



Housing Allowance Case FAQ Updated October 11, 2017

Late last week, Judge Barbara Crabb of the U.S. District Court for the Western District of Wisconsin issued a decision in the longstanding case involving clergy housing allowances. Given the interest and concern with this case, the Missouri Conference's Office of Finance & Administration thought it might be helpful to answer a few of your most common questions. If you have further questions, feel free to email our Director of Finance & Administration, Rev. Nate Berneking (nberneking@moumethodist.org).

Where did this case come from?

Several years ago, the Freedom From Religion Foundation (FFRF) challenged the Internal Revenue Service with respect to Section 107 of the Internal Revenue Code. Section 107 has two sections. First, 107(1) allows "ministers of the gospel" to receive a parsonage without having to pay income taxes on the value of that home, something they'd otherwise be required to do. The second section, 107(2), allows "ministers of the gospel," to receive tax free housing allowances, subject to just a few limitations. These housing allowances are used by clergy to pay for the home, utilities and even furnishings, and they've also been income tax free since Congress adopted 107(2) in 1954.

The FFRF sued the IRS, claiming that both sections of 107 were in violation of the First and Fifth Amendments of the U.S. Constitution. Initially, however, the FFRF lost on procedural grounds. In order to bring a lawsuit in the United States, a party must have actually suffered an injury. Without an injury, a person has no "standing," to sue. In the FFRF's first attempts, they could not show they were actually injured because they weren't trying to claim a parsonage or housing allowance exemption for themselves. They later remedied some of that problem, but abandoned their attempts to challenge 107(1) (the parsonage section). At this point, Judge Crabb sided with the FFRF and declared 107(2) unconstitutional under the First Amendment (she has never ruled on the 5th Amendment argument). The IRS appealed and the Circuit Court for the 7th Circuit reversed her, but only because that court did not think the procedural or "standing" issue had been resolved.

The FFRF then went back last year and gave certain of its employees housing allowances. They then tried to claim them as tax free with the IRS and demanded a refund of the taxes paid on those allowances. The facts get pretty complicated chronologically, but ultimately, the IRS denied their request and they again brought suit, this time with stronger "standing" arguments. The case came back to Judge Crabb.

What did the judge decide and what was the basis for the decision?

Just like her first decision, Judge Crabb found 107(2) unconstitutional based on the First Amendment. The First Amendment states that "Congress shall make no law respecting an establishment of religion." In a famous 1971 case (*Lemon v. Kurtzmann*), the Supreme Court interpreted that "establishment clause" to prohibit Congress from passing laws if (1) they have no secular purpose; (2) the primary effect of a law is to advance or inhibit religion; **or** (3) the law fosters an excessive entanglement with religion. Judge Crabb's opinion is pretty complicated, but she ultimately used (1) and (2) to find 107(2) in violation of the First Amendment. She reasoned



that the tax exemption for housing allowances is only provided to “ministers of the gospel,” and though the IRS interprets that phrase to broadly include religious leaders in all faiths, it still, in Judge Crabb’s eyes, had the effect of exclusively benefitting religious groups with no other secular purpose.

So, can we not claim housing allowances as tax free anymore?

Actually, it’s way too early to tell. For 2017, your tax free housing allowance is safe. First, Judge Crabb has not actually issued a ruling with respect to the FFRF’s remedy. She made some procedural rulings and then simply issued a “declaratory ruling” in which she found that 107(2) violated the U.S. Constitution. She then instructed the parties to write legal briefs on what the remedy should be. Those briefs won’t be fully completed until November 8, 2017, and she won’t officially decide the result until sometime after that.

In the previous iteration of this case, she enjoined the IRS from allowing tax free housing allowances (theoretically requiring pastors to pay taxes on them), but immediately issued a “stay” of that injunction. A “stay” allows everything to remain status quo until a higher court has a chance to decide an appeal. Judge Crabb didn’t even issue an injunction in this most recent case, but at the end of her opinion, she indicated that she wanted to again hear from the parties as to whether or not a “stay” would be appropriate if she issued another injunction.

In other words, it’s too soon to say what Judge Crabb will actually do. If she again stays her decision pending appeal, the courts will take several months to reach a decision. And, even if she enjoins the IRS, her decision will only have power in the Western District of Wisconsin. The appellate court would affect only pastors in the states under that U.S. Circuit (the 7th). Courts in the U.S. Circuit that covers Missouri (the 8th Circuit) will need to rule before it actually affects Missouri pastors. In fact, Congress could change the tax code before all of that happens anyway.

Are there good arguments in favor of having tax-free allowances?

Absolutely. There are always good arguments, but the truth is, the case is a hard one. When Congress adopted 107(2) in 1954, at least one Congressman, Rep. Peter Mack, spoke on the floor and used explicitly religious reasons to justify support of the law. That looks bad to aggressively secular people like those in the FFRF. At the same time, it’s not at all clear that the FFRF couldn’t actually get the housing exemption for its employees if it claimed them as some form of “clergy.” The IRS has allowed a really broad reading of “ministers of the gospel.” If that’s the case, then it again looks like the FFRF could lack standing to bring the lawsuit.

Good lawyers can always make good arguments, and they almost certainly will do that on appeal. We just have to wait and see.

Who’s looking out for clergy interests?

Well, for Missouri pastors, our office will be constantly monitoring the case and providing information. In addition, there are lots of church-based organizations looking to aid in the defense of 107(2). One, the Church Alliance, has even filed briefs in the case to support keeping 107(2)



exactly as it is. The Church Alliance is an organization made up of the pension and benefits wings of several different religious traditions, including our own, Wespath Benefits & Investments.

What should we do?

For now, nothing. Come April 15, 2018, your 2017 taxes will almost certainly be just as they've always been.

We would offer a word of caution to pastors and churches thinking of switching from a parsonage to a housing allowance. Given the uncertainty, it might be a good idea to wait for some clarity. If Congress were to adopt large scale tax reform, something being discussed, this decision could quickly become irrelevant. The future of clergy housing and its tax treatment is just unclear.

Where can we learn more?

You can read the judge's decision here: <http://s3.amazonaws.com/becketnewsite/District-Court-Opinion-in-Gaylor-v-Mnuchin.pdf>

You might also check out Nate's Book, *The Vile Practices of Church Leadership*, available from Abingdon Press. He devotes a lot of attention to clergy housing in Chapter 4.