

TABLE 11.—*At how much less yield expressed in basis points would you be willing to buy tax exempts as compared to your average pretax return on taxable loans and investments?*

BANK'S ASSETS			
\$100,000,000 and over	\$10,000,000 to \$99,000,000	Under \$10,000,000	Total
211	224	207	213

RATINGS					
[Municipals of respondents' community]					
Aaa	Aa	A	Baa	Ba and lower	Total
210	206	220	212	Too few cases	213

5. EFFECTS OF CHANGES IN TAX-EXEMPT STATUS

Just over 300 banks that took part in the survey thought that the average yield of their community's municipals would go up between 200 and 225 basis points if tax exemption were removed, a differential which is about 1 percentage point higher than the actual difference between municipal and corporate bond yields.

If tax exemption were removed and replaced by a Federal guarantee the average yield of municipals would go up, according to respondents, by about 1.50 percentage points, 50 basis points less than if no Federal guarantee were involved and about 25 basis points more than most U.S. Government agency obligations. In the event that a Federal guarantee were added to the tax-exemption feature the yield would be expected to decline by about 25 basis points from the current yield, according to the ABA survey.

A most interesting situation presents itself when the size of banks is taken into consideration in the analysis of the yield differentials in the respondent's community. The spread between the current yield and the yield if tax exemption were removed is reported to be as high as 2.24 percentage points for banks with \$100 million assets, 2.16 percentage points for banks with \$10-\$99 million assets, and 1.79 percentage points for under \$10 million asset banks. It is apparent that the tax-exemption feature is thought to be worth more to the larger banks than those in the smaller asset group. This is what might be expected since the normal tax rates of 22 percent is levied on taxable income of \$25,000 or less while the surtax rate of 26 percent (or a combined rate of 48 percent) is imposed on taxable income over \$25,000. Tax exemption therefore becomes more valuable when a bank nears the \$25,000 taxable income level. Being more likely to exceed that level, and being more sophisticated in subjects of taxation, banks with assets of \$10 million and over are more sensitive to the tax-exemption feature of municipals and attach a higher premium to it.

Similar differences between large and small banks were reported in the spreads between current yield and the yield that would result if tax exemption were removed and replaced by a Federal guarantee. In the event that Federal guarantee were added to the tax-exemption feature, the current yield would drop by 28 basis points, according to banks in the \$100 million and over asset group, 18 basis points for banks with assets of \$10 to \$99 million, and 9 basis points for the small banks. The