



Wespath

BENEFITS | INVESTMENTS

AUMCPBO—NOVEMBER 2018

Wespath Legal Update

Agenda

- **Housing Allowance**
 - Constitutional Litigation
 - Congressional Attention
 - Scenario Planning
- **Tax Cuts and Jobs Act**
 - Moving Expense Payments
 - Unrelated Business Tax Income (UBIT)
- **Other Church Alliance Issues**
 - 403(b)(9) Non-Qualified Church-Controlled Organizations (Non-QCCOs)
 - Church Plan Definition
 - *Form 990* Exemption



Housing Allowance

1954 Code—§119

- General provision: Lodging furnished to any employee is excluded from income **if**:
 - Provided for convenience of the employer,
 - Lodging is on business premises of the employer, **and**
 - Employee must accept such lodging as condition of employment



1954 Internal Revenue Code—§107

- Exclusion for rental value of minister's home (provided as part of compensation):
§107(1) [in-kind housing]
- Exclusion added to statute for allowance paid:
§107(2) [cash housing]
 - To extent used to rent or provide a home
 - Not exceeding fair rental value of the home
 - Including furnishings, utilities, appurtenances



Legal Challenge—Section 107

- First Amendment, U.S. Constitution:
“Congress shall make no law **respecting an establishment of religion**, or prohibiting the free exercise thereof ...”
- Annie Gaylor [officer of the Freedom From Religion Foundation (“FFRF”)] and others filed case against U.S.
 - **Asked court to declare §107(2) unconstitutional**

Judge Barbara Crabb held §107(2) unconstitutional—October 2017

Backstory

- **2002:** Clergy Housing Allowance Clarification Act
- **2010:** FFRF files suit in Eastern District Court, California
 - Dismissal motion for lack of standing
- **2011:** Gaylor and FFRF file in Western District Court, Wisconsin (Judge Crabb)
- **2013:** Crabb ruling: 107(2) violates establishment clause
- **2014:** Court of Appeals dismissal
 - Lack of standing because Gaylor did not ask for tax refund
- **2015:** Gaylor files claim with IRS for housing allowance
- **2016:** Gaylor refiles case

Current Status of Case

- **Defendants appealed to Seventh Circuit Court of Appeals in Chicago**
- Briefs have been filed:
 - Plaintiffs
 - Defendants
 - Intervenors (ministers represented by Becket Fund)
 - Amicus briefs (including Church Alliance; Wespath and GCFA)

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 **FINANCE & ADMINISTRATION**
General Council on Finance and Administration

Oral Arguments

- Court of Appeals heard argument
 - **October 24, 2018**
- Panel
 - Judge Bauer (Ford)
 - Judge Brennan (Trump)
 - Judge Manion (Reagan)
- Advocates
 - Pannucci (government)
 - Goodrich (intermediaries)
 - Chodorow (tax professor, amici)
 - Bolton (FFRF)



Oral Arguments

Key question considered—

Through what lens should we view Section 107?

1. On its own as a tax break only available to ministers?
2. As part of a broader tax scheme about housing that covers other non-religious groups?



Next

- Decision
 - **Early 2019**
- Appeal to Supreme Court?
 - **2019–2020 Term**
- If Supreme Court affirms Judge Crabb's order—**180 days delay** before injunction would take effect

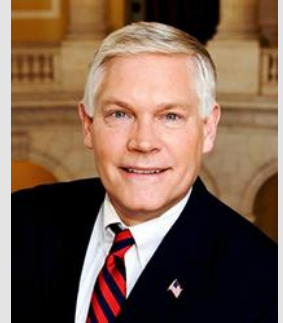


Congressional Support

- **H.Con.Res.129 — 115th Congress (2017-2018)**
- Introducing sponsor: Pete Sessions
 - 24 GOP co-sponsors
- Democrat co-sponsor: Emmanuel Cleaver

Makes this a bipartisan Congressional Resolution in support of the parsonage and housing allowance

Not binding law, but “sense of Congress”



Pete Sessions (R-TX)



Emmanuel Cleaver (D-MO)

What if...?

- The SCOTUS holds §107(2) unconstitutional?
- Church Alliance is analyzing **legislative and non-legislative responses**



Potential Impact

If §107(2) is ruled **unconstitutional**:

- Value of housing/housing allowance **subject to income tax**
- Parsonages remain tax-free while cash housing is taxable
- Search for a legislative response
- Other mitigation steps



Legislative and Other Responses



Legislative Ideas

- Switch Clergy Employment Taxation from SECA to FICA
- Expand Code §119
- “Cure” Code §107(2)



Non-Legislative Idea

- Devise seller financing program for ministers

A background image featuring a pair of ornate scales of justice and a wooden gavel resting on a stack of books. The scales are positioned in the upper half, and the gavel and books are in the lower half. A dark red horizontal band is overlaid across the middle of the image, containing the text.

Tax Cuts and Jobs Act

Tax Cuts and Jobs Act (TCJA)

H.R.1—enacted December 22, 2017
as Public Law 115-97

- Reduced rates
 - **Broadly reduced** corporate (permanently) and individual (temporarily) tax rates
 - **Broadened the base:** Eliminated or repealed moving deductions and exemptions



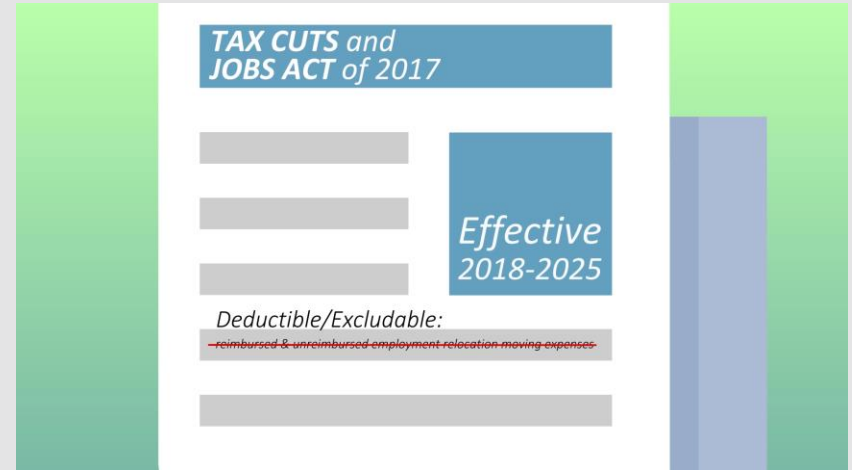
TCJA Impacts

- Moving expense reimbursements—**taxed**
- New taxes [**UBIT (Unrelated Business Income Tax)**] on tax-exempt organizations
 - Tax on qualified transportation fringe benefits for employees (transit and parking)
 - Silo treatment of each line of business



Moving Expense Changes

- Tax Cuts and Jobs Act
- Eliminates deduction and exclusion for employer payments for moving expenses



Impact: New tax liability for clergy

Moving Expenses—The Movie



Reporting Responsibilities

- **Clergy**
 - Reporting of income for taxes
- **Local church or annual conference**
 - Reporting to IRS for tax purposes
- **Annual conference**
 - Reporting to Wespath for employee benefits purposes (CPP, CRSP and RPGA*)



* **CPP:** Comprehensive Protection Plan; **CRSP:** Clergy Retirement Security Program; **RPGA:** Retirement Plan for General Agencies

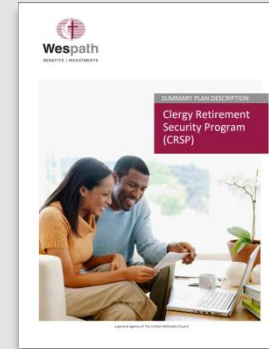
Resources

- **Tax advisers**
- **General Council on Finance and Administration:**
wspath.org/gcfa-tax
- **EY Financial Planning Services:**
wspath.eyfpc.com
- **Wespath Moving Expense Q&A:**
wspath.org/assets/1/7/5236.pdf

Plan Definitions of Compensation

- Clergy plans: CRSP, CPP, UMPIP*, RPGA
- Code §415 Compensation (as included in plan):

“wages, salaries, fees for professional services, and other amounts received ...to the extent the amounts are includable in gross income ...”
- Tax law change makes moving expense reimbursements become **part of plan compensation**



* **UMPIP:** United Methodist Personal Investment Plan

Can't Wespath Simply Amend the Plans?



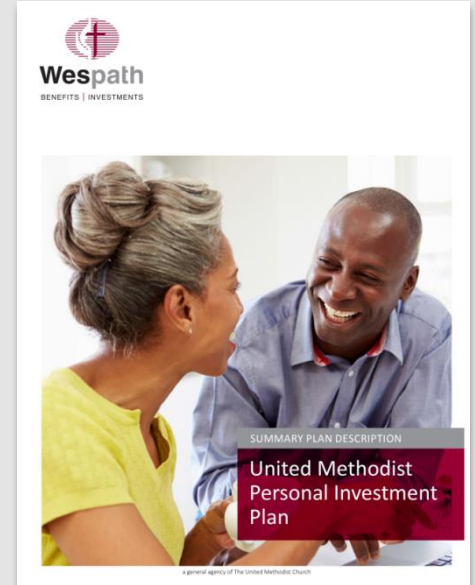
Plan changes to CRSP, RPGA and CPP require **General Conference approval—2020**

Consideration:

Impact sunsets after tax year 2025

UMPIP Amendment

- UMPIP, on the other hand, can be amended before General Conference
- Thus, the Wespath Board of Directors amended UMPIP to remove moving expense payments from compensation for 2018 forward
- **Note:** Those contributing 1% of compensation to CRSP will **also** need to contribute 1% of moving expense payments to get full match



A photograph of a white Gothic Revival church with a prominent steeple. The church features several stained glass windows, including a large central one with a cross and a star. A red banner is overlaid across the middle of the image, containing the text "Tax Cuts and Jobs Act: UBIT".

Tax Cuts and Jobs Act: UBIT

What Is UBTI and UBIT?

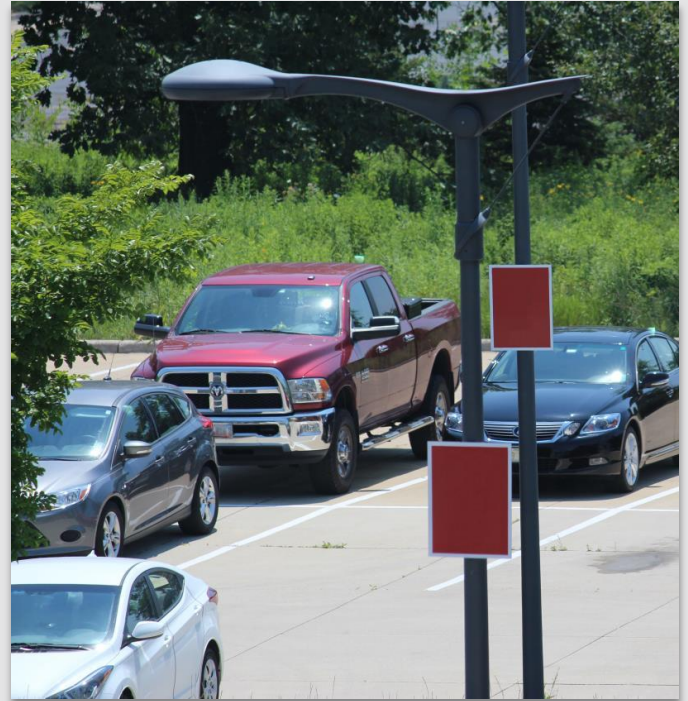
- Tax that a “tax-exempt” organization pays on its unrelated business income:
 - Income from a trade or business
 - Regularly carried on, and
 - Not substantially related to the purpose for the organization’s exemption from tax
- Example (Revenue Ruling 76-402):
 - Tax-exempt museum shows commercial movies at night for an admission fee
 - Income from the commercial movies is **unrelated business taxable income (UBTI)**



Tax Cuts and Jobs Act (TCJA, H.R. 1)

New Section 512(a)(7) – “Church Parking Lot Issue”

- Increases UBTI for tax-exempt organizations equal to amount of qualified transportation fringe benefits (QTFs) disallowed under Section 274
- New Section 274(a)(4) disallows taxable, for-profit employer income tax deduction for QTFs
- **21% corporate tax applies**



Tax Cuts and Jobs Act (TCJA, H.R. 1)

New Section 512(a)(6) – “Siloing”

- Previously, under regulations, if a tax-exempt organization had two or more unrelated businesses, UBTI was calculated by aggregating gross income from the activities and subtracting the aggregate allowable deduction
- Requires UBTI for “more than one unrelated trade or business” to be computed separately
- In the trust and qualified benefit plan context, **37% individual tax** may apply



Section 512(a)(7)

The amount of a tax-exempt organization's UBTI is increased by an amount (*emphasis added*):

- For which a deduction is not allowable under Section 274; **and**
- Which is **paid or incurred** by such organization for:
 - Any QTF*
 - E.g., transportation in a commuter highway vehicle (van pools), transit pass, qualified parking
 - Any parking facility used in connection with qualified parking [as defined under Section 132(f)(5)(C)]



*Qualified Transportation Fringe benefit plan

Concern

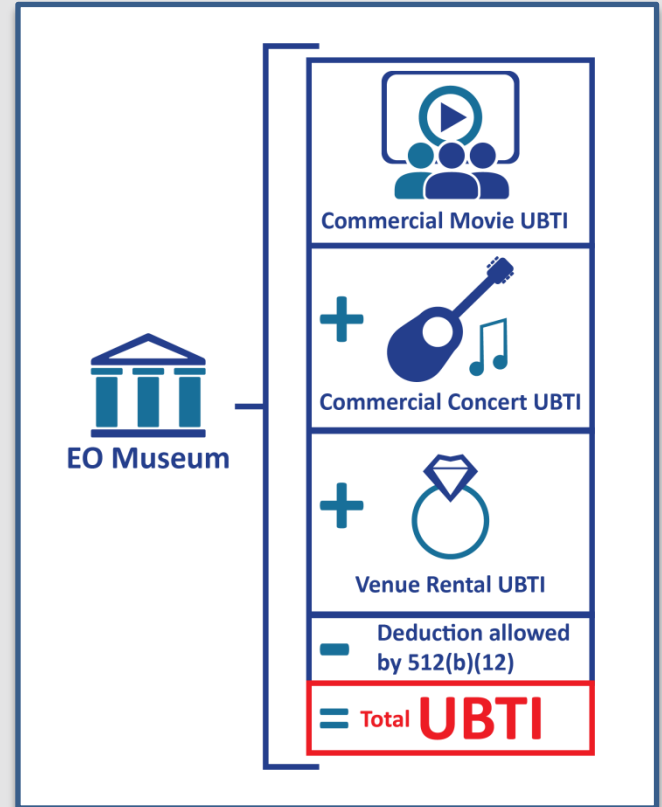
- Most churches and synagogues provide a parking lot
 - Although the parking lot is largely for congregants, it may be used by **employees** during the week
- Churches have never been required to establish cost of providing employees with parking
 - Churches have never had to file *Form 990-T* in order to pay a tax on amounts “spent” by the church to provide parking
- Absent relief, tens of thousands of small churches (volunteer treasurers) may be tasked with filing *Form 990-T* and determining how much tax to pay for their church parking lot
- Many of these churches are in suburban or rural areas, where the amount spent on parking lot is minimal—resulting UBIT will be minimal too

The image shows a Form 990-T, Exempt Organization Business Income Tax Return. The form is for the year 2017 and is for an exempt organization under section 503(c)(3). It includes sections for identifying the organization, reporting business income, and calculating the tax liability. The form is partially filled out, showing various income categories and their amounts.

Section 512(a)(6)

If a tax-exempt organization has
“more than one unrelated trade or business”

- UBTI shall be computed separately for “each such trade or business” (but for each shall not be less than zero)
- And without regard to Section 512(b)(12) (allowed deduction of \$1,000);
- UBTI of the tax-exempt organization shall be the **sum of the above, less the deduction** allowed by Section 512(b)(12)



Concern

- Many church retirement plans invest in a range of alternative investments intended to ensure diversification and increase rates of return
- It is unclear under the new law whether each of these alternative investments would be characterized as an **unrelated trade or business**
- If so, there would be less opportunity to offset gains with losses, leading to a higher UBIT
- The UBIT, in turn, could result in **lower retirement savings** for clergy and church lay workers



Church Alliance Efforts

- **Comment Letter submitted June 26, 2018**
 - Seeking delay of §512(a)(6) and §512(a)(7)
- **Comment Letter submitted August 7, 2018**
 - Offering helpful interpretations of §512(a)(7)
- **Comment Letter likely on interpretations of §512(a)(6)—response to *Notice 2018-67***
- **Meetings with:** Department of Treasury, IRS, House Ways and Means Committee



IRS



Church Alliance Efforts (cont.)

- **Supportive of Repeal Efforts in Congress**
 - Several bills to repeal §512(a)(7) or both §512(a)(6) and §512(a)(7)

Congressmen



Clyburn (D-SC)



Conaway (R-TX)



Walker (R-NC)

Senators



Lankford (R-OK)



Cruz (R-TX)

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Other Church Alliance Issues

403(b)(9) Issue

Internal Revenue Code: Established Practice

A **retirement income account** is a defined contribution program established or maintained by a church, or a convention or association of churches, including a church benefits board, to provide benefits under Section 403(b) for employees of **non-profit, tax-exempt organizations**.



Includes “steeples”
E.g., UMC local churches and annual conferences



Includes QCCOs like church-affiliated daycare programs
E.g., UMC general agencies



Includes non-QCCOs, like denominationally-affiliated universities and hospitals

403(b)(9) Issue

IRS: New Interpretation

A **retirement income account** is a defined contribution program established or maintained ... to provide benefits under section 403(b) for employees of **the church-related organization that established the plan. Non-QCCOs are erroneously excluded from the regulatory definition of a “church-related organization.”**



Includes “steeples”



Includes QCCOs, except in context of pre-approved plan program because IRS has taken the position that QCCOs can become non-QCCOs



DOES NOT include non-QCCOs, like denominationally-affiliated universities and hospitals, which were erroneously omitted

As a result, certain church-affiliated organizations lose the valuable benefits of §403(b)(9) retirement income accounts, face daunting uncertainty, and bear heavy administrative costs.

403(b)(9) Legislation—House and Senators

- Senators Ben Cardin, Pat Roberts and Mike Crapo introduced stand-alone 403(b)(9) bill, S. 674—**March 21, 2017**
- Congressmen Peter Roskam and Ron Kind introduced a House companion, H.R. 2341—**May 3, 2017**



Ben Cardin (D-MD)



Pat Roberts (R-KS)



Mike Crapo (R-ID)

Other Co-Sponsors

Senator



Amy Klobuchar (D-MN)

Congressmen



Mike Kelly (R-PA)



Don Bacon (R-NE)



Lloyd Smucker (R-PA)



Gregory Meeks (D-NY)



Robert Pittenger (R-NC)



Tim Walberg (R-MI)



Mark Meadows (R-NC)



Andy Barr (R-KY)



Barbara Comstock (R-VA)



Ann Wagner (R-MO)



Peter Roskam (R-IL)



Ron Kind (D-WI)

403(b)(9) Legislation—Latest

- **Retirement Enhancement and Savings Act of 2018 (RESA)** was introduced in Senate and House—March 2018
 - Sponsored by Senate Finance Committee Chairman Orrin Hatch and Ranking Member Ron Wyden, and Reps. Mike Kelly and Ron Kind
 - **RESA includes the 403(b)(9) clarification legislative text**
- **House Family Savings Act: 403(b)(9) non-QCCO fix** was included
 - Part of Tax Reform 2.0 package
 - **Passed by House—September 27, 2018**



Hatch (R-UT)



Wyden (D-OR)



Kelly (R-PA)



Kind (D-WI)



Ryan (R-WI)



Brady (R-TX)

Church Plan Rulemaking

- Internal Revenue Code (IRC) Section 414(e) added to the IRC in 1974
 - Defines “church plan”
 - Also “church plan” definition is in ERISA Section 1002(33)
- Final regulations relating to “church plan” definition
 - Issued March 1980
 - Effective September 1974



Church Plan Rulemaking

- Public Law 96-364 [**Multiemployer Pension Plan Amendments Act of 1980 (MPPAA)**] amended IRC 414(e) and ERISA
- Added 414(e)(3)(A):

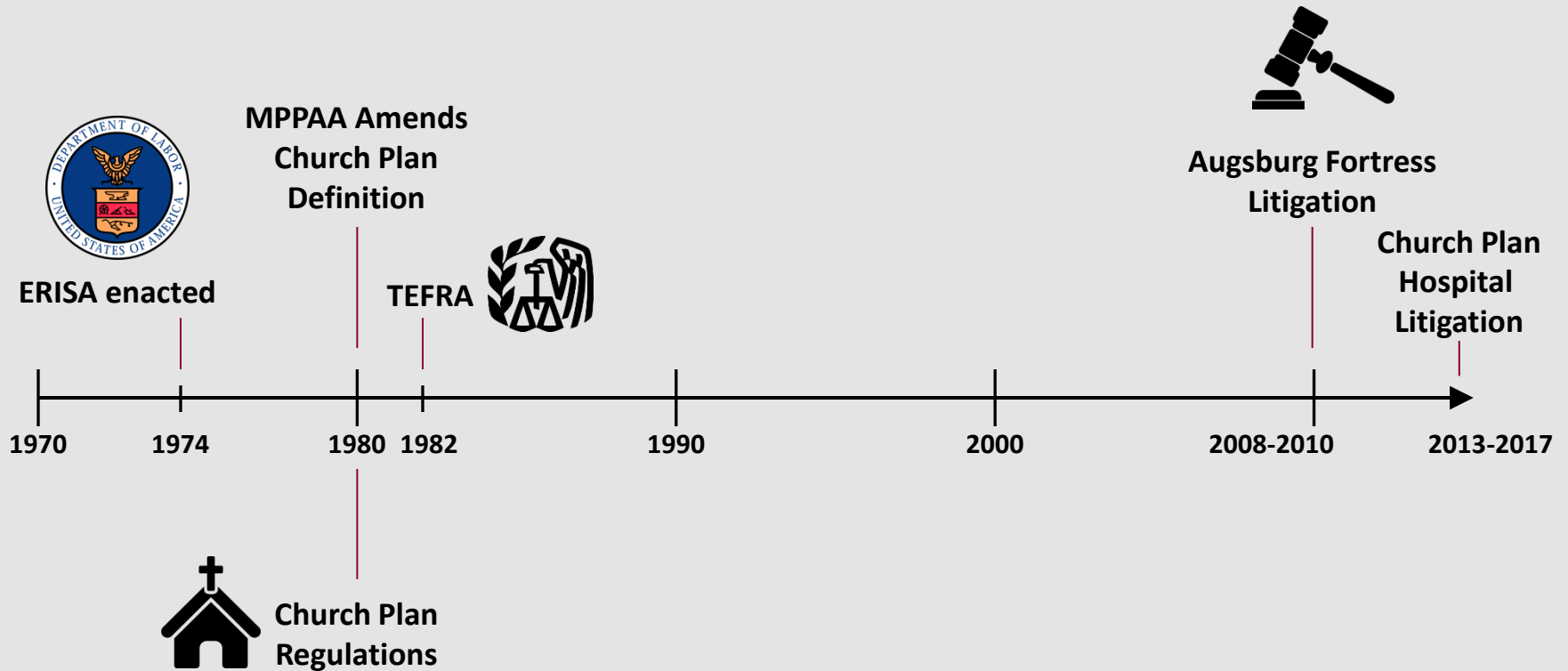


*A **plan established and maintained** for its employees (or their beneficiaries) by a **church or by a convention or association of churches** includes a plan maintained by an **organization**, whether a civil law corporation or otherwise, the **principal purpose** or function of which is the administration or funding of a plan or program for the provision of retirement benefits or welfare benefits, or both, for the **employees of a church or a convention or association of churches**, if such organization **is controlled by or associated with** a church or a convention or association of churches.*

Church Plan Rulemaking

- MPPAA added Section 414(e)(3)(B) (“deemed employees”), which defines “employee” as including:
 - Ministers of a church in the exercise of the ministry, regardless of their compensation source,
 - Employees of any 501(c)(3) entity controlled by or associated with a church or a convention or association of churches, and
 - Former employees
- Among other additions, MPPAA also added Section 414(e)(3)(D), which states:
 - *An organization, whether a civil law corporation or otherwise, is associated with a church or a convention or association of churches if it **shares common religious bonds and convictions** with that church or convention or association of churches.*

Church Plan Rulemaking



Church Plan Rulemaking



June 2017: SCOTUS
Advocate Health Care
Network v. Stapleton



June 2018: Church Alliance
meets with IRS/Treasury

Oct 2018: Possible date for
proposed IRS regulations

July 2018: Church
Alliance meets with
IRS/Treasury



Dec 2017: Andy Hendren finds that
Church Plan Rulemaking is on IRS
priority rules list

Aug 2018: Church Alliance
submits Comment Letter

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Church Plan Rulemaking

[Church Alliance Comment Letter filed \(August 20, 2018\)](#)

- Scope of term “plan”
- What is included in “convention or association of churches”
- Effect of a non-church employer in a multiple-employer church plan
- Types of principal purpose organizations and the ways in which they are used
- Deemed employees
 - Ministers
 - Former employees
 - Employees of a 501(c)(3) organization controlled by or associated with a church, convention or association of churches
 - Controlled by
 - Associated with
- Comments will address: 414(e)(5) ministers
- What is correctable?
- 410(d) ERISA election
- Special rules (in existing regulations)
 - Religious orders and religious organizations
 - “Maintained” by a separately incorporated entity
- Will urge that existing favorable private letter rulings continue to be effective

Church Plan Litigation

- Ongoing in 2018
- May influence church plan rulemaking
- Risks to church plans—mainly in stand-alone employer context



Church Plan Litigation (cont.)

June 2017: SCOTUS decides *Advocate Health Care Network v. Stapleton*

- Church plan may be established by a church-controlled or church associated tax-exempt employer
 - Need not be established by church or denomination

Did *not* decide: 3 questions



Core Lawyer Working Group at SCOTUS

Church Plan Litigation (cont.)

3 questions not addressed by SCOTUS

1. **Constitutionality** of “church plan” exemption from ERISA?
2. **Meaning** of “controlled by or associated with” a church?
3. **Meaning** of “principal purpose of organization”?



Church Plan Litigation (cont.)

Cases since Advocate

- *Medina v. Catholic Health Initiative*
 - 10th Circuit Court of Appeals—**December 2017**
- *Sanzone v. Mercy Health*
 - Eastern District, MO—**August 2018**
- *Rollins v. Dignity Health*
 - Northern District, California—**September 2018**

Form 990 Litigation

FFRF sues IRS over *Form 990* filing— exemption for churches

- Federal District Court for District of Columbia
 - October 11, 2018
- On behalf of Nonbelief Relief, Inc.
 - 501(c)(3)
 - Did not file *Form 990*—3 years
 - IRS revoked tax-exempt status



A close-up, slightly blurred image of the American flag, showing the stars and stripes. The flag is waving, and the colors are vibrant. The stars are in the upper left corner, and the stripes extend across the rest of the frame.

Election 2018

Election 2018—House of Representatives

Forecasting the race for the House



Updated Nov. 1, 2018, at 11:21 AM

6 in 7

Chance Democrats win control (85.0%)

1 in 7

Chance Republicans keep control (15.0%)

↑ Higher probability

Breakdown of seats by party

267 D
168 R

247 D
188 R

227 D
208 R

227 R
208 D

247 R
188 D

AVERAGE

MEDIAN

MAJORITY

CURRENT BREAKDOWN

+59

+38 Democratic seats
AVG. GAIN

+19

10% chance Democrats gain more than 59 seats

80% chance Democrats gain 19 to 59 seats

10% chance Democrats gain fewer than 19 seats

Source:
FiveThirtyEight.com—
projection November 1

Election 2018—Senate

Forecasting the race for the Senate



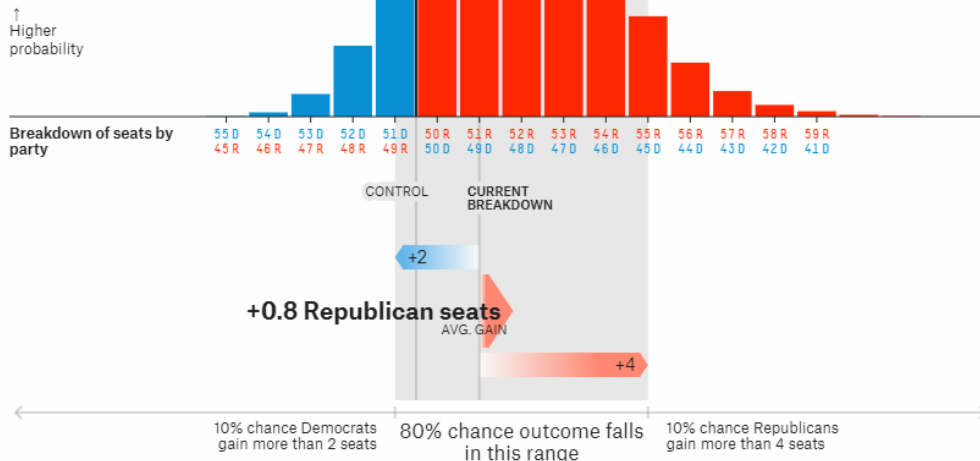
Updated Nov. 1, 2018, at 11:47 AM

1 in 7

Chance Democrats win control (14.9%)

6 in 7

Chance Republicans keep control (85.1%)



Source:
FiveThirtyEight.com—
projection November 1



Wespath and Risk

Mentimeter—1



Mentimeter—2





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