

United States Senate

COMMITTEE ON FINANCE

WASHINGTON, DC 20510-6200

April 24, 2018

The Honorable David Kautter
Acting Commissioner
Internal Revenue Service
1111 Constitution Avenue N.W.
Washington, D.C. 20224

Dear Acting Commissioner Kautter,

Earlier this year, I wrote to Chairman Mark McWatters of the National Credit Union Administration (NCUA) to request information on federal oversight of credit union activity. I appreciated his helpful response on March 28, which outlined NCUA's regulatory positions and approach to the growth and evolution of credit unions in recent decades. The letter also highlighted how the federal credit union sector has expanded and evolved in recent decades, with the largest growing more commercially active and across several fields of membership. Due to this continued evolution, I write today to suggest the Internal Revenue Service (IRS) increase federal credit union transparency by requiring that the largest of these organizations file information returns as Congress set forth in Section 6033 of the Internal Revenue Code (IRC).

As you know, federal credit unions were first established under the Federal Credit Union Act of 1934 for the purpose of promoting thrift among members with a common bond and providing them with a low-cost source of credit, especially to members who were unable to obtain bank credit. To fulfill this purpose, they are the only depository institutions specifically exempted from federal corporate income tax under IRC Section 501(c)(1) and will receive a tax exemption that is valued at approximately \$2.5 billion this year.¹ Congress provided this exemption for express purposes and has an obligation to maintain oversight of credit union activity to ensure that they continue to fulfill its intended vision.

NCUA does important work monitoring the safety and soundness of the National Credit Union Share Insurance Fund and the credit union system. However, the job of monitoring compliance with the IRC and judging whether current activities still fulfill the intent of federal credit union tax-exemption still falls to the IRS and Congress. In recent years NCUA has relaxed credit union field-of-membership rules, expanded commercial lending, and permitted the use of alternative capital in certain circumstances. While these are all well-intentioned decisions, they should give us occasion to pause and review the current state of America's largest federal credit unions.

¹ JCX-3-17, <https://www.jct.gov/publications.html?func=startdown&id=4971>

One important way the IRS ensures transparency and accountability by tax-exempt organizations is the filing of the Form 990 information return, as required by Section 6033 of the IRC.

Congress created mandatory exemptions from this requirement for churches, exclusively religious activities, and certain organizations with gross receipts not more than \$5,000. Congress also allows the Secretary to relieve other tax-exempt organizations from the filing requirement when such filing is not necessary to the efficient administration of tax law.

For decades, the IRS has exempted federal credit unions from the annual information return filing requirement, in part because they are supervised by the NCUA and also because they do not pay the Unrelated Business Income Tax (UBIT). But during that time there is no question that federal credit unions have grown in size and complexity, which should give us pause to reflect whether that exemption is still warranted.

The Form 990 provides greater transparency – to both the IRS and the public – for a tax-exempt organization's operations, including its balance sheets, functional expenses, and compensation. The requirement that tax-exempt organizations file an annual return, when properly administered by the IRS, both protects private information while also ensuring a degree of accountability that a tax-exempt organization is operating within the scope of its tax-exempt purpose. Other complex, commercially active tax-exempt organizations, such as tax-exempt hospitals and large universities, file the Form 990 information return. While these organizations, unlike federal credit unions, pay UBIT, expanding the requirement to these credit unions would lead to better insight into their activity and more information should Congress consider policy changes in the future. The Form 990 is not perfect, and modifications should be considered, but at the very least it provides a baseline of transparency.

Should the IRS consider this change – which is well within the authorities Congress has granted to IRS – it may be appropriate to expand the information return requirement only to the largest federal credit unions or those with expanded commercial activities or fields of membership. I look forward to working with IRS on this issue moving forward and thank you for your continued efforts to ensure the proper function of commercially-related tax-exempt organizations.

Sincerely,

A handwritten signature in blue ink, reading "Orrin Hatch", is written over a horizontal line.

Orrin G. Hatch
Chairman