FOCUS MATTERS.

ADVOGADOS

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Financial Transaction Tax

“Even if it is not possible to establish the Financial Transaction Tax throughout the EU, enhanced cooperation should be envisaged, in order to prevent the common market to be harmed”

Notwithstanding the difficulties that the European Commission (the “Commission”) has encountered, and struggled with, to obtain the approval for the Financial Transaction Tax (the “FTT”) from all the 27 Member States of the European Union (the “EU”), it is important to analyse such proposal, granting an overview of its bases, it’s possibilities of application, even if trough a mechanism of enhanced cooperation, such as it’s effects and next steps until it’s conclusion and entering into force.

On 28 September 2011 the Commission presented a proposal for the introduction of a financial transaction tax in the 27 Member States of the EU.

Such proposal seeks to set up a harmonised tax at EU level to create a solid internal market for financial services. This tax would prevent tax evasion, avoid double taxation and minimise distortions of competition within the EU’s Single Market. The Commission has decided to propose this new FTT to (i) ensure that the financial sector makes a fair contribution at a time of fiscal consolidation in the Member States and (ii) to strengthen the EU Single Market.

Nowadays 10 Member States already possess a FTT similar to the one the Commission has proposed. However, this proposal seeks to impose minimum tax rates and to harmonize the different taxes over financial transactions that already exist in the Member States.

Definition of FTT

A FTT is a tax applied to financial transactions, usually at a very low rate. A financial transaction applies for the exchange of financial instruments ((securities, bonds, shares and derivatives) between banks or other financial institutions.

The European Parliament (the “EP”) voted in favour of the Commission proposal on 23 May 2012, and issued an opinion defending the need to better design the FTT in order to capture more traders and make evasion unprofitable. The EP, although presenting a series of amendments to the proposal, considers that such proposal should be adopted, even if it fails to be adopted by all Member States.

The Commission proposed minimum tax rates for the trading of the bonds and shares of 0.1% and 0.01% for derivative products. The EP considered such tax rates to be sufficient.

Based on the original proposal, the FTT was only based on a “residence principle”. The transactions will be subjected to the FTT if at least one party to the transaction is established in a Member State.

The EP imposed an “issuance principle” whereby financial institutions located outside the EU would also be obliged to pay the FTT if they traded securities originally issued within the EU.

Tax base

One of the major goals of the Commission and of EP is to prevent the evasion to FTT, turning such an evasion more unprofitable than to pay it, trough minimum tax rates. As such, the tax base proposed by the Commission is very broad, aiming to reduce the risks of tax evasion and dislocation of the markets. The tax rate above mentioned is the minimum rate, although, all Member States will be free to apply higher tax rates.

Benefits of the FTT

The Commission aims for the FTT to be applied in all 27 Member States, with the purpose to contribute, like any other tax does, to the public finances. As for the FTT, part of the revenue will go to the EU budget and another part will help finance the budgets of Member States. The Commission estimates that, at a rate of 0.1% to bonds and shares and 0.01% for derivatives, the tax could raise € 57 Billion per year.

It is intended to benefit the companies and the citizens with the FTT, trough the increase in the public accounts, that can be utilise to create economic growth and bring prosperity to the EU.

How will the FTT be charged?

The tax burden will fall on the financial institutions (banks, investment companies, insurance companies, collective investments undertakings and their managers, alternative investment funds such as hedge funds and others). The FTT will be applied to all transactions if at least one party to the transaction is established in a Member State and to all financial institutions that trade securities originally based within the EU.

The FTT will be paid immediately by financial institutions to Member States on the basis of the transactions undertaken, before netting and settlement.

Mitigation of the risk of the tax being passed on to consumers

To prevent such an indirect risk, the Commission has proposed that the FTT should cover only transactions where financial institutions are involved, taxing only the financial sector, not their clients. However, in case private households and enterprises were to purchase or sell financial products, financial institutions could pass on the tax, charging an amount for each transaction.

The Commission will be looking for excessive amounts charged by financial institutions and will intervene if it happens.
Of an extreme importance is the fact that the transactions made on the primary market are exempt from the FTT. This will prevent investments that contribute to the real economy from being subject to the tax.

Next steps

The EP has issued an opinion on the proposal and such amended proposal was discussed by all Member States in the EU's Council of Ministers on 22 June 2012. The Commission will present it to the G20 Summit in November 2012.

Even though some of the Member States are against the application of a FTT, the Commission and the EU intend it to enter into force, even if failing to do so in all Member States, envisaging an enhanced cooperation.

It was proposed by the Commission and adopted by the EP that the FTT will be adopted until 31 December 2013, entering in force on 1 January 2014.

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