

Housing for Your Pastor: Parsonage or Housing Allowance?

P&B MEMO

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Pensions and Benefits USA
Church of the Nazarene





“Should we continue to provide a parsonage and utilities, or should we provide a cash housing allowance and let the pastor purchase his own home?”

It's a question we often receive to which there is no definitive answer. There are advantages and disadvantages to each scenario. One pastor may want to receive a housing allowance that will allow the purchase of homes that will grow in equity and provide a measure of security at retirement. Another may not want the burden of buying, maintaining, and selling property. The information in this Memo is gleaned from the actual experiences of pastors and churches.

Pro Parsonage and Con Housing Allowance

1. In some situations there really is little choice. The parsonage may be connected to or adjoining the church building with no alternative for selling or renting. Unless used for Sunday School rooms, it remains the pastor's home.
2. Churches owning a parsonage may strengthen their ability to attract the pastoral candidate of their choice who may be unable or unwilling to buy a home.
3. In some areas, no property taxes are due on church-owned parsonages.
4. The church handles repairs and maintenance on the parsonage, freeing the minister from such time-consuming worries and expenses.
5. Often a parsonage is a superior accommodation to what a minister could afford to buy in the community.
6. Making a pastoral change is easier when moving from parsonage to parsonage, since securing temporary quarters is unnecessary for house hunting or waiting for occupancy.
7. When the parsonage is sold, the church loses a traditional and meaningful way of showing love and concern for the parsonage family.
8. Many ministers do not have sufficient funds for a down payment.
9. The church that enters the loan business to "give" a pastor a down payment often bears the cost of low interest, and little or no payment on the principal. There may be tax implications as well. State nonprofit corporation laws must be followed carefully. Some states may prohibit such loans. Also, be aware that a loan situation might be trouble-free, but awkward situations could develop.
10. Very often the church cannot afford a housing allowance that fully covers all expenses: real estate taxes, fire and casualty insurance, upkeep, etc. It takes constant review and appropriate board action to keep pace with these inflationary costs.
11. In some locations real estate can move slowly, if at all. Adequate housing may not be available for purchase when needed. Likewise, a home may not sell when it's time for a pastoral change.
12. If the minister purchases the parsonage, any difference between purchase price and appraised value may be considered as taxable income.
13. Appreciation of property is assumed, but depreciation may occur due to natural and man-made disasters or economic conditions. Homes do not always sell at a profit. This is not a concern for the minister in a parsonage.



Remember!

A parsonage may be nicer than a home the pastor could afford.



Remember!

A home may not sell easily during a pastoral change.

Pro Housing Allowance and Con Parsonage

1. A housing allowance may solve the problem of having to build a new parsonage at today's costs, and help the pastor build equity for retirement.
2. With a housing allowance, compensation planning may be more flexible, easier to compare, and simpler to budget.
3. Home ownership suggests permanency and may encourage longer pastorates.
4. A homeowner pays real estate taxes thus permitting him or her more voice in community affairs.
5. A minister gets to choose the type of home and location he or she prefers
6. The minister's family may decorate—even remodel—as they wish without board action.
7. Home ownership becomes an important investment for the future, assuming each property appreciates in value and appropriate equity is established. This growing “earned equity” is portable as the minister relocates, allowing full proceeds to be taken to a new location.
8. Home-owning ministers get a tax break. Within certain limits, the housing allowance used to provide and furnish a home is non-taxable income. Additionally, mortgage interest (up to \$750,000) may be itemized as a deduction. Also, state and local property taxes (up to \$10,000) may be deductible expenses. (See Memo #12: *Who Is a Minister for Tax Purposes?* to see who qualifies for this tax break.)
9. A homeowner can sell a principal residence and may not be required to pay any tax on up to \$500,000 of profit. The exclusion can be used as frequently as every two years. (See IRS Publication 523 for details.)
10. In the event of disability, death, or retirement, home ownership with adequate insurance generally means an immediate move is unnecessary.



Remember!

Home-owning ministers may benefit from special tax breaks.



See:

Memo #12: *Who Is a Minister for Tax Purposes?*

Tax Implications

In addition to the above considerations the local church board should insist that tax implications be explored thoroughly before any decision is made. The following examples represent possible concerns.

1. Extra care should be taken when a parsonage is to be given or sold to a minister at below fair market value. The church may contend this is a gift and is not compensation. However, it is likely this would be challenged by the IRS, forcing the minister to pay taxes on the value of the gift or take the issue to a tax court.
2. Where the church does make such a considerable gift to their minister without reporting it as compensation, the church may jeopardize or call into question its tax-exempt status. In order to have such status, the assets of the corporation cannot accrue to the personal benefit of an individual other than as reportable compensation. Tax-exempt organizations also must be careful that they not pay unreasonable compensation to employees.
3. Another concern involves the sale or rental of the parsonage. The church can be subject to taxation when it receives “unrelated business income.” Be sure to consult with an attorney or tax law specialist before taking such action.

Churches with strong financial resources may have no difficulty if they decide to sell their parsonage and provide a cash housing allowance. However, such a decision should be preceded by careful evaluation and in consultation with the church board, district board of church properties, district superintendent, pastor, and legal or tax counsel.

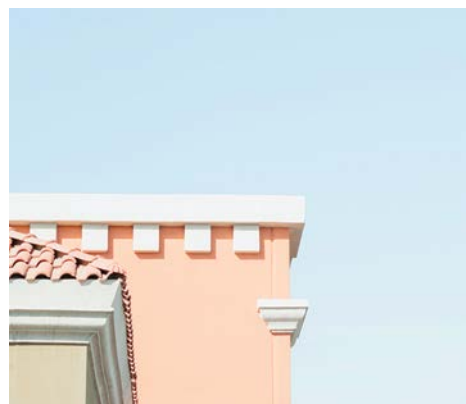
An Alternative—A Housing Reserve

The church board that does not allow its minister to purchase his/her own home, but provides an adequate parsonage and an allowance for parsonage furniture, etc., is still without an answer for its concern about the pastor’s future retirement need. But, there is an alternative. Let’s rephrase the question: “How can we provide our pastor with an adequate salary now and an adequate income at retirement without selling the parsonage?”



Caution!

Carefully explore the impact of selling a parsonage to your pastor before taking any action.



This question can be answered much more easily. A local church may provide a retirement housing reserve by contributing to its pastor's Nazarene 403(b) Retirement Savings Plan account. The benefits of doing this would include:

- The church can contribute and tax-shelter the compensation.
- Interest or gain can be realized on contributions without incurring an immediate tax liability. No tax liability is incurred until funds are withdrawn by the participant.
- Withdrawals at retirement often are at a reduced tax rate or as minister's tax-free housing allowance.
- Numerous withdrawal options allow for maximum flexibility in retirement planning.

The following chart illustrates how a retirement housing reserve could work, assuming a modest cash salary of only \$10,000 per year and assuming an interest rate of 7% (annual effective interest). Upon request, specific illustrations can be provided using current rates.



Idea!

Provide a retirement housing reserve for your pastor by contributing to the Nazarene 403(b) Retirement Savings Plan.



Remember!

Tax liability is not incurred on 403(b) funds until the money is withdrawn, and Nazarene ministers may receive the funds as tax-free housing allowance.

Nazarene 403(b) Retirement Savings Plan Illustrations

<u>Participant's Age</u>	<u>Monthly Deposit Until Age 66</u>	<u>Total Cash at 7% Interest at Age 66</u>	<u>*Monthly Income from Total Cash with Annuity Option at Age 66</u>
30	\$100	\$194,365	\$ 1,465
40	\$100	\$ 88,102	\$ 664
50	\$100	\$ 35,227	\$ 265

*Illustrations only (not guarantees or estimates) if dividends and interest remain unchanged. Annuity option of "life with 60 percent to survivor" with an annuity purchase rate of \$132.71/\$1 of monthly income at age 66 (i.e., \$132.71 buys you a monthly annuity payment of \$1). Annuity purchase rate is subject to change.

And Finally...

As you can see, the question of providing a parsonage or housing allowance has no clear-cut answer. We hope this information will provide insight as you seek to make a decision. As always, if you have further questions about this or other church/clergy financial issues, contact us at pensions@nazarene.org or **888-888-4656**.



The information contained in this memo series is of a general nature reflecting USA Nazarene Church polity. It is not offered as specific legal or tax advice. Each person, local church board, and district should evaluate their own unique situation in consultation with their local legal and tax advisors.

Here are other P&B Memos that might be helpful.

MEMO # 2: *Church Employees or Independent Contractors?*

MEMO # 3: *Tax and Reporting Procedures for Congregations*

MEMO # 4: *Strategies for Structuring Ministerial Compensation*

MEMO # 5: *Minimizing Income Taxes for Church Employees*

MEMO # 6: *Housing Allowance in Retirement*

MEMO # 7: *Financially Caring for the Minister*

MEMO # 8: *The Annual Church Audit*

MEMO # 9: *Workers' Compensation Laws and the Local Church*

MEMO #10: *Can Ministers Opt Out of Social Security?*

MEMO #11: *Auto and Other Business Expense Reimbursements*

MEMO #12: *Who Is a Minister for Tax Purposes?*

MEMO #13: *The Minister's Housing Allowance*



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