GROOM LAW GROUP

Publications

What Church Plans and Governmental Plans Now Have in Common – Plaintiffs' Bar Sets Sights on Some Governmental Plans

PUBLISHED
05/09/2019

SOURCE
Groom Benefits Brief

SERVICES
Litigation
- Employer & Sponsor Litigation

The major class action plaintiffs' firms have been going after church plans for a number of years. Well, not all church plans, mainly those sponsored by church-related entities such as hospitals. The plaintiffs even had a number of early successes, particularly in the 9th Circuit, until the U.S. Supreme Court refuted their principle, and fairly novel, legal theory in *Advocate Health Care Network v. Stapleton*, 137 S. Ct. 1652, 1655 (2017). Church plan litigation has since evolved to focus on more traditional legal theories, including state law claims in addition to ERISA claims. There have been a number of settlements, but the suits have not gone away entirely, and have been expensive to defend.

Now Cohen Milstein, one of the same firms that has challenged church hospitals sponsoring plans not subject to ERISA and PBGC coverage, has focused their attention on governmental plans in a class action complaint similar to their attack on church plans. The case is *Shore v. The Charlotte-Mecklenburg Hospital Authority*, Case No. 1:2018cv00961, filed November 19, 2018 (M.D.N.C.).

Any governmental hospital should be immediately concerned about this development. But beyond governmental hospitals, other government-related entities, such as museums, colleges, universities, water districts and so forth, should also be looking at this situation. In some cases, it might be possible to take steps to mitigate litigation risk. If the church plan litigation is any guide, this governmental plan complaint may be the first of many to come.

Summary of the Complaint

Plaintiffs essentially argue in their complaint that the defendant hospital system (the Charlotte-Mecklenburg Hospital Authority, also known as the Carolinas Healthcare System and Atrium) did not satisfy the definition of a "governmental plan" under Section 3(32) of ERISA, and is therefore not exempt from ERISA, resulting in multiple ERISA violations. A defined benefit plan, a 401(k) plan, and a health plan are claimed to have been erroneously treated as non-ERISA governmental plans.

The complaint does not take the approach plaintiffs originally pursued in the church plan litigation that ultimately proved unsuccessful – trying to reinterpret the definition of church plan decades after the fact – but instead appears focused on alleging that the hospital in question simply does not meet the definition.

To this end, plaintiffs make a number of arguments:

- The plans were not established by a governmental entity, nor are they maintained by a governmental entity.
- The hospital system's governing body (in this case a board of commissioners) is not controlled or elected by a state or political subdivision thereof.
- The hospital system's daily operations are not controlled or overseen by officials of any state or political subdivision thereof.
- The hospital system's employees are not treated in the same manner as government employees.
- No state or political subdivision of a state has fiscal responsibility for the liabilities of the hospital system or the plan.

The particular claims raised by the plaintiffs include the usual breach of fiduciary duty claims, failure to make ERISA minimum funding payments, and failure to make disclosures required under ERISA, file 5500s and so on. Particular allegations include not applying ERISA vesting standards (plaintiffs allege that the pension plan, a cash balance plan, had five year vesting rather than three) and that the health plan had some administrative arrangements with related entities that are asserted to be related party transactions and prohibited transactions under ERISA.

Background – the "Governmental Plan" Definition

The definition of "governmental plan" under ERISA (which is almost parallel to the definition in the Internal Revenue Code), is "a plan established or maintained for its employees by the Government of the United States, by the government of any State or political subdivision thereof, or by any agency or instrumentality of any of the foregoing."

Thus, the battleground in these cases may well be whether the hospital system is an "agency or instrumentality" of the State or a political subdivision of the State (in this case, presumably, the county).

As those familiar with governmental plans know, that is a phrase with a long history – and one still being written. That is because there are a number of revenue rulings – Revenue Ruling 89-49 being a leading one – on the question of what is an agency and instrumentality of a State or political subdivision, as well as numerous private letter rulings, DOL advisory opinions and PBGC opinions. Not coincidentally, the factors raised in Rev. Rul. 89-49 are similar to the arguments asserted in the plaintiffs' complaint.

But we have no actual regulations on the governmental plan definition – yet. Instead, we currently have only an Advanced Notice of Proposed Rulemaking ("ANPRM") dating from 2011 that includes a draft proposed regulation (one step short of a proposed rule). That draft proposed regulation, like the rulings, draws on a number of factors, which it then divides into major and minor factors, leaning heavily on those under Rev. Rul. 89-49 and other prior rulings.

Now, we normally take assertions in plaintiffs' complaints in these types of cases with a large grain of salt. In this case, we particularly do so, since the history of the church plan litigation is that the facts first alleged regarding the lack of relationship between the hospitals and the church often do not turn out to be the case.

What Should Other Governmental Hospital Systems and Other Governmental–Related Entities Be Doing?

Forewarned by some of the arguments made by plaintiffs in this new complaint, other government-related entities that have their own plans might also wish to look at how they fare under the past guidance in this area, as well as under the draft proposed regulations. Tightening up governance and administrative processes and plan language to anticipate potential claims may be helpful.

How the entity's plans may differ in operation from ERISA plans may also be worth reviewing, e.g., to identify potential areas that a plaintiff night wish to challenge, such as longer vesting schedules.

What About an IRS Private Letter Ruling or DOL or PBGC Opinion?

One question may be whether an entity has obtained a governmental plan ruling in the past. Because the IRS has the area under study and is preparing proposed regulations, the governmental plan definition is generally a no-ruling area for the time being. (See, for example, IRS Rev. Proc. 2019-3.) Too, having an IRS ruling has been no barrier to challenge by plaintiffs in the church plan area. A legal opinion may be useful from a fiduciary standpoint, but not binding on plaintiffs, of course.

What Happens When the Governmental Plan Regulations are Issued?

The IRS has continued to state informally that it is working on the governmental plan definition regulations (but not during the current shutdown, of course), and it remains on the guidance plan. While those regulations might modify the definition as to some government-related entities (though no one is expecting a wholesale revision), there may well be transition rules for any entities not meeting the final definition, and the ruling process may be reopened. These would also seem to impact any challenges to governmental plan status, though precisely how remains to be seen.

What About State Retirement Systems?

Plaintiffs in these cases seem likely to go after separate plans of these government-related entities, rather than state employee retirement systems themselves. But a state retirement system often has a number of governmental-related but separately organized entities participating in it on the basis of being agencies or instrumentalities of the government, such as museums, colleges, and universities to name a few. To the extent that plaintiffs begin making allegations about governmental hospitals, the same arguments may also apply to those other types of entities and whether they can participate in the state retirement system. Some state retirement systems have already been keeping an eye on this issue for when the governmental plan regulations are proposed. This litigation may have just made this concern more urgent.

Next Steps

Experience in the church plan, 403(b) plan and similar areas indicates that the recent government hospital challenge probably represents the "tip of the iceberg." We recommend that other government hospitals work with their counsel to carefully review how they might fare if they were the target of similar claims. And other government-related entities such as museums, water districts and colleges should do the same. Depending on the results of the review, a plan sponsor may be able to take some steps to strengthen its legal position on governmental plan status.

What Church Plans and Governmental Plans Now Have in Common – Plaintiffs' Bar Sets Sights on Some Governmental PlansDownload