EUROPEAN ASSOCIATION OF CO-OPERATIVE BANKS

European Association of Public Banks
- European Association of Public Banks and Funding Agencies -

European Banking Federation

ESBG
EUROPEAN SAVINGS AND RETAIL BANKING GROUP

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Brussels, 23 January 2015

Dear Minister XXX,

On behalf of the undersigned associations, the European Association of Cooperative Banks (EACB), the European Association of Public Banks (EAPB), the European Banking Federation (EBF) and the European Savings and Retail Banking Group (ESBG), we are writing to you and your counterparts in the other 10 participating Member States to express our combined concerns that participating Member States are persevering in putting forward a Financial Transaction Tax (FTT) under the enhanced cooperation procedure.

Numerous governments, central banks, independent research analysts and tax experts have expressed the view that the proposed FTT would harm the internal market for financial services and distort competition among operators, merely on the basis of their location in (or connection to) a particular group of Member States.

Introducing an FTT based on a limited territorial scope will put an extremely high pressure on the participating Member States' financial services operators and will significantly increase their governments' dependence on financial markets outside the FTT zone and outside Europe.

Due to its extra-territorial effects, the proposed FTT will impact the entire European economy, inappropriately increasing the costs of funding for all businesses at a time when Europe desperately seeks to restore growth. Failing a comprehensive impact assessment taking into account all the potentially far-reaching implications of the proposed FTT, the governments of the 11 participating Member States are dangerously underestimating its significant economic impact which will seriously damage financial stability in Europe and in the Eurozone.

The scope of the proposed FTT is far-reaching. It will apply to a broad population of financial institutions, encompassing banks, asset managers, insurers, collective investment vehicles, pension funds and regulated markets with no exemptions available for the different types of activity carried on. Its application to a very wide range of products and transactions is likely to reduce the volumes transacted in the countries concerned, and thus impact the liquidity of secondary markets, which include both regulated trading venues and over-the-counter (OTC) activities. With such a broad-based approach, the proposed FTT will negatively impact financial activities that are essential to the functioning of financial markets and our economy as a whole - most notably:

- The issuance and secondary market purchase of sovereign bonds, used by governments to finance their budgets;
- European markets' dynamism, by taxing market making activities, which are key in the provision of liquidity to markets;
- The short term markets, including market making activities, which will be disproportionately hit by the tax because of its flat rate structure, irrespective of maturity;

- The conclusion of derivatives contracts, which are used by financial institutions and companies to hedge their risk exposures;
- Repurchase agreements which, as key instruments in bank lending activities, ensure an efficient movement of collaterals, providing liquidity to markets and facilitating the conduct of monetary policy;
- Corporate access to finance, as the FTT will severely damage issuers' access to capital and investors' access to quality investment opportunities by increasing the cost of secondary market trading in participating Member States; and
- Intra-group transactions, which are vital for a proper liquidity and capital allocation within a group.

The cascading effect makes the effective tax rate of the FTT on securities much higher than the headline rate of 10 bp – in some cases this may be as much as ten times higher – because of the chain of trading and clearing that lies behind most securities transactions. Indeed, a purchase of securities on a trading venue or OTC usually involves a sale and purchase by a number of parties, including market makers, brokers, clearing members and the central counterparty to the clearing system. Each transaction could be subject to the FTT, with only the central counterparty being exempt. In a similar way cascading effects may arise where transactions are carried out within a group or within decentralised sectors or within highly intermediated distribution markets, such as the single European market for UCITS funds. For example, the FTT will also apply when financial instruments are merely transferred between separate entities of a group or a decentralised sector. Equally the FTT will apply to entities distributing financial products to consumers in the Single Market. The negative consequences of the tax will be proportionate to its huge effective magnitude and will dis-incentivise on-exchange trading and clearing, contrary to regulatory reforms implementing the G20 objectives whilst the real economy will mostly have to bear the additional costs arising from the FTT.

The proposed FTT will also impact the relationships with non-EU trading partners. Financial institutions around the world will indeed continue to seek to execute transactions at the lowest possible cost in serving their customers. Given the extraterritorial reach of the proposed FTT outside its participating Member States, the imposition of a FTT will deter persons outside FTT jurisdictions from doing business with such financial institutions within the FTT jurisdictions. If the FTT is adopted as proposed, financial institutions the world over can be expected to reduce their exposure to financial institutions within FTT jurisdictions and to securities within the scope of the FTT, with a commensurate decline in business executed with such institutions and in such securities. We expect the FTT will result in a significant decrease in market volumes, notably from market-makers, and a massive reduction of derivatives volumes. Given its role in supporting economic activity, it would be imperative not to harm the important function of market making activities. In jurisdictions where business is still executed, capital markets will likely require rate or price adjustments for transactions subject to the FTT. The end result would likely be a reduction in the profitability, size and strength of financial institutions within the FTT jurisdictions and hence in their ability to channel funding between investors and issuers in the real economy.

Furthermore, there is an inherent contradiction in the proposed method to tax financial transactions across the EU, which is not uniform and consistent and will create a fragmentation between FTT jurisdictions and non-FTT jurisdictions. This will jeopardise the transmission of monetary policy and is not consistent with the EU's goal of a single market and the regulatory objectives (for example in the desirability of collateral usage) which have been reinforced to ensure financial stability in the EU.

The proposed FTT would not only lower overall tax revenues, but also unfairly marginalise financial institutions in the FTT jurisdictions, with a consequent detrimental effect on the non-financial economy within these jurisdictions. The tax will hamper the ability of companies, borrowers and investors to access finance from capital markets. In the end, we firmly believe that the costs of reduced economic activity in the FTT jurisdictions may far outweigh the perceived benefits of the tax revenues that will be collected under the FTT regime.

Furthermore, the recent research realized for the European Commission shows that the collection of the tax remains a major challenge, raising the issue of the collection cost. Indeed, smaller domestic financial institutions with limited exposure to cross-border activities will face operational challenges that are not proportionate.

We, the undersigned associations respectfully urge the Ministers of the 11 participating Member States to take note of the overwhelming evidence against the merits of FTT and drop the project to safeguard the European economic growth and employment.

Boosting economic activity and increasing labor market participation are the best ways for Member States to improve on the long term the tax collection levels and budgets. The undersigned associations will continue to strongly support this path.

Yours sincerely,

| EACB | EAPB | EBF | ESBG |
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