

maintain these relationships, but I fear that, if the Senate supports the House action, our success in this effort is not assured, to say the least. I should also note, in this connection, that our analysis of our own deposit composition offers little or no basis for a belief that tax treaties or foreign tax credits abroad will substantially ease the impact.

I cannot forecast precisely the time and the volume of deposit withdrawals. But I do feel certain that significant withdrawals will occur. The situation presented would be analogous to, say, an attempt by one of our states to extend its income tax to interest paid on nonresident bank deposits. The banks in that state would simply lose those deposits. But, of course, the impact of this tax is worse since the consequences are international and not solely internal. The adoption of these provisions would have most unfortunate and unnecessary repercussions on our international gold position, on the position of the United States as a world financial center, and even on our internal economy.

*The Interest Equalization Tax Act should be amended by H.R. 13103 to authorize the President to exempt dollar loans made at foreign branches of U.S. banks*

I would like now to turn to an important Interest Equalization Tax matter, which I believe should appropriately be changed by an amendment to H.R. 13103.

Under the terms of an Executive Order issued on February 10, 1965, the Interest Equalization Tax was extended not only to certain foreign loans made by banks in the U.S., but also to loans in U.S. dollars with maturities of one year or more made by branches of U.S. commercial banks abroad to foreign obligors. The extension of the Interest Equalization Tax to these foreign branch loans not only impairs the competitive position of those branches, but at present demonstrably works at cross purposes to the President's over-all balance-of-payments program. I understand that the Treasury Department has taken the position that this matter can only be resolved by legislation, since under the terms of the Interest Equalization Tax Act the terms of the existing Executive Order cannot be appropriately relaxed.

Our foreign branches, in competition with foreign banks, have access to foreign funds in the form of Euro-dollars. The acquisition of these deposits *already in foreign hands* does not affect our balance of payments. The trouble is these potential deposits cannot at present be utilized by our branches to their best advantage—or to the best advantage of the United States.

American-owned business enterprises abroad are understandably unwilling to incur the additional cost of reimbursing our branches for the Interest Equalization Tax on dollar loans maturing in one year or more. As a result, our branches are in effect prevented from making such loans to these firms, which in the normal course of events would be the prime customers of these branches. Naturally, a bank can accept deposits and pay competitive interest rates thereon only if the funds so deposited can be loaned to customers at a proper rate of return. Consequently, the effect of the Interest Equalization Tax on foreign branch loans is to cause our foreign branches to refuse to accept certain dollar deposits from foreigners which, in the absence of tax, could be used to make term loans to the subsidiaries of U.S. businesses. My own experience is that many millions of U.S. dollar deposits from foreign sources for maturities ranging to a year or more have had to be turned down—despite the needs of U.S.-owned firms for foreign money—because of the inability to use these medium-term deposits to make loans for which there is a heavy and unfulfilled demand.

The existing exemption from Interest Equalization Tax for foreign branch loans made in foreign currency is not of practical significance since our branches abroad normally can attract only limited amounts of foreign currency deposits. Moreover, because of the impossibility of covering the foreign exchange risk over a series of years, it is not feasible for our foreign branches to take U.S. dollar deposits from foreigners and to convert such dollars to foreign currency for the purpose of making loans, even if the potential borrower itself is willing to borrow in a foreign currency.

As a result, U.S. subsidiaries, urged by the Government to finance their foreign operations to the maximum extent feasible from foreign sources of funds, have been forced to turn elsewhere. As you know, European capital markets are poorly developed and very congested, and indigenous foreign banks are already unable to meet fully the needs of their own domestic customers. The consequence is growing doubts over the ability of U.S. firms to complete their foreign borrowing programs.

Branches of American banks could make a significant contribution toward breaking this impasse if they are freed from the Interest Equalization Tax.