

3. *Effect of provisions on U.S. balance of payments and monetary policy*

One direction which these domestic dollar deposits may go because of these two provisions in the proposed Act is into investments abroad in other currencies. This would involve the sale of dollars in foreign exchange markets with the bulk of them ending up in the dollar holdings of those central banks that are gaining reserves. In this manner they become a potential claim against the United States gold reserve.

Another direction which the domestic dollar deposits may go is the Eurodollar pool. This would remove these dollars effectively from the control and reporting procedures of the United States and their employment would, thereafter, not necessarily be in accord with U.S. monetary policy. Also some of the funds in the Eurodollar pool are used in a manner involving temporary conversion into foreign currencies. This could create a claim against the U.S. gold reserve as in the case of foreign currency investments that I mentioned before.

4. *Conclusion*

We feel that these two provisions of the Bill are not in the best interests of the United States. The delay in the income tax provisions only slightly mitigates its adverse effect. Capital in this world is notoriously timid; it very seldom goes where it is not wanted. With the warning of future action advertised to the world very little new money will enter and we think a lot will leave well before the end of December, 1971. Both of the taxes proposed are new in concept, not in accordance with the Fowler Committee Report, and would, we think, have a detrimental effect on the United States balance of payments.

II. AMENDMENT NO. 717 TO H.R. 13103—LOANS BY FOREIGN BRANCHES OF COMMERCIAL BANKS REPAYABLE IN DOLLARS

The New York Clearing House Association supports the Dirksen Amendment, amendment No. 717 to H.R. 13103, which would allow the President to exempt dollar loans made by foreign branches of United States banks from the interest equalization tax. In the present situation where United States business abroad in cooperation with the Department of Commerce is exploring every avenue to finance expansion without a drain on the United States balance of payments it seems obvious that this source of foreign financing should not be severely handicapped by a 1% tax penalty. The Voluntary Restraint Program as applied to banks by the Federal Reserve as well as the reports made weekly and monthly by foreign branches of United States banks to the Federal Reserve ensure that this exemption will not be abused. Extending and expanding the principle of flexibility originated in the Gore Amendment to the IET which allows the Executive to move quickly in this fluid area, seems appropriate. We, therefore, feel that this amendment should be adopted as part of H.R. 13103. A detailed memorandum on its purposes is attached.

MEMORANDUM

EXEMPTION FROM INTEREST EQUALIZATION TAX FOR DOLLAR TERM LOANS FROM FOREIGN BRANCHES OF U.S. BANKS

We feel it is in the best interests of the United States to exempt from the Interest Equalization Tax U.S. dollar loans made by the foreign branches of U.S. banks regardless of maturities involved. We believe that this exemption should be attained because it would be of considerable net benefit to the U.S. balance of payments. The present application of this tax restricts the activities of American bank branches in a business that is desirable from a balance of payments point of view and it shifts this business to their foreign competitors. It limits the ability of the American branches to provide a type of financing that the Department of Commerce recommends the U.S. corporations as being in the interest of its balance of payments program.

These dollars are, of course, those deposited in the foreign branches of U.S. banks by foreign owners. In the past some authorities have worried that exempting foreign branch dollar loans from the IET would mean that the head offices of American banks would channel some of their domestic funds to their foreign branches to make these loans. This channel is now blocked by the Federal Reserve Voluntary Restraint Program and the weekly reports to the Treasury made on form 3953.

On the positive side, we feel that the foreign branches of U.S. banks are one of the primary sources looked to by U.S. corporations to finance their operations and