

Legal Counsel for Churches

Corporate Governance for Churches and Their Leaders



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Tax Deductibility for Church Contributions

It's tax season. Your church members may have questions about the tax deductibility of monies paid to the ministry during the year.

As a general rule, charitable contributions made to qualified organization are tax deductible. Churches are qualified organizations. Nonetheless, there are some important rules to keep in mind.

Quid Pro Quo Contributions Rule

A Quid Pro Quo contribution is a payment made to a church partly for charitable reasons and partly for goods or services. If a church member receives a benefit as a result of making a contribution to your church, the donor can deduct only the amount of the contribution that is more than the value of the benefit received. For the excess amount to qualify as a deductible donation, the giver must have had the intent to make a charitable contribution.

For instance, if a contribution of \$100 is made for a church dinner valued at \$40, the charitable contribution part of the payment is \$60. Also, depending on the amount of the charitable part of the contribution, a disclosure statement may be required by the church to the donor. Failure to make the required disclosure may result in a penalty to the church.

The Substantiation and Disclosure Rule

Churches that are tax exempt under section 501(c)(3) of the Internal Revenue Code (IRC) must meet certain requirements for documenting charitable contributions. The federal tax law imposes two general disclosure rules:

1) A donor must obtain a written acknowledgment from a church for any single contribution of \$250 or more before the donor can claim a charitable contribution on his/her federal income tax return;

2) A church must provide a written disclosure to a donor who makes a payment in excess of \$75 partly as a contribution and partly for goods and services provided by the organization.

Recordkeeping Rule

A donor must maintain a record of a contribution of cash, check or other monetary gift to receive a tax deduction. The record must be in the form of either a bank record or a written communication from your church. The written communication from your church may be a receipt or a letter. The receipt or letter you send from your church should include the name of your church, the date of the contribution, and the amount of the contribution. ■

501(c)(3): To Be or Not To Be

The start of a new year begins the practices of filing income tax returns, gathering receipts and finalizing the recordkeeping from last year. Donors may ask if your church is a tax exempt organization under the IRS rules. You may have wondered if your church should apply for a 501(c)(3) status. Now is a good time to have that conversation.

There are two main advantages of having your church classified as a 501(c)(3) organization. First, such organizations under the IRS code are explicitly exempt from federal income tax. Secondly, donors have assurance that their donations are tax-deductible. To qualify for these benefits, most organizations must file an application with the IRS and be recognized as such. Still you wonder, should your church apply for exemption under the 501(c)(3) code.

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The Internal Revenue Service does not require churches to file an application for exemption in order to be tax exempt and receive tax deductible contributions. However, many churches voluntarily file applications for exemption. Many believe that this recognition by the IRS reassures church leaders, members and donors that the church is tax exempt. If your church plans to seek institutional funding from sources like foundations, the IRS designation could be a necessity.

Individual and corporate donors are more likely to support organizations with 501(c)(3) status because their donations are assured of being eligible for a tax deduction. Recognition of exemption under section 501(c)(3) often convinces foundations and other grant-making institutions that they are issuing grants or sponsorships to legitimate recipients.

An IRS determination of 501(c)(3) status is recognized and accepted for other purposes. For example: state officials may grant exemption from state income, sales and property taxes; and the U.S. Postal Service offers reduced postal rates to certain organizations. In other words, the 501(c)(3) status reduces the burden of proving an organization's nonprofit credentials.

If you are considering applying for nonprofit status under the IRS code, you should be aware of three key requirements. First, a nonprofit organization must be organized as a corporation, trust or unincorporated association. Secondly, a substantial portion of your church's operations must further its exempt purpose. Finally,

exempt purposes must be taken from a predetermined list. Religion is included on the list.

Public Inspection Rule

If your church decides to operate under the 501(c)(3) IRS exemptions, you should be aware of the Public Inspection Rule. Your church must make your application for tax exempt status and any annual returns available to the public for inspection, upon request and for no more than a reasonable charge for copying. Each annual return must be made available for a three-year period starting with the filing date of the return. The IRS also makes these documents available for public inspection and copying. These documents must be made available at the church's principal office during regular business hours.

Upon request, an organization must furnish copies of the application and the three most recent annual returns. The requests may be made in person or in writing. For tax years beginning after August 17, 2006, section 501(c)(3) organizations that file unrelated business income tax returns must make them available for public inspection, and the IRS must make those returns publicly available.

If your church decides to apply for exemption under the IRS 501(c)(3) code, you should consider the applicability to your situation. Ultimately, you should make a business case for the benefits and disadvantages of formalizing your church's nonprofit status. ■



All Legal Risks are Not So Obvious.

Churches face legal risks everyday. The only thing worst than mis-managing risks is not seeing the risks in the first place.

Helping clients manage legal hazards is our business. We believe that our church clients should not be surprised in a bad way. We help you identify the legal perils in your path and find workable solutions.

Some legal risks are difficult to spot. Choose a lawyer who will help you keep your footing.

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for Churches



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