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Exempt Organizations

Anticipated IRS Guidance on Church Plans May Be ‘Too Little, Too Late,’ Attorney Says

A much-anticipated revenue procedure pertaining to church plans, which is in clearance at the Treasury Department, may be, as one practitioner described it, “too little, too late” for participants who have lost pension benefits they expected they would receive.

A substantial number of plan terminations and lawsuits in the past 10 years have brought to light a long history of rulings by the Internal Revenue Service in which the agency may have interpreted too broadly an exemption for church plans that has existed under the Employee Retirement Income Security Act and in the tax code since ERISA’s enactment in 1974, according to several pension attorneys interviewed by BNA.

The original church plan exemption in ERISA was narrowly confined to plans established and maintained by churches for church employees, according to Pension Rights Center attorney Eric Loi, who researched the legislative history of the church plan exemption. He told BNA July 11 that a 1980 amendment to ERISA and the tax code only narrowly expanded the exemption to cover church plans that included employees of church-related organizations, and to cover plans maintained by church pension boards whose principal purpose is to maintain benefit plans for church employees and employees of church-related organizations.

“Over the years, the IRS has increasingly broadened its interpretation of narrow statutory language meant to exempt only plans maintained by church pension boards,” Loi said. The result was that almost any plan associated with a church was exempted from ERISA, “improperly denying thousands of lay employees critical pension insurance and other ERISA protections,” he said.

Plan Terminations. Loi said that a spate of recent church plan-related terminations and lawsuits, which have left participants in terminated plans without remedies, have called into question IRS’s interpretive rulings for the past 35 years. He said one of those lawsuits, *Tynes v. Pension Benefit Guaranty Corporation*, D.N.J., No. 04-2725 (unpublished 8/2/05) (153 PBD, 8/10/05; 32 BPR 1790, 8/16/05), prompted IRS in 2007 to place a moratorium on further rulings on requests for church plan status until the agency could assess what was happening and issue a new revenue procedure on church plans under Section 414(e) of the tax code.

Although the Department of Labor and IRS share interpretive jurisdiction in defining “church plans,” Loi said, “in practice they’ve worked out a system where the IRS takes the lead on making definitional interpretations.” Through private letter rulings, IRS established a history of conferring church plan status on plans maintained by internal pension committees rather than external pension boards, he said.

‘Church Plan’ Status. Church plan status provides numerous advantages for employers, Loi said. “When you are a church plan and exempt from ERISA, you save a lot of money because you no longer have to pay PBGC premiums, you no longer have to follow the stringent funding rules under ERISA and the tax code,” he said. Church plans also are exempt from filing Form 5500 annual benefit plan information returns.

Because of their statutory exemption under ERISA, church plans also are not required to keep participants informed about the status of their pension benefits, although church plans may formally elect to operate as ERISA-covered plans.

Not Clear-Cut. Another pension attorney told BNA that participant protections under ERISA are not clear-cut, however, because of deferential standards of review for claims that arise under ERISA. Those standards in many cases “afford arguably greater protec-

tions for the plan” than for plan participants, Charles F. Knapp, a partner at Faegre & Benson in Minneapolis, said July 7.

“It’s not a black-and-white, clear-cut distinction,” Knapp said. “There are some benefits [to participants] with it being an ERISA plan, and there are some benefits to participants with it not being an ERISA plan,” he said.

However, another attorney said that having PBGC-insured pension benefits is a clear advantage for participants in ERISA-covered plans. “Without the protection of ERISA, most people are left out in the cold,” Richard A. Lockridge, a partner at Lockridge Grindal Nauen in Minneapolis, told BNA July 7.

Anticipated Revenue Procedure. The revenue procedure on church plans that is now in the clearance pipeline at Treasury may not satisfy plaintiffs’ attorneys if a recent letter from a Treasury official is indicative of what that new guidance might say. The guidance in some respects may be “too little, too late,” Lockridge said, when asked by BNA to comment on an April 25 letter from Joseph H. Grant, acting commissioner of the Tax Exempt and Government Entities Division at IRS, to Sens. Max Baucus (D-Mont.), Jeff Bingaman (D-N.M.), Tom Harkin, (D-Iowa), and Herb Kohl (D-Wis.).

The IRS letter, responding to questions from the senators about conversions to church plan status, said that the agency:

- lacks authority to allow a church plan that has elected coverage under ERISA to subsequently opt out of ERISA coverage;

- cannot consider the sponsor of a church plan that has not made an ERISA election in the manner specified under the regulations as having made the election simply because it has operated the plan in a particular manner;

- will not issue favorable ruling letters on conversion transactions when a plan sponsor claims to have converted an ERISA-covered plan that is not a church plan to a church plan;

- believes that plans of organizations associated with a church, convention, or association of churches may in appropriate cases be church plans; and

- does not require church plans to obtain a ruling from IRS for recognition as a church plan but is considering guidance that would require an employer that applies for a ruling to notify all plan participants of the effect of such a ruling.

“That would be good,” Lockridge said, addressing the last point, “except for the fact that they say that a church plan does not have to apply for an IRS ruling to be recognized as a church plan, so I think that undercuts the whole thrust of the letter.”

Notice to Participants. The IRS letter contained comments similar to ones made by Ingrid Grinde, IRS employee plans technical guidance manager, during an agency phone forum in March. In that forum, Grinde said that the draft revenue procedure in clearance would require that plan sponsors give notice to participants before IRS would issue a private letter ruling to an entity requesting church plan status under Section 414(e).

“Church plans that don’t elect to be subject to ERISA aren’t subject to as many requirements under the code, and we feel that participants and other interested parties should be notified of this and have an opportunity to comment before a letter ruling is issued,” Grinde said in March.

Insufficient Information. The Pension Rights Center said a notice requirement would not eliminate all of its concerns for the rights of participants in church plans. Through a request under the Freedom of Information Act, the Pension Rights Center learned that between 1999 and 2007, about 85 plans submitted requests to have their PBGC premiums refunded, based on claims that they had converted and had become church plans. “Because of the statute of limitations, they were only allowed to receive six years’ worth of premium refunds,” Loi said.

In doing research on the legislative history of the church plan exemption, Loi said he also discovered a source of useful information on church plans maintained by the Church Benefits Association, a lobbying group for church pension boards. Boards belonging to the group follow rules similar to those required under ERISA, he said.

“The way we want the church plan exemption interpreted would not affect their exemption,” Loi said. Church pension boards typically design their plans in a manner similar to that of multiple employer plans, he said.

Status Quo? Meanwhile, the Pension Rights Center staff has been talking with IRS, DOL, PBGC, and congressional leaders about the legislative history of the church plan exemption, Loi said. “We hope the [forthcoming] guidance will interpret the church plan exemption as it was intended by Congress,” he said.

BY FLORENCE OLSEN

Text of the letter to IRS from Sens. Baucus, Bingaman, Harkin, and Kohl is at <http://op.bna.com/pen.nsf/r?Open=foln-8jnc2>. IRS’s response letter is at <http://op.bna.com/pen.nsf/r?Open=foln-8jnncf>.