CENTER FOR CAPITAL MARKETS COMPETITIVENESS

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March 22, 2021

The Honorable Maxine Waters
Chair
Committee on Financial Services
U.S. House of Representatives
Washington, DC 20515

The Honorable Patrick McHenry
Ranking Member
Committee on Financial Services
U.S. House of Representatives
Washington, DC 20515

Dear Chairman Waters and Ranking Member McHenry:

The U.S. Chamber of Commerce's (the Chamber) Center for Capital Markets Competitiveness (CCMC) writes regarding the hearing on March 17, 2021 titled "Game Stopped? Who Wins and Loses When Short Sellers, Social Media, and Retail Investors Collide, Part II." We submit this letter for the record to explain why a Financial Transaction Tax (FTT) is not a practical policy proposal.

<u>Opposition to an FTT</u>

The Chamber is concerned by proposals to impose an FTT, particularly based on what we know about the history of the FTT in the U.S., the deleterious impacts we know an FTT would have on the retirement community, investors, businesses, and the economy, and the 63% of bipartisan American poll respondents who are overwhelmingly opposed to an FTT.

Historic, Bipartisan Congressional Opposition: The U.S. has already lived through an unsuccessful experiment with an FTT from 1914 to 1965. After more than a half century with an FTT, the tax was ultimately repealed in an overwhelming bipartisan vote by a Democratic Congress. A 1965 report by the Committee on Ways and Means[1] found that taxes like the FTT "were not developed on any systematic basis and are often discriminatory in their application to the taxed industries or to the purchasers of the taxed products." We strongly discourage the Committee from reintroducing an FTT in the U.S.

U.S. Chamber of Commerce: The Chamber has consistently opposed legislation that would impose a financial transaction tax on financial trades, such as equities, bonds, and derivatives. Our 2019 report "Financial transaction taxes: A tax on investors, taxpayers, and consumers,"[2] outlines the numerous, serious drawbacks of an FTT that extend beyond retirement savers and

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[1] U.S. Government Printing Office. 1965. *Excise Tax Reduction Act of 1965, Report of the Committee on Ways and Means, House of Representatives, to Accompany H.R. 8371*. p. 1. Washington. https://www.finance.senate.gov/imo/media/doc/SRpt89-324.pdf

[2] U.S. Chamber of Commerce, Center for Capital Markets Competitiveness. "CCMC 2019 Report." https://www.centerforcapitalmarkets.com/wp-content/uploads/2019/08/CCMC_FTT-Report_v2-DIGITAL.pdf

investors to Main Street, businesses, and the economy. Appendix A includes the Executive Summary from the report and highlights the many negative consequences of an FTT.

Bipartisan Americans: Americans are deeply concerned about proposals to reimpose an FTT and there is robust, bipartisan opposition to an FTT. CCMC recently conducted a national poll to understand views on a proposed FTT. When they learned about an FTT, an overwhelming bipartisan majority of 63% expressed opposition to an FTT. When questioned on the intensity of their opposition, nearly half of voters (49%) expressed strong opposition to an FTT. We are particularly concerned about the chilling effect that an FTT could have on Americans' retirement savings. A majority responded that they would be less likely to invest if such a tax were to be enacted by Congress and a third said such a tax would make them less likely to invest in the market under this tax.

Furthermore, Americans surveyed believe an FTT would undermine Congress' policy priorities, such as growing the economy and jobs and helping Americans get back on their feet following the COVID-19 pandemic, while making it more difficult for Americans to save money for retirement and pay for their children's college. An FTT runs counter to these important policy goals. It is clear from respondents that they believe an FTT would hurt efforts to recover from the impact of the COVID-19 pandemic and harm Americans' ability to save for retirement. Appendix B provides a summary of the polling results.

An FTT Would Place Significant Costs Upon Hard-working American Savers

FTTs have been pitched by various proponents as a painless way to raise vast sums of money from Wall Street to fund other projects under consideration by Congress. However, an FTT is actually borne by everyday investors. The imposition of an FTT means that Americans would either have less saved for retirement, a first home or their children's education, or they would have to extend their work years. It should be noted that many Americans relied on their pension, 401(k) or IRA to ride out the financial crunch created by the COVID-19 pandemic. The extra burden of an FTT placed on hardworking families as they seek to save and rebuild their retirement accounts is not negligible and it would instead hurt long-term investors and families.

Specifically, the tax would result in a massive increase in transactions costs at a time when investors benefit from historically low transaction costs. Commissions for stock trades in the United States are quite low and are free for most retail investors. Institutional investors on average pay a mere 0.03%.[3] However, the taxes proposed by both the Wall Street Tax Act and the Inclusive Prosperity Act would result in a massive increase in transaction costs for investors.

As the costs from an FTT compound over time, 401(k), IRA, and pension plan holders would see a diminution of their accounts. The Chamber has calculated the impact to investors under the Wall Street Tax Act and Inclusive Prosperity Act (See "Appendix C"). The analysis shows that despite working hard to save year after year, retirement savers would find themselves significantly penalized by an FTT. Specifically, a 401(k) participant who saves the average contribution each year would end up with $31,912 less under the Wall Street Tax Act and

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[3] Virtu Global Cost Review, 4Q 2020.
https://www.virtu.com/uploads/documents/Virtu_EQ_GlobalCostReview_4Q20.pdf

$153,401 less if subject to the Inclusive Prosperity Act. In both cases, these significant and unnecessary losses from one's life savings can be entirely prevented by opposing such legislation.

Additional Consequences of an FTT

In addition to the significant negative impact to American retirement savers, the effects of imposing an FTT extend beyond retirement savers, as explained further in Appendix A. The tax also harms consumers who would pay higher prices for groceries and gas, homeowners who would pay higher mortgage rates, and all taxpayers who would pay more as the cost of public projects increases. The cascade of these negative impacts would exacerbate the fiscal pain felt by many American families who are struggling, particularly as they are already falling behind on retirement savings due to COVID-19.

By creating market inefficiencies, the FTT would also harm the ability of businesses to effectively raise capital or make capital more expensive. Impeding capital formation can have adverse ripple effects throughout the economy.

Although supporters claim that an FTT would raise revenue, experience has shown that FTTs would not raise the revenue that proponents expect. By suppressing economic and trading activity and driving more trading offshore, the amount of revenue raised would be far less than estimated. The experience in other countries is that FTTs collect far less than forecast, which is why so many countries that have imposed FTTs have eventually eliminated them.[4]

Conclusion

For these many reasons, we strongly discourage Congress from reintroducing an FTT in the U.S.

We thank you for considering our feedback and welcome answering any questions on this issue.

Sincerely,

Tom Quaadman

cc: Committee on Financial Services

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[4] CCMC 2019 Report. Countries like Germany, Sweden, and Japan have all tried imposing financial transaction taxes, but ultimately eliminated them.

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Appendix A: Executive Summary from "Financial Transaction Taxes: A tax on investors, taxpayers, and consumers," authored by the Center for Capital Markets Competitiveness

FINANCIAL TRANSACTION TAXES:

A tax on investors, taxpayers, and consumers

SUMMER 2019

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FINANCIAL TRANSACTION TAXES:

A tax on investors, taxpayers, and consumers

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The author gratefully acknowledges financial support for this project from the U.S. Chamber of Commerce.
All opinions are those of the author and do not necessarily reflect those of the Chamber or Georgetown University.

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Executive Summary

Proposals for a financial transaction tax (FTT) have surfaced throughout the years in the United States and around the world. Recently, bills have been introduced in Congress that would tax financial transactions at rates of up to 0.5%. Similar bills have been proposed in previous Congresses. Proponents of such a tax contend that it would raise revenue while suppressing allegedly excessive trading activity. This paper examines the economic impact that an FTT would have in the U.S.

Key Findings:

- **Main Street will pay for the tax, not Wall Street.**
  The real burden will be on ordinary investors, such as retirees, pension holders, and those saving for college. They will pay the tax directly when they trade, and pay it again as financial intermediaries pass on the taxes they face as a cost of doing business. FTTs are not actually a tax on financial intermediaries; they are a tax on investors.

- **An FTT will drive up the cost of trading by more than the amount of the tax.**
  The cost to a retail investor who buys a round lot of a $100.00 stock would be $50.00 in direct costs and even more in indirect costs. This represents a more than tenfold increase in the cost of trading in a world of $5.00 commissions.

- **Retirement savings will be hit hard.**
  Under the version of the tax proposed by Sen. Bernie Sanders (D-VT), a typical retirement investor will end up with 8.5% less in his or her 401(k) or IRA after a lifetime of savings. In dollar terms, the average IRA investor would have $20,000 less at retirement as a result of this tax.

- **An FTT will drive up the cost of home mortgages.**
  The yields on mortgage-backed securities will go up because of both the direct impact of an FTT on the cost of trading them and the impact of an increase in benchmark Treasury rates. Because the rate on home mortgages is related to the yields on these mortgage-backed securities, an FTT will be passed on to homeowners through higher mortgage rates.

- **Mutual fund expenses will go up and reduce mutual fund returns.**
  The transaction taxes paid directly and indirectly by mutual funds will increase their costs and decrease returns to investors. This will harm mutual fund investors such as 401(k) participants saving for retirement.

- **Pension fund expenses will go up and pension fund returns will go down.**
  Likewise, the transaction taxes paid by pension funds will reduce their returns, worsening existing problems with underfunded pensions and making it more costly for governments and corporations to provide pensions.

- **Taxpayers will pay more because government financing costs will go up.**
  An FTT on municipal and U.S. Treasury securities will lead to higher interest rates on those securities. This will increase government borrowing costs, which will be borne by all taxpayers, not just investors. This will also increase the cost of capital for public projects, such as infrastructure improvements.

- **Corporate financing costs will go up.**
  While the proposed FTTs do exempt new issues of equity and debt, they would apply to secondary market transactions. Investors will expect higher returns to offset the reduced cash inflows caused by an FTT, which will raise the costs of corporate financing.

- **Hedging costs for producers will go up, and consumers will pay for it.**
  Producers such as farmers, oil companies, and airlines use derivatives such as options and futures to manage their risk. Taxes such as FTTs are part of their cost of doing business that gets passed on to the consumer in the form of higher prices for groceries, gasoline, and travel.

- **GDP will be reduced by more than the net revenue raised.**
  An FTT will depress economic activity in several ways. The higher cost of capital will result in less investment and thus less economic growth, fewer jobs, and less income tax revenue. At the same time an FTT will depress trading activity and send it offshore, resulting in a loss in jobs and tax revenue, consistent with what has occurred in other countries that have experimented with FTTs. European Union economists have estimated that a proposed EU FTT, similar to the ones proposed in the U.S., would actually reduce GDP by more than the revenue raised.

- **FTTs will not raise the revenue that proponents expect.**
  By suppressing economic and trading activity and driving more trading offshore, the amount of revenue raised will be far less than estimated. The experience in other countries is that FTTs collect far less than forecast.

- **An FTT will cause stock prices to fall.**
  Stock prices are a function of after-tax cash flows received by investors. By decreasing the after-tax cash flows investors receive, an increase in taxes will cause the value of stocks to fall. This will hurt retirement savers and impose additional stress on already underfunded state and local pension funds. It will also result in less capital gains tax revenue to the government.

- **FTTs may increase market volatility.**
  In many cases around the world, the experience has been that volatility actually increased after FTTs were enacted due to trading activity shifting and liquidity decreasing, making markets less able to withstand future market stress events.

- **FTTs have consistently failed throughout history.**
  FTTs around the world have generated less revenue than forecast due to trading activity shifting to other jurisdictions. They ended up being scaled back due to their deleterious impact on the economy. Indeed, a Democratic Congress and president wisely scrapped the previous FTT in the United States.

- **The proposed FTTs are more onerous than FTTs in foreign countries.**
  Most countries with FTTs exempt liquidity providers such as market makers from FTTs because of their important role in smoothing market operations. The lack of such an exemption in the proposed FTTs would exacerbate their negative impacts.

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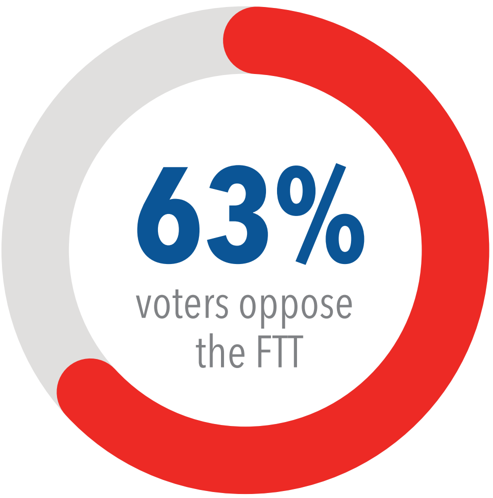
Appendix B: Poll Finds Bipartisan Opposition to Financial Transaction Tax

Poll Finds Bipartisan Opposition to Financial Transaction Tax

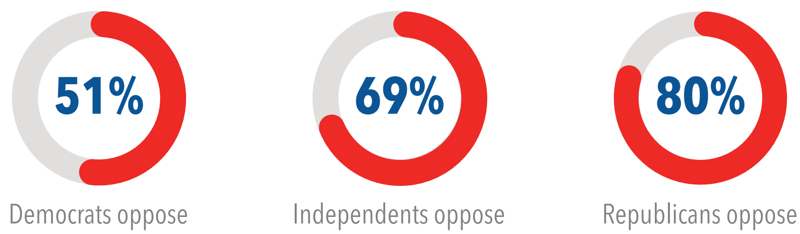
Center for Capital Markets Competitiveness

No matter how you approach a Financial Transaction Tax (FTT), the outcome will be the same: Main Street, consumers, taxpayers, retirees, states, and localities are the ones who will suffer. The U.S. Chamber of Commerce's Center for Capital Markets Competitiveness (CCMC) conducted a poll of 2,000 likely voters nationally to understand their views on a proposed FTT. According to the poll:



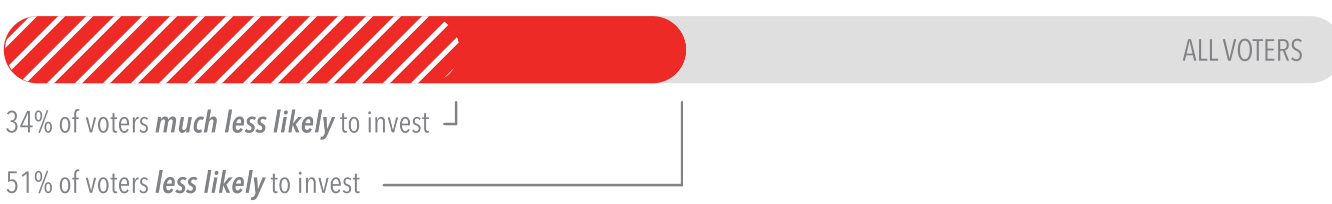
When voters learn about an FTT, nearly two-thirds oppose the tax:

- 63% of voters oppose an FTT, including a majority of Democrats (51%), Independents (69%), and Republicans (80%).
- When questioned on the intensity of their opposition, 49% of respondents expressed strong opposition to an FTT, almost a majority of voters (more than one-in-three Democrats strongly oppose an FTT, along with 57% of Independents and 72% of Republicans).



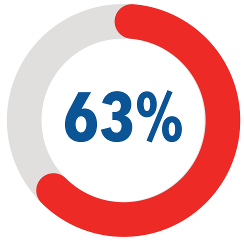
The tax itself is likely to have a chilling effect on voters' retirement savings:

- Half (51%) of voters say that if this tax were to pass, they would be less likely to invest.
- A third (34%) of voters would be much less likely to invest in the market under this new tax.



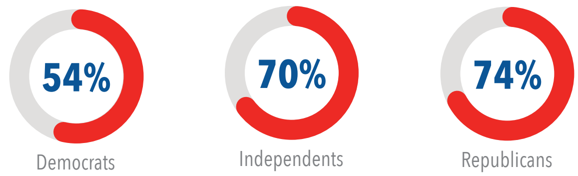
More importantly, voters believe an FTT will hurt efforts to achieve priority policy goals:

ECONOMY

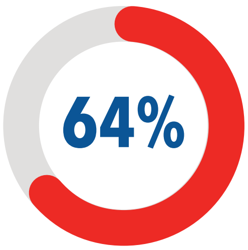


TOTAL VOTERS

- Growing the economy and jobs is the #1 priority voters have for the U.S. Government, but 63% said that an FTT would actually hurt efforts to restart the economy and bring back jobs (Democrats: 54% say it will hurt more than help. Republicans: 74% hurt more than help. Independents 70% hurt more than help).

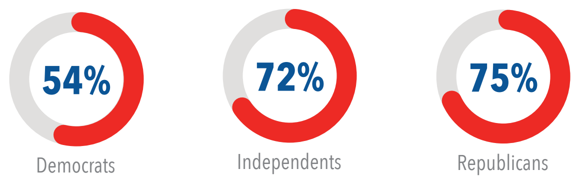


COVID-19 RECOVERY

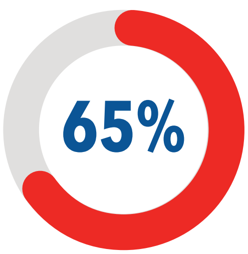


TOTAL VOTERS

- 64% say an FTT will hurt Americans as they're trying to get back on their feet following the COVID-19 pandemic (Democrats: 54% say it will hurt more than help. Republicans: 75% hurt more than help. Independents 72% hurt more than help).

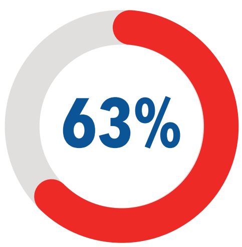


RETIREMENT/EDUCATION



TOTAL VOTERS
RETIREMENT

- 65% say an FTT will harm efforts to ensure Americans have enough money saved for retirement.
- 63% even say an FTT will make it more difficult for Americans to pay for college.



TOTAL VOTERS
EDUCATION

In a rare moment of bipartisanship, Democratic and Republican voters are united in opposition to an FTT. Majorities from both parties believe an FTT would hurt efforts to recover from the impact of the COVID-19 pandemic and harm Americans' ability to save for retirement.

Voters are looking to the federal government to help grow the economy and bring back jobs. They want the government laser-focused on the vaccine effort, along with longer-term goals of making healthcare more affordable and improving education. When voters from both parties speak with one voice, Congress needs to listen: Republicans and Democrats alike understand that an FTT runs counter to these goals.

If you have any questions, please contact Kristen Malinconico, Director, U.S. Chamber Center for Capital Markets Competitiveness, at kmalinconico@USChamber.com.

Methodology: The survey was conducted by Teneo Research. The data was collected online between February 23 and 25, 2021 among a nationally proportional sample of 2,000 likely voters. The survey has a credibility interval of ±2.5% at the 95% confidence level.

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Appendix C: Retirement Investment Scenario

Retirement Investment Scenario

This scenario estimates the impact of a Financial Transaction Tax (FTT) on a 401(k) investor who invests the average 401(k) contribution each year over the lifetime of his or her working career. The cumulative cost of the tax grows each year as the retirement saver loses the compounding of returns on the taxes paid.

A typical retirement investor will end up with $31,912 less under the Wall Street Tax Act and $153,401 less if subject to the Inclusive Prosperity Act.

ASSUMPTIONS

TIME FRAME | An employee makes annual contributions to a 401(k) plan for 45 working years (approximately ages 21 to 66).

ANNUAL 401(K) CONTRIBUTION | At the end of each year, the employee contributes $11,350, which represents the average annual 401(k) contribution including the employee and the average employer match.[1]

RATE OF RETURN | A real rate of return of 5% is used. This is a conservative estimate given that the average inflation-adjusted return on the S&P500 from 1926 to 2020 was 8.5%. The inflation-adjusted real return is used to make the retirement accumulation comparable in spending power to today's dollars.

ACCUMULATION WITHOUT AN FTT

With no FTT, this worker will accumulate $1,812,597 at retirement.

ANALYSIS WITH AN FTT

The impact of the tax will be a function of the tax rate and turnover rate of the funds.

TAX RATE | We assess the impact of an FTT at both the proposed 0.10% rate from the Wall Street Tax Act and the 0.50% rate from the Inclusive Prosperity Act.

TURNOVER RATE | Retirement savers invest in a variety of different funds with widely varying turnover rates. Actively managed funds tend to have higher turnover. This analysis uses a turnover rate of 63%, which is the average turnover of a domestic stock fund according to Morningstar.[2]

RATE OF RETURN | The Wall Street Tax Act would reduce the return by the turnover rate times the tax rate, or 63% * 0.10%, or 0.063%. The rate of return with the FTT becomes 5.0% - 0.063% = 4.937%. For an FTT rate of 0.50%, the rate of return would be reduced to 5.0% - (63% * 0.50%) = 4.685%.

OTHER IMPACTS | No adjustment is made for the increases in transactions costs such as the bid-ask spread that are likely to occur as intermediaries such as market makers pass through the cost of the tax. Nor is any adjustment made for drops in overall asset prices in reaction to the tax. This results in a more conservative estimate of the impact.

Impact of FTT on Lifetime Retirement Savings Accumulation

	Without an FTT	With the Wall Street Tax Act	With the Inclusive Prosperity Act
Annual Real Return	5.000%	4.937%	4.685%
Annual Contribution	$11,350	$11,350	$11,350
Years of Contributions	45	45	45
Accumulation at Retirement (today's dollars)	$1,812,597	$1,780,685	$1,659,196
Change Due to Tax		**$31,912**	**$153,401**

1. Fidelity Investments, Building Financial Futures: trends and insights of those saving for retirement across America, 4th Quarter 2020, https://sponsor.fidelity.com/bin-public/06_PSW_Website/documents/Building_Financial_Futures.pdf

2. Investopedia, Turnover Ratios and Fund Quality. https://www.investopedia.com/articles/mutualfund/09/mutual-fund-turnover-rate.asp