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THE CHURCH PLAN UNDER RECENT PENSION LEGISLATION

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The subject of this discussion is legislation that excludes the "church pension plan" from the purview of the Employee Retirement Income and Security Act of 1974 (ERISA).¹ As modified in conference, the ERISA provided that after 1982 church plans would either have to come under the purview of the ERISA or have to exclude "agencies," such as colleges and hospitals, from coverage.² To be more precise, the churches were faced with three choices: eliminate the agencies; retain the agencies and come completely under the ERISA; or, set up a separate plan, under the purview of the ERISA, for the church agencies. In addition, the statutory provisions of the ERISA were drafted with an emphasis on the hierarchical churches (such as the Catholic Church), and thus presented a number of special problems for the congregational churches. Finally, benefits had been made available to the employees of certain nonprofit institutions to the exclusion of church employees.

The potential problems prompted almost all of the major churches, through their pension plans, to combine in an organization—the Church Alliance for Clarification of ERISA (CACE). Its purpose was twofold: to eliminate the deadline with respect to the excision of agencies, and to clarify other provisions of the Internal Revenue Code. After an initial period of study, CACE decided upon a course of action and commissioned the drafting of congressional bills to accomplish its purpose. Due to the joint jurisdiction of the tax writing and labor committees in both houses

¹ 29 U.S.C. §§ 1001-1381 (1976 & Supp. IV 1980). The ERISA established a program to protect the interests of participants in employee benefit plans by requiring the disclosure and reporting of financial information and by establishing standards of conduct, responsibility, and obligations for fiduciaries of employment benefit pension plans. *Id.* § 1001(b).

² Employee Retirement Income and Security Act of 1974, Pub. L. No. 93-406, § 3(33), 88 Stat. 833 (codified as amended at 29 U.S.C. § 1002(33) (Supp. IV 1980)). Pursuant to the ERISA, church plans can only cover employees of a church agency if the plan was in existence as of January 1, 1974. For taxable years beginning after December 31, 1982, a church plan can no longer cover employees of the related tax-exempt agency. *Id.*

of Congress, it was necessary to prepare three bills. The first two were virtually identical, primarily concerned with the 1982 deadline.³ The third bill addressed miscellaneous tax issues.⁴

Although the sponsors of the bills were able to obtain hearings before the Human Resources and Finance Committees of the Senate, they were unsuccessful in their attempts to address the Labor, Education, and Ways and Means Committees of the House of Representatives. The lead sponsors of the bills were Congressman Conable, and Senators Talmadge and Bentsen. The membership of the affected churches retained the support and cosponsorship of a significant number of members of Congress. As a result, toward the end of the 1980 session, the Senate sponsors were able to have the two basic bills approved by the respective committees as part of the Multiemployer Pension Plan Amendments Act of 1980.⁵ These amendments were approved by the whole Senate and eventually enacted into law.

What does the law do? Simply stated, the provision exempts church plans from all of the provisions of Title I of the ERISA, which includes reporting, disclosure, vesting, funding, fiduciary responsibility, and administration and enforcement requirements.⁶ The law also exempts these plans from the termination of insurance provision which otherwise would have been very expensive.⁷ The statute now provides for a correction period during which a church plan, failing to meet one or more of the requirements, can correct that failure without losing its exempt status.⁸ More importantly, church plans are defined broadly and the law permits "agencies" to be retained or added, with the 1982 deadline deleted.⁹

In addition, the law ensures that annuities can be purchased from

³ *Miscellaneous Pension Bills, 1979: Hearings on S. 1090 Before the Subcomm. on Private Pension Plans and Employee Fringe Benefits of the Senate Comm. on Finance, 96th Cong., 1st Sess. 172 (1979).* Both bills amended the ERISA to permit a church plan to continue after 1982, and to make certain clarifying amendments to the definition of church plans. *Id.*

⁴ *Id.* at 173. This bill provided: (1) allowing all years of service to a church or church agency to be considered as working for one employer when computing the retirement exclusion plan; (2) the option for church employees to elect alternate exclusion allowance for contribution to annuity contracts; and (3) a minimum \$10,000 allowance for annual additions to these contracts with regard to employee compensation. *Id.*

⁵ Pub. L. No. 96-364, § 3, 94 Stat. 1208 (codified at 29 U.S.C. § 1001(a) (Supp. IV 1980)).

⁶ See 29 U.S.C. § 1001 (Supp. IV 1980).

⁷ See 29 U.S.C. § 1301 (1976 & Supp. IV 1980).

⁸ See 29 U.S.C. § 1002(33)(D)(i) (Supp. IV 1980). This section affords church plans a period of time to cure any defects which could prevent church plan status. *Id.*

⁹ See 29 U.S.C. § 1002(33)(C) (Supp. IV 1980). See generally Tracy, *Church Plans*, 60 TAXES 33 (1982). This change in the act also allows pension plans covering employees of these agencies, such as schools, hospitals, and similar institutions, to avoid many ERISA requirements by being included in a retirement plan sponsored by a church or association of churches. See 29 U.S.C. § 1002(33)(c) (Supp. IV 1980).

pension boards,¹⁰ a device traditionally used by congregational churches. The legislation also makes clear that licensed ministers or priests can continue their participation in the plan, regardless of the source of their compensation, provided they are in the exercise of their ministry.¹¹ The plan also can include employees of an exempt organization associated with the church.¹² Finally, the law permits a church plan to retain people who terminate their relationship with the church, under certain circumstances, for at least 5 years.¹³

Perhaps the most important accomplishment of the legislation was the elimination of the 1982 deadline, which would have forced pension plans to exclude agencies or set up a separate plan for each agency or group of agencies.¹⁴ Further, the legislation may permit parish priests to obtain pension plans, pursuant to section 403(b) of the Internal Revenue Code,¹⁵ from an entity of the Church.

While the Catholic Church and other hierarchical churches generally have followed the pattern of dealing with qualified plans under section 401(a) of the Internal Revenue Code,¹⁶ most of the congregational churches have pension plans subject to the exclusion of section 403(b)(2).¹⁷ Section 403(b)(2) was designed for college and university programs set up by the Teachers Insurance and Annuity Association (TIAA), which was a Carnegie Foundation grant. The colleges would simply purchase from TIAA annuities for their employees, and particularly for their faculty. There is no requirement of meeting the discrimination test which exists in the qualified plan under section 401(a).¹⁸ An important aspect of section 403(b)(2) annuities is that the employees may elect to treat a salary increase as a contribution toward the purchase of an annuity.¹⁹

¹⁰ See note 15 and accompanying text *infra*.

¹¹ 29 U.S.C. § 1002(33)(C)(ii)(I) (Supp. IV 1980). Priests or licensed ministers will be considered church employees regardless of their source of compensation if acting in the exercise of their ministry. *Id.*

¹² *Id.* § 1002(33)(C)(ii)(II) (Supp. IV 1980).

¹³ *Id.* § 1002(33)(C)(v)(II) (Supp. IV 1980).

¹⁴ See note 2 and accompanying text *supra*.

¹⁵ I.R.C. § 403(b) (1982). Section 403(b) provides in part that if an annuity contract is purchased for an employee by an organization exempt under section 501(a)(3), or by a public school system, the employee's contributions for the annuity contract are excludable within certain limitations from the employee's gross income, and are not subject to tax until the employee receives payments under the annuity contract. *Id.*

¹⁶ I.R.C. § 401(a) (1982). Section 401(a) sets forth the exclusive purpose rules for plan qualification. To be qualified, a church plan must be established for the exclusive benefit of employees or their beneficiaries. *Id.*

¹⁷ See I.R.C. § 403(b)(2) (1982).

¹⁸ See *id.* § 401(a)(4)(A)-(C) (1982).

¹⁹ Treas. Reg. § 1.403(b)(3) (1966). Under Section 403(b) of the Internal Revenue Code, an

The remaining questions are: what were we unable to accomplish, and what do we still need to do? For procedural reasons, it was not possible to obtain consideration in the House of Representatives and the Senate for the third bill dealing with miscellaneous income tax considerations. CACE has reviewed the legislation and is prepared to introduce it with several minor modifications during the new session of Congress.

The remaining problems relate mostly to the congregational churches that possess pension plans subject to the exclusion of section 403(b). The section 403(b) exclusion imposes an overall 25 percent limit on the annual benefit to which a participant in a church pension plan is entitled.²⁰ This severely restricts the salary annuity option for ministers who normally would make such elections at the end of their careers. The proposed bill would remove some of the inequities caused by the 25 percent limitation by permitting a de minimus amount of \$10,000 to be contributed.²¹ The proposed legislation also permits church employees within agencies to make the special elections under section 415(c)(4) presently limited to colleges, hospitals and certain health agencies.²²

Another proposal, also relating to section 403(b), enables employees to deduct 20 percent of their includable compensation annually as well as make up for past years in which they were employed by the same employer. The bill would permit a minister or lay employee to be treated as if employed by a single employer (the Church) for the purpose of computing the exclusion allowance under section 403(b).²³ The bill would make it clear that section 403(b) annuity contracts are provided by the church whether or not they are provided internally or by a separately incorporated entity, such as a pension board.²⁴ In addition, the bill may include

employee can agree to a reduction in his present salary or to forego a future salary increase in return for his employer's promise to contribute the corresponding amount toward the purchase of an annuity contract. *Id.* See also Comment, *The Contribution Limitations for I.R.C. § 403(b) Tax Sheltered Annuities after ERISA*, 25 CLEV. ST. L. REV. 565, 567 (1976).
²⁰ See I.R.C. § 403(b)(2)(A)-(B) (1982). The annual benefit to which a participant in a defined benefit church plan is entitled may not exceed 25 percent of the participant's annual compensation. Tracy, *supra* note 9, at 41.

²¹ H.R. 5067, 97th Cong., 1st Sess. (1981). This bill establishes a minimum level of compensation for clergy and church employees for the purposes of computing the exclusion allowance for contribution to a church annuity plan. Contributions of up to \$10,000 would be permitted. *Id.*

²² *Id.* The bill extends the same election of alternative exclusion allowance for contribution annuity contracts currently available to those employees and organizations under I.R.C. § 415(c)(4).

²³ H.R. 5067, 97th Cong., 1st Sess. (1981). The bill treats all years of employment by clergy and church as being for the same employer for purposes of the exclusion allowance. *Id.*

²⁴ *Id.* The bill defines annuity contracts to include those provided by a church or church pension board.

further clarifying provisions.²⁵

Although the bill basically exempts church plans from almost all of the difficult problems of the ERISA, the bill does not specifically exempt certain church plans from some of the reporting requirements. We have taken the position, which apparently all churches should, that it would be wise for operating church plans to consider the ERISA and attempt to carry out its purposes. In addition, while church plans are not subject to the restrictive fiduciary responsibility provisions of the ERISA, state law may impose certain requirements.

²⁵ *Id.*