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There Is Separation Between Church and Pension, and It May Impact Your Restructuring

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The Third Circuit recently became the first U.S. Court of Appeals to rule that a pension plan established by a church agency does not qualify as an exempt "church plan" under subsection 4(b)(2) of the Employment Retirement Income Security Act (ERISA). The Third Circuit viewed its decision as coming in the midst of a "new wave of litigation" challenging the prior assumption that entities with sufficiently strong ties to churches, but not the churches themselves, could establish plans exempt from the requirements of ERISA.

The case of *Kaplan v. Saint Peter's Healthcare System*[1] came before the Third Circuit on an interlocutory appeal following the denial of a motion to dismiss by the U.S. District Court for the District of New Jersey. St. Peter's Healthcare System, a nonprofit health care entity with ties to the Roman Catholic Diocese of Metuchen, N.J., sought to dismiss a class action complaint alleging that St. Peter's violated ERISA by failing to provide ERISA-compliant summary plan descriptions or pension benefit statements and that it underfunded the plan by more than $70 million. In support of its motion to dismiss, St. Peter's argued that it qualified for ERISA's church plan exemption and was therefore not required to comply with certain ERISA provisions, including reporting and minimum funding requirements.

Specifically, St. Peter's argued that, pursuant to certain amendments made to the ERISA statute in 1980, a plan established by a church agency (as St. Peter's claimed to be) qualifies as a church plan eligible for exemption from ERISA. St. Peter's supported its position with an IRS private letter ruling issued while the action was pending,

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which construed the same definition of "church plan" to affirm the plan's status as exempt for tax purposes.

The Third Circuit disagreed, however, holding that while the 1980 amendments expressly brought within the exemption plans established by churches but *maintained* by church agencies, the "gateway" requirement that the plan be *established by the church* in the first instance remained intact. Perhaps in *dicta* the court also cast doubt on St. Peter's qualification as a "church agency" under the statute that requires that the agency's "principal purpose" be the administration or funding of the retirement plan, as opposed to the administration of health care. Accordingly, the Third Circuit concluded that a plan established by a church agency is not exempt.

While St. Peter's' liability in connection with the underlying lawsuit remains to be seen, the implications of the ruling will be significant for numerous similarly situated organizations previously thought to fall within the church plan exemption. Indeed, the opinion acknowledges that as of 2012, religiously affiliated hospitals accounted for seven of the country's 10 largest nonprofit health care systems and notes that the IRS issued hundreds of letter rulings similar to that issued to St. Peter's. These organizations now face being subject to ERISA provisions, with which they have not previously been expected to comply. The expense of meeting ERISA's notice and minimum funding requirements will no doubt have a significant impact on church agencies' operations, including any financial restructurings of the agency.

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[1] No. 15-1172 (3d Cir. 2015).