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CHURCH ALLIANCE

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July 17, 2017

The Honorable Orrin Hatch
Chairman
U.S. Senate Committee on Finance
219 Dirksen Senate Office Building
Washington, D.C. 20510-6200

Dear Chairman Hatch:

The Church Alliance is pleased to submit the following comments in response to your request for recommendations on comprehensive tax reform. As you know, churches, synagogues, and other religious organizations are at the heart of communities across our nation. Over the years, a number of important tax provisions have developed that reflect the unique characteristics of these institutions, particularly in the areas of health and retirement security. We look forward to working with you and your staff to pursue comprehensive tax reform that preserves the spirit of these provisions, and helps all Americans save and invest for their future.

ABOUT THE CHURCH ALLIANCE AND CHURCH BENEFIT PLANS

The Church Alliance is a coalition of chief executive officers of thirty-seven (37) denominational benefit programs, covering mainline and evangelical Protestant denominations, two branches of Judaism, and Catholic schools and institutions. These benefit programs provide retirement and health benefits to more than one million clergy (including ministers, priests, rabbis, and other spiritual leaders), lay workers, and their family members.

By way of background, denominational benefit plans are typically maintained by a separately incorporated church benefit organization (often called a pension board or benefit board) designated as the entity that sponsors or administers and maintains the benefit programs for eligible employees within the denomination. These benefit plans are generally multiple-employer in nature and cover thousands of church and

synagogue employers throughout the country, many of which are located in rural communities. These programs often also cover foreign mission organizations and their missionaries. Church benefit organizations thus typically provide retirement and welfare benefits to thousands (or, in the case of the larger denominations, tens of thousands) of clergy and lay workers at multiple locations. Having a centralized program sponsored by one organization serving multiple church employers helps ensure continuity and consistency of employee benefits for the many clergy who move from one church or church-related organization to another to fulfill the ministry of a denomination.

The participating employers covered under these church benefit plans range from synagogues and churches to church-affiliated schools, day cares, and nursing homes. Many are small, local churches with few employees. Oftentimes, the local church's pastor may be that church's only employee. If there are other employees, they are often part-time workers who assist with secretarial or bookkeeping duties or perhaps provide for building maintenance. In addition, many small local churches are staffed by bi-vocational pastors (clergy who work for a secular employer part-time or full-time and pastor a church or churches on the side). Denominational plans also provide benefits to self-employed clergy.

In addition to serving local churches and synagogues, denominational benefit plans cover other church-related organizations that historically have been viewed by denominations as an extension of the ministry and are considered to be within the bounds of the particular denomination with which they are affiliated. For example, participating employers can include church-related nursing homes, daycare centers, summer camps, preschools, colleges, universities, hospitals, and other social service organizations. All of these organizations typically are considered as fulfilling the ministry and mission of the church.

Local churches are typically run by volunteer trustees, vestries, boards of directors, boards of deacons, boards of elders, parish councils, or the like. The individuals who hold these volunteer leadership roles are focused on fulfillment of their church's ministry and have the burden of allocating both human and monetary resources to direct ministry, which leaves them with little time to focus on employee benefit compliance issues. In the case of small to medium-sized churches and synagogues, these individuals may, and usually do, lack the expertise required to understand the various employee benefit legal requirements that must be met. Except in the largest churches, the typical church budget does not support the hiring of outside experts required to assist the local church with employee benefits compliance. As a result, absent the availability of the programs provided through church benefit organizations and church associations, many of these employers would be unable to provide adequate retirement or welfare benefits to their employees.

The benefits provided by church benefit organizations or church associations may be mandated by the denominational polity (the operational and governance structure of a denomination). Over the years, church denominations have organized themselves in a variety of

ways reflecting their own theological beliefs. Some denominations are organized in a “hierarchical” polity, in which a “parent” church organization sets the policy for the entire denomination. Other denominations have organized themselves in a diocesan, synodical or presbyterian structure under which policy-making is carried out on a local or regional level, through representatives drawn from the various churches within the geographic area served by a particular level of governance. Several other denominations, composed of autonomous churches and synagogues, or conventions or associations of churches, cooperate in a “congregational” form of governance in which churches and church ministry organizations are associated by voluntary and cooperative participation.

It is these diverse sets of church polities, and the differing levels of control exercised over churches and church ministry organizations under a particular polity, that present difficulties with employee benefit requirements of the tax code, ERISA, and other laws, most of which were designed with a for-profit, corporate structure in mind. Together with the Constitutional proscription against excessive government entanglement with religion, these considerations have led to the development of a legal framework for church plans that reflects their unique characteristics.

PRIORITIES FOR TAX REFORM

Central to this legal framework are several longstanding provisions of the tax code that have been carefully tailored to the needs of churches and church ministry organizations. Retaining and strengthening these provisions is critical to the retirement security of modestly-paid clergy and others who have devoted their lives to ministry. In addition, a comprehensive federal framework is important to promote clarity and consistency for church plans nationwide. As you move forward with tax reform, we urge your attention to the following issues.

CLARIFICATION FOR § 403(b)(9) PLANS

Clarification of the rules governing church retirement plans is urgently needed to reaffirm current law dating to 1980, and more than 30 years of administrative practice to ensure that all church-affiliated organizations can participate in a church § 403(b)(9) plan. Throughout their history, the advantages of church retirement plans have been open to church clergy and lay workers serving individual churches, as well those of affiliated organizations that advance the mission of the denomination, such as children’s homes, daycare centers, summer camps, nursing homes, retirement centers, preschools, colleges and universities, and other religious nonprofit entities.

The broad availability of these plans is now under threat by a recent IRS and Treasury position that departs from longstanding precedent to restrict the retirement plan options available to employees of certain religiously-affiliated organizations. Under this interpretation, employees of these organizations will no longer be able to participate in § 403(b)(9) plans. This has

significant drawbacks for church retirement plans, but most importantly, for the beneficiaries they serve.

The IRS and Treasury interpretation could mean that clergy and church lay workers lose access to important § 403(b)(9) features, such as access to socially screened investment options that reflect a particular denomination's faith and beliefs, as well as to annuitization choices that can be provided directly by the church benefit program. Moreover, this approach would inevitably lead to higher costs with fewer § 403(b)(9) plan participants over which to spread plan expenses.

Recognizing these implications, bipartisan, broadly supported legislation has been introduced in the House and Senate (H.R. 2341 / S. 674) to clarify the appropriate and intended broad availability of § 403(b)(9) plans. We strongly urge enactment at the earliest possible opportunity, either independently or as part of tax reform. Urgent resolution of this issue is critical to the retirement security of clergy and church lay workers across the nation.

PARSONAGE ALLOWANCE

For nearly 100 years, exclusion from taxation of church-provided housing to clergy has reflected the long-held belief that a clergy member's home is an extension of the church. In addition, the parsonage allowance under § 107 has been important in helping modestly-paid clergy and retired clergy afford housing and move, sometimes frequently, to serve the needs of the church. This is particularly true in rural areas where many congregations are small, pay is low, and clergy are very dependent upon their churches providing or paying for their housing. This important tax policy is subject to commonsense limitations on the rental value of the home subject to the allowance, and applies to just a single property.

Moreover, the parsonage allowance must be viewed in the context of § 119, which excludes secular employer-supplied housing from employees' income under certain circumstances (e.g., an on-site hotel manager's housing). However, as applied to clergy, some § 119 criteria would produce unequal results between denominations that have different theological and polity based practices relating to clergy and housing. § 107 allows clergy of all faiths to share equally in this important tax policy.

Given the continuing need for the parsonage allowance, we strongly urge its preservation as part of tax reform.

RETIREMENT PLAN STREAMLINING/CONSOLIDATION

As described above, church retirement plans have evolved, in some cases over hundreds of years, to reflect the unique characteristics of the denominations and populations they serve. The benefits provided by church plans are often mandated by the denominational polity (the operational and governance structure of a denomination), and are tailored to meet the needs of

clergy and church lay workers who are often modestly paid. Over time, laws have been developed to work with a variety of diverse denominational structures, and to allow employees of religiously-affiliated institutions to have a meaningful opportunity to save for retirement in a manner that comports with their faith.

In this context, proposals to streamline or consolidate the various retirement plan options under the tax code (401(a), 403(b), 401(k), 457(b), etc.) threaten to eliminate provisions that church plans have come to rely upon in providing a secure, stable retirement for their beneficiaries. We caution against any streamlining or consolidation proposal that would undermine these provisions, which would also create severe compliance challenges (in some cases making the plans untenable) and burdensome transition costs for church plans and church-affiliated organizations. Specifically, we urge your preservation of the following provisions that are instrumental to the retirement security of often modestly-paid clergy and lay workers:

- **Different nondiscrimination testing rules.** 403(b) plans maintained by churches and qualified church-controlled organizations are exempt from nondiscrimination rules, based upon Congress's recognition of the difficulty that churches run by volunteers would have in assuring compliance with complex rules without directing their scarce resources away from mission activities; in contrast, plans maintained by larger, more sophisticated non-qualified church-controlled organizations are subject to nondiscrimination testing rules. Similarly, in recognition of the difficulty that church plans have in satisfying certain nondiscrimination rules due to their unique structures, the IRS granted an extension to the effective date of certain nondiscrimination regulations as applicable to church 401(a) qualified plans. These policies reflect the unique workforce characteristics of churches and church-related organizations.
- **Exemptions for church 401(a) plans.** With respect to defined benefit plans, the tax code reflects a number of accommodations to the unique structure of religious denominations and the plans they have designed to assure retirement security of clergy and church workers serving as called throughout their career by their denominations. These tax code provisions allow missionaries, self-employed clergy and chaplains to participate and exempt church plans from various of the qualification requirements applicable to private plans.¹ These exemptions are important because many of the rules that would conflict

¹ Church 401(a) plans are not subject to numerous plan qualification requirements including, qualified joint and survivor annuities under §§401(a)(11) and 417; preservation of accrued benefits during a plan merger or transfer of plan assets under §§401(a)(12) and 414(l); anti-alienation rules of §401(a)(13); benefit commencement requirements of §401(a)(14); the prohibition on reducing retiree vested benefits due to Social Security increases under Code §401(a)(15); and the prohibition on forfeiture of accrued benefits from employer contributions due to withdrawal of employee contributions under Code §401(a)(19), if the employee is 50% vested. Church plans are subject to the pre-ERISA minimum participation standards, minimum vesting standards and minimum funding standards and exempt from the anti-cutback requirements of §411(d)(6). Church plans also have relaxed standards for defining a highly compensated employee under Code §414(q)(9) and domestic relations orders under Code §414(p). There are also specialized or relaxed rules pertaining to churches in computing the limits on employee contributions under Code §§401(a)(17), 402(g)(7) and 415(c)(7).

with the design of plans established to meet the needs of these workers decades ago or otherwise would be unworkable in the decentralized, polity-driven context of a denominational church plan.

- **Flexible investment options for church plans.** Church plans offer broad latitude for denominational benefit organizations (or their investment committees, which are typically composed of individuals with substantial investment expertise) to offer an array of investment alternatives beyond annuity contracts and mutual funds, such as pooled investments in stocks, bonds, collective investment funds and other prudent options that benefit from lower fees and economies of scale. Many church plans also further the missions of their respective denominations by incorporating faith-based screens and positive social purposes in their investment decisions.
- **Self-annuitization feature for church 403(b)(9) plans.** IRS regulations permit sponsors of church defined contribution 403(b)(9) plans to “self-annuitize” benefits, providing valuable flexibility and stability through lifetime retirement income, at a lower cost to participants than purchasing annuities from a commercial issuer. Churches practice their commitment to care for those that serve the church by using these provisions to support these faithful servants and their surviving spouses.
- **Special annual addition limits for church 403(b) plans.** Some church employees and missionaries may have little or no taxable income due to very low compensation. Consequently, church 403(b) plans provide a special annual addition limit of \$10,000 per year (subject to a lifetime maximum of \$40,000), regardless of the beneficiary’s taxable income. This provides clergy, lay workers, and missionaries with an opportunity to create retirement benefits while performing vital church mission work, notwithstanding their low taxable income.
- **Definition of compensation.** The limits on contributions under the different types of plans are based in part on a participant’s compensation. For this purpose, compensation is defined slightly differently with respect to 403(b) plans. The differences are attributable to special rules that should be retained, such as the ability to treat former employees as having compensation for five years (§ 403(b)(3)), and the treatment of clergy (§ 414(e)(5)(B)). From a policy perspective, there is no reason to harm either clergy or former church employees who may need additional retirement savings.
- **Direct contributions by self-employed clergy.** Certain chaplains and self-employed clergy are authorized to make direct contributions to a church plan. Contributions to a § 403(b)(9) plan are deductible by clergy under § 404(a)(10). This is a valuable retirement savings option for clergy who might otherwise lack the opportunity to participate in a church plan.

QUALIFIED RETIREMENT PLAN PARITY WITH IRAS

Church retirement plans are disadvantaged relative to Individual Retirement Accounts (“IRAs”) in several important respects. First, participants are eligible to make a tax-free Qualified Charitable Distribution (“QCD”) directly from an IRA to a charity, but are not permitted to do so from a church retirement plan. Church plans should be allowed to facilitate tax-free QCDs for their members and beneficiaries, making it easier for clergy and other church workers to engage in charitable giving.

In addition, IRAs and church retirement plans are treated dissimilarly regarding required minimum distributions (“RMDs”). The rules applicable to IRAs are more equitable, basing the RMD amount on the age of the recipient. Church retirement plans should be able to offer the same equitable treatment for a clergy member’s surviving spouse.

CORPORATE INTEGRATION

The Church Alliance understands and appreciates the goal of greater parity between the corporate and passthrough tax systems. However, the way in which Congress pursues this goal could have significant implications for churches and other tax-exempt charitable organizations. Specifically, we urge you to avoid any approach to corporate integration that would result in the imposition of new taxes on the earnings that these organizations receive from their investment portfolios. Increased taxation could limit returns to church benefit plan participants, eroding the stability of their retirement. We encourage you to be cognizant of the interaction with the tax exemption for non-profit organizations as you consider corporate integration proposals.

ROTH TREATMENT

Finally, we have taken note of recent discussions about potential limitations on the amount of pre-tax elective deferral contributions to certain retirement plans; contributions in excess of these limits would be treated as post-tax or “Roth” contributions. We have serious concerns that, in addition to not yielding any “real” additional revenue for the government (as it would merely shift the timing of collection, not the incidence of taxation), these proposals could significantly reduce the incentives to save for retirement. This could have severe consequences, particularly for modestly-paid individuals who might not otherwise save for retirement absent the tax incentive provided by deferral.

Like you, we strongly believe that tax reform should make it easier and more compelling for Americans to save and invest for their future – not the other way around. We encourage you to pursue policy solutions that achieve this goal, rather than ones that could frustrate it.

* * *

In closing, the Church Alliance greatly appreciates the opportunity to submit these comments. We are pleased to serve as a resource to the Congress and the Committee on these and related matters. We look forward to our continued work together on these important issues as comprehensive tax reform moves forward. Thank you for your consideration.

Sincerely,

A handwritten signature in black ink, reading "Barbara A. Boigegrain". The signature is written in a cursive style with a large, looping initial "B".

Barbara A. Boigegrain
Chair of the Church Alliance