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District Court Holds That a Public Library Plan is Not a Governmental Plan

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PUBLISHED
04/29/2019

SOURCE
Groom Benefits Brief

SERVICES
Employers & Sponsors
- Retirement Programs
- Fiduciary & Plan Governance

Health Services
- ERISA

Retirement Services
- Financial Institutions & Advisers
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Over the past decade, many governmental entities have been waiting for Internal Revenue Service guidance updating its definition of what is a "governmental plan". However, plaintiffs are not waiting for this guidance and are now turning to the courts.

In an interesting decision out of the Southern District of New York, a court has held that the disability plan of a public library is not a governmental plan. The decision, Skornick v. Principal Financial Group, Principal Life Insurance Company and Brooklyn Public Library, No. 18-CV-4324 (CS) (S.D. N.Y. April 18, 2019), contains some analysis that could raise additional questions for other entities that maintain they are agencies or instrumentalities of a state or political subdivision of a state, and the plans they sponsor or retirement systems they participate in. Notably, this decision follows on the heels of a complaint filed by a prominent plaintiffs' law firm that a North Carolina county hospital system was not an agency or instrumentality of a county, Shore v. The Charlotte-Mecklenburg Hospital Authority, Case No. 1:2018cv00961, filed November 19, 2018 (M.D.N.C.). Regardless of whether these cases are one-off situations or trends, this evolving litigation landscape is an important area for governmental entities and governmental plans to monitor.

How the Case Arose

As is typical for a number of non-ERISA welfare plan cases, the plaintiff was denied a disability payment under a plan of the Brooklyn Public Library, insured by Principal, and as a result brought claims of fraud, breach of contract, negligence and violation of New York law against Principal, and a claim of negligence against the library. As is also typical in these types of cases, Principal then removed to federal court claiming that the plan was subject to ERISA and the state claims were preempted. The library consented to the removal. Thus, the library was claiming, in effect, that its own plans were not governmental plans. That is sometimes a posture in these cases where the short-term goal of the employer and insurer is to get out of state courts, and this procedural history may well have flavored the court's analysis. In any event, under the ERISA definition of governmental plan, this would depend upon whether the library was an agency or instrumentality of a political subdivision.

The Court's Test

In examining whether the library was an agency or instrumentality of the City of New York or the Borough of Brooklyn, the Court relied primarily on Rose v. Long Island R.R. Pension Plan, a Second Circuit case from 1987, and considered one of the leading cases on the governmental plan definition.

The Rose case provides a six-point test, essentially:

1. Whether the entity is used for a governmental purpose or performs a governmental function.
2. Whether the entity performs a function on behalf of a state or political subdivision.
3. Whether there are any private interests involved or the state or political subdivision have the powers and interest of an owner.
4. Whether control or supervision of the organization is vested in a public authority.
5. Whether there is statutory authority for the creation and use of the entity.
6. The degree of financial autonomy and the source of its operating expense.

How the Court Applied the Six Factors

Going through the first two factors of the test, the court found that operating a library was not performing "an essential governmental function", citing New York City's charter that states that "agency" does not include any corporation or institution maintaining or operating a public library. Another fact cited by the court was that the Library operated as a 501(c)(3) nonprofit corporation, and that it did not possess any sovereign powers. The court further observed that the library was chartered by the Board of Regents of the New York State Education Law as an" association" library rather than "public" library. The Board also found that providing free education to the people of Brooklyn was not a governmental function, since other nonprofits perform services that benefit the public.

Discussing the third factor, the court also took notice that the City provides funding to the Library and Library employees can participate in the New York State Retirement System. However, the court stated that this was simply a matter of contract, not the same as the government's ownership of the institution. The court stated that by not doing the hiring and firing, managing its budget, or deciding what books to buy or programs to offer, the City and Borough were not acting like an owner of the library.

As to the fourth factor, that 26 of the 38 board members of the library were or were appointed by public officials was viewed, on the other hand, tipping in favor of governmental status.

On the fifth factor, the court found that though the library was created by state law (it grew out of the Carnegie library movement giving monies to the City to found libraries in the early 1900's), what was envisioned by the statute was more of a contract between the library and the City. Thus, this factor was neutral.

Finally, though the City funded the library, the court viewed the library has having a great degree of financial autonomy as to how to use the government funding, so the court viewed this factor as neutral.

The court also distinguished some Department of Labor opinions in the area, such as DOL Opinion 94-21A holding that the Carnegie Center for Literacy and Learning was governmental, but distinguished that opinion as considering whether that Center could participate in a State retirement system for county employees, not as whether the Center could itself maintain governmental plans. The court also apparently considered that the Center was created by County ordinance was a distinguishing factor.

At bottom, then, the court found that three of the Rose factors weighed against governmental status, one favored governmental status, and two were neutral, so the court held that the library's plan was not a governmental plan.

Conclusion, a Caution and Possible Next Steps

This decision may come as a surprise to some, since it has probably been widely viewed that public libraries will normally be agencies or instrumentalities of a political subdivision. It may be that, with only a few changes to the facts concerning the Brooklyn Public Library, it might have been viewed by the court as governmental as well. But the broader concern raised by the decision is that, though the court in this case stated they were not considering the issue, the court's analysis may create concern that this or other public libraries, and other entities not themselves political subdivisions, may fail to be agencies or instrumentalities of a state or political subdivision, and thus perhaps ineligible to participate in their State retirement systems. The correct treatment of such entities has

been in something of a limbo while the IRS has been drafting proposed regulations in this area. This decision may place more attention on what those will provide.

For now, it may be advisable for such "grey area" entities to review their own facts as to their governmental status. And for State retirement systems to continue to review the participation of agencies and instrumentalities in their plans.

If you have any questions, call David Powell, Lou Mazawey, David Levine or your usual Groom lawyer.

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