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Church-Affiliated Orgs May Have To Comply With ERISA


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Law360, New York (April 21, 2016, 10:29 AM ET) -- Since the early 1980s, the Internal Revenue Service and the U.S. Department of Labor have interpreted the so-called "church plan exemption" to the Employee Retirement Income Security Act of 1974 to permit certain religious-affiliated organizations, such as hospitals, colleges and charities, to establish and maintain retirement plans exempt from ERISA requirements. In Stapleton v. Advocate Health Care Network[1], decided by the Seventh Circuit of the U.S. Court of Appeals on March 17, 2016, the court interpreted ERISA's definition of "church plan" to include only benefit plans actually established by churches, although such plans could be administered by organizations associated with or controlled by churches. Although this shift in authority has been on the horizon, the Seventh Circuit's decision should cause church-affiliated entities to take stock of their retirement plans and past positions.

ERISA, the federal law governing employee benefit plans, imposes certain administrative requirements on employee benefit plans and, in conjunction with the Internal Revenue Code, requires compliance with minimum funding, vesting and nondiscrimination rules applicable to qualified retirement plans. Nevertheless, ERISA exempts "church plans" from its requirements and defines a church plan as a plan "established and maintained ... for its employees ... by a church or by a convention or association of churches which is exempt from tax under section 501 of the Internal Revenue Code." ERISA further states that a church plan includes a plan maintained by an organization "controlled by or associated with a church or by a convention or association of churches." In recent years, plaintiffs attempting to assert claims under ERISA have challenged the exemption of organizations that are not actual houses of worship.

The Seventh Circuit's decision in Stapleton pertained to the benefit plans maintained by Advocate Health Care Network, based in Illinois, and affiliated with the Metropolitan Chicago Synod of the Evangelical Lutheran Church and the Illinois Conference of the United Church of Christ, but not owned or financially supported by either church. Advocate operates 12 hospitals and numerous other health care locations and employs 33,000 employees. Advocate operated its benefit plans, including its defined benefit retirement plan, as exempt from ERISA, largely relying upon earlier letter rulings from the IRS affirming the church plan exemption as to predecessor organizations and plans.

The plaintiffs alleged that Advocate had not administered its pension plan in accordance with ERISA and that participants in the plan were thereby treated less favorably than was required. The district court held that Advocate was not entitled to ERISA's church plan exemption because ERISA's statutory definition of church plan required the plan to be established by a church. The Seventh Circuit affirmed.

Advocate argued that the IRS and DOL had interpreted church plans to include not only those that were established by churches, but also those that were established by religious-based organizations controlled by or associated with churches. The Seventh Circuit declined to defer to the IRS and DOL because it deemed the statute unambiguous. Thus, the Seventh Circuit interpreted ERISA to define "church plan" to include only benefit plans actually established by churches, although a subset of such plans could be those administered by organizations associated with or controlled by churches.

The court referred to a December 2015 decision, Kaplan v. St. Peter's Healthcare System[2], in which the Third Circuit discussed a hypothetical situation wherein Congress enacted a law offering free health care to all disabled veterans. A later clarification that "disabled veterans" included members of the U.S.

National Guard would not be reasonably interpreted to mean that a person who served in the National Guard but who was not disabled would qualify for free health care. Similarly, the Third Circuit reasoned that the initial requirement in ERISA that a church plan must be established by a church cannot be ignored, even though it was later modified by a provision indicating that "church plans" included plans maintained by organizations associated with churches.

Prior to the Stapleton decision by the Seventh Circuit and the Kaplan decision by the Third Circuit, the main concern of religious-affiliated organizations that were not actual houses of worship was whether or not they were sufficiently "associated with or controlled by" an actual church, i.e., whether they were tied closely enough to a church to be entitled to the ERISA exemption. With these decisions on the books, however, the ERISA church plan exemption for all organizations that are not actual churches (or other houses of worship, such as synagogues and mosques) is effectively discontinued in the states covered by the Seventh (Illinois, Indiana and Wisconsin) and Third (Delaware, New Jersey and Pennsylvania) Circuits. For such organizations that maintain defined benefit pension plans, loss of the ERISA exemption may require the contribution of millions of additional dollars to remedy a shortfall in ERISA funding requirements, as well as impose greater administrative burdens in the form of certain nondiscrimination testing, reporting and disclosure obligations required by ERISA. For such entities that maintain defined contribution plans, the concerns will be of a more administrative compliance nature but will be problematic nonetheless.

An issue not fully addressed by either the Seventh or Third Circuits is under what circumstances a religious order will constitute a church for purposes of ERISA preemption. The IRS has defined "church" to include a religious order or a religious organization if the order or organization is an integral part of a church and is engaged in carrying out the functions of a church. Further, in determining if a religious order or organization is an integral part of a church, the IRS considers the degree to which it is connected with and controlled by a church. A religious order or organization carries out the functions of a church if its principal activity is religious in nature, such as "the ministration of sacerdotal functions or the conduct of religious worship."[3]

Under the long-standing interpretation of ERISA's church plan exemption, both the IRS and DOL interpreted a benefit plan established by a religious order to have the exemption without expressly determining whether or not the order itself came under the umbrella of constituting a church. Either the order was a church, or it was controlled by or associated with a church. It did not matter which; both were entitled to the church plan exemption from ERISA . Nevertheless, the Stapleton and Kaplan decisions now leave open the question of whether or not a religious order exempt from income taxes under § 501 of the Internal Revenue Code, in which both worship and benevolent activities occur, might still constitute a "church" within the meaning of ERISA and the code.

Note that the Tenth Circuit, in the 2015 decision of Little Sisters of the Poor Home for the Aged, Denver, Colo. v. Burwell,[4] assumed the health plan that was the subject of that case was a church plan exempt from ERISA but distinguished between church organizations ("churches, their integrated auxiliaries, and conventions or associations of churches, as well as the exclusively religious activities of any religious order") and other organizations such as hospitals, nursing homes and colleges controlled by or associated with churches. Arguably, if a religious order is deemed a church, and if it establishes a benefit plan that provides benefits for the employees of organizations controlled by or associated with the religious order, such an arrangement could still constitute a church plan under ERISA.

Looking forward, it is possible courts that have yet to address the issue may create a conflict that would be resolved by the U.S. Supreme Court. Moreover, it is possible that the DOL and/or the IRS will address the enforcement of the ERISA and Internal Revenue Code requirements for plans that are no longer considered church plans. Finally, a statutory remedy may be considered by Congress. In the meantime, religious-affiliated organizations operating benefit plans that may lose ERISA exemption are encouraged to consult with legal counsel regarding the possible risks resulting from these decisions and their options moving forward.

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[1] Stapleton v. Advocate Health Care Network, 2016 WL 1055784 (7th Cir. 2016).

[2] Kaplan v. St. Peter's Healthcare System, 810 F.3d 175 (3rd Cir. 2015).

[3] Internal Revenue Manual 4.76.6.2.2.

[4] Little Sisters of the Poor Home for the Aged, Denver, Colo. v. Burwell, 794 F.3d 1151, 1167 (10th Cir. July 14, 2015), cert. granted in part, 136 S. Ct. 446 (Nov. 6, 2015).