

Internal Revenue Service  
Tax Exempt and Government Entities  
Exempt Organizations

tax guide for

# Churches and Religious Organizations

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*benefits and responsibilities  
under the federal tax law*

*Congress has enacted special tax laws applicable to churches, religious organizations, and ministers in recognition of their unique status in American society and of their rights guaranteed by the First Amendment of the Constitution of the United States. Churches and religious organizations are generally exempt from income tax and receive other favorable treatment under the tax law; however, certain income of a church or religious organization may be subject to tax, such as income from an unrelated business.*

*The Internal Revenue Service (IRS) offers this quick reference guide of federal tax law and procedures for churches and religious organizations to help them voluntarily comply with tax rules. The contents of this publication reflect the IRS interpretation of tax laws enacted by Congress, Treasury regulations, and court decisions. The information given is not comprehensive, however, and does not cover every situation. Thus, it is not intended to replace the law or be the sole source of information. The resolution of any particular issue may depend on the specific facts and circumstances of a given taxpayer. In addition, this publication covers subjects on which a court may have made a decision more favorable to taxpayers than the interpretation by the IRS. Until these differing interpretations are resolved by higher court decisions, or in some other way, this publication will present the interpretation of the IRS.*

*For more detailed tax information, the IRS has assistance programs and tax information products for churches and religious organizations, as noted in the back of this publication. Most IRS publications and forms can be downloaded from the IRS Web site at [www.irs.gov](http://www.irs.gov), or ordered by calling toll-free (800) 829-3676. Specialized information can be accessed through the Exempt Organizations (EO) Web site under the IRS Tax Exempt and Government Entities division via [www.irs.gov/eo](http://www.irs.gov/eo) or by calling EO Customer Account Services toll-free at (877) 829-5500.*

*The IRS considers this publication a living document, one that will be revised to take into account future developments and feedback. Comments on the publication may be submitted to the IRS at the following address:*

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## Introduction

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**T**his publication explains the benefits and the responsibilities under the federal tax system for churches and religious organizations. The term church is found, but not specifically defined, in the Internal Revenue Code (IRC). The term is not used by all faiths; however, in an attempt to make this publication easy to read, we use it in its generic sense as a place of worship including, for example, mosques and synagogues. With the exception of the special rules for church audits, the use of the term church throughout this publication also includes conventions and associations of churches as well as integrated auxiliaries of a church.

Because special tax rules apply to churches, it is important to distinguish churches from other religious organizations. Therefore, when this publication uses the term “religious organizations,” it is not referring to churches or integrated auxiliaries. Religious organizations that are not churches typically include non-denominational ministries, interdenominational and ecumenical organizations, and other entities whose principal purpose is the study or advancement of religion.

Churches and religious organizations may be legally organized in a variety of ways under state law, such as unincorporated associations, nonprofit corporations, corporations sole, and charitable trusts.

Certain terms used throughout this publication—church, integrated auxiliary of a church, minister, and IRC section 501(c)(3)—are defined in the Glossary on page 27.



## Tax-Exempt Status

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Churches and religious organizations, like many other charitable organizations, qualify for exemption from federal income tax under IRC section 501(c)(3) and are generally eligible to receive tax-deductible contributions. To qualify for tax-exempt status, such an organization must meet the following requirements (covered in greater detail throughout this publication):

- the organization must be organized and operated exclusively for religious, educational, scientific, or other charitable purposes,
- net earnings may not inure to the benefit of any private individual or shareholder,
- no substantial part of its activity may be attempting to influence legislation,
- the organization may not intervene in political campaigns, and
- the organization's purposes and activities may not be illegal or violate fundamental public policy.

### Recognition of Tax-Exempt Status

#### Automatic Exemption for Churches

Churches that meet the requirements of IRC section 501(c)(3) are automatically considered tax exempt and are not required to apply for and obtain recognition of tax-exempt status from the IRS.

Although there is no requirement to do so, many churches seek recognition of tax-exempt status from the IRS because such recognition assures church leaders, members, and contributors that the church is recognized as exempt and qualifies for related tax benefits. For example, contributors to a church that has been recognized as tax exempt would know that their contributions generally are tax-deductible.

#### Church Exemption Through a Central/Parent Organization

A church with a parent organization may wish to contact the parent to see if it has a *group ruling*. If the parent holds a group ruling, then the IRS may already recognize the church as tax exempt. Under the group exemption process, the parent organization becomes the holder of a group ruling that identifies other affiliated churches or other affiliated organizations. A church is recognized as tax exempt if it is included in a list provided by the parent organization. The parent is then required to submit an annual group exemption update to the IRS in which it provides additions, deletions, and changes within the group. If the church or other affiliated organization is included on such a list, it does not need to take further action to obtain recognition of tax-exempt status.

An organization that is not covered under a group ruling should contact its parent organization to see if it is eligible to be included in the parent's application for the group ruling. For general information on the group exemption process, see Revenue Procedure 80-27, 1980-1 C.B. 677.

#### Religious Organizations

Unlike churches, religious organizations that wish to be tax exempt generally must apply to the IRS for tax-exempt status unless their gross receipts do not normally exceed \$5,000 annually.

### Applying for Tax-Exempt Status

#### Employer Identification Number (EIN)

Every tax-exempt organization, including a church, should have an employer identification number (EIN), whether or not the organization has any employees. There are many instances in which an EIN is necessary. For example, a church needs an EIN when it opens a bank account, in order to be listed as a subordinate in a group ruling, or if it files returns with the IRS (e.g., Forms W-2, 1099, 990-T).

An organization may obtain an EIN by filing Form SS-4, *Application for Employer Identification Number*, in accordance with the instructions.

### **Application Form**

Organizations, including churches and religious organizations, that wish to be recognized as tax exempt under IRC section 501(c)(3) must use Form 1023.

A religious organization must submit its application within 27 months from the end of the month in which the organization is formed in order to be considered tax exempt and qualified to receive deductible contributions as of the date the organization was formed. On the other hand, a church may obtain recognition of exemption for time periods prior to the date of its request for tax-exempt status, even if it does not submit its application within 27 months of formation.

**Cost for applying for exemption.** The IRS is required to collect a non-refundable fee from any organization seeking a determination of tax-exempt status under IRC section 501(c)(3). Although churches are not required by law to file an application for exemption, if they choose to do so voluntarily, they are required to pay the fee for determination.

The fee must be submitted with Form 1023; otherwise, the application will be returned to the submitter. Fees change periodically. The most recent user fee can be found at the Exempt Organizations (EO) Web site under the IRS Tax Exempt and Government Entities division via [www.irs.gov/eo](http://www.irs.gov/eo) or by calling EO Customer Account Services toll-free at (877) 829-5500.

### **IRS Approval of Exemption Application**

If the application for tax-exempt status is approved, the IRS will notify the organization of its status, any requirement to file an annual information return, and its eligibility to receive deductible contributions. The IRS does not assign a special number or other identification as evidence of an organization's tax-exempt status.

## **Public Listing of Tax-Exempt Organizations**

The IRS lists organizations that are qualified to receive tax-deductible contributions in IRS Publication 78, *Cumulative List of Organizations Described in Section 170(c) of the Internal Revenue Code of 1986*. This publication is sold to the public through the Superintendent of Documents, U.S. Government Printing Office, Washington, DC. Publication 78 can also be downloaded from the IRS Web site at [www.irs.gov](http://www.irs.gov). Note that not every organization that is eligible to receive tax-deductible contributions is listed in Publication 78. For example, churches that have not applied for recognition of tax-exempt status are not included in the publication. Only the parent organization in a group ruling is included by name in Publication 78.

If you have questions about listing an organization, correcting an erroneous entry, or deleting a listing in Publication 78, contact EO Customer Account Services toll-free at (877) 829-5500.

# Jeopardizing Tax-Exempt Status

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All IRC section 501(c)(3) organizations, including churches and religious organizations, must abide by certain rules:

- their net earnings may not inure to any private shareholder or individual,
- they must not provide a substantial benefit to private interests,
- they must not devote a substantial part of their activities to attempting to influence legislation,
- they must not participate in, or intervene in, any political campaign on behalf of (or in opposition to) any candidate for public office, and
- the organization's purposes and activities may not be illegal or violate fundamental public policy.

## Inurement and Private Benefit

### Inurement to Insiders

Churches and religious organizations, like all exempt organizations under IRC section 501(c)(3), are prohibited from engaging in activities that result in inurement of the church's or organization's income or assets to insiders (i.e., persons having a personal and private interest in the activities of the organization). *Insiders* could include the minister, church board members, officers, and in certain circumstances, employees. Examples of prohibited inurement include the payment of dividends, the payment of unreasonable compensation to insiders, and transferring property to insiders for less than fair market value. The prohibition against inurement to insiders is absolute; therefore, any amount of inurement is, potentially, grounds for loss of tax-exempt status. In addition, the insider involved may be subject to excise tax. See the following section on *Excess benefit transactions*. Note that prohibited inurement does not include reasonable payments for services rendered, payments that further tax-exempt purposes, or payments made for the fair market value of real or personal property.

***Excess benefit transactions.*** In cases where an IRC section 501(c)(3) organization provides an excess economic benefit to an insider, both the organization and the insider have engaged in an *excess benefit transaction*. The IRS may impose an excise tax on any insider who improperly benefits from an excess benefit transaction, as well as on organization managers who participate in such a transaction knowing that it is improper. An insider who benefits from an excess benefit transaction is also required to return the excess benefits to the organization. Detailed rules on excess benefit transactions are contained in the Code of Federal Regulations, Title 26, sections 53.4958-0 through 53.4958-8.

### Private Benefit

An IRC section 501(c)(3) organization's activities must be directed exclusively toward charitable, educational, religious, or other exempt purposes. Such an organization's activities may not serve the private interests of any individual or organization. Rather, beneficiaries of an organization's activities must be recognized objects of charity (such as the poor or the distressed) or the community at large (for example, through the conduct of religious services or the promotion of religion). Private benefit is different from inurement to insiders. Private benefit may occur even if the persons benefited are not insiders. Also, private benefit must be substantial in order to jeopardize tax-exempt status.

## Substantial Lobbying Activity

In general, no organization, including a church, may qualify for IRC section 501(c)(3) status if a substantial part of its activities is attempting to influence legislation (commonly known as lobbying). An IRC section 501(c)(3) organization may engage in some lobbying, but too much lobbying activity risks loss of tax-exempt status.

*Legislation* includes action by Congress, any state legislature, any local council, or similar governing body, with respect to acts, bills, resolutions, or similar items (such as legislative confirmation of appointive offices), or by the public in a referendum, ballot initiative, constitutional amendment, or similar procedure. It does not include actions by executive, judicial, or administrative bodies.

A church or religious organization will be regarded as *attempting to influence legislation* if it contacts, or urges the public to contact, members or employees of a legislative body for the purpose of proposing, supporting, or opposing legislation, or if the organization advocates the adoption or rejection of legislation.

Churches and religious organizations may, however, involve themselves in issues of public policy without the activity being considered as lobbying. For example, churches may conduct educational meetings, prepare and distribute educational materials, or otherwise consider public policy issues in an educational manner without jeopardizing their tax-exempt status.

### **Measuring Lobbying Activity**

***Substantial part test.*** Whether a church's or religious organization's attempts to influence legislation constitute a substantial part of its overall activities is determined on the basis of all the pertinent facts and circumstances in each case. The IRS considers a variety of factors, including the time devoted (by both compensated and volunteer workers) and the expenditures devoted by the organization to the activity, when determining whether the lobbying activity is substantial. Churches must use the substantial part test since they are not eligible to use the expenditure test described in the next section.

***Consequences of excessive lobbying activity.*** Under the *substantial part test*, a church or religious organization that conducts excessive lobbying activity in any taxable year may lose its tax-exempt status, resulting in all of its income being subject to tax. In addition, a

religious organization is subject to an excise tax equal to five percent of its lobbying expenditures for the year in which it ceases to qualify for exemption. Further, a tax equal to five percent of the lobbying expenditures for the year may be imposed against organization managers, jointly and severally, who agree to the making of such expenditures knowing that the expenditures would likely result in loss of tax-exempt status.

***Expenditure test.*** Although churches are not eligible, religious organizations may elect the expenditure test under IRC section 501(h) as an alternative method for measuring lobbying activity. Under the expenditure test, the extent of an organization's lobbying activity will not jeopardize its tax-exempt status, provided its expenditures, related to such activity, do not normally exceed an amount specified in IRC section 4911. This limit is generally based upon the size of the organization and may not exceed \$1,000,000.

Religious organizations electing to use the expenditure test must file IRS Form 5768, *Election/Revocation of Election by an Eligible IRC Section 501(c)(3) Organization To Make Expenditures To Influence Legislation*, at any time during the tax year for which it is to be effective. The election remains in effect for succeeding years unless it is revoked by the organization. Revocation of the election is effective beginning with the year following the year in which the revocation is filed. Religious organizations may wish to consult their tax advisors to determine their eligibility for, and the advisability of, electing the expenditure test.

***Consequences of excessive lobbying activity.*** Under the *expenditure test*, a religious organization that engages in excessive lobbying activity over a four-year period may lose its tax-exempt status, making all of its income for that period subject to tax. Should the organization exceed its lobbying expenditure dollar limit in a particular year, it must pay an excise tax equal to 25 percent of the excess.



## Political Campaign Activity

Under the Internal Revenue Code, all IRC section 501(c)(3) organizations, including churches and religious organizations, are absolutely prohibited from directly or indirectly participating in, or intervening in, any political campaign on behalf of (or in opposition to) any candidate for elective public office. Contributions to political campaign funds or public statements of position (verbal or written) made by or on behalf of the organization in favor of or in opposition to any candidate for public office clearly violate the prohibition against political campaign activity. Violation of this prohibition may result in denial or revocation of tax-exempt status and the imposition of certain excise tax.

Certain activities or expenditures may not be prohibited depending on the facts and circumstances. For example, certain voter education activities (including the presentation of public forums and the publication of voter education guides) conducted in a non-partisan manner do not constitute prohibited political campaign activity. In addition, other activities intended to encourage people to participate in the electoral process, such as voter registration and get-out-the-vote drives, would not constitute prohibited political campaign activity if conducted in a non-partisan manner. On the other hand, voter education or registration activities with evidence of bias that: (a) would favor one candidate over another; (b) oppose a candidate in some manner; or (c) have the effect of favoring a candidate or group of candidates, will constitute prohibited participation or intervention.

### Individual Activity by Religious Leaders

The political campaign activity prohibition is not intended to restrict free expression on political matters by leaders of churches or religious organizations speaking for themselves, as *individuals*. Nor are leaders prohibited from speaking about important issues of public

policy. However, for their organizations to remain tax exempt under IRC section 501(c)(3), religious leaders cannot make partisan comments in official organization publications or at official church functions. To avoid potential attribution of their comments outside of church functions and publications, religious leaders who speak or write in their individual capacity are encouraged to clearly indicate that their comments are personal and not intended to represent the views of the organization. The following are examples of situations involving endorsements by religious leaders.

**Example 1:** Minister A is the minister of Church J, a section 501(c)(3) organization, and is well known in the community. With their permission, Candidate T publishes a full-page ad in the local newspaper listing five prominent ministers who have personally endorsed Candidate T, including Minister A. Minister A is identified in the ad as the minister of Church J. The ad states, “Titles and affiliations of each individual are provided for identification purposes only.” The ad is paid for by Candidate T’s campaign committee. Since the ad was not paid for by Church J, the ad is not otherwise in an official publication of Church J, and the endorsement is made by Minister A in a personal capacity, the ad does not constitute campaign intervention by Church J.

**Example 2:** Minister B is the minister of Church K, a section 501(c)(3) organization, and is well known in the community. Three weeks before the election, he attends a press conference at Candidate V’s campaign headquarters and states that Candidate V should be reelected. Minister B does not say he is speaking on behalf of Church K. His endorsement is reported on the front page of the local newspaper and he is identified in the article as the minister of Church K. Because Minister B did not make the endorsement at an official church function, in an official church publication or otherwise use the church’s assets, and did not state that he was speaking as a representative of Church K, his actions do not constitute campaign intervention by Church K.

**Example 3:** Minister C is the minister of Church I, a section 501(c)(3) organization. Church I publishes a monthly church newsletter that is distributed to all church members. In each issue, Minister C has a column titled “My Views.” The month before the election, Minister C states in the “My Views” column, “It is my personal opinion that Candidate U should be reelected.” For that one issue, Minister C pays from his personal funds the portion of the cost of the newsletter attributable to the “My Views” column. Even though he paid part of the cost of the newsletter, the newsletter is an official publication of the church. Because the endorsement appeared in an official publication of Church I, it constitutes campaign intervention attributed to Church I.

**Example 4:** Minister D is the minister of Church M, a section 501(c)(3) organization. During regular services of Church M shortly before the election, Minister D preached on a number of issues, including the importance of voting in the upcoming election, and concluded by stating, “It is important that you all do your duty in the election and vote for Candidate W.” Because Minister D’s remarks indicating support for Candidate W were made during an official church service, they constitute political campaign intervention by to Church M.

### **Issue Advocacy vs. Political Campaign Intervention**

Like other section 501(c)(3) organizations, some churches and religious organizations take positions on public policy issues, including issues that divide candidates in an election for public office. However, section 501(c)(3) organizations must avoid any issue advocacy that functions as political campaign intervention. Even if a statement does not expressly tell an audience to vote for or against a specific candidate, an organization delivering the statement is at risk of violating the political campaign intervention prohibition if there is any message favoring or opposing a candidate. A statement can identify a candidate not only by stating the candidate’s name but also by other means such as showing a picture of the candidate, referring to political party affiliations, or other distinctive features of a candidate’s platform or biography. All the facts and circumstances need to be considered to determine if the advocacy is political campaign intervention.

Key factors in determining whether a communication results in political campaign intervention include the following:

- whether the statement identifies one or more candidates for a given public office,
- whether the statement expresses approval or disapproval for one or more candidates’ positions and/or actions,
- whether the statement is delivered close in time to the election,
- whether the statement makes reference to voting or an election,
- whether the issue addressed in the communication has been raised as an issue distinguishing candidates for a given office,
- whether the communication is part of an ongoing series of communications by the organization on the same issue that are made independent of the timing of any election, and
- whether the timing of the communication and identification of the candidate are related to a non-electoral event such as a scheduled vote on specific legislation by an officeholder who also happens to be a candidate for public office.

A communication is particularly at risk of political campaign intervention when it makes reference to candidates or voting in a specific upcoming election. Nevertheless, the communication must still be considered in context before arriving at any conclusions.

**Example 1:** Church O, a section 501(c)(3) organization, prepares and finances a full page newspaper advertisement that is published in several large circulation newspapers in State V shortly before an election in which Senator C is a candidate for nomination in a party primary. Senator C is the incumbent candidate in a party primary. The advertisement states that a pending bill in the United States Senate would provide additional opportunities for State V residents to participate in faith-based programs by providing funding to such church-affiliated programs. The advertisement ends with the statement “Call or write Senator C to tell him to vote for this

bill, despite his opposition in the past.” Funding for faith-based programs has not been raised as an issue distinguishing Senator C from any opponent. The bill is scheduled for a vote before the election. The advertisement identifies Senator C’s position as contrary to O’s position. Church O has not violated the political campaign intervention prohibition: The advertisement does not mention the election or the candidacy of Senator C or distinguish Senator C from any opponent. The timing of the advertising and the identification of Senator C are directly related to a vote on the identified legislation. The candidate identified, Senator C, is an officeholder who is in a position to vote on the legislation.

**Example 2:** Church R, a section 501(c)(3) organization, prepares and finances a radio advertisement urging an increase in state funding for faith-based education in State X, which requires a legislative appropriation. Governor E is the governor of State X. The radio advertisement is first broadcast on several radio stations in State X beginning shortly before an election in which Governor E is a candidate for re-election. The advertisement is not part of an ongoing series of substantially similar advocacy communications by Church R on the same issue. The advertisement cites numerous statistics indicating that faith-based education in State X is underfunded. Although the advertisement does not say anything about Governor E’s position on funding for faith-based education, it ends with “Tell Governor E what you think about our under-funded schools.” In public appearances and campaign literature, Governor E’s opponent has made funding of faith-based education an issue in the campaign by focusing on Governor E’s veto of an income tax increase to increase funding for faith-based education. At the time the advertisement is broadcast, no legislative vote or other major legislative activity is scheduled in the State X legislature on state funding of faith-based education. Church R has violated the political campaign prohibition: The advertisement identifies Governor E, appears shortly before an election in which Governor E is a candidate, is not part of an ongoing series of substantially similar advocacy communications by Church R on the same issue, is not timed to coincide with a non-election event such as a legislative vote or other major legislative action on that issue, and takes a position on an issue that the opponent has used to distinguish himself from Governor E.

**Example 3:** Candidate A and Candidate B are candidates for the state senate in District W of State X. The issue of State X funding for a faith-based indigent hospital care in District W is a prominent issue in the campaign. Both candidates have spoken out on the issue. Candidate A supports funding such care; Candidate B opposes the project and supports increasing State X funding for public hospitals instead. P is the head of the board of elders at Church C, a section 501(c)(3) organization located in District W. At C’s annual fundraising dinner in District W, which takes place in the month before the election, P gives a long speech about health care issues, including the issue of funding for faith-based programs. P does not mention the name of any candidate or any political party. However, at the end of the speech, P makes the following statement, “For those of you who care about quality of life in District W and the desire of our community for health care responsive to their faith, there is a very important choice coming up next month. We need more funding for health care. Increased public hospital funding will not make a difference. You have the power to respond to the needs of this community. Use that power when you go to the polls and cast your vote in the election for your state senator.” C has violated the political campaign intervention prohibition as a result of P’s remarks at C’s official function shortly before the election, in which P referred to the upcoming election after stating a position on an issue that is a prominent issue in a campaign that distinguishes the candidates.

### **Inviting a Candidate to Speak**

Depending on the facts and circumstances, a church or religious organization may invite political candidates to speak at its events without jeopardizing its tax-exempt status. Political candidates may be invited in their capacity as candidates, or individually (not as a candidate). Candidates may also appear without an invitation at organization events that are open to the public.

**Speaking as a candidate.** Like any other IRC section 501(c)(3) organization, when a candidate is invited to speak at a church or religious organization event as a political candidate, factors in determining whether the organization participated or intervened in a political campaign include the following:

- whether the church provides an equal opportunity to the political candidates seeking the same office,
- whether the church indicates any support of or opposition to the candidate. (This should be stated explicitly when the candidate is introduced and in communications concerning the candidate's appearance.)
- whether any political fundraising occurs,
- whether the individual is chosen to speak solely for reasons other than candidacy for public office,
- whether the organization maintains a nonpartisan atmosphere on the premises or at the event where the candidate is present, and
- whether the organization clearly indicates the capacity in which the candidate is appearing and does not mention the individual's political candidacy or the upcoming election in the communications announcing the candidate's attendance at the event.

**Equal opportunity to participate.** Like any other IRC section 501(c)(3) organization, in determining whether candidates are given an equal opportunity to participate, a church or religious organization should consider the nature of the event to which each candidate is invited, in addition to the manner of presentation. For example, a church or religious organization that invites one candidate to speak at its well attended annual banquet, but invites the opposing candidate to speak at a sparsely attended general meeting, will likely be found to have violated the political campaign prohibition, even if the manner of presentation for both speakers is otherwise neutral.

**Public forum.** Sometimes a church or religious organization invites several candidates to speak at a public forum. A public forum involving several candi-

dates for public office may qualify as an exempt educational activity. However, if the forum is operated to show a bias for or against any candidate, then the forum would be prohibited campaign activity, as it would be considered intervention or participation in a political campaign. When an organization invites several candidates to speak at a forum, it should consider the following factors:

- whether questions for the candidate are prepared and presented by an independent nonpartisan panel,
- whether the topics discussed by the candidates cover a broad range of issues that the candidates would address if elected to the office sought and are of interest to the public,
- whether each candidate is given an equal opportunity to present his or her views on the issues discussed,
- whether the candidates are asked to agree or disagree with positions, agendas, platforms or statements of the organization, and
- whether a moderator comments on the questions or otherwise implies approval or disapproval of the candidates.

A candidate may seek to reassure the organization that it is permissible for the organization to do certain things in connection with the candidate's appearance. An organization in this position should keep in mind that the candidate may not be familiar with the organization's tax-exempt status and that the candidate may be focused on compliance with the election laws that apply to the candidate's campaign rather than the federal tax law that applies to the organization. The organization will be in the best position to ensure compliance with the prohibition on political campaign intervention if it makes its own independent conclusion about its compliance with federal tax law.

The following are examples of situations where a church or religious organization invites a candidate(s) to speak before the congregation.



**Example 1:** Minister E is the minister of Church N, a section 501(c)(3) organization. In the month prior to the election, Minister E invited the three Congressional candidates for the district in which Church N is located to address the congregation, one each on three successive Sundays, as part of regular worship services. Each candidate was given an equal opportunity to address and field questions on a wide variety of topics from the congregation. Minister E's introduction of each candidate included no comments on their qualifications or any indication of a preference for any candidate. The actions do not constitute political campaign intervention by Church N.

**Example 2:** The facts are the same as in the preceding example except that there are four candidates in the race rather than three, and one of the candidates declines the invitation to speak. In the publicity announcing the dates for each of the candidate's speeches, Church N includes a statement that the order of the speakers was determined at random and the fourth candidate declined the church's invitation to speak. Minister E makes the same statement in his opening remarks at each of the meetings where one of the candidates is speaking. Church N's actions do not constitute political campaign intervention.

**Example 3:** Minister F is the minister of Church O, a section 501(c)(3) organization. The Sunday before the November election, Minister F invited Senate Candidate X to preach to her congregation during worship services. During his remarks, Candidate X stated, "I am asking not only for your votes, but for your enthusiasm and dedication, for your willingness to go the extra mile to get a very large turnout on Tuesday." Minister F invited no other candidate to address her congregation during the Senatorial campaign. Because these activities took place during official church services, they are attributed to Church O. By selectively providing church facilities to allow Candidate X to speak in support of his campaign, Church O's actions constitute political campaign intervention.

**Speaking as a non-candidate.** Like any other IRC section 501(c)(3) organization, a church or religious organization may invite political candidates (including church members) to speak in a non-candidate capacity.

For instance, a political candidate may be a public figure because he or she: (a) currently holds, or formerly held, public office; (b) is considered an expert in a non-political field; or (c) is a celebrity or has led a distinguished military, legal, or public service career. A candidate may choose to attend an event that is open to the public, such as a lecture, concert or worship service. The candidate's presence at a church-sponsored event does not, by itself, cause the organization to be involved in political campaign intervention. However, if the candidate is publicly recognized by the organization, or if the candidate is invited to speak, factors in determining whether the candidate's appearance results in political campaign intervention include the following:

- whether the individual speaks only in a non-candidate capacity,
- whether either the individual nor any representative of the church makes any mention of his or her candidacy or the election,
- whether any campaign activity occurs in connection with the candidate's attendance.
- whether the individual is chosen to speak solely for reasons other than candidacy for public office,
- whether the organization maintains a nonpartisan atmosphere on the premises or at the event where the candidate is present, and
- whether the organization clearly indicates the capacity in which the candidate is appearing and does not mention the individual's political candidacy or the upcoming election in the communications announcing the candidate's attendance at the event.

In addition, the church or religious organization should clearly indicate the capacity in which the candidate is appearing and should not mention the individual's political candidacy or the upcoming election in the communications announcing the candidate's attendance at the event.

Below are examples of situations where a public official appears at a church or religious organization in an official capacity, and not as a candidate.

**Example 1:** Church P, a section 501(c)(3) organization, is located in the state capital. Minister G customarily acknowledges the presence of any public officials present during services. During the state gubernatorial race, Lieutenant Governor Y, a candidate, attended a Wednesday evening prayer service in the church. Minister G acknowledged the Lieutenant Governor's presence in his customary manner, saying, "We are happy to have worshiping with us this evening Lieutenant Governor Y." Minister G made no reference in his welcome to the Lieutenant Governor's candidacy or the election. Minister G's actions do not constitute political campaign intervention by Church P.

**Example 2:** Minister H is the minister of Church Q, a section 501(c)(3) organization. Church Q is building a community center. Minister H invites Congressman Z, the representative for the district containing Church Q, to attend the groundbreaking ceremony for the community center. Congressman Z is running for reelection at the time. Minister H makes no reference in her introduction to Congressman Z's candidacy or the election. Congressman Z also makes no reference to his candidacy or the election and does not do any fundraising while at Church Q. Church Q has not intervened in a political campaign.

**Example 3:** Church X is a section 501(c)(3) organization. X publishes a member newsletter on a regular basis. Individual church members are invited to send in updates about their activities which are printed in each edition of the newsletter. After receiving an update letter from Member Q, X prints the following: "Member Q is running for city council in Metropolis." The newsletter does not contain any reference to this election or to Member Q's candidacy other than this statement of fact. Church X has not intervened in a political campaign.

**Example 4:** Mayor G attends a concert performed by a choir of Church S, a section 501(c)(3) organization, in City Park. The concert is free and open to the public. Mayor G is a candidate for reelection, and the concert takes place after the primary and before

the general election. During the concert, S's minister addresses the crowd and says, "I am pleased to see Mayor G here tonight. Without his support, these free concerts in City Park would not be possible. We will need his help if we want these concerts to continue next year so please support Mayor G in November as he has supported us." As a result of these remarks, Church S has engaged in political campaign intervention.

### **Voter Education, Voter Registration and Get-Out-the-Vote Drives**

Section 501(c)(3) organizations are permitted to conduct certain voter education activities (including the presentation of public forums and the publication of voter education guides) if they are carried out in a non-partisan manner. In addition, section 501(c)(3) organizations may encourage people to participate in the electoral process through voter registration and get-out-the-vote drives, conducted in a non-partisan manner. On the other hand, voter education or registration activities conducted in a biased manner that favors (or opposes) one or more candidates is prohibited.

Like other IRC section 501(c)(3) organizations, some churches and religious organizations undertake voter education activities by distributing *voter guides*. Voter guides, generally, are distributed during an election campaign and provide information on how all candidates stand on various issues. These guides may be distributed with the purpose of educating voters; however, they may not be used to attempt to favor or oppose candidates for public elected office.

A careful review of the following facts and circumstances may help determine whether or not a church or religious organization's publication or distribution of voter guides constitutes prohibited political campaign activity:

- whether the candidates' positions are compared to the organization's position,
- whether the guide includes a broad range of issues that the candidates would address if elected to the office sought,
- whether the description of issues is neutral,

- whether all candidates for an office are included, and
- whether the descriptions of candidates' positions are either:
  - the candidates' own words in response to questions, or
  - a neutral, unbiased and complete compilation of all candidates' positions.

The following are examples of church voter education and voter registration activities.

*Example 1:* Church R, a section 501(c)(3) organization, distributes a voter guide prior to elections. The voter guide consists of a brief statement from the candidates on each issue made in response to a questionnaire sent to all candidates for governor of State I. The issues on the questionnaire cover a wide variety of topics and were selected by Church R based solely on their importance and interest to the electorate as a whole. Neither the questionnaire nor the voter guide, through their content or structure, indicate a bias or preference for any candidate or group of candidates. Church R is not participating or intervening in a political campaign.

*Example 2:* Church S, a section 501(c)(3) organization, distributes a voter guide during an election campaign. The voter guide is prepared using the responses of candidates to a questionnaire sent to candidates for major public offices. Although the questionnaire covers a wide range of topics, the wording of the questions evidences a bias on certain issues. By using a questionnaire structured in this way, Church S is participating or intervening in a political campaign.

*Example 3:* Church T, a section 501(c)(3) organization, sets up a booth at the state fair where citizens can register to vote. The signs and banners in and around the booth give only the name of the church, the date of the next upcoming statewide election, and notice of the opportunity to register. No reference to any candidate or political party is made by volunteers staffing the booth or in the materials available in the booth, other than the official voter registration forms which allow registrants to select a party affiliation. Church T is not engaged in political campaign intervention when it operates this voter registration booth.

*Example 4:* Church C is a section 501(c)(3) organization. C's activities include educating its members on family issues involving moral values. Candidate G is running for state legislature and an important element of her platform is challenging the incumbent's position on family issues. Shortly before the election, C sets up a telephone bank to call registered voters in the district in which Candidate G is seeking election. In the phone conversations, C's representative tells the voter about the moral importance of family issues and asks questions about the voter's views on these issues. If the voter appears to agree with the incumbent's position, C's representative thanks the voter and ends the call. If the voter appears to agree with Candidate G's position, C's representative reminds the voter about the upcoming election, stresses the importance of voting in the election and offers to provide transportation to the polls. C is engaged in political campaign intervention when it conducts this get-out-the-vote drive.

### **Business Activity**

The question of whether an activity constitutes participation or intervention in a political campaign may also arise in the context of a business activity of the church or religious organization, such as the selling or renting of mailing lists, the leasing of office space, or the acceptance of paid political advertising. (The tax treatment of income from such unrelated business activities follows.) In this context, some of the factors to be considered in determining whether the church or religious organization has engaged in prohibited political campaign activity include the following:

- whether the good, service, or facility is available to the candidates on an equal basis,
- whether the good, service, or facility is available only to candidates and not to the general public,
- whether the fees charged are at the organization's customary and usual rates, and
- whether the activity is an ongoing activity of the organization or whether it is conducted only for the candidate.

**Example 1:** Church K is a section 501(c)(3) organization. It owns a building that has a large basement hall suitable for hosting dinners and receptions. For several years, Church K has made the hall available for rent to members of the public. It has standard fees for renting the hall based on the number of people in attendance, and a number of different organizations have rented the hall. Church K rents the hall on a first come, first served basis. Candidate P's campaign pays the standard fee for the dinner. Church K is not involved in political campaign intervention as a result of renting the hall to Candidate P for use as the site of a campaign fundraising dinner.

**Example 2:** Church L is a section 501(c)(3) organization. It maintains a mailing list of all of its members. Church L has never rented the mailing list to a third party. The campaign committee of Candidate Q, who supports funding for faith-based programs, approaches Church L. Candidate A's campaign committee offers to rent Church L's mailing list for a fee that is comparable to fees charged by other similar organizations. Church L rents the list to Candidate A's campaign committee, but declines similar requests from campaign committees of other candidates. Church L has intervened in a political campaign.

**Web Sites:** The Internet has become a widely used communications tool. Section 501(c)(3) organizations use their own web sites to disseminate statements and information. They also routinely link their web sites to web sites maintained by other organizations as a way of providing additional information that the organizations believe is useful or relevant to the public.

A web site is a form of communication. If an organization posts something on its web site that favors or opposes a candidate for public office, the organization will be treated the same as if it distributed printed material, oral statements or broadcasts that favored or opposed a candidate.

An organization has control over whether it establishes a link to another site. When an organization establishes a link to another web site, the organization is responsible for the consequences of establishing and maintaining that link, even if the organization does not have control

over the content of the linked site. Because the linked content may change over time, an organization may reduce the risk of political campaign intervention by monitoring the linked content and adjusting the links accordingly.

Links to candidate-related material, by themselves, do not necessarily constitute political campaign intervention. All the facts and circumstances must be taken into account when assessing whether a link produces that result. The facts and circumstances to be considered include, but are not limited to, the context for the link on the organization's web site, whether all candidates are represented, any exempt purpose served by offering the link, and the directness of the links between the organization's web site and the web page that contains material favoring or opposing a candidate for public office.

**Example 1.** Church P, a section 501(c)(3) organization, maintains a web site that includes such information as biographies of its ministers, times of services, details of community outreach programs, and activities of members of its congregation. B, a member of the congregation of Church P, is running for a seat on the town council. Shortly before the election, Church P posts the following message on its web site, "Lend your support to B, your fellow parishioner, in Tuesday's election for town council." Church P has intervened in a political campaign on behalf of B.

**Example 2.** Church N, a section 501(c)(3) organization, maintains a web site that includes such information as staff listings, directions to the church, and descriptions of its community outreach programs, schedules of services, and school activities. On one page of the web site, Church N describes a particular type of treatment program for homeless veterans. This section includes a link to an article on the web site of O, a major national newspaper, praising Church N's treatment program for homeless veterans. The page containing the article on O's web site does not refer to any candidate or election and has no direct links to candidate or election information. Elsewhere on O's web site, there is a page displaying editorials that O has published. Several of the editorials endorse candidates in an election that has not yet occurred. Church N has not intervened in a political campaign by maintaining a link on O's



web site because the link is provided for the exempt purpose of educating the public about its programs; the context for the link, the relationship between Church N and O, and the arrangement of the links going from Church N's web site to the endorsement on O's web site, do not indicate that Church N was favoring or opposing any candidate.

**Example 3:** Church M, a section 501(c)(3) organization, maintains a web site and posts an unbiased, nonpartisan voter guide that is prepared in accordance with the principles discussed on pages 12 and 13 of this publication. For each candidate covered in the voter guide, M includes a link to that candidate's official campaign web site. The links to the candidate web sites are presented on a consistent, neutral basis for each candidate, with text saying "For more information on Candidate X, you may consult [URL]." M has not intervened in a political campaign because the links are provided for the exempt purpose of educating voters and are presented in a neutral, unbiased manner that includes all candidates for a particular office.

### Consequences of Political Campaign Activity

When it participates in political campaign activity, a church or religious organization jeopardizes both its tax-exempt status under IRC section 501(c)(3) and its eligibility to receive tax-deductible contributions. In addition, it may become subject to an excise tax on its political expenditures. This *excise tax* may be imposed in addition to revocation, or it may be imposed instead of revocation. Also, the church or religious organization should correct the violation.

**Excise tax.** An initial tax is imposed on an organization at the rate of 10 percent of the political expenditures. Also, a tax at the rate of 2.5 percent of the expenditures is imposed against the organization managers (jointly and severally) who, without reasonable cause, agreed to the expenditures knowing they were political expenditures. The tax on management may not exceed \$5,000 with

respect to any one expenditure.

In any case in which an initial tax is imposed against an organization, and the expenditures are not corrected within the period allowed by law, an additional tax equal to 100 percent of the expenditures is imposed against the organization. In that case, an additional tax is also imposed against the organization managers (jointly and severally) who refused to agree to make the correction. The additional tax on management is equal to 50 percent of the expenditures and may not exceed \$10,000 with respect to any one expenditure.

**Correction.** Correction of a political expenditure requires the recovery of the expenditure, to the extent possible, and establishment of safeguards to prevent future political expenditures.

Please note that a church or religious organization that engages in any political campaign activity also needs to determine whether it is in compliance with the appropriate federal, state or local election laws, as these may differ from the requirements under IRC section 501(c)(3).

# Unrelated Business Income Tax (UBIT)

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## Net Income Subject to the UBIT

Churches and religious organizations, like other tax-exempt organizations, may engage in income-producing activities unrelated to their tax-exempt purposes, as long as the unrelated activities are not a substantial part of the organization's activities. However, the net income from such activities will be subject to the UBIT if the following three conditions are met:

- the activity constitutes a trade or business,
- the trade or business is regularly carried on, and
- the trade or business is not substantially related to the organization's exempt purpose. (The fact that the organization uses the income to further its charitable or religious purposes does not make the activity substantially related to its exempt purposes.)

### Exceptions to UBIT

Even if an activity meets the above three criteria, the income may not be subject to tax if it meets one of the following exceptions: (a) substantially all of the work in operating the trade or business is performed by volunteers; (b) the activity is conducted by the organization primarily for the convenience of its members; or (c) the trade or business involves the selling of merchandise substantially all of which was donated.

In general, rents from real property, royalties, capital gains, and interest and dividends are not subject to the unrelated business income tax unless financed with borrowed money.

## Examples of Unrelated Trade or Business Activities

Unrelated trade or business activities vary depending on types of activities, as shown below.

### Advertising

Many tax-exempt organizations sell advertising in their publications or other forms of public communication. Generally, income from the sale of advertising is unrelated trade or business income. This may include the sale of advertising space in weekly bulletins, magazines or journals, or on church or religious organization Web sites.

### Gaming

Most forms of gaming, if regularly carried on, may be considered the conduct of an unrelated trade or business. This can include the sale of pull-tabs and raffles. Income derived from bingo games may be eligible for a special tax exception (in addition to the exception regarding uncompensated volunteer labor covered above), if the following conditions are met: (a) the bingo game is the traditional type of bingo (as opposed to instant bingo, a variation of pull-tabs); (b) the conduct of the bingo game is not an activity carried out by for-profit organizations in the local area; and (c) the operation of the bingo game does not violate any state or local law.

### Sale of merchandise and publications

The sale of merchandise and publications (including the actual publication of materials) can be considered the conduct of an unrelated trade or business if the items involved do not have a substantial relationship to the exempt purposes of the organization.

### Rental income

Generally, income derived from the rental of real property and incidental personal property is excluded from unrelated business income. However, there are certain situations in which rental income may be unrelated business taxable income:

- if a church rents out property on which there is debt outstanding (for example, a mortgage note), the rental income may constitute unrelated debt-financed income subject to UBIT. (However, if a church or convention or association of churches acquires debt-financed land for use in its exempt purposes within 15 years of the time of acquisition, then income from the rental of the land may not constitute unrelated business income.),
- if personal services are rendered in connection with the rental, then the income may be unrelated business taxable income, or
- if a church charges for the use of the parking lot, the income may be unrelated business taxable income.

### Parking lots

If a church owns a parking lot that is used by church members and visitors while attending church services, any parking fee paid to the church would not be subject to UBIT. However, if a church operates a parking lot that is used by members of the general public, parking fees would be taxable, as this activity would not be substantially related to the church's exempt purpose, and parking fees are not treated as rent from real property. If the church enters into a lease with a third party who operates the church's parking lot and pays rent to the church, such payments would not be subject to tax, as they would constitute rent from real property.

Whether an income-producing activity is an unrelated trade or business activity depends on all the facts and circumstances. For more information, see IRS Publication 598, *Tax on Unrelated Business Income of Exempt Organizations*.

### Tax on Income-Producing Activities

If a church, or other exempt organization, has gross income of \$1,000 or more for any taxable year from the conduct of any unrelated trade or business, it is required to file IRS Form 990-T, *Exempt Organization Business Income Tax Return*, for that year. If the church is part of a larger entity (such as a diocese), it must file a separate Form 990-T if it has a separate EIN. Form 990-T is due the 15th day of the 5th month following the end of the church's tax year. (IRC section 512(b)(12) provides a special rule for parishes and similar local units of a church. A specific deduction is provided, which is equal to the lower of \$1,000 or the gross income derived from any unrelated trade or business regularly carried on by such parish or local unit of a church.) See Filing Requirements on page 19.

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# Employment Tax

Generally, churches and religious organizations are required to withhold, report, and pay income and Federal Insurance Contributions Act (FICA) taxes for their employees. Employment tax includes income tax withheld and paid for an employee and FICA taxes withheld and paid on behalf of an employee. Substantial penalties may be imposed against an organization that fails to withhold and pay the proper employment tax. Whether a church or religious organization must withhold and pay employment tax depends upon whether the church's workers are employees. *Determination of worker status* is important. Several facts determine whether a worker is an employee. For an in-depth explanation and examples of the common law employer-employee relationship, see IRS Publication 15-A, *Employer's Supplemental Tax Guide*. If a church or a worker wants the IRS to determine whether the worker is an employee, the church or worker should file IRS Form SS-8, *Determination of Employee Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding*, with the IRS.

## Social Security and Medicare Taxes — Federal Insurance Contributions Act (FICA)

FICA taxes consist of Social Security and Medicare taxes. Wages paid to employees of churches or religious organizations are subject to FICA taxes unless *one* of the following exceptions applies:

- wages are paid for services performed by a duly ordained, commissioned, or licensed minister of a church in the exercise of his or her ministry, or by a member of a religious order in the exercise of duties required by such order;

- the church or religious organization pays the employee wages of less than \$108.28 in a calendar year, or
- a church that is opposed to the payment of Social Security and Medicare taxes for religious reasons files IRS Form 8274, *Certification by Churches and Qualified Church Controlled Organizations Electing Exemption From Employer Social Security and Medicare Taxes*. Very specific timing rules apply to filing Form 8274. It must be filed before the *first* date on which the electing entity is required to file its first quarterly employment tax return. This election does not relieve the organization of its obligation to withhold income tax on wages paid to its employees. In addition, if such an election is made, affected employees must pay Self-Employment Contributions Act (SECA) tax. For further information, see Publication 517, *Social Security and Other Information for Members of the Clergy and Religious Workers*.

Withheld employee income tax and FICA taxes are reported on IRS Form 941, *Employer's Quarterly Federal Tax Return*. Some small employers are eligible to file an annual Form 944 instead of quarterly returns. See the instructions to Form 944 for more information. For more information about employment tax, see IRS Publication 15, *Circular E, Employer's Tax Guide*, and IRS Publication 15-A, *Employer's Supplemental Tax Guide*. See also, IRS Publication 517, *Social Security and Other Information for Members of the Clergy and Religious Workers*.

## Federal Unemployment Tax Act (FUTA)

Churches and religious organizations are not liable for FUTA tax. For further information on FUTA, see IRS Publication 517, *Social Security and Other Information for Members of the Clergy and Religious Workers*.



# Special Rules for Compensation of Ministers

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## Withholding Income Tax for Ministers

Unlike other exempt organizations or businesses, a church is not required to withhold income tax from the compensation that it pays to its duly ordained, commissioned, or licensed ministers for performing services in the exercise of their ministry. An employee minister may, however, enter into a voluntary withholding agreement with the church by completing IRS Form W-4, *Employee's Withholding Allowance Certificate*. A church should report compensation paid to a minister on Form W-2, *Wage and Tax Statement*, if the minister is an employee, or on IRS Form 1099-MISC, *Miscellaneous Income*, if the minister is an independent contractor.

## Parsonage or Housing Allowances

Generally, a minister's gross income does not include the fair rental value of a home (parsonage) provided, or a housing allowance paid, as part of the minister's compensation for services performed that are ordinarily the duties of a minister.

A minister who is furnished a *parsonage* may exclude from income the fair rental value of the parsonage, including utilities. However, the amount excluded cannot be more than the reasonable pay for the minister's services.

A minister who receives a *housing allowance* may exclude the allowance from gross income to the extent it is used to pay expenses in providing a home. Generally, those expenses include rent, mortgage payments, utilities, repairs, and other expenses directly relating to providing a home. If a minister owns a home, the amount excluded from the minister's gross income as a housing allowance is limited to the least of the following: (a) the amount actually used to provide a home; (b) the amount officially designated as a housing allowance; or (c) the fair rental value of the home. The minister's church or other qualified organization must designate the housing allowance pursuant to official action taken *in advance* of the payment. If a minister is employed and paid by a local congregation, a designation by a national church

agency will not be effective. The local congregation must make the designation. A national church agency may make an effective designation for ministers it directly employs. If none of the minister's salary has been officially designated as a housing allowance, the full salary must be included in gross income.

The fair rental value of a parsonage or housing allowance is excludable from income only for income tax purposes. These amounts are *not* excluded in determining the minister's net earnings from self-employment for Self-Employment Contributions Act (SECA) tax purposes. Retired ministers who receive either a parsonage or housing allowance are not required to include such amounts for SECA tax purposes.

As mentioned above, a minister who receives a parsonage or rental allowance excludes that amount from his income. The portion of expenses allocable to the excludable amount is not deductible. This limitation, however, does not apply to interest on a home mortgage or real estate taxes, nor to the calculation of net earnings from self-employment for SECA tax purposes.

IRS Publication 517, *Social Security and Other Information for Members of the Clergy and Religious Workers*, has a detailed example of the tax treatment for a housing allowance and the related limitations on deductions. IRS Publication 525, *Taxable and Nontaxable Income*, has information on particular types of income for ministers.

## Social Security and Medicare Taxes — Federal Insurance Contributions Act (FICA) vs. Self-Employment Contributions Act (SECA)

The compensation that a church or religious organization pays to its ministers for performing services in the exercise of ministry is not subject to FICA taxes. However, income that a minister earns in performing services in the exercise of his ministry is subject to SECA tax, unless the minister has timely applied for and received an exemption from SECA tax.

## Payment of Employee Business Expenses

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A church or religious organization is treated like any other employer as far as the tax rules regarding employee business expenses. The rules differ depending upon whether the expenses are paid through an accountable or non-accountable plan, and these plans determine whether the payment for these expenses is included in the employee's income.

### Accountable Reimbursement Plan

An arrangement that an employer establishes to reimburse or advance employee business expenses will be an accountable plan if it meets three requirements: (1) involves a business connection; (2) requires the employee to substantiate expenses incurred; and (3) requires the employee to return any excess amounts.

Employees must provide the organization with sufficient information to identify the specific business nature of each expense and to substantiate each element of an expenditure. It is not sufficient for an employee to aggregate expenses into broad categories such as travel or to report expenses through the use of non-descriptive terms such as *miscellaneous business expenses*. Both the substantiation and the return of excess amounts must occur within a reasonable period of time.

Employee business expenses reimbursed under an accountable plan are: (a) excluded from an employee's gross income; (b) not required to be reported on the employee's IRS Form W-2, *Wage and Tax Statement*; and (c) exempt from the withholding and payment of wages subject to FICA taxes and income tax withholdings.

### Non-accountable Reimbursement Plan

If the church or religious organization reimburses or advances the employee for business expenses, but the arrangement does not satisfy the three requirements of an accountable plan, the amounts paid to the employees are considered wages subject to FICA taxes and income tax withholding, if applicable, and are reportable on Form W-2. (Amounts paid to employee ministers are

treated as wages reportable on Form W-2, but are not subject to FICA taxes or income tax withholding.)

For example, if a church or religious organization pays its secretary a \$200 per month allowance to reimburse monthly business expenses the secretary incurs while conducting church or religious organization business, and the secretary is not required to substantiate the expenses or return any excess, then the entire \$200 must be reported on Form W-2 as wages subject to FICA taxes and income tax withholding. In the same situation involving an employee-minister, the allowance must be reported on the minister's Form W-2, but no FICA or income tax withholding is required. For further information see IRS Publication 463, *Travel, Entertainment, Gift and Car Expenses*.

One common business expense reimbursement is for *automobile mileage*. If a church or religious organization pays a mileage allowance at a rate that is less than or equal to the federal standard rate, the amount of the expense is deemed substantiated. (Each year, the federal government establishes a standard mileage reimbursement rate.) There are no income or employment tax consequences to the reimbursed individual provided that the employee substantiates the time, place, and business purposes of the automobile mileage for which reimbursement is sought. Of course, reimbursement for automobile mileage incurred for personal purposes is includible in the individual's income.

If a church or religious organization reimburses automobile mileage at a rate exceeding the standard mileage rate, the excess is treated as paid under a non-accountable plan. This means that the excess is includible in the individual's income and is subject to the withholding and payment of income and employment taxes, if applicable.

In addition, any mileage reimbursement that is paid without requiring the individual to substantiate the time, place, and business purposes of each trip is included in the individual's income, regardless of the rate of reimbursement.

No income is attributed to an employee or a volunteer who uses an automobile owned by the church or religious organization to perform church-related work.

# Recordkeeping Requirements

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## Books of Accounting and Other Types of Records

All tax-exempt organizations, including churches and religious organizations (regardless of whether tax-exempt status has been officially recognized by the IRS), are required to maintain books of accounting and other records necessary to justify their claim for exemption in the event of an audit. See [Special Rules Limiting IRS Authority to Audit a Church](#) on page 22. Tax-exempt organizations are also required to maintain books and records that are necessary to accurately file any federal tax and information returns that may be required.

There is no specific format for keeping records. However, the types of required records frequently include organizing documents (charter, constitution, articles of incorporation) and bylaws, minute books, property records, general ledgers, receipts and disbursements journals, payroll records, banking records, and invoices. The extent of the records necessary generally varies according to the type, size, and complexity of the organization's activities.

## Length of Time to Retain Records

The law does not specify a *length of time* that records must be retained; however, the following guidelines should be applied in the event that the records may be material to the administration of any federal tax law.

<i>Type of Record</i>	<i>Length of Time to Retain</i>
Records of revenue and expenses, including payroll records.	Retain for at least four years after filing the return(s) to which they relate.
Records relating to acquisition and disposition of property (real and personal, including investments).	Retain for at least four years after the filing of the return for the year in which disposition occurs.

Records are also important for a tax-exempt organization to maintain to avoid losing its tax-exempt status by engaging in activity that violates the Internal Revenue Code.

# Filing Requirements

## Information and Tax Returns — Forms to File and Due Dates

Churches or religious organizations may be required to report certain payments to the IRS. The following is a list of the most frequently required returns, who should use them, how they are used, and when they should be filed.

<i>Returns</i>	<i>Who Should Use Them</i>	<i>How They are Used</i>	<i>When to File</i>
<p><b>Form W-2</b> <i>Wage and Tax Statement</i></p> <p><b>Form W-3</b> <i>Transmittal of Wage and Tax Statement</i></p>	Organizations with employees.		Furnish each employee with a completed Form W-2 by January 31; and file all Forms W-2 and Form W-3 with the Social Security Administration (SSA) by the last day of February.
<p><b>Form W-2G</b> <i>Certain Gaming Winnings</i></p> <p><small>For more information on reporting requirements for gaming activities, see IRS Publication 3079, <i>Gaming Publication for Tax-Exempt Organizations</i>.</small></p>	Any charitable or religious organization, including a church, that sponsors a gaming event (raffles, bingo) must file Form W-2G when a participant wins a prize over a specific value amount.	The requirements for reporting and withholding depend on the type of gaming, the amount of winnings, and the ratio of winnings to the wager.	For each winner meeting the filing requirement, the church or religious organization must furnish each winner Form W-2G by January 31; and file Copy A of Form W-2G with the IRS by February 28.
<p><b>Form 941</b> <i>Employer's Quarterly Federal Tax Return</i> <i>or</i> <i>Form 944</i>, <i>Employer's Annual Federal Tax Return</i></p>	Small employers that have been notified by the IRS to file Form 944 (see form instructions) may use that form; other employers required to file must use Form 941	Use Form 941 or 944 to report Social Security and Medicare taxes and income taxes withheld by the organization, and Social Security and Medicare taxes paid by the organization.	See form instructions for due dates.
<p><b>Form 945</b> <i>Annual Return of Withheld Federal Income Tax</i></p>		If a church or religious organization withholds income tax, including backup withholding, from non-payroll payments, it must file Form 945.	File Form 945 by January 31. This form is not required for those years in which there is no non-payroll tax liability.
<p><b>Form 990</b> <i>Return of Organization Exempt from Income Tax</i></p> <p><b>Form 990-EZ</b> <i>Short Form Return of Organization Exempt From Income Tax</i></p> <p><b>Form 990-N (electronic postcard)</b>, <i>Electronic Notice for Tax Exempt Organizations Not Required to File Form 990 or 990-EZ.</i></p>	<p>Generally, all religious organizations (See exception to file 990 below) must file Form 990, Form 990-EZ or Form 990-N.</p> <hr/> <p><i>Exceptions to file Form 990, 990-EZ and 990-N</i></p> <p>The following is a list of some of the organizations that are not required to file Form 990, 990-EZ or 990-N.</p> <ul style="list-style-type: none"> <li>■ Churches (as opposed to "religious organizations," defined earlier</li> <li>■ Inter-church organizations of local units of a church</li> <li>■ Mission societies sponsored by or affiliated with one or more churches or church denomination, if more than half of the activities are conducted in, or directed at, persons in foreign countries</li> <li>■ An exclusively religious activity of any religious order</li> </ul> <p>See the form instructions for a list of other organizations that are not required to file.</p>	<p>For tax years 2008 through 2010, the thresholds for determining whether an organization should file Form 990, 990-EZ or 990-N will vary. See <a href="http://www.irs.gov/eo">www.irs.gov/eo</a> for the specific thresholds.</p>	<p>Form 990, 990-EZ or 990-N must be filed on or before the 15th day of the 5th month following the end of the organization's tax year.</p> <p>Form 990-N must be electronically filed.</p>



<i>Returns</i>	<i>Who Should Use Them</i>	<i>How They are Used</i>	<i>When to File</i>
<p><b>Form 990-T</b> <i>Exempt Organization Business Income Tax Return</i></p> <p>For more information on unrelated business income, see Unrelated Business Income Tax (UBIT) on page 12.</p>	Churches and religious organizations.	Churches and religious organizations must file Form 990-T if they generate gross income from an unrelated business of \$1,000 or more for a taxable year.	Form 990-T must be filed by the 15th day of the 5th month after the organization's accounting period ends (May 15 for a calendar year accounting period).
<p><b>Form 990-W</b> <i>Estimated Tax on Unrelated Business Taxable Income for Tax-Exempt Organizations</i></p>	Churches and religious organizations.	<p>If the tax on unrelated business income is expected to be \$500 or more, the church or religious organization must make estimated tax payments.</p> <p>Use Form 990-W to compute the estimated tax liability.</p>	
<p><b>Form 1096</b> <i>Annual Summary and Transmittal of U.S. Information Returns</i></p>	Churches and religious organizations.	Use Form 1096 to transmit Forms 1099-MISC, W-2G, and certain other forms to the IRS.	Form 1096 must be filed by February 28 in the year following the calendar year in which the payments were made.
<p><b>Form 1099</b> <i>Miscellaneous Income</i></p> <p>See the <i>Instructions for Form 1099-MISC</i> for details.</p>	Churches and religious organizations.	A church or religious organization must use Form 1099-MISC if it pays an unincorporated individual or an entity \$600 or more in any calendar year for one of the following payments: gross rents; commissions, fees, or other compensation paid to non-employees; prizes and awards; or other fixed and determinable income.	Churches or religious organizations must furnish each payee with a copy of Form 1099-MISC by January 31; and file Copy A of Form 1099-MISC with the IRS by February 28.
<p><b>Form 5578</b> <i>Annual Certification of Racial Nondiscrimination for a Private School Exempt from Federal Income Tax</i></p> <p>For information on racial and ethnic nondiscriminatory policies, see Revenue Procedure 75-50, 1975-2 C.B. 587 at <a href="http://www.irs.gov">www.irs.gov</a>.</p>	<p>A church or religious organization that operates a private school, whether separately incorporated or operated as part of its overall operations, that teaches secular subjects and generally complies with state law requirements for public education.</p> <hr/> <p><i>Note:</i> It is not considered racially discriminatory for a parochial school to select students on the basis of membership in a religious denomination if membership in the denomination is open to all on a racially nondiscriminatory basis. Further, a seminary, or other purely religious school, that primarily teaches religious subjects usually with the purpose of training students for the ministry, is not subject to the racially nondiscriminatory requirements because it is considered to be a religious rather than an educational organization.</p>	A church or religious organization must file Form 5578 to certify that it does not discriminate based on race or ethnic origin.	<p>Form 5578 must be filed on or before the 15th day of the 5th month following the end of the organization's taxable year (May 15 for a calendar year).</p> <p>If an organization files Form 990 or Form 990-EZ, the certification must be made on Schedule A (Form 990 or Form 990-EZ).</p>
<p><b>Form 8282</b> <i>Donee Information Return</i></p>	Churches and religious organizations.	A church or religious organization must file Form 8282 if it sells, exchanges, transfers, or otherwise disposes of certain non-cash donated property within three years of the date it originally received the donation. This applies to non-cash property that had an appraised value of more than \$5,000 at time of donation.	The church or religious organization must file Form 8282 with the IRS within 125 days of date of disposition of the property; and furnish the original donor with a copy of the form.

# Charitable Contributions — Substantiation and Disclosure Rules

## Recordkeeping

A church or religious organization should be aware of the recordkeeping and substantiation rules imposed on donors of charities that receive certain quid pro quo contributions.

## Recordkeeping Rules

A donor cannot claim a tax deduction for any contribution of cash, a check or other monetary gift made on or after January 1, 2007 unless the donor maintains a record of the contribution in the form of either a bank record (such as a cancelled check) or a written communication from the charity (such as a receipt or a letter) showing the name of the charity, the date of the contribution, and the amount of the contribution.

## Substantiation Rules

A donor cannot claim a tax deduction for any single contribution of \$250 or more unless the donor obtains a contemporaneous, written acknowledgment of the contribution from the recipient church or religious organization. A church or religious organization that does not acknowledge a contribution incurs no penalty; but without a written acknowledgment, the donor cannot claim a tax deduction. Although it is a donor's responsibility to obtain a written acknowledgment, a church or religious organization can assist the donor by providing a timely, written statement containing the following information:

- name of the church or religious organization,
- date of the contribution,
- amount of any cash contribution, and
- description (but not the value) of non-cash contributions.

In addition, the timely, written statement must contain one of the following:

- statement that no goods or services were provided by the church or religious organization in return for the contribution,

- statement that goods or services that a church or religious organization provided in return for the contribution consisted entirely of intangible religious benefits, or
- description and good faith estimate of the value of goods or services other than intangible religious benefits that the church or religious organization provided in return for the contribution.

The church or religious organization may either provide separate acknowledgments for each single contribution of \$250 or more or one acknowledgment to substantiate several single contributions of \$250 or more. Separate contributions are not aggregated for purposes of measuring the \$250 threshold.

## Disclosure Rules that Apply to *Quid Pro Quo* Contributions

A contribution made by a donor in exchange for goods or services is known as a *quid pro quo* contribution. A donor may only take a contribution deduction to the extent that his or her contribution exceeds the fair market value of the goods and services the donor receives in return for the contribution. Therefore, donors need to know the value of the goods or services. A church or religious organization must provide a written statement to a donor who makes a payment exceeding \$75 partly as a contribution and partly for goods and services provided by the organization.

**Example 1:** If a donor gives a church a payment of \$100 and, in return, receives a ticket to an event valued at \$40, this is a *quid pro quo* contribution, and only \$60 is deductible by the donor ( $\$100 - \$40 = \$60$ ). Even though the deductible amount does not exceed \$75, since the *quid pro quo* contribution the church received is in excess of \$75, the church must provide the donor with a written disclosure statement. The statement must: (1) inform the donor that the amount of the contribution that is deductible for federal income tax purposes is limited to the excess of money (and the fair market value of any property other than money) contributed by the donor over the value of goods or services provided by the church or religious organization; and (2) provide the donor with a good-faith estimate of the value of the goods or services.

The church or religious organization must provide the written disclosure statement with either the solicitation or the receipt of the contribution and in a manner that is likely to come to the attention of the donor. For example, a disclosure in small print within a larger document may not meet this requirement.

## Exceptions to Disclosure Statement

A church or religious organization is not required to provide a disclosure statement for *quid pro quo* contributions when: (a) the goods or services meet the standards for *insubstantial value*; or (b) the only benefit received by the donor is an *intangible religious benefit*. Additionally, if the goods or services the church or religious organization provides are *intangible religious benefits* (examples follow), the acknowledgement for contributions of \$250 or more does not need to describe those benefits.

Generally, intangible religious benefits are benefits provided by a church or religious organization that are not usually sold in commercial transactions outside a donative (gift) context.

### ***Intangible religious benefits include:***

- admission to a religious ceremony
- de minimus tangible benefits, such as wine used in religious ceremony

### ***Benefits that are not intangible religious benefits include:***

- tuition for education leading to a recognized degree
- travel services
- consumer goods

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*IRS Publication 1771,  
Charitable Contributions:  
Substantiation and  
Disclosure Requirements,  
provides more information  
on substantiation and  
disclosure rules.*

*Order Publication 1771  
free through the IRS at  
(800) 829-3676.*

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# Special Rules Limiting IRS Authority to Audit a Church

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## Tax Inquiries and Examinations of Churches

Congress has imposed special limitations, found in IRC section 7611, on how and when the IRS may conduct civil tax inquiries and examinations of churches. The IRS may only initiate a *church tax inquiry* if the Director, Exempt Organizations, Examinations reasonably believes, based on a written statement of the facts and circumstances, that the organization: (a) may not qualify for the exemption; or (b) may not be paying tax on an unrelated business or other taxable activity.

### Restrictions on Church Inquiries and Examinations

Restrictions on church inquiries and examinations apply only to churches (including organizations claiming to be churches if such status has not been recognized by IRS) and conventions or associations of churches. They do not apply to related persons or organizations. Thus, for example, the rules do not apply to schools that, although operated by a church, are organized as separate legal entities. Similarly, the rules do not apply to integrated auxiliaries of a church.

Restrictions on church inquiries and examinations do not apply to all church inquiries by the IRS. The most common exception relates to routine requests for information. For example, IRS requests for information from churches about filing of returns, compliance with income or Social Security and Medicare tax withholding requirements, supplemental information needed to process returns or applications, and other similar inquiries are not covered by the special church audit rules.

Restrictions on church inquiries and examinations do not apply to criminal investigations or to investigations of the tax liability of any person connected with the church, e.g., a contributor or minister.

The procedures of IRC section 7611 will be used in initiating and conducting any inquiry or examination into whether an excess benefit transaction (as that term is used in IRC section 4958) has occurred between a church and an insider.

## Audit Process

The following is the sequence of the audit process.

1. If the *reasonable belief* requirement is met, the IRS must begin an inquiry by providing a church with written notice containing an explanation of its concerns.
2. The church is allowed a reasonable period in which to respond by furnishing a written explanation to alleviate IRS concerns.
3. If the church fails to respond within the required time, or if its response is not sufficient to alleviate IRS concerns, the IRS may, generally within 90 days, issue a second notice, informing the church of the need to examine its books and records.
4. After issuance of a second notice, but before commencement of an examination of its books and records, the church may request a conference with an IRS official to discuss IRS concerns. The second notice will contain a copy of all documents collected or prepared by the IRS for use in the examination and subject to disclosure under the Freedom of Information Act, as supplemented by IRC section 6103 relating to disclosure and confidentiality of tax return information.
5. Generally, examination of a church's books and records must be completed within two years from the date of the second notice from the IRS.

If at any time during the inquiry process the church supplies information sufficient to alleviate the concerns of the IRS, the matter will be closed without examination of the church's books and records. There are additional safeguards for the protection of churches under IRC section 7611. For example, the IRS cannot begin a subsequent examination of a church for a five-year period unless the previous examination resulted in a revocation, notice of deficiency of assessment, or a request for a significant change in church operations, including a significant change in accounting practices.



# Glossary

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**Church.** Certain characteristics are generally attributed to churches. These attributes of a church have been developed by the IRS and by court decisions. They include: distinct legal existence; recognized creed and form of worship; definite and distinct ecclesiastical government; formal code of doctrine and discipline; distinct religious history; membership not associated with any other church or denomination; organization of ordained ministers; ordained ministers selected after completing prescribed courses of study; literature of its own; established places of worship; regular congregations; regular religious services; Sunday schools for the religious instruction of the young; schools for the preparation of its ministers. The IRS generally uses a combination of these characteristics, together with other facts and circumstances, to determine whether an organization is considered a church for federal tax purposes.

The IRS makes no attempt to evaluate the content of whatever doctrine a particular organization claims is religious, provided the particular beliefs of the organization are truly and sincerely held by those professing them and the practices and rites associated with the organization's belief or creed are not illegal or contrary to clearly defined public policy.

**Integrated Auxiliary Of A Church.** The term integrated auxiliary of a church refers to a class of organizations that are related to a church or convention or association of churches, but are not such organizations themselves. In general, the IRS will treat an organization that meets the following three requirements as an integrated auxiliary of a church. The organization must:

- be described both as an IRC section 501(c)(3) charitable organization and as a public charity under IRC sections 509(a)(1), (2), or (3),
- be affiliated with a church or convention or association of churches, and
- receive financial support primarily from internal church sources as opposed to public or governmental sources.

Men's and women's organizations, seminaries, mission societies, and

youth groups that satisfy the first two requirements above are considered integrated auxiliaries whether or not they meet the internal support requirements. More guidance as to the types of organizations the IRS will treat as integrated auxiliaries can be found in the Code of Regulations, 26 CFR section 1.6033-2(h).

The same rules that apply to a church apply to the integrated auxiliary of a church, with the exception of those rules that apply to the audit of a church. See section [Special Rules Limiting IRS Authority To Audit A Church](#) on page 22.

**Minister.** The term minister is not used by all faiths; however, in an attempt to make this publication easy to read, we use it because it is generally understood. As used in this booklet, the term minister denotes members of clergy of all religions and denominations and includes priests, rabbis, imams, and similar members of the clergy.

**IRC Section 501(C)(3).** IRC section 501(c)(3) describes charitable organizations, including churches and religious organizations, which qualify for exemption from federal income tax and generally are eligible to receive tax-deductible contributions. This section provides that:

- an organization must be organized and operated exclusively for religious or other charitable purposes,
- net earnings may not inure to the benefit of any private individual or shareholder,
- no substantial part of its activity may be attempting to influence legislation,
- the organization may not intervene in political campaigns, and
- the organization's purposes and activities may not be illegal or violate fundamental public policy.

These requirements are set forth in greater detail throughout this publication.

# Help From The IRS

## IRS Tax Publications to Order

The IRS provides free tax publications and forms. Order publications and forms by calling toll-free (800) 829-3676, or download publications and forms from the IRS Web site at [www.irs.gov](http://www.irs.gov). The following list of publications may provide further information for churches and other religious organizations:

<b>Publication 1</b>	<i>Your Rights as a Taxpayer</i>
<b>Publication 15</b>	<i>Circular E, Employer's Tax Guide</i>
<b>Publication 15-A</b>	<i>Employer's Supplemental Tax Guide</i>
<b>Publication 334</b>	<i>Tax Guide for Small Business (For Individuals Who Use Schedule C or C-EZ)</i>
<b>Publication 463</b>	<i>Travel, Entertainment, Gift, and Car Expenses</i>
<b>Publication 517</b>	<i>Social Security and Other Information for Members of the Clergy and Religious Workers</i>
<b>Publication 525</b>	<i>Taxable and Nontaxable Income</i>
<b>Publication 526</b>	<i>Charitable Contributions</i>
<b>Publication 557</b>	<i>Tax-Exempt Status for Your Organization</i>
<b>Publication 561</b>	<i>Determining the Value of Donated Property</i>
<b>Publication 571</b>	<i>Tax-Sheltered Annuity Programs for Employees of Public Schools and Certain Tax-Exempt Organizations</i>
<b>Publication 598</b>	<i>Tax on Unrelated Business Income of Exempt Organizations</i>
<b>Publication 910</b>	<i>Guide to Free Tax Services</i>
<b>Publication 1771</b>	<i>Charitable Contributions: Substantiation and Disclosure</i>
<b>Publication 3079</b>	<i>Gaming Publication for Tax-Exempt Organizations</i>
<b>Publication 4221-PC</b>	<i>Compliance Guide for 501(c)(3) Public Charities</i>
<b>Publication 4630</b>	<i>Exempt Organizations Products and Services Navigator</i>

## IRS Customer Service

Telephone assistance for general tax information is available by calling:

IRS Customer Service

toll-free at (800) 829-1040.

## EO Customer Service

Telephone assistance specific to exempt organizations is available by calling:

IRS Exempt Organizations Customer

Account Services toll-free at

(877) 829-5500.

## EO Web Site

Visit the IRS Exempt Organizations

Web site at [www.irs.gov/eo](http://www.irs.gov/eo).

*Stay Exempt - Tax Basics for 501(c)(3)s - a free on-line IRS workshop covering tax compliance issues confronted by small and mid-sized tax-exempt organizations, available at [www.stayexempt.org](http://www.stayexempt.org).*

## EO Update

To receive IRS Exempt Organization's Update, a periodic newsletter with information for tax-exempt organizations and tax practitioners who represent them, visit [www.irs.gov/eo](http://www.irs.gov/eo) and click on "EO Newsletter."

Congress has enacted special tax laws applicable to churches, religious organizations, and ministers in recognition of their unique status in American society and of their rights guaranteed by the First Amendment of the Constitution of the United States. Churches and religious organizations are generally exempt from income tax and receive other favorable treatment under the tax law; however, certain income of a church or religious organization may be subject to tax, such as income from an unrelated business. It is also important for a church or religious organization to understand the tax law to avoid losing its tax-exempt status by engaging in activity that violates the Internal Revenue Code.



Department of the Treasury  
Internal Revenue Service

[www.irs.gov](http://www.irs.gov)

Publication 1828 (Rev. 6-2008)  
Catalog Number 21096G