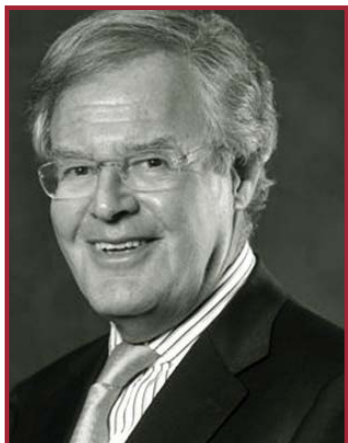


Sharing the burden



Europe's planned tax on financial transactions needs to be better thought through. If not, it could trigger a major loss of transaction volume, says **John Gubert**.

Unless the tax is levied globally, it will not work. The results of a regional adoption of the tax would be catastrophic for governments, corporate issuers, investors and employability, whilst the quantum of global systemic risk would hardly change.

Few would argue that the banking sector needs to pay for the implicit or explicit guarantees it obtains from national governments. The "Tobin tax" is one of those brilliant solutions, which will have serious unintended consequences if introduced in line with the mooted European Financial Transaction Tax.

First of all, the mathematics are flawed. The European Commission believes that a tax of 10 basis points on share and bond trading plus one basis point on derivative transactions will raise approximately EUR 57 billion per annum. But taking the two major European ICSDs (Clearstream and Euroclear) alone and levying such a charge on their transaction flows creates a figure of several hundred billion euros.

So either the estimates are wrong or the Commission expect the pill to be so unpalatable that around 75% plus of all current European transaction volume will evaporate or, more likely, move to alternative centres. London, Brussels, Luxembourg and Dublin would see their financial services industries decimated in the process. Paradoxically, the Commission has been promoting Target2-Securities, which shaves perhaps half a euro off a transaction cost; again using the ICSDs as a surrogate, the added cost of a "Tobin tax" would be more than EUR 2,000 per transaction.

In reality, unless the tax is levied globally, it will not work. The results of a regional adoption of the tax would be catastrophic for governments, corporate issuers, investors and employability, whilst the quantum of global systemic risk would hardly change. And, as Europe is not an island, a shift of risk may help marginally, but it will not alter the macro environment. Firstly, the tax would make European issues that

much more expensive; there would be an immediate yield advantage of up to 10 basis points for non-European issuers over their European counterparts. Secondly, European-based investment funds would be disadvantaged. There would be no rationale for a fund to be based in Europe unless it was targeted at solely European investors. Thirdly, many organisations would look for loopholes with fund-of-fund-style structures being a logical suggestion where trading activity is downstream and offshore, with the only onshore transaction being in the master fund through the purchase and sale by the investor.

Europe would be seen as a protectionist environment, and it has made a half-hearted step in this direction already with some of the Alternative Investment Fund Manager Directive's clauses on the domicile of fund managers. The complexity of identifying if an investor is liable for the tax would deter non-Europeans from using EC-based infrastructures wherever possible. An unintended consequence of the plan could be the migration of the bulk of the international securities market to more hospitable climes. The bankers of Singapore must be praying for the tax to be adopted to give their post-trade infrastructure an unimaginable boost.

There is momentum behind the initiative. Some countries feel that the only real barrier is the City of London. That, though, is one of the problems. Securities governance may be pan-European in structure, but the bulk of global business flows are in London. Unless the EU proves this is not a financial matter, the UK government will surely oppose it and the required unanimity of all EU member states will prevent its adoption. //

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