



*A higher standard.
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Provided by: Evangelical Council for Financial Accountability
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Ministers Opting Out of Social Security

Individuals who qualify for ministerial tax treatment are always subject to the Self Employment Contributions Act (SECA) social security system for services performed in the exercise of ministry *unless* an exemption has been received from the IRS based on the filing with an approval by the IRS of Form 4361.

To claim the exemption from self-employment tax, a minister must:

- File Form 4361
- Be conscientiously opposed to public insurance (which includes insurance systems established by the Social Security Act)
- Desire to opt out because of their individual religious considerations (not because of their general conscience), or because of the principles of their religious denomination—either opposition must be based on religious belief.
- File for other than economic reasons
- Inform the ordaining, commissioning, or licensing body of their church or religious order that they are opposed to public insurance. This includes an opposition for insurance that helps pay for or provide services for medical services (such as Medicare) and social security benefits.
- Establish that the religious organization that ordained, commissioned, or licensed the individual is a tax-exempt religious organization.
- Establish that the organization is a church, convention or association of churches.
- Sign and return the statement IRS mails to the individual to verify that they are requesting an exemption based on the grounds listed on the statement.

Deadline for filing. The application for exemption from self-employment tax must be filed by the date the minister's tax return is due, including extensions, for the second year in which the minister had net ministerial income of \$400 or more. These do not have to be consecutive tax years.

Basis for filing for an exemption from social security tax. Neither economics nor any other nonreligious reason is a valid basis for the exemption. Many ministers are improperly counseled to opt out of social security because it may not be a "good investment." A minister's view of the soundness of the social security program has absolutely no relationship to the application for exemption. Further, there is no basis to opt out of social security because a minister objects to paying the tax or the level of tax paid.

A fundamental consideration is the minister's ability to sign Form 4361 with a clear conscience. Key words in qualifying for exemption from social security coverage on ministerial earnings are "religious principles" and "conscientiously opposed to the acceptance of any public insurance." Religious principles do not simply consist of the conviction that perhaps social security will not be there when you retire or that a better retirement can be purchased through an annuity or other retirement program. The belief must be an integral part of the minister's system of beliefs, the minister's theology.

If a minister opts out and does not have sufficient credits from prior employment or from future non-ministerial employment, neither the minister nor his or her dependents will be covered under social security benefits, survivors' benefits, or Medicare. The decision to opt out of social security should not be taken lightly. First, a minister must act on religious convictions. If a minister untruthfully signs Form 4361, he or she has committed perjury. Second, a minister must be prepared financially with alternatives to the benefits of social security coverage.



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Ministers and Social Security Tax

Social Security taxes are collected on two separate tax systems. Under the Federal Insurance Contributions Act (FICA), the employee pays one half of the taxes and the employer pays the other half. Under the Self-Employment Contributions Act (SECA), the total Social Security tax is paid by the self-employed person, as calculated on taxpayer's Schedule SE.

Ministers are always self-employed for Social Security purposes under the tax law with respect to services performed in the exercise of their ministry, whether employed by a church, integral agency of a church, or a parachurch organization. Ministers are self-employed for Social Security purposes even though they may or may not be employees, depending on the facts, for income tax purposes. Ministers are not subject to FICA-type Social Security taxes, even though they report their income taxes as employees and receive a Form W-2 from their employer. If a church or parachurch organization withholds and matches FICA-type Social Security tax for a minister, the minister is incorrectly being treated as a lay employee.

The Social Security tax status of ministers is based on Sections 1402(c)(4) and 3121(b)(8) of the Internal Revenue Code, which treat ministers as self-employed for payroll tax purposes. Common law employer-employee standards still apply for income tax purposes.

A few clergy may qualify to elect out of self-employment tax under Section 1402(e), the timing of which is conditioned on their self-employment income in the Social Security sense, not the income tax sense. Therefore, Form 4361 must be filed by the due date of the minister's income tax return for the second year in which the minister had \$400 or more of net ministerial income. To opt out of Social Security, a minister must certify that he or she opposes, either conscientiously or because of religious principles, the acceptance of any public insurance (with respect to services performed as a minister), including Social Security coverage. Either opposition must be based on religious belief.

This text is provided with the understanding that ECFA is not rendering legal, accounting, or other professional advice or service. Professional advice on specific issues should be sought from an accountant, lawyer, or other professional.



OPTING OUT OF SOCIAL SECURITY

Q: I heard a prominent financial advisor interviewed recently on a national radio broadcast. A caller asked if ministers should opt out of Social Security. The advisor responded, "Absolutely! Anyone who can get out of Social Security should do so." Do you agree?

A: The financial advisor's response was irresponsible and uninformed because it is based on the common misconception that financial considerations are a legitimate basis for opting out of Social Security. They are not. Ministers may exempt themselves from self-employment taxes with respect to services performed in the exercise of ministry only if several requirements are met. Among other things, the exemption must be filed within a limited time period, and it is available only to ministers who are opposed on the basis of religious considerations to the acceptance of public insurance benefits that make payments "in the event of death, disability, old age, or retirement, or that make payments toward the cost of, or provides services for, medical care." Public insurance includes Social Security and Medicare.

Ministers who exempt themselves from Social Security for invalid reasons may have their exemption questioned in an IRS audit. To illustrate, in 1995 the Tax Court upheld the revocation of a minister's exemption from Social Security on the ground that he did not qualify. The Court noted that the minister's exemption application had been filed on time, but it concluded that the minister was not eligible for exemption because of comments he made during his trial. Among other things, the minister gave the following response when asked whether he was opposed to accepting Social Security benefits on the basis of religious principles (as required by

law to qualify for the exemption): "No. I am not opposed to the—to that, as a religious issue, no. We were advised to—by our accountant, to file for an exemption with the state, providing the state would allow it. And we asked the state to allow it, which they did."

This is an extraordinary ruling that is significant for ministers who are trying to decide whether to file an application for exemption from self-employment taxes (Form 4361). The ruling indicates that filing a timely Form 4361—which contains a certification by the applicant that he or she meets all of the eligibility requirements—may not be enough. The IRS or the courts may later question whether the minister was eligible for the exemption when the Form 4361 was filed.

The court acknowledged that the minister "signed an exemption application stating that he was opposed to public insurance because of his religious principles." However, it found the minister's "trial testimony to be more compelling." *Hairston v. Commissioner, T.C. Memo. Dec. 51,025(M) (1995).*

In summary, opposition to Social Security based entirely on financial considerations is not a basis for exemption. In fact, ministers who heed this "expert's" advice are exposing themselves to substantial penalties, plus back taxes and interest, for doing so. These could easily amount to tens of thousands of dollars.

If you have a financial question, e-mail it to: CFTeditor@christianitytoday.com.

abetting in the substantial understatement of tax. *IRC 6701(b)*. But this approach presents two problems:

- It assumes that the donor claimed a charitable contribution deduction

for the designated gift. In fact, some donors did not get a tax deduction for their gifts because they could not itemize their deductions on Schedule A. Others received a "discounted"

The tax benefit rule is codified in section 111 of the tax code, which states: "Gross income does not include income attributable to the recovery during the taxable year of any amount deducted in any prior taxable year to the extent such amount did not reduce the amount of tax imposed by this chapter."

In several cases, the IRS and the courts have ruled that section 111 requires donors who have received a refund of a charitable contribution made in a prior year should report the refund as taxable income in the year of the refund rather than file an amended return for the year of the contribution deleting that contribution. *See, e.g., Revenue Ruling 75-150.*

KEY POINT. Note that Congresswoman Granger's constituent made his designated contribution to charity "more than two decades ago." According to the IRS, this did not affect his obligation to report the refunded contribution as taxable income.

conclusions

Note the following:

1. So long as a church has not abandoned the project for which designated contributions are solicited, it generally has no legal obligation to return a donor's designated contribution. Quite to the contrary, returning a donor's designated contribution under these circumstances would create the same problems addressed previously in this article.
2. If a church abandons a project for which it solicited designated funds from donors, one option would be for the church to ask donors if they want their contributions to be returned or retained by the church and used for some other purpose. Ideally, donors should communicate their decision in writing to avoid any misunderstandings.
3. Donors should be advised that if they want a refund of their designated contributions they will need to report any refund as taxable income, according to the tax benefit rule. *IRC §111*. The same is true for any accrued interest that is refunded. Some churches have issued donors a Form 1099-MISC under these circumstances to reduce the church's risk of liability for aiding and

Opting Out of Social Security

All ministers are automatically covered by social security (SECA) for services in the exercise of ministry unless an exemption has been received based on the filing with and approval by the IRS of Form 4361. You must certify that you oppose, either conscientiously or because of religious principles, the acceptance of any public insurance (with respect to services performed as a minister), including social security coverage. Either opposition must be based on religious belief. This includes an opposition to insurance that helps pay for or provide services for medical care (such as Medicare) and social security benefits.

To claim the exemption from self-employment tax, you must

- file Form 4361;
- be conscientiously opposed to public insurance (which includes insurance systems established by the Social Security Act) because of your individual religious considerations (not because of your general conscience), or because of the principles of your religious denomination;
- file for other than economic reasons;
- inform the ordaining, commissioning, or licensing body of your church or order that you are opposed to public insurance if you are a minister;
- establish that the religious organization that ordained, commissioned, or licensed you or your religious order is a tax-exempt religious organization;
- establish that the organization is a church or a convention or association of churches; and
- sign and return the statement the IRS mails to you to verify that you are requesting an exemption based on the grounds listed on the statement.



Warning

Opting out of social security is relatively simple. Form 4361 must be filed by the due date of the minister's tax return for the second year with \$400 or more of ministerial income. But the simplicity of opting out should not be confused with the significant difficulty of complying with the requirements for opting out.



Tip

Even though a minister signs Form 4361 and certifies that he or she is opposed to accepting public insurance benefits which is based on earnings from services performed in his or her capacity as a minister, the minister can still purchase life insurance or participate in retirement programs administered by nongovernmental institutions.

Deadline for filing for an exemption

The application for exemption from self-employment tax must be filed by the date your tax return is due, including extensions, for the second year in which you had net ministerial income of \$400 or more. These do not have to be consecutive tax years.

Example 1: A minister ordained in 2010 has net earnings of \$400 in 2010 and \$500 in 2011. An application for exemption must be filed by April 15, 2011, if no extension has been filed. If the minister does not receive the approved exemption by April 15, 2011, the self-employment tax for 2011 is due by that date.

Example 2: A minister has \$300 in net clergy earnings in 2010 but earned \$400 in both 2009 and 2011. An application for exemption must be filed by April 15, 2012, if no extension has been filed. If the minister does not receive the approved exemption by April 15, 2012, the self-employment tax for 2011 is due by that date.

Example 3: A minister, ordained in 2009, earned \$700 net for that year. In 2010, ministerial compensation was \$1,000 and related expenses were \$1,000. Therefore, the 2010 net earnings were zero. Also in 2010, \$7,000 in net self-employment earnings was received from nonministerial sources. In 2011, net ministerial earnings were \$1,500 and self-employment income of \$12,000 was received from nonministerial sources.

Because the minister had ministerial net earnings in 2009 and 2011 that were more than \$400 each year, the application for exemption must be filed by April 15, 2012.

If the minister does not receive the approved exemption by April 15, 2012, the self-employment tax for 2011 is due by that date.

Example 4: A minister was ordained in 2010 with \$1,000 and \$2,000 of net ministerial earnings for 2010 and 2011, respectively. The minister filed Form 4361 in 2011 (this was a timely filing since the last day to file without extensions is April 15, 2012) and the application was approved by the IRS. The minister paid self-employment social security tax on the \$1,000 of net ministerial earnings for 2010 since the Form 4361 had not yet been filed. Based on the approval of Form 4361, the minister can file an amended income tax return for 2010 using Form 1040X (see pages 143-44) and receive a refund of the social security tax paid on the net ministerial earnings for that year.



Tip

If the exemption is approved, it does not apply to nonministerial wages or to any other self-employment income. For example, a bivocational pastor who is employed part-time in a secular job is subject to FICA on the wages from the secular job. If a minister performs independent contractor services unrelated to his ministry, this net profit is subject to social security.

A minister must include with Form 4361 a statement that he has informed the ordaining body of his church of his opposition to the coverage.

Form **4361**
(Rev. January 2011)
Department of the Treasury
Internal Revenue Service

**Application for Exemption From Self-Employment Tax
for Use by Ministers, Members of Religious Orders
and Christian Science Practitioners**

OMB No. 1545-0074

**File Original
and Two Copies**

File original and two copies and attach supporting documents. This exemption is granted only if the IRS returns a copy to you marked "approved."

Please type or print	1 Name of taxpayer applying for exemption (as shown on Form 1040)		Social security number
	Harold T. Baldwin		603-42-8941
	Number and street (including apt. no.) PO Box 183		Telephone number (optional)
	City or town, state, and ZIP code Milton, PA 17647		

2 Check one box: Christian Science practitioner Ordained minister, priest, rabbi
 Member of religious order not under a vow of poverty Commissioned or licensed minister (see line 6)

4 Legal name of ordaining, licensing, or commissioning body or religious order Christian General Conference		3 Date ordained, licensed, etc. (Attach supporting document. See instructions.)
Number, street, and room or suite no. PO Box 5002		7/1/09
City or town, state, and ZIP code Nashville, AR 71852		Employer identification number 48-9017682

5 Enter the first 2 years after the date shown on line 3 that you had net self-employment earnings of \$400 or more, any of which came from services as a minister, priest, rabbi, etc.; member of a religious order; or Christian Science practitioner	10	11
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6 If you apply for the exemption as a licensed or commissioned minister and your denomination also ordains ministers, please indicate how your ecclesiastical powers differ from those of an ordained minister of your denomination. Attach a copy of your denomination's bylaws relating to the powers of ordained, commissioned, and licensed ministers.

7 I certify that I am conscientiously opposed to, or because of my religious principles I am opposed to, the acceptance (for services I perform as a minister, member of a religious order not under a vow of poverty, or Christian Science practitioner) of any public insurance that makes payments in the event of death, disability, old age, or retirement; or that makes payments toward the cost of, or provides services for, medical care. (Public insurance includes insurance systems established by the Social Security Act.)

I certify that as a duly ordained, commissioned, or licensed minister of a church or a member of a religious order not under a vow of poverty, I have informed the ordaining, commissioning, or licensing body of my church or order that I am conscientiously opposed to, or because of religious principles I am opposed to, the acceptance (for services I perform as a minister or as a member of a religious order) of any public insurance that makes payments in the event of death, disability, old age, or retirement; or that makes payments toward the cost of, or provides services for, medical care, including the benefits of any insurance system established by the Social Security Act.

I certify that I have never filed Form 2031 to revoke a previous exemption from social security coverage on earnings as a minister, member of a religious order not under a vow of poverty, or Christian Science practitioner.

I request to be exempted from paying self-employment tax on my earnings from services as a minister, member of a religious order not under a vow of poverty, or Christian Science practitioner, under section 1402(e) of the Internal Revenue Code. I understand that the exemption, if granted, will apply only to these earnings. Under penalties of perjury, I declare that I have examined this application and to the best of my knowledge and belief, it is true and correct.

Signature ▶ Harold T. Baldwin Date ▶ 9/30/11

Caution: Form 4361 is not proof of the right to an exemption from federal income tax withholding or social security tax, the right to a parsonage allowance exclusion (section 107 of the Internal Revenue Code), assignment by your religious superiors to a particular job, or the exemption or church status of the ordaining, licensing, or commissioning body, or religious order.

For Internal Revenue Service Use

Approved for exemption from self-employment tax on ministerial earnings
 Disapproved for exemption from self-employment tax on ministerial earnings

By _____ (Director's signature) _____ (Date)

General Instructions

Section references are to the Internal Revenue Code unless otherwise noted.

Purpose of form. File Form 4361 to apply for an exemption from self-employment tax if you have ministerial earnings (defined later) and are:

- An ordained, commissioned, or licensed minister of a church;
- A member of a religious order who has not taken a vow of poverty; or
- A Christian Science practitioner.

Note. If you are a commissioned or licensed minister of a religious denomination or church that ordains its ministers, you may be treated in the same manner as an ordained minister if you perform substantially all the religious functions within the scope of the tenets and practices of your religious denomination or church.

This application must be based on your religious or conscientious opposition to the acceptance (for services performed as a minister, member of a religious order not under a vow of poverty, or Christian Science practitioner) of any public insurance that makes payments for death, disability, old age, or retirement, or that makes payments for the cost of, or provides services for, medical care, including any insurance benefits established by the Social Security Act.

If you are a duly ordained, commissioned, or licensed minister of a church or a member of a religious order not under a vow of poverty, prior to filing this form you must inform the ordaining, commissioning, or licensing body of your church or order that, on religious or conscientious grounds, you are opposed to the acceptance of public insurance benefits based on ministerial service.

Caution: Very few ministers qualify to file Form 4361. The filing must be based on the minister's conscience or religious principles, not because of a preference to invest retirement funds elsewhere.

A second ordination with a second church generally does not provide a second opportunity for a minister to opt out by filing Form 4361.

Basis of filing for exemption

Neither economics nor any other nonreligious reason is a valid basis for the exemption. Many ministers are improperly counseled to opt out of social security because it may not be a "good investment." Your view of the soundness of the social security program has absolutely no relationship to the application for exemption.

Your first consideration is your ability to sign Form 4361 with a clear conscience. Key words in qualifying for exemption from social security coverage on ministerial earnings are "religious principles" and "conscientiously opposed to the acceptance of any public insurance." Religious principles do not simply consist of the conviction that perhaps social security will not be there when you retire or that a better retirement plan can be purchased through an annuity or other retirement program. The belief must be an integral part of your religious system of beliefs, your theology.



Caution

Opting out of social security is one of the most abused provisions of the tax law that applies to ministers. Too often ministers have opted out because they are concerned about long-term safety of the program or they feel they have a better way to invest the funds. These reasons do not provide a basis to sign Form 4361.

Further, this religious principle must be one that would prevent you from ever asking for the benefits from such a plan based on your church salary. No basis exists for an objection related to paying the taxes or to the level of the taxes to be paid.

If you opt out and do not have sufficient credits from prior employment or from future nonministerial employment, neither you nor your dependents will be covered under social security benefits, survivors' benefits, or Medicare. If you opt out of social security, you should make alternate plans to provide for catastrophic illness, disability, or death, as well as for retirement.

This is not a decision to be taken lightly. First, you must act on religious convictions. Second, you must be prepared financially with alternatives to the benefits of social security coverage.

Although a minister may opt out of social security with respect to ministerial income, the minister may still receive social security benefits related to nonministerial wages or other self-employment income.

Opting back into social security

Until April 15, 2002, ministers could opt back into social security by filing Form 2031. This was a special two-year window based on a law passed in 1999. With the window to opt back into social security closed, there is currently no formal method available for ministers to opt back into social security.