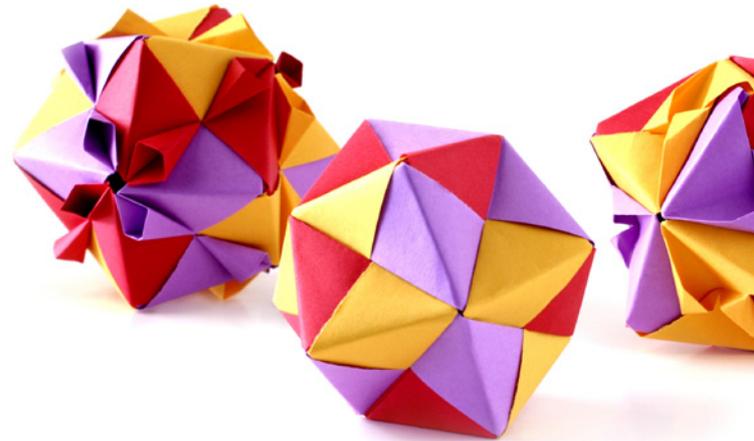


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Europe's Financial Transaction Tax and what it means for Australians



As we recover from the global economic downturn, governments around the globe continue to devise remedial packages of law and policy to ensure all financial-related undertakings are under tight scrutiny and regulation.

One of the more recent developments is the European Commission's revised proposal for a financial transaction tax (**FTT**), a proposal which has its roots in the global financial crisis, and whose stated objectives include exacting a contribution from financial institutions for the costs of the crisis, and seeking to deter future crises, blurring the line between revenue and regulatory measures.

Background

The FTT was initially proposed by the European Commission in the wake of the financial crisis to apply to the whole of the EU, but some Member States (such as Luxembourg, Sweden and the United Kingdom) rejected the proposal.

Despite this, sufficient support for the FTT remained for it to apply to Belgium, Germany, Estonia, Greece, Spain, France, Italy, Austria, Portugal, Slovenia and Slovakia (the **FTT zone**). These are the participating Member States. Some of the participating Member States in the FTT zone have already implemented their own domestic FTTs or are in the process of doing so, which helps the Commission's

argument that an FTT for the FTT zone is needed to avoid fragmentation.

This is the first time that the EU has considered a proposal for a partially harmonised tax. It relies upon a seldom used procedure within EU Treaties, the enhanced cooperation procedure (**ECP**). After the EU Council authorised the use of the ECP for the FTT on 22 January 2012, the Commission issued a revised proposal for the tax on 14 February 2013. There is an intention for the FTT to apply from 1 January 2014, with participating Member States adopting local rules to implement the FTT by 30 September 2013, although it is not clear if such a timeframe is realistic.

Proposal in brief

The objectives of the proposed FTT are to:

- harmonise legislation concerning indirect taxation on financial transactions,
- ensure that financial institutions make a fair and substantial contribution to covering the costs of the recent crisis and creating a level playing field with other sectors from a taxation point of view, and
- create appropriate disincentives for transactions that do not enhance the efficiency of financial markets, thereby complementing regulatory measures to avoid future crises.

The FTT will be imposed by participating Member States only. It is imposed on a broad range of financial institutions (eg credit institutions, funds, securitisation vehicles or any other entity if the average annual value of the financial transactions it has entered into constitutes more than 50% of its turnover). Financial institutions established in the FTT zone will be subject to the FTT when they buy and sell securities, conclude derivatives and materially modify either transaction. In addition, the tax will apply with **extra-territorial effect** in two ways: (1) merely transacting with a counterparty in the FTT zone (whether or not the counterparty is a financial institution) will subject the other party, if it is a financial institution, to the FTT, and (2) if a security is issued by an entity incorporated or registered in the FTT zone, any financial institution which is a party (either for its own account or for the account of another person) to the sale of the security will be subject to the FTT, wherever they are located, subject to limited exemptions.

The tax applies to the trading of shares, bonds and other securities, but also to derivatives, based on the notional value of the derivatives. Exemptions are proposed for limited types of transactions (eg primary market transactions and spot currency transactions) and limited institutions (eg central counterparties and central securities depositories), however, there is no wide market maker exemption, which is likely to result in multiple charges on the simple sale of securities over an exchange.

The FTT on buying and selling securities will be charged at a minimum rate of 0.1%. The minimum rate which applies to concluding or modifying derivatives is 0.01% based on notional value. The FTT could apply to both counterparties to a transaction.

There is a general anti-abuse rule to prevent avoidance of the FTT, with specific provisions aimed at depositary receipt programmes.

What does this mean for Australians?

The extra-territorial effect of the tax means that Australian parties may be subject to the FTT in a wide range of situations. Australian financial institutions could be subject to the FTT where they deal in securities or derivatives issued by an entity in the FTT zone, or where they engage in trading in securities or derivatives with an FTT zone entity (including the Australian branch of a FTT zone headquartered entity). There is a safe harbour provision according to which a financial institution will not be liable

for the FTT if it is able to demonstrate that there is no link between the economic substance of the transaction and the FTT zone, however at this stage it is difficult to confirm in which circumstances the safe harbour provision will apply.

Measures are in place to ensure that the FTT is collected even where the taxpayer is located outside of the FTT zone, for example by making counterparties secondarily liable for the tax. This may result in efforts by counterparties to ensure the cost of the FTT is borne by clients.

It is also possible that the FTT will cause a relocation of certain activities out of the FTT zone, which may generate benefits outside of the FTT zone, although this is not an intended outcome.

The FTT raises a number of legal issues in relation to legality, enforceability, extra-territoriality and the application of taxation treaties. The United Kingdom has challenged the validity of the FTT before the European Court of Justice on the basis of its extra-territoriality aspects.

Watch this space...

The above content is based on current information about the FTT proposals and are subject to change as discussions on FTT within the EU currently progresses.



Siamak Mostafavi
Partner – Paris
Tel +33 14 00 65 337
siamak.mostafavi@allenoverly.com



Andrew Stals
Partner – Sydney
Tel +612 9373 7857
andrew.stals@AllenOverly.com