



## **Rebuttal to Arguments To Reinstate the Stock Transfer Tax (STT)**

- **Proponents argue STT is “huge potential revenue source” and STT “is very, very low.”**

**SIA’s Rebuttal:** SIA believes that any revenue benefits derived from STT would be dwarfed by overall loss in business activities and personal income taxes from job relocations. Securities firms must adhere to “best execution” rules mandated by regulatory authorities. Faced with the STT, these firms are likely to gravitate towards Electronic Crossing Networks (ECNs), Automatic Trading Systems (ATSs)<sup>1</sup> and other alternate trading platforms, which are not within the tax jurisdiction of the State. With the migration of trading to ECNs and ATS, projected volumes on the NYSE, on which any revenue projections are being based would be reduced, ensuring that the State’s revenue projections would not be met.

Although equity trading activity has increased twenty fold over the past 20 years, within the industry, equity business at best has remained stagnant during recent years. With profit margins on trading commissions already measured in pennies, traders and investors would naturally look to alternative trading platforms to find the “best price” to execute trades<sup>2</sup>. This would further depress the equity business (especially since investors have a myriad of alternative investment choices, i.e., debt, options and futures). Consequently, we firmly anticipate that firms would then allocate resources accordingly, including relocating personnel outside New York to meet new administrative demands that these alternative trading platforms require. Also, STT has a high implementation costs associated with “back office” operations, requiring that the STT be added to each trade, and the reprogramming of extensive reporting systems for trade settlement processes and confirmation and notices for customers. To avoid these additional costs, trading activity will migrate to areas outside New York, shifting trading business away from firms that do not have subsidiaries outside the State or that simply cannot afford to relocate. In fact, NYSE member firms are no longer required to maintain their corporate headquarters within a one-mile radius of Wall Street, a requirement the New York Stock Exchange (“NYSE”) once imposed. The STT was phased out in 1981 in recognition that increasingly transient and highly competitive markets might take their business elsewhere if subject to this costly tax. By reinstating this tax, we believe firms will have another reason to relocate out of the State or “dematerialize” where firms “book” their equity trades.

- **Supporters of the STT claim, “The tax applies to any shares listed in NYSE,” regardless of the location of the investor.**

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<sup>1</sup> Although ECNs and ATSs operate in a virtual world, some are headquartered in New York but many have multi-city and state locations.

<sup>2</sup> Gross commissions on trading is already as low as a single penny per share (with profit margins a small fraction of that gross commission).

**SIA's Rebuttal:** This is a misunderstanding of the capital markets and the rules that govern them. For instance, in May 2000, the NYSE rescinded Rule 390, which originally prohibited NYSE listed stock from being traded on other exchanges. Now, NYSE listed companies could be traded on any trading platform, including any other national and international exchanges. By imposing STT on national exchanges in NY, the exchanges' competitive advantage over alternative trading platforms would be further marginalized. Tax policy should be forward looking, taking into account constantly evolving market structure changes the securities industry must undergo. For instance, should the trend towards greater integration of NYSE's specialists system into electronic trading platforms continue, then it is likely that firms mandated by "best execution" requirements would migrate to trading platforms outside the jurisdiction of New York. This undoubtedly would have a negative effect on the NYSE and AMEX, adversely affecting New York City's reputation as the "financial capital of the world," which is already affected by the recent corporate governance controversy.

- **Proponents also contend STT is paid only by shareholders.**

**SIA's Rebuttal:** This is not the basis for sound tax policy. SIA has always maintained that STT is unfair since it would not be distributed evenly over a broad base.

This tax singles out one segment of the financial services industry, which has had progressively lower profit levels as compared to three years ago. STT looks to tax equity investors, including governments, public pension funds and the securities firms that trade stocks for their proprietary accounts<sup>3</sup>, especially those New York-based securities dealers. The securities industry is quite often the shareholder, taxed on one side of the transaction with its customer on the other. Firms are holding inventory as "market makers" or following mandates as "specialists" will feel the brunt of the tax unlike securities dealers trading on the OTC market, who are not subject to the tax. By discriminating against equities as compared to other financial products, the equity business would be further depressed, leading to unnecessary distortion in the flow of capital. We also believe any "flat figure" per transaction would unduly penalize lower priced stocks, which in turn, might encourage "reverse stock splits"<sup>4</sup> to lessen the impact of the costs. This could lead to an overall lowering of trading volume and further reduce the State's expectation of revenue estimates. In short, STT is biased against small broker-dealers and certainly to small investors, who are already disenfranchised about returning to the markets.

- **Some have urge New York to follow other international financial centers which tax stock sales**

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<sup>3</sup> First, the Federal Reserve's latest figures on ownership of all US equities (regardless of where these companies are) show that large institutions own nearly two-thirds of all stock in the United States, including pension funds, governments, insurers, certain equity and hybrid mutual funds (although often these institutions have guidelines on what kinds of stocks they can own, i.e., lower "cap" and "penny" stocks). SIA estimates that institutions hold 75% of all NYSE listed stocks (and the following percent holdings of all stocks by instructional type will likewise be somewhat higher for NYSE stocks). Also, over the past five years, the % of NYSE volume that is institutional ranged from 81% to 87%, depending on the year (45% to 52% of total volume were block trades alone which could easily be effected off the NYSE since they were not done on "the floor").

<sup>4</sup> This is process by which a listed company reduces the overall number of outstanding shares, but in return, the price for that stock rises.

**SIA's Rebuttal:** While this is true, two important points must be made. First, in other countries, these taxes apply on a nationwide basis, so that it is not possible to avoid the taxes simply by executing the trade on another exchange in the same country (if indeed other exchanges in the country exist, which is not always the case). Second, as one might anticipate, offshore trading often develops specifically in an attempt to avoid these taxes.

