Supreme Court Gives Its Blessing for Exempt Church Plan Status for Retirement Plans Maintained by Church-Affiliated Entities

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Practice Area: Compensation and Benefits/ERISA & Religious Organizations

In a closely watched case, the U.S. Supreme Court unanimously overruled several circuit courts of appeal in holding that retirement plans maintained by church-affiliated organizations are exempt from the Employee Retirement Income Security Act of 1974, as amended ("ERISA") as "church plans." *Advocate Care Network et al. v. Stapleton et al.*, U.S. Supreme Court, No. 16-74 (June 5, 2017). Although the *Stapleton* decision only specifically addresses the definition of a "church plan" under ERISA, the decision also impacts certain retirement plan qualification requirements for church plans under the Internal Revenue Code ("Code"), which tracks the ERISA definition of a church plan.

The issue of what plans qualify as "church plans" has been the focus of high-profile litigation recently because church plans are significantly less regulated than non-church plans. For example, church plans are exempt from requirements, or subject only to less onerous pre-ERISA requirements under the Code, relating to:

- minimum coverage and nondiscrimination in favor of highly compensated employees;
- vesting, rates of benefit accrual, and protected benefits;
- qualified joint and survivor annuity and qualified preretirement survivor annuity rules that protect the interests of spouses, widows and widowers;
- Form 5500 annual reporting and the related requirement, in many cases, to have the plan independently audited;
- in the case of defined benefit pension plans like those involved in Stapleton:
    - minimum funding; and
    - insurance premiums payments to (and coverage under) the Pension Benefit Guaranty Corporation ("PBGC").

In lawsuits challenging the church plan status of plans purporting to be church plans, participants have asserted that they have been harmed by the lack of ERISA protection. For example, in some cases plan sponsors have reduced participants' pension benefits, which would not be permissible under ERISA.

For ERISA exemption purposes, ERISA section 3(33)(A) defines the term "church plan" to mean a plan established *and* maintained for its employees by a church. In 1980, Congress added ERISA section 3(33)(C)(i), which states that a plan established and maintained for its employees by a church includes a plan maintained by what the Supreme Court labeled a "principal-purpose organization" – specifically, an organization the principal purpose or function of which is the administration or funding of a plan or program for the provision of retirement or welfare benefits for the employees of a church. For this purpose, employees of a church-affiliated entity are considered employees of a church. The principal-purpose organization does not need to be a legal entity, but must be controlled by or associated with a church. Many church-affiliated nonprofits, such as hospitals and other health care facilities, took the position that so long as their plan was maintained by a principal-purpose organization, such as a benefits committee, the plan was a church plan exempt from ERISA. Over the years, the Internal Revenue Service, Department of Labor, and PBGC all agreed with this view.

In recent years, however, several federal appellate courts had reached a different conclusion, holding that ERISA requires that a plan be *established* by a church in order to be exempt from ERISA as a church plan. Because of the importance of this issue, the Supreme Court agreed to hear an appeal of several such cases.

The plan sponsors in *Stapleton* argued that ERISA section 3(33)(C)(i) augments the ERISA section 3(33)(A) definition of a "church plan" by including retirement plans *maintained* by principal-purpose organizations, regardless of whether the plan was *established* by a church. The plan participants in *Stapleton* argued that ERISA section 3(33)(C)(i) does not eliminate the requirement under ERISA section 3(33)(A) that exempt church plans must be established by a church.

The Supreme Court ruled that the plan sponsors' interpretation of ERISA is correct. According to the Court, "[u]nder the best reading of the statute, a plan maintained by a principal-purpose organization ... qualifies as a 'church plan,' regardless of who established it." Thus, a retirement plan maintained by a church-affiliated organization may be an ERISA-exempt church plan, even if it was not established by a church.

The Supreme Court's ruling is welcome confirmation for church-affiliated organizations, including hospitals and other healthcare facilities, that their plans can be exempt from ERISA even if the plans were not established by a church. However, the Supreme Court refrained from ruling on whether the organizations maintaining the retirement plans in *Stapleton* had adequate ties to churches to be considered "principal-purpose organizations," thus leaving open possible avenues of dispute regarding church plan exemption status.
