World Council of Credit Unions, Inc.

April 30, 2012

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CC:PA:LPD:PR (REG–121647–10)
John Sweeney
Internal Revenue Service
1111 Constitution Avenue NW
Washington, DC

Re: REG–121647–10, Proposed Regulation to Implement the Foreign Account Tax Compliance Act (FATCA) ("Regulations Relating to Information Reporting by Foreign Financial Institutions and Withholding on Certain Payments to Foreign Financial Institutions and Other Foreign Entities")

Dear Mr. Sweeney:

The World Council of Credit Unions (World Council) appreciates the opportunity to comment on the Internal Revenue Service's (IRS) notice of proposed rulemaking to implement the Foreign Account Tax Compliance Act (FATCA). The World Council is the leading trade association and development organization for the international credit union movement. Worldwide, there are nearly 53,000 cooperatively owned not-for-profit credit unions in 100 countries, with more than US$1.2 trillion in savings and 188 million credit union members.

The proposed FATCA regulation would apply to non-U.S. credit unions as "foreign financial institutions" (FFIs) and to U.S. credit unions as "withholding agents." As proposed, FATCA would require most non-U.S. credit unions to register with the IRS as "local FFIs." Credit union systems around the globe are extremely concerned that FATCA will place unreasonable regulatory burdens on credit unions even when they meet the "local FFI" definition because many foreign credit unions are unaware of the IRS FATCA rulemaking and/or do not have the technical capacity to meet the requirements to comply even with the proposal's streamlined rules for "local FFIs."

We strongly urge the IRS to expand the proposed definition of "nonregistering local bank" to include localized non-U.S. credit unions so that small non-U.S. credit unions can comply with FATCA without being required to register with the IRS. Credit unions are in most cases small, localized financial institutions that, like banks, provide their members with access to retail banking services such as lending and deposit products. Unlike banks, however, only people within the credit union's "common bond" of association (such as people who live or work in a specific local area) can become credit union members. The policy reasons for allowing streamlined FATCA compliance for small, local non-U.S. banks therefore apply at least as strongly, if not more so, in the case of small non-U.S. credit unions, which are unlikely to have accounts held by "U.S. persons" who are not residents of the credit union's home country.

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We also urge the IRS to make other changes in the final rule to ease compliance burdens on credit unions worldwide and promote financial inclusion of underserved individuals.

Overview of the World Council's Comments

- We do not support the proposed definition of "nonparticipating local banks" because it does not apply to similarly small and localized credit unions. We strongly urge the IRS to revise

the definition of "nonparticipating local bank" so that small, localized non-U.S. credit unions which meet the other requirements of the proposed "nonparticipating local bank" definition can utilize the streamlined compliance procedures applicable to small, localized non-U.S. banks.

- We also urge the IRS to raise the maximum asset threshold for credit unions meeting the "nonregistering local bank" definition to US$ 1 billion from US$ 175 million.

- We strongly support the proposed definition of "U.S. account" to not include accounts under US$ 50,000 even when a "U.S. person" holds such an account.

- We ask the IRS to allow non-U.S. credit unions meeting the "nonregistering local bank" and "local FFI" definitions to offer U.S. dollar denominated financial products to their members on their websites.

- We urge the IRS to amend the proposed definition of "local FFI" in several other respects to reduce regulatory burdens on non-U.S. credit unions and prevent unintended consequences, such as by allowing credit unions with 95% or more of their accounts held by local residents to meet the "local FFI" definition and allowing national or provincial credit union associations to register with the IRS on behalf of their member credit unions that meet the "local FFI" definition and obtain a single FFI EIN number that could be used by all "local FFI" credit unions that are members of the association.

- We believe that the proposed rule should be modified to permit institutions to receive refunds of money withheld erroneously under FATCA even in the case of a "nonparticipating FFI."

- We also urge the IRS to exempt expressly international workers' remittances from FATCA coverage in order to promote financial inclusion for underserved immigrant populations and their families in developing countries, and support the Credit Union National Association's (CUNA) comment letter on the proposed FATCA rules with respect to FATCA's impact on U.S. credit unions.

World Council's Detailed Comments

"Nonregistering Local Bank" Should Be Expanded to Include Credit Unions

We oppose the proposed definition of "nonregistering local bank" because it would not include credit unions and similar cooperative credit organizations even though credit unions provide their members with retail lending, deposit, and other financial services in the same manner as banks. An institution that meets the "nonregistering local bank" definition would not be required to register with the IRS and instead would only be required to certify to financial institutions that act as "withholding agents" that it is FATCA compliant. We believe that this approach is also appropriate for small, localized non-U.S. credit unions.

We strongly urge the IRS to expand the definition of "nonregistering local banks" that are "deemed compliant" with FATCA to include credit unions and similar cooperative credit organizations. Many small non-U.S. credit unions that have do not have "U.S. accounts" will not have the technical capacity and/or awareness of U.S. law to comply with FATCA unless the IRS expands the definition of "nonregistering local bank" to include credit unions. Non-U.S. credit unions that are not FATCA compliant may risk being blacklisted by other FFIs as "nonparticipating FFIs" and/or face other problems such as having transfers to their members be subject to erroneous FATCA withholding (such as in the case of worker's remittances sent home from the U.S. by an immigrant worker to support his or her family).

Credit unions are not-for-profit, cooperative financial institutions that are democratically governed by their members. Like banks, credit unions primarily engage in retail lending and deposit taking activities but—unlike banks—credit unions face "common bond" restrictions that limit who can become a credit union member to a subset of local residents and/or workers (such as people who live or work in a specific local area), meaning that a credit union is less likely to have U.S. persons as customers than nonregistering local banks would. Non-U.S. credit unions therefore generally only have members who are local residents and/or locally employed because people who do not meet the credit union's common bond requirements are not be eligible to join the credit union or otherwise do business with it.

As proposed, Treasury Regulation § 1.1471–5(f)(2), would define the term "nonregistering local bank" to include only banks as defined under I.R.C. § 581—determined as if the FFI were incorporated in the United States—which engage primarily in the business of making loans and taking deposits from unrelated retail customers. Credit unions in the U.S. are defined pursuant to I.R.C. § 501(c)(14)(A) in the case of state-chartered credit unions and under I.R.C. § 501(c)(1) in the case of federal credit unions (which are federal instrumentalities), *see, e.g.*, Rev. Rul. 69-283 (1969), and are not subject to I.R.C. § 581.

I.R.C. § 501(c)(14)(A) exempts from federal taxation state-chartered "[c]redit unions without capital stock organized and operated for mutual purposes and without profit," but defers to the state's legal definition of "credit union" unless the state has "grossly misused" the term (such as if the state defined the term "credit union" to include joint-stock banks). *See, e.g.*, *La Caisse Populaire Sainte Marie v. United States*, 563 F.2d 505, 509 (1st Cir. 1977).

Section 1.30 of the World Council's *Model Law for Credit Unions*[1] defines the term "credit union" as follows:

> "1. A credit union is a financial cooperative that may accept savings deposits and provide credit and other financial services to members.
>
> 2. A credit union is owned and controlled by its members. Individuals and jurisdictional persons may become members of the credit union if they meet the criteria for membership.

[1] World Council of Credit Unions, *Model Law for Credit Unions* § 1.30 (2011), *available at* http://www.woccu.org/policyadvocacy/legreg.

All members are shareholders and have one vote in the democratic proceedings of the credit union.

3. The objects of a credit union shall be:

a. to accept savings deposits from members;

b. to provide a source of credit for members at a fair rate of interest; and

c. to provide any other financial service required by members."

We strongly urge the IRS to expand the definition of "nonregistering local bank" to include credit unions as defined under I.R.C. § 501(c)(14)(A) and the *Model Law for Credit Unions* and national or provincial law. The IRS should amend proposed Treas. Reg. § 1.1471–5(f)(2)(i) to read as follows (with similar changes made to the documentation requirements for "nonregistering local banks" set forth in proposed Treas. Reg. § 1.174-3(d)(6)(i)) by adding the language underlined below:

> "The FFI must operate and be licensed solely as a bank (within the meaning of section 581, determined as if the FFI were incorporated in the United States) or as a credit union (within the meaning of section 501(c)(14)(A), determined as if the FFI were incorporated in the United States) or similar cooperative credit organization in its country of incorporation or organization and engage primarily in the business of making loans and taking deposits from unrelated retail customers."

We urge the IRS to also include the term "similar cooperative credit organization" in addition to the term "credit union" because credit unions are not always called "credit unions."

For example, a credit union can be called a "savings and credit cooperative organization (SACCO)," a "caisse populaire" in French speaking countries, *see La Caisse Populaire Sainte Marie*, 563 F.2d at 506-10, an Islamic finance cooperative (such as in the case of credit unions in Afghanistan that are supported by the U.S. Agency for International Development's (USAID) Rural Finance and Cooperative Development (RUFCOD) program), a "caha" in Mexico, a "cooperativa de ahorro y crédito" (or sometimes as another type of "cooperativa," such as a "cooperativa multiactiva") in other Spanish speaking countries, a "Spółdzielcze Kasy Oszczędnościowo-Kredytowe" in Poland, and many other names that vary from country to country and from language to language.

The state law definition of "credit union" controls whether or not an institution qualifies as a "credit union" under I.R.C. § 501(c)(14)(A) subject to be U.S. Supreme Court's "gross misuse of name test" set forth in *United States v. Cambridge Loan and Bldg. Co.* 278 U.S. 55, 59-60 (1928) ("The statutes speak of 'domestic' associations, that is, associations sanctioned by the several States. They must be taken to accept, with the qualifications expressly stated, what the States are content to recognize, unless there is a gross misuse of the name."); *La Caisse Populaire Sainte Marie*, 563 F.2d at 509 ("Section 501(c)(14)(A) necessarily implies that state law controls the definition of the term credit union."), *Bellco Credit Union v. United States*, 2009 U.S. Dist. LEXIS 106087, at *2-*3; 104 A.F.T.R.2d (RIA) 7337 (D. Colo. 2009) ("In Colorado, credit unions are cooperative associations that exist for the two-fold purpose of promoting thrift among their members and providing them a source of fair and reasonable credit.").

We strongly urge the IRS to expand the definition of "nonregistering local bank" to include credit unions as defined by I.R.C. § 501(c)(14)(A) (as if the credit union were chartered by a U.S. state) as well as similar credit cooperative organizations, and defer to the national or provincial definition of "credit union" (or an equivalent term) and the *Model Law for Credit Unions* using the "gross misuse of name test."

This approach would be consistent with the agency's policy reasons to proposing the streamlined FATCA compliance procedures for "nonregristering local banks" as well as consistent with the existing law for determining whether an institution is a "credit union" as defined by I.R.C. § 501(c)(14)(A). Further, expanding the definition of "nonregistering local bank" to include similar credit unions would allow small, localized non-U.S. credit unions to be able to comply with FATCA when they otherwise would not have the technical capacity to do so. This would reduce regulatory burdens on those credit unions and thereby help them continue to assist credit union members in bettering their lives by building wealth through access to low-cost credit union financial services.

The Definition of "Nonregistering Local Bank" Should Be Revised to Include Non-U.S. Credit Unions Up to $1 Billion in Assets and Allow U.S. Dollars Denominated Products

We urge the IRS to increase the maximum asset threshold in the "nonregistering local bank" definition to US$ 1 billion in assets on the credit union's balance sheet from the proposed US$ 175 million maximum. We think that FATCA's regulatory burden for institutions that do not meet the "nonregistering local bank" definition will be significant—even in the case of "local FFIs"—and that credit unions with US$ 1 billion in assets will be better able to bear these regulatory burdens than smaller credit unions.

We also ask the IRS to remove the proposed prohibition on "nonregistering local banks" advertising U.S. dollar denominated deposits and other U.S. dollar denominated financial products on their websites. This requirement is overly broad, would make many non-U.S. credit unions ineligible for the "local FFI" definition even when their membership is composed primarily or exclusively of local residents—especially in dollarized economies like Ecuador and El Salvador and countries like Canada with strong trade and travel ties with the U.S.—and is unreasonable given the significant number of U.S. dollars in circulation outside the United States and its role as the primary international reserve currency.

Some countries, such as Ecuador and El Salvador, use the U.S. dollar as their local currency, meaning that Ecuadorian and Salvadoran credit unions' websites advertise U.S. dollar-denominated products to their members because that is the currency used locally in Ecuador and El Salvador. U.S. dollars are also widely circulated in many other countries because of the U.S. dollar's relatively high level of liquidity and low rate of inflation. Further, many credit unions in other countries that have significant trade and travel ties with the United States, such as Canada, offer as standard products accounts denominated in U.S. dollars to serve their members who shop or vacation in the United States.

Modifications to the "Local FFI" Definition

We believe that the definition of "local FFI" should be modified in several respects in order to reduce regulatory burdens on credit unions.

We do not support the proposal to require each local FFI to register with the IRS individually and obtain a unique FFI EIN number. This registration requirement will be unduly burdensome on small credit unions, especially because the proposed definition of "nonregistering local bank"—which is intended to limit FATCA's regulatory burdens on small financial institutions—would not apply to credit unions, as discussed above. Instead, we believe that national and provincial credit union trade associations should be able to register with IRS on behalf of their members that meet the "local FFI" definition and be able to obtain one "FFI EIN" number for all "local FFIs" in the national or provincial credit union system. Although the proposed "expanded affiliated groups" definition under Treasury Regulation § 1.174-5(i)(2) is written for joint-stock companies that are owned top-down in a traditional holding company structure—whereas credit union association are owned by their member credit unions from the bottom up—revising the "expanded affiliated groups" definition to apply to national and provincial credit union associations is one possible way to reduce FATCA's regulatory burdens on localized non-U.S. credit unions.

We also oppose the proposed requirement that "local FFIs" must have at least 98% of their accounts held by local residents and believe that 95% is a more appropriate local resident requirement for "local FFIs." The proposed 98% requirement is too high because some non-U.S. credit unions serve ethnic communities and these credit unions can have more than 2% of their members currently living in the ethnicity's country of origin (but have no or few U.S. persons as members). For example, more than 2% of the members of a Canadian credit union that serves a Polish community in Canada may be residents of Poland. We therefore think that having at least 95% of accounts held by local residents is a more appropriate threshold for the "local FFI" definition.

In addition, we oppose the proposed requirement for local FFIs to recertify their status as a "local FFI" to IRS every three years because this requirement would be overly burdensome and would not provide useful information since credit unions meeting the "local FFI" definition would in general remain "local FFIs." Rather, we believe that a local FFI should be required to inform the IRS if it ceases to be a local FFI, rather than being required to recertify its status to the IRS every three years.

We also ask the IRS to remove the proposed prohibition on "local FFIs" advertising U.S. dollar denominated deposits and other U.S. dollar denominated financial products on their websites. As discussed above in the context of the "nonregistering local bank" definition, countries such as Ecuador and El Salvador use the U.S. dollar as their local currency, U.S. dollars are also in significant local circulation in many other countries, and many credit unions in countries that have significant trade and travel ties with the United States—like Canada—offer as standard products accounts denominated in U.S. dollars to serve their members who shop or vacation in the United States. Like in the context of "nonregistering local banks," the prohibition on "local FFI" credit unions providing information to their members about U.S. dollar denominated financial products on their websites is overly broad, would make many non-U.S. credit unions ineligible for the "local FFI" definition even when their membership is composed primarily or exclusively of local residents, and is unreasonable given the significant number of U.S. dollars in circulation outside the United States and its role as the primary international reserve currency.

We strongly support allowing local FFIs to serve U.S. persons who are residents of that credit union's home country (i.e. local FFIs must certify that it "does not open or maintain accounts for any

specified U.S. person who is not a resident of the country"). We request clarification that a credit union member can be both a resident of the foreign credit union's home country and the U.S. simultaneously, since the agency used the term "resident" and not "domiciliary" in its definition of "U.S. person" in IRS Announcement 2010-16 and similar interpretations. Specifically, we request clarification that credit union can qualify for the local FFI exemption so long as at least the required percentage of its members—we recommend 95%, as discussed above—remain residents of the credit union's home country even if some are also part-time residents of the U.S. under the residency test set forth under Chapter 1 of IRS Publication 519 ("U.S. Tax Guide for Aliens") and similar IRS interpretations.

Definitions of "U.S. Account" and "Financial Account"

We strongly support the proposal to exempt accounts below US$ 50,000 from the "U.S. account" definition even if the account is held by a "U.S. person." We request clarification that the proposed definition of "depository account" includes credit union consumer and business accounts even when those accounts use different nomenclature from banks for equivalent products (such as "share certificate" instead of "certificate of deposit," "share draft account" instead of "checking account," and so forth).

We also support the proposed exclusion from the definition of "financial account" for retirement and pension accounts under proposed Treasury Regulation § 1.1471–5(b)(2)(i)(A).

However, we believe that the proposed definition of tax-favored "non-retirement savings accounts" that are excluded from the "financial account" definition under Treasury Regulation § 1.1471–5(b)(2)(i)(B) is too restrictive and should be expanded. These types of tightly-regulated accounts are similar to tax-advantaged accounts that exist under U.S. tax law—such as Health Savings Accounts (HSAs) and Coverdell Education Savings Accounts (ESAs) in the U.S.—and have a low potential, or no potential, for abuse by U.S. taxpayers.

Not all tax-favored non-retirement savings accounts offered by non-U.S. credit unions meet all four of the proposed requirements for "non-retirement savings accounts." These four proposed requirements are: "(*1*) Contributions to such account are limited by reference to earned income; (*2*) Annual contributions are limited to [U.S.]$50,000 or less under the law of the jurisdiction in which the account is maintained; (*3*) Limits or penalties apply on withdrawals made before specific criteria are met under the law of the jurisdiction in which the account is maintained; and (*4*) Limits or penalties apply by law of the jurisdiction in which the account is maintained to contributions exceeding" US$ 50,000 a year.

For example, not all government registered tax-advantaged accounts outside the U.S. limit "contributions to such accounts . . . by reference to earned income" as required by the proposed definition, yet these types of accounts nonetheless represent a low, or no, risk for evasion of U.S. taxes because of they are tightly regulated and must be registered with foreign governments.

We therefore urge the IRS to revise the definition for "non-retirement savings accounts" in the final FATCA regulation to include "an account that is tax-favored with regard to the jurisdiction in which the account is maintained, subject to government regulation as a savings vehicle for purposes other

than for retirement" without including the four additional proposed criteria excerpted above, such as limiting contributions by reference to earned income. We also request clarification that Registered Education Savings Plans (RESPs), Tax-Free Savings Accounts (TFSAs), and Registered Disability Savings Plans (RDSPs) offered by Canadian credit unions are excluded from the definition of "financial account" pursuant to Treasury Regulation § 1.1471–5(b)(2)(i).

Remittances Exemption for Financial Inclusion

We request an express exemption for workers' remittances (i.e. generally low-value electronic money transfers sent by immigrant workers home to support their families) that are sent using the World Council's IR*net*[2] and similar systems like Vigo and Western Union, in order to promote financial inclusion. The average value of an international worker's remittance is less than US$ 500 (although many transfers are above US$ 500) and most immigrant workers who send remittances are low- or moderate-income individuals who are not attempting to circumvent U.S. tax reporting requirements when they send money home to support their families.

We believe that an express exemption from FATCA for workers' remittances is appropriate to help promote financial inclusion because workers' remittances are generally funded by immigrant workers' wages (and not the types of investment income the proposed rule focuses on in the context of FATCA withholding) and also because similar requirements to FATCA—such as the Financial Action Task Force's international anti-money laundering standards—allow less burdensome reporting requirements for low-value workers remittances in order to promote financial inclusion.[3]

Refunds

We strongly oppose the requirement under proposed Treas. Reg. § 1.1474–5(a) that "nonparticipating FFIs" would be denied refunds of moneys withheld under FATCA even if a withholding agent withholds those funds by mistake. Transfers made to non-U.S. credit unions may be subject to erroneous withholding because some withholding agents may not be familiar with credit unions and because withholding agents will be penalized if they fail to withhold funds when FATCA requires withholding.

While we recognize that prohibiting refunds for "nonparticipating FFIs" is designed to encourage FFIs to comply with FATCA, we are concerned that many withholding agents may err on the side of caution and withhold funds under FATCA when a transfer is being made to a non-U.S. credit union even when withholding is not technically required. We are also concerned that many non-U.S. credit unions may be classified as "nonparticipating FFIs" even if they do not have U.S. accounts and are

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[2] For more information about IR*net* and the importance of worker's remittances in promoting international development, see http://www.woccu.org/financialinclusion/remittances.

[3] *See, e.g.*, Financial Action Task Force, *International Standards on Combatting Money Laundering and the Financing of Terrorism and Proliferation: The FATF Recommendations*, Interpretive Note to Recommendation 10 (Customer Due Diligence) ¶¶ 17, 21 (Feb. 2012), *available at* http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF%20Recommendations%20approved%20February%202012%20reprint%20March%202012.pdf; Financial Action Task Force, *FATF Guidance: Anti-money laundering and terrorist financing measures and Financial Inclusion* (June 2011), *available at* http://www.fatf-gafi.org/media/fatf/content/images/AML%20CFT%20measures%20and%20financial%20inclusion.pdf.

localized because the proposed "nonregistering local bank" definition does not apply to credit unions. The agency should therefore amend proposed Treas. Reg. § 1.1474–5(a) so that any credit union or other person who has had funds withheld under FATCA erroneously is entitled a refund if they do not owe federal income tax.

Thank you for the opportunity to comment on the IRS's proposed regulation to implement FATCA. If you have questions about our comments, please feel free to contact me at medwards@woccu.org or +1-202-508-6755.

Sincerely,

Michael S. Edwards
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Advocacy and Government Affairs