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A financial transaction tax for 11 EU countries

In the wake of the financial crisis, the idea of taxing financial transactions was revived. But it has not gained overwhelming support at either global or EU level so far. Therefore, 11 euro area countries have decided to move ahead on their own through enhanced cooperation. Opinions on the possible impact differ.

Background

The financial crisis has put significant pressure on sovereign debt and taxpayers. From 2008 to 2011, the European Commission approved many state aid measures aimed at keeping the banking sector operational and ensuring enough credit flow to the economy. Their total amount was worth 37% of EU GDP.

In this context, there were many calls for the financial sector to share the costs of the crisis, and its regulation to be improved worldwide. Attention also focused on the dramatic increase in financial transactions in the years preceding the crisis. In 2007, their turnover was worth almost 70 times world GDP, with 88% of this related to derivatives trading.

One measure put forward to address these concerns is the much debated financial transaction tax (**FTT**). Its main objective is to reduce market volatility by making it more expensive for speculators to engage in frequent transactions such as automated high-frequency trading. In turn, the revenue collected could be allocated to different purposes, including fiscal consolidation.

Opponents of the tax argue that it is not possible to define speculative or undesirable financial transactions with much precision. An FTT would thus be the wrong solution to the problem of volatility, and harm growth. They add that, if not introduced throughout the world, the tax could distort financial markets, with transactions moving to countries that had not adopted it.

A 2012 survey shows that a majority of EU respondents (66%) are in favour of an FTT. This percentage is five points up from last year and even higher (73%) in euro area countries.

Debate inside and outside the EU

The attempt to gain international consensus for an FTT at G20 level has failed up to now, with countries such as the United States opposed to the idea. Nevertheless, in 2011 the European Commission put forward a proposal to introduce an EU-wide FTT.

According to the Commission, harmonisation in this field would be beneficial to the internal market: currently, ten EU countries have different forms of FTT, including France and the United Kingdom. Furthermore, it could build momentum for a coordinated approach with the main international partners.

Based on Article 113 TFEU, the proposal is subject to a special legislative procedure requiring unanimity in the Council after consultation of the European Parliament and of the Economic and Social Committee. On 23 May 2012, Parliament backed it, recom-mending a series of modifications.

However, discussions in the Council showed conflicting positions unlikely to be reconciled. On the one hand, France and Germany strongly support the introduction of an FTT. The financial sector is deemed to enjoy a tax advantage due to the current VAT exemption on most financial services.

On the other hand, the proposal encounters fierce opposition from other countries such as the United Kingdom and Sweden. Home to the largest financial centre in the EU, the UK considers an FTT would only be acceptable if implemented globally.

The Council decided to explore alternative routes to meet the same goals, but a debate on 22 June 2012 revealed that it was not possible to reach unanimity in this field.

Enhanced cooperation

On 9 October 2012, 11 Member States (MS) expressed their interest in moving forward with an FTT through enhanced cooperation: Austria, Belgium, Estonia, France, Germany, Greece, Italy, Portugal, Slovakia, Slovenia and

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Spain. All of them belong to the euro area and represent around 90% of the area's GDP.

Article 20 TEU and Articles 326 to 334 TFEU lay down the legal basis for this mechanism. A group of at least nine MS can promote integration in areas of non-exclusive competence of the Union, provided that the same objectives cannot be attained by the Union as a whole within a reasonable period.

Enhanced cooperation is carried out within the EU's institutional structure. It has been used only twice since its introduction by the Treaty of Amsterdam. Neither case (divorce law for international couples and the unitary patent) is in the field of taxation. For the second, proceedings are pending before the Court of Justice, with two MS calling for the Council's Decision authorising enhanced cooperation on the unitary patent to be annulled.

Next steps

Before enhanced cooperation on the FTT can start, the Council has to authorise it by qualified majority, after obtaining EP consent. To this end, the Commission presented a draft authorisation decision in October.

This was discussed initially at the November ECOFIN meeting. According to the press, most countries against an EU-wide FTT are not expected to block the enhanced cooperation process. However, some have expressed concerns about the effects on the single market of an FTT in other countries.

If authorisation is granted, participating countries will negotiate an FTT based on a new Commission proposal. All MS may take part in deliberations, but only participating countries can vote and must decide by unanimity. No such limitation applies to voting in the Parliament, where the ECON Committee voted in favour of enhanced cooperation by a large majority on 29 November.

What the tax could look like

The exact design of the tax is not known at this stage, but is likely to be based on the text put forward by the Commission for an EU-wide tax in 2011. The requests for enhanced cooperation mention that its scope and objectives should be in line with those of the previous proposal.

If so, the tax would apply to all transactions on financial instruments between financial institutions when at least one party to the transaction is located in a participating country. On this principle, taxation would be independent of the transaction's location.

The 2011 text foresaw other measures with a view to minimising relocation risks and the possible negative impact on the economy. They included: a broad scope; a low rate (0.1% on the exchange of shares and bonds; 0.01% on derivative contracts); the exclusion of transactions on primary markets for shares, bonds and currencies.

The Commission reckoned that the tax could raise €57 billion a year if applied across the EU. The estimate will be now revised downwards with major financial centres not participating in the scheme. France called for the new tax to be operational as of 2013.

Reactions and opinions

The solution of a common FTT in only 11 MS got mixed comments. Some analysts claim it will give competitive advantage to EU countries that do not participate. Others argue that the relevant legislation would be complex by nature and create uncertainty and legal disputes. This could drive financial institutions to transfer their activities out of the whole EU.

Some commentators say that an FTT already exists in important trading centres, such as Hong Kong and London, without negative effects on their status. Thus, the tax itself would not be the crucial determinant of trading activity. Its impact would mainly depend on its design.

In 2011, Nobel Prize winning economist Joseph Stiglitz declared that a correctly designed FTT would work if Germany, France, Italy and Spain were to implement it together. All of these countries have confirmed their willingness to take part in the enhanced cooperation process.

The European Parliament has been pushing for progress in the field of financial taxation at global and EU level for more than two years. Its President Martin Schulz welcomed the recent developments as a good beginning.

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