

## **DISCRETIONARY FUNDS GUIDELINES**

Revised March 2009

The subject of discretionary funds has raised a number of questions from both clergy and the laity. These guidelines are intended to bring about uniformity in the handling of these funds and to clarify their use and the requirements as to accountability.

### **Background Information**

The provision in the national canons of The Episcopal Church regarding discretionary funds lies in Title III, Canon 9.5.b(6), which states:

The Alms and Contributions, not otherwise specifically designated, at the Administration of the Holy Communion on one Sunday in each calendar month, and other offerings for the poor, shall be deposited with the Rector or Priest-in-Charge or with such Church officer as the Rector or Priest-in-Charge shall appoint to be applied to such pious and charitable uses as the Rector or Priest-in-Charge shall determine. When a Parish is without a Rector or Priest-in-Charge, the Vestry shall designate a member of the Parish to fulfill this function.

This section originated at the Convention of 1814, at which time all of the Alms and Contributions received at the Administration of Holy Communion were to be put to these uses (providing for the poor and pious and charitable uses). At that time it was customary to have only one celebration of Holy Communion each month. By 1904, however, most churches were having at least one celebration of Holy Communion each week, and often more. For this reason, the Canon was changed to apply to only one celebration per month, and then only to contributions otherwise undesignated. In other words, the loose offering from one communion service per month goes to a fund to be administered by the rector or priest-in-charge, together with “other offerings for the poor.” It is now often customary to supplement the discretionary fund with gifts from individuals and also from the parish’s general operating funds. Of particular importance in the Canon are the words “Alms,” “Contributions” and “Offerings”, which clearly mean that these are funds given to the church and therefore belong not the Rector or Priest-in-Charge, but rather to the church.

Title I, Canon 7.1(f) of The Episcopal Church states as follows:

All accounts of the Diocese shall be audited annually by an independent Certified Public Accountant. All accounts of Parishes, Missions or other institutions shall be audited annually by an independent Certified Public Accountant, or independent Licensed Public Account, or such audit committee as shall be authorized by the Finance Committee, Department of Finance, or other appropriate diocesan authority.

The Canons of The Diocese of East Tennessee require compliance with this provision. For the reasons set forth above, it is clear that discretionary funds are “accounts of the parish” and therefore are subject to being audited, although procedures may be utilized to keep confidential how the funds were used.

In addition, particular attention should be paid to applicable civil law, specifically tax law, which includes the following principles:

- a. Money flowing from an employer (a church) to an employee (the priest) for the employee’s personal use is generally taxable as income to the employee.
- b. Money given in exchange for services is generally taxable as income.
- c. Gifts or donations are deductible by the donor only if given to an exempt organization, and are not deductible if given to an individual, either directly or indirectly.

### **Discretionary Funds Guidelines**

With the foregoing in mind, the following guidelines should be helpful:

1. **Use of funds.** As outlined in Canon III.9.5.b(6) above, permissible uses of discretionary funds are for the poor and for “other charitable and pious purposes.” Obviously, gifts to the poor are the primary purpose. “Other charitable and pious purposes” includes gifts to any recognized charitable organization to which an individual could make a tax-deductible gift, gifts to the church itself, and the purchase of items used in the parish for its purposes, such as vestments, books, and other tools of the trade that will remain the property of the parish. (These are examples only, and not intended to be an exhaustive list). Purchasing books for the priest’s personal library or paying other personal expenses of the priest are not proper uses. Discretionary funds may be used for any legitimate church purpose, but the better practice is for business expenses of the clergy to be paid by the church through an expense account or expense allowance, and not be funded through the discretionary fund.
2. **Recipient of gift: Priest’s Discretionary Fund.** Because discretionary funds are property of the parish, rather than the priest, checks for gifts should be made payable to the parish, rather than to the individual clergy member, even though the gift is intended to go to the priest’s discretionary fund. A gift to the parish is tax deductible, whereas a gift payable to the priest is not.
3. **Restrictions on gift.** A gift to the discretionary fund may either be unrestricted or, if restricted, must be designated for one of the legitimate purposes of the church. In other words, funds cannot be donated to the discretionary fund with the restriction that they be used to pay for individual expenses beneficial to a relative of the donor, such as to pay for

the donor's children's school expenses or the donor's aunt's stay at the nursing home, even if the intended individual beneficiary has a need. Such an attempt to make a gift tax-deductible by funneling it through the discretionary fund violates tax law. The gift will not be tax deductible, and the clergy should not look the other way if such a gift is made, but should instead refuse the gift.

4. **Gifts to clergy.** The discretionary fund is not the proper vehicle for a gift to a priest. While it is possible for an individual to make a gift to a member of the clergy, such a gift is not tax deductible by the donor, nor taxable to the clergy member, and does not go into the discretionary fund. Funds given to clergy for services rendered, such as performing weddings, funerals, et cetera, if passed along to the member of the clergy for personal use, constitute taxable income.
5. **Not property of the clergy.** The priest's discretionary fund is not the priest's money. While he or she has discretion as to which permissible use the funds should be expended on, the funds are not to be used for the clergy member's personal needs, such as sending his or her children to college or taking the family out to eat. Because the funds are property of the parish, discretionary funds, along with any items purchased with these funds, remain at the church when the priest is called elsewhere.
6. **Bank account.** As provided in the *Manual of Business Methods in Church Affairs*, all discretionary funds must be deposited into the general operating account of the congregation, using its federal employer's tax identification number. All gifts and donations intended for the discretionary fund, whether delivered to the church or to the clergy member, shall be deposited into this account, and appropriate receipts should be given to the donors. With approval of the vestry, a separate bank account may be established into which discretionary funds are subsequently transferred. However, this account shall also be in the name of the congregation, such as "Good Shepherd Episcopal Church; Rector's Discretionary Fund." Some expenditures from this account may merit confidentiality, such as payments made on behalf of a member of the congregation with a personal financial need that has been made known to the priest in confidence. Therefore, it may be appropriate to handle this account differently from other church accounts. Cash disbursements and checks made out to "cash" are highly discouraged, and should only be made when there is a real emergency and a check cannot meet the needs. The priest must maintain detailed private records of precisely what is done with the proceeds of all such expenditures. This provides protection for the clergy member in case of an IRS audit or in case a question arises about the propriety of the expenditures.
7. **Audit.** Arrangements must be made for someone other than the clergy member to review this bank account and the associated private records, on a confidential basis, as part of the annual audit. Ideally, a trusted representative of the firm or team doing the audit, or the senior warden or

some other responsible member of the parish, should have a private conference with the priest regarding the records and audit.

8. **Duty of care.** The person administering a discretionary fund is in a position very similar to that of a trustee. He or she is handling funds that are not his or her property. Such person is therefore obligated to use a high degree of care, to refrain from wasting the funds or commingling them with personal funds, and to use them for the purposes for which they were entrusted to his or her care.
9. **Internal Revenue Service.** Remember that the IRS can audit churches, clergy and individual donors.

The foregoing are intended as guidelines only. The exercise of common sense and good judgment is highly recommended in dealing with issues involving discretionary funds. For additional guidance, please see the *Manual of Business Methods in Church Affairs*, which is available at [www.episcopalchurch.org/finance\\_58218\\_ENG\\_HTM.htm](http://www.episcopalchurch.org/finance_58218_ENG_HTM.htm) .

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