

July 8, 2011

The Honorable Douglas Shulman
Commissioner
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, DC 20004

Dear Commissioner Shulman:

The American Bankers Association (ABA)¹ is writing to you to request your attention to a matter relating to credit unions. A “common bond” among credit union members is required in order to have the privilege of tax exemption. Some credit unions now openly flaunt this common bond requirement by allowing anyone to join simply by making a donation. This is an issue that should be of concern to the Internal Revenue Service (the Service), especially in this time of focus on the tax gap, and, thus, we suggest that the Service embark on a closer inspection of the tax-exempt status of these credit unions.

Earlier this year, the ABA wrote to the Service recommending an examination into the membership qualifications for Alliant Credit Union - a state-chartered credit union headquartered in Illinois – whose basis for meeting the “common bond” requirement for qualification as a credit union is by instituting a program that allows anyone in the United States – regardless of where they live – to become a member simply by making a charitable donation of at least \$10 to a specific foundation.

As the Service has recognized, it is the commonality of interests or close relationship among members (the “common bond” requirement) that makes it possible for credit unions to offer its members unsecured loans – the primary purpose for which credit unions were created. A recent ABA analysis found that 37 credit unions with more than \$1 billion in assets openly permit individuals to qualify for credit union membership by joining some related association (see the enclosed material). This allows credit unions gain members who would otherwise not qualify for membership due to a lack of the required “common bond” for membership.

For example, NuVision FCU has the following on its website:

"If you do not qualify based on the above criteria, no problem! You can become a member of the American Consumer Council (Council) as a path to NuVision membership.

¹The American Bankers Association represents banks of all sizes and charters and is the voice for the nation’s \$13 trillion banking industry and its two million employees. The majority of ABA’s members are banks with less than \$165 million in assets. ABA’s extensive resources enhance the success of the nation’s banks and strengthen America’s economy and communities.

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Thanks to a cooperative agreement between NuVision and the Council, members can join NuVision, as well as have access to materials that will aid in improving their financial planning efforts.

We can sign you up for membership in the Council, at no initial cost to you, at the same time you become a NuVision member."

NuVision further writes that, because of its "once a member, always a member" policy, one only needs to sign up initially in the Council and expiration of the Council membership would not affect continued membership in the credit union.

In some of the cases we reviewed, the association appears to be an extension of the credit union and may have been set up solely for the purpose of qualifying the individual for membership in the credit union. For instance, GTE Federal Credit Union (Tampa, FL) has created a CUSavers Club as a path to credit union membership.

The Internal Revenue Code is administered by the Service (26 U.S.C. § 7803), not by the National Credit Union Administration (NCUA), and not by state legislatures or state credit union regulators. Consequently, a state's determination that a particular institution is a "credit union" is not binding upon the Service nor is a decision by the NCUA to treat an institution as a state-chartered credit union for other purposes (such as, for example, share insurance. See 12 U.S.C. § 1781(c)). Tax exemption is not an automatic incident to a state credit union charter. Within limits, the Service has the capacity to arrive at findings of federal tax law independent of state legislatures, state regulators, and even the NCUA.

In fact, during the 1970s, the Service challenged the tax exemption for some state-chartered "credit unions." One such challenge was in the case of La Caisse Populaire Ste. Marie v. United States. In this case, St. Mary's Bank was operating under a state charter that did not specify any limits upon whom the Bank could serve. The Service contended that this omission made the institution more akin to a mutual savings bank than a credit union, and that a mutual savings bank would have been subject to federal taxation. The U.S. Court of Appeals for the First Circuit agreed with the Service's analysis of the necessity for a common bond, but ruled in favor of St. Mary's Bank and restored the institution's tax exempt status based on a finding that the bank actually had a "de facto" common bond. However, the court warned that the "gross misuse" of the credit union name is a potential cause of action.

Following the St. Mary's decision, the Service's Employee Plans and Exempt Organizations Division issued a general counsel memorandum which concluded that state chartered credit unions must have a common bond of occupation, association, or residence, and for a state to authorize a credit union to organize and operate without a common bond would be a "gross misuse of the name... ."

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We strongly urge the Service to examine the operations of these credit unions, which we believe would reveal a lack of foundation for their claims of qualifying for tax-exempt status. The use of other associations set up for the purpose of side-stepping the stringent requirements for qualifying as a credit union is a serious matter that should be addressed by the Service. These institutions should not continue to enjoy tax-exempt status while openly flaunting their noncompliance with the rules that qualify them for such tax-exempt status.

Please feel free to contact me at any time at fmordi@aba.com or 202.663.5317 to discuss these comments further or answer any questions you may have.

Sincerely,

A handwritten signature in black ink that reads "Fran Mordi". The signature is written in a cursive, slightly slanted style.

Francisca N. Mordi

cc: Ms. Marsha Ramirez
TE/GE Director
Exempt Organizations Examinations
Internal Revenue Service
1100 Commerce Street
Mail Stop: MC 4900 DAL
Dallas, Texas 75242

Credit Unions with at Least \$1 Billion in Assets Using Associations to Circumvent Field of Membership Limitations

| | City | State | Total Assets (\$000) | Name of Association | Geographic Limit |
|--|------------------|-------|----------------------|---|------------------|
| Pentagon Federal Credit Union | Alexandria | VA | 14894898 | National Military Family Association, Voices for America's Troops | No |
| Alliant | Chicago | IL | 7592420 | Orphan Foundation of America | No |
| Security Service Federal Credit Union | San Antonio | TX | 6167927 | 50 Plus Club, Consumer United Association | Yes |
| Suncoast Schools Federal Credit Union | Tampa | FL | 5015743 | SSFCU Retirement Association | No |
| Delta Community | Atlanta | GA | 3880849 | GettingAhead Association | No |
| Digital | Marlborough | MA | 3650782 | 8 organizations | No |
| Patelco | San Francisco | CA | 3571214 | Community Association for Engaging Youth | No |
| Kinecta | Manhattan Beach | CA | 3529914 | Consumers Cooperative Society of Santa Monica | No |
| Lockheed Federal Credit Union | Burbank | CA | 2923432 | American Consumer Council | No |
| Mountain America | W Jordan | UT | 2777514 | American Consumer Council | No |
| Addison Avenue | Palo Alto | CA | 2412920 | Financial Fitness Association | No |
| First Technology | Beaverton | OR | 2323792 | Financial Fitness Association | No |
| Tower Federal Credit Union | Annapolis | MD | 2240280 | National Cryptologic Museum Foundation and other associations | Yes |
| Lake Michigan | Grand Rapids | MI | 2164324 | Amnyotropic Lateral Sclerosis (ALS) Association of Michigan | No |
| State Employees Federal Credit Union | Albany | NY | 2118108 | National Fed of Blind and other organizations | ? |
| Northwest Federal Credit Union | Herridon | VA | 2051347 | Financial Awareness Network | No |
| Affinity | Basking Ridge | NJ | 2033751 | Friends of Whitemore and other clubs and associations | No |
| Michigan State University Federal Credit Union | E Lansing | MI | 1962910 | Michigan United Conservation Clubs | No |
| Bellico | Greenwood Vlg | CO | 1912999 | Consumers United Association | Yes |
| Grow Financial | Tampa | FL | 1714212 | Friends of Military Families, LLC | Yes |
| California Coast | San Diego | CA | 1615540 | American Consumer Council | No |
| Founders Federal Credit Union | Lancaster | SC | 1554278 | Friends of York County Library and other organizations | No |
| Chevron | Oakland | CA | 1543584 | Contra Costa County Historical Society and other organizations | No |
| Western Federal Credit Union | Manhattan Beach | CA | 1514287 | Surfrider Foundation or Friends of Hobbs | Yes |
| JSC Federal Credit Union | Houston | TX | 1471215 | Galveston Historical Foundation and other organizations | Yes |
| GTE Federal Credit Union | Tampa | FL | 1411921 | CUSavers | No |
| Ascend | Tulahoma | TN | 1391600 | 50 Plus Club | Yes |
| State Department Federal Credit Union | Alexandria | VA | 1320979 | American Consumer Council | No |
| Affinity Plus | St Paul | MN | 1303401 | Affinity Plus Foundation | No |
| Premier America Credit Union | Chatsworth | CA | 1300733 | Alliance for the Advancement of Arts & Education | No |
| University Federal Credit Union | Austin | TX | 1268447 | University of Texas Longhorn Foundation | No |
| United | St Joseph | MI | 1228405 | American Consumer Council | Yes |
| Stanford Federal Credit Union | Palo Alto | CA | 1213212 | Museum of American Heritage or Friends of Palo Alto Libraries | No |
| NuVision | Huntington Beach | CA | 1191931 | American Consumer Council | No |
| NASA | Upper Marlboro | MD | 1106288 | American Consumer Council | No |
| California | Glendale | CA | 1044938 | Parent Teacher Association, Contributor to Public TV | ? |
| Pen Air Federal Credit Union | Pensacola | FL | 1031284 | Friends of the Navy-Marine Corps Relief Society Member | No |