# For an ambitious EU Financial Transaction Tax worthy of the name

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# Introduction

The recession we are facing as a result of the coronavirus pandemic – together with the urgent need for climate transition – will require unprecedented public investment by the European Union (EU) and its member states.

The EU's absurd debt and deficit rules – combined with the equally absurd legal prohibition on monetary financing of government spending by the European Central Bank – mean that for the time being new taxes will be required to contribute to the recovery. The Next Generation EU recovery plan currently being negotiated lists several potential new sources of revenue.

A 'Robin Hood' tax, or Financial Transaction Tax (FTT), is an obvious initiative that could be a large source of revenue for the EU and its member states. Importantly, it is an initiative based firmly on principles of social justice, in contrast with proposals for regressive consumption taxes that will penalise the poor.

An EU FTT has been under discussion for at least the past decade. The original proposal tabled in 2011 had its limitations, but it would have applied a small tax to the vast majority of financial transactions made in the EU, covering all member states. It was estimated that such a tax would raise €57 billion per year, to be distributed between the EU and member states, and used to transfer funds from the wealthiest in society towards social and environmental goals.

After stumbling in the EU Council, moves were made in 2013 by 11 member states to establish a FTT under the 'enhanced cooperation' procedure. This process has dragged on to this day. The new German-Franco proposal under enhanced cooperation, which involves 10 participating member states, drastically reduces the objectives and scope of the tax, to the point where it is hardly possible to describe it as a Financial Transaction Tax at all.

Since the details of the current German-Franco proposal were made public, we have experienced the coronavirus pandemic – but this pandemic and the resulting economic devastation seem not to have registered in the minds of the officials negotiating this tax.

In May 2020, an important court decision by the Court of Justice of the EU (CJEU) ruled against French bank Société Générale, and affirmed that the Italian government's financial transaction tax was compatible with EU law.

Specifically the court makes it clear a member that taxing trades in derivatives does not violate the free movement of capital, so long as the underlying securities are based in the territory of the state imposing the tax.

This CJEU ruling removes the key justification that has been invoked by opponents of an ambitious FTT that taxes derivatives.

The scale of the economic crisis must be met with a commitment to an ambitious and socially just FTT, worthy of the name.

## The first proposal for an EU FTT in 2011

As a response to public sentiment in the wake of the 2008 global financial crisis, the European Commission made a legislative proposal on 28 September 2011 for a Council Directive on a Financial Transaction Tax (FTT) to apply across the European Union (EU).

While the popular understanding of a FTT was one that would tax banks and financial institutions to fund transfers to meet social and/or environmental goals, as well as discouraging financial speculation, the Commission formally based its proposal on ensuring the proper functioning of the EU's internal market and avoiding the distortion of competition, in order to align it with the powers granted by the EU Treaties.

The proposed 2011 Directive was to amend the 2008 Council Directive concerning indirect taxes on the raising of capital.

The Commission estimated that its 2011 proposal would raise approximately €57 billion each year across the 27 member states (including the UK, but not including Croatia, which had not yet acceded to the EU).

The FTT would apply to the great majority of financial transactions between financial institutions, with limited exceptions. It would apply a tax of 0.1% to exchanges of shares and bonds, and a tax of 0.01% to transactions involving derivative contracts. The FTT would apply to transactions where one party was resident in a member state of the EU. It would not apply to the common transactions of households and non-financial businesses such as payments, loans and insurance.

At the Council meeting of 22 June 2012, it was clear that unanimous support for a FTT did not exist. The Council announced on 29 June 2012 that the proposed Directive on a FTT would not be adopted by the Council "within a reasonable period".

## The FTT proposal under 'enhanced cooperation'

In 2013, eleven member states then requested that the Commission produce a new proposal for a Directive on a FTT using the enhanced cooperation procedure, as provided for under Article 327 of the Treaty on the Functioning of the EU (TFEU).

**ENHANCED COOPERATION**

**The enhanced cooperation procedure requires a minimum of nine member states to participate. It does not affect the possibility for member states that do not participate in the procedure to introduce their own FTT at the national level. It does not preclude non-participating member states from later joining the procedure if it agrees with the underlying Directives.**

In October 2012, the Commission proposed to proceed under the enhanced cooperation procedure, which was endorsed by the Council and Parliament. Some member states opposed even the voluntary enhanced cooperation procedure, arguing that by applying the tax to transactions where only one party was resident in a participating state, it would potentially impact on the tax revenue of the non-participating states.

The eleven states requesting enhanced cooperation were Belgium, Germany, Estonia, Greece, Spain, France, Italy, Austria, Portugal, Slovenia and Slovakia. (Estonia later left the enhanced cooperation process in December 2015.) These states requested that the new Directive be based on the same scope and objectives as the original Commission proposal of September 2011.

On 14 January 2013, the Council authorised the 11 states to establish a FTT among themselves. Britain, the Czech Republic, Luxembourg and Malta abstained on the vote.

On 14 February 2013 the Commission proposed a new Directive for a FTT among the 11 states under enhanced cooperation that was largely the same as its original proposal. It was estimated that these 11 states accounted for 90% of Eurozone GDP, and that the tax would apply to 85% of financial transactions between financial institutions within the participating states.

The Commission estimated that a FTT applied to the 11 member states would raise €30-35 billion per year for the participating states.

## The European Parliament's position on the 2013 FTT proposal

The European Parliament was 'consulted' on the Commission's new 2013 enhanced cooperation proposal. The ordinary legislative procedure, whereby the Parliament has co-equal powers as the Commission and Council, was not applied because the proposal was based on a taxation matter, which is a member state competence.

The Parliament adopted a resolution on 3 July 2013, proposing several amendments to the Commission's proposal. It stated that the FTT's objectives were to "ensure that the financial sector makes a fair contribution to national tax revenues" and to "discourage transactions that do not enhance the efficient allocation of resources by the financial markets".

**Own resources**

The resolution pointed out that, "According to the European Council's conclusions of 8 February 2013 on the Multiannual Financial Framework 2014-2020, part of the revenues from FTT should be allocated to the Union budget as genuine own resources".

The Parliament's position was that "all or part" of the FTT should be used for EU own resources, though the resolution noted the difficulties enhanced cooperation presented to this goal. It notes: "The use of FTT revenue as Union own resources is possible under the enhanced cooperation procedure only if national contributions of participating Member States to the Union budget would be reduced by the same amount and would avoid the disproportionate contribution by participating Member States compared to non-participating Member States."

**Over-the-counter derivatives**

The Parliament resolution expanded the types of financial transactions that should be subject to the FTT, including specifically focusing on high-frequency trading. Importantly, it insisted that, "With a view to strengthening the position of regulated markets, and in particular of stock exchange trading, which is strictly regulated, controlled and transparent, as opposed to unregulated, less controlled and less transparent over-the-counter (OTC) trading, Member States should apply higher tax rates to OTC transactions.

**OTC DERIVATIVES**

A derivative is a financial security that has a value based on an underlying asset or assets – an underlying commodity, currency, bond etc. Over-the-counter (OTC) derivatives trading refers to the largely unregulated trading in derivatives that takes place outside of the framework of regulated markets.

The resolution clarifies that the higher rates "should not apply to financial transactions of OTC derivatives where they objectively reduce risks and therefore serve the real economy".

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**Tax rates**

The Parliament did not specify at what rate OTC derivatives transactions should be taxed at, only saying "Member States shall apply a higher rate" [higher than 0.01%] to these transactions.

It also states that the general rates of 0.1% for shares and bonds, and 0.01% for derivatives, should be the uniform rates, disagreeing with the Commission position that these should be minimum rates.

**Impact on non-participating member states**

Seemingly in a concession to certain member states, the Parliament resolution also stated: "Any harmonisation of FTT amongst participating Member States should not result in extra-territorial taxation infringing the potential tax base of non-participating Member States."

## German-Franco 2019 proposal for a FTT under enhanced cooperation

Years of negotiations and failures to reach agreement on the content of a FTT among the 11 states followed.

In May 2014, an agreement was reached among 10 of the then-11 participating states to apply a tax to equities (i.e., shares) and "some derivatives" by January 2016. Slovenia did not agree. As stated above, Estonia left the enhanced cooperation procedure in December 2015, declaring that the FTT as envisaged would not raise substantial funds and would deter traders.

**The French model – shares only**

In June 2018, Germany and France agreed at a meeting in Meseberg to formulate a new proposal based on the existing FTT in place in France, which taxes transactions only involving domestically issued shares. The two states presented a joint position paper along these lines to the other participating states in January 2019.

At the Council meeting of 14 June 2019 it was revealed that the participating states are discussing a proposal to apply a tax of no less than 0.2 per cent to "the acquisition of shares of listed companies which have their head office in a member state of the EU and market capitalisation in excess of €1 billion".

Policy brief: EU Financial Transaction Tax, August 2020.

The Council note states: “The tax would be levied on the transfer of ownership when shares of listed public limited companies are acquired.”

According to a KPMG analysis, the transactions not subject to the FTT include: “initial public offerings, market making activities, intra-group transactions, repurchase agreements and reverse repurchase agreements, securities lending and securities borrowing buy-sell back and sell-buy back agreements”. There is also an optional tax exemption for pension schemes.

**Distribution of funds raised**

The key sticking point currently among participating states is reportedly the mechanism and formula used to distribute the funds raised between the member states.
A proposal backed by five member states is to distribute the funds according to the states’ gross national income (GNI), regardless of the volume of financial transactions that take place in its territory.

Euractiv, after viewing the proposal, reported that: “According to the estimates included in the discussion documents, Spain would be the main loser, since its revenues would fall by 18.5% to €406 million, compared with estimated revenues of €498 million coming from applying an FTT on its territory.”

Under the GNI formula, Greece, Austria and Portugal would be the big winners (Greece +528.7%, Austria +289.2%, Portugal +100.8%). Spain opposes this method, and German Finance Minister Olaf Scholz is reportedly preparing a compromise proposal.

Revenue raised under the FTT would supposedly go to the EU budget or the – currently non-existent – euro area budget via national contributions. (However, Germany has already indicated that it intends to use the proceeds to pay for a new basic pension starting in 2021.)

All member states are participating in the discussions in order to gain information about the impact of the FTT on their own tax bases, if any. The adoption of the Directive requires unanimous support from the 10 participating states in the Council, following the consultation of the Parliament.

## Analysis of the current FTT proposal

The German-Franco proposal drastically reduces the objectives and scope of the FTT. The new proposal would raise just €3.4 billion per year, according to the German finance ministry (including approximately €1.5 billion for Germany).

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By limiting the scope of the Directive to only stock trading in companies worth more than €1 billion, the FTT will apply to transactions made by approximately 500 companies, including 145 in Germany.

Bonds, derivatives, synthetic investment products and high-frequency trading will not be covered.

Some member states may be worse off in terms of revenue under the proposed FTT. Nine member states already have existing FTTs in place in some form, such as stamp duty (these are Belgium, Cyprus, France, Finland, Greece, Ireland, Italy, Romania and Poland). If a member state joins the enhanced cooperation group it must reform its existing FTTs to align with the EU Directive.

The current FTT proposal will apply only to a small portion of the safest financial transactions. The amount raised per year – €3.4bn – is miniscule. There are no social, environmental or climate-related objectives articulated in the FTT plan.

It will make no discernible contribution towards improving financial stability and discouraging high-risk practices. It is possible that by taxing only the safest transactions, it may have the perverse effect of shifting financial transactions into unregulated markets. Some member states with existing FTTs may see a decline in the amount raised under the EU FTT in comparison with their national schemes.

The funds raised will not constitute new own-resources for the EU; they will go towards the participating member states' national contributions to the EU budget (or future euro-area budget) instead.

This means that instead of being used as a 'Robin Hood' tax as proposed by campaigners – redistributing funds from financial corporations to those on low incomes – the funds raised could theoretically be spent on military, security, or other socially and environmentally damaging projects within the EU budget.

The scale of the economic downturn arising from the coronavirus pandemic means massive public spending and investment will be required to protect incomes, secure jobs, and get to work on the climate-based transformation of our economies.

An ambitious FTT that taxes derivatives and other financial transaction excluded from the current plan is an important tool we can use to this end. Crucially, it is a tool that will not penalise working people and the poor; it will help reduce inequality instead of fuelling it as other proposed, regressive taxes will do.

The German Council Presidency must use its term of leadership to secure such a fair and ambitious tax on financial transactions.

**Table 1: Comparison of 2011, 2013 and 2019 FTT proposals.**

| 2011 COM proposal | 2013 COM proposal | EP position 2013 | German proposal 2019 |
|---|---|---|---|
| Applies to all EU member states | Applies to 11 EU member states under enhanced cooperation | Applies to 11 EU member states under enhanced cooperation | Applies to 10 EU member states under enhanced cooperation |
| Raises approximately €57 billion per year in EU | Raises €30-35bn per year among 11 states | Raises €30-35bn per year among 11 states | Raises €3.5bn per year among 10 states |
| Covers 85% of financial transactions in EU | Covers 85% of financial transactions in EU | Covers at least 85% of financial transactions in EU | Covers financial transactions of only 500 companies in the EU |
| Minimum tax rate of 0.1% on shares and bonds | Minimum tax rate of 0.1% on shares and bonds | Uniform tax rate of 0.1% on shares and bonds | Minimum tax rate of 0.2% to shares of companies worth €1bn+. (Maximum rate of 0.3%).<br><br>Excludes bonds entirely |
| Minimum tax rate of 0.01% on derivatives and other transactions | Minimum tax rate of 0.01% on derivatives and other transactions | Minimum tax rate of 0.01% on derivatives cleared through CCPs, and other transactions.<br><br>Higher rate on OTC derivatives | Excludes derivatives, synthetic investment products and high-frequency trading entirely |
| Funds raised are partly EU own-resources | Funds raised are partly EU own-resources | “All or part” of funds raised are EU own-resources | No funds raised are EU own-resources |

*This analysis of the EU FTT proposal was commissioned by Dr Martin Schirdewan MEP, co-president of the GUE/NGL group in the European Parliament and Die Linke Finance Spokesperson, and is available in German here.*

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