Supreme Court’s Church Plan Decision Restores Order

On June 5, 2017, in a unanimous decision, the U.S. Supreme Court overturned decisions by three federal Circuit Courts of Appeals and held that an employee benefit plan maintained by a church-controlled or church-affiliated organization can qualify as a “church plan” exempt from ERISA regardless of who establishes the plan (Advocate Health Care Network v. Stapleton, No. 16-74, 581 U.S. ___ 2017).

In a concise and clearly written opinion, Justice Elena Kagan restored order in the church plan universe – and validated nearly 40 years of administrative decisions by the Internal Revenue Service, the Department of Labor and the Pension Benefit Guaranty Corporation – by explicitly affirming that church-affiliated hospitals and other organizations can establish benefit plans that should be accorded the same treatment as plans actually established by a church.

The Stapleton decision completely shut down the primary line of argument pursued by plaintiffs in a series of class action lawsuits. The plaintiffs challenged the status of pension plans maintained by hospitals and other church-affiliated organizations as church plans, and sought to bring those plans into the strict regulatory framework of ERISA.

Background

The question presented in the Stapleton case was whether a benefit plan must have been established by a church in order for that plan to qualify for the “church plan” exemption under ERISA. Federal Circuit Courts for the Third, Seventh and Ninth circuits found that the statutory provisions of ERISA indeed created such a requirement and that exemption rulings (and related guidance) issued by Internal Revenue Service, the Department of Labor and the Pension Benefit Guaranty Corporation relied on a mistaken interpretation of ERISA. As originally enacted, ERISA defined the term “church plan” to mean “a plan established and maintained . . . for its employees . . . by a church.” In 1980, Congress modified the definition of church plan – and arguably expanded the scope of the exemption – by adding that “a plan established and maintained . . . by a church . . . includes a plan maintained by an organization . . . the principal purpose or function of which is the administration or funding of a plan . . . .”

Justice Kagan used the term “principal-purpose organization” as a short-hand way to refer to the organization contemplated by the statute. Attorneys representing the plaintiff classes argued that even though the modified definition would allow a church plan to be “maintained” by an organization other than a church, only a church may “establish” a church plan. Under that interpretation of the statute, a plan established by an organization other than a church (including church-affiliated hospitals and schools) could never qualify for the church plan exemption because it was not established by a church itself.

Justice Sonia Sotomayor concurred in the opinion but voiced concerns about the outcome of the case and its impact on the benefits employees may not receive if the protections of ERISA are not extended to these plans. She called on Congress to act. Justice Neil Gorsuch did not participate in the Court’s 8-0 decision.

Nevertheless, the decision leaves open one final line of argument that could be pursued by attorneys representing aggrieved plan participants in church plan cases. So the discussion, and the litigation, may not end here. That is because the Court expressly did not address the question of what attributes or criteria must be met for an organization to be considered a “principal-purpose organization” that is...
capable of maintaining a church plan within the scope of the exemption. That matter will have to be addressed by the Circuit Courts whose decisions have been reversed, potentially District Courts to whom earlier decisions may be remanded by the Circuit Courts, and, of course, any new cases that may be brought or cases that have been suspended pending the outcome of the Stapleton case.

In the meantime, while the Stapleton decision may reduce the price tag for settling cases that still are pending, church-affiliated employers are left to ponder what they can do to shore up the exemptions for their plans.

Considerations for sponsors of church-affiliated plans

We offer the following preliminary thoughts for consideration by sponsors of church plans in light of the Stapleton decision:

• **Formalize plan administration and management** - Any church-affiliated organization that has not established a formal governance structure for plans that it intends to treat as church plans should do so. It is surprising that after 40 plus years since ERISA was enacted that many plan sponsors still lack a formal committee structure to administer their benefit plans. While ERISA is not applicable to church plans the best practices that have evolved over the years would be appropriate for non-ERISA plans.

The employer should formalize the governance structure in a way that would demonstrate that the plan is maintained by an organization that can be recognized as a “principal-purpose organization.” For example, adopting charters and by-laws that affirm the “principal-purpose” and have committee members, who by their presence, support the position that the committee is controlled by or associated with a church.

• **Refine and “rebrand” existing governance structures** - A church-affiliated employer that has already established a formal governance structure for its church plans may wish to reevaluate the existing structure of the committee to ensure that it is absolutely apparent that the committee is functioning under the direction and control of a “principal-purpose organization.”

• **Amend plan documents and disclosure materials if necessary** - Any plan document that is intended to be maintained as a church plan should be reviewed, and amended if necessary, to ensure that it does not contain terms and provisions that invoke ERISA. We are continually surprised at how frequently we see ERISA provisions in plans that are intended to be church plans. ERISA terms or provisions generally can and should be removed. Provisions that explicitly state that the plan is not subject to ERISA are, of course, welcome.

• **Review and inventory all current plans or arrangements** - A church employer should review all plans currently offered by any affiliated organizations and determine which plans could be dissolved or merged into the church plan. For example, many organizations may still be maintaining defined benefit pension plans that are frozen and could be terminated thus mitigating liability. Furthermore, consolidation may minimize fees and expenses, which is another area of potential emerging litigation.

The retirement consulting team at Arthur J. Gallagher & Co. has an established practice working with religious and tax-exempt organizations, and is well versed in the topics covered in this article. Gallagher stands ready to assist on this issue or any other topics.
This material was created to provide accurate and reliable information on the subjects covered, but should not be regarded as a complete analysis of these subjects. It is not intended to provide specific legal, tax or other professional advice. The services of an appropriate professional should be sought regarding your individual situation.

Gallagher Benefit Services, Inc., a subsidiary of Arthur J. Gallagher & Co., (Gallagher) is a non-investment firm that provides employee benefit and retirement plan consulting services to employers. Securities may be offered through Kestra Investment Services, LLC, (Kestra IS), member FINRA/SIPC. Investment advisory services may be offered through Kestra Advisory Services, LLC (Kestra AS), an affiliate of Kestra IS. Not all individuals of Gallagher are registered to offer securities through Kestra IS or investment advisory services through Kestra AS. Neither Kestra IS nor Kestra AS are affiliated with Gallagher. Neither Kestra IS, Kestra AS, Gallagher, their affiliates nor representatives provide accounting, legal or tax advice.