

Q & A

ACCOUNTABLE REIMBURSEMENT POLICIES

The following questions and answers are intended to assist local churches and organizations in establishing and maintaining **accountable reimbursement policies** for their clergy and staff.

1. What is an accountable reimbursement policy and why should we have one?

For business and tax reasons, in most instances, it is in the best interests of the church and its staff to have in place an accountable reimbursement policy to pay for the business expenses that are necessary to do the ministry of the church. These policies are simply a method for claiming and reimbursing professional or business expenses rather than providing an expense allowance. It's as simple as this: A church sets up a budget for the pastor's professional and business expenses, such as travel, continuing education, subscriptions, etc. When the pastor incurs a professional or business expense, s/he submits a claim with backup substantiation. The church either pays the expense directly or reimburses the pastor.

2. Are accountable reimbursement policies only for clergy?

No. The church can set up the policy to cover the business expenses for all staff. When answers or examples refer to pastors, it is for illustration purposes and not meant to exclude other staff.

3. What are the advantages of an accountable reimbursement policy?

There are several advantages to using an accountable reimbursement policy.

- a) Convenience:** Staff reports the business expenses to the church and not to the IRS - this means that none of the expenses are reported on Forms W-2 and there is no need to worry about IRS forms or calculating deductions.
- b) Data:** It gives the church an accurate account of the "cost" of ministry and allows members to understand the financial support necessary for staff to do their work well.
- c) No complex rules:** the **Deason** rule does not apply (it otherwise requires clergy to reduce the deduction for business expenses proportionately if they have a tax exempt housing allowance).
- d) Fewer limits:** Certain limits on business meals are avoided.
- e) Tax savings:** It takes the place of Schedule C and may save on taxes.

4. What are the disadvantages of an accountable reimbursement policy?

There are two minor disadvantages: The clergy person's work expenditures are subject to more review by church members and some privacy may be lost. Also, the funds in the accountable reimbursement budget belong to the church and may not be given to the pastor at year-end if there is money left unspent.

5. What needs to go in an accountable reimbursement policy?

It's as easy as this. All you need is a written policy, which can be as simple as a short paragraph in the form of a resolution or a detailed plan, depending on the church's own needs and structure. This tax packet includes easy to implement sample policies (short and long). Most churches will want to have a budget amount which will "cap" the allowed amount for each staff person. It can be helpful (but it is not required) for the pastor, SPR committee, and finance committee to develop the budget together, with an idea of the types of expenses that can be expected.

6. When should the policy be set up?

The policy should be set up and funded when the church is doing the budget for the upcoming year. Once a written policy is in place, the church only needs to examine the budget funding for the accountable reimbursement policy each year.

7. How should the policy be funded?

Out of the church's budget, just like other expenses of running the church. The church needs to look at its budget and determine what amounts are necessary to pay for reasonable business expenses that fulfill the mission of the church, together with what it can reasonably afford. It is important for the church to realize that business expenses are properly church expenses and not something that the staff must cover from their own personal funds. It is important to review past expenditures (and future needs) carefully to arrive at an amount adequate to pay for the business expenses and at the same time within budget constraints.

8. Can the church reduce the pastor's salary to fund the accountable reimbursement policy?

No. The IRS prohibits salary reductions to cover accountable reimbursement policies.

9. Can monies budgeted in the past for a travel allowance be used instead to fund an accountable policy?

Yes. For example, when the church is setting up its budget, it may reallocate the pastor's travel allowance (or other allowances other than a housing allowance) into an accountable reimbursement policy. By doing so, the church does not have to report the new travel reimbursement as part of the W-2 income.

10. Can the church and the pastor negotiate compensation at the beginning of a new appointment and structure compensation that includes funding of an accountable reimbursement policy?

A pastor coming into a new appointment has the ability to create a salary/compensation/benefit package that includes an adequately funded accountable reimbursement policy. The best approach is to budget for the policy out of church funds because these expenditures are for professional expenses which staff need to do their job.

11. What expenses/categories/items should be part of the policy?

Included in this tax packet is a worksheet designed to help churches determine an acceptable budget for an accountable policy. The worksheet lists examples of appropriate business expenses that may be included (e.g., business automobile expenses, parking, tolls, office supplies, business postage, office equipment, business-use computers, software, professional books/subscriptions, professional dues, religious materials, vestments, business gifts, continuing education, business entertainment, travel, etc.) There may be other business expenses that are appropriate to include, depending on the unique mission of your church. It is important to note that the categories on the worksheet are suggestions for budgeting, not rigid expense categories; the staff person, in consultation with the SPR chair and/or treasurer, or finance committee chair, may shift expenses during the year from one category to another. See also "Examples" at the back of this Q&A for suggestions about proper and improper reimbursements.

12. Should the church reimburse the staff member or pay for their business expenses directly?

Either approach is acceptable. The staff person may submit a bill and ask that the church pay it. Alternately, s/he can substantiate the expense and ask that the church reimburse him/her. We have attached a sample voucher form that can be used to submit requests for payment or reimbursement. Some churches provide certain members of their staff with business credit cards or long distance phone cards (restricted to business use) to make substantiation and bill payment easier. However, a credit card statement alone is not sufficient substantiation (See question 13 below).

13. How should expenses be substantiated?

The IRS requires an adequate accounting by the employee and maintenance of good records by the employer. The IRS requires actual receipts for any expense over \$75.00. The church may use this figure or set a lower limit. (e.g., GCFA requires receipts for all expenses over \$25.00.) The documentation should show (or be listed on the receipt itself): the purchase, amount, date, place and the business nature of the expense. For example, if the pastor purchased a \$10.25 notebook, the substantiation would not require a receipt, but at the very least should state, "Purchased Notebook for \$10.25 on 1/5/01 for keeping accountable reimbursement records for church." A meal expense might state, "\$5.90 lunch on 1/5/01, in Centerville while meeting with district superintendent." Another example is a \$150 expenditure for a continuing education seminar where the staff can submit the invoice for payment by the church to the vendor. Or, if the staff person paid personally, an acknowledgment of payment by way of a receipt for the seminar or the invoice with a front and back copy of a canceled check would be adequate to substantiate the reimbursement to the staff person.

14. When must substantiation/receipts be provided to the church?

The IRS requires that all substantiation of expenses be submitted within 60 days of the expense being paid or incurred. Using the above example of a notebook purchased on 1/5/01, the expense substantiation must be submitted no later than 3/4/01, to qualify as

an accountable reimbursement. It is a good practice to turn in receipts at least every two weeks, to prevent forgetting about expenses or losing back-up receipts.

15. Can the church make advance payments? When must the staff substantiate the expenses?

Yes, it is appropriate to allow advances, if the church wishes to do so and has an adequate accounting system to track the substantiation for or reimbursement of advances. If an advance is given and exceeds the amount of business expense substantiated, the staff person must return the excess within 120 days of the date incurred or paid. (GCFA requires substantiation of travel expenses, and repayment of unused advance amounts, within three business days of travel)

16. Who gets original receipts and documentation?

The church should be given the originals of receipts and written documentation and the staff person should keep a copy. It is unlikely that the staff person would ever need the copies unless s/he needed to substantiate expenses in excess of the amounts reimbursed.

17. Can the church give to the pastor at the end of the year any monies in the accountable policy not spent during the year?

No. The funds budgeted should not be shifted to a bonus or any other type of payment. This could jeopardize the entire accountable reimbursement policy. The monies can be used by the church for other types of expenses (e.g., for mission, to reserves, or as a carry over to the accountable reimbursement budget line for next year).

18. Can the church increase the funding of the accountable reimbursement policy during the year?

Yes. If the church has additional funds or wants to shift budgeted funds from one account to another, it may do so (No shifting is allowed from salary to an accountable policy).

19. Which church officer should be responsible for reviewing the propriety of the items submitted and which officer should be responsible for paying the expenses?

There is no single correct way to handle this responsibility. One method is to have the chair of the SPRC (in consultation with the committee) review and approve the submitted expenses and for the treasurer to handle payment. This avoids conflicts that may arise concerning the appropriateness of a given expense if all of the responsibility is on the treasurer. Under any arrangement, it is important for someone, with credibility and respect to carefully review all of the submitted requests for reimbursement to ensure their appropriateness. Also, someone needs to be in charge of monitoring all expenses to ensure budget compliance, timely reporting, return of any advances and the like.

20. How should confidential items be handled in terms of substantiation and reporting?

When the pastor makes confidential visits to parishioners, s/he may want to write "private" or "confidential visit with church member" on a travel log. The pastor should at least be able to answer any questions or share information about these entries in confidence with the chair of the SPRC.

21. What does the IRS consider to be a properly reimbursable business expense and is it different for a church than a for-profit oriented business?

A business expense is one that is directly related to the purposes and goals of the organization and is reasonably necessary to fulfill those goals. The basic idea applies to all organizations, from the smallest widget manufacturer to the largest business corporations in the U.S., from the smallest rural church to the mega churches, even though the goals of a church are different from the goals of a business. It is necessary that expenses relate to the church's unique mission and **that they not be personal expenses of the pastor.**

For example, it would **not** be proper for a minister to claim a travel reimbursement for the expense of visiting a sick relative who is **not** a member of the church and lives 100 miles away, even if part of the purpose of the trip was to give spiritual comfort. The primary reason for the trip is to visit a relative. If a pastor went on a two-week vacation with his/her family and also preached at two churches during the trip, reimbursement for the travel vacation expenses would **not** be proper. Some of the expenses related to the preaching would be appropriate if the pastor's church encouraged such preaching arrangements during vacations, the pastor obtained approval for this and the pastor incurred additional expenses on the trip for going to those church locations. If the personal nature of the expense is the primary consideration, it is not a business expense. See also the sample list of proper and improper reimbursement items at the end of this Q & A.

22. May a church tell a pastor not to spend funds even if the expense may be a proper business expense?

Yes. The question suggests a conflict between the pastor and the treasurer's or the SPR committee's view of necessary or authorized expenses as they relate to the mission of the church. The best way to resolve most conflicts is to try to understand them, discuss them, and come to some agreement.

For example, it is hoped that most churches would agree that annual conference related committee work and travel are part of each church and pastor's commitment to the connectional system (these would be legitimate business expenses). If a conflict over such conference expenses exists, the DS may be able to facilitate some meeting of minds (or pocketbooks). A difficult problem may arise when the church and the pastor view their mission differently. If the church does not approve of the clergy's involvement in an international mission project and finds it to be outside of the church's mission, the pastor should not submit travel or related expenses for such an activity. These issues should be explored ahead of time with the SPRC to avoid misunderstandings.

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- 23. What happens if a new pastor is appointed in June and the previous pastor has already spent all of the funds in the accountable reimbursement policy account for that calendar year?**

The best answer is that type of situation should not arise in the first place, because the departing pastor, SPRC chair and treasurer should make sure that it does not occur. These individuals all need to monitor the expenses and make sure that the accounts, absent unusual circumstances, are spent proportionally throughout the year. However, if this scenario should occur, it is possible to add to the accountable reimbursement policy for the new pastor, if funds are available elsewhere in the budget.

- 24. Who owns the equipment and other items purchased under the accountable reimbursement policies?**

The church. If a church has paid for items through an accountable reimbursement policy, the equipment or other property belongs to the church, unless there is some other agreement. This issue of ownership usually does not come up until a pastor receives a new appointment and wishes to take equipment with him/her. It is not an issue in relation to travel, continuing education, professional dues or entertainment expenses, which are not "tangible" things. Likewise, it would not often be a problem for office supplies, postage, periodicals or personal religious supplies, such as robes. These items are used up or are so personal that there is limited or no value to the church.

A computer is the most common item that raises this question. In this day and age it is important for the church to supply staff with a computer. However, if the pastor needs a computer, and the church has not budgeted for this purchase, the pastor may want to use accountable funds to make this purchase. While the pastor is at the church, the pastor uses the computer for business purposes. What happens when the pastor, Rev. Dos, leaves?

Rev. Dos decides she likes her computer and wants to take it to her new appointment. She approaches the chair of the SPRC and offers to purchase the computer for current fair market value (a purchase, at fair market value, would not be a taxable event). The SPRC decides to give the computer to Rev. Dos. The gift is a taxable event and the value of the gift for income tax purposes is the current fair market value.

- 25. Do accountable reimbursement policies include the housing allowance?**

No. These are totally separate and need to be established and maintained separately. Accountable reimbursement policies are for business expenses, are available to all church staff, and can be used by any business or organization. Housing allowances relate only to clergy, as ministers of the gospel, and are authorized specifically by Internal Revenue Code § 107. GCFA has a Sample Housing Allowance Form, which may be found under the Q&A on Housing Allowance.

- 26. Do accountable policies include a cafeteria plan (flexible spending plan) for medical reimbursements?**

No. However it is possible to set up cafeteria or flexible spending plans that may allow church staff to have medical reimbursements, dependent care reimbursements, and life

insurance coverage, without income tax consequences. *All of the above arrangements need to be set up properly in a separate resolution or plan, with the assistance of a tax and benefits advisor, and must conform to the applicable Internal Revenue Code provisions.* Churches need to make sure any cafeteria plans are correctly set up by consulting with their own advisors and experts. Conferences participating in the General Board of Pension and Health Benefits HealthFlex Plan are provided with a flexible spending plan.

27. Are there any pension concerns when using an accountable reimbursement policy?

Amounts that are paid as accountable reimbursements are not part of "taxable compensation" for certain pension contribution limitations established by IRS rules. While the new tax law that takes effect in 2002 changes and generally increases contribution limitations, clergy still need to be mindful of limitations.

28. What are the implications of an accountable policy for local church/conference reporting information?

GCFA's Local Church Report to the Annual Conference and Local Church and Pastor Compensation and Expense Worksheet forms that have been changed to show the distinction between **reimbursements** established for the pastor and **allowances** paid to the pastor. In the Report line 66 is for reimbursements and line 67 is for allowances (other than the housing allowance that is put on line 65).

29. How should "ticketless" airline expenses be substantiated?

It is necessary that the documentation show the date, place, amount and business reason for the trip. The IRS has suggested that the itinerary from a travel agency and /or the airline receipt, along with an explanation of the reason for the travel, should be sufficient.

This Q & A is provided to give suggestions for establishing an accountable reimbursement policy. It is important to examine each situation closely to determine the correct result, because each church setting, ministry, budget and pastor are unique. The General Council on Finance and Administration is not engaged in providing legal or accounting services. The services of a competent professional should be sought for legal and tax advice.

Examples of Proper Reimbursement Items*

Reasonable travel and related expenses for attending meetings (e.g., annual conferences, United Methodist meetings, etc.)**

Church-approved trips to preach at another church

Trips to meet with the district superintendent, bishop or director of connectional ministries

Trips to visit members at hospitals, nursing homes or parishioner's homes

Lunch meetings with officers of the church to discuss church business

Supplies for the church office (e.g., paper, pens, forms, notebooks, etc.)

Church-related continuing education

A computer required for church work

Vestments worn for worship

Church-related books and periodicals

Office furnishings and equipment (e.g., desk, chairs, telephone, etc.)

Spouse's travel expenses where the spouse accompanies the pastor **but only if the spouse was required by the church to be present for a business purpose** (e.g., the spouse is an elected delegate to the church meeting or group in charge of registration at the meeting and making a speech to the business meeting, etc.)

Business-related automobile operating expenses (if standard mileage rate was not used)

Long distance telephone calls to church when on vacation

Church-related telephone calls from the parsonage (most telephone expenses are covered under the housing allowance)

Many business related (non-personal) expenses allowable on Schedule C of the IRS tax return

*The items listed are, in most cases, proper. There may be some circumstances in which the church has specifically prohibited purchases. Each individual church must, in consultation with staff, make its own decision about what expenses are "professional and business" expenses and whether it will cover those items.

**If the conference pays a pastor 15 cents per mile for attending a conference meeting, it is proper for the church to reimburse the difference between the church's rate and the 15 cents. For example, if the church reimburses staff travel at 31 cents per mile, in this case, the conference would pay 15 cents per mile and the church would pay 16 cents per mile for mileage.

Examples of *Improper* Reimbursement Items*

Mileage to church from home for daily work (considered personal) - Mileage to home and back to church for lunch break

Meals with friends at which church matters are discussed

Spouse's travel under most circumstances (see example of proper reimbursement in limited circumstances above)

Vacations (including trip to Holy Land) - Books to plan vacation to Holy Land

Trips to visit sick relative

Trips to funeral home where that pastor is paid an honorarium for service (may be deducted on a Schedule C)

Tickets to attend the play "Joseph and His Amazing Technicolor Dream Coat"

Expenditures (e.g., travel, books, phone calls) to research a book or article

Continuing education primarily for personal improvement

A computer used primarily by family

Everyday clothing, including business suits

Alcohol, even as an item on a receipt for a business meal

Medical expenses (may be part of a cafeteria or flexible spending accountable reimbursement policy)

Child care/dependent expenses (may be part of a cafeteria or flexible spending reimbursement plan)

Life or disability insurance premiums

Medical insurance premiums (may be part of a cafeteria or flexible spending plan)

Charitable contributions, tickets to charity functions

Expenditures related to a private business or generating income from a non-church source

Housing related expenses (e.g., utilities, furniture, upkeep (part of housing allowance))

Subscriptions to a national news magazine for the pastor's personal use

*The items listed, in most cases, are improper. There may be some circumstances, particularly where the church has directed the staff person to make the expenditure for church mission, when these items may be proper. Each individual church must, in consultation with staff, make its own decision about what expenses are "professional and business" expenses and whether it will cover those items.