Financial Transaction Taxes

Financial Transaction Taxes (FTTs) exist in many countries and in many forms. In this paper, ASIFMA focuses on the Financial Transaction Tax debate and highlight the plethora of studies which have been conducted in various parts of the world. Whilst not all studies, nor all countries, are covered in this paper, as they are too numerous to list, ASIFMA notes the commonalities between studies written in Asia, Europe and the Americas.

There is a diverse amount of material covering the effects of FTTs, some using historical data to determine actual outcomes, some using historical data to map out theoretical impacts to planned taxes. Many have been commissioned by bodies with stellar reputation and renown. Whilst this paper does not purport to cover all research studies conducted on all FTTs, the prevailing literature almost universally reaches very similar conclusions

That the introduction of FTTs:

- **Generates significantly less revenue than forecast**
- **Reduces asset prices and pension fund values**
- **Reduces trading volume, liquidity and certainty in financial markets**
- **Increases volatility through higher uncertainty, wider bid-ask spreads, and lower volume**
- **Lowers the attractiveness of the market for foreign firms**
- **Increases costs to companies through higher funding costs**
- **Increases costs to the end investor**

ASIFMA (Asia Securities Industry & Financial Markets Association) is an independent, regional trade association comprising a diverse range of over 165+ leading financial institutions from both the buy and sell side, including banks, asset managers, professional services firms and market infrastructure service providers.

Our recommendation would be that any need to raise revenue would be better serviced by alternative mechanisms which would bring less disruption to the financial markets.

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Growing Asia's Markets

Financial Transaction Taxes

REVENUES GENERATED WERE SIGNIFICANTLY LESS THAN FORECAST

Several academic studies analyzing the impact of new FTTs recognized the implicit flaw in assuming elasticity of volume remained the same pre and post implementation. As a result, forecast revenue calculations incorrectly assumed higher than expected volume post implementation.

France

- Studies show that number of **shares traded decreased on average by 19%** within two months after implementation of FTT.[1]

Sweden

- When Sweden implemented an FTT, **60%** of the trading volume of the 11 most actively traded Swedish shares migrated to London to avoid the 2% tax on equity transactions.[2]

Italy

- Studies found a **significant decrease in liquidity** after the tax introduction date.[3]

China

- Comparing 6 months pre and post the increase of stamp in 1997 on SSE and SZSE, **trading volumes decreased 25 – 36%**.[4]

Taiwan

- **Tax revenues increased when the size of the tax decreased** due to the corresponding increase in trading volumes.[5]

An FTT will drive up the cost of trading by more than the amount of the tax.

- Center for Capital Markets Competitiveness[6]

STTs reduce security values and raise the cost of capital for issuers, particularly issuers of frequently traded securities. **STTs also reduce trading volume**….**Lower trading volume in turn reduces liquidity and slows price discovery.**

IMF Working Paper: Taxing Financial Transactions: Issues and Evidence[7]

ASSET PRICES, PENSION VALUES WILL DECREASE

UK – Studies found that **a reduction in stamp duty rate increased the price of shares**.[8]

Sweden - Studies found that the index declined **2.2 percent** on the day that the 1-percent transaction tax was announced, and it declined **0.8 percent** on the day that the 2-percent transaction tax was announced.[9]

Japan - **the reduction in the Japanese FTT had a statistically significant positive price impact** on the affected Japanese stocks.[10]

Europe (Theoretical) - Taking the net present value of all future FTTs yields a total capital loss of EUR 700 bn, corresponding to 2.3% of total security market capitalization or approx. 5% of total EU GDP. Looking at individual asset classes, **the reduction in value for equities will be 1.1% and 3% for bonds**.[11]

US (Theoretical) - The ending value of an investment of $10,000 in a small capitalization active equity fund **would be reduced by roughly 19%** with the proposed tax, after 20 years.[12]

Financial Transaction Taxes

Unclear Revenue Generation, Clear detrimental impact for the wider economy

Liquidity would be materially affected:

The Copenhagen report stated that, following the commission they expect **90% of all derivative trading to move abroad** if an FTT was implemented (20bp tax on bonds and equities, 2bps on derivatives).[13]

There would be a hit to end investor savings

Vanguard stated that, "The proposed US tax would require the everyday investor to **work roughly two-and-a-half years longer** before retiring in order to reach the same retirement savings goals achievable without the tax".[14]

Transaction Costs would increase:

Many studies are aligned that an FTT increases transaction costs. The Center of Capital Markets Competitiveness estimated that a proposed FTT of 50bps would lead to a **300%** increase in the cost of trading 100 shares.[15]

Total equity and bonds owned by households (either directly or indirectly, e.g. through a pension fund) are in the region of EUR 15-20 trillion. Simply transforming the decrease in asset prices to an average per adult EU citizen equates to an impact of approx. EUR 1,000-1,500 per person.

- Copenhagen Economics: Financial Transaction Tax Study

"While some see this as a tax on the securities industry itself, it is actually a tax on working families saving for retirement and college, pension funds that secure retirement for millions, as well as many individual investors, foundations and endowments."

Open Letter in Opposition to Any Form of the Stock Transfer Tax – Alternative & Direct Investment Securities Association, American Council of Life Insurers, American Retirement Association, American Securities Association, Business Council of New York State, Business Council of Westchester, Coalition to Prevent the Taxing of Retirement Savers, Council on State Taxation, Equity Markets Association, Financial Planning Association, Financial Services Institute, Foreign Exchange Professionals Association, Futures Industry Association – Principal Traders Group, Institute of International Bankers, Insured Retirement Institute, Investment Company Institute, Life Insurance Council of New York, Inc., Long Island Association, Managed Funds Association, Modern Markets Initiative, NASDAQ, New York Bankers Association, New York State Economic Development Council, New York Stock Exchange, Partnership for New York City, Securities Industry & Financial Markets Association, SPARK Institute

Cost of Financing would increase

The Oxera study found that **the long-term net impact of the FTT on public finances could actually be negative, making it an extremely inefficient tax**. For countries with relatively high levels of government debt, the loss of government revenues resulting from the impact of the tax on the economy and government funding costs is estimated to be greater than the expected revenues from the FTT. This means that the **FTT could ultimately result in further reductions in public spending** in those countries.[16]

Footnotes

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