To:
The Members of European Parliament

Subject: Proposal for a directive on a financial transaction tax (COM (2011) 594)

Eumedion is pleased to respond to the proposal published by the European Commission on 28 September 2011 for a directive on a common system of financial transaction tax (hereafter: the proposed directive).[1] We would be very grateful if you were to take our comments into account in the Dutch position during the negotiations on the proposed directive.

1. General

Eumedion fully understands that the European Commission seeks possibilities of spreading the social costs of the financial crisis in such a way that these are not borne by taxpayers alone. Furthermore, Eumedion wholeheartedly endorses a number of the goals that form the basis for the proposed directive. The creation of disincentives for certain short-term transactions (high frequency trading) and highly leveraged derivative transactions[2] is highly consistent with Eumedion's core objectives of facilitating the corporate governance structure of listed companies and engaged shareholdership by institutional investors with a long-term investment horizon.

We have serious doubts, however, as to whether the said goal of the proposed directive will actuallt also be achieved. Since the financial transaction tax (FTT) is very broadly based and relates to transactions in all kinds of financial instruments and derivatives, it does not specifically target speculative short-term transactions, e.g. transactions for the implementation of the long-term investment strategies of institutional investors are also disincentivized by the proposed directive. Moreover, since the proposed directive would tax transactions in shares and bonds

[1] Proposal for a Council Directive on a common system of financial transaction tax and amending Directive 2008/7/EC (COM (2011) 594 final).
[2] Explanatory memorandum p. 4-5.

more heavily than transactions in derivatives, even when such transactions in shares and bonds are being carried out by stable and creditworthy institutional investors with long-term goals.[3] Such a measure could discourage institutional investors (pension funds, insurers and managers of investment institutions) from holding shares and bonds in listed companies, precisely in a period in which lending to listed companies is already under pressure. This is not mitigated by the fact that the FTT will not apply to issues of shares and bonds (primary market).[4]

Another problem concerns the infrastructure over which the transactions are carried out. It is usual practice in the financial markets for a chain of parties to be involved in the purchase or sale of a financial instrument or a derivative by an institutional investor. These parties include intermediary ba'nks, dealers, brokers and clearing and settlement parties. A number of 'subtransactions take place in the chain for the purposes of purchase and sale. Since all subtransactions are subject to the FTT in principle, an extremely undesirable cumulation of charges (known as a cascade effect) can take place in the case of a single purchase or sale of a financial instrument or derivative.

A subsequent problem involving multiple FTT charges can occur when institutional investors invest via funds. The purchase and sale transactions of the investor in the funds are taxed, while the investment institution has to carry out transactions in its own portfolio as a consequence of the relevant purchase or sale and these are also taxed in their turn. This means a double charge is made for the same action, the costs of which are borne by the clients of institutional investors and which also creates an unlevel playing field between direct investments and investments via investment institutions. In the case of a sale transaction by an investor in participations in a fund, moreover, it is the remaining investors in the fund who ultimately pay the bill for the FTT on the underlying investments. This situation of multiple charges can have even more adverse effects when the fund (partly) invests in other funds.

What is more, as the European Commission concludes in its own impact assessment, the introduction of the FTT could lead to a considerable loss of economic growth of between 0.53 and 1.79% inside the European Union.[5] This loss is expressed, for example, in the approximately 3 billion that the Dutch pension sector is expected to have to pay for the FTT according to initial estimates, which will be at the expense of the present and future pensions of Dutch citizens. The adverse effects that the FTT will entail for insurers and managers of investment institutions will also ultimately be borne to a significant extent by (private) insured and participants in the relevant investment funds. After all, institutional investors by their nature invest either directly or indirectly

[3] Articles 5, 6 and 8 of the proposed Directive.
[4]Article 1 par. 4 of the proposed Directive.
[5] Executive summary of the impact assessment, p. 10 (SEC (2011) 1103 final).

at the expense and risk of their clients (the final beneficiaries). Should the return on these investments come under pressure, which would happen if the FTT were to be introduced, then it will also be the (private) clients of the institutional investors who will suffer the consequences. Even if the negative effects on the returns for institutional investors remained moderate on an annual basis, this could have major consequences for the pension accrual of individual clients for example, over a relevant longer term.

2. Facilitation of shareholdership in listed companies

Eumedion would like to point out that there are many more effective methods that the European legislature could use to counter high-risk short-term action and facilitate responsible investment policies with long-term goals. These methods – which are capable of achieving fast results if required - are briefly set out below:

- Introduction of specific regulation and supervision in order to counter the adverse effects of high frequency trading and other types of algorithmic trading. A first step in this direction has been taken with the measures contained in the proposals for amending the directive on markets in financial instruments (MiFID II) recently published by the European Commission.
- Removal of existing restrictions on the exercise of voting rights and other shareholders' rights, as set out in our response to the consultation document for the European Securities Law Directive.[6]
- Removal of impediments to the long-term holding of shares in listed companies by pension funds and insurers which ensue from legislation and supervisory rules (Solvency II and the FTK financial assessment framework).
- Facilitation of the publication by listed companies of good quality and relevant information on the most important risks, strategy and other non-financial aspects.

We would be every grateful if you would endeavour to achieve acceptance of these proposals at European level.

3. A less detrimental FTT?

Should the European Union nevertheless still decide to introduce the FTT, which Eumedion believes would be unwise (as stated above), then significant changes should at least be made to its scope and substance, in order to prevent it having extremely detrimental consequences. The fundamental changes required should include the following:

- The FTT should be introduced worldwide. If jurisdictions in which important financial centres are located are exempted from the scope of the FTT, its introduction will not lead to a decrease in undesirable, high-risk transactions in financial instruments, since trading will

[6] http://www.eumedion.nl/page/downloads/SLD_-_investors_position_2010_DEF_II.pdf.

simply relocate geographically to these centres. The goal of the FTT will not be achieved as a result and the EU will, instead, make itself unattractive to financial enterprises in favour of regions where no rules or more flexible ones apply and supervision may be less well developed.

- The FTT percentages should be determined in such a way that their negative effects on the management costs for institutional investors remain as limited as possible. This would not appear to be the case for the rates presently proposed.
- Shares and instruments comparable with shares should not be taxed more heavily than other categories of financial instruments or than derivatives.
- A cumulation of charges as a consequence of a cascade effect should be prevented at all times. The purchase or sale of a certain financial instrument or a derivative should only be taxed once.

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