

Understanding Housing Allowance

by Jerry Rich, FCMM Vice President

The “Housing Allowance” provision in the IRS tax code can represent a significant tax-reduction benefit for ministers when implemented properly.

History

First enacted by Congress in 1921, when most churches provided a parsonage (or “manse”) to the pastor, the exclusion from taxable income was instituted so the federal government would not get involved in examining the practice of churches in providing housing to their ministers. 1954 revisions to the tax code included an equalizing treatment for ministers who provided their own housing through the method of a church designating an appropriate portion of the pastor’s compensation as housing allowance which would then not be considered taxable income.

Today, qualified ministers may utilize this benefit. However, another aspect of minister status can reduce or outweigh the housing allowance exclusion because of the classification of the minister as “self-employed” for Social Security purposes, triggering a higher rate. See SECA discussion below.

Qualifying as a Minister

IRS Publication 517 defines ministers as “individuals who are

duly ordained, commissioned, or licensed by a religious body constituting a church or church denomination. Ministers have the authority to conduct religious worship, perform sacerdotal functions, and administer ordinances or sacraments according to the prescribed tenets and practices of that church or denomination.” Because of the variance of church government and polity, the IRS does not address the credentialing details but does describe some criteria in Publication 517.

I would summarize the guidance as these factors:

1. The person must be credentialed as clergy (i.e. ordained, commissioned, or licensed), and
2. Meet a “balancing test” of the following factors:
 - Have authority to conduct religious worship.
 - Have authority to perform “sacerdotal” functions.
 - Have authority to administer ordinances/sacraments.
 - Have management responsibilities in the local church or denomination.
 - Be considered to be a religious leader by the church or denomination.

Discussion of credentialing is beyond this article, but when
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Ministers Can Receive FCMM Distributions as Housing Allowance

A unique benefit for funds distributed to ministers who contributed to a denominational 403(b)(9) church retirement plan (only) is the designation of distributions from the Plan as housing allowance.

Unlike the annual exercise for ministers to request housing allowance designation from their church each year, FCMM distributions to ministers are designated by the FCMM Board of Trustees as 100% housing allowance eligible. The retired pastor must keep records of actual housing expense in order to document the amount of annual costs that were actually used for housing expenses.

The eligibility for housing allowance designation for retirement distributions is that the funds were contributed while the minister was eligible for housing allowance (i.e. treated as a minister for tax purposes). Status at the time of distribution does not matter.

Just as during active employment years, the same IRS

guidelines apply to the limits for non-taxable housing allowance distributed from church plan retirement funds – the housing allowance exclusion from taxable income is the lesser of three factors: (1) The amount designated; (2) The amount spent for housing; or (3) The fair rental value of similar housing.

Any amount above those qualified housing expenses would be subject to income taxes, reported by the minister for tax filing in a similar way to unused housing-allowance-designated income during employment.

The IRS permits the housing allowance exclusion only for the original participant and not to distributions made to a surviving spouse.

For information on tax reporting for housing allowance, see the FCMM website article “Quick Guide to Tax Reporting for Retirement Distributions – 1099R”.



Contribution Limits (2026)

a church is affiliated with a denomination that practices credentialing, the IRS will likely see more credence in the denominational credential and may see a local credential (i.e. specific to a congregation) as less certain.

In any event, clergy credentials should never be granted for the purpose of tax benefits.

The special tax rules for ministers include:

- Exclusion of a provided parsonage, or the minister’s expense of providing housing, from taxable income
- Self-employed status for Social Security tax (requiring payment of the self-employed “SECA” rate).
- Exemption from mandatory withholding. The minister is still responsible for timely paying the tax.

If a staff member meets the criteria for minister, the IRS requires the employing church to handle the compensation in this way. **IMPORTANT TO NOTE:** The tax aspects of minister status are not separable (exemption from withholding, self-employment income subject to SECA tax, provision for housing allowance exclusion – ALL occur together). If a person meets the criteria for minister, the IRS indicates the person must be treated that way for tax purposes. This is not a status that can be a matter of preference, by either the church or the minister.

Benefit of Minister Housing Allowance

What is it? The exclusion from gross income for income tax purposes (but not exclusion from SE tax) of the amount used to provide a home, limited to the **smallest** of:

- The amount actually used to provide a home, substantiated by documented eligible expenses. (Such documentation is not submitted with a tax return but should be kept in case a tax return is audited.)
- The amount officially designated before payment of compensation (i.e. in advance by the church governing body).
- The fair rental value of the home, including furnishings and utilities.

What may be included in total of actual expenses?

All appropriate expenses related to providing a principal residence (only) are eligible, including mortgage payments, rent, utilities, repairs, furnishings, property insurance, property taxes, maintenance, improvements, and homeowner association dues.

What if the minister lives in a church-provided parsonage?

The rental value of the parsonage is not included in reportable income (W-2, Box 1) but the annual value must be added to taxable income for calculating SECA tax, reported via

Schedule C and Schedule SE on the individual’s tax return. If the minister pays utilities or maintenance, that amount may be designated in advance as housing allowance.

Similarly, the value of the designated housing allowance for ministers providing their own housing is reported via Schedule C and Schedule SE for the purpose of determining SECA tax.

Is the housing allowance reportable to the IRS?

While some ministries include the designated housing allowance in Box 14 of the W-2 as a courtesy to the minister, data in Box 14 is informational to the employee and not required.

EMPLOYEE CLASSIFICATION GUIDE				
Tax Status Comparison				
EMPLOYEE TYPE	Social Security and Medicare Paid by...		PAYCHECK WITHHOLDING REQUIRED?	HOUSING ALLOWANCE CAN REDUCE TAXABLE INCOME?
	STAFF PERSON	EMPLOYER		
Regular Employee	7.65% FICA – EMPLOYEE	7.65% FICA – EMPLOYER	YES	NO
Clergy Employee	15.3% SECA	—	NO	YES

FICA = Federal Insurance Contributions Act
SECA = Self-Employment Contributions Act

More about SECA Tax

For employees other than ministers, the employer must pay the employer’s share of FICA tax for Social Security and Medicare (7.65%), and must deduct the employee’s share of 7.65% from pay up to certain limits.

For ministers, the employer does not pay FICA or deduct FICA. The minister is responsible for SECA instead.

NOTE: When structuring equitable pay for ministers, I believe a best practice is for the church to pay the equivalent of employer FICA to the minister so that half of the SECA tax incurred by the minister is covered. The 7.65% paid to the minister is simply taxable income, but should be considered an employer benefit and not part of the salary base. (Just as employer FICA is not considered part of a non-minister’s base salary.)

