Despite the fact that most STTs have been repealed in the late 1980s–early 1990s, numerous legislative efforts in the United States have been made to reintroduce them, though none have been implemented thus far.[5] India introduced STTs in 2008, and they are still present today. Many other countries have implemented financial transaction taxes, but India tends to have the most comprehensive tax on securities.[6] Taiwan has also adopted the use of STTs. Members of the European Union have recently adopted a proposal for a Council Directive to use FTTs. This report examines the effects associated with STTs in financial markets and the impacts they have in generating state revenue.

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Financial Markets and Securities

Securities are one of the many instruments that are used in financial markets.

Those who advocate for a security transaction tax argue that it will serve as an additional way to raise revenue, reduce speculation, and curb overall volatility in financial markets.[19] Those who advocate against STTs argue that STTs will provide an additional opportunity cost imposed on financial transactions. This may lead to the reduction in the overall value of the securities market, decrease liquidity, and lead to an overall decrease in the efficiency of the financial market, which may potentially drive trade to other foreign markets.[20] In addition, there have been concerns over the likelihood of firms fighting against or evading STTs.[21]

Past research on STTs, regulations associated with their implementation, and the impact they have on the price volatility of securities suggests, "Transaction taxes may have no effect on volatility or, in some cases, may actually increase volatility.[22] The increased cost of trading could therefore lead to large movements in security prices and hence greater volatility. On the other hand, an STT could theoretically reduce excess volatility if it deters certain destabilizing investment behavior that pushes security prices away from fundamentals, eventually leading to sharper price corrections."[23] Fundamentals are referred to as "the qualitative and quantitative information that contributes to the economic well-being and the subsequent financial valuation of a company, security or currency."[24]

It is difficult to properly assess the future market effects that STTs would have since most research done draws from "data [that are] over 20 years old."[25] In addition, there is no present model or indicator that could "estimate how traders would respond to a new tax."[26] Since global financial markets and regulations have evolved, these reports may not be applicable to current market trends.[27]

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[19] C Johan Bjursell, George H.K. Wang, and Jot Yau, "Transaction Tax and Market Quality of U.S Futures Exchanges: An Ex-Ante Analysis," in Review of Future Markets, The Institute for Financial Markets, 2012, http://www.theifm.org/rfm-special-Issue2011.pdf, pp. 114-115.

[20] C Johan Bjursell, George H.K. wang and Jot Yau, "Transaction Tax and Market Quality of U.S. Futures Market: An Ex-Ante Analysis", Institute for Financial Markets, July 2012, accessed on April 15, 2013, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2139586, p. 7.

[21] Mark P. Keightley, "A Securities Transaction Tax: Financial Markets and Revenue Effects," p. 2.

[22] Mark P. Keightley, "A Securities Transaction Tax: Financial Markets and Revenue Effects," p. 2.

[23] Mark P. Keightley, "A Securities Transaction Tax: Financial Markets and Revenue Effects," p. 9.

[24] "Definitions: Fundamentals", Investopedia, 2013, http://www.investopedia.com/terms/f/fundamentals.asp

[25] Mark P. Keightley, "A Securities Transaction Tax: Brief Analytic Overview with Revenue Estimates," Congressional Research Service, June 1, 2012, accessed on March 17, 2013, http://www.fas.org/sgp/crs/misc/R42078.pdf, p. 2.

[26] Mark P. Keightley, "A Securities Transaction Tax: Brief Analytic Overview with Revenue Estimates," p. 2.

[27] Mark P. Keightley, "A Securities Transaction Tax: Brief Analytic Overview with Revenue Estimates," p. 2.

Potential Revenues from Security Transaction Taxes

Estimating the amount of revenue that STTs may potentially create is difficult. "The difficulty comes from uncertainty about future economic conditions, unknown potential behavior responses by taxpayers, and notable differences among legislative proposals."[28]

Table 1: Potential Net Revenue from 0.25% STT, 2007

Reduction in Trading Volume	Projected Annual Revenue, $billion
20%	132.3
50%	82.7
Source: Mark P. Keightley, "A Securities Transaction Tax: Brief Analytic Overview with Revenue Estimates," Congressional Research Service, 3p	

Table 1 provides an estimate for how much revenue a 0.25% STT would create if enacted on SEC regulated exchanges under two different market responses. The first scenario examines what would happen to annual revenue if there was a 20% reduction in trade volume due to the STT. The second scenario examines the potential impact on annual revenue if STTs caused a 50% reduction in trade volume. "In 2007, the SEC reported that the total value of transactions involving U.S. stock, options, and security features as $66.1 trillion. This base does not include bond trading, trading occurring off SEC-regulated exchanges, and other markets."[29] While projected annual revenue is significant, factors such as governmental exemptions and administrative and evasion problems need to be taken into consideration.[30]

STTs India

India has been one of the more recent markets to introduce STTs unlike many of the models that were phased out during the late 1980s-early 1990s.[31] The in the world,” STTs became a viable option for India to generate state revenue as well as reduce market speculation and volatility.[34]

India’s STTs are broken into three different payable rates. A sale of an option in securities is taxed .017%, payable by the seller. A sale of an option in securities where the option is exercised is taxed at .125%, payable by the purchaser. Exercising refers to “acting on a right provided for in a securities contract.”[35] A sale of a futures in securities is payable by the seller and is taxed at a rate of .017%.[36]

Greece, Italy, Portugal, Slovakia, Slovenia, and Spain.[42] The main aim of the FTT is to make the financial and banking sector "pay their fair share of the cost of recovering from the [2008 Global Financial Crisis]."[43] The FTT would have a "minimum rate of 0.01% for derivatives, and 0.1% for every other transaction, including purchases of shares and bonds. Participating countries are free to apply a higher rate. The tax would not be applied to everyday financial activities by people and businesses – such as getting insured, taking out a mortgage, credit card purchases and business lending."[44] The Eurozone FTT is estimated to generate