

# Getting Started Right...Financially!

The establishing of a church creates the need for careful legal, political and financial planning. Let's consider some of the areas:

**FEDERAL REQUIREMENTS** (see <http://www.irs.gov/charities/churches/index.html> for more information)

- a. **Federal Employer Identification Number (EIN):** This is a business's "social security number" and is needed to open a bank account, report payroll, etc. Apply by mail to IRS using their specific form for this purpose. This is not a "tax-exempt" number — there is no such number.
- b. **Non-profit Status** (IRS code 501 (c)(3)): All churches are automatically considered non-profit. Get a copy of IRS publication dealing with non-profit status and avoid the pitfalls implied there. There are strict limits as to how church assets are used; if these are violated, your church could lose the tax-exempt status. Do not take personal ownership of any church purchased assets unless these are included on your W-2 for the year.
- c. **Letter of Determination** from IRS: This is not necessary regardless of what anyone says (see specific statement in IRS instructions for this form), so no notice needs to be given to any governmental body that a new church is in existence. Governmental entities routinely ask for a copy of this letter when you apply to use government resources, such as renting a school, reserving a park, etc. Just send a letter on church letterhead stating that churches are not required to apply for a letter and that your church has not so applied, but that it is a recognized 501 (c)(3) organization.
- d. **Social Security:** Each new church has the temporary opportunity to file for permanent exemption from social security taxes. Churches lose this opportunity forever if not elected within the window of opportunity. Churches filing for exemption have no social security tax liabilities or responsibilities, but its employees must file "self-employment" tax forms and pay the employer's as well as the employee's share of the tax. The church exemption is separate from a minister's exemption (ordained ministers also have a limited time to apply, on Form 4361, and the tax is never paid), applies to all employees, is permanent, and does not reduce the tax, just shifts the entire burden to the employee. I do not recommend that this exemption be taken.
- e. **Filings:** Non-profit churches need to file only 1099's (with 1096's), payroll 941's and W-2's, and UBI (unrelated business income) forms when appropriate.
- f. **Tax Deductibility of Contributions:** Contributions to individuals (such as to a missionary, the pastor or any individual), even if given through the church offering plate as a designated gift, are not tax deductible. Receipts can be given for tax-deductible contributions to the church from the very beginning of the church, but there are special IRS requirements for them. Get the IRS publication regarding tax-deductible contributions.

## STATE REQUIREMENTS

These vary from state-to-state. In some states (Virginia & West Virginia) churches cannot incorporate and must exist as unincorporated bodies with trustees on public record at the courthouse. In other states churches incorporate and are under the requirements imposed upon incorporated bodies. Get local counsel within your state on sales tax laws, real estate taxes, incorporation, etc.

## BANKING & FINANCIAL ACCOUNTING

- a. **Open a bank account** in the name of the church, deposit ALL church monies into that account and pay ALL church expenses from that account. Separate accounts can be opened for designated giving (missions and building). You will need your federal employer identification number to be able to open an account.
- b. **Have the accounts reconciled** monthly by a non-signor. This person could also maintain the church financial books.
- c. **Maintain a double-entry accounting system**, which is required by law of non-profit organizations.

## LIABILITY INSURANCE

Get sound advice regarding the following insurance: property, liability and workman's compensation.

## PASTOR'S COMPENSATION PACKAGE

Part of the planning will involve plans for providing for the needs of the pastor. More often than not the pastor is provided for through temporary support from church missions programs. These churches are investing in a man and his ministry in this new church. Did you catch the word *temporary*? Just how temporary is that support? Isn't that decided by each church investor? Yes, and that means the support will gradually end as the new church informs the churches that it is no longer needed or as those churches feel it is time to end the support. This creates a transition period during which the new church must constantly monitor and make adjustments to the compensation package they are paying their pastor. As the support level drops the compensation level increases. Is there a better way to make it through this transition? I believe there is. Let the church establish the compensation package of the pastor from the beginning. This package will need to take into consideration the needs of the pastor and his family as well as the amount of support raised. All support would be deposited to the church account along with offerings. The church would pay the pastor his full needs. As the offerings increase the new church can inform the supporting churches that the support is no longer needed. During this transition from subsidized operation to full autonomy the pastor is cared for at a constant level and the new church is not in a position of making monthly decisions of increasing the pastor's salary to compensate for ended support. An added benefit involves tax records — all income is derived from one source rather than several making it easier to receive advance documentation on housing allowance separate from salary (such advance documentation is required to claim income as tax-free housing).

- a. **Salary** is the taxable income provided by the church to care for their pastor.
- b. **Benefits** are the non-taxable or tax-deferred payments made to the benefit of the pastor. Rather than paying the pastor a taxable salary and letting him provide for these needs the church can provide them with pre-tax dollars. These benefits should be paid by the church but the pastor should have input into the actual plans (insurance, retirement, etc.).
  - **Housing** expenditures are a tax-free benefit to an ordained minister. The church must document *in advance of giving the money* the amount they are providing the pastor as housing. The pastor must maintain documentation that he used the funds for qualified housing costs. Any housing money received and not used on housing costs becomes taxable income and should be claimed as "other income" when filing tax forms. Get the details to understand this tax break for ministers. This benefit is paid to the pastor along with his salary.
  - **Retirement** should be provided, particularly if the pastor opted out of social security. If the pastor opted out of social security the church should invest what they would have been required by law to invest (employer's share of social security) plus what they can afford into a retirement plan. This benefit can be paid directly to the investment company in the name of the pastor.
  - **Medical Insurance** should be provided through a Christian-based cost sharing program (i.e. Good Samaritan Program 317-894-2000 or Medi-Share 800-795-6274) or a more traditional insurance plan. This benefit can be paid directly to the insurance carrier. If a Christian-based cost sharing program is used (usually costing \$200/month for family coverage) the church could provide an additional **medical wellness** benefit of approximately \$100/month or \$1,200/year to cover medicals, prescriptions, dental and eye care.
  - **Automobile Expenses** due to church business (visitation, errands, etc.) should be reimbursed by the church. This is best covered by a mileage reimbursement from the church at the IRS mileage rate (approximately 35¢ per mile). If the IRS rate is used no records need to be kept on how this money is spent; the only record needed is a mileage log showing date, purpose and place of visit, trip meter readings or beginning and ending odometer readings. This record should be submitted to the church and reimbursement made accordingly. A better way to provide for auto expenses is for the church to purchase a car for the pastor's sole use. The church purchases, licenses, insures, maintains and provides gas for the entire use of the car (church-use **and** all pastor's personal use). The pastor calculates the percentage of the entire use of the car which is actually church-related (keep a log for several months) and that which is personal use. The personal use percentage is used to calculate the taxable benefit the church provided him. The IRS publishes a table for determining the annual value of a vehicle. The table determines that value based upon the purchase price of the vehicle. That value is to be used for each of the first three years of ownership. On the fourth year the annual value is to be redetermined using the table and the NADA book value of the car. The pastor's personal use percentage multiplied by the annual value of the vehicle is the pastor's taxable benefit from the church. The pastor's personal use taxable benefit is added to his salary and reported on his W-2 form.

## MISCELLANEOUS

Further preparation for the organization of a new church can be researched using the following sources:

*Basic Accounting for Churches*, Jack Henry

*Basic Budgeting for Churches*, Jack Henry, Broadman and Holman Publishers

*Business Management in the Local Church*, David Pollock, Moody Press

*Church Law and Tax Report*, Christian Ministry Resources, Matthews, NC

- a. **Best prices:** Cost effective purchases are possible through *National Church Purchasing Group*. Contact them about membership at 1-800-795-6274.
- b. **Obtaining Nonprofit Bulk Mail Permit:** Nonprofit bulk mailing permits can be obtained by churches immediately after beginning regular services. Follow these steps:
  - 1) **Obtain *Publication 417*** — *Special 3rd-Class Eligibility* from the post office. This publication includes *PS Form 3624* — *Application to Mail at Special Bulk 3rd-Class Rates*.
  - 2) **Complete the application.** Include a bulletin with the application. Note:
    - Question #8. You do not need an exemption from the IRS (see *Instructions for Form 1023* — *Application for Recognition of Exemption*). This exemption is for non-profit organizations that are not churches. The government must give them a *letter of determination* showing that the government has determined that they are non-profit. Churches are non-profit by right, not by determination.
    - Section B, Supporting Documentation, #1. This documentation is not required for churches.
    - *Postal Service Checklist for Form 3624*, #1. The post office is supposed to verify that you have included all required information and documentation with the application. If they do not know that churches do not need to supply either an IRS letter of exemption or a complete audited financial statement they will not accept the application.
  - 3) **Take the completed application** to your post office (where you will take mailings) and speak with the bulk mail department. Direct their attention to the sections noted above and ask if they are aware that churches do not need to comply with these requirements. If they are not aware they will likely not accept the application. If they will not,
  - 4) **Mail the application** to:  
Nonprofit Service Center  
Attention Supervisor  
PO Box 3623  
Memphis, TN 38173  
1-901-576-2060 and 2062

Include a bulletin and a letter (on church letterhead) stating that you understand that churches are not required to obtain the IRS letter of exemption or an audited financial statement to apply for a nonprofit bulk mailing permit but that your local post office is not aware of this and thus did not want to process your application. Ask if they will accept your application. I phoned this office first and spoke with Lula Smith. She asked me to send my application direct to her attention.