

TO: Council of Conference Ministers

FROM: Office of General Counsel

DATE: March 12, 2018

RE: Housing Allowance Ruling

## MEMORANDUM

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The Office of General Counsel recommends that the Council of Conference Ministers distribute this memorandum to Local Churches of the United Church of Christ, authorized ministers, and other covenant partners and ministry settings that may be affected by the end of the clergy housing allowance.

### Background

The clergy housing allowance is compensation that is provided to a “minister of the gospel” (as defined by the Internal Revenue Service) by their employer that the minister can exclude from their income for purposes of the federal income tax. The amount excluded from federal income tax is limited to the fair rental value of the home the minister lives in, including furnishing and utilities. The housing allowance is also available to ministers in retirement if the pension is designated as such. (If ministers or Local Churches have specific questions about the housing allowance, how to claim it, or other tax questions, they should contact a qualified CPA.)

### Housing Allowance Ruled Unconstitutional in Federal District Court in Wisconsin

Recently, a court in the Western District of Wisconsin ruled that the clergy housing allowance is unconstitutional as an Establishment Clause violation, because it is a preference for religion. The ruling applies only to 26 U.S.C. § 107(2), which is the clergy housing allowance, and does not apply to 26 U.S.C. § 107(1), which is the parsonage exclusion. This court order thus applies only to those who receive compensation in the form of a clergy housing allowance; it does not apply to ministers who live in church-owned parsonages.

This ruling is being appealed to the Seventh Circuit Court of Appeals, which is the federal appeals court that covers Wisconsin, Indiana, and Illinois. A decision on the appeal is expected before the end of 2018. Until the appeals process is over, the lower court’s ruling will not go into effect.

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## Conferences, Local Churches, Other Ministry Settings, and Ministers Should Be Prepared for the End of the Housing Allowance

One possible outcome of the case is that the Seventh Circuit affirms, or agrees with, the lower court's ruling that the clergy housing allowance is unconstitutional. While that court order applies to states in the Seventh Circuit (Wisconsin, Illinois, and Indiana), the Internal Revenue Service could choose to enforce the Seventh Circuit's decision nationwide to promote consistent tax policy.

Ministry settings should be prepared for this worst-case scenario, even as we acknowledge the outcome may be more positive.

### What Should Conferences, Local Churches, and Other Ministry Settings Do?

- **Conferences, Local Churches, and other ministry settings should continue to designate housing allowances for clergy until all appeals have been exhausted and a final ruling goes into effect.** Office of General Counsel anticipates that you will have plenty of notice before the final ruling goes into effect. The housing allowance is a valuable benefit to ministry settings and clergy and should continue to be provided until further notice.
- Recognize that the end of the housing allowance is a possibility.
- Determine by what amount compensation of your clergy will need to be increased to account for the additional income tax liability should the housing allowance end, and whether you will offer this increase if the housing allowance ends. You may need to consult with an accountant for assistance with this.
- Consider adding a reserve to your budget for some or all of that amount so that a jump in compensation in a future year is not so large or unexpected. If the housing allowance does not end, then you can use the reserve for other purposes.

### What Should Clergy Do?

- Clergy should recognize that the end of the housing allowance is a possibility.
- Ensure that employers are made aware of the issue by providing them with this memorandum and encouraging them to speak with their accounting or legal consultants.
- Do not make financial decisions based on current income, but consider the additional tax liability that you may face if the housing allowance ends, especially if your employer does not increase your compensation to account for the liability.
- Recognize that quarterly tax payments (or voluntary withholding) may need to be increased to account for the additional liability

The Office of General Counsel will provide updates as they become available.