NB 3. Housing Equity Fund Recommendations

The Housing Equity Fund was originally created in 1975 for the purpose of providing a savings fund for pastors living in parsonages to enable them to purchase their own home when they leave the parsonage. The congregation that owns the parsonage contributes at least 1% of the Fair Market Value (FMV) of the parsonage to this fund each year that the pastor lives in the parsonage. Originally created as a mutual fund account, the fund unfortunately created unhelpful tax consequences for participants. Therefore, in order for the fund to work properly and accomplish its intended purpose, it is recommended that it instead be invested in a qualified church retirement plan such as the Eder Retirement Plan. The fund currently serves 29 pastors in the denomination.

The impetus for proposed changes to the Housing Equity Fund has rested for the past several years with the Pastoral Compensation and Benefits Advisory Committee of the Annual Conference in consultation with the Office of Ministry. The recommended changes in this business item are the result of their collaboration with the General Secretary's and Treasurer's offices and Eder Retirement Plan.

Details regarding the problems inherent in the current fund parameters are outlined in the accompanying document. If the proposed recommendations are approved by delegates, the Office of Ministry will work closely with Eder Financial and the Church of the Brethren Treasurer's office to communicate to pastors the needed information regarding the changes in the fund as well as their options for participating in the fund. Some of the important points of the proposed changes (as outlined further in the documents below) include the following:

- Pastors will have a choice regarding whether or not to move existing MMA Praxis Mutual Fund accounts to the Eder Retirement Plan.
- Future contributions to the Housing Equity Fund will be made to the Eder Retirement Plan to a separate account under the pastor's name administered by Eder Financial, Inc.
- Future contributions should be pre-tax contributions in order to take full advantage of the housing allowance which can only be accessed from a church retirement plan like the Eder Retirement Plan. Roth plans and IRAs (even from Eder Retirement Plan) do not qualify for housing allowances in retirement.
- Pastors will be able to request access to these pre-tax funds tax-free before age 591/2 when they leave the parsonage in order to purchase a home. After age 591/2, pastors may use these pre-tax funds for all housing-related expenses tax-free.

Upon the approval by the Mission and Ministry Board at its October 2023 meeting, these recommendations are now presented to delegates by the Office of Ministry and the Pastoral Compensation and Benefits Advisory Committee of the Annual Conference.

Pastoral Compensation and Benefits Advisory Committee
Robert McMinn, Chair
Art Fourman, Laity
Angela Finet, Clergy
Lori Hurt, secular compensation practitioner
Andy Hamilton, District Executive Minister representative
Nancy Sollenberger Heishman, Director, Office of Ministry
Deb Oskin, past chair, continuing in an advisory role

Action of the Mission and Ministry Board

The Mission and Ministry Board at its meeting on Sunday, October 22, 2023, adopted the "Housing Equity Fund Recommendations" by consensus and affirmed the recommended changes as presented for forwarding to the 2024 Annual Conference for adoption.

APPENDIX ONE

Pastors Housing Fund Proposal
Our objective is to create a pathway to permit Pastors Housing Fund contributions to be held in the Eder Retirement Plan (ERP), with respect to existing funds currently held in Praxis Mutual Funds and future contributions. The primary benefit of doing so is that there will be more favorable tax treatment for those funds going forward.

1. The current Pastors Housing Fund accounts are held in Praxis Mutual Funds.
   a. These accounts are for those pastors who live in a parsonage.
   b. They are held in the name of both the pastor and the Church of the Brethren, Inc. (CoBI).
   c. The account is funded by the congregation.
   d. The contributions are taxed to the pastor when made and the earnings on the distributions are taxed.
   e. It is our understanding that these amounts are not treated as eligible for housing allowance.
   f. Funds can be withdrawn with CoBI approval for the purchase of a home or home repairs.
   g. Out of privacy concerns, Eder has not been provided with the names of the individuals with balances at Praxis. We believe most, if not all, of these individuals already have ERP accounts.

2. Proposal for **Existing** Pastors Housing Fund Accounts.
   a. Permit pastors to make after-tax contributions to the ERP from the amounts currently held in Praxis Mutual Funds.
      i. These contributions would then be held as a sub-account in the ERP, subject to the investment and distribution rules of the ERP (which are discussed below).

ii. The amount of permitted after-tax contributions will be limited to the amount held in the Praxis Mutual Funds.

b. These after-tax contributions will be optional. A pastor is free to retain the Pastors Housing Fund account at Praxis with no change. However, if approved, future Pastors Housing Fund contributions will be made to an ERP account (as discussed below).

c. If a pastor chooses to make these after-tax contributions, the amount that can be transferred will be subject to IRS annual limits, so it is possible that the transfer may need to happen over multiple years.

d. Because the Praxis accounts are jointly owned by the pastor and CoBI, CoBI will need to consent to the transfer of these amounts out of the current Praxis accounts. Following the contribution to the ERP, CoBI will no longer have joint ownership of the account.

3. Proposal for **Future** Pastors Housing Fund Contributions.

a. Future Pastors Housing Fund contributions will be contributed by the congregation to the ERP as employer contributions instead of being contributed to the Praxis Mutual Funds.

i. It is proposed that this change be mandatory, meaning that congregations would not be permitted to contribute to the Praxis Mutual Funds but would be required to make Pastors Housing Fund contributions to the ERP.

ii. These future contributions would be made by the congregation only. Pastors will not make pre-tax contributions to the Pastors Housing Fund subaccount in the ERP (though they would be eligible to make regular pre-tax or Roth deferrals to the ERP).

b. The process for determining the amount of the Pastors Housing Fund contribution is not affected by this proposed change.

i. Currently, the PCBAC recommends that a congregation's Pastors Housing Fund contribution be 1% of the fair market value of the parsonage – though congregations can choose to contribute a different amount.

c. The congregation's Pastors Housing Fund contributions will go into a separate pre-tax, restricted Pastors Housing Fund sub-account in the ERP.

i. This sub-account would be subject to the investment and distribution rules of the ERP (which are discussed below).

d. Congregational contributions to the Pastors Housing Fund subaccount will be in addition to any general retirement contributions made by the congregation and/or the pastor.

e. The total contributions to the ERP will be subject to IRS annual limits. Generally, total contributions to a 403(b) plan cannot exceed the lesser of 100% of the participant's compensation for the year or a fixed dollar amount ($66,000 for 2023). Congregations and pastors will want to review in advance whether it is possible that the total contributions (including both the congregation's and the pastor's contributions) could exceed this limit.

4. Tax Considerations.

a. As noted above, Pastors Housing Fund contributions are currently taxable to the pastor upon contribution and earnings are taxed at distribution (if not sooner due to purchases and sales of individual funds).

b. Under the proposed structure:

i. A pastor's after-tax contributions to the ERP will already have been taxed, so would not be taxed upon distribution. Earnings on those contributions will be subject to income tax until distribution and could potentially be eligible for rollover after age 59½ if not used for housing expenses.

ii. A congregation's Pastors Housing Fund contributions to the ERP will not be taxed at the time of contribution. Contributions and earnings will be taxed at the time of distribution and could potentially be eligible for rollover after age 59½ if not used for housing expenses.

iii. Distributions from the ERP are potentially eligible for exclusion from income tax under the housing allowance exclusion, subject to the applicable limits under the Internal Revenue Code.

5. Investment of Pastors Housing Fund Contributions in the ERP.

a. In the ERP, participants are able to choose how their accounts will be invested among the available ERP investment options. If no investment election is made, the contributions are invested by default into the target date fund that most closely matches the participant's projected retirement date – subject to the participant's reallocation of those funds at any time.

b. Contributions to a Pastors Housing Fund account in the ERP would be subject to the same rules. If the pastor has an existing account in the ERP, then new contributions will be invested in the same manner as the pastor's existing account. If the pastor does not have an existing account, the pastor can designate investments and, if no designation is made, the amounts will be defaulted into the applicable target date fund.

c. Pastors will have access to all the resources available to ERP participants, such as investment education, access to Eder Values Investing options and retirement readiness resources.

6. Distribution of Pastors Housing Fund Contributions in the ERP.

a. The ERP has specific rules regarding the timing and form of withdrawals from the ERP. Those rules will be modified to address Pastors Housing Fund contributions.

b. Prior to the pastor attaining age 59½, amounts in the Pastors Housing Fund subaccounts (both the after-tax and pre-tax subaccounts) will only be eligible for withdrawal to satisfy the financial hardship related to the purchase of a principal residence for the pastor (this would exclude mortgage payments). As part of this requirement, the pastor would be required to confirm that the pastor does not have other resources available to satisfy the financial need.

c. When the pastor reaches age 59½, congregation contributions to the Pastors Housing Fund subaccount in the ERP will be eligible for distribution on the same basis as other amounts in the ERP – with slight modification.

i. **Employer Contributions:** For amounts contributed by employers, the ERP provides that:

(1) An active participant (still employed or on a pastoral placement list) can request periodic payments (installments) at age 59½ and an annuity at age 65.

(2) A terminated participant can request periodic payments or an annuity at age 59½.

(3) A terminated participant who is younger than age 59½ can request a distribution prior to age 59½ upon approval by Eder to alleviate a significant financial hardship.

These rules would also apply to employer contributions to the Pastors Housing Fund subaccount plus pastors would be able to request a lump sum distribution of that subaccount at age 59½ - regardless of whether terminated or active.

ii. **After-tax Contributions:** After-tax contributions are subject to the same distribution rules that apply to pre-tax and Roth contributions. For these amounts, the ERP provides that:

(1) An active participant (still employed or on a pastoral placement list) can request a lump sum distribution or periodic payments (installments) at age 59½ and an annuity at age 65 (if the entire account is being annuitized).

(2) A terminated participant can request a lump sum distribution or periodic payments at any time and can request an annuity at age 59½ (if the entire account is being annuitized).

These rules would apply to the after-tax contributions to the Pastors Housing Fund except that pastors would not be able to access those contributions prior to age 59½ except to satisfy the financial hardship related to the purchase of a principal residence for the pastor.

d. Process for distributions.

i. Eder will work with its recordkeeper to establish an application and review process for withdrawals from the Pastors Housing Fund subaccounts.

(1) It needs to be determined whether the CoBI Office of Ministry will be involved with the review process.

ii. Spousal consent will be required for any withdrawal.

7. Next Steps.

a. If approved by the Mission and Ministry Board, the proposal would need to be approved by Annual Conference.

b. If approved:

i. Congregations that have not already adopted the ERP will need to execute an adoption agreement and prepare for implementation.

ii. To facilitate planning, we suggest that CoBI secure permission from the Pastors Housing Fund participants to share the details of their accounts with Eder.

(1) This will identify if any new accounts need to be opened, inform funds transfer, identify potential issues with annual IRS dollar limits, and assist with investment mapping.

iii. The process for electing after-tax contributions from the Praxis Mutual Funds to the ERP would need to be documented.

iv. The Integrated Annual Ministry Agreement would need to be updated to reflect that PHF contributions are now being made to the ERP (the current Agreement indicates that PHF contributions are held in a taxable mutual fund account).

APPENDIX TWO

FACTS TO KNOW ABOUT THE PASTORS' HOUSING FUND

The impetus for proposed changes to the Housing Equity Fund rests with the Pastoral Compensation and Benefits Advisory Committee of the Annual Conference in consultation with the Office of Ministry. The recommended changes are the result of collaboration with the General Secretary's and Treasurer's offices and Eder Retirement Plan. The purpose of the Pastors' Housing Fund is to help pastors who have been living in parsonages to purchase their own home when they leave the parsonage. The congregation that owns the parsonage contributes at least 1% of the Fair Market Value (FMV) of the parsonage to this fund each year that the pastor lives in the parsonage.

According to the 1975 action by Annual Conference, this fund was set up as a Mutual Fund account. However, for it to work properly for its purpose, it needs to instead be invested in a qualified church retirement plan, such as the Eder Retirement Plan.

Here are the problems with investing Housing Equity Funds in mutual funds as contrasted with a church retirement plan:

When Housing Equity Funds from the congregation are invested in a **non-retirement mutual fund (such as Praxis):**

1. These funds are not deferred compensation and are added to the pastor's W-2 Box 1 as taxable compensation. Pastor pays both income and self-employment taxes on these funds.
2. When the mutual funds are sold, the pastor may have taxable gains (in addition to having already paid income and self-employment taxes on the contributions to the fund by the congregation).
3. Mutual funds cannot be designated as housing allowance, so the preferential tax treatment of a designated housing allowance cannot be used, even though the funds will be used to purchase a home.

In contrast, when Housing Equity Funds from the congregation are invested in a special sub-account in the **Eder Retirement Plan:**

1. Contributions from the congregation are treated as deferred compensation (just like the congregation's contribution to the pastor's retirement account, appearing on the W-2 in Box 12, Code E), and are not taxable at the federal level.

2. When the pastor leaves the parsonage, funds in the Pastor's Housing Fund sub-account can be distributed to the pastor for the purchase of a home only (if the pastor is younger than age 59½), and the pastor won't be required to pay income or self-employment taxes on these funds.
3. After age 59½, funds in the Pastor's Housing Fund sub-account can be withdrawn for any purpose. If the funds are used for housing, the pastor will not pay income taxes on the distributed funds. Income taxes will apply to those funds not used for housing.

FACTS TO KEEP IN MIND

- Pastors will have a choice regarding whether to move existing MMA Praxis Mutual Fund accounts to the Eder Retirement Plan where they would be held in a separate post-tax fund (as taxes have already been paid on those funds). If the pastor leaves the existing funds in the mutual funds account, they will continue to pay taxes on those funds annually and those funds will not be eligible for housing allowance treatment.
- Future contributions to the Housing Equity Fund will be made to the Eder Retirement Plan to a separate account under the pastor's name administered by Eder Financial, Inc. Any withdrawals made from this account prior to age 59½ will require the approval of Church of the Brethren, Inc. These future contributions will grow tax-free in a tax-deferred account, similar to a retirement account, specifically set up for pastors' housing.
- Future contributions should be pre-tax contributions in order to take full advantage of the housing allowance which can only be accessed from a church retirement plan like the Eder Retirement Plan. Roth plans and IRAs (even from Eder Retirement Plan) do not qualify for housing allowances in retirement.
- Pastors will be able to request access to these pre-tax funds tax-free when they leave the parsonage in order to purchase a home before age 59½. After age 59½, pastors may use these pre-tax funds for all housing-related expenses tax-free. Also, after age 59½, pastors may use these pre-tax funds for non-housing related expenses, but income taxes will be incurred when those funds are not used for housing.

For more information, contact:

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Deb Oskin, past chair, continuing as advisor for this project