

Cost Estimate of Election Campaign Proposal

Publication date:	2019-09-25	
Short title:	Implement a new financial transaction tax	
Description:	Taxing all financial transactions in Canada at 0.5% of transaction value	
Operating line(s):	New entry under "Other revenues" in Table A1.5 of the Economic Statement. This entry would be titled "Financial transaction tax".	
Data sources:	<u>Variable</u>	<u>Source</u>
	Equity market transactions	Investment Industry Regulatory Organization of Canada
	Bond market transactions	Haver Analytics
	Money markets transactions	Haver Analytics
	Derivatives transactions	Bank for International Settlements/ Depository Trust and Clearing Corporation
	Foreign exchange transactions	Canadian Foreign Exchange Committee
Estimation and projection method:	<p>The tax base was determined from data reported to national and international financial oversight bodies. A methodology previously applied in a European Commission report [SEC(2011) 1102 Final] was used to estimate the potential revenue from the tax. This was projected forward based on recent trends in the value of transactions – recognising that it would be strongly affected by the tax measure.</p> <p>Two important parameters in these calculations are the degree of "relocation and avoidance", and the responsiveness of traders who are not able to relocate their trades. Relocation and avoidance together are estimated to be high: 50 % for transactions such as bond and equity markets, and 90 % for derivatives. This is in line with the European Commission study and other literature on transaction costs in small open economies. Moreover, the share of transactions of derivatives (FX and Interest Rate) with counterparties outside Canada is high – underpinning the notion that they are highly susceptible to relocating.</p> <p>The direct responsiveness of trades among those who do not relocate is also strong. So, for every 0.1 % change in the tax rate, there is a 0.2 % reduction in trading. This is applied to all classes of financial transactions.</p> <p>Growth in transactions to 2029 is assumed to occur at the same rate as that from 2005 to 2016. Exceptions were made in the case of Interest Rate derivatives and Money Market transactions, where the past 5 years have seen almost no growth.</p>	

Uncertainty
assessment:

The estimate has high uncertainty. While there is a good deal of confidence in the historical data, the response of the market to the tax is uncertain. This is reflected in high parameter values for trades to move out of Canada, and in the responsiveness of trades that remain in Canada. This analysis has not attempted to include explicit measures that would require Canadian traders to transact exclusively within Canada.

The estimated revenues could be off by factors of 2 or 3 in either direction (higher or lower). While the experience in other countries provides some guidance, a financial tax of this scale has not been tried in an open economy before. The estimate does not take into account the impact of such a tax on the broader economy.

Cost of proposed measure

\$ millions	2019-2020	2020-2021	2021-2022	2022-2023	2023-2024	2024-2025	2025-2026	2026-2027	2027-2028	2028-2029
Total cost	-3,695	-14,960	-15,688	-16,466	-17,299	-18,191	-19,147	-20,173	-21,275	-22,458

Notes:

Implementation occurs January 1, 2020.

Estimates are presented on an accruals basis as would appear in the budget and public accounts.

Positive numbers subtract from the budgetary balance, negative numbers contribute to the budget balance.

"-" = PBO does not expect a financial cost.