



# Tax Laws for Churches and Ministers Part 1

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Course #3301A

Taxes

2 Credit Hours

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# TAX LAWS FOR CHURCHES AND MINISTERS PART 1

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This course provides an overview of the tax laws for churches, religious organizations, and ministers. It covers the information an accountant needs to know to best assist his or her clients in this area. Part 1 covers the source that guarantees the organizations rights and what is required to qualify for tax-exempt status among other topics.

## LEARNING ASSIGNMENTS AND OBJECTIVES

*As a result of studying each assignment, you should be able to meet the objectives listed below each individual assignment.*

### SUBJECTS

#### **Tax-Exempt Status and Its Ramifications Taxes, Recordkeeping, and Forms to File**

Study the course materials from pages 1 to 46

Complete the review questions at the end of each chapter

Answer the exam questions 1 to 10

#### **Objectives:**

- Recognize the source that guarantees the rights of churches, religious organizations, and ministers.
- Identify what is required to qualify for tax-exempt status.
- Identify the various recordkeeping and filing requirements for churches and religious organizations.

## **NOTICE**

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## EXAM OUTLINE

- **TEST FORMAT:** The final exam for this course consists of 10 multiple-choice questions and is based specifically on the information covered in the course materials.
- **ACCESS FINAL EXAM:** Log in to your account and click Take Exam. A copy of the final exam is provided at the end of these course materials for your convenience, however you must submit your answers online to receive credit for the course.
- **LICENSE RENEWAL INFORMATION:** This course qualifies for **2** CPE hours.
- **PROCESSING:** You will receive the score for your final exam immediately after it is submitted. A score of 70% or better is required to pass.
- **CERTIFICATE OF COMPLETION:** Will be available in your account to view online or print. If you do not pass an exam, it can be retaken free of charge.

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# CHAPTER 1: TAX-EXEMPT STATUS AND ITS RAMIFICATIONS

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## Chapter Objectives

### After completing this chapter, you should be able to:

- Recognize the source that guarantees the rights of churches, religious organizations, and ministers.
- Identify what is required to qualify for tax-exempt status.

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 activities that violate the Internal Revenue Code (IRC).

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 material 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 course 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 course uses the term “religious organizations,” it is not referring to churches or integrated auxiliaries. Religious organizations that are not churches typically include nondenominational 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, including as unincorporated associations, nonprofit corporations, corporations sole, and charitable trusts.

## I. TAX-EXEMPT STATUS

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 exemption, such an organization must meet the following requirements:

- 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 the organization's 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.

## **A. RECOGNITION OF TAX-EXEMPT STATUS**

### **1. 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.

### **2. 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. If the church or other affiliated organization is included on the list, it does not need to take further action in order 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.

### **3. 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.

## **B. APPLYING FOR TAX-EXEMPT STATUS**

### **1. 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 that does not have an EIN should file Form SS-4, *Application for Employer Identification Number*, according to its instructions. If the organization is submitting IRS Form 1023, *Application for*



*Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code* (see below), Form SS-4 should be included with the application.

## 2. Application Form

When applying for recognition as tax exempt under IRC Section 501(c)(3), churches and some religious organizations must use Form 1023. Smaller religious organizations may be eligible to use Form 1023-EZ, *Streamlined Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code*.

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 from the date of its formation as a church, even though that date may be prior to 27 months from the end of the month in which its application is submitted.

### a. **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) website under the IRS Tax Exempt and Government Entities division via [www.irs.gov/](http://www.irs.gov/) (key word “exempt organization user fee”) or by calling EO Customer Account Services toll-free at (877) 829-5500.

## 3. 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.

## C. PUBLIC LISTING OF TAX-EXEMPT ORGANIZATIONS

*Tax Exempt Organization Search (TEOS)* is an online search tool that allows users to search for organizations that are eligible to receive tax-deductible charitable contributions.

### Note



Not every organization that is eligible to receive tax-deductible contributions is listed on *TEOS*. For example, churches that have not applied for recognition of tax-exempt status are not included on *TEOS*. Only the parent organization in a group ruling is included by name on *TEOS*.