CHURCH ALLIANCE

Acting on Behalf of Church Benefits Programs

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Internal Revenue Service
Room 5203, POB 7604
Ben Franklin Station
Washington, DC 20044

Re: Shared Responsibility for Employers Regarding Health Coverage; Proposed Rule

To Whom It May Concern:

The Church Alliance is pleased to comment on the proposed rule from the Internal Revenue Service ("IRS") regarding Shared Responsibility for Employers Regarding Health Coverage under the Patient Protection and Affordable Care Act ("PPACA") (the "Proposed Rule"). The Church Alliance represents numerous church health plans and their hundreds of thousands of participating employers across the United States and is submitting this comment on their behalf.

The Church Alliance is pleased with the federal agencies for their diligent work in rulemaking under the PPACA. The Church Alliance commends the IRS for publishing the Proposed Rule in a timely manner to help employers understand their obligations regarding health coverage of employees under the PPACA in 2014 and after. The Proposed Rule is important to church plans and their participating employers. The unique structure of church health plans, the varied nature of the structures of the organizations that maintain and fund them and the need to prevent excessive entanglement of the federal government in religion necessitate that the IRS make clear that with respect to ministers the final version of the Proposed Rule should apply at the level of the local church, rather than the denominational level.[1] Applying the Proposed Rule at denominational level could lead to significant unintended consequences and undue burden on entire denominations.

[1] For purposes of this comment, "denomination" refers to the national or highest level of a church in the case of a hierarchical church, or a convention or association of churches in the case of congregational churches. A "local church" refers to a local church, parish, mosque, temple, synagogue or other local place of worship. Some denominations also have intermediate organizations, often regional, such as, conferences, presbyteries, synods, or dioceses; these are called "intermediate organizations". Finally, a "minister" refers to a priest, rabbi, imam or other religious leader of a church.

I. Background on the Church Alliance

The Church Alliance is an organization composed of the chief executives of thirty-eight church benefit boards, covering mainline and evangelical Protestant denominations, two branches of Judaism, and Catholic schools and institutions. The members of the Church Alliance currently provide affordable and comprehensive health benefits to approximately one million Americans.

II. Background on Church Plans

For over 100 years, many denominations have established and maintained health and pension benefit organizations or boards. Through these denominational organizations, local churches are able to offer health and pension benefits to ministers and church employees in a cost effective manner. Equally as important, these national denominational church plans are able to take advantage of "economies of scale," allowing individual local churches and their ministers and lay employees to purchase health care coverage for less than it would cost to purchase similar coverage through the small group or individual insurance markets. This approach has allowed thousands of small local churches, many in rural or disadvantaged areas, to provide benefits to ministers and lay employees. In addition, as ministers and other plan participants move from one local church or to another, they can retain their existing health and pension benefits.

III. Shared Responsibility Rules Generally

The Proposed Rule requires common law employers with 50 or more full-time equivalent employees ("Applicable Large Employers") to provide their full-time employees with affordable health coverage, i.e., coverage that does not cost employees more than 9.5% of their household income (based on the lowest cost employee-only coverage option), and provides minimum value, i.e., is a plan that has a 60% or better actuarial value. Most church health plans will easily satisfy the minimum value requirement. Church employers and church plans will be able to understand and abide by the affordability requirement. The Proposed Rule also applies shared responsibility payments, i.e., penalties, to Applicable Large Employers who fail to provide affordable coverage that covers minimum value to full-time employees beginning in 2014 when a full-time employee receives a premium tax credit for exchange-based health coverage.

The Church Alliance has two primary concerns with the Proposed Rule. First, the Proposed Rule relies on the common law standard to determine who is a minister's employer. As a consequence of each denomination's polity, ministers do not always fit neatly into the traditional common law employer-employee relationship. Because a denomination can sometimes exercise some control over ministers serving as "employees" of local churches, the Church Alliance hopes that the IRS will make clear that despite these authorities at the denominational level or at the intermediate organizations, which are often related to matters of church doctrine, the local church should be considered the common law employer of ministers for purposes of the Proposed Rule.

Secondly, the Church Alliance is pleased to see the IRS apply a reasonable good faith interpretation standard to church employers with respect to interpreting the employer aggregation rules under Sections 414(b), (c), (m) and (o) of the Internal Revenue Code (the "Code") with respect to determining who is an Applicable Large Employer. The Church Alliance notes that the IRS has reserved the section of the

Proposed Rule relating to aggregation of employers that are churches or conventions or associations of churches. The Church Alliance hopes that when the IRS proposes future rulemaking or guidance regarding this section that it will consider flexible approaches to the aggregation rules for church employers. The Church Alliance suggests some possible approaches below.

IV. Common Law Employer

The Proposed Rule relies on the common law standard for determining who is an employee of an organization. See Sections 54.4980H-1(a)(13) and (14) of title 26, Code of Federal Regulations (as proposed). The Church Alliance is not opposed to the use of the common law standard for determining who is an employee for purposes of the Proposed Rule. Churches have become accustomed to this standard. However, the Church Alliance has a distinct concern about the applicability of the common law standard to ascertain who is the common law employer of a minister, particularly in some denominations as explained below.

While, courts and agencies consider various factors[2] to determine an employment relationship between the parties, the right to control is perhaps the most important.

> The "right-to-control" test is the crucial test to determine the nature of a working relationship. The degree of control is one of great importance, though not exclusive. Accordingly, we must examine not only the control exercised by an alleged employer, but also the degree to which the alleged employer may intervene to impose control. In order for an employer to retain the requisite control over the details of an employee's work, the employer need not stand over the employee and direct every move made by that employee. Also, the degree of control necessary to find employee status varies according to the nature of the services provided. The threshold level of control necessary to find employee status is generally lower when applied to professional services than when applied to nonprofessional services. *Weber v. Commissioner*, 104 T.C. 378 at 387 (1994), aff'd 60 F.3d 1104 (4th Cir. 1995) (citations omitted).

Courts have applied the common law standard for determining whether a minister is an employee or self-employed on numerous occasions, and churches and their ministers have developed an understanding of the common law standard. See, e.g., *Alford v. United States*, 116 F.3d 334 (8th Cir. 1997); *Radde v Commisioner*, 74 T.C. Memo 1072 (1997); *Weber v. Commissioner*, *supra*; and *Shelley v. Commissioner*, T.C. Memo 1994-432 (1994). In fact, as a result of these cases, many churches typically treat ministers as employees for income tax and employee benefits purposes. Ministers are statutorily defined as self-employed for employment tax (FICA and SECA) purposes. See Sections 1402(c)(2)(D) and 3121(b)(8)(A) of the Code.

The Proposed Rule applies to common law employers that are Applicable Large Employers. In some denominations, determining who has the right to control and direct a minister in the details and means by which he or she perform services is not simple.

In many denominations, the determination of who is the common law employer of a particular minister is relatively simple. In denominations that are more generally decentralized the local church recruits and

[2] Courts and agencies have considered 7-factor, 8-factor and 20-factor tests in determining employment status under the common law standard.

hires ministers from among its denomination's licensed ministers. The local church typically has a personnel committee drawn from its membership that sets standards for services and monitors the minister's performance and often has the right to dismiss the minister. The local church provides the place of work (a sanctuary and an office), and may provide a parsonage (local church-owned housing near the local church). The local church determines the minister's compensation and benefits. Unless the relationship in these cases is that of independent contractor, determined under the common law standard, the minister would be an employee of the local church for purposes of the Proposed Rule.

However, in other denominations, those more hierarchical or connectional in nature, the determination of which organization within the denomination is the common law employer of a minister is more complicated. The United Methodist Church ("UMC") is such a Denomination. In the UMC, no one has ever determined what part of the denomination is the common law employer for income tax and employee benefits purposes. In at least two cases, *Weber* and *Radde*, courts have held that UMC ministers are common law employees for income tax purposes. Neither court decided which political subunit within the denomination was the common law employer, however. The *Weber* court, in fact, specifically did not reach that conclusion: "We need not decide which part of the United Methodist Church is the employer." *Weber supra* at 394

The determination of the applicable employer is critical under the Proposed Rule. For the reasons explained below, the Church Alliance suggests that the local church be treated as the common law employer for purposes of the Proposed Rule in all denominations. This result is supported by many facts and circumstances, as well as a long history of past practice. Moreover, it is necessitated by the Establishment and Free Exercise Clauses of the First Amendment to the Constitution to prevent excessive entanglement in ecclesiastical policies of a church. See, e.g., *Hosanna-Tabor Evangelical Lutheran Church and School v. EEOC*, 565 U.S. ___ (2012).

In many denominations ministers can be censured or removed from their position by ecclesiastical authorities, such as, bishops; intermediate organizations, e.g., a diocese or state convention; or an ecclesiastical court. This sort of authority or control over ministers in certain cases is not a matter of employment relationships but rather is a matter of church doctrine and theological belief. Applying the common law standard to determine which part of a denomination employs a minister under the Proposed Rule based on ever changing facts and circumstances might lead to disparate outcomes for different denominations, which would essentially result in a favoring of one set of beliefs over another in violation of the Establishment Clause of the First Amendment. To avoid excessive entanglement by the IRS and federal courts in the religious authority structures of various denominations, the Church Alliance suggests a rule that can be applied universally to all denominations without such invasive investigation.

In the UMC, for example, control and direction of ministers is diffuse and shared by many entities within the denomination. The UMC itself is not a legal entity. And the UMC embodied by its General Conference, only acts for two weeks once every four years when it makes the denomination's policy (reflected in its *Book of Discipline*). The UMC has permanent agencies, such as its board of pension and health benefits, which are common law employers of their own permanent employees (some of whom are ministers). The primary intermediate organizations of the UMC are its annual conferences (Conferences), geographic subunits, roughly equivalent to states, like dioceses, that exist to carry out the policy of the General Conference.

UMC ministers are all members of a Conference and typically serve local churches within the Conference. Ministers are originally ordained or licensed by Conferences.[3] Conferences have some common law employees, e.g., the lay employees of the Conference agencies, and some ministers who are compensated by and directly serve the Conference. Other ministers are appointed by the Conference's bishop to serve at local churches across wide geographic areas. These appointments are part of the system of ministers' itineracy that is a deeply held part of the UMC belief system. Ministers move from one local church to another from time to time as part of the connectional system of the UMC. The bishops appoint the Conference's ministers according to the needs of the Conference and each local church.

If one reviews the factors used the common law employment test in light of the UMC polity, most of the applicable factors suggest that the local church is the common law employer of ministers. A few of the factors that apply suggest that the Conference might be viewed as the common law employer, and a few of the factors are shared between the Conference and the local church. In some denominations, some of these factors might be viewed to suggest that the denomination itself could be the common law employer.

The local church provides the place of work; typically provides nearby housing (parsonage); provides religious supplies and materials; pays salary on a regular basis, including during periods of vacation and certain leaves; performs tax reporting duties and any elective withholding; and provides expense allowances (utilities, travel, education, etc.). The local church (and charge conference, which is yet another intermediate organizations of the UMC's federal-type structure) determine compensation for ministers. According to UMC doctrine, other than setting minimum salary rules, the Conference does not have authority to determine minister salaries. The local church pays for the employee benefits provided to ministers, e.g., premiums for life and disability insurance, through the denomination's welfare benefit plan, premiums for health insurance through the multiple employer plan[4] maintained by the Conference or through a local small group market plan, and contributions to the denomination's retirement plan. A relations committee of each local church meets regularly with its ministers to evaluate performance.

In the UMC, local churches ultimately pay the premiums (insured plans) or contributions (self-insured plans) for covering appointed ministers in the annual conference's multiple employer health plan. Some Conferences bill local churches directly; others Conferences bill local churches an overall apportionment that covers health coverage, retirement contributions, death and disability coverage for appointed ministers, and also funds the general church (the mission agencies of the denomination) and the agencies of the annual conference (which employs administrative staff, district superintendents, and conference agency staff).

The UMC's *Book of Discipline* states that ministers are not employees of the local church, Conference or any other part of the UMC. However, the UMC realizes that for certain secular law purposes, ministers may be characterized as employees. The *Weber* case is one example. Assuming that UMC ministers generally would be characterized as common law employees of some part of the denomination under the Proposed Rule, it is critical to know which part of the denomination would be considered the employer. The Conferences and local churches in the UMC have long acted under an assumption that local churches

[3] By comparison, the Southern Baptist Convention's congregational structure addresses matters of ordination and licensing of ministers at the local church. This reflects a theological belief in the autonomy of the local church.

[4] Section 2(a) of the Church Plan Parity and Entanglement Prevention Act of 1999 (Public Law 106-244) clarifies that church health plans are multiple employer plans, with numerous participating common law employers.

are the common law employer of ministers appointed to serve them for health plan purposes. A determination to the contrary could put many of the practices of the UMC's Conferences at risk.

For example, with regard to their health plans, Conferences treat the local church as the organization responsible for paying the "premium" to cover ministers appointed to the local church. The Conference invoices the local churches for coverage of its minister(s) and his or her dependents. Though the Conference may set some participation rules, just as an insurance company would in the small group market, the Conference does not pay for the coverage of ministers serving local churches. This is in many ways analogous to a multiemployer plan. Local churches exclude the employer-paid portion of the health coverage from the minister's income under Section 106 of the Code.

The local churches participating in denominations' church health plans, including those UMC health plans, have benefitted from numerous small employer exceptions, notably the small employer exception to the Medicare Secondary Payer Rules and the small business health care tax credit under the PPACA (the Section 45R Tax Credit). If the UMC's Conferences were determined to be the common law employers of ministers, these exceptions and benefits, pursued in good faith, which have allowed local churches to continue to provide robust health benefits to UMC ministers, would be put at risk. A determination that the Conference, or the denomination itself, is the common law employer of ministers at local churches under the Proposed Rule could cause significant financial exposure to the UMC and its Conferences.

Equally as important, a determination that the Conference is the common law employer of ministers for the Proposed Rule may leave the Conference in a situation where it cannot always control whether or not it would be subject to shared responsibility payments (Penalties) under the Proposed Rule. For example, under the UMC's *Book of Discipline* compensation for ministers is set by the local church and charge conference. The local church also manages payroll tasks and deductions for ministers. Therefore, the local church has substantial control over whether the required contribution assigned to the individual ministers for self-only coverage under a health plan would be affordable, i.e., not more than 9.5% of W-2 Wages. Conferences (or their insurers) determine the overall premium charged to the local church, and in many cases suggest a percentage of the premium to be paid by individual ministers, but the ultimate control over these compensation matters is held by the local church. These facts support treating the local church in the UMC as the "employer" for the purposes of the Proposed Rule under the common law standard.

Similar circumstances exist in other denominations with intermediate organizations (dioceses, state conventions, presbyteries or synods), and many denominations or their intermediate organizations have at least some influence over the placement of ministers at local churches and some oversight over their performance (and sometimes removal power).

Moreover, some denominations have not maintained a health plan historically. Health coverage for ministers in these denominations may be provided in some cases by the local church, and in other cases none may be provided. Most local churches in these denominations are unlikely to be Applicable Large Employers under the Proposed Rule. If under the Proposed Rule ministers were considered to be common law employers of the local churches, the Proposed Rule would have little impact on the long-standing practices of that denomination. On the other hand, if the Proposed Rule were applied to the denomination as common law employer (for example, if that denomination, through an agency or a bishop, had the power to terminate ministers from local churches for not complying with religious

doctrine), the denomination as a whole would more likely be an Applicable Large Employer, and could face significant unexpected financial consequences as a result.

For the reasons set forth above, the Church Alliance strongly urges the IRS to apply the employer shared responsibility rule under the PPACA to denominations at the level of the local churches of the denominations.

V. Controlled Group Rules

The Church Alliance commends the IRS for allowing churches and conventions and associations of churches to rely on a reasonable good faith interpretation of Sections 414(b), (c), (m) and (o) of the Code in determining whether a person or group of persons is an Applicable Large Employer. As the IRS states in the preamble to the Proposed Rule:

> Section 4980H applies to all common law employers, including an employer that is a government entity (such as Federal, State, local or Indian tribal government entities) and an employer that is an organization described in section 501(c) that is exempt from Federal income tax under section 501(a). The proposed regulations reserve on the application of the section 414(b), (c), (m), and (o) aggregation rules in section 4980H(c)(2)(C)(i) to government entities and churches, or a convention or association of churches (as defined in §1.170A-9(b)). Until further guidance is issued, government entities, churches, and a convention or association of churches may rely on a reasonable, good faith interpretation of section 414(b), (c), (m), and (o) in determining whether a person or group of persons is an applicable large employer.

The employer aggregation rules are difficult to apply to church employers. Sometimes there can be close religious affinity among employers without there being any shared day-to-day financial and operational control. Sometimes the connection between church employers is only through a denomination or its intermediate organizations, e.g., synods or conventions.

For example, in the Southern Baptist Convention, the state conventions may have the power to remove and reappoint the trustees or directors of certain organizations that are affiliated with the convention to ensure theological integrity. The employer aggregation rules might treat separate and distinct Baptist employers in different geographic locations in a state as one employer. This could have adverse consequences related to the Proposed Rule, e.g., causing small employers to be considered part of an Applicable Large Employer. For example if a state convention has the power to remove and reappoint the directors of a Baptist college and also has the same power to remove and reappoint directors of a small charity in a town across the state, the aggregation rules might treat these two employers that have traditionally had no interaction or affiliation other than their connection to the state convention to be one employer under the Proposed Rule.

Under these circumstances, even if the small charity has only a few employees and has never provided health insurance for them, in 2014, the charity could face shared responsibility penalties under the Proposed Rule as part of an Applicable Large Employer, counted together with the employees (across the state) of the college. The college and charity have no control over one another's day-to-day operations or finances, nor does the state convention for that matter.

Given these types of facts and circumstances, the Church Alliance suggests that the IRS ensure that application of the aggregation rules to churches and conventions and associations of churches be mindful of the unique and varied nature of denominational polities.

The Church Alliance suggests that the IRS consider the provisions related to the employer aggregation rules contained in the proposed Church Plan Clarification Act (S. 3532 in the 112th Congress). Those provisions follow:

> (A) General Rule—Except as provided in subparagraphs (B) and (C), for purposes of sections 414(c) and (m), an organization that is otherwise eligible to participate in a church plan as defined in section 414(e) shall not be aggregated with another such organization and treated as a single employer with such other organization unless—
>
> > (i) one such organization provides directly or indirectly at least 80 percent of the operating funds for the other organization during the preceding tax year of the recipient organization, and
> > (ii) there is a degree of common management or supervision between the organizations.
>
> For purposes of this subparagraph, a degree of common management or supervision exists only if the organization providing the operating funds is directly involved in the day-to-day operations of the other organization.
>
> (B) Nonqualified Church-Controlled Organizations—Notwithstanding the provisions of subparagraph (A), for purposes of this sections 414(c) and (m), an organization that is a nonqualified church-controlled organization shall be aggregated with one or more other nonqualified church-controlled organizations, or with an organization that is not exempt from tax under section 501, and treated as a single employer with such other organizations, if at least 80 percent of the directors or trustees of such organizations are either representatives of, or directly or indirectly controlled by, the first organization. For purposes of this subparagraph, a 'nonqualified church controlled organization' shall mean a church-controlled organization described in section 501(c)(3) that is not a qualified church controlled organization described in section 3121(w)(3)(B).
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> (C) Permissive Aggregation Among Church-Related Organizations—Organizations described in subparagraph (A) may elect to be treated as under common control for purposes of section 414(c). Such election shall be made by the church or convention or association of churches with which such organizations are associated within the meaning of section 414(e)(3)(D), or by an organization determined by such church or convention or association of churches to be the appropriate organization for making such election.
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> (D) Permissive Disaggregation of Church-Related Organizations—For purposes of subparagraph (A), in the case of a church plan (as defined in section 414(e)), any employer may permissively disaggregate those entities that are not churches (as defined in section 403(b)(12)(B)) separately from those entities that are churches, even if such entities maintain separate church plans.
>
> (E) Anti-Abuse Rule—For purposes of subparagraphs (A) and (B), the anti-abuse rule in Treasury Regulation section 1.414(c)–5(f) shall apply.

These provisions reflect a considered and flexible approach to the employer aggregation rules that prevent excessive entanglement between church and state.

VI. Missionaries

The Church Alliance also suggests the IRS adopt some flexibility with respect to the reporting practices of some mission-sending agencies of churches. Some denominations have church employers that are mission-sending organizations. They support missionaries in certain ways. For example, some mission-sending agencies require the missionaries to secure their own funding, and then the organization holds the funds for the missionary's benefit due to their being in foreign jurisdictions for most, if not all, of the year. These organizations are not the common law employer of the missionaries, but rather are more like a trustee of certain funds. The assumption that these missionaries are not common law employees is supported by the court in *Greene v. Commissioner*, T.C. Memo 1996-531 (1996). The court applied an 8 factor test for the common law standard of employment, and found that the foreign missionary for the Assemblies of God church was self-employed not an employee.

However, in certain cases, the mission-sending organizations provide *Forms W-2* for the missionaries, despite not being their employer under the common law standard. The Church Alliance recommends that the IRS consider these sorts of facts in applying the common law standard of employment to missionaries and other extended service and evangelical mission type ministers. The practice of issuing *Forms W-2* on behalf of foreign missionaries by a mission-sending agency should not be determinative of an employment relationship under the common law standard for the purposes of the Proposed Rule.

VII. Conclusion

For the reasons explained herein, the Church Alliance recommends that the IRS apply the employer shared responsibility rule under the PPACA to local churches with respect to ministers. If a denomination or its intermediate organizations were deemed the common law employer of a minister under the Proposed Rule, significant adverse unintended consequences could result. In addition, the Church Alliance urges the IRS to consider flexible and considered approaches to the employer aggregation rules in future rulemaking and guidance applying the aggregation rules to church employers.

We would welcome the opportunity to discuss our recommendations with the IRS at your convenience. Please feel free to contact the undersigned at 202-661-3882 if you have any questions or wish to discuss this matter further.

Sincerely,

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On Behalf of the Church Alliance