Arkansas Association of Defense Counsel

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The ERISA Church Plan Exemption - Debate over "And" and "Or" Continues

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When is a pension or a welfare benefit plan maintained and administered by an entity affiliated with or controlled by a church, or by a bona fide religious organization, a church plan exempt from the requirements and safeguards of the Employee Retirement Income Security Act (ERISA)? This question, one would think, was answered by Congress when it enacted ERISA in 1974 and included a church plan exemption in the body of the act. Or, if it was not addressed in the original statute, Congress surely would have answered the question when it amended the church plan definition in 1980 to save the exemption from a scheduled 1982 sunset.

Not so fast. If Congress answered all questions definitively, there would be less work for lawyers and a reduced case load for federal judges. But the ERISA bar is continually busy arguing about what Congress intended, and the bench has no holiday from its docket. What qualifies as a church plan has been litigated without a definitive answer for the better part of the past 20 years. And still the federal courts are divided on what Congress meant when it defined a church plan. The courts agree that the statutory definition is clear, but nevertheless they reach different conclusions. Recent decisions from the Third and Seventh Circuits signal that perhaps a consensus is beginning to emerge. But district courts in other circuits have reached contrary results.

ERISA was passed in 1974 in response to certain high-profile pension plan failures. Congress established plan funding requirements and other safeguards for pension plans. Congress stated that its purposes for enacting ERISA were twofold: "to protect interstate commerce and the interests of participants in employee benefit plans and their beneficiaries." 29 U.S.C. § 1001(b). To effectuate this purpose, Congress extended the reach of ERISA to any employee benefit plan "established or maintained by an employer engaged in commerce or in any industry or activity affecting commerce." 29 U.S.C. § 1003(a)(1). Thus, with respect to private plans, ERISA compliance is required if the plan was established or is maintained by an employer. The emphasis on "or" in the statutory definition in the preceding sentence has significance for the church plan exemption.

Congress created two notable exceptions to ERISA. Recognizing potential constitutional challenges to the legislation (think about the current religious freedom challenges to the Affordable Care Act), Congress exempted government plans and church plans. Plans "established or maintained" by state and local governments need not comply with ERISA. The original definition of a church plan in 1974 stated:

> 29 U.S.C. § 1002(33) defines "church plan." Subsection (A) provides:
>
> The term "*church plan*" means a plan established and maintained (to the extent required in clause (ii) of subparagraph (b)) for its employees … by a church or by a convention or association of churches which is exempt from tax under section 501 of title 26.

Thus, as stated by Congress, to qualify as a church plan, the plan must be both established and maintained by a church. Did Congress really intend to require both establishment and maintenance for churches, while requiring only establishment or maintenance for government plans? Or was this an overlooked drafting error? No one will ever know. But it is what Congress said in 1974. And now, in 2016, the difference between "and" and "or" is the key to the church plan lock.

The church plan issue has predominantly involved health-care and social services institutions with ties to certain religious organizations. When a religiously affiliated hospital has a pension or welfare benefit plan for its employees, is the hospital's plan

governed by ERISA? This is the issue litigated by the courts. If a church sets up the plan (establishes) and administers the plan (maintains) for the hospital's employees, there is no question that it is a church plan beyond ERISA's reach. The difficulty arises when the hospital, not the church, establishes the plan in the first place. What "maintaining" a plan means involves a detailed discussion beyond the scope of the article. Suffice it to say that "maintenance" involves the administration of plan enrollment, determination of eligibility, and payment or denial of claims. Of course, a hospital's plan is more often than not administered by a third party. The 1974 definition did not discuss the extent to which the hospital, and by extension its third-party administrator, must be tied to the church to bring its plan within the ERISA orbit.

The 1974 act's exemption of church plans was temporary, set to expire in 1982. The act's exemption for preexisting church plans, which covered employees of church-affiliated organizations, would end. The religious community was concerned that the exemption would require two separate plans: one for church employees and another for employees of a church-affiliated organization controlled by the church. Additionally, concern was raised that the requirement that the church "maintain" the plan would extend ERISA coverage to church-sponsored plans administered by third-party financial services firms. Congress considered how to address these concerns in 1980 when it addressed the church plan sunset. The final amendment adopted by Congress states:

(I) A plan established and maintained for its employees (or their beneficiaries) by a church or by a convention or association of churches *includes a plan maintained by an organization*, whether a civil law corporation or otherwise, the principal purpose or function of which 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*.

* * *

(ii) The term employee of a church or a convention or association of churches includes —

* * *

(II) an employee of an organization, whether a civil law corporation or otherwise, which is exempt from tax under section 501 of Title 26 and which is controlled by or associated with a church or a convention or association of churches.

* * *

(iv) An organization, whether a civil law corporation or otherwise, 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.

(emphasis added).

After the 1980 amending, the federal courts did not always focus on the two distinct requirements that a church both establish and maintain the plan. The cases analyzed whether a church-affiliated organization was "controlled by" or "associated with" a church or a church convention or an association of churches, skipping the establishment requirement of the original exemption. For example, in *Catholic Charities of Maine, Inc., v. City of Portland*, 304 F. Supp. 2d 77 (D. Me. 2004), the Catholic Charities was an organization of the Diocese of Portland, which provided financial assistance on an annual basis. It was listed in the official Catholic directory. The mission statement of the Catholic Charities stated that it was to provide services "based on Roman Catholic religious teaching that calls on Catholics to serve those in need" and that "its work (is) a vital part of the ministry of the Roman Catholic church to the people of the State of Maine." The court referred to Department of Labor opinion letters that assessed "bonds and convictions" by analyzing requirements that the organization adheres to the tenets and teachings of the church, including whether the organization is listed in a religious directory and whether the church plays a role in the organization's governance. Dep't of Labor, Advisory Opinions 96-19A, 95-30A, and 95-12A. The court held that this qualified as a non-ERISA church plan.

A similar result was reached in *Friend v. Ancillia Systems Incorporated, Inc.*, 68 F. Supp. 2d 969 (N.D. Ill. 1999), in which the employer was a corporation sponsored by the Poor Handmaids of Jesus Christ, a specific religious order affiliated with the Roman Catholic church. All major decisions of that corporation's board of directors had to be approved by the religious order, which again was listed in the official Catholic directory. The results are much less clear outside of strictly organized, hierarchical churches. Congress recognized that some churches were organized in a less structured fashion

and thus included the language "or convention or association of churches." This language is taken from the Internal Revenue Code. 26 U.S.C. § 6033.

When Congress passed the Revenue Act of 1950, the term "convention or association of churches" was added to the statute at the urging of Baptist leaders. This addition to the statute relieved concerns that the term "church" included hierarchical churches but not churches in which each local congregation is autonomous, such as the Baptist. *See* Whalen, "*Church" in the Internal Revenue Code: The Definitional Problems*, 45 Fordham L. Rev. 885, 925–26, 902–03 (1977). There is no guidance from Congress on what constitutes the "common religious bonds and convictions." As a result, the courts have endeavored to create tests to determine what constitutes common religious bonds and convictions.

The Fourth Circuit attempted to answer these questions in *Lown v. Continental Casualty Co.*, 238 F.3d 543 (4th Cir. 2001). That case decided the ERISA status of the South Carolina Baptist Healthcare Corporation. Baptist Healthcare had severed its formal relationship with the South Carolina State Baptist Convention many years before. It received no funding from the convention or the Baptist church in general. The court articulated a three-factor test to determine whether a civil corporation "shares common religious bonds and convictions" within the meaning of the statute: (1) whether the religious institution plays any official role in the governance of the organization; (2) whether the corporation receives assistance from the religious institution; and (3) whether there is a denominational requirement for employees or patients/customers.

The Fourth Circuit noted particularly that the South Carolina Baptist Convention did not play any role in the governance of Baptist Healthcare. This was the court's primary focus. The three-factor test isolated specific criteria to determine whether the church had a role in governance: "It is true that the South Carolina Baptist Convention and Baptist Healthcare both share the name 'Baptist.' Yet the name is not the thing. Rather, the evidence shows that *Lown* has failed to satisfy any of the criteria for determining common religious bonds and convictions between two entities." 238 F.3d at 548.

The *Lown* factors are subject to criticism because they are not criteria articulated in the statute. Indeed, one could argue that "bonds and convictions" relate to shared religious principles and teachings, rather than corporate governance. It is this author's belief that the *Lown* criteria were proposed as the only objective measure for determining the amorphous concepts of "bonds and convictions." No doubt the religious heritage that Baptist Healthcare shared with the state Baptist convention influenced the manner in which it conducted its business. Nevertheless, the lack of any specific organizational tie between the two entities led the court to conclude that it was governed by ERISA.

In *Chronister v. Baptist Health*, 442 F.3d 648 (8th Cir. 2006), the court affirmed the district court's ruling that the long-term disability plan of Baptist Health, a nonprofit corporation operating hospitals, was not a church plan. Although Baptist Health had severed its formal ties to the Arkansas Baptist State Convention, it nevertheless imposed a denominational requirement on board members and certain officers. Baptist Health management employees were required to attend leadership training emphasizing "Christian principles." Applying the *Lown* criteria, the Eighth Circuit concluded that these facts were not sufficient to establish "common religious bonds and convictions."

These cases provide a sound analytical framework for the consideration of when a religiously affiliated company is "controlled by or associated with" a church. The courts' efforts to analyze the 1980 amendment glossed over the establishment requirement. The factor was simply never analyzed in these cases. The Fourth Circuit in *Lown* did state: "[A] plan established by a corporation associated with a church can still qualify as a church plan." 238 F.3d at 548. However, this was dicta, and the issue was never directly analyzed in *Lown*. This hole in the legal analysis reflects just as much about the ERISA bar, plaintiff and defense, as it does about the courts. The church plan litigation until recent times assumed that the real issue was what constituted a religiously affiliated entity, and therefore accepted, without actually framing the issue, that a religiously affiliated organization could also establish a church plan. As the following section illustrates, it was not until the plaintiffs' bar recognized the potential recovery that could be available by arguing that a religiously affiliated plan, operating as if was not governed by ERISA, was actually a nonexempt plan subject to ERISA, that the cases focused on the establishment requirement.

The AADC thanks David M. Donovan of Watts, Donovan & Tilley for writing this article.

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