

# SECURITIES TRANSACTION FEES

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HEARING  
BEFORE THE  
SUBCOMMITTEE ON  
FINANCE AND HAZARDOUS MATERIALS  
OF THE  
COMMITTEE ON COMMERCE  
HOUSE OF REPRESENTATIVES  
ONE HUNDRED SIXTH CONGRESS  
FIRST SESSION

ON

**H.R. 1256 and H.R. 2441**

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SEPTEMBER 28, 1999

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## SECURITIES TRANSACTION FEES

TUESDAY, SEPTEMBER 28, 1999

HOUSE OF REPRESENTATIVES,  
COMMITTEE ON COMMERCE,  
SUBCOMMITTEE ON FINANCE AND HAZARDOUS MATERIALS,  
*Washington, DC.*

The subcommittee met, pursuant to notice, at 10:10 a.m., in room 2123, Rayburn House Office Building, Hon. Michael G. Oxley (chairman) presiding.

Members present: Representatives Oxley, Largent, Lazio, Shimkus, Fossella, Blunt, Ehrlich, Towns, Stupak, and Luther.

Staff present: Brian McCullough, professional staff member; David Cavicke, majority counsel; Robert Simison, legislative clerk; and Consuela Washington, minority counsel.

Mr. OXLEY. The subcommittee will come to order.

The Chair will recognize himself for an opening statement.

This subcommittee held an oversight hearing at the end of July to examine the impact of the explosive growth in the securities market on fee collections. We heard testimony from the affected industry that bears a large share of the tax burden. Many of us were already aware that fees assessed on all securities market participants generated over \$1.7 billion in fiscal 1998, and a similar amount is expected to be collected this year.

Charging investors and market participants nearly \$3 billion more than the cost of the regulation for the past 2 years borders on criminal. We can all agree that collecting more than five times the costs of running the SEC is not something that was ever intended. Even the most optimistic forecast could not have predicted the exponential growth in market and volume that has occurred in the past 3 years. The surplus revenue collected by these fees is a direct result of this unprecedented growth, and there is no reason to believe that market volume will decrease. As the markets continue to move to extended trading hours, move to decimalization, and more Americans become investors, transaction fee revenue will continue to increase, and that is precisely why we are examining possible solutions.

Chairman Bliley recognized the growing problem of excessive fees several years ago and through considerable effort was able to enact reform of the fee structure. Already, the decreasing fee rate applied to securities registrations is having a noticeable effect. However, because transaction volume never could have been predicted to increase so dramatically, no adjustment was made in the law for transaction fees until fiscal 2007. For this reason, the legislative proposal before us only affects transaction fees.

In a perfect world we would simply make the changes to eliminate the entire excess immediately, but this is Washington. Unfortunately, that means we have other factors to consider and hurdles to cross to achieve our goal. After the oversight hearing in July, I asked staff to examine both bills to provide me with a preliminary overview of each bill. As part of the record, I am submitting a memo from the staff of the CBO to committee staff. The memo is not a final or official cost estimate, but provides us with a reasonable starting point as we continue to examine viable options to address this problem.

[The information referred to follows:]

*September 27, 1999*

MEMORANDUM

To: Majority and Minority Staff, House Committee on Commerce  
From: Mark Hadley and Hester Grippando

As requested, we have begun to review H.R. 1256, the Savings and Investment Relief Act of 1999; H.R. 2441, the Fairness in Securities Transactions Act; and the draft legislation provided to us on September 23, 1999. Each of these proposals would reduce the total amount of transaction fees that the Securities and Exchange Commission (SEC) would collect. This memo responds to your request for information on whether these proposals would affect direct spending and revenues.

All three proposals would affect revenues; therefore, pay-as-you go procedures would apply. In addition, H.R. 2441 would affect direct spending. On balance, we expect that H.R. 1256 and H.R. 2441 would have net costs for pay-as-you-go purposes. We expect that the draft legislation would lead to small pay-as-you-go savings.

Under current law, the SEC charges national securities exchanges, national securities associations, brokers, and dealers transaction fees equal to  $\frac{1}{300}$  of a percent of the aggregate dollar amount of sales of securities. Fees from national securities associations are subject to appropriation action and are recorded as offsetting collections, which are credited to appropriations as an offset to discretionary spending. Fees from other sources are recorded as revenues (governmental receipts).

*H.R. 1256, the Savings and Investment Relief Act of 1999*

H.R. 1256 is similar to draft legislation proposed by Congressman Solomon's staff in September 1998. H.R. 1256 would impose annual limits on the total amount of transaction fees collected (that is, the sum of revenues and offsetting collections). The bill specifies as the annual targets the amounts of revenues projected under current law plus some specified amounts.

For the Solomon proposal, we estimated that the total limit on collections was sufficiently large enough to preclude the possibility that the proposal would affect revenues. We think, however, H.R. 1256 would decrease revenues in some years, because the cap on total fees in those years is not much above the current projections for revenues. We think that the annual loss in revenues would be on the order of the tens of millions of dollars beginning in 2001.

*H.R. 2441, the Fairness in Securities Transactions Act*

H.R. 2441 would reduce the existing transaction fee from  $\frac{1}{300}$  of a percent to  $\frac{1}{500}$  of a percent. The bill would change the budgetary treatment of transaction fees by turning all transaction fees into revenues.

The bill also would require that 10 percent of all fees be deposited as offsetting collections in the account providing appropriations to the SEC, which would allow the SEC to spend about \$50 million annually without additional appropriations action. Such additional direct spending would be greater than the change in estimated revenues.

(In addition, we think that there may be a drafting error in this bill. Under current law, at start of fiscal year 2007 the transaction fee would fall from  $\frac{1}{300}$  of a percent of the aggregate dollar amount of sales of securities to  $\frac{1}{500}$  of a percent. Under H.R. 2441, the fee would remain  $\frac{1}{500}$  of a percent through all of fiscal year 2007, so the bill would increase revenues by about \$500 million in that year.)

*Draft legislation provided on September 23, 1999*

Like H.R. 2441, the draft legislation would reduce the fee from  $\frac{1}{300}$  of a percent of the aggregate dollar amount of sales of securities to  $\frac{1}{500}$  of a percent for fiscal years 2000 through 2006. The draft legislation, however, would require that the

SEC collect 9.5 percent of such fees only to the extent provided in appropriations acts. As under current law, authority to spend the amounts deposited as offsetting collections would be available only to the extent provided in appropriation acts. The draft legislation would expire at the start of fiscal year 2007.

We estimate that the draft legislation would not affect direct spending but would increase revenues by \$1 million a year or less over the 2000-2004 period.

If you have any questions or concerns, please feel free to contact either of us. Mark Hadley may be reached at 226-2860; Hester Grippando may be reached at 226-2720.

cc: Andrew Ehrlich, Congressman Lazio's Office  
Justin Daly, Congressman Fossella's Office

Mr. OXLEY. Both proposals would achieve very similar results, but use different approaches. There are benefits to each method that should be considered. H.R. 2441 uses a rate reduction which leaves the current structure in place and, it appears, would be a very simple change to make. H.R. 1256, on the other hand, utilizes a preset revenue cap. This approach has the benefit of providing the certainty that the problem would not get out of hand again, if market volume exceeds our best estimates.

We heard some initial discussion of the different approaches by the industry witnesses during the previous hearing. I look forward to their continued input and look forward to hearing the views of the Securities and Exchange Commission on both of these bills today, as well as their continued input on any legislative action that this subcommittee contemplates.

That ends the Chair's opening statement.

I now turn to the ranking member, the gentleman from New York, Mr. Towns for an opening statement.

Mr. TOWNS. Thank you very much, Mr. Chairman.

I am pleased, Mr. Chairman, to be at today's hearing, which will focus on an issue which is important to investors, to the security industry and to my home State of New York. In fact, I am the principal cosponsor of one of the bills under discussion today, H.R. 2441, the Fairness in Securities Transactions Act, which was authored by my good friend from New York, Congressman Rick Lazio.

The general issue before us today is whether the revenue from transaction fees imposed on the securities industry have become so burdensome that they are now an unfair tax on investors. Certainly in reviewing adjustments in transaction fees, we must be mindful of the impact of the operations of the Securities and Exchange Commission. No one, including the securities industry, believes that the Commission should function without an adequate budget. Additionally, we must ensure that any fee adjustments are budget-neutral.

Finally, Mr. Chairman, it is my hope that we will continue to discuss this issue in the context of the rapid growth of the securities markets and the great increase in the volume of trading. I look forward to hearing from our witnesses today as we attempt to address the important issue of transaction fee reduction.

On that note, Mr. Chairman, I will yield back.

Mr. OXLEY. I thank the gentleman.

Are there further opening statements?

The gentleman from New York Mr. Fossella.

Mr. FOSSELLA. I will ask unanimous consent to submit my opening statement for the record.

Mr. OXLEY. Without objection.

Mr. FOSSELLA. Mr. Chairman, I would just thank you for having this as a second hearing and to note that once again, we are all concerned about the tremendous growth in these fees. Essentially our goals are very simple: To ensure that the SEC continues to do a fine job of ensuring that our capital markets remain the most efficient and liquid in the world, and at the same time acknowledge that the growth in the market and the volume has just far exceeded what anybody expected.

That is why I want to compliment my distinguished colleague Mr. Menendez and I for introducing the legislation that would increase the cap on the fee. It is very straightforward and has 55 sponsors, 21 of whom are on this committee. I would also be willing to work with anybody to ensure that we cut this tax on capital, because that is exactly what it is that is passed on to the investors, and identify ways to fund the SEC, but at the same time understand that an unnecessary tax on capital is not good for the liquidity, not good for capital markets, and not good for investors.

With that, I yield back, Mr. Chairman.

[The prepared statement of Hon. Vito Fossella follows:]

PREPARED STATEMENT OF HON. VITO J. FOSSELLA, A REPRESENTATIVE IN CONGRESS  
FROM THE STATE OF NEW YORK

Mr. Chairman, I want to thank you for calling this important legislative hearing on Section 31 fees. I know that you have had a longstanding interest in this issue, and I commend you for your leadership on this and many other issues that are important to both securities professionals and ordinary investors in my district and across the United States. I share your commitment to addressing the issue of excessive Section 31 fees in a bipartisan, timely and meaningful fashion.

At the oversight hearing back in July, this Committee heard testimony from industry representatives and regulators that the government collected over \$1.75 billion in SEC fees last year, which is over five times the SEC's budget. The SEC performs an essential function—admirably I might add—of protecting the integrity of the U.S. capital markets, and helping them remain the deepest, most liquid and efficient in the world. *Having said that, there is simply no public policy rationale to justify such an excessive amount of user fee collections.* SEC fees have become a tax on capital formation and on securities trading. This large, hidden, and unintended tax is paid by all investors.

The legislation I have introduced with one of our distinguished witnesses this morning, Congressman Menendez of New Jersey, places a cap on the collection of Section 31 fees. Once the SEC collects a specific dollar amount, the fee shuts off. Our legislation, H.R. 1256, would cap SEC fees at levels closer to what was intended in 1996, when the various SEC fees were restructured. There are several advantages of a cap: One, there is certainty. The SEC, securities professionals, and investors would all know in advance the exact amount to be collected. Two, the cap would ensure that in years when actual dollar volume is greater than projected—a situation that has become a virtual certainty each and every year—there is an upside limit on the amount of fees that can be collected. I must also add that a fee cap, despite some claims to the contrary, can be administered without much difficulty.

Mr. Chairman, I am pleased that our bill has 55 cosponsors from both sides of the aisle, including conservatives, moderates and liberals—reflecting what I believe is the essentially nonpartisan, nonideological nature of this issue. I also want to thank my 20 colleagues on the Committee who have cosponsored H.R. 1256.

Since July's oversight hearing, my staff and I have been exploring various solutions to this excess fee problem. I believe that the essence of meaningful SEC fee reform is, very simply, to have a fee structure that raises enough revenue to cover the SEC's budget—and no more. And while some argue that a rate cut may be the most straightforward method of achieving a reduction in SEC fees, I am concerned that a rate cut alone will not fully address the fundamental problem with the current fee structure: that actual dollar volume growth in the markets has consistently outpaced—by significant amounts—CBO's and OMB's projections. Without some sort of mechanism that would provide for a correction during years in which actual fee collections exceed projections, a rate cut will not solve this serious problem. In

my view, given trends in the markets, dollar volumes will continue to grow at unprecedented rates. This will result in the government continuing to collect far more fee revenue than is needed to fund the SEC.

This situation led Mr. Menendez and me to opt for a cap on fee collections that is embodied in H.R. 1256. Now I want to again state for the record that what I am in favor of is real and meaningful reform that addresses the fundamental problem of a user fee operating as a hidden tax on capital. There are a number of ways in which this problem can be addressed, and I look forward to working with my colleagues on this Committee, as well as my colleagues in the Senate, to craft a legislative compromise that will accomplish the objectives of all interested parties—and one that can be enacted this year. However, I am concerned that unless any such compromise includes some sort of mechanism—whether it be a cap or otherwise—which ensures that taxpayers are not forced to pay more in fees than it costs to run the SEC, we will have failed to address the central problem.

Thank you again, Mr. Chairman, for holding this hearing. I look forward to the testimony from our distinguished panel.

Mr. OXLEY. I thank the gentleman for his leadership.

The gentleman from Michigan.

Mr. STUPAK. Thank you, Mr. Chairman. Thank you for holding this hearing and for the opportunity to have the hearing on the issue of transaction fees.

The fees at issue today are crucial to the efficient operation of our Nation's security markets. Set too high, the fees become a drag on our economy by making equity transactions more costly than other financial transactions. Set too low, the fees do not provide enough resources to the Securities and Exchange Commission, whose oversight of the market is crucial to its operation. Thus, the goals of the fee should be to provide ample resources to the SEC while not creating an undue burden on the equities market.

Mr. Chairman, this year the SEC is expected to collect over \$1.6 billion in fees. The SEC is funded at \$337 million. Clearly, the current fee is set higher than is required for the operation of the SEC. We are here to examine the best method to reduce fees at their appropriate level.

H.R. 2441, the Fairness in Securities Transaction Act, would reduce the level of the fee paid from the current  $\frac{1}{3000}$ th of a percent to  $\frac{1}{5000}$ th of a percent. The National Securities Market Act of 1996 would reduce these fees by 2007. This bill would reduce the fees quicker, to recognize current and expected trading volumes.

H.R. 1256, the Savings and Investment Relief Act of 1999, would set a minimum funding level for the SEC. At the point in the year the funding level is reached, the SEC would then stop collecting the fees.

Although I believe both bills are well-intended, I would have to support the approach taken by H.R. 2441. While I appreciate the increased certainty for a particular funding level under the approach taken by H.R. 1256, I believe its unintended consequences are great.

First, the exchanges have expressed concerns regarding their ability to create an affordable administrative structure necessary to collect the amount of fees collected with the precision required by H.R. 1256. Second, H.R. 1256 would tend to penalize traders before the cap was reached by making them more costly than one conducted afterwards. I do not believe it is appropriate government policy to make trades conducted in the beginning of the year more costly than those conducted at the end of the year. Furthermore,

it is unclear what effect this disparity would have on the efficient operation of our markets and our economy.

Mr. Chairman, I would like to work with you and Mr. Towns and Mr. Lazio to quickly pass H.R. 2441. I understand the problem with the bill, with the pay-go, according to the CBO, so I hope we can work with concerned parties to remedy the deficiencies.

Mr. Chairman, I will listen to our first witnesses, and then I have to run up to Health and Environment Subcommittee as we have some hearings going on there, so I will be bouncing back all day, but thank you again for the hearing and for the opportunity to make an opening statement.

Mr. OXLEY. Are there further opening statements?

[Additional statement submitted for the record follows:]

PREPARED STATEMENT OF HON. TOM BLILEY, CHAIRMAN, COMMITTEE ON COMMERCE

Mr. Chairman, I commend you for holding this hearing today. The Commerce Committee has been committed to ensuring that our markets operate as efficiently as possible. The increasing reliance by Americans on the securities markets for their retirement requires that Congress do everything possible to guarantee the integrity and efficiency of the markets.

To that end, the Commerce Committee moved legislation in 1996 (the National Securities Markets Improvement Act) that was enacted into law. That legislation reduced unnecessary regulatory burdens, improved the efficiency of the markets, and restored the fee structure to its original intent—cost recovery for regulating our securities markets.

Concerns that fees were no longer “user fees”, but had risen to be a tax on investors drove the change in the fee structure. Congress reduced the registration fee rate back to its statutory level to eliminate the excess fee revenue. Appropriators reliance on fee revenue as a funding mechanism was reduced. The outcome: the Securities and Exchange Commission had a more stable funding structure—a goal the Commission supported.

Because the markets have experienced phenomenal growth since enactment of the 1996 legislation, similar concerns regarding the fee structure have been raised again. I do not disagree that the fee problem persists. Congress agreed on the public policy benefits in 1996 when the revenue collected was double the cost of funding the SEC. Now revenue collection of these fees has *increased* to 5 times the cost of their Federal regulation. It is impossible to argue the current fee collection reflects the intent of the 1996 legislation. Overcharging American investors billions of dollars compels us to reexamine this issue.

I commend the Gentlemen from New York, Mr. Lazio, Mr. Fossella, and the Ranking Member of the Subcommittee, Mr. Towns, for their interest and commitment to addressing this problem. I look forward to hearing more about their proposals, as well as the views of the Commission.

Thank you, Mr. Chairman.

Mr. OXLEY. We then turn to our distinguished panel.

Let me invite to the witness stand our colleague from Long Island, the shy and retiring gentleman from Long Island, also a member of the committee, Mr. Lazio, and also the Honorable Robert Menendez from New Jersey. Both of you are welcome. Since you are a member of the committee, Mr. Lazio, we will begin with you.

**STATEMENT OF HON. RICK LAZIO, A REPRESENTATIVE IN  
CONGRESS FROM THE STATE OF NEW YORK**

Mr. LAZIO. Thank you very much, Mr. Chairman. Let me begin by thanking you for conducting these series of hearings, bringing in not just those of us who serve in the House, but also industry experts who have been commenting on this, and later on we will hear from the SEC. I want to thank Mr. Towns for his leadership on this issue and Mr. Fossella and Mr. Menendez for their commit-

ment to reducing these fees. I am so pleased that we have the attention of Mr. Ehrlich as well.

I want to say that this issue is one of great importance to American investors and to securities markets. As Mr. Stupak has mentioned, the amount of these fees now collected far exceed the purpose for which they were intended, the funding of the Securities and Exchange Commission. The excess fees represent a tax on capital formation, as Mr. Fossella has noted, and I want to say again how pleased I am that you have recognized it is time for Congress to revisit the issue of security transaction fees.

The two bills before us today will take two different approaches to this goal. I think this has already been referenced. H.R. 2441, the bill that myself and Representative Towns and others have sponsored, and that would reduce transaction fees from the current  $\frac{1}{3000}$ th of 1 percent to  $\frac{1}{5000}$ th of 1 percent. H.R. 1256, introduced by Congressmen Menendez and Fossella and others, provides for a continuation of the current fee rate with an annual cap on fees collected.

Mr. Chairman, I have been working on this for a couple Congresses. I have been tugging at your arm now to try and address this issue, and again I want to thank you for your concern.

Because of concerns raised about the compliance with the Budget Enforcement Act, I have made some revisions to my bill. Citing a memo provided to me yesterday from the Congressional Budget Office, which the Chairman, I think, has referenced, I quote that memo: "the draft legislation would not affect direct spending, but would increase revenues by \$1 million a year or less over the 2000 through 2004 period." In fact, the CBO preliminarily determined that H.R. 1256, which is based on a bill which was scored budget-neutral last year, would result in an annual loss in revenues on the order of tens of millions of dollars beginning in 2001, because the caps have not been revised in the bill. I think the importance of this new draft is that we now have a bill that scores neutral, according to the Congressional Budget Office.

The revised bill will maintain the same reduced rate of  $\frac{1}{5000}$ th of 1 percent while changing the allocation of fees collected between general revenues and offsetting collections.

I believe that this new bill provides the most workable approach to reducing securities transaction fees while maintaining the SEC's budget and not imposing burdensome new requirements on those involved in collecting the fees, securities firms, securities market and the SEC. Our bill is supported by all of the major securities and options markets, groups representing securities professionals, and major securities firms.

I would like to include in the hearing record a letter from these groups supporting this legislation, a letter dated July 26, 1999, and I would ask unanimous consent, Mr. Chairman, if that could be provided for the record.

Mr. OXLEY. Without objection.

[The information referred to follows:]

NEW YORK STOCK EXCHANGE, BOSTON STOCK EXCHANGE, CHICAGO STOCK EXCHANGE, NASDAQ STOCK MARKET, THE OPTIONS CLEARING CORPORATION, THE SPECIALIST ASSOCIATION, AMERICAN STOCK EXCHANGE, CHICAGO BOARD OPTIONS EXCHANGE, CINCINNATI STOCK EXCHANGE, PACIFIC EXCHANGE, SECURITIES INDUSTRY ASSOCIATION, MERRILL LYNCH & CO., INC., PAINEWEBBER INCORPORATED, PRUDENTIAL SECURITIES INCORPORATED  
*July 26, 1999*

The Honorable RICK LAZIO  
*U.S. House of Representatives*  
*Washington, D.C. 20515*

DEAR CONGRESSMAN LAZIO: On behalf of the above-listed organizations, we commend you for introducing H.R. 2441, the Fairness in Securities Transactions Act. This legislation will reduce fees on securities transactions while maintaining full funding for the Securities and Exchange Commission. The amount of fees now collected by the SEC greatly exceeds the SEC's appropriated budget. We believe that fee revenues in excess of the SEC's budget represent a tax on capital which penalizes investors and businesses and puts the U.S. securities markets at a competitive disadvantage. As organizations involved in the payment and collection of securities transaction fees, or who represent the market professionals who pay such fees, we have a strong interest in bringing the fees paid more into balance with the appropriated budget of the SEC. We applaud your leadership in developing this legislative approach, which we believe will address the issues raised by the Budget Act in the consideration of fee reduction legislation.

Your bill is equitable to investors and easy to administer. We also believe that your bill will resolve concerns that have been raised about Budget Act problems and will maintain full funding for the SEC, a high priority for U.S. securities markets and market participants.

We also believe that H.R. 2441 is consistent with the approach taken in the National Securities Markets Improvement Act of 1996 (NSMIA). NSMIA restructured various SEC fees with the intention of creating a predictable funding source for the SEC and reducing, over time, the fees collected by the SEC. This legislation extended the transaction fee to Nasdaq-traded securities and provided that the fee will be reduced from the current  $\frac{1}{300}$  of one percent to  $\frac{1}{500}$  of one percent in fiscal year 2007.

NSMIA was intended to bring SEC fee collections more in line with the level of funding appropriated by Congress. This goal has been thwarted, however, because market averages have greatly increased to levels unforeseen in 1996, and trading volume has increased substantially since that time. As a result, actual collections of transaction fees are significantly exceeding the levels projected during consideration of NSMIA, and they are projected to do so into the future. The revenue generated by Section I transaction fees alone in fiscal year 1998 was \$476 million, which exceeded the SEC's entire appropriated budget of \$315 million. In fiscal year 1999, total SEC fee collections are expected to exceed \$1.6 billion, more than four times the Commission's appropriated funding of \$337 million.

Fees collected in excess of the cost to the government of the supervision and regulation of securities markets and professionals are in contradiction of the clear and unambiguous Congressional intent expressed in Section 31(a) of the Securities Exchange Act of 1934. Section 31(a), which was added as part of NSMIA, clearly states Congress's intent that transaction fees be used solely to recover SEC operating costs.

Again, we commend your recognition of this problem and your leadership in introducing this important legislation. We hope that early hearings can be held on this bill, and we look forward to working with you throughout the legislative process.

Sincerely yours,

NEW YORK STOCK EXCHANGE, BOSTON STOCK EXCHANGE, CHICAGO STOCK EXCHANGE, NASDAQ STOCK MARKET, THE OPTIONS CLEARING CORPORATION, THE SPECIALIST ASSOCIATION, AMERICAN STOCK EXCHANGE, CHICAGO BOARD OPTIONS EXCHANGE, CINCINNATI STOCK EXCHANGE, PACIFIC EXCHANGE, SECURITIES INDUSTRY ASSOCIATION, MERRILL LYNCH & CO., INC., PAINEWEBBER INCORPORATED, PRUDENTIAL SECURITIES INCORPORATED

Mr. LAZIO. Thank you.

For some time now, the SEC has been collecting securities transactions fees and other fees far in excess of its budget which is provided through congressional appropriations. This fiscal year, total

SEC fee collections are expected to exceed \$1.6 billion, more than four times the SEC's budget of \$337 million.

These fees are paid directly by American investors when they trade securities. Any fee reduction will benefit directly the more than 70 million investors who hold stocks individually or through professionally managed investments such as mutual funds and 401(k) plans. Excess transaction fees represent an indirect tax on investors, many of which you know, Mr. Chairman, are of modest income and modest means.

I favor a strong and effective Securities and Exchange Commission, and I know that the securities industry has always supported full funding for the SEC, but it is not fair to have ordinary investors pay more than four times the cost of government regulation.

Congress certainly did not intend for SEC fee collections to so greatly exceed the SEC's budget. When Congress passed the National Securities Markets Improvement Act in 1996, it included the statement that transaction fees are designed to recover the costs to the government of the supervision and regulation of securities markets. But increased trading volume and increased stock prices, unforeseen even 3 years ago, have driven fee collections to record levels.

NSMIA also provided for the eventual reduction of the transaction fee to  $\frac{1}{8000}$  of 1 percent for fiscal year 2007, but that is too long to delay fee relief and too much time to pay \$1 billion a year more than the cost of industry regulation. We need an interim reduction now, as provided in my bill, so that this money can be more productively used in the U.S. economy. American investors deserve congressional action in the near future. I hope this hearing will be the beginning of a process to continue to implement important changes to the SEC's fee structure begun by Chairman Bliley and Chairman Oxley with the passage of NSMIA in 1996.

In conclusion, I just want to compliment again my colleague Mr. Fossella. We have a difference of ideas that we offer to the committee, but it certainly reflects no difference among each of our positions in terms of the need to reduce these fees for a more fair allocation for consumers and investors, and so it does not reflect at all on our personal relationship, which I am proud to say is very strong.

Thank you, Mr. Chairman.

[The prepared statement of Hon. Rick Lazio follows:]

PREPARED STATEMENT OF HON. RICK LAZIO, A REPRESENTATIVE IN CONGRESS FROM  
THE STATE OF NEW YORK

Mr. Chairman, I thank you for calling this hearing today on legislation to reduce securities transaction fees. This is an issue of great importance to American investors and to the securities markets. The amounts of these fees now collected far exceed the purpose for which they were intended—funding the Securities and Exchange Commission. These excess fees represent a tax on capital formation. I am pleased that you have recognized that it is time for Congress to revisit the issue of securities transaction fees.

There are two bills before us today which take two different approaches to this goal. H.R. 2441, the Fairness in Securities Transactions Act, which Mr. Towns and I have introduced, along with a number of other Committee members, reduces transaction fees from the current  $\frac{1}{3000}$  of one percent to  $\frac{1}{5000}$  of one percent. H.R. 1256, introduced by Congressmen Menendez and Fossella and others, provides for continuation of the current fee rate, with an annual cap on fees collected.

Because of concerns raised about compliance with the Budget Enforcement Act, I have made some revisions to my bill. Citing a memo provided to me yesterday from the Congressional Budget Office, "the draft legislation would not affect direct spending but would increase revenues by \$1 million a year or less over the 2000-2004 period." In other words, this legislation has no revenue loss—this is a slight revenue gain. In fact, the CBO preliminarily determined that H.R. 1256, which is based on a bill which was scored budget-neutral last year, would result in an "annual loss in revenues . . . on the order of the tens of millions of dollars beginning in 2001" because the caps have not been revised in the bill.

My revised bill will maintain the same reduced rate of  $\frac{1}{5000}$ th of one percent, while changing the allocation of fees collected between general revenues and offsetting collections.

I believe that my revised bill provides the most workable approach to reducing securities transaction fees while maintaining the SEC's budget and not imposing burdensome new requirements on those involved in collecting the fees—securities firms, securities markets, and the SEC.

My bill is supported by all the major securities and options markets, groups representing securities professionals, and major securities firms. I would like to include in the hearing record a letter from these groups supporting this legislation. (Letter of July 26, 1999, attached at end)

For some time now the SEC has been collecting securities transaction fees, and other fees, far in excess of its budget, which is provided through Congressional appropriations. This fiscal year, total SEC fee collections are expected to exceed 1.6 billion dollars, more than four times the SEC's budget of 337 million dollars.

These fees are paid directly by American investors when they trade securities. Any fee reduction will benefit directly the more than 70 million investors who hold stocks individually or through professionally managed investments such as mutual funds and 401(k) plans. Excess transaction fees represent an indirect tax on investors.

I favor a strong and effective Securities and Exchange Commission, and I know that the securities industry has always supported full funding for the SEC. But it is not fair to have ordinary investors pay more than four times the cost of government regulation.

Congress certainly did not intend for SEC fee collections to so greatly exceed the SEC's budget. When Congress passed the National Securities Markets Improvement Act (NSMIA) in 1996, it included the statement that transaction fees are designed to recover the costs to the government of the supervision and regulation of securities markets. But increased trading volume and increased stock prices, unforeseen three years ago, have driven fee collections to record levels.

NSMIA also provided for the eventual reduction of the transaction fee to  $\frac{1}{5000}$ th of one percent in fiscal year 2007. But that is too long to delay fee relief and too much time to pay one billion dollars a year more than the cost of industry regulation. We need an interim reduction now, as provided in my bill, so that this money may be more productively used in the U.S. economy. American investors deserve Congressional action in the near future.

I hope this hearing will be the beginning of a process to continue to implement important changes to the SEC's fee structure begun by Chairman Bliley and Chairman Oxley with the passage of NSMIA in 1996.

Mr. OXLEY. I thank the gentleman.

Now, Mr. Menendez.

**STATEMENT OF HON. ROBERT MENENDEZ, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW JERSEY**

Mr. MENENDEZ. Thank you, Mr. Chairman. I want to thank you and Mr. Towns for holding this hearing. I know there are a lot of pressing matters you would all like to see accomplished by the end of the session, so I appreciate how seriously you have taken up this issue.

For more and more Americans from all walks of life, the securities market has become a major vehicle for savings and investment. And while we in Congress sometimes have honest disagreements about how to accomplish those goals, we all agree that encouraging savings and investment is essential. That is why what has hap-

pened with section 31 fees in recent years is a trend we need to address.

These fees were intended by Congress to cover the operating expenses and costs of the Securities and Exchange Commission, and that is a necessary and valid purpose which I totally, and I know Congressman Fossella and all of us for that matter, totally support. Consumers and investment firms benefit from the market, and it is not unreasonable to ask market participants to help pay the costs of the very agency that ensures that the market runs efficiently. However, it is not reasonable to have these participants pay fees that amount to five times the funding necessary to keep the SEC operating. That is no longer a fee, it is a tax.

That is why Congressman Fossella and I introduced the Savings and Investment Relief Act, H.R. 1256. It is nearly identical to a bill which I introduced in the last Congress with Jerry Solomon, the distinguished former Chairman of the House Rules Committee.

Our approach is straightforward. It simply caps section 31 fees once they have reached the amount necessary to ensure the SEC is fully funded. We base that amount on the deal reached in 1996 as part of the National Securities Markets Improvement Act; in other words, the amount the Congress originally intended. We then added an additional cushion of \$20 million per year. Finally, even beyond that cushion, the cap is adjustable if the SEC's needs require it, but keep in mind that for the SEC's needs to go beyond the base cap and the cushion, it would need to have a rather significant increase in its budget needs. That is why our bill, I believe, has broad bipartisan support with 505 cosponsors, 21 of whom are on the Commerce Committee, and several of whom are members of the House Democratic and Republican leaderships.

There are those who believe that a transaction fee rate cut has advantages over the cap Mr. Fossella and I propose because they argue a rate cut would provide a uniform fee collection throughout the year and because a cap could cause market participants to make decisions based on when the cap would kick in, thus destroying the market. I would like to address those two major points. Let me take the second one first.

It is not supportable to argue that section 31 fees would distort a multi-trillion-dollar marketplace. For instance, on a \$15,000 stock trade, the fee is less than 50 cents. Investors make decisions based on the conditions of the market and the performance of stocks. The price fluctuation of stock prices will dwarf the cost of these fees. They are important in the aggregate, that is why we are all concerned about it, but at these levels are simply not decisive, I believe, in any individual transactional situation.

Now, let me take the other point. I argue that it is actually the rate cut proposal that lacks predictability. That is because if the CBO overestimates the market growth rate, we may find at the end of the year that the fees have not generated the amount necessary to fully fund the SEC, and it will be too late in the process to correct it. Conversely, if the CBO underestimates the growth rate, we will soon be right back where we are today, trying to seek some other form of relief before the committee. Given that the CBO has, understandably, rarely predicted the market accurately, and has usually used overly conservative assumptions of market dollar

volume growth that have significantly understated actual collections, this is a problem that the rate proposal has that the Committee needs to consider.

This situation has been and may be further exacerbated as technological innovations, online investing, greater participation, the growth of mutual funds, and changes in the market structure spur even greater and unanticipated dollar volume growth rates. So unless there is some sort of an adjustment mechanism installed that accounts for dollar volume growth rates which differs significantly from the CBO projections, a mechanism that may be very difficult to develop given market volatility, the current rate proposal will not solve the problem. And, of course, if we do consider adding an adjuster, which I think is one that will seriously have to be considered if that is the process by which the committee decides to adopt, one of the key benefits of the rate cut proposal, namely uniform collections throughout the year, is undermined, begging the question of why the cap is not better suited to solve the problem in the first place. That is why I argue that it is the cap that best provides predictability and certainty for both consumers and the SEC. Let us solve the problem without having to revisit it.

Last, Mr. Chairman, let me say that while that is my strongly held opinion that I share with Mr. Fossella, having worked on this issue over the last two Congresses, I want to stress the similarity of purpose we share with our colleagues, Mr. Towns and Mr. Lazio, who support the rate cut proposal. Ultimately, our goal is relief for the investor, relief for the industry, and insuring the SEC's very valid purpose. That is all—all of those are our mutual goals. We want to make sure, however, that we give that type of relief, and we look forward to working with you, Mr. Chairman, and the leadership of the committee and our colleagues to try to accomplish that goal.

[The prepared statement of Hon. Robert Menendez follows:]

PREPARED STATEMENT OF HON. ROBERT MENENDEZ, A REPRESENTATIVE IN  
CONGRESS FROM THE STATE OF NEW JERSEY

Thank you, Mr. Chairman and Mr. Towns for calling this hearing. I know there are a lot of pressing matters you would like to move on before the end of the session, so I appreciate how seriously you have taken this issue.

For more and more Americans, from all walks of life, the securities market has become a major vehicle for savings and investment. And while we in Congress sometimes have honest disagreements about how to accomplish this goal, we all agree that encouraging savings and investment is essential.

That's why what has happened with Section 31 fees in recent years is a trend we need to address.

These fees were intended by Congress to cover the operating costs of the Securities and Exchange Commission. And that is a necessary and valid purpose which I totally support. Consumers and investment firms benefit from the market—it is not unreasonable to ask market participants to help pay the costs of the very agency that ensures that the market runs efficiently.

However it is *not* reasonable to have these participants pay fees that amount to five times the funding necessary to keep the SEC operating. That is no longer a fee—it is a tax.

That's why Congressman Vito Fossella and I introduced the Savings and Investment Relief Act, H.R. 1256. It is nearly identical to a bill I introduced in the last Congress with Jerry Solomon, the distinguished former Chairman of the House Rules Committee.

Our approach is straightforward. It simply caps Section 31 fees once they have reached the amount necessary to ensure the SEC is fully funded. We base that amount on the deal reached in 1996, as part of the National Securities Markets Im-

provement Act—in other words, the amount the Congress *originally intended*. We then added an additional cushion of \$20 million per year. Finally, even beyond that cushion, the cap is adjustable if the SEC's needs require it—but keep in mind that for the SEC's needs to go beyond the base cap *and* cushion, it would need to have a huge and unlikely increase in its budget needs.

That's why our bill has broad bi-partisan support with 55 co-sponsors, 21 of whom are on the Commerce Committee, and several of whom are Members of the House Democratic and Republican Leaderships.

There are those who believe that a transaction fee rate cut has advantages over the cap Mr. Fossella and I propose because, they argue, a rate cut would provide a uniform fee collection throughout the year, and because a cap could cause market participants to make decisions based on when the cap would kick in, thus distorting the market.

To take the second point: It is not supportable to argue that Section 31 fees would distort a multi-trillion dollar marketplace. For instance, on an over \$15,000 stock trade, the fee is less than 50 cents. Investors make decisions based on the conditions of the market and the performance of their stocks. The price fluctuation of stock prices will dwarf the cost of these fees; they are important in the aggregate, but, at these levels, are simply not decisive in any individual transactional situation.

And on the first point: I argue that it is actually the *rate cut* proposal that lacks predictability. That's because if the CBO *overestimates* the market growth rate, we may find at the end of the year that the fees have not generated the amount necessary to fully fund the SEC—and it will be too late in the process to correct it. Conversely, if the CBO *underestimates* the growth rate, we'll soon be right back where we are today.

Given that the CBO has, understandably, rarely predicted the market accurately, and has usually used overly-conservative assumptions of market dollar volume growth that have significantly understated actual collections, this is a problem with the rate cut proposal worth considering.

This situation has been, and may be further exacerbated as technological innovations, online investing, greater participation, the growth of mutual funds, and changes in the market structure spur ever greater and unanticipated dollar volume growth rates. So unless there is some sort of "adjuster mechanism" installed that accounts for dollar volume growth rates which differ significantly from CBO projections—a mechanism which may be difficult to develop given market volatility—the current rate cut proposal will not solve the problem.

Of course, by adding an adjuster, one of the key benefits of the rate cut proposal—namely uniform collections throughout the year—is undermined, begging the question of why the cap is not better suited to solve the problem in the first place.

That is why I argue it is the cap that best provides predictability and certainty for both consumers and the SEC. Let's solve this problem without having to revisit it.

Of course, while that it is my strongly held opinion—having worked on this issue over two Congresses—I want to stress that the similarity of purpose I share with my colleagues who support the rate cut proposal, is far greater than the differences of method that separate our bills. This is especially true of my colleagues Mr. Towns and Mr. Lazio, who have worked very hard on this issue on behalf of America's investors and savers. I thus look forward to working with them, this Committee, my Leadership, and with all interested and involved parties, to find a fair and workable solution to the problem of these excess fee collections.

Thank you.

Mr. OXLEY. Thank both of you for your excellent testimony.

Let me begin with both of you and ask, there has been some discussion that perhaps we could meld the two approaches legislatively; that is, to follow the concept of reducing the fees, and yet have an overall cap at the same time that would protect us both on the short end and the long end.

Do you have any comments in that regard, and particularly if that is agreeable, how do we get from here to there to be able to put that together, just mechanically?

Mr. LAZIO. Mr. Chairman, let me comment on that, if I can, because I was here when we received some testimony suggesting that perhaps a blend might not be inappropriate.

We have, subsequent to that, made this change in the bill which did speak to the issue of scoring and the Budget Enforcement Act, which was a problem. Mr. Stupak had referenced it in terms of getting a waiver, and I think we have now made the adjustments so a waiver is no longer necessary.

In my opinion, and I, like Mr. Menendez, would support either of these methodologies if it was these two or nothing, but I think that with the change that has been made, building on the rate reduction or the rate fee that was set back in the 1996 act with the rate reduction set to kick in in 2007, there is more equity in terms of investor participation. Whether you trade early or trade late in the year, it seems to me you should not be punished by paying excessive fees as an investor simply because you ended up trading earlier in the year. You have 70 million investors that now participate in the market, either through mutual funds or retirement plans or through direct investment. It seems to me as well for SEC, it is not inappropriate to ask the SEC to be both authorized and appropriated through this Congress, that the Congress has an oversight rule over the SEC which it should diligently discharge.

So while this version, this revised version, continues to speak to an offset, a 9.5 percent offset, I think in terms of overall fairness and in terms of ensuring that there is adequate cash-flow, that this revised bill is superior to a blend or to H.R. 1256.

Mr. OXLEY. I did not hear the last part.

Mr. LAZIO. I think my position would be that the revised bill is a superior version to either a blend of the two versions or, if I have the number, Mr. Menendez and Mr. Fossella's bill, I think it is H.R. 1256. I am not sure if it was a matter of compromise, I think, for the sake of getting the votes, that would be certainly something that I would not stand in the way of, but if it was a matter of just currently what is the best vehicle for getting the reduction and getting relief to the investors, I think an across-the-board, year-long rate reduction is the fairest and most effective thing to do.

Mr. OXLEY. Mr. Menendez.

Mr. MENENDEZ. Mr. Chairman, I would just say, again, we have mutual goals, but let me just point out this to the committee. No. 1 is one of the things that we seek to do through our legislation is to create predictability, and the fact of the matter is, once you blend and you have an adjuster clause, which I think is needed under any set of circumstances if you adopt Mr. Lazio's approach, then one of the major advantages of Mr. Lazio's and Mr. Towns's bill is somewhat undermined, which is that you have uniform collections throughout the year. The mere fact if you have an adjuster actually that has to kick it, it really does not provide for that uniform collection throughout the year, which begs the question of why have the cap in the first place.

Second, I believe that our fee cap actually creates predictability, creates predictability for the budgeteers, it creates predictability for the SEC. And as I understand, part of what you will hear from the SEC today on both of these bills is they are concerned about the funding as it relates to them, and ours clearly provides insurance for them that their budget will be met, plus. So therefore, while we are certainly open to compromise, we question whether the nature of it in the first place doesn't beg the question as to the rate cap

being the more appropriate way to go on pay-go issues, on the question of predictability, and on the question that if you have an adjuster at the end of the day, don't you provide for the uncertainty that some are concerned about in terms of our legislation, because at some point the fee will be obviously adjusted so that, in fact, you can meet the necessity of the SEC.

So therefore, this argument about long-term, steady, one rate under the Lazio proposal is somewhat undermined at the end of the day.

Mr. LAZIO. Mr. Chairman, if I could just respond briefly. There is a reason why all of the stakeholders, basically all the stakeholders, are supporting the approach of H.R. 2441 with Mr. Towns and myself, and I would say with all due respect to Mr. Menendez that the revised edition, which includes a 9.5 percent offsetting revenue for the SEC, is no different than the current version and creates no new cap that would be similar to the version that would be supported by Mr. Menendez. It simply is an adjustment that would allow us to score budget-neutral, and it is based on the CBO conferences that we have had.

Mr. OXLEY. Thank you.

The Chair's time has expired.

The gentleman from New York Mr. Towns.

Mr. TOWNS. Thank you very much, Mr. Chairman.

Let me ask Mr. Menendez, how do you respond to the fact that if you trade early, you know, you have to pay the fee, and if you trade late, you are not penalized? I mean, how do you respond to that?

Mr. MENENDEZ. Well, Mr. Towns, I would just simply say what I said earlier, that transaction fees that are substantial in the aggregate, all of the fees that are collected, which is why we are all concerned in the first place, because it far exceeds the need of the SEC, in essence, it is a tax, they are relatively small as a result of an individual trade, as a percentage of an individual trade. So I think it is unlikely that sellers would time their trades until after the fee shuts off. Stocks are sold primarily for other reasons: a declining or increasing market, to lock in capital gains, to free up cash. So I think investors are also not likely to risk having the value of their holdings decline while waiting for the fee to shut off.

Moreover, the cap would only serve to reduce the tax on capital, and any reduction would simply benefit investors. As a matter of fact, this concept of an annual cap is not necessarily a new concept. It might be new in the context of the SEC, but we already have it under the Oil Spill Liability Trust Fund.

So I think that, in fact, we have an opportunity that will, in terms of the individual trade, not affect anybody's judgment. People are going to make those judgments for other reasons in the marketplace, and at the end of the day, all investors are benefited because once we have the fee cap, we have no greater collection of that fee for the rest of the year, and I don't think that that is going to disproportionately affect any individual trade in the context of the small percent. I mentioned earlier in my testimony, for example, for the \$15,000 trade, we are talking about 50 cents. That is not going to make somebody decide whether or not they are going to

move their trade in order to make sure they take care of whatever the market conditions are at the time.

Mr. TOWNS. Let me ask you, what is your problem with the other bill?

Mr. LAZIO. Well, I would say, Mr. Towns, that there are four or five issues, I think, that separate the two bills. One is the equity issue. I agree with Mr. Menendez that this would not likely result in market distortions in terms of people making decisions about wanting to invest. I think it is an equity issue, though. The equity issue is why should somebody who trades later in the year have to pay a different price than someone who trades earlier in the year? Why should they pay a higher tax? It seems like it is just patently unfair to investors to fix this tax based on the timing of their decision.

Second of all, it is an easier bill to implement. It does not require additional regulation; it does not require costly computer reprogramming or other administrative costs by securities firms, and those are collected fees, stocks or options exchanges, NASD; it would not require monitoring or rebates relevant in class action litigation if the cap is not properly administered. Third of all, it is consistent with NSMIA, the current law that we operate under, which reduces the transaction fee to  $\frac{1}{8000}$  of 1 percent effective in the year 2007.

Our version would simply accelerate the rate reduction already approved by Congress in 1996 and would not impose any new system which would be in effect for only a limited time. As I said before, no extensive rulemaking authority for the SEC would be granted as a result of this bill, and it maintains funding for the SEC, full funding for the SEC, generous funding overall, scores out at neutral, zero, so we have no Budget Enforcement Act issue, and I think that is the reason why you have every major exchange, every major stakeholder supporting the version which you have been the prime cosponsor.

Mr. TOWNS. All right. Thank you very much, Mr. Chairman. My time has expired.

Mr. OXLEY. I thank the gentleman.

The gentleman from New York Mr. Fossella.

Mr. FOSSELLA. Thank you, Mr. Chairman. I want to also compliment both Mr. Towns and Mr. Lazio for being at the vanguard of this debate.

I guess to use the analogy, Mr. Menendez and I want to run the ball down the field, and you want to throw the ball down the field, but we both want to score, and perhaps we can, I am sure Mr. Menendez would agree, form an offensive pattern, combining both the run and the throw, and at the end of the day, we will score that touchdown. So I want to compliment you on that.

I guess what, Mr. Chairman, what you alluded to earlier is the other parts to this game, the budgeteers and the authorizers and the appropriators. I guess integral to this is also the fact that the Chairman of the SEC Mr. Levitt testified before this hearing a couple of months ago that he would support a cap, or, if I heard him correctly, prefer that to the other. I assume that is still true. I have not heard anything to the contrary.

So I guess what we are trying to do is put a lot of different pieces together. We all understand, this is important to me as it is to Mr. Menendez and Mr. Lazio and Mr. Towns, because so many of the people are constituents or work for the financial service industry, are affected directly by any tax on capital, but again, the more important issue is across this country there are more than 70 million investors that are adversely affected by an unnecessary and, I think, a repugnant tax.

So I would just throw out the question that if we can somehow find that solution, perhaps it is a combination of the two, and that is fine, but I still think the intent of the legislation is to cap, or to fund the SEC with a degree of certainty. If that is the intent, then we should try everything we can to ensure that the SEC is appropriately funded. How we again combine those run and pass patterns, I am open-minded about, but I still think, as Mr. Menendez said, this provides the highest degree of predictability and certainty, which Congress is pursuing to fund the SEC.

I yield back, Mr. Chairman.

Mr. OXLEY. The gentleman yields back. Are there further questions?

The gentleman from Minnesota.

Mr. LUTHER. Thank you, Mr. Chairman. Just a couple of quick questions. Again, thanks for your excellent presentations.

One of the arguments, as I understand it, for doing this is because there is, in effect, discrimination against this form of investment versus other forms of investment. If we have an inordinately high tax, or whatever, even if it is as small as has been said here, has there ever been an attempt to quantify what is called discrimination by looking at the taxes, subsidies on various forms of investment; has that ever been quantified? I have seen the argument presented, but I am just wondering if there is anything to quantify that.

Mr. LAZIO. I am not aware of it, Congressman. I think right now we are at \$1.6 billion in terms—\$1.66 billion in terms of what fees are collected for the SEC's current budget, which is \$337 million, and current offsetting revenues of \$501 million. So it is far in excess, obviously, of over four, four and a half times of what is necessary to fund the SEC, and it doesn't just hit the big guys, it hits the smaller investors, and we have sort of evolved from the Nation of savers to a Nation of investors. So those of us who have blue-collar districts with people who invest or are trying to have some pension security or retirement security through the stock market, they are affected by this. Everybody is affected by this, and it seems as a basic issue of equity that we reduce the amount of fees to more closely proximate, but still far exceed, the cost of the SEC operation.

Mr. LUTHER. Just one other question. Has there ever been an attempt to quantify other expenses related to securities other than just the cost of the SEC, for example?

Mr. LAZIO. It includes transactional fees. I wouldn't know the answer to that, quite frankly. I would not be surprised at all if either the committee staffs or GAO would have some answer to that, or the SEC itself.

Mr. MENENDEZ. If I might, I would like to go to the first question and just for the Committee's consideration impose what your question, I think, inherently implies. No. 1, as has been said, this is almost five times as much. It is supposed to be as the SEC presently needs. It is supposed to be a fee. That was what the 1996 agreement was all about, was to fund the SEC, make sure that its vital role is fully funded, and for what it is doing and maybe even for an expanded role within that context. The bottom line is it is not supposed to be a tax.

In essence, the committee, in its consideration, I would say, has to consider whether or not, if the section 31 fees are going to be used for, which, in essence, they are, for programs outside of the Securities and Exchange Commission, then obviously even jurisdictionally it would change the nature of the fees, and, in fact, a fee to a tax, and it might even very well be considered something that the Ways and Means Committee would consider.

So I would hope that at the end of the day, and I think this is where the Chair and the ranking member and others are headed, that the committee clearly doesn't insure or justify the deleting of the section 31 fees with the funding of the SEC. It should be a user fee and not a tax, and, in fact, at the end of the day, if that is the course the committee takes, then we will have fully met what all of us in 1996 voted for the purpose of the act in the first place, which was to have a fee that funded the SEC and does not in essence use it as a tax for a variety of other programs, including programs that are outside of the jurisdiction of the committee.

Mr. LUTHER. I yield back, Mr. Chairman. Thank you.

Mr. OXLEY. Are there further questions for the distinguished panel?

Thank you both for an excellent presentation.

Mr. OXLEY. We will now call up the second panel, which is made up of Executive Director James McConnell from the Securities and Exchange Commission. Mr. McConnell, welcome to the panel. You may begin whenever you want to.

**STATEMENT OF JAMES M. McCONNELL, EXECUTIVE  
DIRECTOR, SECURITIES AND EXCHANGE COMMISSION**

Mr. McCONNELL. Thank you, Mr. Chairman.

Chairman Oxley, Ranking Member Towns and members of the subcommittee, I appreciate this opportunity to appear today on behalf of the Securities and Exchange Commission regarding securities transaction fees. The SEC's fee collections have been a subject of concern ever since 1983 when the Commission first began contributing more to the U.S. Treasury than was required to fund the agency.

In 1996, the National Securities Markets Improvement Act mandated a fee structure designed to do four things: Gradually reduce total fee collections; extend transaction fees to the over-the-counter market instead of only exchange-listed securities; provide the SEC with a stable, long-term funding structure; and gradually align fee collections with the funding needs of the SEC.

Today, market growth and activities have pushed fee collections much higher than anticipated in 1996, far beyond what is needed to fund the agency. But we believe the key phrase in this is what

is needed to fund the agency. As was evident at a hearing last March before the Senate Subcommittee on Securities and also at a hearing held last July by this subcommittee, all parties to this discussion seemed to share the goal of ensuring that the SEC is fully funded and that it is appropriate for fee collections to cover the cost of the services and regulation that we provide for the industry.

NSMIA has succeeded in eliminating the funding uncertainties that plagued the SEC for years, but it has failed to reduce total collections. Efforts to undertake a further comprehensive reduction in fees have been restricted by several factors, primarily the Budget Enforcement Act. As you know, the BEA splits our fee collections into two different categories, mandatory and discretionary. The mandatory receipts by law must be deposited into the Treasury, while the discretionary collections are available to our appropriators to fund the agency.

House Resolutions 2441 and 1256 have been creatively crafted to reduce fees and accommodate the restrictions on the BEA. The result, however, is that the entire amount of the fee reduction in both proposals comes from the 30 percent of total fee collections that is currently available to the appropriations committees to fund the SEC. The original version of H.R. 2441 would reduce the amount available to offset appropriations by approximately \$2.6 billion over 7 years, and H.R. 1256 will reduce it by \$2 billion over the same period.

We are concerned that reductions of this size could seriously jeopardize the SEC's funding.

In this current environment of tremendous activity and change, it is imperative that funds be available to support both current levels and much-needed increases in resources. Any funding structure, whether it is implemented by a cap or a rate reduction or some other mechanism, must provide for full and stable long-term funding that allows the agency to adequately protect investors.

I welcome this discussion on fee collections. Thank you for inviting me, and I ask that my written testimony be submitted for the record. Before moving to questions, however, I would like to point out that subsequent to our preparation of the written testimony, we received a revised version of H.R. 2441. We understand that this version satisfies the scoring problems that we referred to in the written testimony. There are some other changes, including timing, that we need to analyze, and I am prepared to discuss the new proposal today. However, we believe that it still does not ensure full and stable long-term funding for the SEC.

I would be happy to answer any of your questions at this time.  
[The prepared statement of James M. McConnell follows:]

PREPARED STATEMENT OF JAMES M. MCCONNELL, EXECUTIVE DIRECTOR, U.S.  
SECURITIES AND EXCHANGE COMMISSION

Chairman Oxley, Ranking Member Towns, and Members of the Subcommittee: On behalf of the Securities and Exchange Commission (SEC or Commission), I appreciate this opportunity to appear before the Subcommittee today to discuss securities transaction fees and current proposals to address the issue of fee collections in excess of the cost of funding the SEC. The SEC shares the Subcommittee's concern regarding excess fee collections. The existing fee structure, last revised in 1996, was the product of many years of negotiations, involving many players with competing interests. However, tremendous market growth in recent years has pushed fee col-

lections far beyond the levels anticipated during those negotiations. The SEC welcomes an inclusive and reasoned dialogue on potential solutions to the problem of excess fee collections.

Given the complexity of the fee collection issue, I will first review the history of SEC fees, the fee agreement contained in the National Securities Markets Improvement Act of 1996 (NSMIA), the Budget Enforcement Act (BEA), and SEC's efforts to address fee issues before addressing the current proposals.<sup>1</sup>

#### *History of Fees*

Federal securities laws direct the Commission to collect three different types of fees: registration fees, transaction fees, and fees on mergers and tender offers. Securities registration fees (Section 6(b) fees) are paid by corporations and investment companies when they register securities for sale. These were first enacted at a rate of  $\frac{1}{500}$ th of 1 percent under Section 6(b) of the Securities Act of 1933. Starting in 1990, the Section 6(b) fee rate was increased yearly through the appropriations process. The first  $\frac{1}{500}$ th of 1 percent goes directly to the U.S. Treasury and is unavailable for funding the SEC. The amount over the  $\frac{1}{500}$ th of 1 percent (called offsetting collections) can be used to fund the agency through appropriations.

Transaction fees (Section 31 fees) are paid when securities are sold. These were enacted at a rate of  $\frac{1}{3000}$ th of 1 percent on exchange-listed securities under Section 31 of the Securities Exchange Act of 1934 (Exchange Act). Proceeds from this fee are deposited directly in the U.S. Treasury and are not available to fund the agency.

Fees on mergers and tender offers are paid by corporations directly to the U.S. Treasury and also are not available to fund the agency.

The SEC's fee collections have been a subject of concern since 1983, when the Commission first began contributing more to the U.S. Treasury than was required to fund the agency. In 1988, the Securities Subcommittee of the Senate Committee on Banking, Housing, and Urban Affairs requested that the SEC examine its fee collections and funding structure. The report prepared by the SEC in response to this request was the first step in the process that eventually led to the compromise reached in Title IV of NSMIA.<sup>2</sup>

#### *Fee Agreement in NSMIA*

Title IV of NSMIA mandates a fee structure that was the result of extensive negotiations between six different Congressional Committees, the Administration, and the SEC.

In general, the NSMIA fee structure was designed to:

- gradually reduce total fee collections;
- "level the playing field" by extending Section 31 transaction fees, which had previously only applied to transactions involving exchange-listed securities, to securities subject to "last sale reporting" in the over-the-counter (OTC) market;
- gradually align fee collections with the funding needs of the SEC; and
- provide the SEC with a stable, long-term funding structure.

NSMIA set in motion a gradual reduction in Section 6(b) registration fee rates over a ten-year period intended to more closely align fee collections with the funding needs of the SEC. Specifically, NSMIA authorized the Commission to collect securities registration fees at the rate of  $\frac{1}{500}$ th of 1 percent of the aggregate offering price in fiscal year 2006, declining annually from  $\frac{1}{340}$ th of 1 percent in 1998. In fiscal year 2007, the rate will be further reduced to  $\frac{1}{1500}$ th of 1 percent. In addition, NSMIA classified the portion of the Section 6(b) fees in excess of  $\frac{1}{500}$ th of 1 percent (*i.e.*, the portion declining from 1998 to 2006) as offsetting collections that can be used directly to fund Commission operations, subject to prior approval by the Commission's appropriations committees. After fiscal year 2006, Section 6(b) fee revenue will only go into the General Fund of the U.S. Treasury and will not be available to fund Commission operations.

NSMIA also provided equity in the application of Section 31 fees by authorizing the SEC to collect these fees on transactions involving securities subject to "last sale reporting" in the OTC market. Unlike the Section 31 fees imposed on sales of exchange-listed securities, these new OTC fees are classified as offsetting collections and, therefore, can be used to fund Commission operations, subject to approval by the Commission's appropriations committees. Under NSMIA, all Section 31 fees will fall to  $\frac{1}{500}$ th of 1 percent in fiscal year 2007.

<sup>1</sup> See also Statement of the U.S. Securities and Exchange Commission Concerning Securities Transaction Fees, Before the Subcommittee on Finance and Hazardous Materials of the House Committee on Commerce (July 27, 1999).

<sup>2</sup> Report submitted in response to the request of the Securities Subcommittee of the Senate Committee on Banking, Housing and Urban Affairs (S. Rpt. 100-105), December 20, 1988.

Because the fees collected by the SEC are tied—directly and indirectly—to market activity, they are nearly impossible to predict accurately. The fee rates established in NSMIA were based on 1996 projections of market activity. However, the tremendous growth in the markets over the past few years has far exceeded the 1996 estimates on which NSMIA was based, resulting in fee collections well in excess of original estimates. Unfortunately, the potential for either excess collections or shortfalls is inherent in activity-based fees.

While the NSMIA fee structure has eliminated the funding uncertainties and crisis situations that surrounded the agency's funding from the late 1980s to the mid-1990s, it has not reduced total collections due to unexpectedly strong market activity. Moreover, the SEC's long-term funding structure remains at risk. Notably, current estimates of the Congressional Budget Office (CBO) indicate that the SEC will collect \$285 million in offsetting collections in fiscal year 2007, which would not even be enough to fund the agency today.

#### *Budget Enforcement Act*

The rules enacted as part of the BEA have restricted efforts to undertake a comprehensive fee reduction. The BEA splits our fee collections into two different categories: "mandatory" and "discretionary." Under the BEA, any fees in existence prior to 1990 are deemed mandatory and are deposited directly into the General Fund of the U.S. Treasury; they are unavailable for SEC use. The SEC's fees that fall into this category are:

- the first 1/50th of 1 percent of Section 6(b) registration fees;
- Section 31 fees on transactions involving exchange-listed securities; and
- fees on mergers and tender offers.

These fees, which account for nearly 70 percent of total SEC collections, are estimated by CBO to exceed \$1.1 billion in fiscal year 2000. Because these collections currently are protected by the BEA rules, they cannot be reduced without a corresponding increase in revenues or decrease in federal spending elsewhere. According to CBO's estimates, to fully repeal these fees, other collections flowing to the Treasury's General Fund would have to increase by \$9.6 billion over the next seven years, or spending from the General Fund would have to be reduced by the same amount.

The remaining 30 percent of SEC collections, deemed "discretionary", were not in existence prior to 1990 and are unaffected by the requirements of the BEA. These fees are the offsetting collections that have traditionally been used by our appropriators to fund the agency. Specifically, they are:

- Section 6(b) registration fees collected above 1/50th of 1 percent; and
- Section 31 fees on transactions in securities subject to "last sale reporting" in the OTC market, as enacted in NSMIA.

As the traditional source of SEC appropriations, these offsetting collections are crucial to full and stable funding of the SEC.

The following chart shows the current CBO estimates of total fee collections broken down between mandatory and discretionary under the BEA.

(\$ in millions)

Fiscal Year	Mandatory	Discretionary	Total Collections
2000 .....	\$1,155	\$501	\$1,656
2001 .....	\$1,206	\$498	\$1,704
2002 .....	\$1,260	\$503	\$1,763
2003 .....	\$1,314	\$516	\$1,830
2004 .....	\$1,422	\$508	\$1,930
2005 .....	\$1,544	\$552	\$2,096
2006 .....	\$1,675	\$601	\$2,276
2007 .....	\$783	\$285	\$1,068

As the chart illustrates, total fee collections are projected to increase through fiscal year 2006, and then fall sharply in 2007 when the final NSMIA fee reductions go into effect.

We understand that there may be a major change in the budget rules under the BEA in the event that an on-budget surplus materializes as expected, which could have an important effect on the fee debate. Specifically, there is a possibility that fee rates could be changed without having to accommodate the requirement of an offsetting revenue increase or spending cut for any reduction in fees classified as mandatory under the BEA.

### *Fee Reductions by the Commission*

The Commission recognizes the magnitude of excess fee collections, and has tried to reduce fees, where possible, when it is within its authority to do so. The Commission has taken two specific actions to reduce fees and administrative burdens. In 1996, fees for filing certain disclosure documents were eliminated, saving public companies an estimated \$8 to \$12 million per year. While this is a small amount relative to the size of the industry, the elimination of these fees significantly reduced the administrative burden on registrants and the SEC. This year, the Commission responded to industry concerns that there was a double counting of transactions in the OTC market imposing an unfair burden on certain market participants. The Commission encouraged and actively supported changes in industry practices to eliminate this problem and approved NASD rule proposals to implement this change in March 1999.

### *Fee Reduction Proposals*

Two members of the Subcommittee have introduced bills this session to address the issue of excess fee collections. The bills take different approaches to addressing this issue. Representative Lazio has introduced H.R. 2441, the "Fairness in Securities Transaction Act", which attempts to address the issue by reducing the Section 31 fee rate. Representative Fossella has introduced H.R. 1256, the "Savings and Investment Relief Act of 1999", which attempts to address the issue by capping total Section 31 fee collections. Both bills involve complex budget scoring and related issues.

*H.R. 2441.* Representative Lazio's bill would reduce the Section 31 fee rate from  $\frac{1}{3000}$ th of 1 percent to  $\frac{1}{5000}$ th of 1 percent on transactions involving both exchange-listed securities and securities subject to "last sale reporting" in the OTC market. In an attempt to alleviate the BEA issues raised by a fee rate reduction involving the "mandatory" portion of our fee collections, the bill redesignates 90 percent of the fees collected on last-sale-reported securities as mandatory (*i.e.*, general revenue) from the current 100 percent as discretionary (*i.e.*, offsetting collections available to fund the agency). The bill also redesignates 10 percent of the fees collected on exchange-listed securities as discretionary from the current 100 percent as mandatory. In effect, the bill reallocates 90 percent of combined Section 31 fee collections to general revenue, leaving only 10 percent as offsetting collections available to fund the agency.

H.R. 2441 raises several problems in its current form. The bill does not provide the SEC with full and stable long-term funding. The reallocation of Section 31 fees significantly reduces the amount of offsetting collections available to fund the agency, making shortfalls in Commission appropriations more likely. Although the bill contains a provision to address possible shortfalls, we do not believe that the proposed language provides the necessary assurance of full funding for the Commission in the event of a shortfall. The language appears to allow the Appropriations Committees to increase Section 31 fees through a supplemental appropriation to address a shortfall. However, this mechanism would not operate in a timely fashion. It appears that the proposed mechanism would go into effect after the fact—when a fee revenue crisis had already occurred—making it difficult for the SEC to operate effectively in the event of a fee revenue crisis. The mechanism would appear to require our appropriators to move a supplemental appropriation through Congress in an emergency situation when quick action would be necessary to avert such a crisis.

In addition, the bill does not take into consideration the timing of fee collections. The SEC collects transaction fees twice a year—on March 15 (for four months) and on September 30 (for eight months). The larger collection in September occurs well after supplemental appropriations bills normally are enacted. Thus, H.R. 2441 has serious operational problems that need to be addressed.

The bill also eliminates a portion of the Exchange Act (enacted as part of NSMIA) that provides for the continuation of offsetting fee collections in the event of a lapse of appropriations at the beginning of a fiscal year. The enactment of Section 31(d)(3) of the Exchange Act solved a serious administrative problem for the agency and eliminated potential interference with the capital raising process and confusion in the financial community. We strongly oppose its deletion.

While we defer to the Congressional Budget Office (CBO) as the technical experts on budget scorekeeping issues, we believe that there may be some scoring problems with the bill. Although the bill attempts to alleviate the BEA issues, reducing the fee rate alters the economic model CBO uses to estimate fees. Revised fee estimates may potentially create scoring problems.

*H.R. 1256.* Representative Fossella's bill would cap the dollar amount of Section 31 fees that can be collected in fiscal years 2000 through 2006. In an attempt to alleviate the BEA issues, the bill also combines the mandatory and discretionary

categories of Section 31 fees. Of the total Section 31 fees to be collected in each fiscal year, a specified amount of fee collections is designated as general revenue, and the remaining amount of fee collections, if any, up to the cap for that fiscal year is designated as offsetting collections.

H.R. 1256 also raises a number of concerns in its current form. First, the bill does not provide the SEC with full and stable funding. H.R. 1256 includes the same language as H.R. 2441 addressing insufficient fee collections. As discussed above, this language does not provide adequate protection for full SEC funding in the event of a shortfall in fee collections. This bill thus exposes the SEC to the possibility of an emergency budget situation that could severely impact Commission operations.

Second, the bill does not specify the degree of precision required in implementing a cap or what to do if fee collections exceed the cap. To cut off fee collections precisely when the cap has been reached would be administratively difficult, if not impossible, under the current fee collection system. To effectively implement such a tight cap, the SEC would have to develop a complex and potentially costly record-keeping system that could track fee collections by the exchanges and the National Association of Securities Dealers (NASD) to determine when the fee cap has been reached.

Over the past few months, the Commission staff has had an opportunity to discuss with industry participants the administrative and technical issues associated with implementation of a fee cap. These discussions have revealed a number of issues. The New York Stock Exchange (NYSE) staff indicated that their collection process is not entirely automated. There is currently at least a six-week gap between the time a transaction takes place on the NYSE and the time when volume information on that transaction is reported to the SEC. As a result, the NYSE currently does not have the ability to provide timely information with respect to the collection of Section 31 fees. The NYSE staff also represented that the automation of their fee collection process could not begin until mid-2000 due to Y2K and decimalization system enhancements. The NASD staff made similar comments with respect to the American Stock Exchange. The NASD staff did indicate, however, that it would have no serious programming problems with implementing a cap on an annual basis for NASDAQ.

Finally, we believe that H.R. 1256 may also have CBO scoring problems similar to H.R. 2441, resulting in revised CBO estimates for the outyears.

#### *Conclusion*

Today, we are faced with total fee collections well above both the cost of funding the SEC and the levels anticipated in NSMIA. CBO's estimates for fiscal year 2000 fee collections are \$1.66 billion. Not only is that amount far greater than our funding requirements for fiscal year 2000, but 70 percent of that figure is unavailable to fund the agency because of the restrictions imposed by the BEA rules.

Reducing fee collections, however, presents many of the same issues that required years of Congressional negotiation resulting in the compromise embodied in NSMIA. As the Commission has stated in the past, any alternative funding mechanism must:

- provide full and stable funding for the SEC;
- spread the costs of regulation among those who benefit;
- consider the effect of market conditions on collections; and
- address the competing interests of all parties.

Both H.R. 2441 and H.R. 1256 raise a number of concerns. Most significantly, neither bill provides a sufficient funding mechanism for the SEC. In particular, the fee rate reduction contained in H.R. 2441 could likely result in a serious funding shortfall for the SEC in the event of a downturn in market activity. Based on our discussions with industry participants, we believe that the fee cap proposal in H.R. 1256 would be more difficult to implement, especially in light of the Y2K issues and the lack of specificity in the bill.

The SEC would welcome the opportunity to discuss the current proposals in greater detail. The Commission staff is available to discuss these proposals in more detail and to provide assistance in crafting solutions to our concerns. We appreciate the help and support of all the interested parties in ensuring that the SEC remains adequately funded regardless of the funding approach taken.

Mr. OXLEY. Thank you, Mr. McConnell. Let me begin, your testimony states that H.R. 2441 does not properly take into account the timing of the fee collections by the SEC, and you state that this presents problems regarding a supplemental funding legislation

that might be necessary. Could the SEC under its own rules alter the timing of its collections?

Mr. McCONNELL. I don't believe so. I believe the timing is set in the law.

Mr. OXLEY. Could you pull the microphone closer?

Mr. McCONNELL. I don't believe we have the authority. The timing is in the law that we collect twice a year, in March and at the end of September, the section 31 fee charges. That would require a change to NSMIA.

Mr. OXLEY. It would require a change in the statute?

Mr. McCONNELL. Yes.

Mr. OXLEY. Does the Commission believe the transaction volume will increase or decrease given the change in the markets that—many experts obviously think the market volume will increase because of conversion to decimals and the extension of hours for trading. If volume continues to increase or at least remain steady, is there still a concern of funding shortfalls, and, if so, why?

Mr. McCONNELL. Well, I have been advised by my Chairman to never predict the direction of the market, as he so often has stated, but we have experienced in the past—certainly ups and downs with respect to transaction activities after 1987 and 1989. There were downturns in the level of transactions.

Mr. OXLEY. In volume?

Mr. McCONNELL. In the volume.

Mr. OXLEY. How long did that last?

Mr. McCONNELL. I don't know precisely. In 1987, it was at least a year. In 1989, it was a shorter period, but there are blips that occur.

Mr. OXLEY. Well, if the market were to go down, you would still have significant transactions.

Mr. McCONNELL. Well, in fact, short-term decreases in the market oftentimes result in increases in transactions because of the selling activity, but you stretch that out over a year period perhaps, and we have seen absolute decreases in the total level of transactions.

Mr. OXLEY. The sponsor and the cosponsor of H.R. 2441 have an amended draft of their legislation that was provided to you. Does the amended version alleviate the Budget Enforcement Act issues, in your estimation?

Mr. McCONNELL. From our analysis, it does alleviate those Budget Enforcement Act problems. It would seem to score budget-neutral.

Mr. OXLEY. Thank you.

Let me yield to my friend from New York, Mr. Towns.

Mr. TOWNS. If it was a perfect world, which you know it is not, but my colleague and I, we are working on it, trying, what would you like to see that is not in either one of these bills? Is there anything?

Mr. McCONNELL. Well, in a perfect world I think a fee rate reduction is much easier—it is a better system for the industry. It is predictable. People can make business decisions knowing exactly what they encounter. The problem with that is that the Budget Enforcement Act makes the world somewhat imperfect with respect to the SEC's funding.

We may have an opportunity here, though, that has been discussed a little bit. The Budget Enforcement Act does provide for the elimination of pay-go restrictions in the event of on-budget surpluses. No one really knows how that works, but it does seem to offer the opportunity to deal with fee rate reductions without necessarily having to satisfy all the requirements of pay-go. It is an opportunity that has just come to us. No one has really implemented that, but I think it is something we can throw into the discussion on this issue as to how to lower fee collections.

Mr. TOWNS. Thank you very much, Mr. Chairman. I yield back.

Mr. OXLEY. Gentleman from New York Mr. Fossella.

Mr. FOSSELLA. Just a couple of questions. What is the budget of the SEC this year?

Mr. MCCONNELL. Our current budget is approximately \$340 million.

Mr. FOSSELLA. H.R. 1256 provides for fiscal year 2000 \$463 million. I am just curious as to how do you square that circle, the funding, appropriate funding, for the SEC, when you are over \$100 million more under this legislation than what the SEC currently receives?

Mr. MCCONNELL. Our understanding is that the amount made available under H.R. 1256, actually coming from the offsetting collection, is much less than that. It is \$287 million in the first year, so that the appropriators would have to make up the difference between what they are typically relying on through offsetting collection to achieve full funding. The shortfall occurs because just the amount that is available from the offsetting collections gives them the scoring.

Mr. FOSSELLA. So you are concerned that the appropriators themselves may not fund adequately the SEC?

Mr. MCCONNELL. Exactly.

Mr. FOSSELLA. With respect to—and Mr. Levitt testified before this committee, I guess, a couple of months ago or so, I forget the specific date, and I thought it was his, if I heard him correctly, that the cap was preferable to a rate cut. Again, if the intent here is a user fee to fund with a degree of certainty the SEC—and from your perspective I guess your main concern is that you get that check, right?

Mr. MCCONNELL. That is correct.

Mr. FOSSELLA. Everything else being equal, what is more certain than a specific cap?

Mr. MCCONNELL. We stand by—

Mr. FOSSELLA. And with that, you know, predictability and certainty, you know, depending on the volatility of the volume of the market, are we to assume that that is less predictable than the SEC will receive no more than X amount of dollars each year?

Mr. MCCONNELL. As it currently stands with the proposals before us, the SEC still believes that the cap is preferable. It offers us the best protection, the lowest amount of risk with respect to us receiving adequate funding. So we would still support a cap given what we know today and given what is available today.

Mr. FOSSELLA. Thanks, Mr. McConnell.

Thank you. I yield back, Mr. Chairman.

Mr. OXLEY. The gentleman from Illinois Mr. Shimkus.

Mr. SHIMKUS. Just two mischievous questions, Mr. Chairman. If there were no transactions, zero, would there be a role for the SEC which would require funding?

Mr. MCCONNELL. If transactions weren't occurring on the exchanges?

Mr. SHIMKUS. If there were no transactions. This is a theoretical question.

Mr. MCCONNELL. The role for the SEC is law enforcement. We must ensure that people aren't perpetrating fraud against investors through all manner of mechanisms. We also have the function of registering—

Mr. SHIMKUS. I am trying to address the question of as transactions decline—

Mr. MCCONNELL. Right.

Mr. SHIMKUS. [continuing] is the law enforcement aspects of the SEC—would they decline proportionately with the number of transactions?

Mr. MCCONNELL. Actually, we believe that if there is a change in the market direction, and if it would go down and things decline, you would see more need for enforcement because people would be more concerned about what is happening to their investments in a declining market, and there would be perhaps greater possibility to have accounting fraud and those matters. So we don't think our enforcement requirements would go down at all in a declining market.

Mr. SHIMKUS. And these fee rates were initially increased by whom and why?

Mr. MCCONNELL. Well, the original 1933 act establishes registration fees on securities, and then the 1934 act establishes the  $\frac{1}{300}$  of 1 percent of the transaction fee on the exchanges. NSMIA extended that  $\frac{1}{300}$  of 1 percent to the entire marketplace, both exchanges and the over-the-counter market.

Mr. SHIMKUS. So, my question is, was there a fee increase identified with this budgeted base to increase the ability of the Federal Government to fund other operations? Talk to me about this 1990 fee increase that the appropriators imposed upon us.

Mr. MCCONNELL. Well, the 1996 NSMIA funding mechanism started out by trying to deal with the registration fees that people believed were way too high. The 1996 registration fees paid by companies to go public was also way in excess, far in excess of what our funding needs were. So we attempted to address that problem through a long-term reduction in those registration fees.

In addition, there had been a long-standing proposal to extend the transaction fees to the entire marketplace, as a matter of equity as much as anything else. That was  $\frac{1}{300}$  of 1 percent. So both transactions occurred at the same time. The  $\frac{1}{300}$  of 1 percent extension also provided a little bit more stability to the appropriations process by broadening the fee collection population.

Mr. SHIMKUS. But the equity debate that you just mentioned is still part of this new debate with the cap versus the fee?

Mr. MCCONNELL. Correct. I mean, we believe that the cap can be set at a level most easily to protect the agency's resources.

Mr. SHIMKUS. But not to promote equity in the transactions across the year?

Mr. MCCONNELL. It could have that negative effect.

Mr. SHIMKUS. That's all, Mr. Chairman. I yield back.

Mr. OXLEY. Gentleman yields back.

The gentleman from Oklahoma is—let me then ask you a couple of other questions before we complete your appearance. In your testimony you state that H.R. 2441 deletes section 31(d)(3), and that you oppose that deletion. Could you explain to the committee what that section does and why you oppose it, propose the deletion?

Mr. MCCONNELL. I think that the revised version changes that, but I will double-check, but basically that is the provision that allows continuation of the fee in the absence of an appropriation. That has been a very—before we had that protection, it created a lot of uncertainty in the marketplace as to what fees to pay, and it also created uncertainty with respect to the SEC's funding arrangement under those fees. That was built in to provide certainty in the marketplace, and certainty that there would be a continuation of the fees collected to support the SEC's budget going into the new year.

Mr. OXLEY. Yes. I think it is—my understanding is the revised version does take care of that—

Mr. MCCONNELL. I believe, yes.

Mr. OXLEY. [continuing] and reinstates the section. Thank you.

Does the Commission believe that investors, given a rate cap as proposed in 1256, would time their investment decisions based on whether or not a transaction fee was applied, or would that proposal have any overall market behavior change in it?

Mr. MCCONNELL. As a general matter, we don't believe that on a separate transaction or individual trade that the  $\frac{1}{300}$ , whether it is there or not, would affect an investment or business decision. In the aggregate that is obviously a huge number, but when it gets down to individual trades, we don't think it would affect market activity.

Mr. OXLEY. Let me ask you, how common are user fees applied to regulated entities to pay for their Federal regulation?

Mr. MCCONNELL. It has become fairly common. There are a number of agencies that rely upon user fees for a portion of their budget. The SEC may be somewhat unusual in that basically our entire budget now is supported by these offsetting fee collections.

Mr. OXLEY. And you think that may be unique? I don't know. I think it probably is.

Mr. MCCONNELL. It is unusual. I would have to do some work to say that we are unique, but we are definitely unusual in that respect.

Mr. OXLEY. I know the FCC, for example, gets some funding from license fees and that kind of thing.

Mr. MCCONNELL. They do.

Mr. OXLEY. Gentleman from New York.

Mr. TOWNS. Not a question, just sort of a suggestion, recommendation. I am anxious to move this, and I think in order to do it we need to walk down every avenue, every road, every street. And I think I would feel comfortable if the SEC would submit for the record what you feel should be done in order to make both bills, you know, stronger. I think that if you could submit that for the record, and we could leave the record open for that information, to

review that, because, Mr. Chairman, I am hoping we can get this and get together and sort of move this legislation. I don't want to leave anything out, and I think that by getting that input from the SEC, it would be very, very valuable in terms of some of the things that you said earlier and others that you might feel that would strengthen the bills. And I would appreciate that kind of information coming, Mr. Chairman.

Mr. OXLEY. I think that is a worthy idea and would recommend that to Mr. McConnell, from SEC's staff. And we want to pledge to work with you, and our staff also, to come to a good conclusion on this issue, and would also point out that the CBO was unable to testify today, but I am going to leave the record open for—I am sorry, OMB, I get all those bean counters mixed up. I knew it was a B. I will ask unanimous consent that the record remain open for 5 days to allow that information to be available to the committee.

And again, Mr. McConnell, we thank you for your testimony. If there is no further business to come before the subcommittee, we stand adjourned.

[Whereupon, at 11:10 a.m., the subcommittee was adjourned.]  
[Additional material submitted for the record follows:]

EXECUTIVE OFFICE OF THE PRESIDENT  
OFFICE OF MANAGEMENT AND BUDGET  
October 7, 1999

The Honorable MICHAEL G. OXLEY  
United States House of Representatives  
Committee on Commerce  
Rayburn House Office Building, Room 2125  
Washington, DC 20515-6115

DEAR REPRESENTATIVE OXLEY: Thank you for seeking the Office of Management and Budget's (OMB) views on H.R. 2441, the Fairness in Securities Transactions Act, and H.R. 1256, the Savings and Investment Relief Act of 1999.

All securities market transactions and registrations require regulation and oversight to maintain the investor confidence that makes American securities markets the most liquid and trusted in the world. The fees on transactions (Section 31) and registrations (Section 6(b)) collected by the SEC help offset the costs of necessary and valuable oversight and regulation of these markets. While the cost of the fee is likely passed to consumers, transaction fees comprise a small portion of the cost of trading securities. The SEC fee assessed on securities transactions is  $\frac{1}{300}$  of one percent, or thirty-three cents on a transaction of \$10,000. In comparison, the cheapest Internet brokerage charges consumers five dollars to make a typical stock transaction. We believe the cost of the transaction fee is more than outweighed by the liquidity and integrity of U.S. securities markets.

The current level of activity on U.S. securities markets, reflecting one of the longest bull markets in history, has generated fee collections well above our original expectations when the National Securities Markets Improvement Act (NSMIA) was enacted in 1996. Presently, the fee collections available to the SEC are fully adequate to fund the Commission's activities. Due to phased reductions in registration fees as provided in NSMIA, however, in future years fee collections will be insufficient to fund the SEC's activities, necessitating the provision of general fund appropriations. While we project that the level of offsetting collections available for the SEC's use under NSMIA will be sufficient to fully fund the Commission's program needs through fiscal year 2006, enacting either H.R. 2441 or H.R. 1256 would cause the collections available to the SEC to fall short of the Commission's funding needs starting in the 2000 or 2001 fiscal year, respectively, and in future fiscal years. Moreover, even if the SEC relied upon previously collected fees to make up the funding shortfall, these fees would be exhausted by fiscal year 2003, only delaying the funding shortfall. Large increases in direct appropriations for the SEC would unnecessarily divert needed funds from other priorities in the Commerce/Justice/State appropriations bill.

H.R. 1256, in particular, raises other concerns. Both the SEC and the self-regulatory organizations (SROs) would need to modify their reporting systems, jeopardizing a smooth transition for the Year 2000 and the conversion to decimalization. It

is also unclear whether SROs will be able to immediately stop collecting fees once the cap is reached, or what occurs if fees are collected in excess of the cap.

In conclusion, the structure and rate of fees imposed on U.S. securities markets are complex issues that should be discussed with all affected parties. Congressional staff, OMB, and other interested parties concluded extensive negotiations regarding fees in the securities markets with the passage of the NSMIA in 1996. NSMIA was intended both to ensure equitable treatment of U.S. securities markets and to provide more stable funding for the SEC. New legislation altering fee collections and SEC funding—if enacted without adequate consideration or input from all affected parties—could upset the delicate balance so carefully crafted in 1996, and jeopardize the stability and oversight on which our securities markets thrive.

Thank you for your interest and involvement in this matter. I look forward to working with you on this issue.

Sincerely,

JACOB J. LEW  
*Director*