May 13, 1991

Honorable Thomas R. Carper, Chairman
Subcommittee on Economic Stabilization
Committee on Banking, Finance and Urban Affairs
131 Cannon House Office Bldg.
U.S. House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

In anticipation of your Subcommittee's May 15th hearing on the economic implications of interstate banking, the American Bankers Association (ABA) seeks to submit information on the state tax aspects. The American Bankers Association (ABA) is the national trade and professional association for America's commercial banks of all sizes and types. Assets of ABA member banks are about 95 percent of the industry total.

In April, the Conference of State Bank Supervisors (CSBS) testified before the House Subcommittee on Financial Institutions regarding the Treasury Department's financial services reform proposals. The CSBS is concerned that the repeal of the McFadden Act limitations on interstate branching by national banks will prohibit states from imposing nondiscriminatory franchise taxes on the income from Federal obligations of banks not headquartered in the state. As you know, there is a debate going on about the possibility that interstate branching proposals could cause the states to lose a portion of their taxing authority over branches of out-of-state banks. Some authorities have stated that there would be no such effect. Nevertheless, to insure that states can tax these branches, we would support language included in the legislative history or possibly in the statute to affirm the state taxing authority. We believe that if a bank is physically located in a state, it should pay its fair share of tax in that state.

We believe that the converse is also true. If a bank is not located in the state, either with a physical presence (bricks and mortar), regular employees located in the state, and a substantial amount of assets in the state, there should be no jurisdiction for state taxation of that bank. There is a Federal statute which establishes such a jurisdictional rule for state
taxation of retailers and manufacturers, but it does not cover financial institutions. Instead, several states have adopted a "market state" approach developed by the Multistate Tax Commission. Under this approach, an out-of-state financial institution is subject to tax based on such flimsy connections with the state as twenty credit card customers or a single overnight loan of federal funds. Thus, the lender will likely be subject to tax in both its home state and the customer's home state, resulting in double taxation.

Moreover, the increased compliance costs associated with these market state taxes will be passed on to the residents of the taxing jurisdiction in the form of higher interest rates or a reduction in lending which, based on our economic studies, will adversely affect the local economy. It is clear that one of the implications of banks doing business across state lines is the need to have a uniform rule for when a state may tax an out-of-state bank. Federal legislation is the most expedient method for determining when a state may and may not properly tax banks operating across state lines.

On behalf of the commercial banking industry, the ABA appreciates this opportunity to comment on the state taxation of banks that are headquartered out-of-state. We are available to work with the members of the Subcommittee and the staff on the issues raised in this letter.

Sincerely,

[Signature]

Henry C. Ruempler

cc: All members of Economic Stabilization Subcommittee