FROM:
THE AMERICAN BANKERS ASSOCIATION
THE NEWS BUREAU
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ADDRESS OF M. MONROE KIMBREL

Vice President of The American Bankers Association, before the Annual Convention of the Montana Bankers Association, Many Glacier Hotel, Glacier National Park, Friday Morning, June 15, 1962. Mr. Kimbrel is chairman of the board of the First National Bank, Thomson, Georgia.

In the past few months I have had many opportunities to attend state bankers conventions and participate in their programs. Several times I have been requested to discuss legislation that affects banking.

Looking over my schedule a few months ago, I became concerned because there were a number of requests for talks on legislative matters, and it seemed I would have to repeat myself before each group.

My fears were not well founded. Although I have discussed the legislative situation several times, the only repetition has been in the titles. In fact, I am having as much trouble as many of you in keeping up with the changes on banking's legislative front. Every time that I prepare a talk I cross my fingers and hope that not too much of it will have to be changed.

There are about a dozen bills in Congress that have a direct bearing on the banking industry. However, the interest of most bankers is centered on one bill--the Revenue Act of 1962 known as H. R. 10650. To be more specific, the interest of most bankers is centered on two provisions of this bill--Section 8 which deals with taxation of savings and loan associations and mutual savings banks, and Section 19 which proposes a withholding tax on dividends and interest.

In view of this, I would like to spend these few minutes in taking a look at the current status and prospects of H. R. 10650.

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I don't think it is necessary for me to go into the complete background on Section 8. As you know, legislation was passed in 1951 which attempted, but ultimately failed, to impose a fair tax on the mutual financial institutions. Many subsequent efforts to correct the inequity were unsuccessful. As a result, commercial banks have been paying income taxes at the regular corporate rate while these competing institutions have been paying comparatively little or, in many cases, no income taxes at all.

In January of 1960, all groups representing commercial banking joined forces and decided upon a common objective--remove the tax shelter which these institutions enjoy in the form of a statutory bad debt provision.

After studying the matter, both the President and the Treasury were convinced of the merits of the arguments of commercial bankers, and they supported tax uniformity. We, of course, would be rather naive if we failed to understand another basic reason for the favorable support. The Administration needed additional revenues to offset some of the other provisions of the bill.

Last summer, Congressman Wilbur Mills, chairman of the House Ways and Means Committee, held hearings on the President's recommendations for new tax laws. All the associations representing the commercial bank's viewpoint coordinated testimony. Commercial banking made an excellent showing at the hearings. Mr. Mills put tax legislation at the top of his Committee's agenda when Congress reconvened in January.

The Ways and Means Committee did report a bill to the House, and it passed on March 29 by a vote of 219 to 196.

The Senate Finance Committee is now holding executive sessions on the bill.

It seems obvious that both the Senate Finance Committee and the savings and loan industry have accepted the idea that the mutual thrift institutions

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should pay more federal income taxes. The big question, of course, is how much. Spokesmen for the savings and loan associations admit increased taxation is inevitable, and they have even expressed a willingness to accept the formula which was approved by the House.

As you recall, that provision would give them three alternatives: (1) They could deduct 60 per cent of taxable income to add to their bad debt reserves; (2) they could add an amount sufficient to bring the balance in the reserve for losses on real property loans to 3 per cent of such loans outstanding at the close of a taxable year; or (3) they could deduct an amount necessary to bring reserves to a reasonable amount if they could demonstrate to the Treasury a need for a greater reserve than is permitted under the first two alternatives.

Undoubtedly, most savings and loan associations would select the first alternative and pay taxes on only 40 per cent of their income. This tax would amount to roughly 18 per cent of total income. That would be about half of the 35 per cent average tax paid by the commercial banks.

When the Senate Finance Committee held hearings on this provision in the bill, Secretary of the Treasury Dillon urged the Committee to amend the provision so mutuals would have the choice of paying taxes on 66 2/3 per cent of income or making additions to bad debt reserves at the rate of 3 per cent of net loan growth.

Joseph C. Welman, president, Bank of Kennett, Kennett, Missouri, and past president of the A.B.A., testified on behalf of the A.B.A. He said, "The Treasury proposal represents the irreducible minimum of net income which can be taxed and still approach the twin goals of adequate tax revenues and equity among financial institutions."

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The A.B.A. spokesman said that in 45 metropolitan areas not one penny of federal income tax was paid by savings and loan associations in 1960.

He also told the Committee that his bank with $13-million in assets paid $92,391 in federal income taxes for 1960. He pointed out that "This was 9 times greater than the total combined federal income tax paid in 1960 by all 126 member savings and loan associations in the state of Missouri. . . . As a matter of fact," he added, "if you include all the member savings and loan associations in the neighboring states of Arkansas, Iowa, Nebraska, and Tennessee, our small bank wouldstill have paid 2½ times more federal income tax than the total paid by all of these associations combined."

We feel confident that if any tax bill is passed by Congress this year it will contain a provision taxing savings and loan and mutual savings institutions. Just how much tax they will have to pay is hard to say at this time, but I can assure you that we have made every possible effort to inform the Congress of the facts which support our case for tax justice.

The withholding provision of H. R. 10650 cannot be discussed with as much certainty as the one on tax uniformity. The withholding provision provides that payers of dividends and interest be required to withhold federal income tax at the rate of 20 per cent.

As you know, the A.B.A. has long felt the government should take all reasonable steps to collect taxes due on interest and dividends. However, we have also maintained the position that withholding is neither practical nor workable. A system has not yet been devised that would not impose unreasonable hardship on many taxpayers. Nor has one been devised that would not be unduly burdensome and costly to banks and other dividend and interest payers.

The A.B.A. and many bankers from all parts of the country have cooperated with the Treasury Department in trying to work out some practical

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solution. We believe that a sound, reasoned approach is the only way to solve anything. However, to date we don't think any solution has been found.

We have taken the stand that the mass educational program being conducted by the Treasury with the cooperation of commercial banks and other dividend and interest payers, together with increased use of automatic data processing equipment on returns, will substantially reduce the reporting gap.

Joe Welman made a strong argument against withholding when he appeared before the Senate Finance Committee. He stressed the severe operating and cost problems which would arise in banks, particularly the small banks throughout the country, in dealing with both the government and their customers with respect to savings accounts, government and corporate bonds, trust accounts, and stock transfer and dividend paying operations.

In addition to discussing the main points in his testimony, he obtained permission from the chairman to submit a detailed memorandum outlining the A.B.A.'s objection to withholding.

Here are a few of the highlights from the supplemental testimony:

The case for withholding mightbe overstated. About 95 per cent of all dividend payments are reported on tax returns and over 65 per cent of interest is reported. About 93 per cent of interest included in information documents now being furnished to the Treasury is being reported on tax returns.

Evidence indicates that the informational program to educate taxpayers is bringing results and the program should be continued and given a fair trial before being discarded.

Automatic equipment will make it possible for the Internal Revenue Service to spot underreporting.

Efforts are being made to increase the number of criminal prosecutions in particularly flagrant violations. Widespread publicity of these cases can do much to reduce noncompliance.

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Additional progress could be made by placing a direct question about interest and dividend income in the individual tax forms.

Increased complications in our tax laws make self-assessment more difficult.

The government Savings Bond program will suffer.

Withholding will impair the functioning of the government bond market.

Withholding may run counter to our balance of payments efforts because investment in dollar claims will be relatively less attractive.

Mr. Welman also discussed the multitude of problems withholding would create for a trust department of a commercial bank.

If, however, after considering all these objections, the Senate Committee still insists on some form of withholding, the following suggestions were made: (1) make exemption certificates good until revoked by the taxpayer, instead of requiring renewal each year; (2) make exemption certificates available to charities, colleges, and other tax-exempt organizations; (3) make exemption certificates available to tax-exempt organizations and to nontaxable individuals regardless of whether they hold their investments directly or through a trust or other fiduciary relationship; (4) exclude from withholding interest on government and commercial marketable securities; and (5) delay the effective date of any withholding program until January 1, 1964, so banks will have at least a year to prepare for such a program.

Secretary Dillon agreed to accept the first and second of these recommendations in his testimony before the Senate Finance Committee May 10.

The Senate Finance Committee has completed hearings on the two provisions of the bill which we have been discussing. It has announced additional hearings on the provision dealing with taxation of overseas investments.

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What will happen in the next month or so is hard to tell. I do not have a crystal ball, and the proceedings could take several courses.

With the sharp break in stock market prices, the Administration has been looking for ways to bolster the economy. President Kennedy said he thinks the tax bill now under study by the Senate Finance Committee would be a step in the right direction. He said the investment incentive provision in the bill would help speed modernization of plant and equipment. He also said he would not withdraw his support for withholding.

This indicates the Administration will continue its efforts to push the bill through.

This, however, will not be easy. Senator Harry Byrd, Democrat of Virginia and chairman of the Senate Finance Committee, has declared his opposition to the withholding and the investment incentive provisions. But following President Kennedy's remarks about the importance of the bill at his press conference last week, Senator Byrd said he would not attempt to delay a Senate vote on the bill.

Senator Byrd has proposed that a combined account number, automatic data processing system be put into effect before resorting to the burdensome and costly withholding system. Many other senators have been receptive to this suggestion, which was proposed by the A.B.A. and other groups. Two Republican members of the Committee--Senator Williams of Delaware, who is the ranking minority member on the Committee, and Senator Bennett of Utah--have suggested several alternatives to the withholding proposal.

Some observers in Washington now believe that even if the withholding provision as now written were approved by the Senate Finance Committee, it would be defeated on the floor of the Senate.

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If a bill without withholding were passed by the Senate, such a bill would then go to a Senate-House conference; and chances are the House conferees would insist on including withholding. They might well argue that since they stood up to the pressure and passed a withholding provision, why shouldn't the Senate stand up to the same pressure.

Then, too, there is always the possibility that if a tax bill without a withholding provision were passed by Congress, it might be vetoed by President Kennedy.

To make predictions that much more difficult, Republican leaders, upon hearing about the broad tax reform that the Administration has in mind for next year, have suggested that the entire tax bill now before the Senate Committee be dropped and that Congress consider the whole tax question after it receives the President's new proposal.

I understand that the Senate Committee in the executive session will go through the bill section by section--as the House Ways and Means Committee did--and make tentative decisions as they go. These announcements may start coming out in about a week or so. I will be looking forward to reading about them just as I am sure you will be.

In closing I would like to make two points: First, I believe this bill has given bankers a sound education in the working of our legislative processes. We have been following this bill through every complication that a bill can encounter. The experience should be useful to us in dealing with legislative matters in the future.

As you know, the President has established three interagency committees to study legislative and administrative practices relating to (1) the operations of financial institutions, (2) the operations of federal credit programs, and (3) the operations of corporate pension funds and other private retirement and

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welfare programs. The reports are due this November. The A.B.A. has informed the chairman of each committee that it desires to present the Association's views at the appropriate time.

The Administration's legislative program in the financial field in the 88th Congress will undoubtedly rely heavily on the recommendations of these three committees. Our experiences in this tax bill should give us the background necessary to make our views known on other legislative matters in the future.

The second point that I want to make is this: I feel that we have made our case for tax uniformity and that savings and loan associations will be taxed on a more equitable basis. If the bill does not go through this year, I believe that we will see tax uniformity legislation next year.

I think this will be the inevitable result of a good job of collecting the facts and making a logical presentation of our arguments.

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