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### Florida Taxation of Edge Act Corporations and Foreign Bank Agencies

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# Florida Taxation of Edge Act Corporations and Foreign Bank Agencies

E.N. ROUSSAKIS\*

*The author examines the effects of Florida's documentary stamp, franchise and intangible personal property taxes upon international banking activity in Florida. Though he asserts that the state legislature fully intended to promote Florida as a center of international banking and commerce, the author contends that these taxes are actually an impediment to such development. He vigorously argues that the taxes should be revised in order to fulfill the legislature's objectives.*

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## I. INTRODUCTION

The rapid development of Miami into a specialized Latin American banking center calls for legislative responsiveness to a key aspect of Florida's foreign banking regulation—taxation.<sup>1</sup> Revision and simplification of the existing tax legislation would remove major impediments to the growth of international financial transactions in Florida. This action would establish and promote Florida as a center for international commerce and trade by allowing banks to operate at attractive profit margins.

By enacting House bill 1250 into law in June 1977,<sup>2</sup> the Florida Legislature encouraged international banking corporations to establish themselves in the "Gateway of the Americas," foreseeing the aid that the banks could give to the international business com-

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1. For a discussion of the effects of the International Banking Act of September 1978 on Florida's international banking legislation, see Roussakis, *Review of Key Provisions of Both State and Federal International Banking Laws for Florida*, 11 LAW. AM. 530 (1979).

2. 1977 Fla. Laws, ch. 77-157 (current version at FLA. STAT. § 659.67 (1979)).

munity of the state. Since 1977, this objective has been serviced through increased international banking activity, the vehicles of which have been local banks, Edge Act corporations of large out-of-state banks<sup>3</sup> and agency offices of foreign banks.<sup>4</sup> The latter two institutions have become the core of the international banking community of Florida and have significantly contributed to the economic growth of the state. Their continued activities can only increase the influence of Florida in national and world economics, providing the legislature acts to ease the tax burdens imposed upon them.

Edge Act corporations and foreign agencies are subject to a franchise tax,<sup>5</sup> an intangible property tax<sup>6</sup> and a documentary stamp tax.<sup>7</sup> The first is a corporate income tax and is therefore levied on taxable income. The two latter taxes are specialized taxes levied only upon financial assets. The discussion below is a review of the key provisions of each of these two latter taxes, and of their implications upon international finance transactions in Florida.

## II. INTANGIBLE PROPERTY AND DOCUMENTARY STAMP TAXES

The intangible personal property tax, enacted in 1971, is imposed on all intangible personal property held as of January 1 of each year.<sup>8</sup> Intangible personal property is defined as, "all personal property which is not in itself intrinsically valuable, but which derives its chief value from that which it represents."<sup>9</sup> Among the most common types of taxable property are bills, notes, loans, accounts receivable, bonds, stocks and other obligations or credits. The annual tax is imposed at the rate of \$1 per \$1,000 (0.10%) of the just valuation of taxable intangible assets held by the taxpayer as of January 1.<sup>10</sup>

The documentary stamp tax is levied on documents in general,

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3. Under § 25(a) of the Federal Reserve Act (the so-called Edge Act), the activities of an Edge Act corporation are restricted to servicing the international financial requirements of domestically-based clients and overseas customers. Thus, an Edge Act corporation may receive foreign deposits but may only receive domestic demand deposits if they are incidental to or for the purpose of carrying out transactions overseas. Federal Reserve Act, ch. 6, § 25(a), 41 Stat. 378 (1919) (current version at 12 U.S.C.A. § 615 (1979)).

4. Foreign agencies are offices of foreign banking corporations organized and licensed under the laws of Florida. On May 31, 1979, 10 foreign agencies were operating in Miami and three more had received state approval to operate.

5. FLA. STAT. § 220.63 (1979).

6. *Id.* § 199.112.

7. *Id.* § 201.01.

8. *Id.* § 199.103.

9. *Id.* § 199.023.

10. *Id.* § 199.032.

and, more specifically, on those instruments whose primary purpose is to secure the payment or repayment of money or the transfer of property. Taxable instruments include promissory notes, bonds and other certificates of indebtedness, original issues of stock, stock transfers, drafts or bills of exchange, deeds and other instruments relating to the purchase or transfer of real property. The taxed documents are generally subject to a rate of 15 cents per \$100 (0.15%), with a few exceptions. For example, instruments relating to the transfer of real property are taxed at a rate of 30 cents per \$100 (0.3%). The tax is levied at the time of the execution of the document and is paid by the purchase of stamps or by the use of meter machines.

Initially, the documentary stamp tax was applied regardless of whether the instrument was of domestic or foreign origin. In 1977, however, as part of the effort of the Florida Legislature to promote international banking activity in the state, the tax was amended to exempt instruments of foreign origin. Section 201.23(1)(a) excludes from such taxation "all promissory notes . . . and other written obligations to pay money . . . if the makers thereof or the obligors thereunder, at the time of the making or execution thereof, are individuals residing outside the United States or business organizations or other persons located outside the United States."<sup>11</sup> This language could have provided incentive for foreign bankers to continue their present efforts and expand their activities within the state.

Unfortunately, an important limitation on this exemption renders the section inapplicable to transactions involving obligors or beneficiaries of financing where a majority of their equity securities is owned by persons or organizations located within the United States.<sup>12</sup> This provision disqualifies many multinational corporations and foreign subsidiaries of United States corporations from realizing the benefits of the new section. By placing these entities outside the scope of the exemption, the limitation significantly diminishes the intended effect of the legislation to encourage international banking activity in Florida.

Moreover, certain statutory ambiguities in the tax enactment appear to hinder the attempts of the legislature to establish Florida as a worldwide commercial center. The effect of the laws upon the following areas is unclear: (1) third country trade financing transac-

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11. *Id.* § 201.23(1)(a).

12. *Id.* § 201.23(2)(c).

tions;<sup>13</sup> (2) United States discounting of letters of credit issued to foreign beneficiaries by Florida banks; (3) financing domestic transactions of foreign corporations doing business within the United States; and, (4) international transactions as defined by regulation K of the Board of Governors of the Federal Reserve System with respect to "goods in storage."<sup>14</sup>

Unfortunately, however, the effect of the documentary stamp and intangible property taxes upon domestic Edge Act corporations and foreign agencies is quite significant. The combined annual effect of these taxes is shown in Table 1. As the table indicates, the tax impact is especially large on seven-day credits, where it is equivalent to a 7.75% annual tax rate. The implicit annual tax rate on shorter term financing (e.g., overnight) is considerably higher. Such credits, however, are not actively financed by domestic Edge Act corporations and foreign agencies. The annual tax rate is lower on longer term credits because the documentary stamp tax is applied per individual transaction, and with longer term credits there are fewer transactions per year.

TABLE 1  
ANNUALIZED COST OF THE DOCUMENTARY STAMP AND  
INTANGIBLE TAXES PER EUROCREDIT MATURITY  
(In Percentage Points)

Eurocredit Maturity	Number of Transactions <sup>a</sup> (per annum)	Annualized Tax Rate		
		Documentary Stamp Tax	Intangible Tax	Total
7-day	51	7.65% <sup>b</sup>	.1% <sup>c</sup>	7.75%
30-day	12	1.8	.1	1.9
60-day	6	.9	.1	1.0
90-day	4	.6	.1	.7
180-day	2	.3	.1	.4
360-day	1	.15	.1	.25

<sup>a</sup>The number of transactions for a given maturity is the number of loans of that maturity required to keep a sum of money loaned out for a year. To keep the number of transactions in whole numbers a 360-day year is assumed.

13. Specifically, an arrangement whereby a third country handles the financing of an agreement between two other countries. Hypothetically, Brazil might contract to ship coffee to Hong Kong. A bank in a third country will arrange a loan to Brazil to pay for the coffee upon certification of shipment. The buyer will then pay back the loan upon receipt of the goods. The payment and rate of interest is provided for in the initial contract.

14. Corporations Engaged in Foreign Banking and Financing Under the Federal Reserve Act, 12 C.F.R. §§ 211.1-.112 (1979).

<sup>b</sup>With the rate of documentary stamp tax equivalent to 0.15%, a seven-day line of credit would entail an annualized tax effect of  $0.15\% \times 51 = 7.65\%$ . Similarly, for lines of credit of longer maturity, the annualized effect of this tax would depend on the corresponding number of such transactions per annum.

<sup>c</sup>As this tax applies on all intangible assets outstanding as of January 1 of each year, regardless of maturity, its annual rate has been kept constant throughout.

Edge Act and foreign lending agencies must satisfy customer demand for credit in order to remain competitive with other lenders. Refusal to extend short term credit to a customer could result in a loss to the bank of all of that customer's business. For this reason, these institutions cannot control the maturity-mix of their portfolios strictly. The maturity-mix of their portfolios, and therefore their tax exposure, will necessarily reflect the needs of individual borrowers.

### III. THE EURODOLLAR MARKET

A review of prevailing trends indicates that since the mid-1970's the Eurodollar market has become increasingly liquid. This result may be attributed to the slack economic growth of Western European countries and Japan and the consequent excess liquidity of their domestic financial systems. Financial institutions of both OPEC (Organization of Petroleum Exporting Countries) members and the United States have significantly supported this market also. Participation by United States banks, however, has occurred to a lesser extent than in the past, due to a rise in domestic credit demand.<sup>15</sup> A natural consequence of this state of affairs has been an increased competitiveness among lenders, a result which has depressed contractual spreads to very low levels.<sup>16</sup>

Figure 1 illustrates the spread between Eurodollar prime-rate lending and the Eurodollar certificate of deposit rate since January 1975. As may be seen in the figure, the spread in the Eurodollar market has been significantly narrower than the corresponding spread in the domestic market. Moreover, the Eurodollar spread, as a result of increasing competitive pressures, has declined steadily to a low of thirty-seven basis points, compared to a spread of 157 basis points in the domestic market.<sup>17</sup>

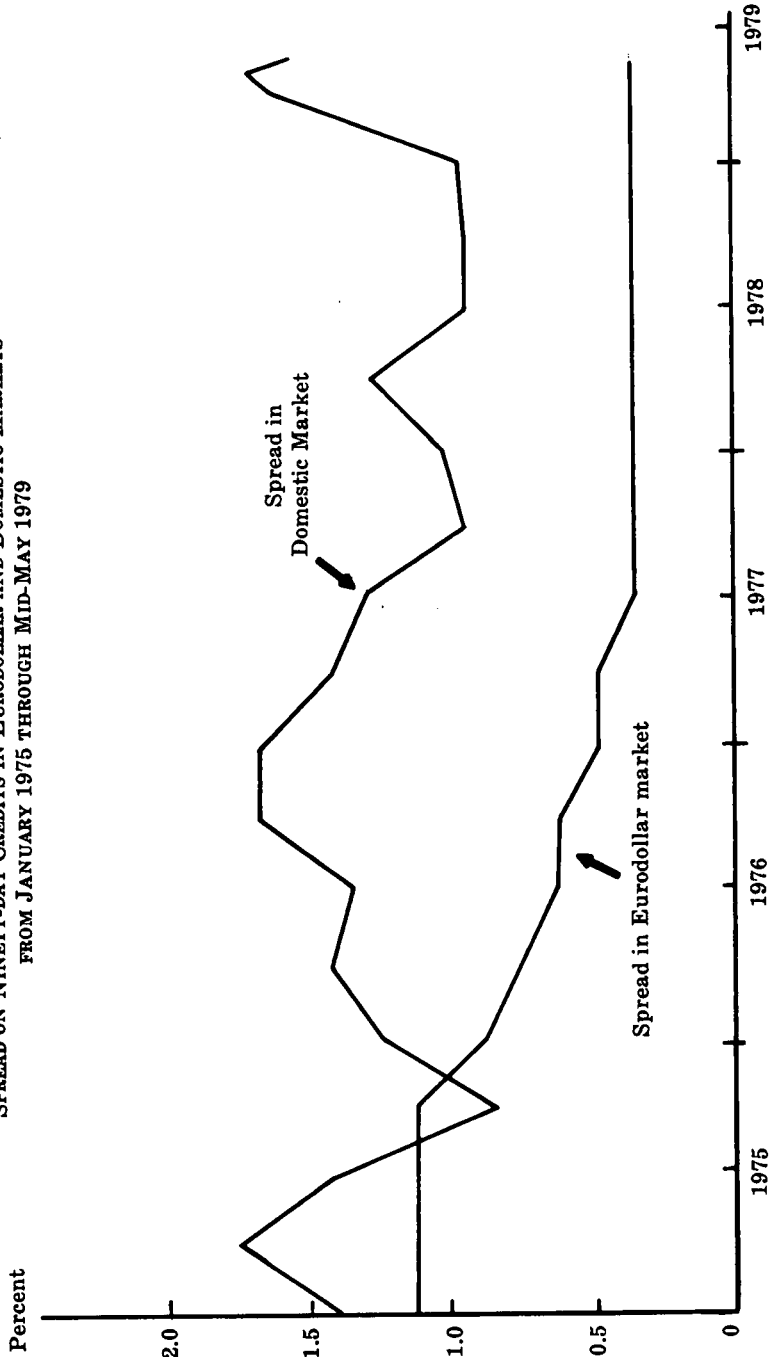
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15. van den Adel, *The Lenders Will Go On Competing In 1979*, *EUROMONEY*, March 1979, at 127.

16. As used here, a contractual spread is the difference between the interest rate a bank pays its depositors and the interest rate it charges its best customers.

17. A basis point is one-hundredth of 1 percent; thus the difference between a rate of 11.75% and a rate of 10.18% is 157 basis points.

FIGURE 1  
 SPREAD ON NINETY-DAY CREDITS IN EURODOLLAR AND DOMESTIC MARKETS\*  
 FROM JANUARY 1975 THROUGH MID-MAY 1979



\*Eurodollar prime rate minus Eurodollar CD rate for ninety-day credits; U.S. prime rate minus U.S. CD rate similar credits.

Sources: BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, ANNUAL STATISTICAL DIGEST 1971-1975 121 (1976); FED. RES. BULL. (Financial and Business Statistics) at A26-27; WORLD FINANCIAL MKTS., Mar. 1978 at 4, 9 (published by Morgan Guaranty Trust Company of New York) and following updates.

More detailed data on the recent Eurodollar spread are shown in Table 2, which identifies the relative level of the prime and certificate of deposit rates for different Eurocredit maturities as of May 11, 1979. As seen in this table, the spread is constant for prime-rate Eurocredits of different short term maturities. This spread is associated with minimal lending costs because Eurobanks have no legal reserve requirements or deposit insurance fees.<sup>18</sup> Competition among lenders in the Eurodollar market is unlikely to ease in 1979. As a result, spreads are expected to remain low.<sup>19</sup> In light of a study published by the Organization for Economic Cooperation and Development (OECD) suggesting that the long term trend in spreads is downward,<sup>20</sup> this narrowing of spreads should not be viewed as a temporary phenomenon.

TABLE 2  
PRIME AND CERTIFICATE OF DEPOSIT RATES IN THE  
EURODOLLAR MARKET AND THE SPREAD ON  
SHORT TERM EUROCREDITS, MAY 11, 1979  
(In Percentage Points)

Eurocredit Maturity	Prime Rate	Certificate of Deposit Rate	Spread from Lending to Prime Borrowers*
7-day	10.62%	10.25%	.37%
30-day	10.81	10.44	.37
90-day	11.12	10.75	.37
180-day	11.49	11.12	.37
360-day	11.49	11.12	.37

\*This spread consists of 12 basis points representing the offer-bid rate increment in the London interbank market plus 25 basis points in lieu of compensating balance requirements.

Source: Telephone conversation with Eurocredit Department of Morgan Guaranty Trust Company of New York (May 11, 1979).

18. In an unregulated market the cost of making a loan is merely the interest paid to obtain the funds to lend plus administrative costs. Most domestic banks, however, also have to pay for deposit insurance, an expense which raises the cost of acquiring funds. In addition, domestic banks cannot lend out all the funds they acquire from depositors; the banks are typically required to keep reserves in the form of cash or noninterest-bearing accounts. As a result, domestic banks pay interest on a larger volume of funds than they lend out. This raises the cost of making loans and increases the spread between the rate banks charge borrowers and the rate banks pay depositors. Eurodollar deposits need not be insured nor are they subject to reserve requirements.

19. Given, however, that spreads are close to the minimum required to cover risks and costs, spreads may widen somewhat. See van den Adel, *supra* note 15, at 127.

20. Organization for Economic Cooperation and Development, *Interest Rates, 1960-1974* (Paris: OECD Financial Statistics, 1976).



Borrowers find the narrowing of Eurocredit spreads hard to resist. "The result: a swollen spate of new borrowings taken out to replace old."<sup>21</sup> Past loans are renegotiated on more favorable terms, and there is an "astonishing willingness by banks to replace their competitors' loans (and eventually, because this is a free market, their own) with new financings at fractional spreads and greatly stretched maturities."<sup>22</sup> Several less-than-prime borrowers have thus succeeded in obtaining loans at spreads that approach those charged to prime borrowers, and sometimes at longer maturities.<sup>23</sup>

Foreign borrowers are much more cost-orientated as a result of these opportunities now available in the Eurodollar market. While "[t]raditionally, a borrower would approach only its investment (or merchant) banker to arrange for a big loan; today a borrower will approach various banks and ask them to bid for its business."<sup>24</sup> The specific loan is eventually given to the bank (or syndicate) which offers such financing at the lowest cost.

As a consequence of this borrowers' market, international banks have had to accept lower profit margins.<sup>25</sup> Moreover, as competitive pressure continues to build and further reduces the spreads, the profit levels of these institutions should continue to decline to the lowest level capable of sustaining investment activity.<sup>26</sup>

These developments characterize the international setting in which Florida-based Edge Act corporations and foreign agencies operate. The performances of these entities in the highly competitive international financial markets have been subjected to an unfortunate yet effective constraint—Florida's documentary stamp tax and intangible property tax. The effect of these taxes is illustrated by Table 3.

As indicated by this table, domestic Edge Act corporations and foreign agencies sustain losses on loans maturing within one year. For example, for seven-day loans refinanced throughout the year, the annual spread is a constant .37%, while their taxes are 7.75%. This results in a loss of 7.38%. On loans of longer maturity (*i. e.*, 30-day, 90-day and 180-day), losses decline because of the lower turnover of these credits, and consequently, the less frequent imposition of the documentary stamp tax.<sup>27</sup> On Eurocredits of one-year matu-

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21. *The Drive to Refinance in the Euromarkets*, EUROMONEY, Oct. 1978, at 115.

22. *Id.*

23. van den Adel, *supra* note 15, at 124.

24. Saade, *Spreads May Swing Upwards, But the Long-Term Trend is Down*, EUROMONEY, Dec. 1978, at 73.

25. *Id.*

26. *Id.*

27. See Table 3 *supra*.

TABLE 3  
AFTER-TAX SPREAD OF SHORT TERM EUROCREDITS

Eurocredit Maturity	Number of \$1 Million Loans per Year	PERCENTAGES			DOLLARS*		
		Spread from Lending to Prime Borrowers <sup>a</sup>	Annualized Tax Rate <sup>b</sup>	After-Tax Spread	Spread from Lending to Prime Borrowers	Annualized Taxes	After-Tax Spread
7-day	51	.37%	7.75%	-7.38%	3,700	77,500	-73,800
30-day	12	.37	1.9	-1.53	3,700	19,000	-15,300
90-day	4	.37	.7	-0.33	3,700	7,000	- 3,300
180-day	2	.37	.4	-0.03	3,700	4,000	- 300
360-day	1	.37	.25	+0.12	3,700	2,500	+ 1,200

\*Assuming \$1 million loans, per type of maturity, on the books throughout the year.

<sup>a</sup>Per Table 2. Regardless of credit maturity, the annual spread will always be a constant rate.

<sup>b</sup>Per Table 1.

ity, taxes are paid only once, *i.e.*,  $(1 \times .15\%) + .10\%$  or  $.25\%$ . Thus, the after-tax spread on each loan is a small but positive  $.12\%$  ( $.37\% - .25\%$ ). Naturally, as the term of the Eurocredit extends further, the after-tax spread increases as the tax burden is reduced.

#### IV. FINANCING OPERATIONS OF EDGE ACT CORPORATIONS

The tax implications depicted above may be a little less severe for domestic Edge Act corporations than for domestic foreign agencies. While the operations of foreign agencies are restricted to international financial markets, Edge Act corporations have a limited access to United States financial markets in that federal regulations allow Edge Act corporations to accept domestic deposits also, provided they are derived from non-United States residents (aliens).<sup>28</sup> These funds may in turn be lent domestically to United States businesses as long as the individual transactions of the businesses involve international trade (*i.e.*, exporting and/or importing activity). This loophole enables Edge Act corporations to obtain funds in United States financial markets at the prevalent certificate of deposit rate and to lend such funds at the prime rate. The spread that Edge Act corporations realize from such activity thus reflects the spread prevailing in United States financial markets.

As United States banks have been pricing loans in the domestic market at a figure well above the certificate of deposit rate, spreads in the domestic market have been significantly higher than spreads in the Eurodollar Market. The interest rates on these loans generally reflect the competitive pressure of the domestic commercial paper market, which serves as the major alternate source of financing for well-known domestic corporations.<sup>29</sup> Moreover, this larger spread covers the banks' higher costs of maintaining loanable funds in the domestic market.<sup>30</sup> Figure 1 identified the recent United States spread as equivalent to 157 basis points.<sup>31</sup> The effect of Florida taxes upon Edge Act financing in the domestic market, based on this spread, is depicted in Table 4.

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28. 12 C.F.R. § 211.7(c)(2) (1978).

29. While corporate borrowers are generally willing to pay slightly higher interest rates for the convenience of a bank loan, the corporations may find it more economical to issue commercial paper should interest rates become too high.

30. These higher costs reflect, in part, reserve requirements and deposit insurance fees.

31. See note 17 *supra*.

TABLE 4  
AFTER-TAX SPREAD ON SHORT TERM DOMESTIC CREDITS, MAY 18, 1979

Credit Maturity	PERCENTAGES				DOLLARS*			
	Number of \$1 Million Loans per Year	Spread from Lending to Prime Borrowers <sup>a</sup>	Annualized Tax Rate <sup>b</sup>	After-Tax Spread	Spread from Lending to Prime Borrowers	Annualized Taxes	After-Tax Spread	
7-day	51	1.57%	7.75%	-6.18%	15,700	77,500	-61,800	
30-day	12	1.57	1.9	-0.33	15,700	19,000	- 3,300	
90-day	4	1.57	.7	+0.87	15,700	7,000	+ 8,700	
180-day	2	1.57	.4	+1.17	15,700	4,000	+11,700	
360-day	1	1.57	.25	+1.32	15,700	2,500	+13,200	

\*Assuming \$1 million loans, per type of maturity, on the books throughout the year.

<sup>a</sup>FED. RES. BULL., June 1979, at A26-27 (although the figures expressed in the FEDERAL RESERVE BULLETIN are weekly averages, the author obtained the certificate of deposit rate for May 18, 1979 (10.18%) directly from the Federal Reserve Board).

<sup>b</sup>From Table 1.

Note: The after-tax spread depicted above is larger when compensating balances are required. An offset to this spread, however, is the required reserve (see, e.g., note 19 *supra*) and the FDIC insurance premium.

As indicated in Table 4, the after-tax spread of domestic Edge Act corporations is negative on short term loans of less than ninety-day maturity (*i.e.*, seven- and thirty-day loans). By contrast, on longer maturity loans (*i.e.*, ninety-day loans and over), the after-tax spread is positive and increases as the maturities lengthen. Thus, unlike Euromarket financing, which generates a positive after-tax spread on loans of one-year maturity and over,<sup>32</sup> domestic financing generates such a spread on loans of ninety-day maturity and over. This difference in profitability between Euromarket and domestic financing is clearly attributable to the higher spread in the internal market.

Current reports, however, identify this domestic spread as not being reflective of the actual margin realized in the internal bank loan market. The real spread is actually much narrower because of lower-than-prime lending rates.

The much-publicized prime rate means nothing anymore, laments a banker from the nation's capital. Currently 11.75%, this is the interest rate large money-center banks post as applying to their best corporate customers, with less credit-worthy businesses scaled up from there.

The competition is such, this banker confides, that the base rate for the most ardently sought customers these days is often the federal funds rate plus  $\frac{1}{2}$  percentage point. Federal funds . . . [are traded] lately at an annual interest rate of around 10.25%.<sup>33</sup>

As a result of this, the lending rate for the best customers is lowered to 10.75%, which is one percentage point less than the prime rate.<sup>34</sup> The actual domestic spread is accordingly reduced by one percentage point to .57%.<sup>35</sup> This means that a positive after-tax spread in Table 4 can only be realized on loans of 180-day maturity and over.<sup>36</sup> Obviously, this narrows the spread differential between the Eurodollar and internal bank loan markets and reduces the benefits Edge Act corporations may derive from domestic operations.

The combined after-tax spread of Edge Act corporations, which is essentially a composite of their Euromarket and domestic operations, will thus normally lie between the low Euromarket spread and

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32. See Table 3 *supra*.

33. Janssen, *Main Worry of World Bankers Is Excess of Liquidity Weighing on Interest Rates*, Wall St. J., May 15, 1979, at 21, col. 3.

34. The prime rate reported for May 1979 was 11.75%. FED. RES. BULL. June 1979, at A26.

35. Or 57 basis points.

36. .57% — .40% = +.17%.

the higher domestic spread. Its precise level at any moment in time will reflect the activities of each individual Edge Act corporation as affected by such domestic variables as prevailing financial conditions in the internal market, business demand for international financing, and the current competitive climate.

Although Edge Act corporations can generate a more favorable after-tax spread than foreign agencies, this spread only represents the gross margin of the institutions. Out of this spread, these corporations must still meet their operating expenses as well as pay the franchise tax on net profits, and provide a profitable after-tax rate of return for their investors. In fact, at the current rate of inflation, "the spread is too small to contain anything like an adequate offset to the erosion of capital"<sup>37</sup> which these institutions have been sustaining, much less generate an attractive after-tax return.

Clearly, some cushioning against these adversities may be realized through the lengthening of loan maturities, which minimizes the overall effects of the state documentary stamp and intangible personal property taxes. A more meaningful alternative for Florida-based Edge Act corporations and foreign agencies, however, is the "booking" of their loans at their out-of-state offices which are subject to lower taxes. Two locations offer this alternative: the State of Illinois and offshore banking facilities. In the State of Illinois, foreign loans are only subject to a four percent yearend corporate income tax, while in the Bahamas and Cayman Islands such financing entails no tax cost whatsoever. Consequently, managers of domestic Edge Act corporations and foreign agencies are constantly confronted with the choice between staying internationally competitive, thus justifying the investment of the parent corporation, or compromising for a slower rate of asset growth by complying with Florida's tax provisions.

Unlike Edge Act corporations and foreign bank agencies, domestic commercial banks have no alternative in the "booking" of their international credits. As a result, all of their international financing transactions are subject to Florida's documentary stamp and intangible personal property taxes. It is ironic that domestic commercial banks, the backbone of Florida's financial structure, should be subject to such undue tax burdens which so adversely affect their international competitiveness.

Florida's documentary stamp and intangible taxes thus have inequitable effects upon domestic banking institutions engaged in

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37. H. Wallich, *International Banking—Five Years After Herstatt* (May 14, 1979) (address given at the Annual Convention of the Banker's Association for Foreign Trade).

international financing, by encouraging the growth of out-of-state assets of domestic Edge Act corporations and foreign agencies. The paradox is that the final impact of these taxes may be contradictory: that is, ultimately these taxes deprive the Florida economy of the growth momentum originally intended while benefitting the state(s) and offshore centers where international transactions are booked. An argument may and should be made that elimination of these taxes would enhance the growth potential of Florida as an international banking center.

One of the immediate effects of such a measure would be the transfer within the state of the loan portfolios currently managed out-of-state.<sup>38</sup> Such a shift would significantly increase the size of the portfolios of domestic Edge Act corporations and foreign agencies. Such an increase may even amount to as much as 100% of the domestic portfolios currently maintained by these institutions. Potentially, of course, the improved tax climate in Florida could generate additional assets by "booking" in-state loans for the out-of-state offices of Edge Act corporations and foreign agencies.<sup>39</sup>

Increases in the loan portfolios of domestic Edge Act corporations and foreign agencies will also augment employment within the institutions themselves and generate greater tax revenues through the state franchise tax on corporate profits. For example, by doubling the loans made by these institutions over a one-year period, current employment levels could expand about fifty percent. The increased size of the loan portfolios would necessarily call for loan administration clerks and officers (*i.e.*, assistant vice presidents) with salaries ranging from \$14,000-\$30,000 respectively.<sup>40</sup> This rise in employment will generate additional spending, which will permeate the state's economy and stimulate additional growth.

Increased foreign asset growth of domestic commercial banks, Edge Act corporations and foreign agencies will generate additional income which will clearly contribute to a larger taxable base. It is the belief of local international bankers that the ensuing increase in the volume of corporate tax revenues will offset state tax revenue

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38. The existence of these out-of-state loan portfolios is a sensitive area in the banking community. Florida bankers are reluctant to go on record concerning the potential implications resulting from the elimination of these state taxes.

39. Miami-based Edge Act corporations and foreign agencies are unwilling to disclose the amounts of their loan portfolios currently managed out-of-state. It is an unspoken assumption in the banking community that elimination of Florida's intangible property tax and documentary stamp tax would result in the shifting of out-of-state loans to domestically-held portfolios.

40. Interview with Nicholas Cross, Lloyds Bank International Ltd., in Miami, Florida (May 9, 1979).

losses resulting from the elimination of the documentary stamp and intangible property taxes.<sup>41</sup>

## V. CONCLUSION

This study traces the combined effects of state documentary stamp and intangible property taxes upon the international banking activity of Florida-based Edge Act corporations and foreign agencies. Whatever their original purpose may have been, continued imposition of these taxes undermines the competitive position of these two institutions in their respective markets, and thereby thwarts legislative efforts to promote international banking activity in Florida.

Review of prevailing trends in the Eurodollar market indicates that the spreads realized have been narrowing to unprecedented low levels. It is generally recognized that Eurodollar spreads can no longer be viewed as "an adequate contribution to covering risk and expenses."<sup>42</sup> While the margins are slightly better in the domestic market, to which only Edge Act corporations have partial access, the competitive position is still unfavorable due to the tax structure. What has kept Edge Act corporations and foreign agencies functioning, despite the low operating margins, has essentially been the longer term loans in their portfolios which are subjected to a lower tax rate and consequently achieve positive after-tax spreads. Further, loans to nonprime borrowers and compensating balances have also generated similar improved after-tax spreads. Most importantly, by booking loans in either tax-free offshore offices or out-of-state offices subject to lower tax rates, the possibility of asset growth within these institutions has been maintained.

This raises the question of whether continuation of the documentary stamp tax and intangible property tax is in the best interest of the state. As a source of state revenue these taxes are relatively unimportant because they are unrelated to income or profits, and further, because they force loan transactions to "move" out-of-state. Their continued existence depresses international banking activity, a result which in turn stunts state growth by creating lower employment levels, payrolls and tax revenues. The incompatibility of these taxes with state legislative efforts to promote Florida as a center of international commerce and trade is as evident as it is unfortunate.

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41. Meeting with representatives of Miami-based Edge Act corporations, at Bank of America International of Florida (Mar. 2, 1979).

42. H. Wallich, *supra* note 37.



If elimination of these taxes is deemed inappropriate, the legislature should at least attempt to minimize their adverse effects. This could be done by prescribing the annual imposition of the current documentary stamp tax rate. For instance, both the documentary stamp and intangible property tax rates could be simultaneously imposed on January 1 of each year. This would result in a combined effect from both the documentary stamp plus intangible property taxes of .25% (.15% + .10%). Thus, the after-tax spread on loans of different maturities would be the same—small but positive—margin as that depicted in Tables 3 and 4 for 360-day credits.

Such an alternative, however, only perpetuates the existing loophole whereby banks “book” loans out-of-state. If narrowing of the Eurodollar spread persists, elimination of these taxes will be required to repress this out-of-state “booking” activity. This response would be compatible with legislative efforts to encourage international financial transactions within the state. A major obstacle to the development of Miami as a specialized Latin American banking center will have been removed, and the ability of Florida to act as a center for international commerce and trade will be dramatically enhanced.