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THE GLOBAL REACH OF THE PROPOSED EU FINANCIAL
TRANSACTION TAX DIRECTIVE: CREATING MOMENTUM
THROUGH INTERNAL LEGISLATION?

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Abstract

In the wake of the 2008 financial crisis, taxation of the financial sector has forcefully re-emerged on the European Union political agenda. One proposal – rightly or wrongly – received much political attention: a broad-based tax on financial transactions. What had for years existed as a utopia in the minds of grass roots movements, reached a legal and political milestone during Commission President Barosso’s State of the Union speech on 28 September 2011. There he presented a proposal for an EU Directive on a financial transaction tax installed across the 27 EU Member States. It was then an explicit objective of the Union that it would lead by example, and that its pan-European implementation would prove the global feasibility of a financial transaction tax (FTT). The Cannes G-20 Meeting early November 2011 under French chairmanship was expected to launch the global dimension of the FTT, using the momentum created by the proposed EU FTT Directive two months earlier. However, the European sovereign debt crisis caused the EU to teeter on the brink of political, financial and economic collapse, and momentum for a global FTT seemed utterly lost. Nonetheless, political discussions within the Union continued, and at the time of writing – Spring 2012 – discussions in the Council were on-going for some form of pan-EU.

The global implementation of the EU FTT Directive is a tale of divided political views between Member States of the Union, the pursuit of an elusive single voice in the G-20, and the use of legal instruments for political reasons. In this paper, it will serve as a case-study for the EU seeking to shape global financial governance in the wake of the 2008 financial crisis, in line with its binding, law-oriented mission statement of Article 21 TEU. In light of this, this contribution investigates EU (im)potence to affect legal and institutional processes in global (financial) governance.

Keywords

Financial Taxation – European Union – Global Financial Governance – G20

1. Introduction

In the wake of the 2008 financial crisis, taxation of the financial sector has forcefully re-emerged on the European Union political agenda.¹ Since then, several EU Member States and the European Parliament have sought to stimulate this idea in the form of a financial transaction tax (FTT). What had for years existed as a political utopia in the minds of grass roots movements, reached a legal and political milestone during Commission President Barosso's State of the Union speech on 28 September 2011. There he presented a proposal for an EU Directive on a financial transaction tax installed across the 27 EU Member States, to serve as an example for the world. In a previous paper I have outlined key features of such a global implementation.² I argued that the Union would have to propose a binding multilateral treaty, with as broad as possible a global membership. This multilateral Convention would establish the legal framework within which to levy, manage and disperse the proceeds of an international FTT – and in short, would imply thorough reform of the global financial governance system as it exists at present. The Cannes G-20 Meeting early November 2011 under French chairmanship was expected to launch the global dimension of the FTT, using the momentum created by the proposed EU FTT Directive two months earlier. However, the European sovereign debt crisis and Greek Drama yet again reached new heights, and with the EU teetering on the brink, momentum for a global FTT seemed utterly lost. Nonetheless, political discussions within the Union continued, and at the time of writing – Spring 2012 – discussions in the Council were on-going. Thus, the EU proposal may yet become law, if not at global, then at regional level.

The global implementation of the EU FTT Directive is a tale of divided political views between Member States of the Union, the pursuit of an elusive single voice in the G-20, and the use of legal instruments for political reasons, with an as of yet unwritten conclusion. In this paper, it will serve as a case-study for the EU seeking to shape global financial governance in the wake of the 2008 financial crisis, in line with its binding, law-oriented mission statement of Article 21 TEU. In light of this, this contribution investigates EU (im)potence to affect legal and institutional processes in global governance required for implementation of the FTT.

2. The Union's Mission in Global Financial Governance

The 2001 Laeken Declaration on the future of the European Union strongly asserted a global role for the EU in its characteristically grand language:³ *‘Does Europe not, now that is finally unified, have a leading role to play in a new world order, that of a power able both to play a stabilising role worldwide and to point the way ahead for many countries and peoples?’* The European Convention started work soon after that declaration was made, in order to draw up a Constitutional Treaty for the European Union. In an early draft produced by the Commission (called the Penelope project), that institution's proposal of December 2002 contained the following provision under the heading ‘external economic relations policy’:⁴ *“Article III – 97 External economic action by the Union shall contribute to the harmonious development of the world economy. To that end the Union shall adopt a single*

¹ This contribution was closed on 21 March 2012.

² Bart Van Vooren, *The EU as a global Robin Hood: Proposal for a Multilateral Convention on a Global Financial Transaction Tax*, CLEER Working Papers 2011/4 (2011). [Hereafter: Van Vooren, EU as Robin Hood]

³ European Council, Laeken Declaration on the Future of the European Union, 14-15 December, 2001, subheading ‘Expectations of Europe's citizens’.

⁴ European Commission, *Feasibility Study, Contribution to a Preliminary Draft, Constitution of the European Union*, 4 December 2002, Available from: http://ec.europa.eu/economy_finance/emu_history/documents/treaties/Penelope%20pdf_en.pdf [Last Accessed 19 March 2002] I am grateful to Joris Larik for pointing me to this provision.

position in relations with non-member countries and in international organisations with responsibilities for economic and financial matters. It shall support the effectiveness and transparency of the financial markets in order to reduce financial volatility and speculation at global level.” This Commission proposal took the EU single voice far beyond the comparatively narrow scope of the Common Commercial Policy. However, the call for unified EU representation in global economic governance writ large was not picked up by the Convention, and it did not find its way into the draft Constitution or the Lisbon Treaty. Should this have happened, a strong case could have been made that the Union would have a legally binding obligation to implement a financial transaction tax, or a global measure with equivalent effect of reducing financial volatility and speculation.⁵ Even so, the Union could still reap great benefits from the successful global implementation of the FTT.⁶ First, success in this regard would be supportive of the Union’s self-imposed image of the value-based international actor;⁷ and second, it would do much to provide post-Lisbon legitimacy towards its own citizens through effectiveness as an international actor. An FTT would have as its purpose the financing of global public goods such as the Millennium Development Goals and additional funding to climate change; and therefore respond to calls for a fairer contribution of the financial sector to society writ large. Additionally, such a tax would have a significant regulatory impact towards a more stable financial system which is currently dominated by non-binding soft law.⁸ In sum, the FTT would lead to - and require a sea-change to international financial law and governance with the European Union guiding the way in line with its constitutional objectives.⁹

Even though no mission statement for the EU in global financial governance has been included in EU primary law, the more general legal obligations to that end are nevertheless pertinent. A role for the Union whereby it ‘stabilizes’ the world, and ‘points the way ahead’ is not merely a moral imperative, but a legally binding obligation embedded in primary law. Article 3(5) TEU states that in its relations with the wider world, ‘*the Union shall(...) contribute to peace, (...) the sustainable development of the Earth, solidarity and mutual respect among peoples, free and fair trade, eradication of poverty (...) as well as to the strict observance and the development of international law, including respect for the principles of the United Nations Charter.*’ (Emphasis added) The language “shall” indicates the binding nature of this mission statement, which has been confirmed by the Court of Justice in a recent judgment of 22 December 2011 concerning the global reach of the Emissions Trading Scheme. Here the Court affirmed that this article imposes a substantive, legal obligation on the Union “to contribute to the strict observance and the development of international law.”¹⁰ Thus, the Union is not just morally, but in fact legally obliged to pursue equality amongst wealthy and poorer nations, to support their development and ensure ‘fairness’ between them. In doing so, the TEU not only imposes substantive requirements on EU international relations, but also a strong methodological imperative: according to Article 3 TEU and confirmed in Article 21(1) TEU, the EU ‘*shall be guided by the principles which have inspired its own creation and which it seeks to advance in the wider world: (...) respect for the principles of the United Nations Charter and international law.*’ In other words, the Union must pursue a just and fair global order, entrenched in multilateral

⁵ On such effects see Van Vooren, EU as Robin Hood, 10-14.

⁶ Though certainly, the hazards and pitfalls are equally great. See Van Vooren, *o.c.*, EU as Robin Hood.

⁷ U. Khaliq, *Ethical Dimensions of the Foreign Policy of the European Union - A Legal Appraisal* (Cambridge, Cambridge University Press, 2008); R.Petrov and P. Leino, ‘Between ‘Common Values’ and Competing Universals - The Promotion of the EU’s Common Values through the European Neighbourhood Policy’, 15 *European Law Journal* (2009).

⁸ Chris Brummer, *Why Soft Law Dominates International Finance - and Not Trade*, 13 *Journal of International Economic Law* 623-643(2010), 627.; Ernst Baltensperger and Thomas Cottier, *The Role of International Law in Monetary Affairs*, 13 *Journal of International Economic Law* 911-937(2010), 935.

⁹ See Joris Larik, “Entrenching Global Governance: The EU’s Constitutional Objectives caught between a sanguine world view and a daunting reality”, in Bart Van Vooren, Steven Blockmans & Jan Wouters (eds), ‘The EU’s role in global governance: the legal dimension’, Oxford University Press, forthcoming 2012.

¹⁰ Case C-366/10, Air Transport Association of America (ATAA), of 21 December 2011, nyr, para 101.

solutions based on the rule of law. The global implementation of a financial transaction tax through a multilateral, binding international convention requiring unprecedented positive change to international financial governance does exactly that.

If the argument stemming from EU primary law is perhaps slightly abstract and legalistic, the connection to expectations of European citizens should be less so. Indeed, the financial transaction tax is a concrete iteration of where the Laeken Declaration in the abstract invoked of EU citizens' wishes. This is underlined by the Commission's public consultation on the FTT which ended in April 2011. That consultation clearly showed that civil society across the European Union broadly supports the financial transaction tax.¹¹ From the Commission's summary report,¹² it is clear that NGOs and trade unions are strongly in favour of a broad-based financial transactions tax and that individual citizens also 'generally favour' such a broad-based levy. Conversely, and unsurprisingly, financial organisations and businesses, consultancies and their relevant representative organisations generally oppose any and all types of additional tax burden on the financial sector or financial markets in general.¹³ Thus, given the broad popular support amongst European citizens it is submitted that successfully working towards the FTT at global level would bring the Union *legitimacy through effectiveness*. Individual Member States will be unable to exert sufficient influence in the G-20 to realize a global financial transaction tax, but should the Union manage to speak with its proverbial single voice in a sustained lobbying effort at the highest echelons, success may be within reach with commensurate effects on the EU's standing in the hearts and minds of European citizens.

In the remainder of this contribution I shall trace the EU's efforts in placing the FTT on the global political agenda, so as to draw conclusions on the EU's ability to deliver on its mission statement of pursuing a multilateral law-based governance agenda, and to deliver upon its citizens' wish have the financial sector contribute more fairly to society writ large.

3. A Global FTT: Political Context at EU and International Level

At their September 2009 meeting in Pittsburgh, political momentum post-financial crisis was such that G-20 leaders agreed to pursue a number of deep changes to global economic governance. They agreed to set up 'a framework for strong, sustainable and balanced growth', 'an international regulatory system for banks and other financial firms that would reign in the excesses that led to the crisis', and 'to reform the global economic governance architecture to meet the needs of the 21st century'.¹⁴ Through these transformations, they wished to curb excessive risk-taking and recklessness in the global financial system, which was perceived as the root cause for the financial crisis of 2008. However, the Pittsburgh communiqué did not refer to international financial taxation in any form, and focused on reforming capital requirements,¹⁵ compensation in the financial sector, improved over-the-counter (OTC) derivatives markets,¹⁶ and moral hazard problems related to systemically important financial institutions (SIFIs). It did however request that the IMF prepare a report 'on the range of options (...) as to how the financial sector could make a fair and substantial

¹¹ All responses to the consultation as well as a summary by the Commission are available at: <http://ec.europa.eu/taxation_customs/common/consultations/tax/2011_02_financial_sector_taxation_en.htm> (Last accessed 16 August 2011)

¹² Commission summary report, May 2011, available at: <http://ec.europa.eu/taxation_customs/resources/documents/common/consultations/tax/financial_sector/summary_results_en.pdf>.

¹³ 'Banks and markets oppose financial transaction tax, *EurActiv*, 18 August 2011 <<http://www.euractiv.com/en/euro-finance/banks-markets-oppose-financial-transaction-tax-news-507022>>.

¹⁴ G-20 Leaders' Statement, The Pittsburgh Summit, 24-25 September 2009, 2.

¹⁵ *Ibid*, 8.

¹⁶ *Ibid*, 9.

contribution toward paying for any burdens associated with government interventions to repair the banking system.¹⁷ The IMF delivered that report by the June 2010 G-20 summit in Toronto.¹⁸ In the lead-up to that event, the European Council strongly voiced its support for the FTT:

‘The EU should lead efforts to set a global approach for introducing systems for levies and taxes on financial institutions with a view to maintaining a world-wide level playing field and will strongly defend this position with its G-20 partners. The introduction of a global financial transaction tax should be explored and developed further in that context.’¹⁹

Upon delivery of the report the Toronto Summit merely ‘thanked’ the IMF, and beyond the mentioning of a few generic principles in the final summit communiqué, the EU did not succeed at having the idea discussed more substantively at that meeting.²⁰ What seemed a tempest in a teapot was no longer even mentioned in the Declaration of the Seoul Summit in November 2010. The communiqué from the February 2011 G-20 meeting of Finance ministers and Central Bank governors only cursorily referred to the financial transaction tax, in preparation of the G-20 meeting in Cannes on 4 November 2011. The intensions of the French Presidency were quite clear in this regard. On 20 September 2010, Nicolas Sarkozy addressed the General Assembly of the United Nations, where he stated that:

‘(...)as the future president of the G-20 and the G8 (...) I will strive to promote the idea of innovative financing (...)[W]e must find new sources of financing to fight against poverty (...)We can decide here to implement innovative financing, the taxation of financial transactions. Why wait? Finance has been globalized. Why shouldn’t we demand that finance contribute to stabilizing the world through a minuscule tax on each financial transaction?’ (emphasis added)

Whether President Sarkozy was truly committed to the fight against poverty, or saw this as a pet project to woo voters in preparation for the French presidential elections in April 2012, is a political question beyond the purview of this contribution. Undoubtedly both factors played an important role, with the end result being that France was the most vocal EU Member State favouring the global, and if not possible, EU-level implementation of the financial transaction tax. However, this points to the first central obstacle to the EU pursuing the global implementation of the financial transaction tax. Indeed, in the highlighted portion of the quoted speech by Mr. Sarkozy, it said that *he himself*, as president of the G-20 and G-8 would be promoting the idea of a financial transaction tax. This in opposition to the 27 Member States *qua* European Union, using its political capital and diplomatic resources to convince the global community of the merits of this idea. The European Council of June 2010 may have adopted conclusions that it support the exploration of a global financial transaction tax, but the Member States themselves are entirely divided as to whether this is truly a key issue on its international relations to-do list.

The United Kingdom and Sweden have been the most vocal, sceptical Member States on the merits of this idea. For example, speaking in September 2010 the Chancellor of the Exchequer stated that he could not see in practice how the FTT would work, and that ‘while it has been discussed for many decades, it would be discussed for many more decades to come.’²¹ Germany had been more receptive to the idea. This EU Member State indeed defends the FTT in principle – with its Finance Minister stating that the technical problems are not insurmountable, and that the tax provides an answer to the financial sector contributing its fair share to financing public coffers, but he stated explicitly that his

¹⁷ *Ibid*, 10.

¹⁸ International Monetary Fund, *A Fair and Substantial Contribution by the Financial Sector*, Final Report for the G-20 (June 2010).

¹⁹ European Council Conclusions, Brussels, 17 June 2010, 6-7.

²⁰ K. Lannoo, ‘The EU’s Response to the Financial Crisis: A mid-term review’, CEPS Policy Brief No. 241 (April 2011), 6.

²¹ ‘Finance Ministers Fail to Agree on EU Financial Transaction Tax’, *Taxation International* 7 September 2010.

country would not introduce such a tax unilaterally.²² The first crucial obstacle to Union success on the international scene as regards the financial transaction tax therefore lies within itself: On the one hand we have France, supported by other Member States such as Austria, Belgium, the Netherlands, Italy, and Spain, in favour of the global or EU financial transaction tax. On the other hand we have the UK joined by Malta, the Czech Republic and Sweden who are far more sceptical of the idea. These countries offer legal, political and economic resistance to the notion that the FTT would provide for a fairer contribution of the financial sector; that it would stabilize financial markets, and that it would remove much of the ‘useless’ gambling-like financial transactions. One oft-quoted example is Sweden, having unsuccessfully adopted such a tax similar to the FTT from the mid-1980s. The tax was progressively widened in scope and heightened in rate, and by 1990 more than 50% of its securities trading activity moved to London and other financial centres.²³ Because of this real risk of geographical relocation, Sweden is urging other G-20 countries not to adopt the FTT, but rather to opt alternatives to the taxation of financial transactions.²⁴ Whether or not the Swedish example is due to design flaws in the tax, in political minds there is an undeniable apprehension towards any risk of geographical relocation with commensurate effects on financial centres and national economies. Given the crucial role of London in global finance, and commensurate revenues for UK public coffers, the United Kingdom is the most vocal intra-EU opponent to the EU-wide or global implementation of the financial transaction tax. The reasons for this are not merely related to the risk of relocation of ‘the City’ to third countries, but rather of a public financial nature. Indeed, the United Kingdom actually has a form of financial transaction taxation, from which it receives up to six billion pounds annually.²⁵ A global or EU FTT with funds earmarked for funding climate change or the fight against global poverty is therefore not beneficial for UK public budgets.

As regards support from the EU institutions, the European Parliament is most supportive of the FTT. In a Resolution of 8 March 2011,²⁶ the EP stated that, in its opinion, the EU should promote the introduction of an FTT at global level, failing which the EU should implement an FTT at European level as a first step.²⁷ In spite of the cold reception at G-20 level in June 2010, during 2011 the idea of an EU-level financial transaction tax has slowly begun to gain traction: in June 2011 Commission President Barroso spoke favourably of that option, and he indicated that during the autumn of 2011 the Commission would publish a proposal to that effect.²⁸ Similarly, at the joint Sarkozy-Merkel meeting of 16 August 2011,²⁹ both leaders stated that they would push towards taxing ‘corporate’ transactions.³⁰ The idea(1) underlying the European implementation of the financial transaction tax is that the Union would ‘lead by example’, and that other nations would follow suit once the EU has proven that the FTT does not have the feared relocation effects on financial markets. However, at the technocratic level that enthusiasm has so far not been uniformly shared with political leadership.

²² ‘Finance Ministers Fail to Agree on EU Financial Transaction Tax’, *Taxation International* 7 September 2010.

²³ European Parliament, Special Committee on the Financial, Economic and Social Crisis, ‘Crisis Management, Burden Sharing and Solidarity Mechanisms in the EU: A Follow-up Study to Financial Supervision and Crisis Management in the EU’, (June 2010), 42.

²⁴ However, the Leading Group report argues that this is a poor example due to design problems in the Swedish tax. See note 58, 17.

²⁵ European Commission, *Impact Assessment accompanying the proposal for a Council Directive on a common system of financial transaction tax and amending Directive 2008/7/EC*, Vol 9, Brussels 28 September 2011 SEC(2011) 1102 final

²⁶ European Parliament, Resolution on innovative financing at global and European Level, (8 March 2011).

²⁷ *Ibid.*, para 16

²⁸ ‘Barroso to push for financial transaction tax’, *European Voice*, 21 June 2011.

²⁹ A transcript of the press conference is available at: <<http://www.businessinsider.com/live-coverage-the-big-merkel-sarkozy-meeting-youve-been-waiting-for-2011-8>>.

³⁰ ‘Merkel and Sarkozy plan ‘true economic government’’, *EU Observer*, 18 August 2011.

Politically the tax Commissioner may support the FTT,³¹ but in reality the Commission services clearly take a more sceptical stance. During the second half of 2010, the Commission published two thoroughly researched Communications which clearly disfavour the FTT idea (both at EU or global level) on the basis of technical, legal and institutional hurdles.³² We can thus already observe that a second obstacle to the EU acting as an effective global actor is institutional: a disjunction between the technocrats' – not wholly unjustifiable – belief that the EU better spend resources on less utopian pursuits than the global FTT, and the top-down political pressure to work out a credible proposal and give it their full backing. This tension was replicated in conversations by the author with an official of DG ECFIN,³³ and was also put as a question of the House of Lords EU select committee to Commissioner Semeta: “My understanding was that your own directorate and that of ECFIN were sceptical in giving that advice to the Commission President but that Mr Barroso wanted to bring about and propose the financial transaction tax as a kind of counterweight at the time of the financial crisis. Were those the origins? Did you give advice that FTT was a difficult thing to introduce?”³⁴ When the Commissioner avoided the question, the Chairman of the Committee continued: “I understand that, but did you have reservations when you discussed it in the Commission about whether this was a viable tax and should be brought forward? Did you and DG ECFIN have those reservations?”³⁵ Mr. Semeta replied that his services had initially concluded that a financial activities tax³⁶ was equally viable to the financial transaction tax, but that they decided to present the latter for the FTT provided greater potential revenues. However, the scenario that it was President Barroso who pushed the Commission services to draw up an FTT proposal is evidenced by the fact that Commissioner Semeta in a speech of October 2010 has gone on record *against* the transaction tax.³⁷ Thus it happened that on 28 September 2011 in his “State of the Union” speech, Commission President Barroso presented a proposal for an EU Directive on the FTT, to be implemented by 1 January 2014 across all 27 Member States.³⁸ Speaking to the House of Lords EU Select Committee on 16 February 2012, Commissioner Šemeta, strongly defended the EU-line, and confirmed that this EU-level proposal must be seen as a stepping stone to the eventual global implementation of the FTT. He also made explicit reference to the need to have the UK on board if this is to be successful:³⁹

“An EU financial transaction tax can help to address many of the major challenges that we are confronted with as a Union today. It will deliver significant revenues, complement our regulatory framework for a more stable and responsible financial sector and contribute to a stronger single market. Moreover, by implementing a well-designed and well-functioning FTT across Europe, we can pave the way for a global approach, an objective which, like us, the UK Government have also committed to within the G20. An EU FTT can achieve this without compromising our competitiveness, without increasing unemployment or driving business from Europe. An EU FTT can achieve this without undermining the strength of the financial services industry in the EU. It is

³¹ Algirdas Šemeta EU Commissioner for Taxation and Customs Union, Audit and Anti-Fraud, ‘Taxing the Financial Sector’ Press Conference Brussels, 7 October 2010, SPEECH/10/530, 07/10/2010.

³² Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions on Taxation of the Financial Sector, Brussels COM(2010) 549/5; European Commission Staff Working Document, Taxation of the Financial Sector, Brussels COM(2010) 549.

³³ Conversation with official of DG Tax, October 2011.

³⁴ House of Lords, Select Committee on European Union, Unrevised transcript of evidence taken on the Financial Transaction Tax, 16 February 2012, 4.

³⁵ Ibid.

³⁶ A tax on the balance sheet of a financial institution rather than the transaction itself.

³⁷ Algirdas Šemeta EU Commissioner for Taxation and Customs Union, Audit and Anti-Fraud “Taxing the Financial Sector”, Press Conference Brussels, 7 October 2010, SPEECH/10/530, 07/10/2010

³⁸ European Commission, *Proposal for a Council Directive on a common system of financial transaction tax and amending Directive 2008/7/EC*, Brussels COM(2011) 594 final (Brussels, 28 September 2011).

³⁹ House of Lords, Select Committee on European Union, Unrevised transcript of evidence taken on the Financial Transaction Tax, 16 February 2012.

in the overall European interest to have strong financial centres in London as well as in Paris and Frankfurt. In this context, we need the UK on board, actively engaged in the discussions on the design, fine-tuning and implementation of the financial transaction tax.”⁴⁰

In Cannes, on 3-4 November 2011, the EU proposal for a global financial transaction tax fell – if not on stony ground – far short of the result the French Presidency had hoped for. The meeting in Cannes was entirely dominated by the European sovereign debt crisis, notably in light of the Greek Prime Minister’s surprise announcement that a bail-out to his country would have to be approved by popular referendum. However, at his evening press conference on 4 November 2011, President Sarkozy stated that after Cannes “the financial transaction tax is still on the table, and that is an amazing achievement!”.⁴¹ However, the language of the G-20 Summit is as usual rather less enthusiastic:

“We agree that, over time, new sources of funding need to be found to address development needs. We discussed a set of options for innovative financing highlighted by Mr Bill Gates, such as Advance Market Commitments, Diaspora Bonds, taxation regime for bunker fuels, tobacco taxes, and a range of different financial taxes. Some of us have implemented or are prepared to explore some of these options. We acknowledge the initiatives in some of our countries to tax the financial sector for various purposes, including a financial transaction tax, inter alia to support development.”⁴²

Thus, little has changed since the Toronto summit of June 2010, and it is uncertain what the G-20 in Mexico will bring. In the following subsection I examine the EU proposal for a Directive implementing the FTT at regional EU level, and assess its potential as a stepping stone for global implementation. At this juncture, we may conclude that as regards the EU position on a global FTT, both horizontal (intra-institutional) and vertical (EU – Member State) dividing lines exist. Whereas the Tax Commissioner now defends the EU line, yet agreement by all 27 Member States is still lacking, it is clear that the latter schism is the most damaging to the single EU message in pursuit of the global financial transaction tax.

4. Essential Features of the EU Proposal for an FTT Directive

4.1 Objectives of the EU Proposal

When James Tobin proposed to levy a small percentage on all spot conversions of one currency into another, the objective was to ‘throw sand in the wheels of the excessively efficient international money markets’,⁴³ i.e. to deter short-term speculative currency transactions. The idea of deterring what are perceived as excessively risky activities by financial institutions is integral to the idea of the EU-wide financial transaction tax, and additionally the Union wishes “to complement regulatory measures aimed at avoiding future crises”.⁴⁴ However, there is deep disagreement on the economic merits of the FTT, essentially reflecting different economic schools’ ideologies on the desirability of regulatory intervention in markets. As a consequence, reaching consensus on the FTT proposal has been a vast hurdle towards implementing the tax at European - let alone global - level. In the previous subsection I have already indicated that this is but one of the many obstacles to global implementation of the FTT.

⁴⁰ House of Lords, Select Committee on European Union, Unrevised transcript of evidence taken on the Financial Transaction Tax, 16 February 2012, uncorrected evidence, 2.

⁴¹ The press conference was streamed live via a dedicated website, which is currently no longer available.

⁴² Cannes summit final declaration, ‘Building our common future: renewed collective action for the benefit of all’, 4 November 2011, para 82.

⁴³ J. Tobin, ‘A Proposal for International Monetary Reform’, 4 *Eastern Economic Journal*(1978), 153-159.

⁴⁴ European Commission, *Proposal for a Council Directive on a common system of financial transaction tax and amending Directive 2008/7/EC*, Brussels COM(2011) 594 final (Brussels, 28 September 2011), 12. (preamble para 1)

The Commission proposal makes clear proposals in this respect, and indicates the following chief objectives for implementing an EU wide FTT:⁴⁵

- i. The first objective is to ensure that financial institutions make a fair contribution to covering the costs of the recent crisis, and to ensure that financial services which are exempted from VAT are treated equally to other sectors. Related to this argument, though not mentioned as an objective for the EU-FTT per se, is that the EU foresees that the projected revenue of an EU-wide FTT (57 billion Euros) would gradually displace national contributions to the EU budget, thereby helping to relieve national budget deficits.
- ii. Second, market correction, namely to correct behaviour such as trend-chasing and short-termism out of step with the real economy, and complement on-going regulatory initiatives to ensure systemic, macro-economic stability. The FTT does this by limiting perceived excesses across the EU-27 Member States, and create appropriate disincentives for transactions that endanger the stability and efficiency of financial markets.

If the EU would manage to transform these objectives into a coherent message to the world, the proposed EU Directive on an FTT is an important stepping stone for global implementation in that it provides crucial regulatory inspiration for its global implementation. From the perspective of market correction notably, the EU directive makes important regulatory choices, underlining the maturity of the proposal and its complementarity to the G-20 Pittsburg Statement to reform global financial governance for the 21st century. In essence, the EU Directive sets up a harmonized system in order to limit financial transactions which are not desired for their rationale (speculative), large volume (compared to real economy) or high speed (high-speed algorithmic trading). What is rather unfortunate however, is that the Commission proposal does not make an explicit connection to innovative financing for development or climate change. Elsewhere I have argued that this is a political mistake on the part of the Union.⁴⁶ This because if it had done so, it could create political momentum through projecting itself as a “Global Robin Hood”, taxing the rich and giving back to the poor. By short-sightedly connecting potential revenue of the FTT Directive to the negotiations on the next multi-annual budget cycle, the Union has lost an important source of political legitimacy to its citizens, and grass roots movements across the world. Thus, it would be important to rectify that error in translating the EU proposal to a global message, and it would be crucial for the Union to emphasize the FTT as integral to global redistributive justice. In any case, in setting up a system of taxing financial transactions, there are three distinct concerns which need to be addressed at EU and at global level. First, a targeted FTT would have to be meticulously designed to reduce the risk of geographic relocation to non-tax jurisdictions. Second, it is necessary to ensure that the FTT does not hamper the real economy by limited access to capital. Third it is necessary to ensure that tax incidence does not befall individual citizens.

4.2 Core Legislative Choices in the EU Proposal

A commonly quoted statistic is that in 2007, the volume of financial transactions stood at a level 73,5 times higher than nominal world GDP, owing largely to the growth in derivatives trading.⁴⁷ In particular, trading on derivatives markets expanded significantly stronger than trading on spot markets: in 2008, the volume of derivatives trading was 66 times higher than world GDP, whereas spot trading amounted to only 8 times world GDP. The argument goes that this indicates the skewed relationship between needs of the real economy and the international financial markets. Intervention is then necessary because only a small share of transactions stem from ‘useful’ hedging activities and the

⁴⁵ *Ibid.*, 2.

⁴⁶ Van Vooren, EU as Robin Hood.

⁴⁷ S. Schulmeister, Short-term Asset Trading, long-term Price Swings and the Stabilizing Potential of a Transactions Tax, WIFO - Austrian Institute of Economic Research (October 2010), 19.

greatest part of transactions is purely speculative.⁴⁸ Of speculative trading, high speed algorithmic trading is considered particularly harmful since it is based on the trades of others thereby amplifying fluctuations away from equilibrium based on real economic indicators.⁴⁹ The nature of the EU's FTT is such that it would correct market behaviour through rendering speculative trades more costly, in particular high frequency technical trading which is automatized to chase trends in the short term. Through rendering such trades more expensive, the FTT would curb speculation and improve market efficiency, increase transparency, reduce excessive price volatility, and create incentives for longer-term investments with added-value for the real economy by freeing up resources for more productive uses.⁵⁰ Counterarguments to the FTT consider that it would limit parties' ability to hedge risk,⁵¹ thereby reducing liquidity and increasing short-term volatility of asset prices. The EU Directive clearly chooses to follow the Keynesian line of reasoning in this debate. This is distinctly illustrated by the taxable amount of the FTT on derivatives. Namely, the EU proposal takes the notional amount at the time the derivative agreement is purchased/sold, transferred, concluded or modified.⁵² This implies that derivatives are taxed on the basis of the value of the underlying principal, which implies a potentially large amount of tax to be paid compared to the actual amounts changing hands between parties to the derivative contract. Even though the proposal sets the tax rate at 0.01% instead of the 0.1% for other transactions, this is clearly intended to render short term, speculative trades in financial derivatives much more costly.

Further illustrative of the fact that the focus of the Directive is on trading which is not useful for the real economy but speculative, are the following three mitigating elements:

- First, the tax is set at a low rate to minimise impact on the cost of capital for non-financial investment purposes.
- Second, there is the exclusion from the scope of the FTT of transactions on primary markets both for securities (shares, bonds) – so as not to undermine the raising of capital by governments and companies – and for currencies.
- Third, the exclusion of financial transactions for example with the European Central Bank (ECB) and with national central banks, from the scope of the FTT, so that the directive will not affect the refinancing possibilities of financial institutions or the instruments of monetary policy.

Further, with its market correction objective in mind, the EU Directive aims to install an FTT which is broadly defined in scope as regards products, transactions, types of trade and financial actors, as well as transactions carried out inside a financial group. For example, the definition of *financial institutions* includes investment firms, organised markets, credit institutions, insurance and reinsurance undertakings, collective investment undertakings and their managers, pension funds and their managers, holding companies, financial leasing companies, special purpose entities, and foresees in delegated powers to the Commission so that it may set targets for 'significant' activities of other entities whereby it would also be classed as a financial institution. As regards *financial transactions* the proposal includes spot transactions (shares, bonds, currencies) and derivatives transactions (forwards, futures, options, swaps, currency derivatives, commodity derivatives...),⁵³ and this both on organized markets and 'over-the-counter' (OTC) transactions between financial institutions. This aspect illustrates the choice for a sweepingly broad financial transaction tax, but also raises an important question for global implementation. Namely, it is clear that the EU legal order is well-suited

⁴⁸ *Ibid.*, 20.

⁴⁹ *Ibid.*

⁵⁰ D. Baker, 'The Benefits of a Financial Transactions Tax', *Centre for Economic and Policy Research* (December 2008), 3.

⁵¹ K. Alexander, 'International Financial Regulatory Reform and Financial Taxes', *13Journal of International Economic Law* (2010), 900. (Himself a proponent of the FTT, but quoting a number of counter-arguments).

⁵² See note 44, p 9.

⁵³ Impact assessment accompanying proposed Directive, see note 25, volume I, 39.

for the kind of EU-wide harmonized approach necessary to implement this tax. Indeed, Member States are obliged to implement this Directive by 2014 if it enters into force as planned, and Member States are only given discretion to impose a higher tax rate than required by the Directive, if they so desire. This has important implications at global level. It is indeed questionable whether the 'nature of governance' in the global financial system as it stands can accommodate the level of legal cooperation needed to install this tax? It is beyond the scope of this contribution to assess the legal changes needed to the global financial legal order. However, in different contributions I have argued that this would require nothing less than a revolution in global financial governance.⁵⁴

Having pointed to the fact that the EU Directive clearly has the market-intervention objective of limiting transactions that are not considered useful, we must now point to another, and very contentious issue surrounding the FTT. Namely, that of relocation. Relocation covers two distinct phenomena, namely that financial transactions would disappear altogether, or they would be avoided through engineering or geographic relocation outside of the taxing jurisdiction. Now more than ever, financial markets operate at global level. Implementing the financial transaction tax in a regionally or nationally fragmented way exponentially increases the risk of financial engineering to avoid the tax; with financial institutions fleeing the area where it has been implemented. Furthermore, there would be the incentive to avoid taxes through integration (conducting transactions within businesses rather than between them), resulting into larger financial institutions. In the proposed EU Directive, the FTT will be levied on the basis of the *residence principle*. This implies taxation in a Member State on the basis of establishment of financial actors, independent from the location of the transaction. This aspect is meant to increase geographic distribution across its territorial field of application, i.e. to avoid that the burden of the tax is concentrated solely in the financial centres. However, it does illustrate that the tax can only truly be effective if participation is as inclusive as possible. Indeed, if the FTT would be implemented only in the Eurozone, might we not see simply see massive relocation from Euro countries to The City, UK? Furthermore, if the FTT would be implemented at EU level, how does this impact EU financial markets? The simulations of the EU's impact assessment implementing the tax in the EU-27 considers "a relocation of securities markets by 10%, a relocation of spot currencies by 40% and a relocation of derivatives instruments of 70% or 90%."⁵⁵ Relocation here implies the move of activities outside of the taxing jurisdiction, as well as their disappearance altogether. However, this is partially to be expected and even desirable, since it is one of the core objectives of the EU FTT: to the extent that algorithmic trading is considered harmful, such trading is currently about 40% of all transactions. It is these which would be rendered economically unviable, and which would be impacted the most.

A final point is that of *tax incidence*, where an important critique is that it is uncertain where the burden of the tax would fall. According to the IMF, the real burden may fall largely on final consumers rather than earnings in the financial sector in the form of reduced returns to saving, higher costs of borrowing, and/or increases in final commodity prices.⁵⁶ Commissioner Segeta ceded that point when asked about it on the day the EU Directive was launched, but argued that it is not problematic.⁵⁷ On the one hand, he argued that the Directive defines taxpayer such that financial institutions will be liable, even if the private person is involved. Hence, whether the financial institutions pay, or pass it on to the consumer, depends on the competitive environment. Taking into account that there are more than 8800 banks in the EU, the argument goes that competition is sufficiently strong so that the possibility to pass this tax on to individual consumers is rather limited.

⁵⁴ See Van Vooren, EU as Robin Hood, *o.c.* and Bart Van Vooren, 'Global Implementation of the Financial Transaction Tax: Utopia or Opportunity to Reform the International Financial Legal Order', in D. Kochenov & F. Amtenbrink, CUP, forthcoming 2013.

⁵⁵ Impact assessment, volume 1, see note 25, 49.

⁵⁶ See note 18, 21.

⁵⁷ Q&A with the press at Algirdas Semeta Press Conference on the FTT, 28 September 2011, transcript on file with author.

On the other hand, he argued that what taxes would befall individual citizens, would only be relevant for high income households. According to the Commissioner, citizens at a lower level of income, or middle income, do not engage in speculation in financial instruments. Hence there is a progressivity to the tax incidence, mainly linked with those who have a higher level of income. A similar argument has been made at global level. An expert report commissioned by the Leading Group argued that there would be a trickle-down effect whereby proportional to their involvement, economic market participants who benefit from globalisation would pay a small contribution equal to their involvement.⁵⁸ To avoid individual citizens being negatively affected as much as possible, the EU proposal excludes from its scope the lending and borrowing activities of private households, enterprises or financial institutions, and other day-to-day financial activities, such as insurance contracts, mortgage lending, payment transactions or credit card payments. What would be included in the scope of the tax is then the subsequent trading of these via structured products (derivatives), but those are not activities engaged in by ordinary citizens. Similarly, spot currency transactions are excluded to preserve the free movement of capital,⁵⁹ but derivatives based on currency transactions are included.⁶⁰

These being essential characteristics of the EU's proposal, in the following penultimate section I examine the FTT Directive as a stepping stone for global implementation, and the potential for the Union to shape global financial governance through this initiative.

5. The EU FTT Directive as a Stepping stone: Creating Alliances at the G-20.

As mentioned, the June 2010 Toronto G-20 Summit Declaration only cursorily mentioned financial taxation, and the level of "consensus" reached by the Leaders was limited to say the least. However, within the limited paragraphs on financial taxation, there is room to accommodate the stated objectives of innovative financing and market correction.⁶¹ The relevant paragraphs stated the following:

'21. We agreed the financial sector should make a fair and substantial contribution towards paying for any burdens associated with government interventions, where they occur, to repair the financial system or fund resolution.

22. To that end, we recognized that there is a range of policy approaches. Some countries are pursuing a financial levy. Other countries are pursuing different approaches. We agreed the range of approaches would follow these principles:

- Protect taxpayers;
- Reduce risks from the financial system;
- Protect the flow of credit in good times and bad times;
- Take into account individual countries' circumstances and options; and,
- Help promote a level playing field.

23. We thanked the IMF for its work in this area.'⁶²

The above quotation of the Toronto Summit Declaration does not make a connection between a financial levy and dispensing the revenue towards the innovative financing for climate change or in support of the Millennium Development Goals. The only statement on the distribution of the revenue

⁵⁸ Leading Group, 'Globalizing Solidarity: The Case for Financial Levies', *Report of the Committee of Experts to the Taskforce on International Financial Transactions and Development* (June 2010), 6, available at: <www.leadinggroup.org>.

⁵⁹ The Commission has gone this route not to violate Article 63 of the TFEU

⁶⁰ See note 44, 8.

⁶¹ Toronto Summit Declaration, 5.

⁶² *Ibid*, 18.

is the ‘protection of taxpayers’, language which is deliberately open-ended on connecting taxation to refunding taxpayers for the bail-outs in a number of advanced economies. We have seen that the EU FTT Directive states that it is meant to serve as (i) a new source of revenue to meet post-crisis budgetary needs, (ii) to recover costs from the ‘bailouts’ of financial institutions, and (iii) to cover the costs of potential future financial crisis.⁶³ That being the EU’s objectives, they are in rather strong contrast with the objectives for which civil society has advocated the financial transaction tax.⁶⁴ Often using the currency-specific Tobin Tax as the most popular example, the argument has traditionally been that proceeds should be earmarked for the funding of global public goods. This includes development and support for the MDG’s, initiatives focusing specifically on health care, or the environment and combating climate change. Asked about any such earmarking at a press conference, Commissioner Segeta made clear that there was no such earmarking written into the EU proposal.⁶⁵ He pointed to the fact that the EU together with its Member States is the biggest donor in the world. The FTT will contribute to Member State and EU budgets at a ratio to be decided in the multi-annual financial framework, but at any rate will contribute to public coffers. Thus, according to the Commissioner, through alleviating pressures on public coffers, the FTT will contribute to financing for development and climate change.

I submit that especially the argument of replenishing public coffers post-crisis bailouts will not provide sufficient traction towards installing the FTT at global level. Furthermore, the merely indirect contribution to global public goods will not suffice to garner global support. Indeed, and this is a purely political-strategic decision, if the EU wishes to have an FTT installed at global level it must emphasize the ‘fair contribution’ perspective. This is so because G20 significant countries such as China, India, Australia and Canada did not engage in bailouts as many European countries and the USA have done. This argument would therefore have less traction. Hence, in mustering political support for a global FTT, and in designing the distribution of FTT proceeds, it is best to focus on earmarking revenue for the provision of global public goods.

Aside from the final recipients of the ‘fair contribution’ to be made by financial institutions, the language in the Toronto Summit Declaration is deliberately vague on the national, regional or global level at which to pursue a financial levy. The reference to government interventions ‘*where they occur*’ came at the request of countries such as India, Canada, Japan and China which did not bail-out their financial sectors. These do not feel as compelled as Western nations to have the financial sector compensate them for their interventions. The quotation of the 2011 Cannes Summit Declaration earlier in this contribution replicates that schism between different nations at G-20 level: “Some of us have implemented or are prepared to explore some of these options. We acknowledge the initiatives in some of our countries to tax the financial sector for various purposes, including a financial transaction tax, inter alia to support development.”⁶⁶ Notably Canada has been a vocal opponent, with its Finance Minister stating that “We will continue leading that charge against a transactions tax and I am confident that our allies on this point, who are the emerging economies, will stay with us and join us in opposing what we view as a counterproductive tax. ... I am actually confident that we have enough of them in the G20 that we will be successful on that initiative”⁶⁷ Canadian opposition explains why the Toronto Summit Declaration was so light on the topic of an FTT, and also shows the importance of the EU Directive and French presidency building momentum towards the Cannes summit. The fact that this summit has been overshadowed by the European sovereign debt crisis then decimated any such

⁶³ See note 25, Volume I, 25-26.

⁶⁴ Such initiatives include robinhoodtax.org or financialtransactiontax.eu; underwritten by diverse grassroots social movements.

⁶⁵ Algirdas Semeta Press Conference, 28 September 2011, transcript on file with author.

⁶⁶ Cannes summit final declaration, ‘Building our common future: renewed collective action for the benefit of all’, 4 November 2011, para 82.

⁶⁷ Quoted in John Greenwood, “Clark Sings Praises of Basel Rules on Capital,” *Financial Post*, October 5, 2011

momentum, as it was rather clear that the European Union had – to put it colloquially – ‘bigger fish to fry’. In any case, the distinction between some countries pursuing the financial levy and other countries having different approaches makes clear that while a global FTT is not excluded, enthusiasm is certainly highly limited and common agreement is lacking. The key for the EU proposal to succeed is then not to merely emphasize its innovative financing aspect, but to argue that it is compatible with the BRIC nations’ regulatory vision. Prior to the 2008 crisis, Western nations’ approaches were broadly deregulatory, whereas for Indian, China or Japan the opposite was true. Since the latter countries have been less averse to regulating their financial sectors,⁶⁸ they view this as one of the key reasons for not having had to bail out their financial institutions. India could be one important BRIC nation the EU might sway to the pro-FTT camp. While currently sceptical, arguing that it might hurt its domestic banks, it has in the early 2000’s already argued in favour of the financial transaction tax at global level. Therefore, if the EU wishes to realize the FTT, it must emphasize the systemic market corrective function of international financial taxation, and push an FTT complementary with emerging powers’ vision on regulating finance. In this sense, the EU is to actively engage the changed power structure of global economic governance as part of the process of installing the FTT.

6. Conclusion

The objective if this contribution was to examine the global potential for the EU’s FTT proposal in a multi-polar world, in line with its binding, law-oriented mission statement of Article 21 TEU. What is certain is that the European Union in primary law has a strongly worded obligation to pursue multilateralism based on the rule of law. In light of this, it has been argued that the global financial transaction tax carries with it great potential for ‘legitimizing’ the European Union as a global actor through effective implementation of its FTT proposals – the EU as a global Robin Hood. However, this contribution has pointed to numerous internal and external obstacles to any such role for the EU on the global playing field. The first obstacle to EU global success lies within itself: strongly divided opinions between the Member States, and within the EU institutions themselves, on the merits of the global or regional financial transaction tax. Within the EU institutions, we have seen that Commissioners Barroso and Semeta did not agree on its merits, but that the latter realigned himself in light of political pressure from the highest echelons. Thus, from the Commission perspective we have seen a ‘single voice’ emerge. However, the same is not true for agreement between the Member States themselves. At the time of writing, Spring 2012, discussions within the Council are on-going on the EU-wide implementation of the FTT. Indicators for agreement among the EU-27 were not good. Early February 2012, a splinter group of EU countries led by France and Germany – joined by Austria, Belgium, Finland, Greece, Spain, Portugal and Italy – asked the Danish Presidency to fast-track plans for the FTT, possibly even through enhanced cooperation.⁶⁹ Thus, potential for an EU single voice delivering a single message on the global stage is minimal at best.

Assuming then that the European Union does manage to pull together, obstacles globally are equally, if not more, insurmountable. I have pointed to the fact that such would require a revolution in the way global finance is governed, and the Toronto and Cannes summits have shown that at present, the global FTT is a stillborn idea. Should the Union wish to trod onwards with a global financial transaction tax, the Union can only partially transpose its objectives to the global level. First, while the EU should certainly emphasize the market corrective and regulatory function as set out in the proposed EU Directive; it should pursue this tax towards raising extra funds for global public goods where funds are currently lacking due to significant public deficits. Indeed, (EU Member) States should not view this as an opportunity to replenish public coffers of those nations which have bailed out financial institutions. Clearly, widely different responses across the globe – especially in Asia –

⁶⁸ Special Section on International Banking, *The Economist*, 15 May 2011.

⁶⁹ EU Observer, Nine EU countries form splinter group on financial tax, 8 February 2012

would hinder consensus and render the FTT even more unlikely at G-20 level. Second, the market corrective function should be framed such to assure G-20 members geographical relocation will not pose grave risks to the major financial centres and the economies of the countries that host them. As a consequence, this section concludes that the *global option* in function of *market stabilization* and the provision of *global public goods* is the only feasible avenue towards implementing a global financial transaction tax. This, then, sets the stage for the legal and institutional features of a multilateral financial transaction tax convention. The features of such a multilateral convention, are discussed in a forthcoming contribution by the same author.⁷⁰

⁷⁰ Bart Van Vooren, 'Global Implementation of the Financial Transaction Tax: Utopia or Opportunity to Reform the International Financial Legal Order', in D. Kochenov & F. Amtenbrink, CUP, forthcoming 2013.

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