



The Robin Hood Tax

Pre-Budget Submission to HM Treasury, March 2010

Introduction

This submission is made by those organisations that collectively make up the Robin Hood Tax Campaign.

The Robin Hood Tax campaign is a movement bringing together dozens of organisations that work to reduce poverty in the UK and overseas, and campaign to tackle climate change. They have come together during the economic crisis to campaign for a new deal between banks and society. A full list of participating organisations can be found on our <http://robinhoodtax.org.uk>

Robin Hood Taxes are Financial Transaction Taxes (FTTs). The objective of the Robin Hood Tax campaign is to charge a tiny tax on speculative banking and financial transactions that would raise billions to tackle poverty and climate change, at home and abroad.

Because of the financial crisis, frontline services at home – like the NHS and our schools – are under fire. At the same time, poor communities and the environment are being hit hard – as aid and green budgets are slashed by rich countries.

Our argument is simple.

We are suffering from a crisis that was made in the finance sector. It is only right that they should make a proper contribution to putting right the damage they caused. Banks and financial institutions need to rebuild a social contract with the rest of society by helping avoid cuts in spending on vital public services, paying for progress towards the Millennium Development Goals and tackling climate change.

The best way to do this is through levying an internationally agreed set of transaction taxes agreed by the G20, but we are also clear that the UK can – and should – implement and extend unilateral transaction taxes.

A unilateral start will not only raise useful income, but would also be an act of global leadership, setting an example that we believe would be swiftly followed by other countries who face the same difficulties.

In particular this Budget should be used to introduce a stamp duty of 0.005 per cent on sterling foreign exchange transactions wherever they take place in the world.

What the Chancellor should say

- The Government is committed to G20 agreement on a range of FTTs including foreign exchange, derivative and equity trading, and will work with, and lobby, other G20 members to win support for this. The proceeds of such taxes should be split 50 per cent for domestic spending, 25 per cent for international development and 25 per cent for international work to tackle climate change.
- The Government is committed to examining the potential for implementing and extending unilateral and multi-lateral transaction taxes in the UK, across the EU and with other supportive countries such as Japan.
- The Government will introduce an immediate sterling Currency Transaction Tax (CTT) of 0.005 per cent on sterling transactions in the wholesale foreign exchange market that would not only raise around £3 billion in revenue, but also demonstrate to other countries the value and practicality of transaction taxes.

The Robin Hood Taxes we need

The Robin Hood Tax campaign is calling for the creation of international FTTs of three broad types:

The first type of tax is based on the classic form of financial transaction tax envisaged by James Tobin in 1972 on foreign exchange dealing. We are, however, proposing that this tax be charged at a much lower rate than that envisaged when it was first proposed.

Our proposal is for a tax on wholesale foreign exchange transactions, at a rate of 0.005 per cent. Transactions of low value or those with retail customers of banks should be exempted from this charge.

The second category is for a FTT to be charged on all derivative, swap and bond transactions plus all contracts for difference. Because bonds are traded in place of interest rate swaps they are grouped together for this purpose here. Again, it is proposed that a tax of 0.005 per cent (half a basis point) be charged on transactions in these financial products.

Finally the Robin Hood Tax campaign proposes a type of tax where the UK already leads the field – a charge of 0.5 per cent on all transactions in shares.

Why we need Robin Hood Taxes

The Robin Hood Tax campaign argues that all three categories of FTTs are needed internationally. There are three reasons for saying so.

The first is to raise revenues from banks and related organisations to help pay for the economic crisis they have caused.

Secondly, we believe that such a tax will reduce the risk of another financial crisis by encouraging a more risk-averse approach to banking – though we do not suggest that transaction taxes are an alternative to properly regulating the financial system.

Third, we believe that a specific pool of funds must be created for use in the future to help fund the relief of poverty at home and abroad, and believe that Robin Hood Taxes could help achieve this goal, and thus establish a new social contract between finance and the rest of society.

How much would Robin Hood Taxes raise?

We are quite realistic: Robin Hood Taxes won't solve all the world's problems by themselves. They can't.

Estimates of the amount they might raise vary. Transaction taxes will reduce volume, and affect income from other taxes on bank and finance house profits, and on the super-rich individuals at the top of such institutions.

But we are confident that the net tax take can increase substantially. A wide-ranging recent review¹ suggested that around the world they might raise as much as \$400 billion annually. That figure falls within the range of all recent estimates. It's also fair to note that a significant part of this revenue might arise in the USA because of the size of its financial markets. This is one reason why we think that it is reasonable to earmark half the proceeds for international spending so that there is an element of global redistribution built into the design of the tax system.

In the UK the proceeds of Robin Hood Taxes would be significant. Currently the UK's stamp duty on shares raises revenue of between £3bn and £4bn a year². A sterling CTT would likely yield in excess of £3 billion,³ and so we are confident that combined with the third category of transactions – derivative, swap and bond transactions plus all contracts for difference – the eventual revenue generated would be tens of billions.

The UK would also raise considerable sums from the proposed two new Robin Hood Taxes. This is because London is in all cases the biggest or one of the biggest trading centres for the assets that would then be subject to the tax.

Start the ball rolling with a sterling CTT

Getting international agreement for a full Robin Hood Tax system will not be easy. But we do not believe that we need to wait until every G20 country is prepared to back this approach.

The UK Government is ideally placed to show moral leadership to the rest of the world by demonstrating that transaction taxes are workable, fair and can raise worthwhile revenue. This is because unilateral CTTs are now entirely workable because of the changes that have occurred in the way that the banks conduct such transactions.

While it may have been the case in the past that a sterling CTT could not be implemented unilaterally, this is no longer so. Historically, the global foreign exchange (FX) market was made up of disparate parts not necessarily connected to each other. Trades were executed manually by phone between counterparties, and settled through a variety of systems with few linkages between them.

¹ <http://www.taxresearch.org.uk/Documents/IMFTaxingBanks.pdf> 9-3-10

² http://www.hmrc.gov.uk/stats/stamp_duty/table15-1.pdf 9-3-10

³ <http://www.stampoutpoverty.org/?lid=10738>

Today, the different components of the global FX market are built on the same technical platforms, use the same electronic messaging providers and trade electronically using the same systems. These trades are then settled through either the recently established Continuous Linked Settlement (CLS) Bank – which now settles around 75 per cent of all global FX transactions – or through the high value domestic settlement systems run by the world’s central banks.

At this ‘wholesale’ settlement level, the world’s domestic systems are linked to the CLS Bank and to each other. Trades are settled electronically and efficiently, producing real financial gains to international financial institutions, who certainly would not want to sacrifice these benefits. However, these benefits are conditional on participation in the relevant national and international settlement systems. It is this participation that makes a sterling CTT on wholesale transactions feasible today.

Sterling trades are ultimately settled either through the CLS Bank or the UK’s high value settlement system, CHAPS. The use of a common messaging provider – SWIFT – conveys significant cost savings to participants, but also enables records to be kept of all sterling transactions and allows these records to be cheaply and efficiently relayed to the UK’s tax collecting authorities. Given that banks trading in sterling hold central accounts at the Bank of England (for settling domestic transactions or for inputting to the CLS system) the sterling CTT, once identified, can be cost-effectively collected from these central accounts. In order to avoid market distortions, the proposal is to levy the sterling CTT at the rate of half of one basis point – 0.005 per cent.

This rate would have a minimal effect on spreads. A 0.005 per cent increase in the spread is well within normal market fluctuations - spreads of all the major currencies commonly fluctuate by 1 basis point, sometimes more. In recent years the overall trend has been for spreads to narrow (between 1986 and 2006 for example the \$/£ currency market spread decreased by 4.68 basis points), meaning a tax at this low rate would only increase spreads to levels seen a few years ago. Indeed we are confident that when other currencies also start to charge 0.005 per cent transaction taxes this could also easily be absorbed by the market.

About 7.5 per cent of the world’s currency trades are in sterling. That would imply that the total potential revenue from a Robin Hood Tax on UK currency trading should raise approximately \$4.9 bn a year, or more than £3.2 bn. Of course this is a small sum compared to the total potential revenues that Robin Hood Taxes might yield, but it would bring total UK revenues from them to more than £6 billion.

Countering the arguments against

Banks and finance houses have some of the most sophisticated and well-resourced lobbyists in the world. It is one reason why finance became so powerful before the crash. We are sure that they are lobbying hard against transaction taxes, but this is precisely because they are one of the most effective and surgical ways of taxing banks and institutions such as hedge funds.

There are two common arguments against transaction taxes.

How can we be sure that the Robin Hood Tax charges will not fall on consumers?

We argue that there is no need for any part of the Robin Hood Tax charge for which we argue to fall on consumers.

First of all, and perhaps rather obviously, this tax will never be charged directly to consumers. It will only be charged on bulk transactions in foreign exchange and complex financial products – largely conducted by banks, hedge funds and other institutions and certainly not by ordinary individuals. (Share dealing is a little different, but the UK already levies a stamp duty on such transactions and we are not calling for any changes in the Budget on stamp duty.)

Secondly, we argue that while banks and others could seek to pass on the cost of this tax to consumers this need not happen. Regulation could support this objective. Bank charges and rates to small businesses, individual customers and personal borrowers must be properly regulated to reflect the cost of providing those services, and not increased to cover costs incurred in other areas of bank operations. We suggest this regulation is streamlined with other bank regulation already under discussion. (See footnote⁴ for additional robust arguments that suggest changes in the market place would prevent the pass-through of costs.)

The finance sector is the most profitable on the planet. Before the crisis, bank profits were around \$800 billion a year, and were expected to double within ten years. According to a recent report by McKinsey, they make profits per employee of 26 times the average for all sectors. Not all banks are back to pre-crisis levels of profit, but recent results such as those posted by Barclays and other big banks show that recovery is well under way. As US economist Jeffrey Sachs said: "Wall Street has had the most profitable year in its history. It made profits of \$55bn (£37bn) in the midst of the biggest downturn since the Great Depression."⁵

But it is not just banks that will pay the tax. All institutions that buy and sell financial products on a significant scale and frequency will pay. This also includes hedge funds. Before the recession global hedge fund profits were running at \$300-\$600 billion profit a year.

Together banks and hedge funds were therefore making profits of around \$1,250 billion a year. And these are profits after the cost of unjustified bonus payouts to top staff. The kind of sums that experts estimate might be raised by a system of FTTs can easily be found from the profits of financial institutions and is not unreasonable – particularly given the moral duty on banks to help pay for the damage caused by a recession largely made in the finance sector.

Even to the extent they can pass on extra costs it will tend to fall on high net worth individuals who benefit from the financial transactions, not a regular user of high-street bank services. The Robin Hood Tax is a progressive tax that will largely be paid by banks, hedge funds and the like and after that by those who can most afford to pay an extra contribution.

⁴ <http://www.taxresearch.org.uk/Documents/IMFTaxingBanks.pdf> 9-3-10

⁵ <http://www.guardian.co.uk/business/2010/mar/09/jeffrey-sachs-robin-hood-tax>

What about the Robin Hood Tax reducing the liquidity in markets?

The argument of many who oppose Robin Hood Taxes is that they would reduce liquidity in financial markets. In this context liquidity is argued to be important because, in theory, if markets are sufficiently liquid no single transaction will be sufficiently significant to alter the price at which trades take place. The theory that significant liquidity of this type is optimal is, of course, based on the logic of the efficient market hypothesis, a theory that has now been questioned by the UK's Financial Services Authority, amongst others.

The reality is that theory and practice have clearly not coincided. The current exploitation of the euro in the face of problems within the Greek economy is clear indication that trades are being undertaken in large quantity with the explicit aim of moving prices whilst it is very obviously the case that the consequence of that movement in price is damaging to Greece and the whole population of Europe.

The problem in this case is not insufficient liquidity, it is an excess of liquidity that is causing the problem. Fewer trades, with marginal activity discouraged by the existence of Robin Hood Taxes would be of great benefit, and not a hindrance. The fact that some very significant groups within Europe and elsewhere are now arguing for certain products to be banned to reduce risk in financial markets is itself indication of this. Robin Hood Taxes would produce similar benefits in markets that would remain open.

It is our argument that the issue of liquidity is now historical. The basis of the argument is flawed. The reality is that Robin Hood Taxes would enhance the effectiveness of markets and not reduce them.

What is needed now

The Budget debate provides the opportunity for all political parties to show their support for the Robin Hood Tax, not just on an ideal international level but starting here and now in the UK with a unilateral sterling CTT.

Without new sources of government revenue, cuts will hit vital public services, poverty relief, prevent the world fulfilling the Millennium Development Goals and reduce funding available to tackle climate change.

The Robin Hood Tax can also be part of the policy response to the economic crisis by helping reduce irresponsible banking and putting pressure on bank bonus pay-outs. Unlike other proposals for tax increases such as a rise in VAT, the Robin Hood Tax is progressive and falls on those who not only can afford to pay it, but bear a large share of the responsibility for the downturn.

Robin Hood Taxes can deliver on these issues. Now is the time to commit the UK to such taxes.