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Reviving the Call for a Global Financial Transaction Tax (FTT)

The Forthcoming Brisbane G20 Summit

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The G20 Leaders' Summit will take place on 15 and 16 November in Brisbane, Australia. The Summit is expected to discuss a wide range of global policy issues and challenges from corruption to taxation to employment to financial regulation to growth strategies. It is expected that the Brisbane Action Plan, which would be discussed at the Summit, will outline an action plan which would be implemented by member-countries in the coming months.

Given the lackluster approach of member-countries towards implementing action plans adopted at previous summits, it remains to be seen how much of Brisbane agenda will be accomplished by them (individually and collectively) before the G20 Leaders meet for the next Summit in Turkey in 2015.

The Brisbane Summit offers an opportunity to civil society groups to renew the demand for a financial transaction tax (FTT). Not long ago, this issue was put on the table at Cannes Summit (2011) due to persistent campaigning by a range of international civil society groups. The Interim Report of the G-20 on Fair and Substantial Contribution by the Financial Sector (2010) had proposed a flat rate levy on all financial institutions and "financial activities tax" on profits and remuneration in order to pay for future financial clean-ups and reduce systemic risk. But the proposal got diluted at the G-20 meeting held at Busan (Korea) in June 2010, which called for implementation of the levy taking into account individual country's circumstances and options.

Despite the strong resistance by many G20 member-countries against a FTT, civil society groups should not retreat from this key demand. Rather renewed efforts and mass campaigns should be launched in each member-country of G20 to influence political leaders to accept this demand.

Transaction Taxes Are Not New

Contrary to the popular perception, financial transaction taxes are not new. Many G20 countries had experimented with a wide range of transaction taxes in the past and some countries continue to levy such taxes today.

India, for instance, introduced a Securities Transaction Tax (STT) on the trading in the equity markets some 10 years ago with the twin objectives of raising additional tax revenue and maintaining market integrity. The STT has undergone modifications in tune with the market developments over the years but it is still being levied on listed securities on stock exchanges and in units of mutual funds. In 2013, India also introduced a Commodity

Transaction Tax (CTT) of 0.01 percent on commodity futures contracts (e.g., gold, copper and oil) traded in the Indian markets.

The Policy Objectives

As I have argued elsewhere, the policy objectives for a FTT are essentially two-fold: to raise revenue; and to restore stability and integrity in the financial markets. According to estimates made by Bill Gates (founder of Microsoft) in a report to the G20 on new sources of finance for development, a tax on financial transactions could generate about $50 billion from G20 member-countries. Some other estimates claim that a global financial transaction tax could generate as much as $250 billion if a wide range of transactions are included. The resources raised through FTT could be better utilized to support programs to fight hunger and poverty, and pay for climate mitigation and adaptation costs.

The Rationale

Apart from revenue potential, there are several other justifications for the adoption of a global transaction tax. Such a tax could facilitate the monitoring of international financial flows by providing a centralized database on such flows, which is the need of the hour. This could be particularly valuable to the poor and developing countries where large information gaps exist.

Unlike many other services, no value added tax (VAT) is imposed on financial transactions in many jurisdictions. By taxing diverse financial transactions, a strong message would be conveyed that private banks and financiers must share the costs of the global financial crisis.

Given the fact that majority of transactions carried out by speculators and high frequency traders are short-term and speculative, this tax can curb speculative tendencies that induce excessive volatility and fragility in the financial markets. While a small tax is unlikely to discourage long-term investors such as pension funds. The argument that the FTT would trigger a liquidity squeeze in financial markets lacks evidence. As argued by Avinash Persaud, "During calm times, when markets are already liquid, high-frequency traders are contrarian and support liquidity, but during times of crisis, they try to run ahead of the trend, draining liquidity just when it is needed most, as we saw with the Flash Crash on 6 May 2010. If a transaction tax limits high-frequency trading it may even provide a bonus in improving systemic resilience."

Is a FTT Feasible?

Much of the criticism of the FTT is centered on the question of its practicability and technical feasibility. It is often argued that the imposition of such a tax is a difficult proposition since the volumes traded are too high. If the modern electronic system can enable large-scale financial transactions within and across borders, why can't the same technology be used to collect taxes?

Critics also argue it is almost impossible to get all the countries to agree on a common global tax. Nevertheless, a beginning can be made with a few countries coming together on this issue even if a strong consensus across territories is not possible immediately. Europe can take the lead and introduce the FTT at the European level. The G20 member-countries could also impose such a tax unilaterally or collectively. An agreement among the leading financial centers could also contain the threat of relocation of financial activities to other places.

The Political Will

The issues raised by FTT are more political than technical. Its adoption requires strong political will, particularly among the G20 member-countries. The recent experience (for instance, money laundering related to drug trafficking) shows that international cooperation among countries is possible if there is a political will. A similar cooperative initiative is required to address myriad implementation issues related to FTT.

Another common criticism of FTT is related to evasion. All taxes (e.g., income tax and property tax), for that matter, are open to evasion but this is not sound enough reason for not having them. Concerted efforts should be made to check loopholes, as no policy measure can be foolproof.

While supporting the case for a global financial transaction tax, no one argues that all problems related to global financial markets would be resolved. In the present times, no single policy instrument alone can fix global finance. Nevertheless, such a tax could serve as a first step towards building international cooperation on global financial reforms. If it is used in conjunction with other policy instruments (for instance, capital controls), FTT does offer an attractive mechanism to reform the inherently unstable global financial markets.