

ACCOUNTABLE REIMBURSEMENT POLICIES Q&As

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. Also, at the end of this document, there are some examples of proper and improper expense reimbursements.

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 perform the duties of a United Methodist pastor. 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: The pastor sets aside a portion of his/her compensation in the church budget for 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 clergyperson'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 are "use it or lose it" funds and may not be given outright to the pastor at year-end if there is money left unspent. However, unused funds may be carried forward to the next year without penalty.

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). The amount agreed upon by the pastor and the church will create a budget amount which will "cap" the allowed amount.

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?

From the portion of the pastor's compensation that is set aside for professional and business expenses. It is important for the church to realize that business expenses are properly church expenses and related professional 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" or "restructure" the pastor's salary to fund the accountable reimbursement policy?

The IRS has stated that it is currently reviewing some aspects of this issue. But until further notice from the IRS, churches should avoid these types of arrangements. The pastor's base salary may be reduced when s/he goes to a new appointment to create an Accountable Reimbursement Account but the base salary may not be reduced to increase the amount of the ARP after that. The pastor may designate a portion of any future increases in compensation to increase the amount of the ARP.

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 W-2 income.

10. Can the church and the pastor negotiate compensation at the beginning of a new appointment 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.

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

Attached to the sample "long-form" 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. Also see the examples at the end of these Q & As 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. This tax packet includes 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.

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 \$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 occur within a reasonable time (within 60 days will be deemed reasonable) of the expense being paid or incurred. Using the above example of a notebook purchased on 1/5/01, the expense substantiation should 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 a reasonable time (within 120 days will be deemed reasonable) of the date incurred or paid.

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 the extended ministry of the pastor 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 who 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. Also see the ***sample list of proper and improper reimbursement items at the beginning of these Q&As.***

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 or the pastor's extended ministry. The best way to resolve most conflicts is to try to understand them, discuss them, and come to some agreement.

Annual conference related committee work and travel are part of each church and pastor's commitment to the connexional system (these would be legitimate business expenses). If a conflict over such conference expenses exists, the IDS 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.

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 this 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, the church would need to add funding for the last six months of the year to the accountable reimbursement policy because this would be a part of the compensation package promised for the new pastor,.

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

If a church has paid for items through an accountable reimbursement policy, technically the equipment or other property belongs to the church, unless there is some other agreement. However, in the Virginia Conference everything purchased through a pastor's Accountable Reimbursement is purchased with funds coming from the pastor's compensation package not from church funds. 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 they have 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. . For any items such as computers or other equipment there should be a clear understanding concerning ownership of the item before the purchase takes place.

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.

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. Pastors participating in the Conference Health Plan have a cafeteria plan (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 took 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 reimbursement policy for local church/conference reporting information.

On the Virginia Conference Pastor's Compensation Report Line 1 should contain the base salary for the pastor (excluding the Accountable Reimbursement) and the Accountable Reimbursement amount should be reported on Line 4a with any other cash allowances other than housing or heat reported on Line 3.

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.

These Q & As are 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 Virginia Conference is not engaged in providing legal or accounting services. The service 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 conference, United Methodist meetings, etc.)**
- Church-approved trips to preach at another church
- Trips to meet with the district superintendent, bishop or conference council director
- 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.)
- Spouses travel expenses where the spouse accompanies the pastor **but only if the spouse was required 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 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)
- Most 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.

**If the conference pays a pastor 28 cents per mile for attending a conference meeting, it is proper for the pastor to seek reimbursement for the difference between the IRS rate of 40.5 cents and the 28 cents paid by the Conference.

2005

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 Dreamcoat"
- 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. Each individual church may, in consultation with staff, make a decision about what expenses are "professional and business" expenses and whether it will cover those items. If the pastor has any doubt about whether the church will approve the reimbursement for a particular item under the reimbursement account, the pastor should clear the purchase with the person who has approval authority for the account before he or she makes the purchase.

2005