

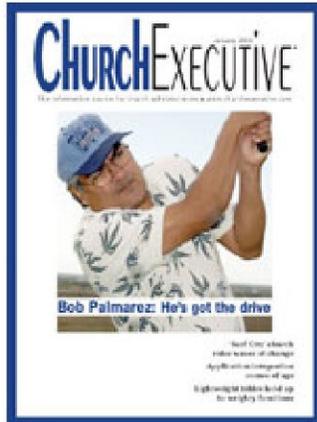
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Tax Issues, by Frank Sommerville, JD, CPA
How to document church expenses

Every church should adopt and follow a "qualified expense reimbursement plan." The tax regulations describe all the elements of such a plan. The employee must submit adequate documentation of allowable expenses to an authority that approves payment of those qualified expenses. You can find a prototype plan at www.wkpz.com. New guidance from the Internal Revenue Service (IRS) provides a plan that can eliminate most paper and still meet the tax regulations.

Adequate documentation

The IRS requires that all expenditures by a church further the church's exempt purposes. Expenses incurred by employees are subject to this rule. The employee is required to prove that they spent money for the item(s) and that they used the item(s) exclusively for church purposes. The employee should present a receipt to prove that they spent the money. The church may (but is not required to) reimburse an expense without a receipt if the amount sought is less than \$75 and is not for a room at a hotel.

The employee should also report how this expense furthers the church's exempt purposes. For example, if a minister purchases a book, they may report that they used this book in sermon preparation.

Certain types of expenses have additional documentation requirements. These include travel expenses, entertainment expenses, gifts, and purchases of computers, cell phones and automobiles. The required additional documentation is explained below.

For travel expenses, the employee must report the purpose of the trip and demonstrate significant activities if overnight travel is involved. For example, a minister may report that they traveled to Toledo to attend a denominational conference, but should include the dates of the conference and where the conference was held. Conferences and conventions that are held outside of North America are under special rules and would require a schedule of

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the conference activities that a minister attended each day.

Ministers frequently entertain others as part of their job. For each entertainment expense, the minister must give the names of those entertained, their relationship to the church and how this entertainment furthered the church's exempt function. The minister must include information about the substantive business discussion that occurred before, during or after the entertainment. For example, a recent court case approved a deep sea fishing trip as a valid entertainment expense when the participants had sat through a business meeting the day before the trip. The company documented the preceding meeting by the materials that it presented at the meeting and the agenda.

Gifts must include the name of the recipient of the gift and their business relationship with the church. The church may reimburse a maximum of \$25 per recipient.

Since computers, cell phones and automobiles are susceptible to personal use, the tax laws require that the church must require a detailed accounting of their use. This does not apply to computers that are housed 100 percent at the church's primary offices.

Timely documentation

The employee must submit the expense reimbursement request along with required documentation in a timely manner. The IRS provides a safe harbor definition of "timely" to be within 60 days of incurring the expense, or within 30 days after returning from a business trip.

Electronic documentation

As many churches have discovered, the required documentation standards use a lot of paper and require a great deal of storage space. Additionally, many of the receipts printed on thermal paper actually disappear within one year from the date of printing. This means that in order to maintain the documentation, the church actually has to copy the receipts adding to the filing and storage burden. In Rev. Rul. 2003-106, the IRS analyzed a company's plan for utilizing electronic documentation thus reducing the paper burden on both the company and the employee.

When receipts are required, the revenue ruling indicated that the church may accept electronic receipts which are then supplemented by the employee with an electronic expense report. Electronic receipts must meet the same requirements as paper receipts. They must show who sold the item(s), how to find them, the date of the sales transaction, a description of the item purchased, the amount paid for the item, and what medium the purchaser used to pay for the item.

The electronic receipt that is included on a credit card statement may meet most receipt requirements unless the additional documentation rules described above apply. In those cases, the employee must supply the additional information and/or paper receipt. The employee may supply the extra information electronically if the employee signs the electronic information submission. For example, the employee may submit an auto mileage log showing where they went on church business, the miles driven and the reason for the trip. The church may scan the actual paper receipts and save the electronic file. It should retain the electronic file as long as needed to prove the expense to the IRS.

A paper receipt is required for all hotel expenses, cellular phone expenses, actual auto expenses and for all expenses that exceed \$75.

Church-issued credit cards

Many churches are issuing credit cards to church employees who are likely to incur business expenses. The church must have a written agreement with the employee that requires repayment of personal items and unauthorized charges within 60 days of the charged item. For states whose labor laws may prohibit such a blanket withholding, the church should consider using the employee's credit cards and avoiding church-issued credit cards. The church would then only pay the expenses documented and the employee would be required to pay the bill for any undocumented expenses.

Frank Sommerville, JD, CPA, is a shareholder in the law firm Weycer, Kaplan, Pulaski & Zuber, P.C. in Dallas, TX, and board-certified in tax law by the Texas Board of Legal Specialization. If you have questions about expense reimbursement plans, e-mail Sommerville at fsommerville@nonprofitattorney.com.

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