FEES COLLECTED UNDER THE SECURITIES ACT OF 1933 AND THE SECURITIES EXCHANGE ACT OF 1934: HEARING, 106 CONGRESS, 1ST SESSION, MARCH 24, 1999; S. HRG. 106-475

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FEES COLLECTED UNDER THE SECURITIES ACT OF 1933 AND THE SECURITIES EXCHANGE ACT OF 1934

HEARING

BEFORE THE

SUBCOMMITTEE ON SECURITIES

OF THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

ONE HUNDRED SIXTH CONGRESS

FIRST SESSION

ON

THE EFFECTS OF THE EXCESSIVE FEES COLLECTED UNDER FEDERAL SECURITIES LAWS AND THEIR IMPACT ON THE FINANCIAL MARKETS AND ON THE ECONOMY AS A WHOLE

MARCH 24, 1999

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FEES COLLECTED UNDER THE SECURITIES ACT OF 1933 AND THE SECURITIES EXCHANGE ACT OF 1934

WEDNESDAY, MARCH 24, 1999

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
SUBCOMMITTEE ON SECURITIES,
Washington, DC.

The Subcommittee met at 10 a.m., in room SD–538 of the Dirksen Senate Office Building, Senator Rod Grams (Chairman of the Subcommittee) presiding.

OPENING STATEMENT OF SENATOR ROD GRAMS

Senator GRAMS. I would like to call this hearing to order.

Good morning. Today, the Subcommittee on Securities is meeting to receive testimony on and consider the effects of the excessive fees collected under the Federal securities laws and their impact on the financial markets and on the economy as a whole. Since their enactment in the 1930's, Section 6(b) of the Securities Act of 1933 and Section 31 of the Securities Exchange Act of 1934 have authorized the assessment of fees against securities registrations and transactions on the securities exchanges. For most of their existence, these fees have remained consistent with their intended and appropriate purpose—to reimburse the Government for the costs of the Securities and Exchange Commission (SEC) regulation. It is encouraging that all the witnesses this morning have noted in their written testimony that they support fully funding the SEC—they just do not want to do it five times a year.

Since 1983, these fees have risen to a level which has surpassed the annual SEC's budget, thus making the agency a net contributor to the Federal budget. Although the National Securities Markets Improvement Act of 1996 was a good first step to a long-term solution, work still remains to be done.

To illustrate just how excessive these fees have become, the SEC requested $360.8 million for fiscal year 2000. Collections of Section 6(b) and Section 31 fees in fiscal year 2000 are estimated to exceed $1.5 billion—and if history repeats itself, that actual amount will likely grow. If these amounts are in the ballpark, the Federal Government collects nearly five times the SEC's budget in user fees. Normally, this practice would be disturbing. However, in a time of high budget surpluses, it is incomprehensible that we would continue this backdoor tax on capital formation and investment.

Although critics will deride proposals to reduce these collections as tax breaks for Wall Street, the facts do not support his assertion. That is because Wall Street firms pay transaction fees only when they are trading for their own account, and do not pay the registration fees on securities that they underwrite at all.

The fact is that every investor in America is paying these backdoor taxes. When a young couple saves for their children's college education, they pay this tax. When a retiree invests his or her retirement in the market, they pay this tax. When a pension fund invests its capital in the market, the individual participants in the plan pay the tax indirectly through lost capital. And this example only covers the transaction fees.

When Section 6(b) fees are also considered, the impact is even more dynamic to the entire economy, because excessive registration fees remove capital from the economy before it has had a chance to even grow. If the nearly $1 billion in collections are allowed to be used by American businesses rather than being sent to Washington, it is anyone's guess how great an impact it could have. How many jobs, how many businesses, how much economic growth could American businesses provide annually by leveraging this money? Could it be $2 billion? $5 billion? Or $10 billion? Clearly, reducing the barriers to economic growth must continue to be a goal, and reducing these fees is a very good first step to reducing the cost of economic growth.

I look forward to working with the panelists and other interested parties to try to find some workable solutions which ensures reliable funding for the SEC while reducing the burden on American investors and on American businesses.

Senator Bunning.

OPENING COMMENTS OF SENATOR JIM BUNNING

Senator BUNNING. Thank you, Mr. Chairman.

I would like to thank all the witnesses for coming before the Subcommittee to testify today.

User fees should be used only for the purpose for which they were collected. They should not be used to balance the budget. The budget is balanced. We are currently collecting way too much money in user fees than the Securities and Exchange Commission needs to offset its budget.

This backdoor tax on capital is an unfair burden to investors and to brokers. With more and more people investing in the market, fee collections have boomed to outrageous levels. These fees are passed on to the investor. Many of these are small, first-time investors. Although the fees are a small percentage, and that percentage will decrease over the next 8 years, the SEC still will be collecting much more money than it needs. This money belongs to the taxpayers and should be given back.

I do believe that the SEC needs adequate resources to fulfill their mission, and with the explosion of small investors and the relatively new options such as on-line investing that are bringing more and more new investors every day, the job will only become more difficult. But we can still fulfill their budgetary needs and give money back to the taxpayers.

I thank you, Mr. Chairman.

Senator GRAMS. Thank you very much, Senator.

Chairman Levitt, we welcome you to the Subcommittee and we look forward to your opening statement.

OPENING STATEMENT OF ARTHUR LEVITT CHAIRMAN, U.S. SECURITIES AND EXCHANGE COMMISSION ACCOMPANIED BY: JAMES McCONNELL, EXECUTIVE DIRECTOR

Chairman LEVITT. Thank you very much, Chairman Grams and Members of the Subcommittee. Thank you for the opportunity to testify teday regarding the Securities and Exchange Commission's fee collections and funding structure.

The Federal securities laws direct the Commission to collect three different types of fees: Registration fees, transaction fees, and fees on mergers and tender offerings.

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. This situation has been exacerbated in recent years as tremendous market growth has pushed fee collections far beyond initial projections. These projections were based on a fee structure that was revised 3 years ago.

The National Securities Markets Improvement Act (NSMIA) in 1996, mandated a fee structure designed to do four things: One, reduce total fee collections; two, extend transaction fees to the over-the-counter market, instead of only the exchange-listed securities; three, provide the SEC with a stable, long-term funding structure; and four, reduce the SEC's reliance on fee collections, thereby increasing the amount of new budget authority to fund the agency.

Specifically, the legislation set in motion a gradual reduction in registration fees over a 10-year period, so that fee collections would be more closely aligned with the funding needs of the SEC.

In addition, those transaction fees were extended to the over-the-counter market in an effort to treat comparable securities in a consistent manner. As I expect that you will agree, because these fees collected by the Commission are tied to market activity, they are nearly impossible to predict with any degree of accuracy. The fee rates in the NSMIA were based on projections of nearly 4 years ago, and I think it is fair to say that a lot has happened over that period of time. Our markets have experienced almost explosive growth, and the result has been collections that are way above what was estimated.

While the NSMIA has succeeded in eliminating the funding uncertainties that surround the agency's funding, it has failed thus far to reduce collections. Efforts to undertake a further comprehensive fee reduction have been restricted by several factors, including the Budget Enforcement Act (BEA). That Act splits our fee collections into two different categories: Mandatory and discretionary. The mandatory fees—those that are deposited directly into the Treasury and are unavailable for SEC's funding use—account for about 70 percent of SEC's collections. The discretionary fees—those that are available for use by our appropriators—comprise the remaining 30 percent. And because the mandatory fees are protected by BEA rules, they cannot be reduced without a dollar-for-dollar increase in revenues, or a decrease in Federal spending.

I absolutely recognize the seriousness and the magnitude of this issue, and I have to say that I endorse the observations made in your opening statements.

Wherever possible, we have tried to reduce fees. We have taken specific action in two areas. First, we eliminated fees for certain filing disclosure forms; and second, just yesterday, we approved the NASD proposal to address concerns that there was a double counting of transactions in the over-the-counter market.

Now, these actions just begin to scratch the surface. I welcome this discussion on fee collections, and, as I move forward, I am hopeful that we can achieve the same level of cooperation among all participants as we did with respect to the NSMIA negotiations.

Quite frankly, before I came to the SEC I do not think I ever contemplated a number as infinitesimal as 1/300th of 1 percent. But far more importantly, this issue can have a direct effect on the SEC's ability to help protect investors and assure the market's viability.

We are dealing with a number of different committees and different agencies, and, whatever path that we take, I look forward to working with all of these groups so that the SEC is adequately funded to fulfill its mission to protect investors, and we are able to address constructively the overfunding issue that brings us to this chamber today.

Thank you.

Senator GRAMS. Thank you very much, Chairman Levitt. It was my error—I had the opportunity to come down and meet you this morning, but I did not introduce you to the Subcommittee, and I apologize for that.

Our first witness, of course, was the Chairman of the Securities and Exchange Commission, Arthur Levitt. Accompanying him is Mr. James McConnell, Executive Director of the Securities and Exchange Commission. Again, I welcome you to the Subcommittee and I apologize for not giving you the proper introduction as we began this morning. But I want to thank you very much for your testimony.

Chairman LEVITT. Thank you.

Senator GRAMS. I have a couple of questions I would like to ask.

Currently fees collected under the Securities Act generate, as we have said, approximately five times the SEC's annual budget. Chairman Levitt, has your agency calculated how drastically the market volumes and issuances would have to decline before net revenues to the Government would drop below the level of funds provided in the SEC's budget?

In other words, at the current levels, is there any level that you have thought of where the market would have to decline in trading or activity that would not produce the budget of $360 million today? Are we in any kind of jeopardy of underfunding your activities by cutting these fees?

Chairman LEVITT. I do not know the precise level that the market would have to decline. The last time that discretionary fee collections did not come up to the amount of money it took to fund the agency was in 1995, so it is theoretically possible.

Mr. McConnell, do we have a fix on the precise number that it would take?