VENABLE LLP

TO	Diocese of Fall River Joe Harrington Vice Chancellor of Administration Michael Carroll General Counsel Peter Powers Director of Human Resources	DATE	April 3, 2023
FROM	Christopher N. Moran, Esq. Stephanie M. Loughlin, Esq.	EMAIL	CNMoran@Venable.com SMLoughlin@Venable.com
		PHONE	(410) 244-7604 (Chris) (202) 344-4874 (Stephanie)
RE	**Diocese of Fall River Aggregation Rules Analysis for Employee Retention Credit**		

Privileged & Confidential – Attorney-Client Communication

Roman Catholic Bishop of Fall River (a Corporation Sole) d/b/a Diocese of Fall River (the "Diocese" or the "Corporation Sole") is a Roman Catholic Diocese serving Southeastern Massachusetts, Cape Cod, and nearby islands such as Nantucket. The Diocese includes parishes, schools, and numerous ministries. Some of these ministries, including Saint Vincent's Services, Inc., and various nursing homes and social service agencies, are separately incorporated. This memorandum analyzes whether the separately incorporated entities and the unincorporated parishes, ministries, and schools that are part of the Diocesan corporation (these unincorporated entities being the "Diocesan entities") can be treated as separate employers for purposes of the Employee Retention Credit ("ERC") in Section 2301 of the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act"), and Section 3134 of the Internal Revenue Code of 1986 (the "Code").

Overview of Diocese and Diocesan Entities

The Diocese operates under both civil law and canon law. The Diocese was incorporated by the Massachusetts legislature in 1904 as a "Corporation Sole" to facilitate the ownership and orderly transfer of Diocesan property for civil law purposes. The Diocese has a single officeholder, the Bishop of Fall River. Under civil law, the Diocese holds legal title to the assets of all entities that are part of the Corporation Sole, which includes the Chancery Office, the Diocesan schools, and the parishes and parish schools.

The Bishop leads and guides Catholics and Catholic institutions in the Diocese's territory. By virtue of his office, the Bishop serves as Chairman or President of the separately incorporated organizations within the Diocese and has authority to appoint the members of their boards of directors. The Bishop does not own the assets of the Diocesan entities and is not involved in their day-to-day operations. While the Bishop is the sole officeholder for the Corporation Sole, each Diocesan entity has a finance council or similar body that functions like a board of directors. Under canon law, each Diocesan entity is a juridical person, similar to a civil law corporation, with ownership of its own assets.[1]

Chancery Office

The Chancery Office represents the central operations and assets of the Corporation Sole. It provides administrative services and programmatic and financial support to the Diocesan entities and the separately incorporated entities. The Chancery Office administers the various employee benefit programs of the Diocese and provides loans to and holds deposits of excess funds for the Diocesan entities. The employee benefit plans sponsored by the Diocese are treated as multiemployer plans. The Chancery Office also supports many of the Diocese's ministries. The Chancery Office has a taxpayer identification number, and files its own employment tax return. The financial statements of the Chancery Office do not include the operations or activities of the Diocesan entities.

Diocesan Schools

In 2020, there were five high schools in the Diocese: Bishop Connolly High School in Fall River, Bishop Stang High School in Dartmouth, Bishop Feehan High School in Attleboro, Saint John Paul II High School in Hyannis, and Coyle and Cassidy School in Taunton. Coyle and Cassidy, which also served middle school students, merged into Bishop Connolly after the end of the 2019-2020 academic year. The high schools, along with the Little Flower Early Education Center in Attleboro (serving infants to PreK), Saint Francis Xavier Middle School in Hyannis (which subsequently merged into Saint John Paul II High School), and Saint Margaret Primary School in Bourne (a PreK to Grade 4 school that closed after the end of the 2019-2020 academic year) are commonly referred to as the Diocesan schools, and are operated by the Roman Catholic Bishop of Fall River Catholic Education Center, which has a taxpayer identification number, is the employer of record for the teachers, staff, and administrators of the Diocesan schools, and files a single employment tax return. The schools do not have separate taxpayer identification numbers.

Parishes and Parish Schools

There are nearly 80 separate parishes within the Diocese. Each parish is operated by its pastor or parish administrator, subject to the norms of Church law, and is funded primarily by its own collections. The parishes pay an annual assessment to help fund the central administration of the Diocese. Each parish maintains its own bank accounts, has its

[1] Code of Canon Law, Book I, Title VI, Chapter II, Can. 114, §1, Can. 116, Can. 120, §1; Book V, Can. 1256.

own taxpayer identification number, and files its own employment tax return. There are 15 parish schools. Some of these schools are operated under the taxpayer identification number of the parish. Others have their own taxpayer identification number.

<u>The Employee Retention Credit and the Aggregation Rules</u>

Under Section 2301(d) of the CARES Act, all persons treated as a single employer under Section 52(a) or (b) of the Code, or Section 414(m) or (o) of the Code, are treated as a single employer for ERC purposes.[2] Because Section 52(a) refers to corporations related by common stock ownership and Section 52(b) defines common control by ownership of stock in a corporation; profits or capital in a partnership; the beneficial interest in a trust or estate; or individual ownership in a sole proprietorship, these Code sections are not applicable to the Diocesan entities, which are unincorporated, or to the separately incorporated entities because they are organized as nonstock corporations.[3] Thus, this memorandum analyzes only the aggregation rules under Section 414.

The term "person" when used in the Code is broadly defined to include an individual, trust, estate, partnership, association, company, corporation, *or other unincorporated association or group*.[4] Because the aggregation rules under Section 414 apply to "persons," not just "corporations," separate incorporation (or the lack thereof) does not determine if Diocesan entities are aggregated and treated as a single employer.

Q/A 7 of Notice 2021-20 states that persons that are members of a controlled group under Section 414(m) or (o) of the Code are treated as a single employer for various purposes of the ERC, including for purposes of determining whether the employer is a "small employer" or "large employer," whether the employer's operations were fully or partially suspended due to COVID-19-related government orders, and for purposes of determining whether the employer experienced a significant decline in gross receipts. The employer size thresholds are based on the number of regular, full-time employees the employer had in 2019. Therefore, in applying the aggregation rules to determine the employer's size, the aggregation analysis looks at whether two or more persons would be treated as a single employer in 2019. For determining whether the employer's operations were fully or partially suspended or whether the employer experienced a significant decline in gross receipts, the aggregation analysis looks to 2019, 2020, and 2021.

Neither Notice 2021-20 nor any other IRS guidance on the ERC interprets the substantive requirements of the aggregation rules under Section 414(m) and (o) of the Code (or Section 52(a) and (b) of the Code).[5] Notice 2021-20, Q/A 9 states that tribes and tribal entity employers should use a "reasonable, good faith interpretation in determining how the aggregation rules apply." While the direction to use a "reasonable, good faith" interpretation is addressed specifically to tribal governments and tribal entity employers,

---

[2] *See also* Notice 2021-20, Q/A 9, p. 24, 2021-11 I.R.B. 922 (March 2, 2021).

[3] *See* Code Sections 52(a) and 1563(a); Code Section 52(b) and Treas. Reg. 1.52-1(c)(2).

[4] Code Section 7701(a)(1); Treas. Reg. 301.7701-6(a).

[5] Notice 2021-20, Section II.E, p. 13.

such a standard is generally applicable when the IRS has not issued regulatory guidance interpreting a statutory provision.[6] Furthermore, as discussed below, the Treasury Department and the IRS have historically applied a similar "reasonable, good faith" standard for churches and religious organizations in determining how the aggregation rules apply. Therefore, churches should use a reasonable, good faith interpretation of how the Section 414 aggregation rules apply for purposes of the ERC.

Overview of Aggregation Rules Under Section 414 of the Code

In 1989, the IRS published Notice 89-23, which instructed nonstock, tax-exempt organizations to use a "reasonable, good faith" standard for determining whether to treat one or more tax-exempt organizations as a single employer under the aggregation rules in Section 414 of the Code. Notice 89-23 provided a safe harbor whereby two organizations would be treated as members of a controlled group if (1) at least 80% or more of the trustees or directors of one organization were representatives of the other organization, or were appointed by the other organization (the "governance control test"); or (2) one organization provided at least 80% of the operating funds for the other organization, and was directly involved in its day-to-day operations (the "financial control test").[7]

In 2007, the IRS issued Treasury Regulations under Section 414 of the Code. Treasury Regulation 1.414(c)-5(b) provides, in general, that two tax-exempt organizations will be treated as a single employer for purposes of Section 414(b), (c), (m), and (o) of the Code if at least 80% or more of the trustees or directors of one organization are representatives of the other organization or are directly or indirectly controlled by the other organization (the "governance control" test). A trustee or director is controlled by another exempt organization if the other organization has the general power to remove the trustee or director and appoint a new trustee or director. A trustee or director is a representative of another exempt organization if the trustee or director is also a trustee, director, agent, or employee of the other exempt organization. Because the Bishop is the sole officeholder for the Diocese and has the power to appoint the members of the governing bodies of the separately incorporated entities, all these entities would be treated as a single employer if the governance control test applied to the Diocese.

However, Treasury Regulation 1.414(c)-5(a) states that the governance control test does not apply to "churches" or conventions, associations of churches, or elementary or secondary schools controlled, operated, or principally supported by churches. For purposes of applying the aggregation rules, the Diocese is considered a church or a convention or association of churches.[8] Treasury Regulation 1.414(c)-5(a) permitted churches (including

[6] *See, e.g.*, Notice 2018-67, 2018-36 I.R.B. 409 (August 21, 2018) (stating that a tax-exempt organization can rely on a "reasonable, good faith" interpretation of Section 512(a)(6) of the Code to determine whether it has more than one unrelated trade or business); Notice 2019-9, 2019-4 I.R.B. 403 (December 31, 2019) (instructing tax-exempt organizations to base their positions on a "reasonable, good faith" interpretation of Section 4960 of the Code).

[7] Notice 89-23, 1989-1 C.B. 654, Part V.B.2.a. While Notice 89-23 was largely obsoleted by the 2007 regulations, Part V.B.2.a of Notice 89-23 was not obsoleted. *See* Rev. Rul. 2009-18, 2009-27 I.R.B. 1.

[8] Code Section 3121(w)(3)(A).

related elementary or secondary schools) to continue using the reasonable, good faith, standard established in Notice 89-23 to determine which entities are in their controlled groups.[9] Thus, under the 2007 Treasury Regulations, even if a church appointed 80% or more of the members of the governing body of another church or school, the use of the governance control test to determine aggregation was optional for these entities.

2015 PATH Act and Church Plan Clarification

In 2015, Section 336 of the Protecting Americans from Tax Hikes ("PATH") Act amended Section 414(c) of the Code to clarify the application of the employee benefit aggregation rules to churches. Under Sections 414(c)(2)(A) and Section 414(e)(3) of the Code, churches, conventions or associations of churches, or elementary or secondary schools that are controlled, operated, or principally supported by a church or convention or association of churches (collectively "churches") and other "qualified" church-controlled organizations are treated as a single employer under Sections 414(c) and 414(m) of the Code only if (i) one such organization provides at least 80% of the operating funds for the other organization and (ii) there is a degree of common management between the organizations such that the organization providing the operating funds is directly involved in the day-to-day operations of the other organization (i.e., the "financial control" test in Notice 89-23). Examples of "churches" and "qualified" church-controlled organizations are the Chancery Office, the Diocesan schools, the parishes, and the parish schools.

Section 414(c)(2)(B) establishes a different rule for "nonqualified" church-controlled organizations or "NQCCOs," which are those organizations within the Diocese (other than elementary or secondary schools) that offer goods, services, or facilities to the public and normally receive more than 25% of their revenue from government sources and/or providing such services. Examples of NQCCOs are the Diocesan health care facilities, housing corporations, and social services organizations that receive substantial revenue from patients, tenants, and/or government grants. Because NQCCOs receive at least 25% of their revenue from government sources and/or providing services to the public, they cannot be aggregated with churches or "qualified" church-controlled organizations under the financial control test. However, one NQCCO is aggregated with another NQCCO if at least 80% of the NQCCO's directors or trustees are representatives of, or are controlled or appointed by, the other NQCCO.

Application of the Aggregation Rules to the Diocese for ERC Purposes

As noted above, the IRS has not issued specific guidance interpreting the substantive requirements of the aggregation rules for purposes of the ERC; instead, the CARES Act relies on the previously developed standards in Section 414 of the Code. Under these standards, the Treasury Department, the IRS, and Congress have generally allowed churches and "qualified" church-controlled organizations discretion in determining how to apply the aggregation rules. For example, instead of applying the bright line governance test for determining common control of tax-exempt organizations, the

[9] T.D. 9340; 72 Fed. Reg. 41128, 41138 (July 26, 2007); Treas. Reg. 1.414(c)-5(e).

Treasury Regulations issued in 2007 permitted churches and qualified church-controlled organizations to continue using the "reasonable, good faith" standard under Notice 89-23 for determining the members of their controlled groups. NQCCOs are subject to the bright line 80% governance test for determining aggregation.

Diocesan Entities

The Diocese and the Diocesan entities that are part of the Corporation Sole would not be treated as a single employer under the financial control test first published in Notice 89-23 and later codified in Section 414(c)(2)(A) of the Code. Neither the Diocese (including the Chancery Office) nor any of the parishes, parish schools, or Diocesan schools provides at least 80% of the funding for the other entity or is involved in the day-to-day management of the activities of the other entity. Therefore, neither of the two parts of the financial control test is reflected in the relationship between the Diocese and the Diocesan entities or among any of the Diocesan entities.

Absent any requirement for the Diocese and the Diocesan entities to treat themselves as a single employer, it is reasonable to conclude that the Diocese can rely on the "reasonable, good faith" standard set forth in Notice 89-23 and incorporated in the 2007 Treasury Regulations in determining the members of its controlled group for the ERC. Furthermore, Notice 2021-20, Q/A 9, states that a "reasonable, good faith" standard applies to tribal governments and tribal entities. This standard is generally applicable when the IRS has not issued guidance interpreting a statutory provision. We believe that a "reasonable, good faith" interpretation of Section 2301(d) of the CARES Act and Section 414 of the Code includes treating each Diocesan entity with a separate tax identification number as a separate employer for ERC purposes because (i) these entities have separate employees; (ii) neither the Bishop nor the Diocese is regularly involved in the day-to-day operations of the Diocesan entities (and vice versa); (iii) none of the Diocesan entities provides at least 80% of the funding for the other entity; and (iv) no election has been made under Section 414(c) of the Code to treat any of these entities as a single employer for determining compliance with the nondiscrimination requirements under Section 403(b) of the Code.

Separately Incorporated Entities in the Diocese

While the governance control test in Section 414(c) and the Treasury Regulations does not apply to the Diocese, its parishes, its schools, or the Chancery Office, this test does apply to Diocesan NQCCOs. The entities in the Diocese that meet this definition, including Saint Vincent's Services, the social service agencies, and the nursing homes, are separately incorporated. By virtue of his office, the Bishop serves as the President or Chairman of each of these organizations and has authority to appoint the members of their respective boards of directors. However, by definition, an NQCCO receives at least 25% of its support from government sources and/or providing services to the public, and thus the Diocesan NQCCOs cannot be aggregated with the Diocese or its parishes or schools under the financial control test.

Under Section 414(c)(2)(A), two or more NQCCOs are aggregated with each other and treated as a single employer only if at least 80% of the directors or trustees of one NQCCO are representatives of or controlled by another NQCCO. Thus, while the Bishop is the President of the NQCCOs and has authority to appoint the members of their respective boards of directors, the Bishop is not an NQCCO and therefore, the Bishop's authority to appoint the members of the NQCCOs' respective boards of directors is not a basis for aggregating the NQCCOs. It is our understanding that in 2019, Assisi Housing Corporation, St. Dominic's Apartments, Inc., and Oscar Romero House, Inc. shared the same three directors. We further understand that none of the other separately incorporated organizations have the authority to appoint at least 80% of the members of the governing body of another separately incorporated organization and in 2019, 2020, and 2021, none of the other separately incorporated organizations had an 80% overlap in the composition of their governing bodies. Thus, these other separately incorporated organizations should be treated as separate employers for purposes of the ERC.

Conclusion

Based upon the analysis above, the Diocesan entities that are part of the Corporation Sole would not be treated as a single employer under the financial control test in Section 414(c)(2)(A) of the Code. Further, no election has been made under Section 414(c) to treat any of the Diocesan entities as a single employer for purposes of determining compliance with the employee benefit plan nondiscrimination rules. Thus, we believe that the Diocese and the entities that are part of the Corporation Sole should use a "reasonable, good faith" interpretation of Section 2301(d) of the CARES Act and Section 414 of the Code in determining whether the Diocese and any of the Diocesan entities are treated as a single employer for purposes of the ERC. We further believe that a "reasonable, good faith" interpretation of Section 2301(d) of the CARES Act and Section 414 of the Code includes treating each of the Diocesan entities with a tax identification number as a separate employer for purposes of the ERC.

Saint Vincent's Services, Inc., Catholic Social Services, Inc., and the nursing homes that are part of the Diocese of Fall River each meet the definition of a "nonqualified church-controlled organization" or NQCCO. These organizations are separately incorporated and not part of the Corporation Sole. We believe the governance control test in Section 414(c)(2)(B) applies to determine if these organizations are treated as a single employer for purposes of the ERC. Under the governance control test, two or more NQCCOs are aggregated and treated as a single employer only if at least 80% of the directors or trustees of one NQCCO are representatives of or controlled by another NQCCO. It is our understanding that in 2019, 2020, and 2021, Assisi Housing Corporation, St. Dominic's Apartments, Inc., and Oscar Romero House, Inc. shared the same three directors. We further understand that in 2019, 2020, and 2021, none of the other separately incorporated organizations that are part of the Diocese had at least an 80% overlap in the composition of their governing bodies. Thus, except for Assisi Housing Corporation, St. Dominic's Apartments, Inc., and Oscar Romero House, Inc., each of the separately incorporated organizations should be treated as a separate employer for ERC purposes.