

to make it simple, we have assumed each is the sole such affiliate. Each of these companies had 1968 earnings of \$1 million.

If we start with Company X, whose situation most reflects the subsidiary of a mature company in the United States, a mature direct investor, we find the company had earnings, without any growth, averaging \$1 million in the base period, but was paying dividends of 50 percent of distributable income.

By definition, 50 percent also was being reinvested. It is assumed that the U.S. parent was not sending money abroad to that affiliate, and this again would be typical of ITT and other mature companies.

However, by virtue of the requirements for repatriation as they are written, in 1968 that company can only retain 35 percent of the amount it reinvested during the base period. That is, 35 percent of a half million dollars, which is \$175,000, as shown lower in the column.

By definition, if you earn \$1 million and you retain \$175,000 you have to distribute \$825,000, that is an 82½-percent dividend payout rate, and I submit that, with this rate, it would be difficult to sustain operations. Nobody in the United States, anxious to continue in business, would consider a distribution at that level, and certainly not if they were going to compete and grow.

Obviously, if the 1968 earnings, instead of being \$1 million, hopefully had grown to \$1.5 million, then that 82½-percent payout could only increase accordingly.

We have also shown Company Y, just like Company X, except that instead of paying out 50 percent and bringing it back to the United States year after year, it completely reinvested the earnings in expansion and new projects in Europe. Accordingly, Company Y had no dividends, so it retained earnings of \$1 million. As with Company X, nothing was sent abroad by way of a direct transfer of capital.

Applying the same formula to the base which is now \$1 million, 35 percent of \$1 million is \$350,000. Therefore, under the program, Company Y, assuming it is the only foreign affiliate of the direct investor, can pay out \$650,000, or 65 percent.

Now we come over to Company Z, which is really another case of Company Y, paying out nothing and retaining all. However, during the 1965-66 base period, we assume it received a yearly average of \$1 million in additional capital.

Applying the formula provided by the regulations, 35 percent of \$2 million is \$700,000. Now Company Z has earned, in 1968, the same \$1 million. Therefore, simple arithmetic tells you that if it can retain \$700,000, it has to pay out only \$300,000 of that \$1 million, or 30 percent.

Chairman PROXMIRE. At this point, will you clarify Company Z? What capital transfers could be and could not be? Would they be transfers from foreign accounts or from domestic?

Mr. HAMILTON. Well, the most classic example, I think, would be an increase in equity in the foreign affiliate by a U.S. investor or a long-term loan to that affiliate. We are not sure exactly what the regulations mean, but we think it could also mean increases in the current account between the parent and the subsidiary.

Chairman PROXMIRE. Does it make any difference whether it is from this country or from abroad?