NOTE
from: General Secretariat

to: Coreper/Council


2. The Presidency's assessment of these discussions is contained in a Presidency progress report (Annex). The Presidency intends to submit the progress report to the Council (ECOFIN) meeting of 22 June 2012 as its contribution to an orientation debate among Ministers.
3. At the Council (ECOFIN) the Presidency intends to invite the Council (ECOFIN) to discuss the strands of work below and to give orientations on how to proceed, separately or in parallel, concerning the possible taxation of the financial sector in the EU:

1) continuation of the work on the introduction of a financial transactions tax based on the Commission proposal focused on a step-by-step approach starting with a narrow based transactions tax (e.g. similar to a stamp duty);

2) more in depth examination of alternative ways of regulating or taxing the financial sector in a harmonised or coordinated way, i.e. bank levies, FAT or other.
PRESIDENCY PROGRESS REPORT

Introduction and progress of work

1. The Proposal for a Council Directive on a Common System of Financial Transaction Tax (FTT) and amending Directive 2008/7/EC was presented by the Commission on 28 September 2011. The Proposal has been discussed by The Working Party on Tax Questions - Indirect Taxation (FTT) at seven meetings. The first meeting was held during the Polish Presidency in December 2011. The last meeting during the Danish Presidency took place on 1 June 2012.

2. The state of play on this file has also been discussed at the Council (ECOFIN) on 13 March 2012, with subsequent discussions at the informal ECOFIN on 30 March 2012. These discussions revealed that while continuing further technical examination of the Commission proposal it is necessary to look also at the possibilities of alternative solutions.

3. The Working Party completed the first technical examination of the Proposal on 6 March 2012. On the three subsequent meetings the Working Party has followed the two track approach outlined by ECOFIN by examining in parallel:

   1) FTT (including elements of stamp duty), and

   2) Alternative ways of taxing and regulating the financial sector as well as the current level of taxation of the financial sector.

4. For this process, the Presidency has composed Room Documents outlining a non-exhaustive list of topics of discussion for the further technical examination by the Working Party. The documents are based on the outcome of the previous meetings and attempt to pursue compromises within the framework of the Proposal. The possibilities for a step by step approach have been discussed. Elements of a stamp duty were also included in the issues of discussion in order to comply with the two track approach from ECOFIN.
5. The Commission services have provided seven additional Technical fiches with further explanation of certain elements of the proposal, including *inter alia* a paper regarding different methods of taxing financial activity covering labour taxation, bank levy, direct regulation, corporate tax and activity taxes, a paper on revenue estimation, macroeconomic impacts, etc.

**Objectives to be reached through taxation of the financial sector**

6. During the discussions a number of the potential aims of financial sector taxation have been touched upon.

7. The proposal has been tabled by the Commission to harmonize Member State taxes on financial transactions by creating a common system of financial transaction tax.

8. The Commission emphasizes the importance of securing that the financial institutions make a fair contribution to cover the cost of the pending global financial crisis and ensuring that the financial sector is taxed on comparable terms with other sectors. The Presidency's assessment of the discussions is that this objective is generally shared by Member States.

9. Furthermore, the Commission argues that there is a need to create appropriate disincentives for transactions that do not enhance the efficiency of financial markets. Thus, according to the Commission proposal a financial transaction tax might complement regulatory measures aimed at avoiding future crises. The Presidency's assessment of the discussions is that Member States are divided on this objective, with some delegations strongly disagreeing with the view of the Commission and others supporting it.

10. Finally, the proposal aims at creating a new source of own resources of the EU budget with a view to replace the national contributions. This element is discussed in the context of the Multiannual Financial Framework.
11. Member States have also made reference to the European Council conclusions of 1 and 2 May 2012, which state that “The European Union is taking all necessary measures to put Europe back on the path to growth and jobs. This requires a two-pronged approach, covering both measures to ensure financial stability and fiscal consolidation and action to foster growth, competitiveness and employment”. The Presidency's assessment of the discussions is that some Member States see the proposal as compatible with this strategy while others fear that the effects will be detrimental to growth, jobs, competitiveness and financial stability.

**Budgetary and economic impact**

12. The Commission's Impact Assessment accompanying the proposal analyzed the economic impacts of the proposed financial transaction tax and other approaches (e.g. the Financial Activity Tax). As additional information, the Commission provided technical fiches (cf. par. 5 above).

13. The Commission estimates that the total revenue from the proposed financial transaction tax for EU as a whole will amount to approximately 57 bn. € annually. However, the exact size of this estimate depends on market reactions and the risk of tax avoidance and tax fraud. About one third of this revenue is expected to be generated by taxing trading, borrowing and lending in securities (bonds and shares), and two thirds are expected to come from taxing derivatives.

14. The Impact Assessment accompanying the proposal has estimated that impact of the FTT on the GDP of the EU would be - 1.76 % in the long run and - 0.53 % after taking into account the mitigating effects. Subsequent supplementary analysis by the Commission concluded that the possible long term effect on GDP will be around - 0.28 %. The Commission also indicated that this negative effect could be further reduced if the revenue was to be used to promote growth.

15. Some Member States disagree with the Commission's estimates as regards impacts on GDP as well as the underlying assumptions and the distribution of tax revenue. Further analysis with respect to the budgetary and economic impact of the proposal may be useful.
The tax base

16. During the technical examination of the proposal the Working Party has discussed elements of the tax base such as derivatives, government bonds, repurchase agreements (RePos), undertakings for collective investment in transferable securities (UCITS) and pension funds. The discussion has been based on a stepwise approach in order to contribute to compromises and has included various proposals on the way as regards various elements of the tax base: no amendments to the text of the proposal, gradual implementation of provisions by delaying the entry-into-force or introduction at a lower tax rate, rewriting of provisions and exemption of certain elements from the tax base, etc.

17. The topic of pension funds turned out to be a particularly complicated area due to the fact that this issue must be seen in close context with the taxation of UCITS and banks in general because pension schemes differ among Member States. With regard to UCITS there is also an issue relating to the fact that the proposal on FTT suggests exempting first time issuance of financial instruments whereas this is not the case concerning primary transactions in UCITS. This might be seen by some as distortion between investing through UCITS and, e.g., limited liability companies.

18. No actual compromises have been reached during the debate on the tax base so far but the Presidency has noted a strong tendency, if a proposal on FTT is to be adopted, to exempt RePos and government bonds or to phase in taxation of these instruments over a longer period of time. As regards taxation of derivatives, a possible route seems to be their inclusion into the tax base at a later point in time. On the issue of high frequency trading and speculative trading in derivatives and other financial instruments the discussion revealed doubts that taxation is the most efficient way to regulate harmful financial transactions. Direct regulation could be an alternative solution which would however not in itself generate any revenue for government budgets.
Relocation and tax planning

19. In the proposal there are a number of tax avoidance and evasion provisions in order to deal with this particularly mobile tax base.

20. One of the essential discussions relating to this matter is whether the tax should be levied on the basis of where the person undertaking the financial transaction is established (residence) as proposed by the Commission or on the origin of the financial instrument (issuance) or a combination of both principles. The current proposal is based on the residence principle. One of the reasons is that numerous products, namely derivatives, often come without a place of issuance. During the debate in the Working Party there seemed to be a general interest among those Member States who support the proposal in maintaining the residence principle while using the alternative issuance principle on some financial instruments in order to avoid tax evasion.

Tax rates and taxable value

21. According to the Proposal there will be different tax rates on derivatives and other financial instruments respectively. Thus, the rate on derivatives is 0.01 % (of the notional value) whereas the rate on other financial instruments is 0.1 %. The question is whether it is necessary to differentiate tax rates even further on various financial instruments in order to reach similar effective tax rates. Conversely, concerns have also been raised that differential rates on financial instruments may affect market behaviour. Another object of concern has been that the effective tax rate on risk hedging using the notional amount will become disproportionately high. These questions are of highly technical character and may require additional technical examination.
Alternative ways of taxing and regulating the financial sector

22. At the meeting on 1 June 2012 the Working Party on Tax Questions – Indirect Taxation (FTT) looked at alternative ways of taxing and regulating the financial sector and their pros and cons. Though a number of Member States saw discussions on a step-by-step introduction of the FTT (as discussed in previous meetings) as the most promising way forward, some Member States were opposed to such an approach and indicated their preference to focus further discussions on alternatives (bank levy, FAT; action through direct regulation of the financial sector, coordination between Member States, action only at the level of individual Member States). Others saw discussion on alternatives as complementary to the discussions on FTT, while some did not see good prospects for reaching a decision on any of the alternatives to an FTT. It was noted that direct regulation of the financial sector falls into the remit of other Working Parties of the Council.

Possible way forward

23. The Presidency has looked at the various aspects and elements of the financial sector taxation, with a view to identifying what could be achieved at an early stage.

24. Some Member States are of the opinion that, if the first track – the introduction of a tax on financial transactions – were to be explored further with the aim of an introduction of the tax in a not too distant future, further work should focus on a step-by-step approach. This could mean starting with a narrow based transactions tax mainly applying the tax to secondary market transactions with shares, bonds (but not government bonds) and possibly UCITS, with a possibility to extend the tax to other financial instruments (including e.g. derivatives) at a later stage. The discussions in the Working Party also show that a number of Member States are against harmonisation of financial sector taxation at EU-27 level. Some would prefer the second track (consisting of identifying other ways of regulating or taxing the financial sector and the extent to which these require action at EU-27 level, consistent with the principle of subsidiarity).