



INFORMATION FOR RETIRED MINISTERS REQUESTING HOUSING ALLOWANCE AND COMPLETING IRS FORM 1040

Purpose

The purpose of this document is to:

- Explain the terms *housing allowance designation* and *housing allowance exclusion* available to eligible ministers;
- Explain the process for making a housing allowance designation; and
- Assist ministers in determining their housing allowance exclusion and the taxable portion of their pension from the Pension Plan and/or TIRA for income tax reporting purposes.

Background

Section 107 of the Internal Revenue Code allows ministers to exclude a "housing allowance" from their gross income. The exclusion includes an amount paid to a minister as part of his or her compensation to the extent used to *rent or provide a home* and to the extent such amount does not exceed the *fair rental value of the home, including furnishings and appurtenances such as a garage, plus the cost of utilities*. Code § 107(2). *See also* Treas. Reg. § 1.107-1.

The Internal Revenue Service has issued guidance extending the housing allowance exclusion to **retired ministers**. Pursuant to the guidance, amounts paid to a minister *as part of his or her compensation for past services* are excludable under Code Section 107(2), to the extent used for expenses directly related to providing a home. IRS Rev. Rul. 63-156. In other words, a retired minister of the gospel can designate housing allowance on his or her pension that represents compensation earned for his or her past services that were in the exercise of ministry.

In contrast, Revenue Ruling 72-249 provides that a minister's surviving spouse cannot exclude housing allowance from a surviving spouse pension unless the housing allowance is designated with respect to a pension that is compensation to the surviving spouse for *the spouse's* past services that were in the exercise of ministry. *See also* IRS Publication 517 at www.irs.gov/publications/p517/index.html; IRS PLR 8404101 (1984).

Key Terms

Housing allowance designation— This is the amount requested by the retired minister and designated by the Pension Fund Board as housing allowance. The minister's housing allowance designation is only an *estimate* of his or her expected housing expenses for the year.

Housing allowance exclusion— This is the amount a retired minister may legally exclude from income taxes and is limited to *the lesser of* –

- (1) the amount officially designated as housing allowance; **or**

- (2) the amount the minister actually spent for owning, operating or renting his or her principal residence; **or**
- (3) the fair rental value of the minister's principal residence furnished, plus utilities.

The housing allowance designated by the Pension Fund Board on behalf of the retired minister is not necessarily equal to the amount that may be excluded as housing allowance. ***In all cases, the individual retired minister is responsible for maintaining records of housing expenses and for reporting the taxable amount of his or her pension on the 1040 Income Tax Return.***

Steps Needed to Designate Housing Allowance

Retiring ministers can designate their initial housing allowance on their retirement application. The Pension Fund Board has designated 60% of the retired minister's pension as housing allowance for the year in which his or her pension begins. However, a retiring minister can officially request a different percentage or dollar amount on his or her retirement application. The initial housing allowance designation applies for the remainder of the calendar year following the designation.

During the fall of each year following the initial designation, Pension Fund will mail a letter to all retired ministers requesting them to designate their housing allowance for the next calendar year. This letter states that the Pension Fund Board will designate 60% of the retired minister's pension as housing allowance for the next calendar year, unless the minister officially requests a different percentage or dollar amount on the letter and timely returns that request to Pension Fund.

Prior to making a housing allowance designation for a calendar year, the minister should review his or her actual housing expenses for the past year, consider anticipated maintenance expenses, and obtain a figure for the fair rental value of the home, furnished. In doing so, the minister can use Pension Fund's *Housing Allowance for Retired Ministers Worksheet* which is enclosed with the annual housing allowance designation letter and also available upon request. After determining an appropriate housing allowance request, the minister should complete and return the Pension Plan retirement application or the designation request, as applicable.

Pension Fund will provide a letter confirming the minister's housing allowance designation.

Completing the Form 1040

Step 1

The minister must determine the amount actually spent on housing during the calendar year by gathering receipts for housing expenses such as rent or mortgage plus interest, property taxes, insurance (homeowner's or renter's), utilities (gas/oil, electricity, water/sewer/trash, local phone), furnishings, repairs and maintenance.

Step 2

The minister must compare his or her housing allowance designation in effect for the calendar year with his or her *actual housing expenses* and his or her *home's fair rental value*. **The housing allowance exclusion is the lowest of these amounts.** Generally, if there is no longer a

mortgage on the home, the retired minister will be limited to the lower of either the actual expenses or the housing allowance designation.

If the actual expenses were lower than the amount designated, the housing allowance exclusion is limited to the amount actually spent. If the actual expenses were higher than the amount that was designated, the housing allowance exclusion cannot be greater than the designated amount.

Here are some examples:

		Minister A	Minister B	Minister C	Minister D
1	Total Pension Amount	\$35,000	\$35,000	\$35,000	\$35,000
2	Housing Allowance Designation	\$21,000	\$21,000	\$17,500	\$17,500
3	Fair Rental Value	\$24,000	\$15,000	\$17,500	\$17,500
4	Actual Expenses	\$16,494	\$18,289	\$21,081	\$14,533
5	Housing Allowance Exclusion <i>(lowest of 2, 3 or 4)</i>	\$16,494	\$15,000	\$17,500	\$14,533
6	Taxable Pension Amount <i>(line 1 minus line 5)</i>	\$18,506	\$20,000	\$17,500	\$20,467

The 1040 Individual Income Tax Return

Form 1099-R lists the total amount of pension distribution in Box 1. If a housing allowance was designated, Box 2b will be checked indicating "Taxable amount not determined."

On the Form 1040, U.S. Individual Income Tax Return, locate line 16.¹

1. On line 16a, record the amount from Box 1 of the Form 1099-R provided by Pension Fund.
2. Subtract the housing allowance exclusion from the amount listed in Box 1 of Form 1099-R. Record the difference on line 16b. This is the taxable amount of the pension. Do not leave line 16b blank.
3. Here is an example of what line 16 might look like:

16a Pensions and annuities **16a** 35,000 **b** Taxable amount **16b** 18,506

¹ In light of recent tax code changes, the IRS has issued a draft of a revised Form 1040 for 2018. In this draft, instead of lines 16a and 16b, you should complete lines 4a and 4b in the same manner discussed above.

Important Notes

IRS Forms: Retired ministers often ask what IRS form is needed to report housing allowance. *There is no special form for reporting a minister's housing allowance.* The process described above is similar to that used when completing Schedule A – Itemized Deductions. For example, an individual may report total charitable contributions on Schedule A. The IRS does not ask for an accounting of all charitable contributions on Schedule A, but rather the individual tax filer records a total in that category, keeping accurate records in the event that the IRS questions the amount claimed. Likewise, retired ministers must keep accurate documentation of housing expenses in the event of an IRS audit.

Turbo Tax: If using TurboTax to complete the 1040, retired ministers may need to contact TurboTax to obtain information on how to accurately complete the tax return. Here is some information you may need when contacting Turbo Tax:

1. The Pension Plan is a defined benefit plan and the TDRA is a defined contribution plan.
2. The minister satisfies the required minimum distribution (RMD) rules in taking his or her pension.
3. TurboTax asks for the amount used to purchase the annuity, which is not applicable to the TDRA or Pension Plan.

PLEASE NOTE: *The information provided in this document is not intended to provide or be a substitute for specific individualized accounting or tax planning advice.*

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