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Supreme Court Rules on Church Plan Question

In a unanimous decision, the U.S. Supreme Court held that a plan maintained by a church-related "principal purpose organization" qualifies as an ERISA-exempt church plan, regardless of who established it.

Background

ERISA requires employee pension benefit plans to meet certain standards in areas such as minimum funding, vesting, reporting and disclosure, and fiduciary responsibility. ERISA also requires defined benefit plans to be covered by PBGC plan termination insurance that guarantees plan benefits up to certain limits. Similarly, ERISA requires employee welfare benefit plans to meet reporting and disclosure as well as fiduciary requirements. However, ERISA provides an exemption from the pension and welfare plan requirements for "church plans" that do not opt into ERISA coverage.

ERISA also generally preempts state laws that relate to employee benefit plans (other than those that pertain to insurance, banking or securities) and allows parties to sue in the federal district courts regardless of the amount in controversy or the citizenship of the parties. Church plan sponsors that do not elect into ERISA coverage may be subject to state law claims.

When originally enacted, ERISA defined a "church plan" as a plan established *and* maintained for its employees by a tax-exempt church (which includes a convention or association of churches). Plans in existence on January 1, 1974 were temporarily allowed to cover employees of church-related, tax-exempt agencies. In 1980, before the temporary rule expired, Congress permanently expanded the definition of "church plan" to include plans that covered such employees, and modified it to include plans maintained by tax-exempt organizations that were either controlled by, or associated with, a church, with the principal purpose or function of administering or funding benefits for church employees.

Despite more than 30 years of IRS-issued private letter rulings confirming the church plan status of these organizations, many class action lawsuits were brought recently by participants of plans established by church-affiliated hospitals. These lawsuits challenged the plan's eligibility for ERISA's church plan exemption based on the

premise that the plan was not *established* by a church. The lower courts have disagreed on the statutory interpretation: some of the courts ruled that a plan had to be *established* by a church to be exempt from ERISA, while others ruled that any plan that was *maintained* by a tax-exempt organization controlled by or associated with a church would be eligible for the exemption. (See our May 4, 2015 *For Your Information*.)

Supreme Court Rules Exemption OK for Plans Maintained by Church-Affiliated Entities

On June 5, the Supreme Court settled the matter. In the case of *Advocate Health Care Network v. Stapleton, et al.,* the Court examined the 1980 amendment to the statute, focusing on the fact that "church plan" was originally defined in ERISA Section 3(33)(A) as "a plan established and maintained … by a church … or by a convention or association of churches" before it was amended in 1980. The 1980 amendment stated that "a plan established and maintained" by a church (or a convention of association of churches) includes "a plan maintained" by a church-related entity whose principal purpose is to fund or administer retirement or welfare benefits (a "principal purpose organization").

The Court concluded that if Congress had omitted the two words "established and" from the 1980 amendment, the plan participants would have prevailed in this case. However, since those two words were included in the statute and the Court must give effect to every clause and word of a statute – it construed those two words as removing the requirement that a church has to establish the plan to be exempt from ERISA for plans maintained by principal purpose organizations. Justice Elena Kagan explained that the Court's interpretation of the statute had a strong foundation in logic: "If A is exempt, and A includes C, then C is exempt." The Court further noted that the establishment and maintenance requirements are closely related (because a plan could never be maintained if it was never established), and ERISA uses the terms "establish" and "maintain" almost interchangeably in other sections.

The Court found the evidence provided by the plan participants about the legislative intent of the 1980 amendment (such as committee hearing excerpts and floor speeches from individual lawmakers) unconvincing. While the participants claimed that the primary purpose of the change was to put congregational churches on an equal footing with more hierarchical churches, the Court stated that a more plausible explanation was to disentangle the government from defining what a church is, and how a church's mission could be carried out (as some claim IRS did in 1977 in General Counsel Memorandum 37266 when it denied church plan status to a plan established by a hospital run by an order of Catholic Sisters).

The Court did not address other arguments made by the participants – that the hospitals' pension plans are not church plans because the hospitals do not have the requisite association with a church, or that their internal benefits committees do not count as "principal purpose organizations." Rather, the court said that "nothing we say in this opinion expresses a view of how they should be resolved."

Justice Sotamayor's Concurring Opinion

Justice Sonia Sotamayor issued a concurring opinion in which she agreed that the Court correctly interpreted ERISA's statutory text, but stated that she was troubled by the outcome. The lack of congressional debate on this question made it seem as if Congress had not thoroughly considered the implications, and that it could hardly have been foreseen that the church plan exemption could apply to hospitals that employ thousands, earn billions of

dollars in revenue, and compete with secular hospitals that have to comply with ERISA. She also wrote that "this current reality may prompt Congress to take a different path" and that the provisions that govern the organizations that can qualify as principal purpose organizations need to be construed with a view toward effecting ERISA's broad remedial purposes.

An Undisputed Decision

Eight justices were unanimous about this decision – recently confirmed Justice Neil Gorsuch did not hear arguments or participate in the decision.

Next Steps for Participants

It remains to be seen what participants in these plans can do next to address their concerns about the security of their pensions. One potential avenue would be to challenge those aspects the Supreme Court did not address, such as the hospitals not having the requisite association with a church, or that their internal benefits committees do not meet the criteria for being principal purpose organizations. Another possibility would be state law causes of action (such as breach of contract, or fiduciary breaches under trust law) in the hopes of gaining concessions such as contributions to improve funding levels.

In Closing

The Supreme Court's decision provides relief to tax-exempt organizations associated with churches that established plans otherwise subject to ERISA, most notably with respect to PBGC premiums and ERISA's minimum funding requirements for defined benefit plans. If the Court had ruled against church plan status, the affected organizations would have been forced to expend millions of additional dollars on premiums and contributions. On the flip side, participants in severely underfunded defined benefit plans maintained by these entities will be left unprotected if the plans become insolvent. Plan sponsors aiming to avert further lawsuits and retain their plans as key attraction and retention tools need to think through how best to avoid that result.

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