

MEMO# 27081

March 7, 2013

Financial Transaction Tax ("FTT") Proposal Under European Union Enhanced Cooperation Procedure; Related Coalition Letter

[27081]

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TO: SECURITIES OPERATIONS ADVISORY GROUP RE: FINANCIAL TRANSACTION TAX ("FTT")
PROPOSAL UNDER EUROPEAN UNION ENHANCED COOPERATION PROCEDURE; RELATED
COALITION LETTER

Details of the EU FTT Proposal Released

The European Commission ("EC") has released a detailed proposal for a Council Directive to implement a financial transaction tax ("FTT") under the European Union's ("EU's") enhanced cooperation procedures. Presently, eleven countries [\[1\]](#) are considering supporting the proposal. The EU estimates that the FTT could raise €31 billion per year.

Introduction

The tax would apply broadly and have significant extraterritorial effect. Specifically, the FTT would apply to a transaction involving a financial institution so long as (1) either party is "established" in a participating Member State ("MS") or (2) the financial instrument being traded is issued in any participating MS. The proposal thus combines a "residence" principle (based upon the investor's status) with an "issuance" principle (based upon the traded instrument's status).

The tax rate, set separately by each MS, would be at least 10 basis points for most financial instruments and at least 1 basis point for derivatives. For financial instruments, the tax liability generally would be based upon the purchase price. For derivatives, the tax liability generally would be based upon notional amount; the proposal contemplates an anti-abuse rule that would apply if the terms of the derivative were designed to minimize the notional amount.

Scope (Establishment)

The proposal's scope is very broad. [\[2\]](#) A financial transaction would be taxable if at least one party is "established" in a participating member state ("MS") and a financial institution

established in a participating MS is a party to the transaction. The financial institution may be acting (1) for its own account or for the account of another person or (2) in the name of a party to the transaction.

“Establishment” likewise would be defined very broadly. [\[3\]](#) Separate rules are provided for financial institutions and for others (such as operating companies and individuals).

A financial institution would be treated as established in a participating MS if, among other things: (1) it is authorized by the authorities of that MS to act; (2) its registered seat is within that MS; or (3) it has a branch within that MS. A financial institution that is not treated as established in a participating MS under the above tests nevertheless would be treated as so established if: (1) it is a party to a financial transaction with another financial institution that is established in a participating MS (under the above tests) or with a party that is not a financial institution but that is treated as established in the MS; or (2) it is a party to a financial transaction in a financial instrument such as a stock or bond, in a structured product, that is issued in a participating MS, or in a derivative that is traded on an organized venue or platform.

A person that is not a financial institution (including, among others, operating companies and individuals) would be deemed to be established in a participating MS if: (1) its registered seat or its permanent address (in the case of an individual) is in the MS; (2) it has a branch in that MS in respect of financial transactions carried out by that branch; or (3) it is a party to a financial transaction in a financial instrument such as a stock or bond, a structured product, or an exchange-traded derivative that is treated as issued in a participating MS.

The term financial institution also would be defined broadly. [\[4\]](#) The term expressly would include, among others, investment firms, funds organized as UCITS (and their managers), alternative investment funds (and their managers), pension funds, and similar vehicles. Thus, the FTT expressly would apply to all portfolio transactions involving investment funds and pension funds.

Scope (Transactions)

Most financial transactions would be subject to the FTT. The tax would apply not only to purchases and sales of stocks and bonds and transactions involving derivatives, but also to exchanges of financial instruments, to repurchase and reverse repurchase agreements, and to securities lending and borrowing agreements. The proposal contains an anti-avoidance rule.

The proposal would exclude primary market transactions from FTT. Primary market transactions would include initial issuances of securities (such as stocks and bonds) and transactions with specified institutions such as the European Central Bank. Because the redemption of shares or units in a fund would not be treated as a primary market transaction, the redemption would be taxable.

Most transactions subject to FTT, such as the purchase of a stock, would be treated as two separate transactions. Only one financial transaction would be deemed to arise, however, on repurchase and reverse repurchase agreements and on securities lending and borrowing agreements. To prevent certain cascading of tax, a financial institution would not be liable for the tax if the financial institution acted in the name of or for the account of another financial institution; only this second financial institution would pay the tax.

In the investment company context, each purchase or sale of a portfolio security subject to the FTT would cause the fund to incur a 10 basis point tax; the fund also would be jointly and severally liable for the 10 basis point tax liability of its financial institution counterparty. Purchases of fund shares or units would not be a taxable event under the FTT. Investor redemptions, however, would cause the fund to incur tax if either the fund or the fund investor were established in a participating MS.

Chargeability

FTT would be chargeable for each financial transaction at the moment it occurs and payable by the financial institution involved.

ICI and Coalition Letter to EU Tax Commissioner

The ICI and other trade associations sent the attached letter to EU Tax Commissioner Algirdas Semeta reiterating our strong opposition to FTTs. The letter expresses our serious concern with FTTs and with this FTT's extraterritorial impact. The proposal's use of both residency and issuance tests is both unprecedented and inconsistent with existing norms of international tax policy. Finally, the letter summarizes the substantial negative impact of an FTT on investors and markets.

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[Attachment](#)

endnotes

[1] The eleven EU member states that are considering the proposal are Austria, Belgium, Estonia, France, Germany, Greece, Italy, Portugal, Slovakia, Slovenia, and Spain. These countries are proceeding together because an EU-wide proposal advanced by the EC did not receive the unanimous support required for such a comprehensive tax proposal.

[2] See Article 3 of the proposal.

[3] See Article 4 of the proposal.

[4] See Paragraph 1(8) of Article 2 of the proposal.