

October 10, 2011

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

Dear Commissioner Shulman:

The American Bankers Association (ABA)<sup>1</sup> is writing to you to request your attention regarding an issue involving a credit union's possible violation of the requirement for "common bond" with respect to its members. According to a recent Credit Union Journal posting, the United Federal Credit Union (St. Joseph, MI) is in the process of entering into a purchase and assumption agreement with Griffith Savings Bank (Griffith, IN). The fact that credit union, which is a tax-exempt entity, plans to purchase and assume the assets and liabilities of a taxable financial institution is a serious matter that deserves attention from the IRS, especially given the large federal deficits facing the United States. We urge the Internal Revenue Service (IRS) to closely scrutinize this transaction as we believe it would have a serious impact on the question of whether the credit union will become open to customers who do not fall within the "common bond" requirement for membership in the credit union.

According to Credit Union Journal, all the depositors of Griffith Savings Bank will become members of United Federal Credit Union by joining American Consumer Council (ACC). In effect, the credit union would circumvent the "common bond" requirement by having all the customers of the bank join an organization (ACC) – regardless of the fact that these customers have nothing else in common – and this would then allow them become members of the credit union. This process turns the "common bond" requirement on its head because it allows anyone, regardless of location to become a member of the credit union simply by joining the ACC. The ABA believes that allowing the depositors of Griffith Savings Bank to become members of United Federal Credit Union by joining an associational group represents a gross misuse of the "common bond" requirement, and therefore, strongly urge the IRS to give this matter very close scrutiny.

Earlier this year, ABA wrote the Service stating that "a *common bond* among credit union members is required in order to have the privilege of tax exemption." As we pointed out in that letter, some credit unions openly flaunt this "common bond" requirement by allowing anyone to become a member by joining an association.

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<sup>1</sup>The 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.

An essential feature of a credit union is that its members share a “common bond.” As the Service has recognized,<sup>2</sup> it is this commonality of interests or close relationship among members that makes it possible for credit unions to offer its members unsecured loans – the primary purpose for which credit unions were created.

The Internal Revenue Code is administered by the Service (26 U.S.C. § 7803), not by the National Credit Union Administration (NCUA). Consequently, a determination by NCUA that a particular institution is a “credit union” is not binding upon the Service.

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 credit union actually had a “de facto” common bond, as it served members of French-Canadian background in Manchester and the surrounding area. However, the court warned that the “gross misuse” of the term credit union is a potential cause of action.

United Federal Credit Union’s purchase and assumption of the assets and deposits of Griffith Savings Bank and permitting the depositors of Griffith to join United Federal Credit Union through an association represents a gross misuse of the common bond requirement. If the transaction goes forward and the customers of the bank are automatically converted to members of the credit union through the ACC membership, we strongly recommend that the credit union’s tax exemption should be examined to determine whether its qualifications for tax exemption continue to be met. In fact, if the transaction goes forward, we believe that there would be sufficient evidence for the IRS to revoke United Federal Credit Union’s tax-exempt status. This veiled attempt to expand its membership to include people who do not have a “common bond” is a gross misuse of the term “credit union” because it flaunts the rules.

Moreover, the IRS should be troubled that a tax-exempt credit union can acquire a taxable bank and assimilate its customers who do not have any “common bond” into its membership simply by allowing the depositors join an association. This transaction expands the not-for-profit sector and the credit union tax expenditure at the very time the Congress is trying to reduce the federal deficit and the growing federal debt of the United States. .

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

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<sup>2</sup> 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... .”

Sincerely,

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

Francisca N. Mordi

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