December, 2012

Tax and Legislative Developments Affecting Ministries

Presented by:
Dave Moja, Tax Partner
Agenda:

• Health Care In 2013
• Health Care in 2014
  • Individual Mandate
  • Employer Mandate
• Miscellaneous, including:
  • Executive Compensation
  • Independent Contractor vs. Employee
  • Unrelated Business Income Tax
Health Care Reform in 2013
2013 Compliance

• **No Exemptions** for Churches, Foreign Mission Agencies or Religious Orders

• No requirement to have a health plan

• 2013 FSA in cafeteria plan limited to $2500

• Small employer health care credit (business) or refund (exempt organization) still available
Form W-2 Reporting

- Employer provided medical in 2012 on W-2 issued January, 2013
- Small Employer: < 250 W-2 forms
- Medical includes: insurance premium and allocated self insurance expense
- Medical does not include: HSA, MSA, employee contribution to FSA, dental, vision
Notices

- Summary of Benefits & Coverage ("SBC")
  - Provide to participants & beneficiaries at first open enrollment period after Sept. 23, 2012
  - Required provisions & glossary
  - Required format

- State Exchange Option
  - Provide notice to employees by March 1, 2013
  - Content & format not yet issued
Additional Tax

• **0.9% Medicare tax** on higher paid workers
  • Applies to earnings in excess of Single: $200,000; Married filing separate: $125,000; Married: $250,000

• **3.8% tax on net investment income** of higher earning tax payers
  • Applies to net investment income of individuals with AGI in excess of Single: $200,000; Married filing separate: $125,000; Married: $250,000
Additional Tax-Ministers

• No exemption from taxes specifically for ministers

<table>
<thead>
<tr>
<th></th>
<th>0.9% Medicare Tax</th>
<th>3.8% Investment Tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>Potentially applies to minister</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Housing allowance counted toward applicable threshold</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>Housing allowance subject to tax</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>Exemption from SECA exempts from tax</td>
<td>Yes</td>
<td>No</td>
</tr>
</tbody>
</table>
Health Plan Non-Discrimination

• No discrimination favoring “Highly Compensated” employees

• Highly Compensated: highest paid 25% of employees

• Applied to self insured and medical reimbursement for many years

• New application to insured plans (enforcement deferred)
# Health Plan Non-Discrimination

<table>
<thead>
<tr>
<th>Non-discrimination in eligibility</th>
<th>Self-Insured or HRA</th>
<th>Insured Plan</th>
<th>Premium Credit or Refund</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>No</td>
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</table>

| Non-discriminatory in benefit    | Yes                 | Yes          | Yes                       |

<table>
<thead>
<tr>
<th>Consequence of Non-compliance</th>
<th>Taxation of benefit to highly compensated</th>
<th>Substantial penalties to employer</th>
<th>Ineligible for credit or refund</th>
</tr>
</thead>
</table>

| Law in effect?                   | Yes (for many years)                     | Delayed                          | Yes, if want credit or refund   |
Health Care Reform in 2014
Individuals
2014 Compliance: Individual Coverage Requirement

- Starting 1/1/2014, most individuals must have health insurance

- Exceptions
  - Without coverage for under 3 months
  - Can’t afford insurance (but assistance available)
  - Eligible for Foreign Earned Income Exclusion
2014 Compliance: Individual Coverage Requirement

Religious Exceptions

1. "Amish" type group
   • Opposed to acceptance of any retirement benefit, medical or death insurance, public or private; In existence since 1950

2. Religious expense sharing ministry participant
   • Members share expenses with each other; ministry in existence since 1999
2014 Compliance: Individual Coverage Requirement

Penalty will be greater of:

- $695 a year; max. $2,085 per family, or
- 2.5% of household income over income tax filing threshold

Penalty phased in:

- $95/year in 2014
- $325/year in 2015
- $695/year in 2016
Health Care Reform in 2014
Employers
2014 Compliance: Employer Coverage Requirement

Over 200 Full Time Employees
- Automatic enrollment after 90 days
- Effective after issuance of guidance (2014)

50 or more FTE*
- Must offer coverage
- Effective 2014

* 30 or more hours/week
2014 Compliance:
Measuring Size: 50 or more FTE

1. Employees regularly working 130 hours a month or more

2. Add hours of employees regularly working less than 130 hours a month, and divide by 120

3. Sum of full-time employees (#1) and number of equivalent part-time (#2), is FTE

4. Special rules for seasonal, part year, etc.
2014 Compliance: Large Employer Penalties

- Employer subject to penalty if employee obtains coverage from Insurance Exchange
- Penalty if no plan offered
  - $2,000 x (FTE employees less 30)
- Penalty if plan is too expensive
  1. $2,000 x (FTE employees less 30), or
  2. $3,000 x Employees eligible for subsidy
2014 Compliance: Reporting of Coverage to IRS

Annual report to IRS and Employee

- Reporting information about employees covered, portion of premium paid by employer, other information per regulations
- Due by Jan. 31 of following year
- Guidance in process
Compensation

Congress & public concerned about nonprofit executive & minister pay

• Panel on the Nonprofit Sector
• IRS Executive Compensation Initiatives
• Congressional Hearings (Grassley Six)
• Increased Form 990 reporting
Executive Compensation

Two Tax Issues

1. Are all benefits or assistance to executive being reported accurately?
   - Automatic Excess Benefit

2. Is the total value of all benefits, taxable and non-taxable reasonable?
   - Excess Benefit or Private Inurement
Executive Compensation

Accurate Reporting of Benefits

1. Identification
2. Valuation
3. Taxation
4. Documentation
Rebuttable Presumption

What is it?
1. Disinterested board or subcommittee
2. Approval before payment
3. Rely on Appropriate Data
4. Concurrent record

What does it do?
1. More knowledge => Better Decisions
2. Put IRS on Defensive
3. Protect board members, even if loose
Executive Compensation

Recommendations

• Get information on comparable organization compensation practices

• Use “Rebuttable Presumption Process”

• Consider professional assistance
  • If unsure of correct handling of executive benefits
  • If unsure of reasonableness
Independent Contractor, or Employee?
Who Cares?

- Internal Revenue Service
- Department of Labor (and state equivalents)
- Worker’s Compensation Board
- Unemployment insurance agency
- Health reform enforcement agencies
Why Does IRS Care?

Estimated Tax Gap (billions)

- Unpaid Income Tax
- Unpaid FICA/SECA

Employee

Independent Contractor

$120

$100

$80

$60

$40

$20

$-

www.capincrouse.com
IRS Assistance

• **Form SS-8**: Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding

• **Form 8952**: Voluntary Classification Settlement Program

• IRS Publications 15 & 15A

• Quarterly SSA/IRS Reporter
  • http://www.irs.gov/businesses/small/article/0,,id=109886,00.html
Sports Facilities & Coffee Shops
## Unrelated Business Income Tax

### Basic Law

1. **Business Activity**
2. **Regularly Carried On**
3. **Unrelated to Exempt Purpose**

### Exceptions

- **Passive Investments:** (but not debt financed)
  - Interest
  - Dividends
  - Rent from real estate

- **Member Convenience**
- **Sale of donated items**
- **Volunteer Labor**
Sports, Coffee, and UBI

2011 Private Letter Rulings:

Distinguish Ministry from Business

Multiple ways of avoiding UBI

Address questions:

• Does a sports center ministry generate UBI?
• Can an organization that only operates a coffee shop be tax exempt?
Ecumenical Community Center Income

Income from Public:
• Fitness Center-Not UBI
• Sports & recreational fees-Not UBI
• Learning & technology center-Not UBI
• Dance, music and art lessons-Not UBI
• Theater performances-Not UBI
• Debt Financed Rents-Not UBI
<table>
<thead>
<tr>
<th>Why isn’t there any UBI?</th>
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<tbody>
<tr>
<td>Location</td>
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<tr>
<td>Fees</td>
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<tr>
<td>Activities</td>
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<tr>
<td>Rent-DFI Exception</td>
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Medical Rehab. & Fitness Center

- Hospital operated fitness center
- Member categories included general public

<table>
<thead>
<tr>
<th>Member Category</th>
<th>UBI?</th>
<th>Why Not?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hospital Patient</td>
<td>No</td>
<td>Exempt purpose of hospital</td>
</tr>
<tr>
<td>Community members receiving health and fitness</td>
<td>No</td>
<td>Nominal fee or free Instruction &amp; education-exempt purpose</td>
</tr>
<tr>
<td>instruction</td>
<td></td>
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## Medical Rehab. & Fitness Center

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<th>UBI?</th>
<th>Why Not?</th>
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<tr>
<td>Hospital employees</td>
<td>No</td>
<td>Convenience of members exception</td>
</tr>
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</table>
| Community members using for exercise & health | No | “Community Recreational Facility”  
• Fees lower than comparable facility  
• Researched affordability to community |
Non Exempt Coffee Shop Organization

- Provides family friendly, good community environment
- Supported by sales of coffee
- Service & menu like commercial coffee shop
- All profits go to various charitable activities

**IRS:** Coffee shop is unrelated business; “social” and “recreational” are not exempt purposes; profits going to charity irrelevant
Contrast w/ Rev. Rul. 68-72

Organization w/ supervised coffee shop

• Connects college age youth with church leaders, educators, and leading businessmen of the community

• Hold discussions on religion, current events, and social problems

• Personal & vocational guidance provided

• Nominal admission charge
Coffee Shops, Book Stores & “Convenience of the members”

- Exception based on usage
- Doesn’t matter if accomplishes the exempt purpose
- Usage by members, attendees, students
- No promotion to public
- Public usage minimal
  - May have to pay UBIT on regular public usage
Miscellaneous Issues
Can’t swap pay for reimbursement

Revenue Ruling 2012-25

1. Attempts to turn taxable payment into non-taxable reimbursement

2. If worker gets the same amount, regardless of expenses, it is all taxable

3. Proactively plan by reducing compensation to allow reimbursement only when expenses incurred
Minister’s Housing Allowance Status

*Driscoll vs. Commissioner*

- Supreme Court rejected appeal
- Only one house for housing allowance

*Freedom From Religion Foundation, Inc. vs. United States*

- FFRF still challenging constitutionality
- Dist. Court ruled it has standing 8/29/12
Group Exemption Maintenance

- Group exemption: Allows a group of related organizations to be tax exempt w/o separately filing w/ IRS

- Central organization must annually report changes in group to IRS

- Recent letter ruling held an organization was not exempt, because central organization had not reported them

- IRS Survey of 2000 central organizations
Questions?
Thanks!
For your time and attention

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