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A financial transaction tax would worsen the state's fiscal crisis

BY: TERRY DUFFY

As the bewitching hour neared for the General Assembly to resolve its almost 12-month state budget impasse, an issue that actually goes back decades, lawmakers felt pressure to resolve the stalemate that threatens many aspects of our state's economy. This unfortunate standoff is endangering the funding for our schools, health care, infrastructure and a slew of other state-provided services. It is leaving a stack of unpaid bills and a number of worried citizens, this life-long Illinois resident included.

Our people and businesses are fleeing to other states in search of better opportunities. Census data show Illinois' population has decreased for the first time since the 1980s. Chicago is on a path to lose its title as the third-largest U.S. city within next 10 years.


PHOTO BY BLOOMBERG
CME Executive Chairman Terry Duffy

To reverse these dire trends, our elected officials must come together to develop a long-term plan that will address the state's finances. Unfortunately, some of our lawmakers floated a careless and short-sighted proposal, one that, if enacted, could turn this fiscal crisis into a fiscal disaster. This measure, known as a financial transaction tax, would not only fail to resolve the fiscal problem; it would make matters significantly worse and instigate a fiscal death spiral.

To those in Springfield, on the campaign trail and elsewhere who may view this so-called plan as some sort of a magic bullet, be warned: a financial transaction tax is an old idea with a dismal, global track record. This proposal would have a disastrous impact—not only on the state and our residents, but also on investors globally and our broader economy.

First, it is based on flawed math. The several-billion-dollar revenue projections its proponents are making cannot possibly come to pass. They are basing their estimates on the unfeasible idea of taxing the notional value of the contracts traded which, in simple terms, would be the equivalent of taxing a realtor on the total value of the home she sold vs. the commission she made. That is not only unfair, but not possible.

Instead, the harsh reality is that this policy would drastically increase the cost of using all markets—stock, futures and options—making individual trades prohibitively more expensive.

How much more? At CME Group, for example, our average rate per contact is 80 cents. By adding $1 per contract for agricultural products, and $2 per contract for all others, it would increase costs by up to 800 percent. That's no small drop in the bucket.

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Looking at this proposed hike another way, the average rate for financial contracts such as interest rate and stock futures, is 50 cents. If lawmakers were to add a $2 fee to that transaction, this levy would be the same as raising the cost of gas from $2 per gallon to $10 per gallon overnight. I can assure you that this dramatic and unfair increase would drive many customers—important liquidity providers—away from cash and futures markets and out of Illinois to other venues, places that don't have a transaction tax.

A loss of market participants means that some of Illinois' biggest agribusiness people—farmers, ranchers and other end users—also would pay more to hedge commodity price risks, and additional costs would be passed on to consumers in the form of higher food or gas prices. A decline in trading activity also means that the tax would ironically collect less revenue than originally projected, thus eliminating its very purpose.

Overseas markets have already learned their lessons from the damage done by implementing similar plans. Countries ranging from India, to Sweden, to Hong Kong to Canada have imposed varying forms of this type of tax over the last 30 years, all with dismal consequences. A 2011 study by the European Commission, which has been weighing such a tax for more than five years, found that a 0.1 percent tax on securities could reduce future GDP growth by 1.76 percent. It's no wonder why the talks between several Eurozone countries that are considering such a levy have stalled. They got the memo; it's time that we do the same.

We all understand the urgent need to solve the state's fiscal crisis, but we must also recognize the current deficit was years in the making. It cannot be remedied overnight by bad policy that only makes matters worse.

Instead, the state must honor the agreements our elected officials voted for and at the same time work with public and private sectors to develop a long-term plan to attract new residents, retain jobs and generate growth. Let's take a long view and work together to make the right fixes—not false promises which in the end will only chase away more residents and yet another industry.

Terry Duffy is executive chairman and president of CME Group.