

what analogous to a tax on depositing money 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, and may be summarized as follows:

The mere publication of the proposed German Coupon Tax in March, 1964 (according to 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% of the amount that had been purchased by foreigners in each of the preceding months. The parliamentary approval of the tax bill on January 27, 1965, and February 12, 1965, again resulted in an excess of sales over purchases. All in all, 550 million DM of foreign funds were withdrawn from Germany through the excess of sales over purchases of foreign-owned German bonds in the fourteen-month period beginning with the publication of the proposed tax act and ending in April 1965. This spectacular figure must be compared with that of the net purchases by foreigners in the fourteen-month period immediately preceding the publication of the proposed tax act. In this period, the purchases of German bonds by foreigners totalled 2.36 billion DM.

The German Central Bank article further points out that, following the enactment of the Coupon Tax, there was a rise of more than 1% 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 added upward pressure on interest rates in this country?

PROPOSED INCOME AND WITHHOLDING TAX ON INTEREST ON FOREIGN-OWNED BANK DEPOSITS

The proposed tax on interest affects a larger deposit total than the proposed estate tax, for it includes time deposits of banks, corporations, trusts and other entities as well as those of individuals. Apparently the draftsmen of H.R. 13103 recognized a potential undesirable effect of this proposed tax which they sought to mitigate by deferring the application of this withholding tax until January 1, 1972. However, in our opinion, substantiated by the German experience with the bond interest withholding tax cited above, the mere existence of the provisions in the law will itself result in withdrawal of deposits. 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 for 1972, can become an active force in the sensitive international market.

PROPOSED ESTATE TAX ON FOREIGN-OWNED BANK DEPOSITS

Under the proposed law, the estate tax provisions would become immediately effective. Our member banks advise us that some individual deposits have already been withdrawn and that steps have been taken to move additional deposits. This experience seems to illustrate the fact that the proposed estate tax on bank deposits is contrary to the purpose of H.R. 13103 to encourage the investment of foreign funds in the United States. The facts are that it is too easy to move such funds to dollar accounts in foreign banks outside the control of the United States or to have the deposit made through a closely held foreign corporation and, therefore, the estate tax revenues from this source to our government would be minuscule (Treasury estimate \$300,000 per year) and not worth the risk of potential loss of dollar deposits.

EFFECT OF INTEREST AND ESTATE TAX PROVISIONS OF HR 13103 ON SMALLER BANKS

The tax changes affecting bank deposits of foreigners as proposed in HR 13103 could be particularly damaging to approximately 115 of our American members that have no branches abroad which might be able to acquire some of the deposits shifted from this country. The loss of these deposits would do serious damage to such banks. Large banks with foreign branches may be able to attract some of these departing deposits back into their branches, and the depositor would then be free of tax. Some of us without foreign branches may have to consider opening such branches in order to avoid extinction of an important source of our foreign business. Others simply cannot do that and the loss of these deposits would do serious damage to such banks. Business related to these deposits would presumably also be lost when the deposits were transferred to other banks or branches abroad or simply repatriated. Many of these banks have spearheaded in their communities the U.S. Government's export promotion