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IIF Council for Asset and Investment Management Raises Concerns that the Proposed EU Financial Transaction Tax Could Hurt Savers and Pensioners

Potential Impact on Market Liquidity Could be Severe

Washington, D.C., April 23, 2013 – *The IIF's Council on Asset and Investment Management (CAIM) today released a position paper on the proposed EU Financial Transaction Tax (FTT). While acknowledging that the proposed FTT is motivated by worthwhile goals, CAIM raised concerns that any revenue it would generate would be considerably outweighed by the potential costs in terms of burden on end-users of financial services, potentially weaker economic growth and job losses. In sum, the proposed EU FTT would likely prove ineffective and fail to meet its goals***.**

The Council addresses a number of concerns in its position paper regarding the impact of the FTT, which it believes could result in considerable harm not only for institutional investors and financial markets, but also for the real economy, sovereign debtors, private investors and financial stability more broadly. CAIM's assessment of the FTT's key drawbacks is detailed in the attached position paper and summarized below:

- **Burden on private investors:** In line with the European Commission's own assessment, CAIM members believe that a large part of the burden would fall on end-users of financial services: households and small businesses will not escape the tax burden. In particular, savers and pensioners would very likely experience lower returns on their investments.
- **Risks to economic growth:** The Council highlights the significant empirical evidence that suggests financial transaction taxes lead to lower liquidity, higher volatility, higher transaction costs, lower asset prices and a higher cost of capital—ultimately resulting in lower investment activity, job losses, and lower GDP growth.
- **Higher cost to hedge risks:** The EC itself expects a 75% drop in derivatives transaction volumes over time. This will affect not only "speculative" trading but also essential hedging activities for risk management undertaken by both institutional investors and non-financial firms. Market participants with short-term hedging needs could decide to keep certain positions open, exposing themselves to undesired risks.
- **Potentially dramatic impact on European repo markets:** Transactions in the European repo market—some €5.6 trillion in size—play a vital role not only in bank funding but in investors' short-term liquidity management and in monetary policy. As repos tend to be high-frequency transactions (e.g. overnight), a series of transactions could result over the course of a year in a cumulative tax liability of about 25% p.a.—which could severely inhibit this key market.
- **Higher cost of sovereign funding**: Taxation on secondary market transactions in government bond markets would have a direct and negative impact on liquidity and funding costs. This is particularly relevant for short-term bonds in a low interest rate environment, where the marginal cost of an FTT could be prohibitive. This would impair primary markets in these securities and reduce market access for countries already facing challenging market conditions.
- **Concerns about extraterritoriality:** With jurisdiction in only 11 EU member countries, an EU FTT would create a non-level playing field, with market participants within the FTT area placed at a competitive disadvantage. Given the very high mobility of capital, financial transactions, market activity and jobs could shift to preferred tax jurisdictions.

"A financial transaction tax would ultimately hurt savers and pensioners, at a time when many are already struggling to achieve adequate returns," stated Walter Kielholz, Chairman of the Board of Directors, Swiss Re. "Moreover, the FTT could greatly reduce liquidity and impair financial stability, particularly against the backdrop of still-fragile financial markets. Imposing such a tax would create additional headwinds to growth and job creation in Europe."

"We are deeply concerned that the proposed EU FTT could create unintended investment incentives, contradicting the principles of sound investment management," notes Richard Kushel, Deputy Chief Operating Officer, BlackRock. "We fear, for instance, that the tax could have a particularly negative effect on some of the most safety-conscious investors, whose portfolios invest in shorter-duration bonds, as these are subject to a greater number of transactions. Worse still, the tax would penalize hedging transactions and other forms of risk management."

The potential risks to the market environment, including the impact on long-term investors, should be carefully considered in assessing the case for implementing an EU financial transaction tax.

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About the IIF and the Council for Asset and Investment Management (CAIM)

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The Council for Asset and Investment Management (CAIM) comprises long-term investors including 30 insurers, pension funds, sovereign wealth funds and asset managers, which collectively account for some $20 trillion in assets under management. More information about the Institute of International Finance is available at www.iif.com.