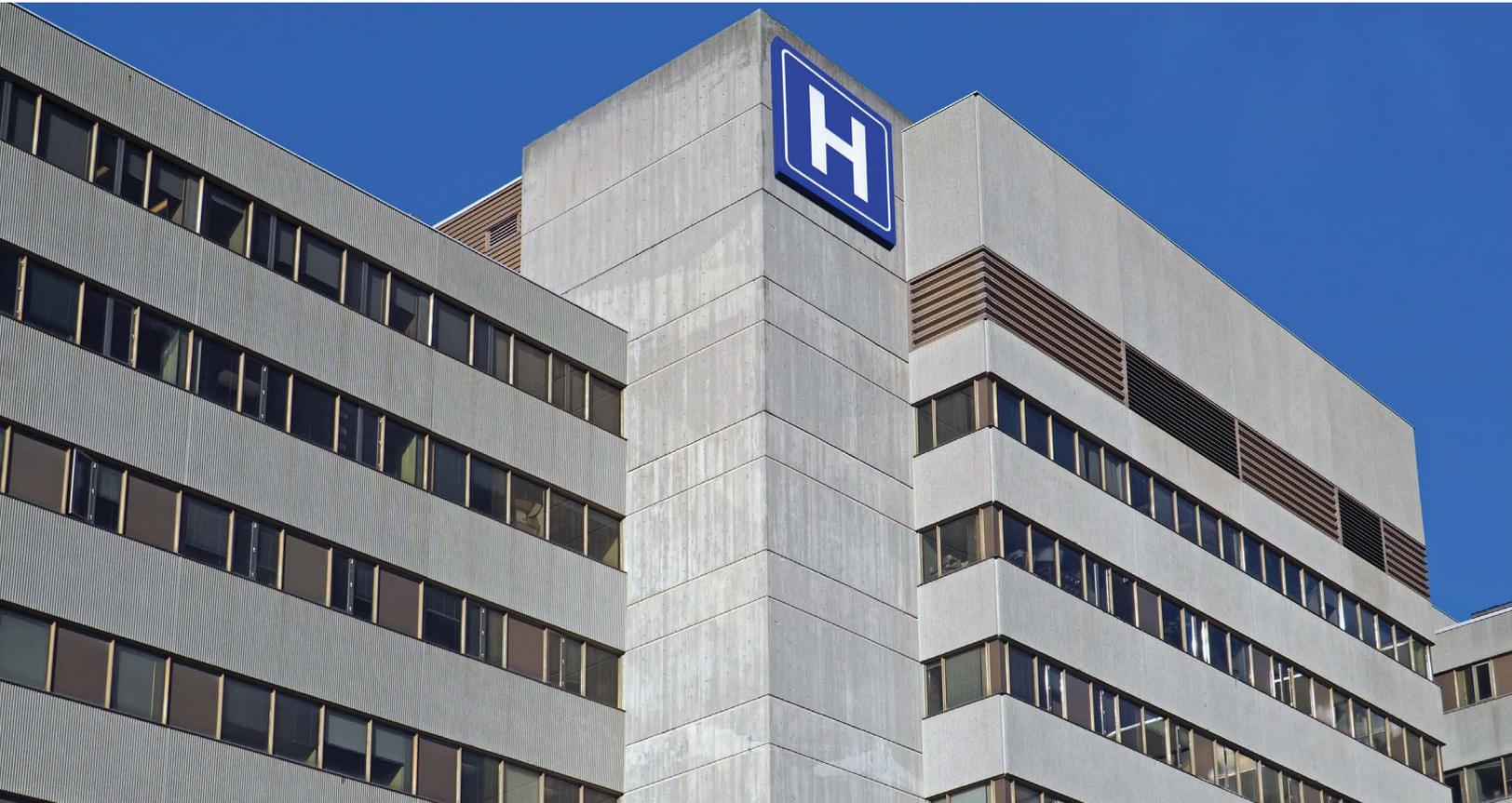


## Compliance for Church Plans

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**Questions:** We are a church-affiliated hospital and we offer benefits to our employees. Since we've always been told our plans are considered "church plans," we haven't filed Form 5500 filings, including for our group health plan which has over 300 participants. How do we know if we are still considered a church plan? And if we are, how does that impact our compliance requirements?

### Summary:

Whether or not plans are properly considered "church plans" has been the subject of significant litigation in recent years. Challenges have been raised to plans sponsored by various church-related entities, such as hospitals, orphanages, schools, etc. The U.S. Supreme Court issued a decision on June 5, 2017, that was in keeping with long-time guidance from the three federal agencies that administer and enforce ERISA, namely that entities that are not churches themselves, but have church affiliations, can sponsor "church plans."

If a plan is determined to be a church plan, it is exempt from most ERISA requirements (including COBRA), unless the

church makes a one-time irrevocable election to be governed by ERISA. Whether or not a church can make an irrevocable election with regard to welfare plans like health plans, as opposed to qualified retirement plans, is unclear. Being exempt from ERISA, however, is a double-edged sword. While its requirements designed to protect plan participants do not apply, the *protections* of ERISA preemption also do not apply. So state law claims, including claims for punitive damages, may be brought in lawsuits concerning those plan benefits.

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#### **Detail:**

##### ***Church Plan Defined:***

ERISA defines a church plan as a plan “established and maintained” by a church or association of churches exempt from tax under Internal Revenue Code Section 501. ERISA further provides that a church plan includes a plan maintained by an organization, whose “principal purpose or function is the administration or funding of a plan or program for the provision of retirement benefits or welfare benefits, or both, for the employees of a church or a convention or association of churches, if such organization is controlled by or associated with a church or a convention or association of churches.” ERISA Section 3(33).

For years, the three federal agencies that enforce ERISA (the Internal Revenue Service, the Department of Labor, and the Pension Benefit Guaranty Corporation) interpreted the ERISA definition of a church plan to include plans sponsored by employers that are not churches, but which have church affiliations, such as hospitals, orphanages, schools, and retirement homes. More recently, however, lawsuits have been instituted challenging plans that were sponsored by large church-affiliated hospitals. Three federal appellate court decisions in 2015 and 2016 each concluded that a plan isn’t an exempt “church plan” unless a church originally established the plan. In Advocate Healthcare Network v. Stapleton<sup>1</sup>, the Supreme Court overturned all three appellate court decisions in a unanimous opinion issued on June 5, 2017, holding that ERISA’s church plan exemption applies to both (1) plans established and maintained by churches; and (2) plans maintained by principal purpose organizations controlled by or associated with a church or a convention or association of churches. The Court did not explain, however,

what qualifies as a “principal purpose organization” or what it means to be “controlled by” or “associated with” a church. Litigation has continued over the meaning of these terms.

##### ***Principal Purpose:***

According to the plain language of ERISA, the “principal purpose organization” must maintain the plan for the principal purpose of plan administration or funding. In Stapleton, the Supreme Court merely concluded that the plan does not have to be initially established by a church and offered no opinion on whether a church-affiliated hospital’s internal benefits committee was a principal purpose organization. Thus, it remains unclear what it means to be a principal purpose organization. Are plans that are established and maintained by a church-affiliated employer alone considered to be plans maintained by a principal purpose organization? Or does there need to be a specific benefits committee or similar entity to create a principal purpose organization? Or is it something else? Is maintaining the plan the same as administering it or does the internal benefits committee also need to have the power to amend or terminate the plan as well? While there have been decisions subsequent to Stapleton on some of these issues, there is ongoing litigation.

##### ***Controlled By:***

ERISA does not define “controlled by” but the phrase has been interpreted by courts as referring to corporate control. This would include factors such as the ability to select board members and other powers and responsibilities usually set forth in governance documents like bylaws and charters.

### **Associated With:**

Under the plain language of ERISA, an organization is “associated with” a church or a convention or association of churches if it “shares common religious bonds and convictions with that church or convention or association of churches.” Proponents of church plan status will point to the inclusion of the tax-exempt entity in the church’s official directory and the entity’s inclusion under the church’s group tax exemption letter under Code Section 501(c)(3) as evidence that the “associated with” requirement has been met. Some courts apply a three-factor test to determine if an organization is “associated with” a church: (1) whether the religious institution plays any official role in the governance of the organization; (2) whether the organization receives assistance from the religious institution; and (3) whether a denominational requirement exists for any employee or patient/customer of the organization.

### **Ongoing Litigation:**

As you can see, the Stapleton case has not put an end to the question of whether plans maintained by universities, hospitals and other organizations associated with churches are church plans. In September 2018, a federal district court in California denied a motion to dismiss a complaint that was filed against a church-affiliated hospital, on the grounds that the employee/plaintiffs of the hospital had sufficiently alleged that the internal benefits committee of the hospital was not a principal purpose organization and that the hospital was not associated with a church.<sup>2</sup> The parties entered settlement negotiations in 2021, meaning the church plan exemption

at issue ultimately will not be decided by the court.<sup>3</sup> While this is not a final decision on the merits it does provide confirmation that challenges to church plan status will be ongoing.

On the other hand, on August 27, 2018, a federal district court in Missouri granted a motion to dismiss filed by a church-affiliated hospital, finding that the hospital’s benefits committee was a principal purpose organization and that the hospital and committee were controlled by a church.<sup>4</sup>

And on March 27, 2020, the Eighth Circuit ruled on several issues of the church plan exemption, ultimately finding that a hospital’s internal benefits committee constituted a principle purpose organization.<sup>5</sup> In Sanzone v. Mercy Health, the court applied ordinary meanings to the terms “maintain” and “organization.” There, the court concluded that “maintain” means “to continue something” or “to care for (property) for purposes of operational productivity,” and that an “organization” meant “an administrative and functional structure” or “a group of people who work together in an organized way for a shared purpose.”

### **Implications of Church Plan Status:**

If a plan is found to be a church plan, then it is exempt from ERISA and its many disclosure and reporting requirements. This means that churches have greater flexibility in their plan design, structure and operation. Almost all litigation has focused on church retirement plans because of ERISA’s funding and vesting requirements for those plans. There are, however, implications for group health plans and other welfare benefit plans as well. For example, a church plan is not required to have a summary



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plan description or to follow ERISA's strict claims procedures rules. ERISA's civil penalties and broad fiduciary duties do not apply. And, Form 5500s are not required for church plans. While these things sound favorable, there are disadvantages to being exempt from ERISA.

#### **Disadvantages of Being Exempt from ERISA:**

ERISA preempts (supersedes) state laws governing employee benefits to allow uniform administration of benefits for employers operating in multiple states. ERISA requires claimants to follow the plan's claims and appeals process and to exhaust those procedures before filing a lawsuit. Lawsuits are brought in federal court, not state court. State claims including misrepresentation, fraud, breach of contract, etc., some of which can lead to punitive damages, are not permitted. ERISA limits remedies to the value of the benefit not provided. Jury trials are not permitted, and the decisions made by plan administrators are generally subject to an "abuse of discretion" standard of review that is favorable to plan administrators. Church plan participants, however, are free to bring lawsuits in state court and to file state law claims, including claims for punitive damages, and they have the right to demand a jury trial.<sup>6</sup>

#### **COBRA Implications:**

Since church plans are exempt from ERISA, this means that COBRA does not apply to church plans. However, instead of federal COBRA rights, many states have "mini-COBRA" statutes designed to fill in the gaps when federal COBRA

does not apply. Sponsors of church plans must review the state laws of all the states where participants live to ensure compliance with any applicable mini-COBRA statutes.

#### **Electing to be Covered by ERISA/ Church Plans with ERISA Language:**

A church plan administrator may elect to be covered by certain aspects of ERISA, but the only way to make such an election is to attach an affirmative statement to either a Form 5500 or a request for a determination letter (only applicable to retirement plans). In a recent private letter ruling, the IRS confirmed that there is no alternative form of election.<sup>7</sup> An ERISA election is almost always in the context of a retirement plan and there is some question as to whether a welfare plan would qualify for such an election.

But what happens when a "non-electing" church plan contains ERISA language? Plan document providers are normally accustomed to drafting plan documents for plans that are subject to ERISA. Thus, a church plan sometimes will be drafted with ERISA language (including claims procedures) in the document by mistake. When this happens, the church plan does not become subject to ERISA because of that language being included. As mentioned above there is only one route to becoming an ERISA-covered church plan. However, the plan has likely given participants a contractual right to the ERISA provisions, even though they would not otherwise apply.

## **Conclusion:**

According to the Supreme Court, church plans do not have to be established by a church in order to meet the requirements for an ERISA-exempt church plan. Following the Court's decision in 2017, there is still a lot of uncertainty regarding the requirements for being considered to be a church plan. Therefore, it is important for plan sponsors to have their church plan status reviewed by benefits counsel to be sure that their plans continue to qualify as a church plan. Counsel also can advise as to whether or not decisions to treat the plans as exempt from ERISA (specifically, a decision not to file a Form 5500) are appropriate based on church plan status.

#### **References**

- 1 - <https://www.law.cornell.edu/supct/cert/16-74>
- 2 - [https://www.gpo.gov/fdsys/pkg/USCOURTS-cand-3\\_13-cv-01450/pdf/USCOURTS-cand-3\\_13-cv-01450-14.pdf](https://www.gpo.gov/fdsys/pkg/USCOURTS-cand-3_13-cv-01450/pdf/USCOURTS-cand-3_13-cv-01450-14.pdf)
- 3 - <https://benefitslink.com/src/ctop/rollins-v-dignity-health-ndcal-settlement-approval-10192021.pdf>
- 4 - <https://jnswire.s3.amazonaws.com/jns-media/b7/09/894706/10718051798.pdf>
- 5 - <https://caselaw.findlaw.com/us-8th-circuit/1907872.html>
- 6 - The Church Plan Parity and Entanglement Prevention Act of 1999 does limit the application of state insurance laws which might otherwise require a church plan covering many churches to be licensed as an insurance company but that Act would have no effect on participant employee suits with regard to benefits or administration of a church plan.
- 7 - <https://www.irs.gov/pub/irs-wd/201826009.pdf>. Only the party who requests a private letter ruling may rely on the ruling but this sole method of making an ERISA election has also been recognized by the Department of Labor (DOL Advisory Opinion 95-07A)



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