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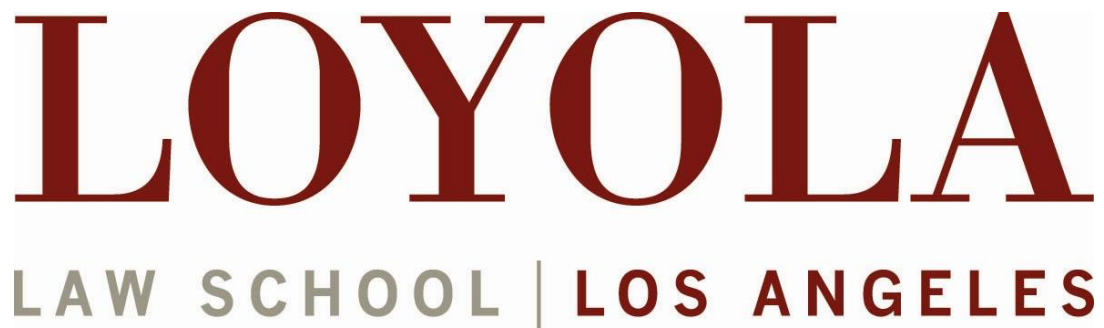
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AN OVERVIEW OF TAX
ISSUES FOR RELIGIOUS
CONGREGATIONS

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An Overview Of Tax Issues For Religious Congregations

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Ellen P. Aprill

Religious freedom has its price.

MANY TAX LAWYERS ARE ASKED TO SERVE on the governing bodies of their religious congregations. Yet religious congregations are subject to some unique rules that tax lawyers are unlikely to have encountered. This article discusses the issues that I have most often been asked, or should have been asked, in the many years that I have been giving pro bono advice to religious congregations of my own religious tradition, locally, regionally, and nationally. The issues discussed are: a) requirements for setting compensation, b) lobbying and political activities, c) substantiation of charitable contributions, d) charitable fundraising, e) payroll taxes and withholding for clergy, f) parsonage and housing allowances, and g) discretionary funds. The discussion of applicable rules is designed to be accessible to lay leaders and congregational staff, whether volunteer or professional. Different groups of leaders and volunteers have interest in different topics; each topic is designed to stand alone, and thus there is some overlap in coverage. Moreover, to be as inclusive as possible of our country's many different religious traditions, I have used the terms "religious congregation" and "clergy," although the Internal Revenue Code uses the terms "church" and "minister" of the gospel, which it has interpreted broadly. *See, e.g.* IRC §§170(b)(1)(A)(i), 508(c)(1)(A), 7611, 107, 1402(c)(4), 3121(b)(8)(A). (All section references are to the Internal Revenue Code unless otherwise indicated.)

OVERVIEW • Religious congregations are exempt from income tax, but nonetheless must comply with many tax laws. They must also comply with other applicable federal and state laws, particularly state corporate laws applicable to nonprofit religious organizations and state property and sales tax laws.

Exempt Status

Exemption And Reporting

Religious congregations are not required to file an application with the IRS to be exempt under section 501(c)(3), but many do file Form 1023, application for exemption, to be on the published IRS list of section 501(c)(3) charities eligible to receive tax-deductible contributions. §508(c)(1)(A); Publication 78, *Cumulative List of Organizations Described in Section 170(c) of the Internal Revenue Code of 1986*, available at <http://www.irs.gov/charities/article/0,,id=96136,00.html>. Religious congregations do not need to file the annual federal information returns (Form 990) required of other kinds of charities. §6033(a)(3)(A)(i). State filing laws, however, may differ.

Intermediate Sanctions

The law designed to reduce the risk of revocation of exempt status does not exempt religious congregations and requires that, in setting compensation for clergy and others, particular care be taken in obtaining comparables and in recording the basis for the compensation package. §4958. *See below.*

Political Activities And Lobbying

Religious congregations cannot intervene in elections and are limited in the amount of lobbying they can do. §501(c)(3). *See below.*

Contributions, Fundraising

Dues And Fees

Religious congregations must acknowledge contributions of \$250 or more (including dues); and they must inform members of the value of goods or services (other than intangible religious benefits) received in exchange for contributions. §170(f)(8). Difficult issues arise in connection with religious education and with donation of automobiles. *See below.*

Fundraising

Various fundraising activities, such as advertising in tribute books or newsletters and sale of scrip, must be done carefully so as not to subject religious congregations to the federal tax on unrelated business income. *See generally* §§511-514. That is, exempt organizations—including religious congregations—are not taxed on income related to their exempt purposes, but are subject to income tax on income from unrelated activities. Being subject to unrelated business tax will not jeopardize exempt status, unless such unrelated activities come to dominate the organization. Fundraising activities may also be subject to state and local regulation. *See below.*

Many congregations have begun to encourage their members to consider sophisticated estate planning techniques, such as charitable lead trusts or charitable remainder trusts, to benefit the congregation. Such plans must comply with all applicable tax rules, and members should consult their own tax advisors to understand the consequences.

Issues For Clergy And Other Staff

Income Tax Withholding, Social Security, Medicare

Clergy are subject to a unique set of tax rules regarding their compensation. Those regularly employed by a congregation are almost always consid-

ered to be employees, but withholding of income tax is not required and they are subject to self-employment rather than employee payroll taxes. §§3401(a)(9), 1402(a)(8), 1402(c)(4), and 3121(b)(8)(A). Their compensation should be reported on Form W-2, with no social security or Medicare tax withheld, not on Form 1099. *See below.*

Parsonage Or Housing Allowance

Clergy may exclude from income for purposes of the income tax the fair rental value of their housing, if certain requirements, including formal action by the religious congregation's board, are met. §107; Treas. Reg. §1.107-1. The amount of this housing allowance, along with clergy salary, is, however, subject to self-employment tax. §1402(a)(8). *See below.*

Discretionary Funds

An official statement of the religious congregation about the purpose and use of discretionary funds will help protect clergy from any assertion that these funds represent additional income to them. *See below.*

Other Employee Issues

For both clergy and non-clergy employees, some benefits are subject to income tax and payroll taxes and some are not. In many cases, the tax consequences of benefits, such as medical benefits and tuition discounts, will depend on how they are structured and to whom they are offered. For non-clergy employees, failure to comply with withholding and payroll tax laws risks the particularly stringent penalties on those who had the responsibility to deposit these funds. *See* §6672.

SUMMARY OF “INTERMEDIATE SANCTION” PROVISIONS APPLICABLE TO TAX-EXEMPT ORGANIZATIONS • The tax law makes it especially important to obtain comparable data in setting compensation. Some years ago

Congress passed legislation, known as intermediate sanctions, requiring that nonprofit organizations pay reasonable compensation. §4958, Teas. Reg. §53.4958-4. Violation of these rules can lead to imposition of sizeable excise taxes on senior staff and organization managers (which include directors or trustees) of the organization. §§4958(a)-(b), (f)(2); Treas. Reg. §53.4958-1(d)(2).

The IRS has issued regulations regarding this legislation. Treas. Reg. §53.4958-1 through §53.4958-8. These regulations give a presumption of reasonableness for compensation (and other transactions, such as sales and contracts) if and only if the organization follows very specific procedures. Treas. Reg. §53.4958-6. The procedures include the organization obtaining and relying upon appropriate data as to comparability for compensation of those who have substantial influence over the organization and who receive total economic benefits above a specified amount (\$110,000 for 2009 and 2010). IRS Notice 2009-94.

These procedures also require that the organization concurrently record the compensation package, the basis for the compensation package (including the comparables), and those who voted on the compensation package. Under the regulations, even small organizations (defined as those with gross receipts under \$1 million) must obtain three comparables to have the benefit of the presumption or reasonable compensation.

This law does not exempt religious organizations, although the regulations state that the IRS will comply with the Church Audit Act. Treas. Reg. §53.4958-8(b). Under the Church Audit Act, the IRS could seek to impose these taxes only if it has a reasonable belief that such taxes are due and various notice requirements have been met. *See generally* §7611. The IRS has proposed but not finalized regulations under the Church Audit Act.

RULES REGARDING LOBBYING AND POLITICAL ACTIVITIES BY SECTION 501(C)

(3) ORGANIZATIONS • The Internal Revenue Code distinguishes political campaigns from attempts to influence legislation. §501(c)(3).

All section 501(c)(3) organizations, including religious congregations, are prohibited, at risk of losing exemption, from participating in political campaigns. In general, political campaigns are defined for this purpose as campaigns by candidates for elective office. *Id.* (This prohibition was first introduced by Lyndon Johnson as an amendment in 1954. See *Charities, Churches, and Politics*, available at <http://www.irs.gov/newsroom/article/0,,id=161131,00.html>.) In *Branch Ministries v. Rossotti*, 211 F.3d 137 (D.C. Cir 2000), a federal appellate court upheld revocation of a church's exemption for running anti-Clinton newspaper ads. (The church had claimed, among other arguments, that the political campaign prohibition violates the First Amendment.)

Tax-exempt charities, including religious congregations, cannot endorse or oppose any candidate, directly or indirectly. They also cannot contribute any money or resources to any candidate's campaign or political party or rank candidates, even if the ranking is the result of neutral process. See Rev. Rul. 2007-41; *The Association of the Bar of the City of New York v. CIR*, 858 F.2d 876 (1988), *cert. denied*, 490 U.S. 1030 (1989); *IRS Tax Guide for Churches and Religious Organizations*, available at <http://www.irs.gov/pub/irs-pdf/p1828.pdf>. Avoid statements from the pulpit, at any official function, or in any official publication—including activities of any social action committee—that name candidates or that comment on their positions, because such statements are likely to be treated as being the position of the organization. *Id.*

Not all activities involving campaigns for elective office are considered prohibited political activity. Charities can register voters, conduct candidate debates, distribute general voter education

information, or run get-out-the vote operation on election day—but only if these activities are conducted in a nonpartisan manner. See FS 2006-17, available at <http://www.irs.gov/newsroom/article/0,,id=154712,00.html>. A debate will not be considered nonpartisan unless all qualified candidates are invited to attend. See Rev. Rul. 86-95, 1986-2 C.B. 73.

In addition, clergy or other senior staff can on their own behalf and on their own time take a public position on a candidate or sign an endorsement letter published in a newspaper. See Rev. Rul. 2007-41, 2007-1 C.B. 1421; *IRS Tax Guide for Churches and Religious Organizations*. If the clergy's affiliation with the religious congregation is shown, however, accompanying language (such as "Affiliation for identification purposes only") should clearly disclaim the congregation's involvement. *Id.*

Although any involvement in a political campaign for elective office is prohibited, religious congregations, like other charities, can participate in lobbying to a limited degree. §501(c)(3). For tax purposes, lobbying is distinguished from intervening in electoral politics. *Id.* Lobbying is defined as an attempt to influence legislation, either directly through legislators or indirectly through grass roots campaigns which ask citizens to contact their legislators. See Treas. Reg. §1.501(c)(3)-1(c)(3). (Taking such positions on initiatives or propositions is considered lobbying, not political campaign activity. See Treas. Reg. §56.4911-2(b)(1)(iii).)

Under the Code, lobbying by charitable organizations is permitted to a limited extent; it cannot be a substantial part of the organization's activities. §501(c)(3); Treas. Reg. §1.501(c)(3)-1(c)(3). The meaning of substantial is not clear, but it is clear that it means more than dollars spent. See *Haswell v. U.S.*, 500 F.2d 1133 (Ct.Cl. 1974), *cert. denied*, 419 U.S. 1107 (1975). (Organizations other than churches can choose to have their lobbying activities subject to specified dollar limits, but this option is not available to churches. §501(h), (h)(5)(A).) The

Supreme Court has upheld the constitutionality of the lobbying limits, although the case did not involve a religious organization. *Regan v. Taxation with Representation*, 461 U.S. 540 (1983).

SUBSTANTIATION AND QUID PRO QUO REQUIREMENTS • To deduct contributions of cash or by check of less than \$250, the donor must have a bank record or a written communication from the religious congregation (including electronic mail correspondence) showing the congregation's name, the date of the contribution, and the amount of the contribution. §170(f)(17). Offering envelopes are no longer sufficient to substantiate donations; religious congregations may wish to start providing periodic summaries of cash contributions to their members.

If charitable contributions total \$250 or more, however, donors must substantiate the contribution with a contemporaneous acknowledgment. §170(f)(8). Substantiation requirements for deductible contributions of \$250 or more may be satisfied for several such contributions with one or more contemporaneous acknowledgments. Treas. Reg. §1.170A-13(f)(1). Since each payment is considered separately, contributions of less than \$250 are not subject to these heightened substantiation requirement, even if they exceed \$250 in the aggregate. *Id.*

The acknowledgment must provide (1) the amount of cash paid and a description of any property transferred, (2) a statement of whether goods or services were provided for consideration, in whole or part, for such cash or property, (3) a description and good faith estimate of the value of any goods or services so provided, and (4) a statement by organizations providing intangible religious benefits that they do so. Treas. Reg. §1.170A-13(f)(2).

The written acknowledgment is contemporaneous if the taxpayer obtains it on or before the earlier of the taxpayer's filing date for the original return for the taxable year in which the contribu-

tion was made or the due date, including extensions, for such return. Treas. Reg. §1.170A-13(f)(3).

Goods or services are provided for consideration if the "the taxpayer receives or expects to receive goods or services in exchange for payment." Treas. Reg. §1.170A-13(f)(6).

Goods and services received in connection with fundraising may be disregarded and thus need not be acknowledged if either they have value of not more than two percent of the amount contributed, up to a maximum (for 2010) of \$96, or if the goods received are only token items with the charity's name and logo or low-cost items worth no more than \$9.60 when the taxpayer makes at least a minimum payment of \$48. Treas. Reg. §1.170A-13(f)(8); Rev. Proc. 2009-50. (These numbers are adjusted for inflation annually.)

Newsletters of less than commercial quality and low-cost items provided for free without advance orders also are deemed to have insubstantial value. Rev. Proc. 90-12, 1990-1 C.B. 471.

The charitable contribution consequences of quid pro quo contributions—contributions that are partly a charitable contribution and partly consideration for return benefits in the form of services or goods—that exceed \$75 must be disclosed; that is, the amount above the fair market of goods and services received that is deductible as a charitable contribution. §6115; Treas. Reg. §1.6115-1(a)(1). Failure to satisfy these rules subjects the charity to penalties of \$10 per contribution, with a maximum of \$5,000 per event or mailing. §6714.

The burden is on the taxpayer to show that all or part of a payment to a charitable organization is a contribution or gift. Treas. Reg. §1.170A-1(h)(1). A charitable deduction is not allowed for a payment to charity for goods or services (other than for intangible religious benefits) unless (a) the amount exceeds the fair market of the goods or services and (b) the taxpayer intends to make a payment in excess of such fair market value. Treas. Reg. §1.170A-1(h)(2). In determining this excess, if any,

the taxpayer may rely on the value of the goods and services as provided by the donee organization, unless the taxpayer knows the donee's stated value or good faith estimate of value is unreasonable. Treas. Reg. §1.170A-1(h)(4).

Dues paid to a religious congregation for membership are deductible; what is received in return for dues is deemed to be an entirely intangible religious benefit.

Recent decisions by the Ninth Circuit Court of Appeals, involving suits by a family named Sklar against the IRS Commissioner, concluded that the part of the payments by parents to a Jewish religious day school for religious education are NOT deductible as charitable contributions. *Sklar v. CIR*, 549 F.3d 1252 (9th Cir. 2008), *cert. denied*, 130 S.Ct. 53 (2009) *Sklar v. CIR*, 282 F.3d 610 (9th Cir. 2002). There is no IRS or judicial authority permitting deduction for costs of religious education; these costs are seen as payment for education, not a contribution that results in an intangible religious benefit.

In the case of donations of automobiles, new rules generally limit any deduction above \$500 to the amount for which the charity sells the car. §170(f)(12).

An organization may use any reasonable methodology in making a good faith estimate of the value of goods and services it provides. Treas. Reg. §1.170A-13(f)(7). For goods or services that are not generally available in a commercial market, the good faith estimate may use goods or services that are similar or comparable even if they do not have the unique qualities of those offered by the organization. Treas. Reg. §1.6115-1(a)(2).

Acknowledgment for unreimbursed out-of-pocket expenses is satisfied if the taxpayer has records of the expenditures and obtains a timely statement from the organization describing the services provided by the taxpayer and whether the organization provided any goods or services in consideration for them. Treas. Reg. §1.170A-13(f)(10).

LAWS REGARDING CHARITABLE FUND-RAISING • Charitable fundraising, including that conducted by religious organizations, is subject to federal, state, and local laws.

Charitable contributions are deductible for income tax purposes only to the extent that they exceed the fair market value of what is received. Treas. Reg. §1.170A-1(h)(2). NOTE: The deductible contribution must be reduced by the fair market value of what is received, not the cost to the congregation. Thus, having the goods or services donated to a religious congregation does not prevent reduction of the deductible amount.

Additional federal disclosure laws apply to payments above \$75 that involve both a charitable donation and a receipt of goods or services. §6115. Any fundraising event that costs more than \$75 and involves the provision of a meal, such as a dinner dance or the typical "rubber chicken" dinner, will be subject to these rules. In such cases, the reduction in deductible contribution needs to be disclosed on the solicitation/invitation or receipt for the event. *Id.* A sample disclosure would look like this:

The estimated value of each ticket for the [name of event] [dinner/lunch/gala] is [\$XX]. Only the amount of your contribution in excess of the value received in exchange for your contribution is tax deductible.

Auctions require particular care. See Treas. Reg. §1.170A-1(h)(5), Example 2. Fair market value of what is received needs to be established. In many cases, the amount paid is below fair market value and thus there is no charitable contribution deduction. In other cases, the amount bid will be the only indication of fair market value. Also, in a few states, such as California, the religious congregation must charge—and pay—sales tax on auction items.

Raffles and lotteries require particular care and state laws, including state gambling law, must be consulted. Under federal law, if someone wins \$600 or more gambling (and gambling includes raffles), the religious congregation must issue a form W-2G,

the form for reporting gambling winnings, and if winnings amount to more than \$5,000, the congregation must withhold. §3402(q).

Sales of advertising, scrip, magazines, candy, etc. will be exempt from tax on unrelated income if they meet some of the special exceptions to that tax. The most likely exceptions are (1) having substantially all the work conducted solely by volunteers or (2) having the sales activities not be regularly carried on—that is, sales activities conducted only a few weeks a year are not subject to tax. §§512, 513(a)(1).

Religious organizations need to determine whether they are subject to state and local solicitation or disclosure requirements.

Passive income received by religious congregations in the form of dividends, interest, rent for real property, and royalties is not subject to income tax. §512(b)(1), (2). It is important, however, that the rent be charged for space, not for services. Also, if anywhere between 10 and 50 percent of rent received is attributable to personal property, the amount attributable to rental of personal property is taxable. §512(b)(3). If more than 50 percent of the rent received is for personal property, all of the rental income received is taxable. *Id.* Thus, religious congregations that rent out not only social halls but also tables and chairs, etc. for non-religious purposes need to take great care. Also, debt-financed income, even if passive, will generally be subject to income tax. §514.

PAYROLL TAXES AND WITHHOLDING FOR CLERGY

• Although clergy who work regularly part or full-time are, with only rare exceptions, employees of their religious congregations, they are subject to a special set of rules when it comes to income tax withholding and liability for social security and Medicare taxes. (Note that while there is a limit to the amount of wages to which social security taxes apply, there is no longer any limit on the taxes for Medicare.)

Income tax withholding is not required for clergy, although they may elect to have income tax withheld. §3401(a)(9).

There are special rules in the Code requiring that clergy be treated as self-employed for purpose of social security and Medicare taxes (but please note, only for this purpose). §§1402(a)(8), 1402(c)(4), 3121(b)(8)(A); *Social Security and Other Information for Members of the Clergy and Religious Workers*, IRS Publication 517, available at <http://www.irs.gov/pub/irs-pdf/p517.pdf>. That is, they are subject to self-employment tax, under SECA (the Self-Employment Contribution Act), rather than taxed as employees under FICA (Federal Insurance Contribution Act) on the amounts they are paid. In essence, this means that they are liable for both halves of this tax, where in the case of employees, the employee pays half and the employer pays half.

For clergy, because they are treated as self-employed, the social security tax is 12.4 percent of wages up to \$106,800 in 2009 and 2010. Social Security Administration Notice 2009-80. Medicare tax is 2.9 percent of all wages. (For clergy, these taxes apply to net self-employment earnings; that is, based on an algebraic formula, one-half of the tax is deducted on their personal tax return in calculating the amount on which they pay self-employment tax.)

Although parsonage/housing allowances are excluded from income tax, they do constitute wages for purposes of social security and Medicare tax. §1402(a)(8). That is, clergy are subject to SECA (meaning they must pay both halves of the payroll tax) on all the wages they receive as clergy—both their salary and their parsonage/housing allowance.

In the vast, vast majority of situations, religious congregations should report the income of clergy who work regularly for the religious congregation on Form W-2, NOT Form 1099. That is, the law treating clergy as self-employed for purposes of

Medicare and Social Security does NOT make them independent contractors rather than employees for purposes of reporting income. The amount of income reported is reduced by the amount of parsonage/housing allowance properly claimed by the clergyperson, although it can be listed in the “other” box on the W-2. If the congregation has withheld amounts to help clergy satisfy payroll tax obligations, such amounts are reported as additional income tax withheld and not as social security or Medicare tax withheld.

If religious congregations reimburse their clergy for half of the payroll taxes, as some do, this reimbursement must be reported as additional income and is itself subject to payroll taxes (subject to the rules that permit certain income tax and payroll tax deductions for people subject to self-employment tax.)

Clergy employed by religious congregations remain employees for other purposes of the Code and for state law purposes. Thus, for example, they may deduct miscellaneous itemized deductions, including unreimbursed employee expense, only to the extent these exceed two percent of adjusted gross income. As employees, they are also eligible for employee fringe benefits, such as cafeteria plans, medical plans, etc. and for coverage as employees under the congregation’s insurance plans.

Erroneously treating clergy as self-employed independent contractors poses several kinds of risks and disadvantages for the clergy. Many tax-free fringe benefits, such as cafeteria plans, are available only to employees. Audit risk is much lower for employees. If clergy are audited, the IRS in almost all cases will reclassify them as employees and the clergy/taxpayer is then likely to be liable for taxes, interest, and penalties for deductions improperly taken on Schedule C instead of as unreimbursed employee expenses. Generally, health plans and insurance contracts cover only employees.

OVERVIEW OF RULES REGARDING CLERGY’S PARSONAGE OR HOUSING ALLOWANCE •

Clergy are defined by the tax law as those who are ordained, commissioned, or licensed. Treas. Reg. §1.1402(c)-5. Clergy who are hired to fill administrative or other positions and who do not function as clergy or teachers of theology are not entitled to parsonage/housing allowances. (A case challenging the constitutionality of the parsonage/housing allowance on First Amendment establishment clause grounds is currently being heard in California. *Freedom from Religion Foundation, Inc. v. Geithner*, No. 09-2894 (E.D. CA).) The IRS requires that clergy be hired to function as clergy on a substantial basis to be entitled to parsonage or housing allowances.

Clergy who function as such in the congregation are entitled to exclude from income the lowest of the following three numbers: (1) the portion of their income designated in advance by their employer as a housing/parsonage allowance; (2) the amount the clergy in fact used to pay for housing-related expenses; (3) the fair rental value of the home (furnished) plus utilities. §107; Treas. Reg. §1.107-1. Thus, particularly in the year a clergy person buys a house and pays a down payment, all actual housing expenses may not be excludible from income. Legislation passed in May 2002 and now codified in section 107 makes clear that housing allowances are limited to fair market rental value.

For any amounts to be excluded, there must be a housing/parsonage allowance adopted (1) by official action and (2) in advance of the time the amounts to be excluded are earned by services. Treas. Reg. §1.107-1(b). Applicable IRS regulations list the following as examples of official action: employment contract, board minutes, board resolution, and congregational budget. *Id.*

Some congregations follow the practice of having the clergyperson estimate, before the year begins, the housing expenses for the coming year and

use that estimate as the basis of a board resolution. Such practice is perfectly acceptable.

As noted, it is also permissible to set the allowance in the clergy's employment contract, since the contract is in writing, approved by the board and adopted before the amounts are earned.

Amounts that come within the parsonage allowance include: down payment, mortgage payments on loan to purchase or improve home (both principal and interest); real estate taxes, property insurance; utilities (electricity, gas, water, trash pickup, local telephone charges); furnishings and appliances (purchase and repair); structural repairs and remodeling; yard maintenance and improvements; maintenance items (household cleaners, light bulbs, pest control), *subject, however, to the limits described above.*

The amount of the parsonage allowance reduces the amount reported as compensation on the clergyperson's W-2 (or Form 1099, in those rare cases where the clergyperson is operating as an independent contractor), so it is important that the amounts be supplied by the clergy to the congregation in time to prepare the required form. It is recommended that the congregation have the clergyperson substantiate the amount claimed as a parsonage allowance.

In general, clergy do not need to work full-time to be eligible for the parsonage allowance. (Under the facts of the revenue ruling recognizing a Jewish cantor as a minister of the gospel for purposes of section 107, the cantor was employed full-time by the congregation. Rev. Rul. 78-301.)

Remember that anyone receiving the parsonage allowance must be treated as self-employed for purposes of social security and Medicare (payroll) taxes. They are subject to SECA, not FICA.

Clergy are permitted both to exclude housing from income and to deduct mortgage interest. §265(a)(6).

CLERGY DISCRETIONARY FUNDS • Religious congregations must exercise oversight of discretionary funds to protect both the clergy and the members who contribute. Clergy discretionary funds raise two different kinds of issues: income to clergy and deductibility for donors.

To avoid the former, the clergy cannot use the funds for personal purposes. (If they can, all monies in their discretionary fund could be deemed taxable income to them.) Examples of inappropriate personal purposes include such uses as professional dues, fees to attend conferences, tickets for the clergy or their family to attend events and dinners, gifts to others from the clergy, and satisfaction of personal pledges by the clergy.

To accomplish the latter, the clergy must be acting as an agent of the religious congregation. That is, the funds do not come from the clergy personally; they come from the congregation through the discretionary fund. Clergy act as agents of the congregation. The money is the property of the congregation, and the congregation's governing board must retain oversight over the funds to ensure that they are spent for religious, educational, and charitable (i.e. tax-deductible) purposes. Charitable for these purposes means relief of the poor, distressed, and needy. The IRS defines "needy" for these purposes to include not only financial impoverishment but also "a person who is temporarily not self-sufficient as a result of a sudden and severe personal or family crisis." Treas. Reg. §1.170A-4A(b)(2)(ii)(D). (Moreover, these funds cannot be used for political purposes, that is, they cannot be used for participating in an election campaign, at risk of losing the religious congregation's exemption.)

The bank account for the discretionary fund should be an account of the congregation, albeit one for which the clergy has signing authority. A sample resolution to accomplish these goals might look like this:

The clergy act as agents of this congregation in disbursing funds from their discretionary funds. These funds remain

the property of the congregation. The clergy of the congregation are authorized to use the monies contributed to their discretionary funds for needs and projects consistent with the religious, educational, and charitable purposes of the congregation. No monies from these discretionary funds shall be used or distributed for personal purposes of the clergy or their family. The purposes for which discretionary funds have been used shall be reviewed annually by the then-President and or any delegates appointed by the then-President, including, should the President so choose, outside auditors.

Oversight by the congregation should not violate the purpose of these funds—which is to allow the clergy to decide how to use these funds through exercise of their discretion within the broad permitted categories. Use of discretionary funds need not require prior approval, but all distributions must be reviewed for consistency with permitted

uses. Thus, even use of discretionary funds for particular individuals must satisfy charitable purposes and be subject to review, but review should not violate confidentiality or expose any recipients of funds to embarrassment. The necessary oversight must be done with care and sensitivity. It can be accomplished by having the clergy report by category on the kind of uses to which they had put the funds and the amounts expended in each category, along with more detailed review annually of each distribution by one or two officers or outside auditors who are under an obligation to keep details about any individual recipient confidential. The purpose of such review is not to second guess or direct the clergy's use of the funds, but only to ensure that each use of the fund is within the permitted purposes.

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