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Tax Corporate Stock Buybacks that Enrich Executives and Worsen Inequality

Corporate executives have increasingly been directing their companies to purchase shares of their own stock in a strategy to drive up share prices. When firms buy their own, it reduces the number of outstanding shares and increases the price of each share, which rewards shareholders and executives. Stock buybacks exacerbate the racial wealth gap, worsen economic inequality, and divert resources from the real economy which harms workers.

Buybacks are a bonanza for the executives that make the decision to buy back shares. The *Harvard Business Review* noted the that buybacks are motivated by "'this simple truth: Stock-based instruments make up the majority of [corporate executives] pay, and in the short-term buybacks drive up stock prices."[1] Buybacks divert resources from investing in worker wages and benefits, productivity enhancing capital upgrades, or research and development.

Taxing stock buybacks would raise revenue and discourage companies from pursuing this strategy that puts the interests of lavishly paid executives ahead of reinvesting in longer term business health, in workers and in the broader economy.

Stock buybacks have surged — even during pandemic: Share buybacks have soared in recent years in conjunction with rising executive compensation through stock-based pay packages. Corporate stock buybacks were essentially considered market manipulation before the Securities and Exchange Commission (SEC) gutted the regulation in 1982.[2] Before the rule change, S&P 500 companies spent about 2 percent of profits on buybacks, but between 2009 and 2018, S&P 500 companies spent $4.3 trillion on buybacks — more than half of their income.[3] In 2018, the first full year under the 2017 Tax Cuts and Jobs Act (TCPA), S&P 500 companies spent $806 billion on buybacks.[4] In 2019, the banking industry alone bought back $156 billion shares.[5] Even during the pandemic, companies bought back $521 billion shares of stock rather than reserving resources to support their workers and communities.[6] Already, 2021 buybacks are showing signs of approaching the 2018 record levels.[7]

Executives win big from buybacks: The executives that implement share buyback schemes profit handsomely.[8] Executives now receive the bulk of their compensation from stock awards and stock options — often more than 80 percent — which encourages them to take actions like share buybacks to boost stock prices for their own benefit.[9] Former SEC Commissioner Robert Jackson reported that "executives personally capture the benefit of the short-term stock-price pop created by the buyback announcement."[10] A 2020 University of Massachusetts paper found that corporate insiders frequently sell their own shares during corporate buybacks.[11]

Stock buybacks worsen the racial wealth gap: Corporate strategies that focus on boosting share prices enrich the overwhelmingly white executives and shareholders while leaving Black and Latinx families further behind. Black and Latinx households each own only 1 percent of the total stock market value — figures that have not budged for the past 30 years — while white families hold 90 percent of the stock market value.[12] Over 60 percent of white families own some stock, directly or through mutual funds or retirement accounts, but two-thirds of Black families and three-quarters of Latinx families have absolutely no stock holdings at all.[13] The typical value of these investments by those Black and Latinx families is only $15,000 — less than one-third the typical $50,000 holdings of white families.

Share buybacks exacerbate economic inequality: The strength of the stock market is not the best metric for assessing broad-based economic health because stock ownership is highly concentrated in the hands of the very wealthiest families. The wealthiest 10 percent of households control 88 percent of the stock market and the top 1 percent alone own 53 percent of the market.[14] The half of households with the lowest net worth own less than 1 percent of the stock market (and only about a third have *any* stock or mutual fund stocks).[15] A $1 trillion increase in stock market value would deliver nearly $440,000 to each of the richest 1 percent of households while the few stockholding households in the bottom half of net worth get only $330.

Stock buybacks divert resources from investing in companies and jobs: Stock buybacks harm workers and undermines long-term economic growth by shifting revenues from capital investments and workers' wages and benefits. A 2021 American Compass study found that the number of companies that extracted more value from their firms (including share buybacks) than they invested in new capital expenditures had risen from only 6 percent of companies before 1985 to 49 percent of companies in 2017.[16] Studies have found that share buybacks are associated with downsizing and wage stagnation.[17] In the two months after the TCJA slashed corporate taxes, S&P 500 companies dedicated 106 times more money to share buybacks ($160 billion) than wage increases ($1.5 billion).[18]

Tax manipulative stock buy backs: Congress should tax stock buybacks to curb excessive shareholder payouts to wealthy executives and shareholders to fund needed public investments. Even a 1 percent tax on stock buybacks would generate $12.5 billion annually.[19] A stock buyback tax would be a down payment on comprehensive buyback reform proposals to prohibit manipulative stock buybacks and empower workers to have a greater say in corporate decision-making.

Endnotes

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[6] Pisani, Bob. "Stock buybacks surge to likely record highs, but a tax from Congress poses a threat." *CNBC.* October 27, 2021.
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[10] Securities and Exchange Commissioner Jackson Jr., Robert J. Jackson. [Speech]. "Stock Buybacks and Corporate Cashouts." June 11, 2018.
[11] Palladino, Lenore. "Do corporate insiders use stock buybacks for personal gain?" *International Review of Applied Economics.* Vol. 34, Iss. 2. 2020.
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[13] FRB. Survey of Consumer Finances (SCF). Stock Holdings by Race or Ethnicity. 2019.
[14] FRB DFA.
[15] *Ibid*; FRB SCF. Stockholdings by Percentage of Net Worth. 2019.
[16] Cass, Oren. American Compass. "The Corporate Erosion of Capitalism." March 2021 at 1 to 2.
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[19] Davidson and Weaver (2021).