Generally, those expenses include rent, mortgage payments, utilities, repairs and other expenses directly relating to providing a home. If a minister owns a home, the amount excluded from the minister's gross income as a housing allowance is

limited to the least of: (a) the amount actually used to provide a home, (b) the amount officially designated as a housing allowance or (c) the fair rental value of the home. The minister's church or other qualified organization must designate the housing allowance by official action taken *in advance* of the payment. If a minister is employed and paid by a local congregation, a designation by a national church agency won't be effective. The local congregation must make the designation. A national church agency may make an effective designation for ministers it directly employs. If none of the minister's salary has been officially designated as a housing allowance, the full salary must be included in gross income.

The fair rental value of a parsonage or housing allowance is excludable from income only for income tax purposes. These amounts are *not* excluded in determining the minister's net earnings from self-employment for Self-

Employment Contributions Act (SECA) tax purposes. Retired ministers who receive either a parsonage or housing allowance aren't required to include the amounts for SECA tax purposes.

As mentioned above, a minister who receives a parsonage or rental allowance excludes that amount from his income. The portion of expenses allocable to the excludable amount is not deductible. This limitation, however, does not apply to interest on a home mortgage or real estate taxes, nor to the calculation of net earnings from self-employment for SECA tax purposes.

IRS Publication 517, *Social Security and Other Information for Members of the Clergy and Religious Workers*, has a detailed example of the tax treatment for a housing allowance and the related limitations on deductions. IRS [Publication 525](#), *Taxable and Nontaxable Income*, has information on particular types of income for ministers.

# **Social Security and Medicare Taxes — Federal Insurance Contributions Act (FICA) vs. Self-Employment Contributions Act (SECA)**

The compensation that a church or religious organization pays to its ministers for performing services in the exercise of ministry is not subject to FICA taxes. However, income that a minister earns in performing services in the exercise of his ministry is subject to SECA tax, unless the minister has timely applied for and received an exemption from SECA tax.

# **Payment of Employee Business Expenses**

A church or religious organization is treated like any other employer as far as the tax rules on employee business expenses. The rules differ depending upon whether the expenses are paid through an accountable or non-accountable plan, and these plans determine whether the payment for these expenses is included in the employee's income.

## **Accountable Reimbursement Plan**

An arrangement that an employer establishes to reimburse or advance employee business expenses will be an accountable plan if it: (1) involves a business connection, (2) requires the employee to substantiate expenses incurred and (3) requires the employee to return any excess amounts.

Employees must provide the organization with sufficient information to identify the specific

business nature of each expense and to substantiate each element of an expenditure. It isn't sufficient for an employee to aggregate expenses into broad categories such as travel or to report expenses through the use of non-descriptive terms such as miscellaneous business expenses. Both the substantiation and the return of excess amounts must occur within a reasonable time.

Employee business expenses reimbursed under an accountable plan are: (a) excluded from an employee's gross income, (b) not required to be reported on the employee's IRS Form W-2, *Wage and Tax Statement*, and (c) exempt from the withholding and payment of wages subject to FICA taxes and income tax withholdings.

## **Non-accountable Reimbursement Plan**

If the church or religious organization reimburses or advances the employee for business expenses, but the arrangement does not satisfy the three requirements of an accountable plan, the amounts paid to the employees are considered wages subject to FICA taxes and income tax withholding, if applicable, and are reportable on Form W-2. (Amounts paid to employee ministers are treated as wages reportable on Form W-2, but are not subject to FICA taxes or income tax withholding.)

For example, if a church or religious organization pays its secretary a \$200 per month allowance to reimburse monthly business expenses the secretary incurs while conducting church or religious organization business, and the secretary is not required to substantiate the expenses or return any excess, then the entire \$200 must be



reported on Form W-2 as wages subject to FICA taxes and income tax withholding. In the same situation involving an employee-minister, the allowance must be reported on the minister's Form W-2, but no FICA or income tax withholding is required. For further information see IRS [Publication 463, Travel, Entertainment, Gift, and Car Expenses](#).

One common business expense reimbursement is for automobile mileage. If a church or religious organization pays a mileage allowance at a rate that is less than or equal to the federal standard rate, the amount of the expense is deemed substantiated. (Each year, the federal government establishes a standard mileage reimbursement rate.) There are no income or employment tax consequences to the reimbursed individual provided that the employee substantiates the time, place and business purposes of the automobile mileage

for which reimbursement is sought. Of course, reimbursement for automobile mileage incurred for personal purposes is includible in the individual's income.

If a church or religious organization reimburses automobile mileage at a rate exceeding the standard mileage rate, the excess is treated as paid under a non-accountable plan. This means that the excess is includible in the individual's income and is subject to the withholding and payment of income and employment taxes, if applicable.

In addition, any mileage reimbursement that is paid without requiring the individual to substantiate the time, place and business purposes of each trip is included in the individual's income, regardless of the rate of reimbursement.

No income is attributed to an employee or a volunteer who uses an automobile owned by the church or religious organization to perform church-related work.

# **Recordkeeping Requirements**

## **Books of Accounting and Other Types of Records**

All tax-exempt organizations, including churches and religious organizations (regardless of whether tax-exempt status has been officially recognized by the IRS), are required to maintain books of accounting and other records necessary to justify their claim for exemption in the event of an audit. See [Special Rules Limiting IRS Authority to Audit a Church](#). Tax-exempt organizations are also required to maintain books and records that are necessary to accurately file any federal tax and information returns that may be required.

There is no specific format for keeping records. However, the types of required records frequently include organizing documents (charter, constitution, articles of incorporation) and bylaws, minute books,

property records, general ledgers, receipts and disbursements journals, payroll records, banking records and invoices. The extent of the records necessary generally varies according to the type, size and complexity of the organization's activities.

## **Length of Time to Retain Records**

The law does not specify a length of time that records must be retained; however, the following guidelines should be applied in the event that the records may be material to the administration of any federal tax law.

**TYPE OF RECORD****LENGTH OF TIME TO  
RETAIN**

Records of revenue and expenses, including payroll records.

Retain for at least four years after filing the returns to which they relate.

Records relating to acquisition and disposition of property (real and personal, including investments).

Retain for at least four years after the filing of the return for the year in which disposition occurs.

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Filing Requirements

Information and Tax Returns — Forms to File and Due Dates

Churches or religious organizations may be required to report certain payments or information to the IRS. The following is a list of the most frequently required returns, who should use them, how they are used and when they should be filed.

Forms	Who Should Use Them	How They are Used	When to File
<b>Form W-2</b> <i>Wage and Tax Statement</i> <b>Form W-3</b> <i>Transmittal of Wage and Tax Statement</i>	Organizations with employees.	Use Form W-2 to report employee wages and the taxes withheld from them. Use Form W-3 to transmit Forms W-2 to the Social Security Administration.	Furnish each employee with a completed Form W-2 by January 31; and file all Forms W-2 and Form W-3 with the Social Security Administration (SSA) by the last day of February.
<b>Form W-2G</b> <i>Certain Gaming Winnings</i> For more information on reporting requirements for gaming activities, see IRS <a href="#">Publication 3079, Tax-Exempt Organizations and Gaming</a> .	Any charitable or religious organization, including a church, that sponsors a gaming event (raffles, bingo) must file Form W-2G when a participant wins a prize over a specific value amount.	The requirements for reporting and withholding depend on the type of gaming, the amount of winnings and the ratio of winnings to the wager.	For each winner meeting the filing requirement, the church or religious organization must furnish Form W-2G by January 31; and file Copy A of Form W-2G with the IRS by February 28.
<b>Form 941</b> <i>Employer’s Quarterly Federal Tax Return</i> or <b>Form 944</b> <i>Employer’s Annual Federal Tax Return</i>	Small employers that have been notified by the IRS to file Form 944 (see form instructions) may use that form; other employers required to file must use Form 941.	Use Form 941 or 944 to report Social Security and Medicare taxes and income taxes withheld by the organization, and Social Security and Medicare taxes paid by the organization.	See form instructions for due dates.
<b>Form 945</b> <i>Annual Return of Withheld Federal Income Tax</i>		If a church or religious organization withholds income tax, including backup withholding, from non-payroll payments, it must file Form 945.	File Form 945 by January 31. This form is not required for those years in which there is no non-payroll tax liability.
<b>Form 990</b> <i>Return of Organization Exempt From Income Tax</i> <b>Form 990-EZ</b> <i>Short Form Return of Organization Exempt From Income Tax</i> <b>Form 990-N (e-Postcard)</b> <i>Electronic Notice for Tax-Exempt Organizations Not Required to File Form 990 or 990-EZ</i>	Generally, all religious organizations (see exceptions to file Form 990 below) must file Form 990, Form 990-EZ or Form 990-N.  <div>Exceptions to file Form 990, 990-EZ and 990-N</div> <p>The following is a list of some of the organizations that are not required to file Form 990, 990-EZ, or 990-N.</p> <ul style="list-style-type: none"><li>■ Churches (as opposed to “religious organizations,” defined earlier)</li><li>■ Inter-church organizations of local units of a church</li><li>■ Mission societies sponsored by or affiliated with one or more churches or church denomination, if more than half of the activities are conducted in, or directed at, persons in foreign countries</li><li>■ An exclusively religious activity of any religious order</li></ul> <p>See the form instructions for a list of other organizations that are not required to file.</p>	The thresholds for determining which form to file, Form 990, 990-EZ or 990-N are found at <a href="http://www.irs.gov/charities">www.irs.gov/charities</a> .	Form 990, 990-EZ or 990-N must be filed on or before the 15th day of the 5th month following the end of the organization’s tax year.  For 990-N must be electronically filed.

Forms	Who Should Use Them	How They are Used	When to File
<b>Form 990-T</b> <i>Exempt Organization Business Income Tax Return</i> For more information on unrelated business income, see <a href="#">Unrelated Business Income Tax (UBIT)</a> .	Churches and religious organizations.	Churches and religious organizations must file Form 990-T if they generate gross income from an unrelated business of \$1,000 or more for a taxable year.	Form 990-T must be filed by the 15th day of the 5th month after the organization's accounting period ends (May 15 for a calendar year accounting period).
<b>Form 990-W</b> <i>Estimated Tax on Unrelated Business Taxable Income for Tax-Exempt Organizations</i>	Churches and religious organizations.	If the tax on unrelated business income is expected to be \$500 or more, the church or religious organization must make estimated tax payments.  Use Form 990-W to compute the estimated tax liability.	Form 990-W is for computation purposes only and does not need to be filed.
<b>Form 1096</b> <i>Annual Summary and Transmittal of U.S. Information Returns</i>	Churches and religious organizations.	Use Form 1096 to transmit Forms 1099-MISC, W-2G and certain other forms to the IRS.	Form 1096 must be filed by February 28 in the year following the calendar year in which the payments were made.
<b>Form 1099-MISC</b> <i>Miscellaneous Income</i> See the <i>Instructions for Form 1099-MISC</i> for details.	Churches and religious organizations.	A church or religious organization must use Form 1099-MISC if it pays an unincorporated individual or an entity \$600 or more in any calendar year for gross rents; commissions, fees or other compensation paid to non-employees; prizes and awards; or other fixed and determinable income.	Churches or religious organizations must furnish each payee with a copy of Form 1099-MISC by January 31; and file Copy A of Form 1099-MISC with the IRS by February 28.
<b>Form 5578</b> <i>Annual Certification of Racial Nondiscrimination for a Private School Exempt from Federal Income Tax</i> For information on racial and ethnic nondiscriminatory policies, see Revenue Procedure 75-50, 1975-2 C.B. 587 at <a href="http://www.irs.gov">www.irs.gov</a> .	A church or religious organization that operates a private school, whether separately incorporated or operated as part of its overall operations, that teaches secular subjects and generally complies with state law requirements for public education.  <hr/> <b>Note:</b> It is not considered racially discriminatory for a parochial school to select students on the basis of membership in a religious denomination if membership in the denomination is open to all on a racially nondiscriminatory basis. Further, a seminary, or other purely religious school, that primarily teaches religious subjects usually with the purpose of training students for the ministry, is not subject to the racially nondiscriminatory requirements because it is considered to be a religious rather than an educational organization.	File Form 5578 to certify that the school does not discriminate based on race or ethnic origin.	Form 5578 must be filed on or before the 15th day of the 5th month following the end of the organization's taxable year (May 15 for a calendar year).  If an organization files Form 990 or Form 990-EZ, the certification must be made on Schedule A (Form 990 or Form 990-EZ).
<b>Form 8282</b> <i>Donee Information Return</i>	Churches and religious organizations.	A church or religious organization must file Form 8282 if it sells, exchanges, transfers or otherwise disposes of certain non-cash donated property within three years of the date it originally received the donation. This applies to non-cash property that had an appraised value of more than \$5,000 at time of donation.	The church or religious organization must file Form 8282 with the IRS within 125 days of date of disposition of the property; and furnish the original donor with a copy of the form.
<b>Treasury Form 90.22.1,</b> <i>Report of Foreign Bank and Financial Accounts</i>	See form instructions	See form instructions	See form instructions



# **Charitable Contributions— Substantiation and Disclosure Rules**

## **Recordkeeping**

A church or religious organization should be aware of the recordkeeping and substantiation rules imposed on donors of charities that receive certain quid pro quo contributions.

## **Recordkeeping Rules**

A donor cannot claim a tax deduction for any contribution of cash, a check or other monetary gift made on or after January 1, 2007, unless the donor maintains a record of the contribution in the form of either a bank record (such as a cancelled check) or a written communication from the charity (such as a receipt or a letter) showing the name of

the charity, the date of the contribution and the amount of the contribution.

## **Substantiation Rules**

A donor can't claim a tax deduction for any single contribution of \$250 or more unless the donor obtains a contemporaneous, written acknowledgment of the contribution from the recipient church or religious organization. A church or religious organization that doesn't acknowledge a contribution incurs no penalty; but without a written acknowledgment, the donor can't claim a tax deduction. Although it's a donor's responsibility to obtain a written acknowledgment, a church or religious organization can assist the donor by providing a timely, written statement containing:

- name of the church or religious organization, , date of the contribution,
- amount of any cash contribution, and

- description (but not the value) of non-cash contributions.

In addition, the timely, written statement must contain one of the following:

- statement that no goods or services were provided by the church or religious organization in return for the contribution,
- statement that goods or services that a church or religious organization provided in return for the contribution consisted entirely of intangible religious benefits, or
- description and good-faith estimate of the value of goods or services other than intangible religious benefits that the church or religious organization provided in return for the contribution.

The church or religious organization may either provide separate acknowledgments for each single contribution of \$250 or more or

one acknowledgment to substantiate several single contributions of \$250 or more.

Separate contributions aren't aggregated for purposes of measuring the \$250 threshold.

## **Disclosure Rules that Apply to Quid Pro Quo Contributions**

A contribution made by a donor in exchange for goods or services is known as a quid pro quo contribution. A donor may only take a contribution deduction to the extent that his or her contribution exceeds the fair market value of the goods and services the donor receives in return for the contribution.

Therefore, donors need to know the value of the goods or services. A church or religious organization must provide a written statement to a donor who makes a payment exceeding \$75 partly as a contribution and partly for goods and services provided by the organization.

## **EXAMPLE 1**

If a donor gives a church a payment of \$100 and, in return, receives a ticket to an event valued at \$40, this is a contribution, and only \$60 is deductible by the donor ( $\$100 - \$40 = \$60$ ). Even though the deductible amount does not exceed \$75, since the contribution the church received is in excess of \$75, the church must provide the donor with a written disclosure statement. The statement must: (1) inform the donor that the amount of the contribution that is deductible for federal income tax purposes is limited to the excess of money (and the fair market value of any property other than money) contributed by the donor over the value of goods or services provided by the church or religious organization; and (2) provide the donor with a good-faith estimate of the value of the goods or services.

The church or religious organization must provide the written disclosure statement with

either the solicitation or the receipt of the contribution and in a manner that is likely to come to the attention of the donor. For example, a disclosure in small print within a larger document may not meet this requirement.

## **Exceptions to Disclosure Statement**

A church or religious organization isn't required to provide a disclosure statement for quid pro quo contributions when: (a) the goods or services meet the standards for insubstantial value or (b) the only benefit received by the donor is an intangible religious benefit. Additionally, if the goods or services the church or religious organization provides are intangible religious benefits (examples follow), the acknowledgment for contributions of \$250 or more doesn't need to describe those benefits.

Generally, intangible religious benefits are benefits provided by a church or religious organization that are not usually sold in commercial transactions outside a donative (gift) context.

- Intangible religious benefits include:
  - admission to a religious ceremony
- de minimis tangible benefits, such as wine used in religious ceremony

**Benefits that are not intangible religious benefits include:**

- tuition for education leading to a recognized degree
- travel services
- consumer goods

IRS [Publication 1771](#), *Charitable Contributions: Substantiation and Disclosure Requirements*, provides more information on substantiation and disclosure rules.

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# **Special Rules Limiting IRS Authority to Audit a Church**

## **Tax Inquiries and Examinations of Churches**

Congress has imposed special limitations, found in IRC Section 7611, on how and when the IRS may conduct civil tax inquiries and examinations of churches. The IRS may only initiate a church tax inquiry if an appropriate high-level Treasury Department official reasonably believes, based on a written statement of the facts and circumstances, that the organization: (a) may not qualify for the exemption or (b) may not be paying tax on an unrelated business or other taxable activity.

## **Restrictions on Church Inquiries and Examinations**

Restrictions on church inquiries and examinations apply only to churches

(including organizations claiming to be churches if such status has not been recognized by the IRS) and conventions or associations of churches. They don't apply to related persons or organizations. Thus, for example, the rules don't apply to schools that, although operated by a church, are organized as separate legal entities. Similarly, the rules don't apply to integrated auxiliaries of a church.

Restrictions on church inquiries and examinations do not apply to all church inquiries by the IRS. The most common exception relates to routine requests for information. For example, IRS requests for information from churches about filing of returns, compliance with income or Social Security and Medicare tax withholding requirements, supplemental information needed to process returns or applications and other similar inquiries are not covered by the special church audit rules.

Restrictions on church inquiries and examinations don't apply to criminal investigations or to investigations of the tax liability of any person connected with the church, such as a contributor or minister.

The procedures of IRC Section 7611 will be used in initiating and conducting any inquiry or examination into whether an excess benefit transaction (as that term is used in IRC Section 4958) has occurred between a church and an insider.

## **Audit Process**

The sequence of the audit process is:

1. If the reasonable belief requirement is met, the IRS must begin an inquiry by providing a church with written notice containing an explanation of its concerns.
2. The church is allowed a reasonable period in which to respond by

furnishing a written explanation to alleviate IRS concerns.

3. If the church fails to respond within the required time, or if its response is not sufficient to alleviate IRS concerns, the IRS may, generally within 90 days, issue a second notice, informing the church of the need to examine its books and records.
4. After issuance of a second notice, but before commencement of an examination of its books and records, the church may request a conference with an IRS official to discuss IRS concerns. The second notice will contain a copy of all documents collected or prepared by the IRS for use in the examination and subject to disclosure under the Freedom of Information Act, as supplemented by IRC Section 6103 relating to disclosure

and confidentiality of tax return information.

5. Generally, examination of a church's books and records must be completed within two years from the date of the second notice from the IRS.

If at any time during the inquiry process the church supplies information sufficient to alleviate the concerns of the IRS, the matter will be closed without examination of the church's books and records. There are additional safeguards for the protection of churches under IRC Section 7611. For example, the IRS can't begin a subsequent examination of a church for a five-year period unless the previous examination resulted in a revocation, notice of deficiency or assessment or a request for a significant change in church operations, including a significant change in accounting practices.

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# Glossary

***Church.*** Certain characteristics are generally attributed to churches. These attributes of a church have been developed by the IRS and by court decisions. They include:

- distinct legal existence;
- recognized creed and form of worship;
- definite and distinct ecclesiastical government;
- formal code of doctrine and discipline;
- distinct religious history;
- membership not associated with any other church or denomination;
- organization of ordained ministers;
- ordained ministers selected after completing prescribed courses of study;

- literature of its own; , established places of worship;
- regular congregations;
- regular religious services;
- Sunday schools for the religious instruction of the young; and
- schools for the preparation of its ministers.

The IRS generally uses a combination of these characteristics, together with other facts and circumstances, to determine whether an organization is considered a church for federal tax purposes.

The IRS makes no attempt to evaluate the content of whatever doctrine a particular organization claims is religious, provided the particular beliefs of the organization are truly and sincerely held by those professing them and the practices and rites associated with the organization's belief or creed are not



illegal or contrary to clearly defined public policy.

***Integrated Auxiliary of a Church.*** The term integrated auxiliary of a church refers to a class of organizations that are related to a church or convention or association of churches, but are not such organizations themselves. In general, the IRS will treat an organization that meets the following three requirements as an integrated auxiliary of a church. The organization must: • be described both as an IRC Section 501(c)(3) charitable organization and as a public charity under IRC Sections 509(a)(1), (2) or (3);

- be affiliated with a church or convention or association of churches; and
- receive financial support primarily from internal church sources as opposed to public or governmental sources.

Men's and women's organizations, seminaries, mission societies and youth groups that satisfy the first two requirements above are considered integrated auxiliaries whether or not they meet the internal support requirements. More guidance as to the types of organizations the IRS will treat as integrated auxiliaries can be found in the Code of Regulations, 26 CFR Section 1.6033-2(h).

The same rules that apply to a church apply to the integrated auxiliary of a church, with the exception of those rules that apply to the audit of a church. See [Special Rules Limiting IRS Authority to Audit a Church](#).

***Minister.*** The term minister is not used by all faiths; however, as used in this booklet, the term minister denotes members of clergy of all religions and denominations and includes priests, rabbis, imams and similar members of the clergy.

***IRC Section 501(c)(3).*** IRC section 501(c)(3) describes charitable organizations, including churches and religious organizations, which qualify for exemption from federal income tax and generally are eligible to receive tax-deductible contributions. This section provides that:

- an organization must be organized and operated exclusively for religious or other charitable purposes,
- net earnings may not inure to the benefit of any private individual or shareholder,
- no substantial part of its activity may be attempting to influence legislation,
- the organization may not intervene in political campaigns, and
- the organization's purposes and activities may not be illegal or violate fundamental public policy.

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# Help From The IRS

## IRS Tax Publications

The IRS provides free tax publications and forms. Download publications and forms from the IRS website at [www.irs.gov](http://www.irs.gov). The following publications may provide further information for churches and other religious organizations:

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<b><u>Publication 1</u></b>	Your Rights as a Taxpayer
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<b><u>Publication 15</u></b>	<i>Circular E, Employer's Tax Guide</i>
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<b><u>Publication 15-A</u></b>	<i>Employer's Supplemental Tax Guide</i>
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<b><u>Publication 334</u></b>	<i>Tax Guide for Small Business (For Individuals Who Use Schedule C or C-EZ)</i>
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**Publication**  
**463**

*Travel, Entertainment, Gift,  
and Car Expenses*

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**Publication**  
**517**

*Social Security and Other  
Information for Members of  
the Clergy and Religious  
Workers*

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**Publication**  
**525**

*Taxable and Nontaxable  
Income*

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**Publication**  
**526**

*Charitable Contributions*

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**Publication**  
**557**

*Tax-Exempt Status for Your  
Organization*

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**Publication**  
**561**

*Determining the Value of  
Donated Property*

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**Publication**  
**571**

*Tax-Sheltered Annuity Plans  
(403(b) Plans) for  
Employees of Public Schools  
and Certain Tax-Exempt  
Organizations*

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**Publication**  
**598**

*Tax on Unrelated Business  
Income of Exempt  
Organizations*

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**Publication**  
**910**

*Guide to Free Tax Services*

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**Publication**  
**1771**

*Charitable Contributions:  
Substantiation and  
Disclosure Requirements*

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**Publication**  
**3079**

*Tax-Exempt Organizations  
and Gaming*

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**Publication**  
**4221-PC**

*Compliance Guide for  
501(c)(3) Public Charities*

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**Publication**  
**4573**

*Group Exemptions*

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**Publication**  
**4630**

*The Exempt Organizations  
Product and Services Catalog*

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## **IRS Customer Service**

Telephone assistance for general tax information is available by calling: IRS Customer Service toll-free at 800-829-1040.

## **EO Customer Service**

Telephone assistance specific to exempt organizations is available by calling: IRS Exempt Organizations Customer Account Services toll-free at 877-829-5500.

## **EO Website**

Visit the IRS Exempt Organizations website at [www.irs.gov/eo](http://www.irs.gov/eo).

StayExempt —Tax Basics for Exempt Organizations — online courses available at [www.stayexempt.irs.gov](http://www.stayexempt.irs.gov).

## **EO Update**

To receive IRS *EO Update*, a periodic newsletter with information for tax-exempt organizations and tax practitioners who represent them, visit [www.irs.gov/eo](http://www.irs.gov/eo) and click on “Free e-Newsletter.”