Financial Transaction Tax

European Commission Publishes Revised Draft Directive on Financial Transaction Tax

SUMMARY

Following a European Council decision to allow eleven member states of the eurozone (including France, Germany, Spain and Italy) to introduce a financial transaction tax or “FTT” using the “enhanced cooperation” mechanism, the European Commission published a revised draft FTT directive last week.

The tax would be paid

- by financial institutions
- on transactions in financial instruments
- if either:
  - at least one of the parties were located in the FTT zone; or
  - the financial instrument were issued by an entity established in the FTT zone (except for non-traded derivatives) – the “issuance principle”.

The draft contains few changes from the Commission’s original draft directive of 2011, the addition of the issuance principle described above being one of the most significant.

Sales and purchases of shares and bonds would be taxed at 0.1%, derivative contracts at 0.01%. The tax would be introduced from the start of 2014.

INTRODUCTION AND BACKGROUND

Background

In the wake of the financial crisis there has been much debate around the world on how the financial sector should be taxed.
In October 2010 the European Commission published a communication on the relative merits of an FTT and a “financial activities tax” as means of taxing the sector. After lobbying from France and Germany, the European Commission published a draft directive on a common system of financial transaction tax on 28 September 2011.¹

While a significant number of member states supported the proposal, several (most notably the United Kingdom, Sweden and the Czech Republic) were strongly against it. Discussions at EU Council level in 2012 served to make clear that the objectives of a common system of FTT, as outlined in the Commission’s initial proposal, could not be attained within a reasonable period of time by all of the EU member states together.

Since the Commission tabled its original proposal, several member states have legislated for financial transaction taxes (France, with effect from 1 August 2012²; Hungary, from 1 January 2013; Italy, from 1 March 2013). Others have announced plans to introduce similar taxes. Some member states already had taxes covering at least some of the ground of the proposed FTT: the United Kingdom, for example, has its stamp duty and stamp duty reserve tax regime.

At the same time Austria, Belgium, Estonia, France, Germany, Greece, Italy, Portugal, Slovakia and Slovenia and Spain (the “Participating Member States”) agreed to move forward with a harmonised FTT. (The Participating Member States are the member states of the eurozone minus Cyprus, Finland, Ireland, Luxembourg, Malta and the Netherlands.) In October 2012 the Commission issued a draft decision authorising use of the enhanced cooperation procedure, which allows at least nine member states to adopt measures that will apply only to those member states (and not to all EU member states). This decision was approved by the European Parliament on 12 December 2012 and by the ECOFIN Council on 22 January 2013. On 14 February the Commission published a revised draft directive for a harmonised system of FTT in the eleven Participating Member States as the next step in this procedure.³

The draft directive is, as expected, largely based on the initial proposal for all 27 member states published in September 2011. The main changes are:

- an exemption for the issue (but not redemption) of units in UCITS funds and alternative investment funds;
- an exemption for restructurings;

³ All of the documents published by the Commission, including the original and revised draft directives and related impact assessments, are available at: ec.europa.eu/taxation_customs/taxation/other_taxes/financial_sector/index_en.htm.
the introduction of an issuance principle to catch instruments issued by entities established in the FTT zone but traded by parties outside it; and

the inclusion in the directive itself of anti-avoidance rules.

We discuss these changes in more detail below.

Comparison with the French transaction tax

The scope of the French transaction tax – charged at 0.2% on the acquisition price of the instrument – is very limited by contrast with the proposed EU FTT.

- It applies only to the acquisition of shares or certain similar instruments, such as stock warrants and convertible bonds. Depository receipts are also within the scope of the tax. By contrast, transactions on straight bonds, UCITS units and derivatives are not covered.

- It applies only to shares or instruments issued by companies with a market capitalisation over €1 billion.

- Only shares issued by French companies are captured. Shares issued by non-French companies, even those listed in France, are not subject to the tax.

In fact, in these respects the French tax is closer to the UK's stamp duty/SDRT regime than to the draft FTT.

Impact

The Commission estimates that the tax could raise of the order of €31 billion a year. At this stage that figure must be highly conjectural, especially if significant financial business migrates to non-FTT-zone financial centres as a consequence.

It is not yet clear whether part of the revenue would go not to the Participating Member States, but to the EU itself as "own resources".

Next steps

The revised draft directive will have to be adopted unanimously by a meeting of the EU Council at which only the Participating Member States will be allowed to vote. Then, according to the draft directive, each Participating Member State is to adopt and publish by 30 September 2013 the laws, regulations and administrative provisions necessary to comply with the FTT directive. The FTT is to come into effect on 1 January 2014.

OVERVIEW

Economic scope. The FTT would be charged:

- on financial institutions;
- in respect of financial transactions.
Territorial scope. The FTT would apply where:

- at least one party was a financial institution; and
- either:
  - at least one party was established in a Participating Member State; or
  - the financial instrument was issued in a Participating Member State (except for non-traded derivatives),

unless:

- the “economic substance” of the transaction is not linked with the Participating Member States.

Liability. Where both parties to a transaction are financial institutions, both would have to pay FTT. Where only one is, it would only be subject to a single charge.

Rates. The draft directive sets out minimum rates:

- 0.01% for derivatives; and
- 0.1% for other transactions.

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ECONOMIC SCOPE

Financial institutions

Basic definition. “Financial institution” is broadly defined and includes:

- banks and other “credit institutions”;
- broker-dealers and other “investment firms”;
- regulated markets and other organised trade venues or platforms;
- insurance and reinsurance companies;
- undertakings for collective investments in transferable securities (“UCITS”) and their managers;
- pension funds and their managers;
- alternative investment funds (“AIFs”) and their managers;
- securitisation special purpose entities; and
- other entities if both:
  - the annual value of their financial transactions is over 50% of their annual turnover; and
  - they are engaged in certain financial activities including trading in financial instruments or the acquisition of holdings in undertakings (potentially of very broad application).  

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4 Most of these terms are defined by reference to EU regulatory directives.
**Exclusions.** Some institutions are excluded from the scope of the draft directive. The exclusion takes two forms. In some cases it applies only to the institution itself and its counterparty may still be taxed (and if its counterparty fails to pay, the institution takes on its FTT liability). In others, the institution casts its mantle over the transaction as a whole, and its counterparty also benefits from the exclusion.

- Exclusion for the institution itself:
  - certain market intermediaries in their role as such:
    - central counterparties ("CCPs");
    - central securities depositories ("CSDs"); and
    - international central securities depositories ("ICSDs").
  - member states when managing public debt;
- Exclusion for institution and counterparty:
  - the European Central Bank, the European Financial Stability Facility and the European Stability Mechanism;
  - certain other EU institutions, including the European Investment Bank, in respect of some transactions;
  - international organisations or bodies (other than those listed above) recognised as such in their host states, within the limits set out in the conventions establishing them or their headquarters agreements with their host states – for example, the International Monetary Fund; and
  - transactions with the central banks of EU member states.

There is no specific exclusion for central banks outside the EU or other national government agencies.

**Financial transactions**

**Basic definition.** "Financial transaction" is also broadly defined. It includes:

- the purchase and sale (including issue – but see the exemptions below – and redemption) of:
  - shares;
  - bonds;
  - money market instruments; or
  - units of UCITS and AIFs;
- repos and stock loans; and
- the conclusion or modification of most forms of derivative agreement (whether or not over financial instruments).

Transactions that do not involve financial instruments or derivatives would not be subject to the FTT. The Commission aims to keep most day-to-day financial activities relevant to individuals and non-financial businesses outside the FTT. These include insurance, mortgage lending, consumer lending, payment services and spot currency transactions. It is not clear whether life assurance would be classified as insurance and kept out of the FTT: life assurance is often a form of investment in shares and other
securities. Syndicated lending to corporates also seems likely to fall outside the FTT, on the basis that such loans should not be transferable securities as defined for the purposes of the directive.

The FTT would not be limited to trades on organised markets, but would also cover other types of trade, including over-the-counter trades.

Repos and stock loans would be viewed as a single taxable transaction. (The original draft raised the possibility that they might be viewed as two transactions.) A fixed-price repo is economically equivalent to a secured loan, which would not be taxed at all. However, repos and stock loans are implicated in short selling, which the Commission wants to curb. Including stock loans within the FTT charge means that transfers of non-cash collateral under derivatives, repos and stock loans would attract an additional FTT charge (or charges if the collateral is substituted).

**Primary market exclusion.** The issue of shares, other equity securities and bonds would be excluded from the FTT. The revised draft would allow the issue of shares or units in UCITS and AIFs to benefit from this exclusion. The transfer of shares from an underwriter to a purchaser as part of an issue of shares would also be excluded.

**Mergers and takeovers.** In order to comply with the Capital Duties Directive\(^5\), the new draft directive exempts those reorganisations that are exempt from capital duties, such as mergers, spin-offs and acquisitions of shares giving majority control in a company in return for the issue of shares by the acquirer. The liquidation of a wholly-owned subsidiary is also exempt.

**Groups.** Many transaction taxes provide for intra-group transactions to be exempt. Not so the FTT. In fact, the rules for intra-group transactions are more stringent. Intra-group transfers “of the right to dispose of a financial instrument as owner and any equivalent operation implying the transfer of the risk associated with the financial instrument” are specifically included, even if they fall outside the basic definition of “financial transaction”.

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**TERRITORIAL SCOPE**

**The three elements of the restriction**

As noted in the overview, the FTT would be subject to a territorial restriction. This has three elements:

- at least one party to the transaction must be established in a Participating Member State; and
- a financial institution established in the territory of a Participating Member State\(^6\) must be:

\(^5\) Directive 2008/7/EC.

\(^6\) It will be seen below that a financial institution may be treated as established in a Participating Member State even if it is established outside the FTT zone in every meaningful sense.
Financial Transaction Tax
February 2013

- party to the transaction on its own account;
- party to the transaction for the account of another person; or
- acting in the name of a party to the transaction;
- with an exclusion where the taxpayer “proves that there is no link between the economic substance of the transaction and the territory of any participating Member State”.

Non-financial institutions
Non-financial-institutions would be “established within a participating Member State”:
- if they have their registered seat\(^7\) there; or (failing that)
- if they have a branch there (but only for transactions carried out by that branch).

Financial institutions
The draft directive sets out a hierarchy of rules for determining whether a financial institution is “established in the territory of a participating Member State”. Financial institutions would pay FTT to their member state of establishment, at the rate set by that member state.

A financial institution would be established in the first of the following:
- a participating member state from which it has its authorisation (but only for transactions covered by the authorisation);
- a participating member state in which it is authorised or otherwise entitled to operate (but only for transactions covered by the authorisation);
- the participating member state where it has its registered seat;
- the participating member state where it has its permanent address or usual residence;
- a participating member state where it has a branch (but only for transactions carried out by the branch);
- the participating member state where the counterparty to the financial transaction is established.

Clearly, the final bullet makes the definition of “establishment” much broader than the term itself would suggest.

It appears that a financial institution which is “established in the territory of a participating Member State” would be treated as “established in a participating Member State” for the purposes of the requirement that “at least one party to the transaction must be established in a participating Member State”.

\(^7\) For individuals, where they have their permanent address or usual residence.
Issuance principle
Onto this broad definition of “establishment” the revised draft directive has grafted an *issuance principle*: if the financial institution is not otherwise established in a member state, it is to be treated as established in the Participating Member State in which the financial instrument or structured product was issued. This is intended to stop parties or financial intermediaries from relocating in order to avoid the FTT. The rule does not apply to derivatives unless they are traded on an organised platform.

Examples
How this would apply is illustrated below.

**Example 1.** German Sub, the German subsidiary of US Bank (and authorised in Germany), enters into a transaction with the Frankfurt Branch of French Bank (authorised in France and passported into Germany).

The tests are applied in order until one of them gives a Participating Member State:

<table>
<thead>
<tr>
<th></th>
<th>German Sub</th>
<th>French Bank</th>
</tr>
</thead>
<tbody>
<tr>
<td>Authorisation from</td>
<td>Germany</td>
<td>France</td>
</tr>
<tr>
<td></td>
<td>✓</td>
<td>✓</td>
</tr>
</tbody>
</table>

German Sub is “established” in Germany for the purposes of the transaction. It will pay FTT to Germany at the rate set by Germany. French Bank is “established” in France and will pay FTT to France at the French rate.
**Example 2.** The transaction is an off-market transaction between the branches of US Bank and French Bank in a third country outside the EU (both authorised in the third country).

![Diagram](image)

The tests are applied in order until one of them gives a Participating Member State:

<table>
<thead>
<tr>
<th>US Bank</th>
<th>French Bank</th>
</tr>
</thead>
<tbody>
<tr>
<td>Authorisation from</td>
<td>Authorisation from</td>
</tr>
<tr>
<td>Third Country</td>
<td>Third Country</td>
</tr>
<tr>
<td>x</td>
<td>x</td>
</tr>
<tr>
<td>Authorisation in</td>
<td>Authorisation in</td>
</tr>
<tr>
<td>Third Country</td>
<td>Third Country</td>
</tr>
<tr>
<td>x</td>
<td>x</td>
</tr>
<tr>
<td>Registered seat</td>
<td>Registered seat</td>
</tr>
<tr>
<td>US</td>
<td>France</td>
</tr>
<tr>
<td>x</td>
<td>✔</td>
</tr>
<tr>
<td>Address/Residence</td>
<td></td>
</tr>
<tr>
<td>US</td>
<td></td>
</tr>
<tr>
<td>x</td>
<td></td>
</tr>
<tr>
<td>Branch</td>
<td></td>
</tr>
<tr>
<td>Third Country</td>
<td></td>
</tr>
<tr>
<td>x</td>
<td></td>
</tr>
<tr>
<td>Counterparty</td>
<td></td>
</tr>
<tr>
<td>France</td>
<td></td>
</tr>
<tr>
<td>✔</td>
<td></td>
</tr>
</tbody>
</table>

For the purposes of this transaction, both US Bank and French Bank are “established” in France and should pay FTT to France at the French rate.

In other words, a financial transaction with a non-FTT-zone branch of any FTT-zone financial institution would be subject to FTT unless it fell within the exclusion for transactions not linked with the FTT zone.

**Example 3.** The London branch of US Bank sells shares in a German company (which has a secondary listing on the London Stock Exchange) to UK Bank.

![Diagram](image)
The tests are applied in order until one of them gives a Participating Member State:

<table>
<thead>
<tr>
<th></th>
<th>US Bank</th>
<th>UK Bank</th>
</tr>
</thead>
<tbody>
<tr>
<td>Authorisation from</td>
<td>UK</td>
<td>x</td>
</tr>
<tr>
<td>Authorisation in</td>
<td>UK</td>
<td>x</td>
</tr>
<tr>
<td>Registered seat</td>
<td>US</td>
<td>x</td>
</tr>
<tr>
<td>Address/Residence</td>
<td>US</td>
<td>x</td>
</tr>
<tr>
<td>Branch</td>
<td>UK</td>
<td>x</td>
</tr>
<tr>
<td>Counterparty</td>
<td>UK</td>
<td>x</td>
</tr>
<tr>
<td>Instrument issued</td>
<td>Germany</td>
<td>✓</td>
</tr>
</tbody>
</table>

For the purposes of this transaction, both US Bank and UK Bank are “established” in Germany and should pay FTT to Germany at the German rate, under the issuance principle.

**Exclusion**

As noted above, if the taxpayer could prove that there was “no link between the economic substance of the transaction and the territory of any participating Member State”, the transaction would be excluded from the scope of FTT.

The draft does not go into any detail on what this means. Economic substance linked to the FTT zone might refer to:

- the assets or liabilities underlying transactions;
- where financial institutions carry out the necessary activities for transactions; or
- perhaps both.

Looking at the asset or liability underlying a transaction, the Commission (or the European Court of Justice) might see a link with a member state in the case of a credit default swap (to take just one example) over an FTT-zone corporate, financial institution or sovereign credit.

The draft does not make it clear whether a financial institution would need to apply for the exclusion on a case-by-case basis (surely unworkable) or claim it in its FTT return. What is clear is that the burden of proving that a demanding and nebulous condition has been met is firmly on the taxpayer.

**TAX POINT, TAXABLE BASE AND RATES**

**Tax point**

The FTT would be charged on each financial transaction when it occurred, rather than, for example, when individual cashflows arose under that transaction. The fact that a transaction was subsequently cancelled or rectified would be irrelevant except in the case of errors.
**Taxable base**

The taxable base would depend on whether or not the financial transaction constituted a derivative. In the case of transactions which were not derivative agreements, the taxable amount would be the consideration paid or owed under the transaction. It would not matter whether the consideration came from a party to the transaction or a third party. The taxable amount would, however, be the fair market value where the consideration was lower than the market price or where a transaction took place between group entities. Settlement netting would be ignored.

By contrast, for derivative agreements the taxable amount for FTT purposes would be the notional amount of the derivative at the time of the financial transaction. Where there was more than one notional amount, the taxable amount would be the highest amount. Netting would also be ignored when calculating the taxable amount with respect to transactions on derivative contracts.

**Rates**

Participating Member States would be free to set their own FTT rates as a percentage of the taxable amount. However, the draft directive specifies that these rates shall not be lower than 0.1%, other than in the case of financial transactions relating to derivative agreements, in which case the minimum rate is 0.01%. The lower rate for derivative agreements reflects the fact that the taxable base for such transactions would not be the consideration for the transaction but the (higher) notional amount of the derivative.

The difference between taxing a transaction as a derivative on 0.01% of the notional amount or under the default rules on 0.1% of the consideration would vary from transaction to transaction. Options would be taxed as derivatives. Whether this would be an advantage would depend on the ratio of the option premium to the notional value of the contract.

**COMPLIANCE OBLIGATIONS**

Liability for FTT would fall on each financial institution or entity treated as such which was a party to the transaction (whether for its own account or otherwise) or on whose account the transaction had been carried out. Where a financial institution only acted for the account of another financial institution, that other institution would be liable for the FTT. The draft directive imposes joint and several liability on each party to a transaction for the FTT due by a financial institution, if the latter fails to pay the tax. This joint and several liability can extend to persons other than financial institutions. The draft directive further empowers Participating Member States to extend the scope of this joint and several liability to other parties. It would be for Participating Member States to prescribe the registration, tax accounting and other compliance obligations required to account for and collect FTT. Financial institutions would have to make a return on the 10th day of each month in respect of FTT chargeable in the previous month.
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Any FTT due would have to be paid either (i) when the tax became chargeable, in the case of an electronic transaction; or (ii) within three working days from when the tax became chargeable, in all other cases.

ANTI-AVOIDANCE

The draft directive requires member states to adopt measures to prevent tax fraud and evasion. The original draft directive required member states to adopt measures to prevent avoidance and abuse as well; the Commission has now drafted its own anti-abuse rules.

The first is a general anti-abuse rule. By way of background, in December 2012 the Commission issued a recommendation that all member states should introduce a general anti-abuse rule in their domestic legislation. It has adopted that drafting here with minimal changes. The rule applies where an arrangement:

- “lacks commercial substance”;
- “defeats the object, spirit and purpose of the tax provisions”; and
- any other purpose it may have “appears at most negligible”.

The arrangement is to be ignored and the transaction taxed on its economic substance.

The second is a specific anti-abuse rule targeted at the use of depositary receipts. This applies where depositary receipts are issued over underlying securities from the FTT zone in order to escape an FTT charge under the issuance principle, again, if any other purpose appears “negligible”. Where trade in the depositary receipts has replaced trade in the underlying securities “to a significant extent”, the burden of proving that the depositary receipt was not issued to avoid FTT is on the taxpayer. (Note that the taxpayer will usually not have been involved in the issue of the depositary receipt.) Where the rule applies the depositary receipt is to be treated as if issued where the underlying security was issued.

INTERACTION WITH OTHER TAXES

Apart from VAT, it is intended that there should not be any tax on financial transactions other than the FTT. Of course, most financial transactions do not give rise to VAT, although the Principal VAT Directive⁸ provides for the possibility of an “option to tax” in respect of such transactions.

It will be for national jurisdictions to determine whether the cost of FTT is available as a deduction from gains made on financial transactions subject to it.

⁸ Directive 2006/112/EC.
COMMENTARY

Compatibility with EU law

Questions have been raised as to whether a directive in this form introduced only in part of the EU’s territory would be compatible with EU law. In particular –

- Would it actually meet the requirements of the enhanced cooperation procedure?
  - Would it enhance integration?
  - Would it create no barriers to trade or distortions of competition?
  - And would it – in particular the rule treating a non-FTT-zone financial institution transacting with an FTT-zone institution as itself established in the FTT zone – respect the competences, rights and obligations of non-participating member states?

- Would the proposed establishment rules – under which FTT-zone financial institutions operating in member states outside the FTT zone through branches would be treated less favourably than those operating through subsidiaries – be compatible with the freedom of establishment required under the EU treaty?

- Would the proposed rules – particularly as they relate to derivatives – be compatible with the treaty right to free movement of capital?

Implications

The FTT would clearly have a range of implications.

**Short-term transactions.** The rate of tax takes no account of the duration of the transaction. It would therefore have its strongest impact on short-term transactions. These include high-frequency trading transactions, which the Commission would happily see reduced. But they may also include market-making, the short-term derivatives used by banks to manage risk and the short-term repos they use to manage liquidity. The tax would apply each time a transaction is rolled over.

**Complex transactions.** The more separate transactions, the more charges. A redemption of units in a UCITS may require the fund to sell securities, giving rise to double or (in the case of a fund of funds) triple charges. A floating-to-fixed interest-rate swap hedging a floating-rate loan would be chargeable, where a simple fixed-rate loan would not. Hedging an equity derivative for a customer by buying the relevant equities would incur an additional charge. Synthesising one derivative by combining others would give rise to multiple charges. And so on.

**Principal and agency models.** In some jurisdictions brokers and clearing members of exchanges act as principals in a chain of transactions ultimately between non-market-participants. In the UK such market intermediaries benefit from exemptions from stamp duty and SDRT. No such exemption is envisaged for FTT, so this market structure would create a cascade of FTT charges. The new Commission impact assessment recognises that the issue exists, but suggests merely that those market participants could act as agents rather than principals without reducing the value of their activities.
Financial Transaction Tax
22 February 2013

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**ADRs.** How would American Depositary Receipt programmes be affected by FTT? ADR programmes would be subject to FTT if reasons for putting them in place other than FTT avoidance were negligible. There are clearly already commercial factors leading to the use of ADR programmes: US investors find ADRs attractive because they offer dollar cashflows and larger denomination "shares". As a result, the targeted anti-abuse rule may not have much impact because factors other than FTT avoidance will not usually be negligible as reasons for putting the programmes in place. The anti-avoidance rule does not seem intended to catch *bona fide* ADR programmes.

**Subsidiarisation.** There would be a strong incentive for financial institutions headquartered in the FTT zone to use subsidiaries rather than branches outside the FTT zone, to the extent they do not already do so. Of course, other factors such as local regulatory capital requirements would also be relevant.

**Intra-group transactions.** As noted above, there is no specific intra-group exemption, and indeed some transactions within groups may be caught where they would not be if they were between unconnected parties. That said, groups may be able to replace some cross-border transactions with notional transfers between branches of the same entity. FTT will incentivise groups to carry out internal restructurings through asset rather than share sales, although VAT and other transfer taxes, particularly on real estate transfers, will then be relevant. Some intra-group reorganisations might be structured so as to fall within the exemption for mergers and takeovers, as long as the structure is not so artificial as to be caught by the general anti-avoidance rule.

**Mergers and takeovers exemption.** More generally, that exemption does not require that the acquiror be established in the FTT zone to benefit from the exemption when it acquires an FTT-zone target in a share-for-share exchange.

**Economic impact of the tax.** Banks would no doubt seek to pass on the economic burden of FTT in their standard-form documentation for underwriting, repos and stock loans. This would incentivise non-FTT-zone counterparties to deal with non-FTT-zone financial institutions.

**Rates.** Although Participating Member States would in theory be free to set rates of FTT above the minimum, it is difficult to see any of the significant players exercising that freedom in practice. A Participating Member State doing so would put its own financial sector at a competitive disadvantage.

**Compliance burden.** A financial institution authorised by a Participating Member State would only have to deal with FTT in that Participating Member State, unless a counterparty in another Participating Member State defaulted on its FTT liability. A financial institution established elsewhere, however, might have to deal with FTT as a matter of course in any Participating Member State where one of its counterparties was established, and possibly others as well under the issuance principle.

**Enforceability.** The revised draft directive brings into sharper focus the issue of how the FTT will be collected when the institution liable has neither head office nor branch in the FTT zone. Under the
previous proposal at least one party had to be in a jurisdiction applying the FTT and was therefore available to be pursued for the tax of both parties (once the secondary liability rules were applied). Liability under the issuance principle is not as easily enforced.

The current draft of the directive does not offer a mechanism to ensure that FTT is collected when a transaction subject to it takes place outside the FTT zone. The draft provides that each Participating Member State shall implement its own collection system.

Two existing tax regimes similar to the FTT may illustrate how the issue may be addressed.

The UK has grappled with enforcement in designing its system of stamp duty and SDRT. Where listed shares are held and traded through CREST\(^9\) (the central securities depository for the UK), the 0.5% SDRT on ordinary transfers is collected through CREST. How then to deal with shares transferred into clearance services or depositary receipt schemes? The UK’s solution was to impose a 1.5% “season-ticket” charge on the issue or transfer of chargeable securities into clearance services or depositary receipt schemes – which it could police more easily than any subsequent transfers – and allow clearance services to agree to operate a 0.5% per-transaction charge and enforce it on HMRC’s behalf instead. This elegant solution has been unravelling since the European Court of Justice found that the season-ticket charge contravened the Capital Duties Directive\(^10\) in the first of the HSBC cases\(^11\).)

The French financial transaction tax provides a similar example. French law makers have taken advantage of the fact that transfers of shares listed in France are systematically centralised through Euroclear France and by requiring Euroclear France to collect the tax.\(^12\) Collection is said to be the reason why the French FTT has been limited to shares issued by French issuers, as in practice the tax would have been difficult to collect on instruments not centralised in Euroclear France.

The merit of this mechanism is that it provides certainty that transfers of shares within the scope of the tax will be taxed effectively, even when carried out between foreign counterparties. However, it cannot constitute a viable solution for collecting the FTT on unlisted instruments or on instruments that are not required to be centralised in institutions such as Euroclear. It is worth noting in this context that the UK

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\(^9\) Now operated by Euroclear UK & Ireland.

\(^10\) Directive 69/335/EEC; since replaced by Directive 2008/7/EC.


\(^12\) In the case of ADRs, which are not registered in Euroclear France’s registries, the collection of the French transaction tax must be done directly by the (mostly foreign) brokers who have dealt with the purchase order. As the French transaction tax has only been applicable to ADRs since 1 December 2012, it is difficult at present to assess whether and how this measure is enforced.
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has seen some substitution of transactions in shares by transactions in derivatives to which SDRT does not attach.

Global FTT. Finally, the territoriality provisions in the draft directive have not been framed with global rollout in mind. The draft does not offer any credit mechanism for any FTT levied otherwise than under the draft directive, or allow for a tax treaty override to prevent double taxation, although the Commission’s impact assessment refers to the use of tax treaties to prevent double taxation within the EU. Of course, a network of tax treaties would take some time to put in place.

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