

It is our understanding that many leading foreign countries, including England, Germany, the Netherlands, and Sweden also do not impose a withholding tax on interest paid on deposits of nonresident aliens, so that our domestic banks would be placed at a disadvantage with respect to competition on this point from these important financing countries.

May I take a little time to point out the experience of Germany, which, when it was concerned over an excessive inflow of capital, took a step that was somewhat analogous to placing a tax on the interest on money deposited in banks. The German Government proposed and later enacted a tax on bond coupons paid to foreigners. This experience is described in the monthly bulletin of the German Central Bank for June 1965.

It may be summarized as follows:

The mere publication of the proposed German coupon tax in March 1964, in accordance with which interest paid on German bonds owned by foreigners was to be subject to a withholding tax, reduced foreign purchases of such bonds to about 50 percent of the amount that had been purchased by foreigners in each of the preceding months of that year. The parliamentary approval of the tax bill in January of 1965 and February of 1965 again resulted in an excess of sales over purchases. All in all, 550 million deutschemarks of foreign funds were withdrawn from Germany through the excess of sales over purchases of foreign-owned German bonds in the 14-month period beginning with the publication of the proposed tax, and ending in April 1965.

This spectacular figure must be compared with that of the net purchases by foreigners in the 14-month period immediately preceding the publication of the proposed tax act. In this period the purchases of German bonds by foreigners totaled 2.36 billion deutschemarks.

The German Central Bank article further points out that following the enactment of the coupon tax, there was a rise of more than 1 percent per annum in the interest rate level prevailing in Germany. The coupon tax is cited by the Central Bank as one of the contributing causes. Do we need this kind of upward pressure on interest rates in this country?

We point out that the proposed tax on interest affects a larger deposit total than the proposed estate tax, for it includes time deposits of banks, corporations and others, as well as individuals and apparently it was recognized that a potentially undesirable effect existed when the bill was drafted to defer the application of this withholding tax until January 1972.

However, in our opinion, substantiated by the German experience with the interest withholding tax cited above, the mere existence of the provisions in the law will itself result in withdrawal of deposits, as I believe was mentioned by Mr. Barth.

Our member banks have advised us that this process has already begun following passage of H.R. 13103 by the House. It is clear that the anticipation of action, even as distant as that presently proposed by 1972, can become an active force in the sensitive international money market.

On the matter of estate tax, the provisions would become immediately effective. Our member banks have advised us again that some deposits have already been withdrawn, and that steps have been taken