LEBA WMBA

WMBA/LEBA RESPONSE TO THE COMMISSION'S CONSULTATION PAPER:

TAXATION OF THE FINANCIAL SECTOR

About the Wholesale Market Brokers' Association [WMBA] and the London Energy Brokers Association [LEBA] (together here collectively termed "WMBA")

The WMBA is the European Industry Association for the wholesale intermediation of Over-the-Counter (OTC) markets in financial, energy, commodity and emissions markets and their traded derivatives. Our members are Limited Activity firms that act solely as intermediaries in the said wholesale financial markets. As Interdealer Brokers (IDBs), the WMBA members' principal client base is made up of global banks and primary dealers. The replies below to the questions in the paper should be seen in the context of WMBA members acting exclusively as intermediaries, and not as own account traders. (Please see www.wmba.org.uk and www.leba.org.uk for information about the associations, its members and products.) For this reason, some of the questions in the Consultation Paper are not entirely relevant to WMBA members' activities even though they are to most of their clients. Further, some answers take into account industry views and experience.

Operating as the hub of the global financial market infrastructure, IDBs are MiFID compliant and highly regulated intermediaries by virtue of their regulatory authorisation and from being subject to supervision under CAD as Limited Activity firms. Our members are neutral, independent, and multi-lateral and provide free, fair and open access to their trading venues for all suitably authorised and regulated market participants. IDBs do not take positions in the markets in which they operate and their collective service as the gateway to the global financial marketplace creates price discovery and significant liquidity. All transactions, whether executed via voice, hybrid or fully electronic means, are immediately captured at the point of trade, are subject to straight-through-processing, and are made available for transparent and timely transaction reporting to the relevant regulators.

Introduction

WMBA welcomes the opportunity to comment on the Commission's assumptions and request for further related evidence contained in its Consultation Paper "*Taxation of the Financial Sector*" Our response is made from the viewpoint of Limited Licence/Limited Activity firms operating in the wholesale markets and is limited to general observations regarding the scope application and use of the proposed taxes.

Regardless of opinions concerning the quantum of taxation borne by the financial sector, the WMBA strongly asserts that neither VAT nor a tax on Financial Transactions provide a practical or a fair way to raise capital from the sector. Serious difficulties arise from the sequential nature of transactions, the global scope of financial markets and the utility of transactions in raising capital, defraying risk and providing investment vehicles to facilitate the saving process. Each of these functions is necessary and valuable both for financial stability from a macroprudential perspective and for individual end users from a microprudential taxpayer standpoint.

VAT

WMBA would challenge the concept that financial services firms are under-taxed as a result of their transactions being exempted from VAT. VAT has two elements based on (1) the provision, and (2) the receipt of goods and services, with the VAT payable being the net of the two. Financial services firms who purely provide exempted supplies are unable to recover VAT paid in respect of goods and supplies and hence, unlike firms providing VATable services, this results in an indirect tax in the UK of 20% on all the firms' costs (excluding employment costs).

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Coverage of Financial Services Taxation

To be effective for international financial transactions, any tax needs to be introduced on a global basis to avoid an immediate migration effect to non-European centres resulting in a threat to Europe as a competitive financial centre. Whilst the message from the G20 summits since the advent of the global financial crisis has been that taxpayers' money should not be used again to cover bank losses, not all G20 member countries were willing to support the concept of an FTT, believing instead that the outcome could better be achieved via regulatory and prudential supervision. Further, the IMF has noted that an FTT would not meet the requirements of improving the management of systemic risk on a national or global basis. This would suggest that it would not be possible to implement the adoption of an FTT on a global basis and hence the WMBA would respectfully request that the Commission reconsider the implementation of additional taxes on the financial sector and replace it with additional prudential requirements for risk based capital as laid out by the G20.

WMBA agrees with the Commission's analysis that the financial sector has benefited from substantial public support during the crisis but feel that this is limited principally to the banking sector and, hence, a basic financial transaction tax on the whole sector would not be a **fair or reasonable response to the underlying causes of the crisis.** The current proposal would result in standard, high frequency transactions with minimal risk, which did not contribute to the financial crisis, taking the majority of the tax burden. This strategy is contrary to the G20 risk based proposal and the "polluter pays" principle and the WMBA are of the opinion that if FTT is introduced, it should not only be on the value of the underlying but graduated in accordance with instrument, size and potential risk.

The WMBA believes that a much greater contribution to improving the safety of the financial sector and managing global systemic risk can be made by addressing the 'too big to fail' issue relating to banks and insurers through the development of a resolution process currently being studied by the Bank for International Settlements in Basel.

Scope of Financial Transaction Tax (FTT)

IDBs did not contribute to the financial crisis and were regarded by many as providing risk mitigation through their activities to keep markets open and liquid permitting banks to reduce risk and balance sheet exposure.

Any tax on their activities would have to be recovered by increasing charges resulting in lower market liquidity and higher transactions costs for bank users and the economy as a whole.

The Commission is proposing that the Financial Transaction Tax will be cumulative throughout the lifecycle of a trade and the WMBA is concerned as to how this will affect its members who act as intermediaries dealing on a riskless principal basis between client counterparties. WMBA would respectively request that the Commission consider implementing an exemption from FTT for any Limited Activity firm and firms acting as a central counterparty (similar to that operated by the UK HMRC in respect of the Panel on Takeovers and Mergers Levy).

WMBA considers that to avoid an increase in the cost of capital, all primary issues should be exempted from the scope of FTT. Similar exemptions should therefore also be given to those transactions that constitute hedging and lead to a mitigation of extant risk sets.

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Scope of Financial Activity Tax (FAT)
When calculating the rent-taxing FAT (FAT2) and the Risk Taxing FAT (FAT3), the Commission has made the assumption that excessive returns are due to unduly risky activities. However, the WMBA would maintain that profits can also be drawn up by efficiency and economies of scale which would be unfairly taxed under these proposals.

As mentioned above, to avoid regulatory arbitrage it is essential that any tax is introduced on a global basis. WMBA is of the opinion that as a result of divergent accounting standards (accrual vs. cash basis; historic vs. mark to market basis) in some G20 countries, this could not be achieved without substantial accounting and auditing costs.

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Member Firms
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- EBS Group Ltd
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- Reuters Transaction Services Ltd
- Sterling International Brokers Ltd
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