FTT – Collection methods and data requirements

Specific Contract No3 TAXUD/2013/DE/314 based on Framework Contract No TAXUD/2012/CC/117

Final Report
EY - October 2014

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Abstract

This EY report (i) reviews the collection mechanisms of certain existing financial transaction taxes (FTTs), (ii) considers the challenges which EU FTT poses with regard to collection models and data requirements (iii) how and whether these challenges could be overcome, (iv) assesses the pros and cons of a range of theoretical collection models, and (iv) provides a view on what an overall collection approach might look like if an EU FTT is adopted as proposed by the European Commission in early 2013. The collection approaches considered have to deal with significant collection and enforcement challenges under the proposed EU FTT Directive which can be addressed to various degrees. There is no one clear path to follow, but considering decentralised and centralised approaches to collection, we believe that the latter are likely to be the preferred types at least for some asset classes, provided the challenges we have identified can be adequately overcome.
Centralisation could, in theory, be through:

- following the transactions themselves to the central points of transactions processing at CCP or CSD level;
- following the reporting of transaction to Trade Repositories or Authorised Reporting Mechanisms;
- a new utility (or utilities) if existing infrastructure cannot be leveraged successfully.

There are various functions which a central collection mechanism could perform in relation to collection, reporting and enforcement. The type of central model will, to a large extent, depend upon what functions it needs to perform and the capacity to overcome the commensurate data and other challenges.

Résumé

Ce rapport d'EY (i) examine les mécanismes de perception utilisés dans le cadre de certains impôts sur les transactions financières (TTF) existants, (ii) étudie les défis que pose la UE TTF en termes de modèles de perception, (iii) évalue les points positifs et négatifs d'une série de modèles de perception théoriques, et (iv) donne un aperçu de ce à quoi pourrait ressembler une approche de perception globale si une UE TTF est adoptée. Les mécanismes de perception envisagés soulèvent importants défis de recouvrement et d'exécution en matière de la directive UE TTF proposée qui peuvent être adressées à des degrés divers. Il n'y a pas un seul chemin à suivre, mais comparant les approches décentralisées et centralisées de perception, nous croyons que les dernières sont à préférer au moins pour certaines classes d'actifs, à condition que les défis que nous avons identifiés peuvent être surmontés de manière adéquate.
La centralisation peut, en théorie, s'effectuer :

- Soit par le suivi des transactions elles-mêmes jusqu'au point central de traitement de ces transactions au niveau du *CCP* ou du *CSD* ;
- Soit par le suivi des déclarations de ces transactions aux référentiels centraux (« *Trade Repositories* ») ou aux mécanismes certifiés d'établissement des déclarations (« Authorised Reporting Mechanism ») ;
- Soit par la création d'un nouvel instrument (ou de plusieurs) si l'infrastructure existante ne peut être utilisée avec succès.

Un mécanisme de perception centralisé peut accomplir de multiples tâches en lien avec la perception, la déclaration ou la mise en œuvre de l'impôt. Le type de modèle centralisé dépendra, dans une large mesure, des fonctions qu'il lui sera nécessaire de réaliser et de sa capacité à traiter les données appropriées et toute autre difficulté rencontrée.

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1. Executive Summary

The proposed harmonised European framework for a set of national financial transaction taxes ('EU FTT') is significantly more ambitious than any other existing tax regime for financial transactions, in particular with regard to the wide instrument scope and geographic reach. Commensurate with that ambition, the challenges of collecting the tax are similarly unprecedented.

In this report we have considered the current collection mechanisms for a number of current transaction taxes. None of these systems provide a comprehensive solution which should be replicated for EU FTT collection. However, they do have features which could be incorporated into an EU FTT collection system.

Whilst the Participating Member States ('PMS') that are negotiating EU FTT have many variables which are controllable, much of the difficulty in collection stems from uncontrollable factors, namely the complexity of dynamic financial markets and the evolving complex global regulatory environment.

These features present an inherently difficult environment over which to impose EU FTT collection. In order to maximise the chances of implementing an efficient and effective collection system, PMS would, in our view, need to address certain aspects of the primary rules, irrespective of the collection system. The key is to ensure the primary rules are simple and capable of automatic processing, the collection procedures are clear and the burden of compliance is reduced as far as possible by using pre existing data and processes.

In this report we consider a range of collection systems. At one extreme we consider taxpaying Financial Institutions ('FI') calculating, paying and reporting their own EU FTT liability. We then consider a potential system under which they could delegate tax payment and reporting to other FIs, typically those that intermediate in the chain between buyer and seller. We also consider tax collection at a central level. The direction of travel for most asset classes is to have mandated central places where trading occurs, (e.g. trading venuesin the EU) and for those trades to then be novated to Central Counterparties ('CCPs')) to centrally assume counterparty risk and then for legal ownership to be transferred at Central Securities Depositaries ('CSD'). Underpinning all this is transparency of each trade to the regulatory bodies through legislation like MiFID (for equities), EMIR (derivatives) and from 2016 MiFID II (a wide range of financial transactions).

Aligning EU FTT tax collection to this drive towards market centralisation provides PMS with an opportunity to exhibit a degree of control over tax collection which might otherwise be very difficult to assert. Market participants also are likely in many cases to benefit from centralisation if it is designed in such a way as to increase efficiency and reduce risk. Euroclear UK and Ireland's CSD central system (i.e. CREST) for collecting the UK's Stamp Duty Reserve Tax ('SDRT') is a central system which is effective and well regarded by HMRC and market participants alike.

This report considers, but does not conclude, upon the most desirable form of centralisation. It does, though raise the key question of what kind of functionality should a central collecting agent have? At one extreme it could merely be a postbox to send tax receipts to PMS; at the other it could have the capacity to check tax calculations, reconcile and match data between market participants and have resources to promote standardisation of market practice. Depending upon the answer to this question, the most likely candidates to operate central collection functions

could be CCPs/CSDs where transactions are currently processed with limited underlying data on a net basis with regard to only certain types of transaction, or a trade repository where daily transaction data is housed across a wide range of transaction types. In short, should the EU FTT collection follow the transaction processing or the reporting of the transaction? The transaction processing route would tend to be preferable for a simpler tax where minimum central functionality is all that needed (rather like SDRT and CREST). Alternatively, a more complex tax requiring higher central functionality may indicate leveraging data repositories where gross data is housed and could be used. We recognise that since data repositories do not process transactions, requiring them to use the data to provide an EU FTT collection function is a totally new role for them. Centralisation of collection also puts EU FTT at the heart of a domain where regulation and regulators are in charge.

Any type of central EU FTT collection would need close co-operation with EU regulatory bodies. The collection approaches considered have to deal with significant collection and enforcement challenges under the proposed EU FTT Directive which can be addressed to various degrees. The challenges are listed in our report as are some potential remedies on how to overcome these challenges. There is no one clear path to follow, but considering decentralised and centralised approaches to collection, we believe that the latter are likely to be the preferred types at least for some asset classes, provided the challenges we have identified can be adequately overcome.

Given the limited data available to base our conclusion on, we have been unable to quantify the likely costs to build or operate any of the collection systems. We have, though, indicated the likely relative costs of the models and indicated where cost is most likely to be incurred. EU FTT is likely to be more costly to operate than most local transactions taxes. It is clear to us that central collection models will be incrementally more costly to build since they are likely to overlay systems and processes which most individual FI would need to build in any event. It is possible that these additional costs are justified by the benefits which centralisation potentially affords, but we cannot be certain of that. So the cost issue remains an important uncertainty and challenge.

Beyond that, there are major challenges particularly in the area of data and in the area of global tax collection where PMS currently have limited tools to enforce compliance. The data challenge could be addressed to some extent by further alignment to regulatory reporting and the geographic challenge can to some extent be addressed by at least making tax collection accessible for non PMS FI's. If PMS can agree upon an EU FTT we do believe that nothwithstanding that matters of tax collection are generally derogated to Member States, tax collection should be harmonized as much as possible and this is likely to give rise to benefits for PMS and FIs alike.

Whilst this report is far from being a detailed roadmap on EU FTT tax collection, we do hope it provides a useful structure for Member State discussions and a basis for them to consider what detailed further work is necessary in this important area.

2. Methodology and assumptions

2.1 Methodology

This report has been prepared for the EU Commission. Under EU principles, matters of tax collection are – in the first instance – the responsibility of the Member States. However, it has been made clear through discussions in the relevant Council working group that a harmonised approach to collection would be desirable. The Explanatory Memorandum to the proposed EU FTT Directive holds that the methods applied by the participating Member States for the collection of the EU FTT due should be uniform, to the extent necessary to avoid complications in the collection of the tax through differing collection methods and ensuing unnecessary compliance costs.[1]

The scope of this independent report is purely about the basics of tax collection: EY has not been asked to consider the efficacy of the EU FTT policy and policy objectives.

Our methodology has required us:

- to analyse the design and performance of existing collection systems using experience of EY tax professionals in each selected jurisdiction, supplemented by publicly available information,
- to consider the range of issues that EU FTT collection presents by using EY specialists in the field of tax, law, operations, IT, regulation and market business models, and:
- to consult, informally, with FIs across the spectrum of banking, broking, asset management, insurance and infrastructure in order to supplement and refine our analysis.

Discussions have been held with market participants inside the EU FTT zone, in the wider EU and outside the EU. Market participants have informally contributed to our study on the basis that their input should not be seen as implicit or explicit support of EU FTT.

Due to the scope and agreed methodology of our study, our analysis is not generally supported by underlying quantitative analysis or empirical data. As a consequence, the report should not be seen as a basis for definitive policy conclusions.

2.2 Assumptions

Our work reflects a number of assumptions and caveats. In particular, we were asked by the Commission to assume the following and have not challenged these assumptions:

[1] Proposal for a Directive concerning the implementation of enhanced cooperation in the area of financial transaction tax, COM (2013) 71 final, p.13.

- an EU FTT Directive will be adopted as proposed by the Commission in February 2013;[2] However, upon the Commission's request, one amendment has been taken into account, as we have been asked us to assume that the proposed EU FTT Directive will not require payment on the transaction date but on the settlement date;

- there is no deliberate non-compliance;

- there are no behavioural effects (such as relocation of activity or substitution between financial products) which adversely affect collection of EU FTT;

- the focus of the study should be on primary EU FTT liability rather than on potential Joint and Several Liability (JSL) in the event that the primary liability is unpaid.

[2] The proposed Directive, very briefly, seeks to tax derivatives (of all kinds) at 1 basis point on inception, and secondary market transactions in all types of securities at 10 basis points. Rates could vary between PMSs. The broad scope means that transactions like repos, stock loans, collateral transactions, derivative variations are often taxable. Each legal entity is a taxable person for FTT purposes if they are classified as an FI, this would include banks, asset managers, insurance companies, all types of funds including UCITS funds and retirement plans. Taxable parties to transactions include buyer, seller and intermediary - i.e. all parties are taxed, although there is a limited exemption where one FI is acting on behalf of another FI. FIs are taxed on a global basis with regard to transactions based on a complex waterfall test taking into account factors such as country of regulatory authorisation, country of establishment of the FI, residence of the counterparty and place of issuance of the instrument. Transactions are taxed on a gross basis, at the time they are entered into. There are no exemptions for intragroup transactions. These factors, amongst others, mean that the EU FTT is very different from other existing national FTTs.

3. Review of selected national FTTs from a collection and compliance viewpoint

This section reviews existing FTTs in five selected countries – Belgium, France, Italy, Switzerland and the UK – from the perspective of their collection methods both in design and in practice. It relies on publicly available information, the extent of which differs from country to country.

National FTTs are significantly different in design to the proposed EU FTT, in particular in terms of the geographical scope or breadth of in-scope instruments. Also, these taxes do not require daily tax payments (monthly in Italy and France). In addition, they have wider market making/intermediary exemptions than the proposed EU FTT Directive and levy tax either on a residence or an issuance basis.

Three of the selected FTTs – in Belgium, Switzerland and the UK (SDRT) – are mature and operate with low compliance costs for taxpayers and infrastructure, with the Swiss and UK FTTs also proving to be cost efficient from a tax authority perspective. The maturity of these taxes, clarity of the rules, integration of collection into market participants' trading and settlement systems and a collaborative approach on the part of the tax authorities to developing guidance and operating procedures all appear to have contributed to this.

Recently introduced FTTs – in France (FFTT) and Italy (IFTT) – have imposed significant compliance costs on taxpayers and market infrastructure, with as yet uncertain success for the tax authorities in terms of revenues collected and administrative costs. Some systems, e.g. Belgium (TOB), are considered to have scored well in terms of effectiveness because of the simplicity of their design. Although both FFTT and IFTT follow the SDRT model of also involving the Central Securities Depository (CSD) in collection and reporting processes (in addition to direct payment and reporting), this interface is as yet insufficiently integrated to deliver the advantages experienced by the UK tax authority. Collection difficulties and costs have been exacerbated by complexity and a lack of clarity in the primary rules. Particular difficulties have been encountered by the Italian authorities with regard to IFTT on equity derivatives, especially since such contracts are not generally taxed on a transaction by transaction basis by other national FTTs and therefore there has been little experience to learn from.

An overview of key features of some existing national FTTs (Belgium, France, Italy, Switzerland and United Kingdom) can be found in Appendix 1. The remainder of this section reviews the collection and compliance aspects of each of these five national FTTs in turn, from the perspective of taxpayers, infrastructure operators and tax authorities.

3.1 Belgium

Background

Belgian FTT (Taxe sur les Operations Boursières ("TOB") is levied on the sale and purchase of 'publicly' tradable securities and in some instances on repurchases of accumulating shares of certain corporate investment funds. The rates vary between 0,09% and 0,25% (a capped amount per transaction applies).

The TOB's distinguishing features are that both the purchaser and seller are liable and that the first financial professional intermediary, if Belgian, is accountable for paying the tax.

There are a number of exemptions from the TOB but the key element of its (limited) scope is that - in practice – transactions not involving Belgian professional intermediaries that are not executed in Belgium are not liable.

An average of €130m per annum from 2008 to 2012 was collected from self-assessment by the financial intermediaries, estimated to represent about 0.2% of Belgian total tax revenue and 0.05% of Belgian GDP.

Appendix 1 sets out in more detail the scope and key features of the Belgian FTT.

Taxpayer perspective (how easy to collect/comply)

Collection costs are estimated to be low, as the tax is levied by self-assessment, and only 100 or so FIs are required to file the monthly tax return. Transactions are often carried out online so the banks' accounting systems can calculate automatically how much is due, further lowering compliance costs.

An amendment to the current scope of the law has been proposed, to tax transactions executed outside Belgium for the account of Belgian residents (documents of the Parliament, 53 K 1564/001). This proposal is still pending two years after it was lodged.

Available exemptions are detailed in the relevant section of the summary overview included in Appendix 1 to this report.

Infrastructure perspective (how easy to operate, what incentives to operate)

The Belgian FTT does not place obligations on infrastructure providers.

Tax authority perspective (what it does to enforce collection)

The tax authorities process monthly returns and selectively audit those judged to have a high risk of non-compliance.

During the second half of 2012, the Belgian tax authorities introduced initiatives to increase its FTT audit activity in relation to certain derivative and non-traditional financial instruments (e.g. trackers, boosters). This was in the face of a market perception that such instruments were not being treated consistently for Belgian FTT purposes (some financial intermediaries applying exemption, others levying FTT). The increased audit activity, however, led to criticism from Belgian FIs and the industry association and appears now to have been scaled back.

There are inherent risks in relation to collection and the model which underlies the collection of the Belgian FTT. No restrictions on foreign settlement providers exist. Belgian debt securities enjoy a beneficial transaction tax treatment compared with foreign debt securities. Non-resident holders have numerous exemptions not available to Belgian holders.

Use of a Belgian intermediary may in some cases trigger the application of transaction tax, whereas no such tax would apply if a foreign intermediary were used[3].

3.2 France

Background

The French Financial Transaction Tax ("FFTT") is due on the transfer of the legal ownership of listed equities of large companies established in France (including similar instruments and depository receipts provided that the underlying securities are French equities), on cancelled high frequency trading orders where trading is carried out in France and on credit default swaps on sovereign debt. There are a number of exemptions, for example derivatives are out of scope and there is a market-making exemption for financial intermediaries (see Appendix 1 for more details). Approximately €702m in 2014 was collected. The tax is collected via an executing broker, if present, or via the custodian, if not. Appendix 1 sets out in more detail the scope and key features of the FFTT.

Taxpayer perspective (how easy to collect/comply)

The French FTT reporting model is complex. Depending on where each transaction settles, the reporting "route" (i.e., the person liable to the reporting and the person to whom the reporting should be made) may be different. It may also be that the person liable to the tax is different from the person liable for collection and reporting. From a practical point of view, this means that each entity executing in-scope transactions has needed to put in place processes to identify the accounts in which each transaction settles, in order to determine whether it is responsible for the reporting and, if so, what it should report and to whom. In practice, this is far from straightforward.

The volume of information to be reported is significant, for instance, even exempt transactions have to be reported).

FFTT legislation provides for nine exemptions. See Appendix 1 to this report.

Several entities responsible for reporting transactions have encountered issues retrieving required reporting information in cases where they were not involved in transactions. This is notably the case where the person responsible for the reporting is a client of a Euroclear member, and is not the taxpayer in the transaction (Euroclear France is the CSD for French equities). From a practical standpoint, this kind of situation has been dealt with through contractual arrangements for the transmission of the relevant information, which has led to additional costs and complexity for market players.

[3] See advance tax ruling n° 400.180 d.d. 17 March 2005.

The deadline set to comply with FFTT regulations was regarded as particularly short by market players, with the law on FFTT published in March 2012 and entry into force on 1 August 2012 (i.e., less than a five month deadline). Market players are still in the process of implementation. Administrative guidelines on the practical application of the tax were not published until mid-August 2012, after the entry into force of the tax.

In addition, there are outstanding concerns around the clarity of primary liability rules, such as the identification of transactions in scope (especially regarding non-French instruments, such as depository receipts), issues with best practice guidelines, intraday versus deferred settlement transactions, as well as difficulties in the application of the market-maker exemption and in the identification of the taxpayer in case of executing chains of transactions

Infrastructure perspective (how easy to operate, what incentives to operate)

The law on FFTT provides specific reporting obligations and liabilities for the Central Securities Depository (CSD), i.e. Euroclear France. First, the CSD must collect the tax and the reporting data from its members and pay the tax to the French tax authorities. In addition, it has to identify and report specific taxpayers. A monthly reporting requirement assists the French Administration in the monitoring of enforcement and compliance. However, this adds to the administrative burden that the tax represents to the CSD. The compilation of such reports involves significant IT input by the CSD and taxpayers, since it has to transform raw reporting data from taxpayers into operational information to be transmitted to the tax authorities.

Tax authority perspective (what it does to enforce collection)

According to the French tax authorities, FFTT revenues have been lower than expected. The French government expected €1.6bn of revenue for 2013, with only €690m collected. Estimated revenues for 2014 are €702m. The majority of the revenues are understood to have come from non-French taxpayers. However, enforcement of the tax outside France has been met with varying levels of success, given the challenges of collection presented in territories where there is no jurisdiction to audit.

3.3 Italy

Background

The IFTT is due on the transfer of legal ownership of shares (listed and non-listed), similar instruments, depository receipts provided that the underlying securities are Italian equity and equity derivatives of a company resident in Italy. There are a number of exemptions, for example on certain defined market-making activities for financial intermediaries (see Appendix 1 for more details). Approximately €159m of IFTT was collected in 2013, generally collected via the financial intermediary closest to the client or directly from the purchaser if no FI is present. Appendix 1 sets out in more detail the scope and key features of the IFTT.

Taxpayer perspective (how easy to collect/comply)

Registration compliance is a particular issue for IFTT. The reporting system appears to be costly to implement, particularly in setting up and implementing the IFTT Register.

The current wording of the IFTT law does not consider a number of common scenarios encountered by financial intermediaries, and with no specific guidelines issued, compliance has been seen as burdensome. Lack of guidelines has made it especially difficult to apply the market-maker exemption in the case of derivatives.

In some cases, foreign taxpayers do not understand whether the IFTT legislation overrides their domestic legislation, for example in the case of provisions for gifts/inheritance. Taxpayers are also faced with difficulties for high frequency trading "HFT" IFTT calculations, due to lack of official guidelines on best practice.

Although equity transactions liable for the FTT are similar under the Italian and French systems, the rate varies markedly between OTC and on-exchange transactions.

The market-maker exemption is applied for IFTT on a transaction basis, rather than by status, therefore increasing complexities for companies to remain compliant. Other applicable exemptions are detailed in the relevant section of the summary overview included in Appendix 1 to this report.

For counterparties located in a 'black listed' country, issues remain on identification of the liable party, double payment of taxes, netting and reporting obligations.

Infrastructure perspective (how easy to operate, what incentives to operate)

Both residents and non-residents with a bank account in Italy pay IFTT by completing an F24 form using an appropriate 4 digit tax code, i.e. equity, derivatives or HFT codes and Tax Identification Number ('TIN') allotted by the Italian Revenue Agency to the intermediary. Where an intermediary does not have a bank account in Italy, IFTT is paid via bank transfer quoting separate IBAN for Equity, Derivative and HFT IFTT, TIN, tax payment codes and the reference period.

Separate codes for interest and penalties are provided for late or omitted payment. Although all the tax codes can be found on the website of the Italian Revenue Agency, this represents an added layer of complexity to the operation of the tax.

Persons obliged to pay the tax can apply to the Italian Central Depository for the purposes of calculating and paying IFTT and dealing with the relevant reporting requirements. Alternatively, IFTT obligations can also be met through an Italian permanent establishment (if any), through an appointed tax representative (where there is no permanent establishment in Italy), or directly by the foreign person. To ease operation, the Italian Revenue Agency recently released the annual IFTT return and its software. The annual return instructions confirm that the filing deadline is 31 March 2014 for transactions occurred in the period March – December 2013 for Equity IFTT and HFT IFTT and September – December 2013 for Derivative IFTT.

Tax authority perspective (what it does to enforce collection)

According to October 2013 figures published by the Italian Ministry of Finance ("MOF"), revenues raised from the Equity and HFT IFTT for the period March – September 2013 and for Derivative IFTT for September 2013 amounted to €159m. This is significantly lower than the expected amount of annual revenue of €1bn, and it appears unlikely that this forecast will be met.

On 8 August 2013, MOF released a document containing responses to the certain questions asked by the Industry groups in connection with Equity IFTT ("FAQ 1"), an

unofficial English translation of which was published by MOF on 22 August 2013 on its website.

On 27 August 2013 MOF released a document containing responses to specific questions asked by the Industry groups about Derivative IFTT ("FAQ 2"), an unofficial English translation of which was published by MOF on 2 September 2013 on its website.

Both these documents clarify, and provide specific examples of, cases where exemptions/exclusions apply.

3.4 Switzerland

Background

Swiss FTT is due on the legal transfer of ownership of equities and bonds if one of the parties is a Swiss securities dealer. There are a number of exemptions, for example proprietary trading by professional brokers and all derivative trading instruments (see Appendix 1 for more details). CHF 1,107m of Swiss FTT was collected in 2012 and is collected by securities dealers on behalf of both of the purchaser and the seller who are both liable. Appendix 1 sets out in more detail the scope and key features of the Swiss FTT.

Taxpayer perspective (how easy to collect/comply)

The Swiss stamp tax is regarded as having low compliance and administrative costs for taxpayers, and high compliance rates, although no precise estimates of compliance costs are available.

Compliance costs are also said to be low because dealers integrate the calculation of the tax into their internal accounting systems. Moreover, there are built-in mechanisms to encourage compliance. Dealers collect the tax, simplifying administration by eliminating the need for individual end-users to do this. All securities dealers are required to register with the tax agency, regardless of status. Moreover, there is an incentive to register, as this is a pre-requisite for dealer exemption for purchases intended for their own trading portfolio. Other exemptions are detailed in the relevant section of Appendix 1. Dealers are also required to maintain a transactions register. This simplifies the tax assessment and verification in general. As administrative procedures have been designed collaboratively, building this around banks' internal systems and procedures, this has also reduced taxpayers' errors and created a trusting relationship with taxpayers.

The Swiss authorities have put measures in place to tackle non-disclosure of security dealer status, for instance, bank/broker liability in the case of non-disclosure. The securities dealers are still required to register all transactions and remit transfer taxes on trades closed between themselves and other parties, for example if pension funds trade securities directly without the support of a broker.

One area of uncertainty on the taxpayer's side relates to situations where a Swiss branch of a foreign bank is a securities trader in Switzerland. Building on a court decision of the early 80's, these branches claimed to have been mere remittance offices relaying client orders to their head offices. Therefore, they claimed not to have

been traders or brokers. This has been challenged by the tax authorities for a number of years, resulting in considerable back taxes.

Infrastructure perspective (how easy to operate, what incentives to operate)

The Swiss FTT does not place obligations on infrastructure providers as the onus to calculate and remit taxes is on the securities dealer only.

Tax authorities' perspective (what they do to enforce collection)

Swiss FTT is a transactional tax which will is due even if the taxpayers (banks and brokers) have no income tax liability (for example due to losses brought forward). Hence, the revenue authorities have put considerably more scrutiny on stamp tax audits than before.

Administrative costs to the tax authorities are believed to be low, in part, because the small number of registered dealers (about 400) requires only a small number of tax officers (about 10) to administer the tax. Moreover, Swiss tax authorities only audit Swiss securities dealers every five years (due to the Swiss limitation period). Shorter audit cycles may be applied in case of previous errors or misconduct on the taxpayer's side. However, the authorities are becoming stricter especially with regard to structures basically set-up to optimise Swiss FTT (e.g. insertion of exempt investors such as funds).

3.5 United Kingdom

Background

UK Stamp Duty Reserve Tax is a tax of ½% of transfers of chargeable securities. It is payable by the purchaser, and financial intermediaries can qualify for wider exemption. It has typically raised in excess of £2.0bn per annum.

Taxpayers (how easy to operate, what incentives to operate)

SDRT is a mature tax (almost 30 years old) so the fundamental principles are settled and generally well-known. There is a large volume of guidance available both from HMRC and Euroclear UK & Ireland (as operators of CREST) to assist taxpayers and accountable persons (such as brokers, custodians and other financial intermediaries). It continues to develop in line with market practice, for instance, it recently developed a new solution for handling the increasing market practice of net settlement (SDAS, cfr. Section 7).

The "accountable person" (typically a broker, custodian or other financial intermediary acting for the purchaser or, in some cases, the seller) is required to give notice and pay the tax to HMRC. For transfers effected in CREST, a comprehensive system of data inputs is used to provide the required reporting information directly to HMRC. Typically market participants will have configured their internal trading and settlement systems architecture to produce and send to CREST automatically in most cases the required reporting information.

For transfers effected outside CREST (including off-market trades in unlisted securities or trades in listed securities which are not settled through CREST such as M&A activity), manual reports and payments must be made to HMRC giving details including the identities of the parties, the agreement date, the security, the number sold, the price paid and details of any alleged exemption. Although more time-consuming than reporting and paying through CREST, the manual reporting and payment process is generally well-understood and is straightforward.

There are built-in mechanisms to encourage compliance. Penalties and interest will be payable if SDRT is not reported correctly and paid by the required date ('accountable date'). CREST helps to reduce administration costs, minimising the scope for under-reporting, compared to a system of manual reporting and payment of self-assessed tax liabilities.

There are a number of reliefs which are important in the context of capital markets transactions. Please refer to the relevant section of the summary overview included in Appendix 1 to this report.

Infrastructure (how easy to operate, what incentives to operate)

For transfers effected in CREST, the settlement instruction will include a number of data inputs relevant to the collection and reporting of SDRT, including:

- the parties' identities,
- security description, volume and price,
- agency status (identifying whether party buys or sell as principal or agent),
- "Transaction Stamp Status" (an alphanumeric flag indicating the applicable rate or alleging an exemption), and
- "Trade System of Origin" (a flag indicating on which market or exchange, if any, the trade was made or reported).

Since market participants will use CREST to settle transactions in UK securities generally and since those participants will also have configured their internal trading and settlement systems architecture to generate the SDRT relevant data inputs automatically wherever possible, use of CREST to report and pay SDRT as part of the overall settlement process is inherently encouraged.

Tax authority (what it does to enforce collection)

From HMRC's perspective, SDRT is very efficient and cheap to collect through the CREST system. Due to being able to leverage existing market institutions, infrastructure and technologies, HMRC has kept its SDRT administration costs very low - 0.21p per £ collected in 2008 for SDRT and stamp duty combined (HMRC, 2009). However, typically this cost is reported to be about 0.1% of revenue collected. Of around 100 FTE employees at the stamp office approximately only 20 cover SDRT.

Table UK stamp duty reserve tax cost per £ collected

Period	Cost per £ collected
2008 (¥)	0.21p
2007 (¥)	0.12p
2001 (†)	0.9p

Source: ¥ HMRC (2009); † IFS (2002)

Table UK stamp duty reserve tax cost per transaction

Period	Transactions per year (nearest million)	Total Cost	Cost per transaction
July 2012 – June 2013	399 m	£ 24.0 m	0.6p
Apr 2012 – Mar 2013	391 m	£ 23.4 m	0.6p
Apr 2011 – Mar 2012	438 m	£ 21.9 m	0.5p

Source: Transactions explorer (2013)

Collecting tax through a CSD like CREST offers important advantages for tax administration by lowering compliance costs for taxpayers, lowering administrative costs for the tax agency, and reducing the scope for under-reporting tax compared to the case if broker-dealers were required to self-assess the tax liability and make manual reports and payments in all cases.

4. Challenges to the collection of EU FTT

In line with the structure of the study as per the Commission's request, we will first identify and list the collection challenges in relation to EU FTT as currently proposed.

In subsequent chapters of this report, we consider various types of collection models and whether and to what extent those models can overcome these challenges. We also indicate what possible solutions are available.

The challenges below have been grouped into four categories which, in our view, correspond to the main criteria for effective tax collection, in case of EU FTT:

- the clear determination of EU FTT liability, including five challenges (i.e. C1 to C6),
- the effective remittance of the tax, including three challenges (i.e. C7 to C9), and
- the support for compliance and enforcement (by tax authorities), including five challenges (i.e. C10 to C14)
- the need for any EU FTT collection model to be cost-efficient to introduce and operate (C15)

Although these challenges are applicable to the collection of any tax, both the cost challenge (given the scale and reach of the proposed EU FTT) and the compliance and enforcement challenge (given the global scope of the proposed tax requiring collection outside the EU FTT zone) are of particular relevance. .

4.1 Clear determination of EU FTT Liability

Potentially unclear primary rules (C1)

As with any tax, collection of EU FTT presupposes a correct determination of the liability. Whatever the final outcome of PMS negotiations, the rules should be as clear as possible.

For a financial transaction tax, in particular, this means that tax liability determination rules must allow for:

- systematic processing, i.e., inclusion in automated flagging processes and/or rules engines;
- straightforward non-fact specific application.

Recent experience of implementation of French and Italian FTT has shown that, where rules are not clear, this can have significant effects both on market transactions and on collection itself. For example, as a consequence of Italian FTT, markets have been disrupted due to a lack of clarity on counterparty status, such as where a broker/dealer headquartered in a black-listed country executes Italian cash equity transactions through a white list country branch. Also the primary rules have not been clear as to what the "on exchange" rate is in some circumstances. The complexity of

the rules and uncertainty around their application carries a risk in the context of EU FTT given the potential for PMS to apply different interpretations of the same rules – both with regard to substantive liability and with regard to collection and enforcement.

The EU FTT has many unique design features and it is being applied to a vary complex and dynamic tax base. Given this, it can be expected that existing tax law precedent will have limited value in these circumstances. This further underscores the need for clear rules.

Certain proposed EU FTT rules inhibit automation (C2)

There are some examples throughout the proposed Directive of rules which are not capable of automatic processing. As well as the need for clear primary liability rules, rules need to be capable of automatic processing by computer systems using prescribed logic and drawing upon static data. An example of a provision in the proposed Directive which is incapable of automatic processing is the economic link test (article 4(3)). This exempts EU FTT where it can be shown there is no economic link to a PMS. This test has been the subject of clarification questions posed to the Commission by Member States. The clarification given by the Commission appears to suggest this relief will be highly limited and subject, in essence, to a facts and circumstances test.

From an operational point of view, just as with anti-avoidance measures (for example the anti-avoidance provisions of articles 13 and 14 of the proposed EU FTT Directive), rules that require fact specific tests (weighting up facts and circumstances)cannot be reduced to algorithms and decision trees. Leading to uncertainty in primary rules, such elements do not facilitate accurate compliance on a daily basis as well as automatic processing.

Data challenges (C3)

The proposed Directive requires significant information in order to calculate EU FTT. In summary, there are at least three new sources of data that would need to be obtained for EU FTT, namely:

- data on EU FTT zone instrument issuance,
- data on EU FTT counterparties, and
- information on how each executed trade of an FI is to be treated for EU FTT purposes (for example, the applicability of intermediary relief).

In addition to these new data requirements there are more generic issues which relate to data, namely:

- data protection, and
- netting.

Typically, large FIs have a complex systems architecture made up of many legacy systems that interact in a sub-optimal way. The data challenge the industry is facing is

already increasing as regulators require more and better quality data (for instance the Basel Committee on Banking Supervision is requiring significant improvements in risk data). The additional data requirements posed by EU FTT should be seen against this backdrop. Depending on the final design of EU FTT, IT changes could well be needed for hundreds of systems for a typical large FI.

Automated transaction processing works by applying well-defined rules to transaction data and reference data, in order to calculate liability and initiate payment instructions. EU FTT would require the following reference data to be available:

- An "EU issuance" database. This would require identification of securities treated as issued in the EU FTT zone. There are several existing reference data identifiers for security identification, the globally most recognised being CUSIP and ISIN, in addition to instrument data supplied by national numbering agencies (NNAs), by exchanges and by recognised data vendors such as Thomson-Reuters or Bloomberg in each country. However, such services do not automatically identify EU FTT issuance and there are also additional challenges. For example, there are mapping issues because NNA codes do not always correlate ISIN codes, and there are sometimes intellectual property issues to consider. Either existing databases would need to be adapted to include EU FTT zone issuance details, or an entirely new database would need to be built. Although such services currently do have an element of geographical identification, this is often based on the place a security is "listed" which is not necessarily where it has been "issued".

- A trade taxonomy database. Identification of whether a financial transaction is in scope and at what rate is fundamental to collection. The definition of in-scope transactions is largely drawn from EU financial regulation. This is helpful, especially since, after the introduction of MiFID II and MAD II from the second quarter of 2016, many daily transactions will require reporting and therefore FIs will have to expand transaction reporting to identify some of the transactions which are in-scope transactions for regulatory purposes. In this respect, EU FIs will be organising their product data in a way which facilitates EU FTT compliance. However EU FTT has a broader scope than required even under full implementation of the pipeline of current EU legislation and EU legislative proposals, for instance intragroup transactions, repos, collateral etc. In the case of securities lending, the EU has only recently proposed transaction reporting. EU FTT zone countries' FIs will need to build reference databases for in-scope transactions solely for EU FTT purposes. Where there are gaps between tax reporting and regulatory reporting, this will make it more difficult for PMSs' tax authorities to use regulatory data to cross check tax receipts against the data provided to the regulator.

  Outside the EU, this "trade taxonomy" data challenge will be much greater. FIs that are not subject to EU reporting will need to establish whether the transactions they are undertaking are of the nature described by the appropriate EU FTT (MiFID) definition, even though they would not need to apply these definitions for other purposes. FIs typically have a taxonomy of products which is several hundred items long, and each product would need to be coded for its status under the Directive as either exempt, chargeable to the lower rate for derivatives or chargeable to the higher rate for secondary market transactions. Although the correct categorisation will be straightforward for the majority of cases, it will represent a major task,

especially for those institutions that are only within the scope of the tax due to the counterparty principle.

This trade taxonomy database will be needed for each firm to identify the capacity in which the taxpayer itself is acting (the capacity of the counterparty might be separately sourced from an FTT counterparty database). This information needs to be identified for each transaction, i.e. whether a person is acting on its own account, in its own name but for the account of another person (undisclosed agent) or acting in the name of a party to the transaction (disclosed agent). So, FIs would need to assess, across all markets and asset classes, how their commercial and contractual relationships are to be viewed under EU FTT. Establishing themselves as counterparties will be relatively easy, but trying to understand how they might be regarded as acting on their own account or for someone else's will be a harder task. Once such judgements have been made, each type of trade will need to be flagged within the system for the right EU FTT designation.[4] The trade taxonomy database would also need to hold reference data of EU FTT exempt transaction types. Articles 3(2) and (4) of the EU FTT proposal provide exemptions for particular categories of entity and transactions respectively, for which further reference data would need to be available.

- An EU FTT FI counterparty database. There is currently a global initiative to provide a unique reference number for all FIs: the Legal Entity Identifier project. Under EMIR, entity codes are also being issued for derivative counterparties and we understand one million such codes need to be issued. Whilst MiFID requires counterparties to be identified, it does not go so far as mandating legal entity identifiers. However, it is anticipated that MiFID II will increase the level of legal entity information needed for reporting. Counterparty verification is important for a number of core processes which FIs undertake, for example, for Anti Money Laundering under the forthcoming fourth Money Laundering Directive (MLD IV), FATCA, credit risk assessment, etc. Ultimately the Legal Entity Identifier project may provide a global reference database which will assist in many of these processes. However, the unique codes issued will not provide any information on whether the counterparty is an EU FTT zone party or not and unless this global initiative can be aligned to FTT requirements, FIs themselves will need to assess their principals' and counterparties' status for FTT purposes and indeed the status of all their entities and branches, often running to thousands for the largest banks. PMSs could simplify this task by producing a list of entities which are FIs established in their territory. This currently does not exist and will be a major exercise to build and maintain. However, this will only enable FIs to be identified, whereas FTT liability is due on transactions with all legal persons (including individuals) that are residents of EU FTT zone countries. Given this, each FI will really need to re-paper its

[4] There is therefore further information which non-EU11 FIs will need to obtain about their counterparties (including principals under agency contracts) in order to determine their own FTT liability. This relates specifically to the place of deemed establishment of the counterparty for FTT purposes (Article 4(1)(f) of the EU FTT proposal). It is not practical to place the onus on a non-EU11 FI to obtain this information in relation to its counterparty (particularly as in many cases the FI would be seeking to prove a negative). Therefore PMS's would need to ensure the counterparty principle is practical from a collection perspective, it would need to be accompanied by a requirement on PMS-established persons in relation to a particular transaction to notify their counterparty of their PMS-established status and that, in the absence of such notification there would be no liability on a non-PMS FI.

entire customer reference system in order to capture the full scope of its EU FTT liability.

- The EU FTT counterparty question is further complicated by the "waterfall" test for EU FTT establishment. Under the Directive, FIs become "established" in the EU FTT zone following a complex "waterfall" test, commencing with authorisation as the initial test, followed by a more traditional test of registered seat etc. Current regulatory reporting does not require the identification of the authorisation status of the counterparty or the branch through which the transactions are carried out. However, this information is relevant in determining whether there is any liability and to which PMS (which could potentially affect the rate of EU FTT due).

Even where there are sources of data which seem broadly comparable to the data required for EU FTT, the operational challenge of reconfiguring that data to precisely meet EU FTT requirements is likely to be large. As well as the data required above to meet specific primary liability requirements, market participants may also need to build and deploy other data systems to support second order effects of EU FTT, for example data to support the mitigation of joint and several liability risks on EU FTT.

Proposed EU FTT requires gross transaction data (C4)

The proposed EU FTT Directive includes within the scope of financial transactions that involve the purchase and sale of a financial instrument, or the conclusion of derivatives contracts, the gross transactions in each case, "before netting or settlement" (Article 2(2)(a) and (c)).

From a collection perspective, there is potentially a significant challenge in ensuring taxation of gross (i.e. pre-netted) transactions given the prevalence and benefits of netting across the financial industry.

Once transactions are netted, the gross information is lost to parties subsequently involved, for instance, custodians, CSDs, transfer agents etc. This represents a particular challenge in relation to collection models involving market participants that perform centralised functions such as depositary and clearing functions, since very often such functions are undertaken using net data. Often the transactions which are subject to central clearing and settlement bear little relationship to the gross transactions above the level of clearing and exchange members and therefore any collection system involving central infrastructure needs to take this into account.

Challenge of wide transaction scope (C5)

The range of transactions proposed to be taxed under the draft EU FTT Directive presents a challenge because:

- some transaction types do not currently attract operational taxes, such as the vast majority of derivatives, and therefore there is/are no tax collection practice/procedures to leverage from;

- asset classes vary in terms of trading venues, clearing, settlement and custody functions and therefore the most appropriate collection method for one asset class may not be feasible for another, reducing the capacity for harmonization;

- with such a wide scope of transactions on a global basis the operational and IT requirements will be that much more significant than for a narrower tax.

Data privacy and data protection are obstacles to collection systems based on cross border transaction data transfer (C6)

Where a collection approach requires data to be passed from one market participant to another, that process will need to adhere to laws on data privacy. Even when permissible under such laws, the handling and management of that data will need to be governed by data protection procedures. Given existing EU harmonisation, this is primarily an issue for the passing of information from or between participants outside the EU. For instance, in the US, generally third party data cannot be transferred cross border without the permission of that third party. However, certain "safe harbours" apply. Other countries, such as South Korea, do not allow data to be transferred offshore even with a counterparty's consent.

Beyond the legal issues surrounding data, there will be commercial issues which inhibit certain collection models from operating. For instance, an asset manager is unlikely to appoint one broker dealer to do all its EU FTT compliance, if that would require it to disclose all the transactions it has undertaken with other broker dealers, since that data will be commercially sensitive.

4.2 Challenge of ensuring effective EU FTT remittance

Potential misalignment with cash flow (C7)

The proposed FTT Directive envisages liability on the part of FIs which may not be associated with any cash flow at the time EU FTT is due, for instance a contract variation with respect to a derivative. Lack of alignment with cash flow causes a collection challenge. Even in cases where EU FTT liability could be withheld from cash payments, a collection model involving a third party to calculate and pay over tax may separate transaction cash flows from tax cash flows.

Challenge of payment on settlement date (C8)

We note that the Commission's assumption is that the proposed EU FTT Directive could change such that the tax payment date for electronically executed transactions will be settlement date, typically two or three days after execution.

This change would be significantly beneficial from a collection perspective compared to payment on the date of execution.

However, tax payments upon settlement date would still prove to be challenging as there are a number of scenarios where additional post trade processing may be

required in order for tax liabilities to be calculated with certainty. Such scenarios include changes in the allocations of trades to specific accounts and legal entities, identification and resolution of trade breaks with exchanges, clearing houses and counterparties, and kerb trading or other activities where orders occur outside of general market regulations and/or opening hours.

There could be operational benefits for both market participants and the tax authorities if a number of additional days were to be allowed.

Challenge of operating intermediary relief (C9)

The proposed Directive provides for a limited form of 'intermediary relief' in article 10(2) which stipulates that:

> "Where a FI acts in the name or for the account of another FI only that other FI shall be liable to pay FTT" (hereafter referred to as 'intermediary relief').

From an operational perspective, the intermediary relief will be difficult, for instance:

- FIs will need to identify whether their counterparties are defined as FIs or not to determine whether the exemption is in theory available
- Order fulfilment is often achieved through complex mechanisms, often electronically, and therefore tracing what trades are "on behalf of another FI" will be operationally difficult

Although regulatory reporting requires capacity in which an order is executed, this does not precisely align to the intermediary relief in the proposed EU FTT Directive (cfr. Section 7.3).

4.3 Challenge of ensuring effective compliance and enforcement

Matching and reconciliation of transaction data (C10)

Certainty that the correct tax is being paid, is enhanced by the ability to match and reconcile data from different sources, for example matching transaction settlement data with tax data, or matching and reconciling data from each separate counterparty to a transaction.

The breadth of the proposed EU FTT makes the task of reconciling relevant data particularly difficult, especially since much of the data required for reconciliation will need to be compiled purely for EU FTT purposes, as noted above.

Potential conflicts between EU regulation and EU FTT collection (C11)

EU FTT will of course be superimposed over a highly regulated industry. The collection mechanisms for EU FTT may be able to take advantage of certain aspects of

regulation, but those regulations also provide obstacles to the extent they conflict with collection requirements.

There is limited scope within our study to consider all the possible interactions between collection mechanisms and regulation, but we would offer the following examples and observations:

- Alignment between EU FTT collection and overall market structure is a regulatory issue. We would expect regulators to take an interest in EU FTT collection if the collection mechanism conflicts with the overall design of the regulatory framework in Europe. For example, a design principle behind EMIR is to simplify and de-risk clearing and settlement processes. If EU FTT collection were perceived to conflict with these objectives, we would expect regulators to be concerned.

- Operational risk at a firm level. Particularly for the larger regulated firms, regulators will have scrutiny over their IT programs and operational risk procedures. The introduction of EU FTT and its collection procedures represents an area of risk, both for individual firms and for markets. Regulators will want to be sure that when EU FTT is "switched on" markets remain stable, liquidity is available and trades do not fail *en masse* (this is a risk if FIs are required to make changes to their systems and processes simultaneously). The choice of collection system will potentially affect these issues.[5]

Due to the range of regulation issues which are potentially affected by EU FTT collection, close working co-operation with national and supra-national regulators in designing EU FTT collection would be desirable, especially if collection models which require the centralisation of data needed to determine FTT liability are to be used.

National laws and national market practices may inhibit harmonised collection methods (C12)

Whilst PMSs are working towards an enhanced co-operation Directive applicable in each of the 11 PMSs, such a Directive - as is the case for any harmonised tax legislation – will need to be able to interact effectively with the national legal systems in each PMS and their respective market practices. Indeed, the process of legislating for EU FTT will entail 11 different exercises in transposing the Directive into national laws, and PMSs may do this in different ways, with further avenues for differing interpretation.

For instance, although MiFID is a Directive applying equally to all Member States, regulators take different views on issues such as the level of granularity of transaction reporting or different legal interpretation of substantive terms. So, in general terms, the detailed application of any EU rule could lead to different local practices which may be a barrier to harmonised collection systems.

5 For instance, with Italian FTT, certain small FIs have ceased to trade Italian stocks and derivatives due to the complexity and uncertainty of collection and reporting. Larger FIs have also suffered dislocation in trading due to uncertainties over issues such as the correct application of the distinction between white list and black list countries.

Similarly, when it comes to local market practices, the banking or asset management structures of national markets vary considerably, with some PMSs having large domestic banks that dominate and others having a much more fragmented system with many smaller banks. In some markets, banks operate the functions of broker/dealer, clearer and custodian. In others, all these functions tend to be in separate businesses.

This may result in different views on the practicality of different collection approaches. Consideration will be needed by each PMS of the viability of different collection models in the context of its market structure and participants.

An example of how national considerations might influence the choice of collection systems would be the German constitutional requirement for taxes. Under German constitutional law, a tax breaches constitutional principles if the payment of the tax is in effect left to taxpayers with no systematic compliance control possibility for tax authorities. This rule was developed by the German Constitutional Court in the field of capital yield taxation, in particular interest income, before the current flat tax regime. At that time, the income taxation of capital yields was largely based on a self-declaration system which – combined with the strict banking secrecy in place – resulted in many taxpayers not declaring capital yields. Accordingly, in the absence of efficient control by the tax authorities (because of banking secrecy laws), capital yield taxation was insecure. The German Constitutional Court ruled that such a "structural implementation gap" was unacceptable and on these grounds ruled against the self-declaration income taxation system applicable at that time.

We note that in some German tax literature, commentators have discussed whether or not the EU FTT, as proposed by the Commission, would result in a structural implementation gap such that the tax would similarly contravene German constitutional law principles. It would be up to the courts to decide whether measures aimed at ensuring broad tax collection were sufficient to defeat any potential challenges on grounds of the German constitution to the EU FTT. However, it may illustrate one potential national barrier to a harmonised collection scheme.

Enforceability is an issue from the perspective of collection of EU FTT on a global basis (C13)

The proposed Directive envisages a global geographical scope for the tax, particularly having regard to the counterparty principle and the issuance principle. Our study has not considered the legal basis of the charge to EU FTT for non-residents, though in the following paragraphs it does consider the practicality of EU FTT collection outside the EU FTT zone.

The essential building blocks of that framework within the PMSs are likely to include:

- **Access to data by tax authorities**. Data subject to regulatory reporting obligations are required to be kept available for the competent (regulatory) authority for at least five years. Both MiFID and EMIR in principle allow competent (regulatory) authorities to transmit confidential data (other than that received from competent authorities of other Member States) in accordance with national law, and EMIR expressly refers in its recitals to tax authorities among the bodies requiring access to this data for the purpose of their functions. Relevant information disclosure gateways could therefore be established to enable tax authorities to have access to this data. But for data

not subject to regulatory reporting, new data retention and tax authority access requirements would need to be laid down by each PMS for FIs established there.

- **Exchange of information between PMS tax authorities**. Since data obtained from another competent (regulatory) authority is in principle not permitted under MiFID or EMIR to be transmitted further, international exchanges of EU FTT information would likely need to be made between tax authorities. Within the EU, information exchange would be based on Directive 2011/16/EU of 15 February 2011 on administrative co-operation in the field of taxation, which repealed Directive 77/799/EEC. This would provide a mechanism for exchange of information on request, spontaneous exchange of information, presence in the offices where the administrative authorities of another Member State carry out their duties or presence during administrative enquiries, and simultaneous controls. However the current Directive would not cover automatic exchange of EU FTT information and this would hamper the effectiveness of Member States' enforcement, as provision of information would rely on the requesting Member State being aware that information is required and the requested Member State's tax authorities then obtaining that information from the local regulator or taxpayer directly.

- **Mutual assistance in recovery**. Council Directive 2010/24/EU of 16 March 2010, concerning mutual assistance for the recovery of claims relating to taxes, duties and other measures, has been in force in the Member States since 1 January 2012 and would be applicable to EU FTT. However this would apply only to established and non-contested claims to tax, limiting its value as an enforcement tool.

The challenge of creating a compliance and enforcement framework to maximise EU FTT collection is all the greater in relation to FIs liable to the tax outside the PMSs. The particular additional challenges outside the PMSs include:

- **Multiple contact points.** Whereas, within the PMSs, information is likely to be held and kept available for the regulatory and tax authorities in the single Member State where the entity is authorised, FIs in non-PMS countries (both in and out of the EU), and without any branch in the PMSs, are likely to be required to deal directly with the tax authorities of each PMS. This would be burdensome as it would require registration as an FI for EU FTT purposes in each PMS and reporting (including nil reporting) while registered as an FI.

- **Exchange of information between PMS and non-PMS tax authorities and mutual assistance in recovery.** While tax authorities may lay down information reporting and payment obligations for FIs outside their jurisdiction, enforcing these will essentially rely on exchange of information and mutual assistance mechanisms, where the challenges are greater than between PMSs (see below). Non-PMS EU Member States would be subject to information exchange obligations under Directive 2011/16/EU of 15 February 2011 on administrative co-operation in the field of taxation and to mutual assistance in recovery obligations under Council Directive 2010/24/EU of 16 March 2010 ('MARD'). However a non-PMS tax authority, which does not obtain FTT information for its own purposes, will not be in a position to provide the same level of spontaneous information as PMS tax authorities. With some third (non-EU) countries, the Council of Europe/OECD Convention on Mutual Administrative Assistance in Tax Matters could in principle be applicable to EU FTT tax given its scope, particularly in relation to exchange of information on request. However, as noted above, spontaneous exchanges are unlikely to be extensive and further co-operation in relation to automatic exchange of information, simultaneous tax examinations, tax examinations abroad and assistance in recovery and service of documents is only catered for where there is mutual agreement between the countries concerned. A number of third countries with significant financial markets, including China, Brazil, Russia, Singapore and Switzerland (as well as some of the PMSs) have already signed but not yet at present ratified the Mutual Assistance Convention.

When EU FTT collection mechanisms are set up in the PMSs, it will be important to ensure that they are accessible for FIs established outside the PMSs, to the extent the countries concerned do not set up their own EU FTT collection mechanism. To have a global tax which PMSs have confidence is being globally complied with would require a large degree of global co-operation with non-EU states and may need the development of models which, in effect, use parts of the financial system to encourage global compliance.

Existing tax authority audit tax collection and enforcement procedures will not be sufficient to support FTT (C14)

A tax which for most PMSs is new will require new resources for tax authorities to implement, monitor and enforce. The proposed EU FTT provides a unique challenge to PMSs' tax authorities.

Without centralisation of collection functions and with incomplete alignment with existing transaction reporting, a fresh architecture to support the tax compliance environment would also have to be built.

Building a process to receive payments and process tax returns from PMS FIs is itself a major challenge depending on the solutions sought. But if the collection system is to be regarded as effective globally, PMSs will need to have mechanisms to verify payments received, have the ability to identify areas of non-compliance and have tools available to audit taxpayer returns and the operational processes being used.

Some of these tasks could potentially be performed by parts of the financial industry itself, but in order for this to be effective there would need to be a framework designed to make this happen, and, especially outside the FTT zone, economic

incentives to achieve a transfer of these burdens to market participants would need to be established.

In short, the existing tax compliance resources currently within each PMS are unlikely to be sufficient to quickly deploy and run an effective EU FTT.

4.4 Uncertain cost and economic model for tax collection is an obstacle to designing collection models (C15)

Financial markets and PMSs alike have a shared interest in cost efficient collection of EU FTT. For instance, PMSs will be concerned that:

- if the operation of a collection system for FTT via financial market infrastructure ("FMI") within the PMSs makes the overall FMI more expensive, that process may migrate to other FMI not responsible for EU FTT collection.

- if, similarly, collection costs are material to profit margins, this could lead to further unintended reductions in transaction volumes, over and above the reductions anticipated as a result of the cost of the tax itself.

Clearly, market participants will only voluntarily build new tax collection systems either for their own compliance or where they perceive a business opportunity to offer services related to EU FTT compliance to other market participants. This represents a particular challenge to the development of new, potentially centralised, collection models, since these models by definition require market participants to invest in them not for their own use, but for the use of third parties. Where a collection model is prescribed by PMS obligating a third party to collect tax, then the economic model for building and operating such a system needs to be established and funded.

In the section below "A comparative analysis of collection models" we have expanded on some cost issues presented by a range of collection options.

Overall conclusion on the challenges to the collection of EU FTT

We believe this section has captured the main issues which need to be weighed up in considering the component elements of a potential collection system.

The given challenges can be addressed to various degrees. Further in this report, we will deal with some potential solutions as we will assess whether and to what extent these challenges can be overcome.

5. Identifying potential approaches in the light of EU FTT collection challenges

5.1 Method

Given the challenges for the collection of the proposed EU FTT identified in the Section 4, we identified a number of critical factors that we believe PMSs and market participants would be likely to attach importance to in choosing a method for the collection of EU FTT.

In the light of those factors, we set out a range of approaches to be considered for the collection of the proposed EU FTT. We assessed the pros and cons of these conceptual collection approaches using three different sets of hypothetical financial transaction scenarios.[6] This resulted in a number of preliminary observations as a basis for further discussion with market participants. On the basis of the preliminary observations, further discussions were held with market participants to assess the conceptual collection approaches in more detail.

Our informal discussions with market participants principally in the banking, asset management and market infrastructure sectors have enabled us to deepen our analysis.

5.2 Design principles for effective and efficient EU FTT collection

Introduction

Following the identification of collection and enforcement challenges, we listed a number of principles for an effective and efficient collection of EU FTT. This was not performed on a quantitative basis and the factors should not be seen as scientific, given they are not specifically weighted nor prioritised.

These principles have served the purpose of facilitating a more structured conversation with market participants, and enabled us to ask them how they would rate the importance of any of the principles mentioned, or whether any important principle is missing.

The conversation with market participants was complemented by some further internal thinking, after which the below list of ten design principles (DPs) was developed (DP1 to DP 10).

List of design principles

We identified the following design principles:

[6] The followoing transaction scenarios were discussed with market participants: (i) purchase/sale of cash equities (chosen because cash equities are currently the most common asset class which attracts tax on purchases or sales of financial instruments), (ii) interest rate derivatives (chosen because this instrument is typically not taxed internationally and interest rates are the largest component of European derivative volumes), and (iii) fund unit redemption (chosen so that issues associated with investment in European fund platforms could be explored since they present different collection issues from the other two sets of facts which are core banking activities).

- **Alignment with data processes and reporting (DP1)**

  Regulations, including MiFID, MiFID II, EMIR, and the Dodd-Frank Act, require market participants (or in some cases, their delegates) to collate and report trade and transaction data, and market participants are therefore already making significant investments in their application and data infrastructure to meet the current requirements.

  This will provide a potential opportunity for data produced for non-EU FTT purposes to be made available and re-used for EU FTT purposes. Aligning EU FTT reporting requirements with those defined by existing regulations, and implementing data standards that make use of existing data elements that are already captured and reported, would mean that the incremental operational costs of EU FTT could be contained, and the cost and risks associated with compliance lowered. In Section 7 below we consider the scale of the data gap.

- **Operational risk mitigation (DP2)**

  Operational risk can manifest itself in many ways.

  With regard to EU FTT collection, we can envisage there being potential risks at the inception of a collection system and for there to be ongoing risks too.

  Different collection systems will result in different impacts on the scale and breadth of the "change footprint" for each FI. The greater number of simultaneous changes to systems, front to back, the greater the potential is that transactions fail due to reconciliation errors, unmatched confirmations etc. The consequences of such failures include counterparties not being in the position they expected to be in, with resulting customer risks, through to financial risks.

  Even if clearing and settlement would be dependent on EU FTT collection – which option has not been considered – one can still envisage operational risks if trades suffer from a delay in processing due to systems not being adequately prepared with the resulting remediation and workarounds. Whilst we would envisage such problems to be most acute at inception, however, these will be an ongoing operational risk to manage for changes in products, markets, IT and other aspects.

  Although it is difficult to extract operational risk of collection from the overall operational risk of EUFTT, nonetheless, we consider that when designing collection systems, the potential for operational risk needs to be assessed and minimised.

- **In-built capacity to reduce tax risk (DP3)**

  It is expected that tax authorities will need a collection and reporting mechanism that has integral checks and balances to ensure that the right amount of EU FTT is collected and reported, and that non-compliance is minimised.

  Market participants will also benefit from such controls, especially where there is significant concern about features such as joint and several liability which could result in a taxpayer being exposed to an obligation to pay EU

FTT in the event that counterparties default or do not correctly observe responsibilities with regard to EU FTT liability.

The design of a collection and reporting mechanism should therefore give adequate consideration to:

- data retention,
- right of audit,
- real time checks and balances,
- early identification of delinquent market participants.

There are many practical problems to overcome, but in theory a collection system that could match the tax paid on individual transactions between two counterparties would be an ideal outcome.

As both timing and data availability are of key importance, ongoing checks and balances as information is passed on between market participants (i.e. the establishment of an 'audit trail') seems preferable rather than relying only on a post-event audit by the relevant tax authorities.

Market participants will also want a level playing field to be maintained after the introduction of EU FTT. A market where certain participants do not apply EU FTT in some circumstances, where others do, will be an unwelcome feature of any compliance environment and will lead to market distortions. It is highly desirable that collection mechanisms give rise to market conformity with respect to the practical application of EU FTT.

- **Alignment with cash flows (DP4)**

  From a practical perspective, it would be advantageous and more efficient for collection responsibility to be aligned, so far as possible, with the funds paid as part of a transaction. Without such alignment, separate arrangements will need to be made to effect payment, requiring payment instructions and a separate tax payment.

  In the event that a party that does not participate in a trade assumes certain collection responsibilities, a robust system of payment instructions would need to be developed.

- **Minimisation of collection and reporting points (DP5)**

  Minimising collection and reporting points would be beneficial both from the tax authorities' point of view and from an industry perspective.

  Minimising the number of collection and reporting points may help to ease the compliance burden for some market participants. For instance, smaller FIs may not want to build systems and processes required to make direct payments to PMSs.

  For the tax authorities themselves, rationalisation of reporting and collection will make administration of the system easier.

It is our understanding that, under EMIR, potentially one million entity codes may be issued. Whilst some of these may not overlap with entities that pay EU FTT (for example some swap counterparties may not fall under the EU proposed FTT FI definition), it does give an indication of the vast numbers of daily payments which might be theoretically due, and suggests that some kind of rationalisation of the payment structure would be highly desirable.

- **Harmonisation across geographies, asset classes and execution venues (DP6)**

  PMSs will seek to avoid market distortions and will therefore be motivated to ensure that collection and reporting mechanisms are consistent across geographies (to the extent possible under jurisdictions' legal frameworks). It is also desirable that the burden of EU FTT administration is broadly equivalent to ensure that certain national markets are not preferred solely because of differences in tax administration.

  Promoting consistency across asset classes (and their execution venues) will present a greater challenge due to the way different products are transacted. Commonality should be achieved wherever possible, and where it cannot be achieved, flexibility based upon consistent underlying principles for collection and reporting should be sought.

- **Maximisation of process automation (DP7)**

  Market participants have invested heavily in streamlining their front to back processes to achieve acceptable rates of straight through processing (STP). Containing the cost per trade in this way is critical against an economic backdrop of compressed profit margins, the competitiveness of global capital markets and the significant burden of regulation.

  Being rules-based, in theory it should be possible to maintain STP rates in relation to computing, reporting and collecting transaction taxes. But, as discussed above, this requires clear rules and availability of the data required to compute the tax arising from each transaction.

  Reporting and collection mechanisms should not place such a burden on the front-to-back processing of a transaction such that it requires human intervention. This will means the PMS would need to be careful not to stipulate new elements that need to be captured or flagged, or resort to messaging standards which lie outside the current scope of financial network facilitators such as FIX, Omgeo and especially SWIFT message types. The completeness, accuracy and availability of reference data will be key and any requirement for market participants to report based on data that cannot reasonably be obtained at the time the calculation is required will increase operational risk and cost.

- **In-built globalaccessibility (DP8)**

  Organisations domiciled outside the PMSs may have a requirement to be able to report and pay EU FTT. The reporting and collection mechanisms will have to allow access to organisations globally. Challenges, including those with respect to enforceability, right of audit, and data privacy therefore will need to be addressed.

It should be noted that market circumstances may differ geographically. Apart from the model to be chosen, it may be necessary to address the framework requirements (e.g. agreements to be entered into, exchange of information etc.) to be put in place to allow collection and enforceability outside the PMSs.

- **Alignment with current market practices (DP9)**

  From an operational perspective, EU FTT collection will be less costly to build and run and have have less operational and tax risk if tax collection and other aspects of EU FTT align to market practices.

  For instance, the various Buy Side/Sell Side trading arrangements using market practices such as riskless principal do not easily correlate to the draft Directive's intermediary relief. Equally, the prevalence of netting within financial markets means that visibility of gross data is only readily present at certain parts of the financial system and collection methods need to recognise this. Another example of alignment would be to consider the common arrangements between Buyside firms, like asset managers, and broker dealers, for example investment banks, under which the broker dealers often take on functions like regulatory reporting in respect of transactions which the broker dealers execute on behalf of their client. Allowing the flexibility within a tax collection model to follow this kind of commercial arrangement would be an example of using this design principle in practice.

- **Simplicity and clarity of tax collection procedures (DP10)**

  Clear andunambiguous rules are also vital for the process of tax collection. In this regard, it would be helpful for any legislation adopted to be as prescriptive as possible with regard to collection procedures. . Clear collection rules and procedures are particularly important for collection models where tax collection involves parties other than the taxpayer in the collection of the tax. The fundamental starting point is to establish legal capacity under which tax collection operates and the potential for joint and several liability. In this regard, our working assumption is that the collecting agent is not liable for the tax of its principal. The detailed legal framework as to how principals, agents and tax collection agents operate under any model would be critical, particularly in relation to joint and several liability for the proposed EU FTT.

Mapping collection challenges to design principles

Having listed the fifteen challenges (in Section 4) and the 10 design principles above, at this point in our methodology we considered whether, at least in general terms, the design principles for collection systems are covering areas which could potentially address these challenges.

The table below records this exercise. So for instance if under Design Principle 1, "collection systems align with data processing and reporting", then, theoretically, this goes some way to addressing the data challenge, because to the extent EU FTT uses data which is already available, then the challenge of having to build unique reference data is reduced. Similarly, if the collection system is aligned to existing data processing and reporting then, Challenge 5 "data privacy and protection" should be

reduced, since existing data processing should already have got over these hurdles. This table has a number of subjective judgements and should be seen as a general check that in considering the design for potential collection systems, the principles we are intending to work from do tie back to the challenges we have identified.

Reference Table

	Group1 - Clear determination of EU FTT liabilty						Group2 – Effective Remittance			Group 3 – Support for compliance and enforcement					Group 4 - Cost
	C1 Potentially unclear primary rules	C2 Inhibit automation	C3 Data Challenges	C4 Gross transaction data	C5 Wide transaction scope	C6 Data privacy & protection	C7 Misalignment cash flow	C8 Payment on settlement date	C9 Intermediary relief	C10 Matching transaction data	C11 Conflicts regulation - collection	C12 National laws and practices	C13 Global enforceability	C14 Existing tax collection and enforcement	C15 Uncertain cost and economic model
DP1 - Alignment with data processes and reporting			√		√	√				√	√	√	√		√
DP2 – Operational risk mitigation	√	√	√				√	√		√					
DP3 – In-built capacity to reduce tax risk	√	√	√		√				√	√			√	√	
DP4 - Alignment with cash flows		√		√			√	√		√					√
DP5 – Minimisation of collection and reporting points		√							√				√	√	√
DP6 – Harmonisation across geography, asset classes and execution venues		√			√				√	√				√	√
DP7 – Maximisation of process automation	√	√		√			√			√			√	√	√
DP8 – In-built global accessibility	√					√						√	√	√	
DP9 – Alignment with current market practices		√	√		√	√	√			√	√	√	√		√
DP10 – Simplicity and clarity of collection procedures	√	√	√						√	√			√	√	√

List of Challenges

Group 1 - Clear determination of EU FTT Liability

C1 Potentially nclear primary rules

C2. Certain proposed EU FTT rules inhibit automation

C3. Data challenges

C4. Proposed EU FTT requires gross transaction data

C5. Challenge of wide transaction scope

C6. Data privacy and data protection are obstacles to collection systems based on cross border transaction data transfer

Group 2 - Challenge of ensuring effective EU FTT remittance

C7. Potential misalignment with cash flow

C8. Challenge of payment on settlement date

C9. Challenge of operating intermediary relief

Group 3 - Challenge of ensuring effective compliance and enforcement

C10. Matching and reconciliation of transaction data

C11 Potential conflicts between EU regulation and EU FTT collection

C12 National laws and national market practices may inhibit harmonised collection methods

C13 Enforceability is an issue from the perspective of collection of EU FTT on a global basis

C14 Existing tax authority audit tax collection and enforcement procedures will not be sufficient to support FTT

Group 4 – Uncertain cost and economic model for tax collection is an obstacle to designing collection models (C15)

6. Four theoretical approaches for EU FTT collection

6.1 Introduction

We have identified a range of four potential approaches to the collection of EU FTT, depending on the extent to which the proposed EU FTT payment (and associated reporting) obligations rest with the person liable to EU FTT, or are concentrated or centralised among a smaller number of collection agents.

The approaches outlined are at a conceptual level and are intended to be generic.

They take into account our analysis of existing collection regimes and the unique aspects of the proposed EU FTT. They are not drawn directly from any existing domestic transaction tax collection regime. However, we refer where appropriate and as a 'reference system' to comparable models in jurisdictions that have a domestic FTT collection system.

The descriptions of the four collection approaches are not necessarily exclusive and overlaps are possible between features and elements of one or more of the model(s). Also, consideration of four separate models does not suggest that ultimately only one model should be applied, as different collection models (for example for different asset classes) may be able to co-exist. Indeed, where any given model cannot adequately address specific challenges, features from other models may be added. Due to differences in markets etc., there may be value in having flexibility built into any EU FTT collection model, however, this needs to be balanced against an overall design objective of consistency and harmonisation.

6.2 Approach 1: Self-administered

Description

Under Approach 1 ('Self-administered'), all FIs determine, pay and report EU FTT due from them under the proposed Directive. This is the most straightforward and unambiguous approach to tax collection. It is a common collection method for transaction taxes. It would require each FI to build processes to enable it to compute its own taxes and pay to the relevant PMS. However, the design of EU FTT is such that even with a self-administered approach, a number of data dependencies will need to be met outside the taxpayer firm, in particular transaction identifiers to note EU FTT zone issuance and counterparty identifiers to enable EU FTT primary liability to be determined.

Under a self-assessment model, we would envisage that there would be a market demand for:

- IT vendors to supply software to enable FTT calculation, workflow management tools etc.;
- data suppliers to build systems to supply reference data; and:
- FIs to offer EU collection services to other FI's on a contractual basis.

Such developments would assist taxpayers with the task of compliance.

In practice, this model will often mean that EU FTT collection is undertaken by the financial intermediary closest to the seller or the buyer (the principal), i.e. at the bottom of the chain of intermediaries (this assumes all other FIs are able to claim intermediary relief under Article 10(2).) Such relief may have to be dependent upon the passing of information such as information to enable the counterparty rule to operate. It is common for any FI to look to the support of organisations such as asset servicers, fund administrators, transfer agents, prime brokers and custodians, to offer services in relation to operational taxes. We would expect market forces to similarly apply to EU FTT collection services which should therefore be permitted to contractually, not legally, transfer collection obligations to third parties.

Reference model

A reference point for this model is the Belgian tax on stock exchange transactions ("Taxe sur les operations boursières" or "TOB"), which (in principle) applies to secondary market transactions in respect of securities that qualify for trading on a stock exchange that are intermediated by a Belgian FI and carried out or concluded in Belgium where the buyer/seller is a resident other than an institutional investor.

From a collection point of view, the TOB assigns collection responsibilities to the first Belgian financial intermediary, i.e. the financial intermediary that has received the initial instruction to buy or sell the securities from the buyer or seller.

Alignment to design principles

We consider that the self-administered approach most takes into account design principles 4, 6 and 10. The apporach aligns to cashflow since the principals to transactions, the buyers and sellers, are most likely to have control of cash payments and receipts since they will need to make payments on the underlying transaction. It is also a harmonized system in so far as all FIs pay their own tax and there are no special variations for assets classes, countries etc. However, we can anticipate that contractural arrangements for tax collection would emerge across the supply chain resulting in a *de facto* less harmonized collection system. Similarly, whilst in principle the approach is a simple approach, i,.e every FI pays its own tax, there will be plenty of organic developments within the system over time such that the approach may not be a as simple in practice as the rules suggest. This approach has particular problems with design principles 3, 5 and 8. Since there is no centralisation of any collection function, there is by definition no reduction in collecting points and no capacity to reduce tax risk in the system. It is also inaccessible globally since there is no system to connect to support compliance.

6.3 Approach 2: Delegation of collection responsibilities

Description

This approach is a variant of the self-administered model (Approach 1) involving potential legal delegation of collection and reporting obligations to another FI involved in the financial transaction (which could be a party acting as an agent for the liable party itself and/or a further intermediary involved). The approach could also be used in connection with other collection models where FIs either prefer to use the services of an agent for business reasons or where they have no direct access to the collection functionality.

With this approach, other intermediaries involved are free to accept such responsibility for which they would need to have received the relevant data. Delegation would enable a degree of flexibility and allow the market to determine where best to concentrate the burden of calculation, reporting and payment. It will also allow PMSs to prescribe collection mechanisms which best fit their circumstances. This model is also used quite frequently in transaction tax collection models.

The approach would/may require:

- an audit trail requirement establishing by whom EU FTT collection/reporting has been assumed for any given transaction, and
- the exclusion of certain FI types from assuming EU FTT collection delegation responsibilities or the creation of an approval or registration process for agents.

The key differences between the likely outcome of "self-administered" and "delegation" models is that a delegation model is:

- a transfer of collection responsibilities which is legally recognized by a Directive or derogated PMS regulation, and
- the delegation system could be one that is prescribed by PMSs, rather than under the self-administered model whereby the practical aspects of collection could be undertaken by a variety of organizations on a contractual basis.

In this respect, a PMS could prescribe what type of organisation could accept collection responsibility and therefore exercise more control over the overall collection system than a self-administered system.

We would expect this delegation option to be most relevant to smaller financial institutions, funds, pension funds, etc. who are unlikely to invest in their own resources to build EU FTT rules engines, technical tax resources etc.

Reference model

The allocation of withholding responsibilities under the US Qualified Intermediary (QI) regime could serve as a reference model for a delegation collection approach, since it prescribes a set method of tax withholding whereby FIs can elect to assume either primary withholding obligations or secondary/residual withholding obligations.

The QI regime presents two options:

- a QI may itself perform the withholding due, remitting tax to the tax authority itself, or
- it may authorize an upstream custodian to perform its withholding. Typically this occurs through the use of omnibus accounts with the upstream custodian based in the country of domicile of the asset.

Alignment to design principles

We consider that the delegation model most takes into account design principles 7,8 and 9. It potentially facilitates automation since the processing of transactions is often

undertaken , or at least managed, by intermediaries such as broker/ dealers or agents such as custodians or transfer agents. By also designing a tax collection system which harnesses their roles in the supply chain this potentially allows for both maximum process automation and aligns with market practices. It also facilitates global accessibility since for buyers and sellers outside of the EU FTT zone will often trade in EU FTT instruments or with EU FTT zone counterparties using EU FTT zone FIs for specific capabilites such as direct market access to trade venues, local custody of assets etc. This approach, though, has particular problems when judged against design principles 6 and 10. With the potential to delegate collection to intermediaries, it may prove difficult to achieve harmonization and simplicity. There is scope for confusing about which FI is meant to be collecting tax on what and it may prove that delegation is taken up in certain markets and/or for certain assets classes and not others, resulting in a patchwork approach not consistent with a harmonization goal.

6.4 Approach 3: Central Clearing or Settlement

Description

Under Approach 3 ("Central clearing or settlement"), EU FTT would be administered as part of existing central clearing or settlement processes. EU FTT collection responsibility would lie, by design, with the CCP clearing the transaction or the CSD settling the transaction.

Each FI involved in the transaction who might be liable to EU FTT (or their appointed agent) would be required, or would be offered the option, to provide the central party (CSD or CCP) with (i) information to denote what EU FTT (if any) is due to which PMS and (ii) the funds to pay any EU FTT due (or authority to withhold this tax from funds due to them in the settlement process). The CCP/CSD would then act as collecting/paying agent for the FIs using this collection model.

It is important to note that the CCP/CSD model does not necessarily imply collection of tax as a pre-condition to clearing/settlement ("Delivery versus Payment"). There are operational risks with such a process. In addition, it may not be legally achievable or be possible, for example, when the chargeable transactions are not settled through the CSD. However, CSDs/CCPs could still be used as a collection mechanism "off line" to the actual clearing and settlement processes. In essence this is how part of the CREST system works for Stamp Duty Reserve Tax in the UK. CREST is used to compute and collect SDRT for UK equity market participants such as broker dealers and custodians even when CREST is not required to transfer legal title. For example, if fund A sells UK chargeable securities to fund B and both funds use the same custodian, this transfer does not need to be processed by CREST, it is processed by the custodian itself. There are no movements in the account which the custodian holds with CREST, however the custodian will send data on these "non-settling own account transfers" to CREST for SDRT to be processed along with the other transactions which are Delivery Versus Payment ("DVP") transactions. In addition, the CREST system will be offering the possibility to send gross trades for SDRT assessment to the CREST system through Stamp Assessed Trade (SAT) instructions.

By analogy, CSDs/CCPs could be considered as collection models since the apparatus they already operate under, for example pre-existing IT interfaces with market participants to process for high volume real time transactions, and a strong regulatory

environment, are all assets which could form the basis for an EU FTT centralised collection model.

Under this model it is not necessary that CCP/CSDs will *determine* liability. The gross data required to calculate primary liability may not, therefore, need to be transferred to the CCP/CSD. Instead a flagging system would be used representing the output of the rules engines housed at broker/dealer level. However, the CCP/CSD will require the flags to be submitted in the same format and will have sufficient information from this flagging system to provide a measure of quality assessment over the data submitted to it in this form (as an option it might be possible for a CCP/CSD to also compute primary liability in some circumstances). The CCP/CSD would require an audit trail back to the source data to support substantiation of the calculation upon audit.

Reference model

Domestic FTT collection models that rely on CSDs are the SDRT in the UK (collected by Euroclear UK & Ireland) and the recently introduced French FTT (collected by Euroclear France). We are not aware of any transaction tax collection mechanism that is integral to central clearing processes.

Alignment with design principles

We would consider that this approach most takes into account design principles 3,4,5,7 and 9. A central clearing or settlement solution has the potential to match data , if the net data challenge can be overcome. This would reduce tax risk as would having a central collection function with central resources capable of facilitating consistent compliance. This approach reduces the number of tax collection points and through sitting alongside existing transaction processing aligns to existing market practices, cashflows and automatic processing. Design principles 6 and 8 are more challenging for this approach. CCP/CSD collection is limited to certain asset classes and seems unlikely to be appropriate outside of the EUFTT zone.

6.5 Approach 4: New Utility

Description

Under Approach 4 ('New Utility'), a dedicated tax collection utility (or utilities) would carry out collection and reporting. This would be an alternative form of centralised tax collection. The functions of the utility would be separate from clearing and settlement on the taxable transaction itself. However, this does not, *per se*, preclude one of those parties being involved in development of such a utility as well as carrying out some or part of the collection task. The utility would centralise data and have the effect of standardising reporting and rules engines used across industry. A new utility approach is another form of centralisation comparable to the CCP/CSD model. The key differences between a new utility and the CCP/CSD model are that the CCP/CSD model is aligned to the clearing and settlement infrastructure of markets, whereas the new utility model is aligned to the regulatory reporting environment. In this regard, since the utility is likely to be receiving detailed gross data across a wider range of asset classes, it could more easily compute primary liability than could the CCP/CSD model. Many FIs are likely to want to keep control of primary liability calculation, but the utility calculation could act as a reconciliation or as a method of matching primary

liability with a counterparty. As with the CCP/CSD model, the utility model holds out the prospect of putting EU FTT compliance in an environment which is strongly regulated, it potentially re-uses data that is already being reported, and therefore leverages existing infrastructure.

Both the CCP/CSD and regulatory reporting environments are undergoing considerable change both regionally in the EU/EEA and globally. Both are changing to increase the role of centralisation of core systemic functions such as clearing and settlement and to increase the scope, frequency and detail of daily transaction reporting.

A new EU FTT collection utility would require a significant system build to enable connectivity with FIs and it may need its own rules engines and reference databases in order to fulfil its collection task (depending upon functionality required).

An industry utility model would most probably exist as an adjunct to transaction reporting services which are increasingly being deployed globally by major infrastructure players. It could be envisaged that the Commission or PMSs authorise and regulate such utilities.

Reference model

From a regulatory perspective, comparable systems exist for transaction reporting, for instance under EMIR, MiFID and CFTC regimes, where reporting is required to be made to a series of trade repositories/approved reporting mechanisms. Data is collected on a transaction by transaction basis, daily, using standard templates. The transaction data is available either directly or indirectly to cross border regulatory bodies, like ESMA and/or local regulatory bodies.

Gaps between existing transaction reporting data and data needed for the proposed EU FTT are significant and would need to be closed. In addition, the proposed EU FTT logic would have to be incorporated into the collection mechanism. In addition, the lack of access to cash to pay for the tax due must be considered.

Alignment with design principles

We would consider that this approach most takes into account design principles 1,2,3,5,6,7 and 8. Clearly this approach most aligns to existing data processes and reporting. It is globally accessible and asset class agnostic. By being completely separate from transaction processing one could argue that it therefore reduces operational risk. If it dovetails with existing automatic reporting of transactions for regulatory purposes, then it could also be an automatic process. It could be a system which reduces tax risk too if it standardises market practice on compliance and provides auditability. It most fails Design Principles 4 and 9. Transaction reporting is delinked from cashflow and tax collection is a new function for transaction reporting, hence it is not aligned to current market practice.

Approaches 3 and 4 - overlaps

Whilst our analysis continues on the basis that central collection might be embedded within, or sit alongside, either CCP/CSD or trade reporting, to some extent this is an arbitrary distinction. For many purposes it is more important to consider whether central collection functions are minimal or significant rather than to consider what type of entity should operate collection. As stated above, a central functionality could be operated by a new utility or by an existing CSD/CCP.

7. Practical considerations for assessing the theoretical EU FTT collection models

In Section 6 we identified four theoretical collection models. Before weighing up the pros and cons of these models, there are a number of key topics which need explanation in order to assess how viable these theoretical models are in practice, particularly in the context of EU financial markets. The key topics are:

- EU FTT would apply to a regulated industry undergoing significant regulatory reform; how might this impact EU FTT tax collection?
- if EU FTT collection is going to leverage the existing EU financial market infrastructure, how attractive is that landscape for tax collection?
- if EU FTT collection is going to leverage existing and future state transaction reporting, how big is the gap between future state regulatory transaction reporting and the data required for EU FTT?

7.1 The ongoing significant EU regulatory reform of the financial services industry

The current and future structure of EU financial markets is important for EU FTT collection, particularly in relation to counterparty identification. Counterparty identification is needed for non-PMS established FIs so that they can determine whether EU FTT is chargeable and to which PMS. It is also important for PMS FIs since they will need to manage joint and several liability risks on counterparties. In addition where PMS FIs are acting as collection agents, they need to pay the right PMS on behalf of their clients.

MiFID I, which took effect in November 2007, defined three different formal categories of trading venues as follows:

- Regulated markets (typically exchanges)
- Multi-lateral trading facilities (MTFs)
- Systematic internalisers

In addition, there were other mechanisms which facilitated direct trading between financial institutions, for example:

- Dark pools (off-exchange facilities that allow trading of large blocks of shares through quantity discovery models, with prices posted publicly only after trades are done). These are operated by exchanges, MTFs or investment firms;
- Bi-lateral (e.g. counterparty to counterparty, with no intervening mechanism). These consist of crossing networks for order-driven markets, or single-dealer platforms for quote-driven markets.

MiFID II, which will take effect from January 2017, introduces a further category of "Organised Trading Facilities".

Our general observations regarding collection processes for the three existing MiFID I categories are as follows.

Regulated markets (Exchanges)[7]

Regulated markets are significant trading venues for cash equities and selected fixed income and exchange-traded derivatives such as commodities. Regulated markets are usually aligned with central clearing facilities (called central counterparties) through models which are strongly-coupled (i.e. vertically-integrated) or have open-access arrangements. Regulated markets may also be integrated with national central securities depositaries for cash instruments such as equities or fixed income securities (e.g., in the case of equities, in Germany, Italy or Spain). The legal position for business is that the regulated market is a place where the function of price discovery is fulfilled in setting a central reference price. As of May 2014, there were 99 entities listed by ESMA as regulated markets, with some organisations registering multiple entities.

Once a trade has been made between the dealing counterparties, a legal contract can be established through a process known as novation with the CCP which acts as "buyer to every seller and seller to every buyer" in the marketplace. The CCP can thereby mitigate the counterparty risk that would otherwise exist between the dealers until the trade is settled. The CSD will receive settlement instructions from custodians where book-entry transfer is required (otherwise cash settlement occurs for derivative trades). These arrangements will be subject to revision from 2015 as the Target 2 for Securities project (T2S) begins to roll out.

The trend in respect of settlement has been for CSDs to receive an increasing percentage of their transaction data on a netted basis. This has delivered market efficiencies and cost reduction for market participants but had reduced the visibility to the CSD of the ultimate counterparties involved.

Multilateral trading facilities (MTFs):[8]

MTFs are significant venues for trading cash equities, liquid fixed income instruments, and certain derivative instruments. MTFs also dominate the dark markets, with upwards of 50% of all dark MTF activity taking place on BATS ChiX and UBS MTF according to Thomson Reuters. Estimates of dark venue trades accounted for around 8% of European equity trades according to an IMA study from March 2014. As of May 2014, there were 145 entities listed by ESMA as MTFs; ESMA does not specify which

[7] Regulated markets were defined under MiFID I L1 text Art 4.14 as: "…a multilateral system operated and/or managed by a market operator, which brings together or facilitates the bringing together of multiple third–party buying and selling interests in financial instruments – in the system and in accordance with its non-discretionary rules – in a way that results in a contract, in respect of the financial instruments admitted to trading under its rules and/or systems, and which is authorised and functions regularly and in accordance with the provisions of Title III". This definition is concurrent with the MiFID II Art 4.21 definition issued in the official L1 text in April 2014.

[8] Multi-lateral trading facilities (MTFs) were originally defined under MiFID I L1 text Art 4.15 as: "a multilateral system, operated by an investment firm or a market operator, which brings together multiple third–party buying and selling interests in financial instruments – in the system and in accordance with non–discretionary rules – in a way that results in a contract in accordance with the provisions of Title II". This definition is concurrent with the MiFID II Art 4.22 definition issued in the official L1 text in April 2014.

MTFs operate as 'lit' or 'dark'; it was estimated that there were at least 35 'dark' pools operated by regulated markets, MTFs or financial institutions in Europe according to the Tabb Group in 2012. This number could change considerably once the new category of organised trading facilities (OTFs) is introduced under the onset of MiFID II/R in January 2017.

MTF trades are also similarly centrally cleared via CCPs and settled via CSDs for cash instruments. These arrangements will also be subject to revision from 2015 as the Target 2 for Securities project (T2S) begins to roll out.

Systematic internalisers:[9]

As of May 2014, there were 12 entities listed by ESMA as systematic internalisers in equities carrying only a nominal volume in comparison with regulated markets or MTFs above, but this category could well be expanded by more financial institutions who either prefer or are not allowed to operate as organised trading facilities (defined by Article 4.23 of MiFID II to mean "a multilateral system which is not a regulated market or an MTF and in which multiple third-party buying and selling interests in bonds, structured finance products, emission allowances or derivatives are able to interact in the system in a way that results in a contract in accordance with Title II of this Directive"). All the current systematic internalisers listed by ESMA fulfil orders in equities within that specific financial institution without the need to go outside that financial institution.

Bilateral

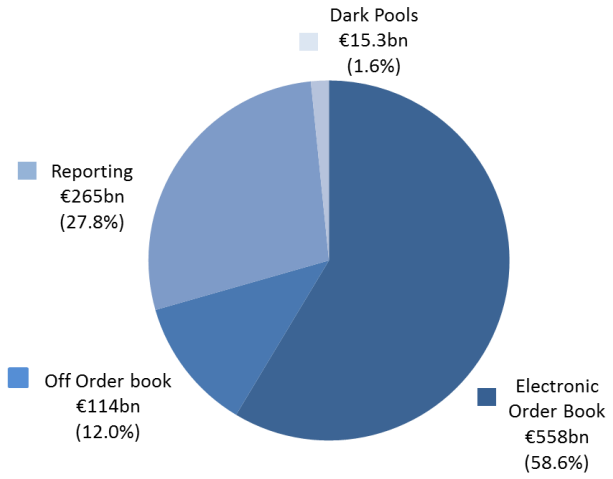
Many in-scope EU FTT transactions would be executed b-laterally and not on trading venues. This situation will face revision as soon as MiFID II comes into effect, by which time FIs will need to classify themselves into the categories listed above. The Liikanen measures – which aim to separate proprietary trading from other types of trading such as market making, matched principal and agency – are also scheduled to take effect across the Euro-zone from January 2017 to coincide with MiFID II. Certain OTC derivatives, and other instruments that are deemed ineligible for clearing – typically illiquid, non-standardised instruments or securities not admitted to trading - will likely continue to be transacted on a bilateral basis. This will include securities financing transactions. Securities borrowing and lending, repos/reverse repos and taxable collateral transfers will continue to be transacted on a bilateral basis until MiFID II takes effect.

Impact of market structure

[9] Systematic internalisers were defined under MiFID I L1 text Art 4.7 for equities to mean "an investment firm which, on an organised, frequent and systematic basis, deals on own account by executing client orders outside a regulated market or an MTF". This definition has been revised significantly under Article 4.20 of MiFID II to read: "an investment firm which, on an organised, frequent systematic and substantial basis, deals on own account when executing client orders outside a regulated market, an MTF or an OTF without operating a multilateral system. The frequent and systematic basis shall be measured by the number of OTC trades in the financial instrument carried out by the investment firm on own account when executing client orders. The substantial basis shall be measured either by the size of the OTC trading carried out by the investment firm in relation to the total trading of the investment firm in a specific financial instrument or by the size of the OTC trading carried out by the investment firm in relation to the total trading in the Union in a specific financial instrument. The definition of a systematic internaliser shall apply only where the pre-set limits for a frequent and systematic basis and for a substantial basis are both crossed or where an investment firm chooses to opt-in under the systematic internaliser regime".

The major issue from an EU FTT collection standpoint of the trading venue structure in the EU is counterparty identification. Essentially bilateral trading and systemic internalisers are the only trade venues that provide direct counterparty identification. Exchanges and MTFs do not provide for counterparty identification. The counterparty in such cases is the CCP. If the proposed EU FTT Directive requires FIs to "look through" the CCP to the other side of the transaction then this creates issues for large amounts of financial transactions. The ESMA data for the month of December 2013 can be used as a proxy for the scale of this problem. In the following diagram, dark pool and electronic order book are all MTF and regulated market transactions.

Monthly European Equity trading turnover by transaction type
December 2013: $952bn



Source: FESE, ESMA

Whilst equity transactions have much more frequency than bond transactions, there are many more Fixed Income products that trade OTC, between a client and a market maker. This is most evident when considering that the Tax Reference data service provides data on 300,000 Fixed Income securities, while the ESMA register of shares admitted to trading on EU Regulated Markets only totals 5,925.

Bond trading is generally off-exchange, with Euroclear Bank, Clearstream Bank and some national CSDs settling transactions. This provides them with the identity of the participants to a trade at the account level. Euroclear and Clearstream are Europe's pre-eminent (I)CSDs with a combined EU market share of around 85% in international bond settlement, however, it is also worth noting that most European countries have established their own CSD which could be looking to extend its service offerings under CSDR, TS2 and MiFID II.

Exchange groups have started to invest in Fixed Income electronic platforms, with recent deals highlighted by the acquisition of eSpeed by NASDAQ OMX. Electronification of the Fixed Income market is evolving and will be accelerated by the regulatory drive for transparency; however, this has typically been evident so far only with smaller trades for the retail market via retail MTFs or exchanges. The status is mixed with the non-government bond market, for example, conducted predominantly by voice, whereas market share of the inter-dealer government bond market is led by the Italian MTS electronic platform, majority-owned by the London Stock Exchange Group. So, whilst counterparty identification is currently much less of a problem in

fixed income markets, the trend is towards market structures more in line with cash equities.

Our overall estimate of the amount of trading through the categories of trade venue, by asset class, in the EU can be represented as follows:

	Equities	Fixed income	Exchange traded derivatives	OTC derivatives
Regulated Markets ('RMs')	70 -75%*	Nominal	90 – 95%	NA
MTFs / Multi-dealer plaforms	20 -25%*	<10%	5 – 10%	<5%
Systematic Internalisers	Nominal	NA	NA	NA
Bilateral/Single-dealer platforms	See below*	>90%	Nominal	>95%
Total	**100%**	**100%**	**100%**	**100%**
*An estimated 5 – 20% of equity trades occur bilaterally; percentages for RMs/MTFs assume a 5% off-RM/MTF figure (EY estimates)				

A conclusion from this table is that where counterparty identification is required for EU FTT purposes, this is clearly a significant issue for the prevalent market structure in cash equities and exchange traded derivatives, whereas this is a significantly less of a problem in fixed income and OTC derivatives. However, the direction of travel for these latter catergories with regard to regulation is not likely to worsen counterparty identification for EU FTT purposes.

7.2 Considerations specifically relating to EU infrastructure as an EU FTT collecting agent

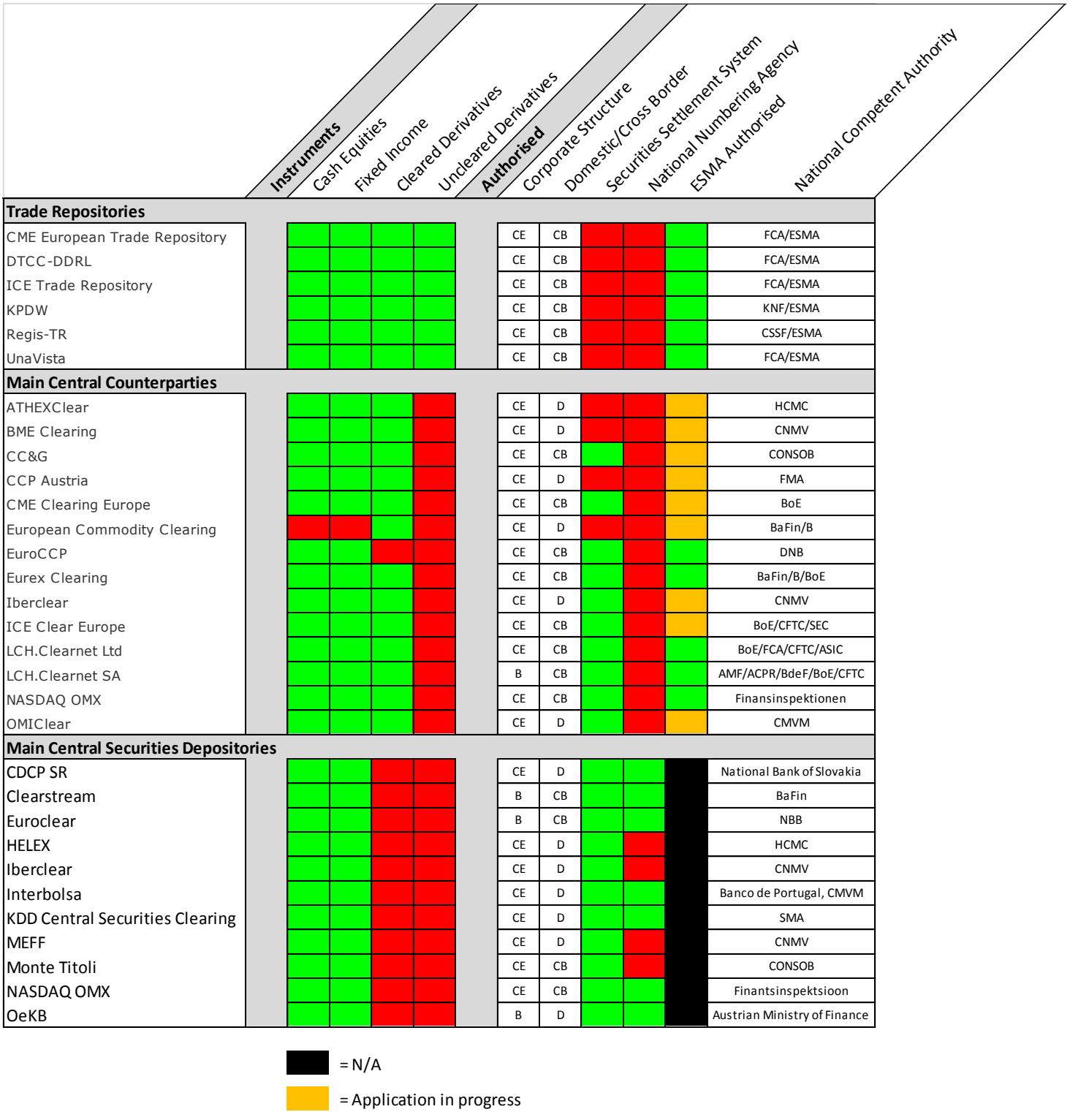
Overview

Europe's financial market infrastructure potentially offers a number of options for a centralised approach to EU FTT collection. In addition to the reporting mechanisms introduced under MiFID, we have considered the functions performed and asset classes supported by the authorised Trade Repositories (TRs), trading venues, CCPs and CSDs. The geographic nexus of Europe's FMIs is complex; combining the domestic and cross-border services of both small entities and large groups; headquartered in Europe and overseas.

FMIs operate in all 11 PMS, however, our analysis of the entities authorised to provide market infrastructure services confirms that there is no single entity or group currently supporting all asset classes and with the national coverage required to collect EU FTT.

Europe has historically had a complex and fragmented market infrastructure topology. As at 23 June 2014, the consolidated register of trading venues maintained by ESMA contained 254 different entities recognised under MiFID that support and service European equities markets. The ESMA register comprises 99 RMs, 143 MTFs and 12 SIs, with some market infrastructure groups operating more than one RM, MTF or SI.

Supporting these trading venues are a number of Trade Repositories, a deep cross border Central CounterParty (CCP) market with more than 20 entities; two significant (International) Central Securities Depositories ((I)CSDs) in Euroclear Bank and Clearstream, together with a diverse group of national Central Securities Depositories (CSDs). CSDs were originally established to serve national equities markets along geographic boundaries. A section of the EU FMI sector is highlighted below:



Key:
ACP - Autorité de Contrôle Prudentiel et de Résolution
AMF - Autorité des Marchés Financiers
ASIC - Australian Securities & Investment Commission
B – Banking licence
BaFin - Bundesanstalt für Finanzdienstleistungsaufsicht
BdeF - Banque de France
BoE - Bank of England
CE – Commercial entity – no banking licence
CFTC - Commodity Futures Trading Commission
CONSOB - Commissione Nazionale per le Società e la Borsa
CNMV - Comisión Nacional del Mercado de Valores
CMVM - Comissão do Mercado de Valores Mobiliários
CONSOB - Commissione Nazionale per le Società e la Borsa
CSSF - Commission de Surveillance du Secteur Financier
DNB - De Nederlandsche Bank
ESMA - European Securities and Markets Authority
FCA - Financial Conduct Authority
FMA - Austrian Financial Markets Authority
HCMC - Hellenic Capital Markets Commission
KDPW - Krajowy Depozyt Papierów Wartosciowych S.A.
KNF - Polish Financial Supervision Authority
NBB - National Banque Belgique
SEC - Securities & Exchange Commission
SMA - Slovenian Securities Market Agency

Vertical and horizontal business models have become more clearly defined over recent years; some of the larger market infrastructure entities are now participating in a multitude of cross-border trading, clearing, settlement and information services activity, while others have remained pre-eminent in a clearly defined segment.

Interoperability of market infrastructure

The fragmented nature of FMIs in Europe indicates that centralised approaches to EU FTT collection would need market infrastructure entities to work together.

CCP interoperability, for example, has existed for many years, cross border CCP-to-CCP links for equity, fixed income and derivative asset classes being recognised by the CPSS in its report into the interdependencies of payment and settlement systems (June 2008). The subsequent economic crisis limited further progress in CCP interoperability. Support for inter-CCP links, however, continues to evolve. In June 2013, ESMA produced its final report of the "Guidelines and Recommendations for establishing consistent, efficient and effective assessments of interoperability arrangements" for CCPs, as mandated under Article 54(4) of EMIR. This has been augmented by the Level 1 text released earlier this year for MiFID II and MiFIR, which sets out new requirements of open access to CCPs. Further details are expected to be provided in the Technical Requirements due later this year.

Not all CCP functions are harmonised. There are principally two different netting models used by CCPs across Europe, namely Trade Date Netting (TDN) and Continuous Net Settlement (CNS). CCPs have not harmonised onto one model and the respective models used differ between markets. This could create difficulties, in the handling of failures and the different recycling periods, when assessing EU FTT. Our analysis indicates that the assessment and collection of EU FTT is best performed independently of the settlement process. Consequently, it will not be necessary to consider at this point the differences between TDN and CNS.

For the purpose of completeness, it is worth noting that there is a category of recognised Clearing Houses that operate across Europe that are neither a CCP nor authorised under EMIR. These are supervised by their domestic regulator under the CPSS/IOSCO guidelines and are not considered to be of sufficient materiality for consideration in this report.

There are acknowledged demarcation lines between the respective entity types, particularly at the CSD level. The manner in which each national market and asset class is supported relies on a combination of local rules together with a unique network of bilateral and multilateral commercial relationships. An example of this is evidenced by the long standing CSD arrangements between DTCC, SegaInterSettle and certain European CSDs in respect of their Crest Depository Interest and Depository Interest activities.

When assessing Europe's current market infrastructure topology and potential EU FTT collection models, it is helpful also to consider the size and type of business that is transacted in each segment of EU securities markets. Given the various forms of financial instruments involved, each type of business has very unique features and these are borne out in the relevant market infrastructure entities operating in all except the bilateral markets.

Taking derivatives as an example, there are more than 20 CCPs operating in Europe with many seeking or having already secured EMIR authorisation and members of the European Association of Clearing Houses (see below diagram). Whilst CCPs operate

directly with their Clearing members and are aware of the identity of transacting parties at the point of novation, their primary function is risk management and risk mitigation. Consequently, it is not a natural service extension for CCPs to operate a tax collection service and neither market convention nor CCP rules provide for a CCP to publicly identify the participants to each side of a trade, other than as a specific regulatory obligation.

OTC Derivative CCP Clearing Solutions - Europe

Asset Class	Instrument Type	Status		Mandatory Clearing	CCPs
Credit	Single Name Corporate	🟢		TBC	EUREX, ICE CLEAR CREDIT
	Single Name Sovereigns	🟢		TBC	ICE CLEAR CREDIT
	Index (Untranched)	🟢		TBC	ICE CLEAR CREDIT
Interest Rate	Plain Vanilla Swap (Fixed/Float)	🟢		TBC	CME CLEAR , EUREX, KDPW,LCH, NADAQ OMX
	Inflation Swaps	🟡	H2 14	*	EUREX, ICE, CME
	Asset Swaps	🟡	H2 14	*	EUREX, ICE, CME
	Interest Options (Swaptions/Caps/Floors)	🟢		TBC	NASDAQ OMX
	FRAs	🟢		TBC	CME, EUREX, KDPW, LCH, NASDAQ
	OIS	🟢		TBC	CME, EUREX, KDPW, LCH, NASDAQ
	Cross Currency Swaps	🔴		*	None
	Zero Coupon	🟢		TBC	CME, EUREX, KDPW, LCH, NASDAQ
	Basis Swaps	🟢		TBC	CME, EUREX, KDPW, LCH, NASDAQ
Equity	CFD	🟢		*	LCH
	Vanilla Single Stock	🟢		TBC	HOLLAND CLEARING HOUSE, LCH, MEFF, NASDAQ OMX
	Vanilla Index	🟢		TBC	HOLLAND CLEARING HOUSE, LCH, MEFF, NASDAQ OMX
	Dividend	🟢		TBC	HOLLAND CLEARING HOUSE, LCH, MEFF, NASDAQ OMX
FX	NDF	🟢		TBC	LCH, CME
	CSF	🟢		TBC	CME
	FX Swaps	🔴		*	None
Commodity	Forward	🟢		TBC	CME, LCH, NADAQ OMX, ECC, MEFF
	Swap	🟢		TBC	CME, LCH, NADAQ OMX, ECC
	Option	🟢		TBC	CME, LCH

Source: CCP data, ESMA Clearing Discussion Paper 2013/925

Key :

- 🔴 No plans announced or known
- ⚪ Implemented and currently offered
- 🟡 In progress or expected

The type of business cleared by each CCP differs quite significantly, with the largest entities maintaining a strong market share of particular asset classes, i.e. swaps, short term interest rate products and long term interest rate products. Outside the derivative area, in the EU there are also 30 CSDs' products. Their functionality varies significantly. Europe's CSDs have a history of collaborating and of establishing mutually beneficial commercial arrangements to enable them to support their core markets. CSDR is opening this segment of the market up to increased competition at the same time as Europe's equities markets are harmonising to T+2 settlement periods and Target2S project is centralising settlement through the ECB.

It is evident from the research performed that no single existing entity or group of entities has all of the requisite components in place at present to provide the full coverage necessary for the collection of EU FTT. The FMIs have, however, a history of working together in order to meet market demands and address any absence within their own structure of certain services in key geographic locations.

Principle 20 of the CPSS-IOSCO Principles for financial market infrastructures (April 2012) sets out the key considerations for an FMI that establishes a link with one or more FMIs, including that they should identify, monitor and manage link-related risks. As a footnote to this principle, CPSS-IOSCO advises that FMIs in all link arrangements should meet the key consideration within Principle 18 of providing open access to other FMIs as a pre-condition for the establishment of links between FMIs of the same type.

Some CCPs and CSDs (including (I)CSDs) have a banking licence. Whilst this does not simplify the case for a centralised or new utility model, it further highlights the diverse and fragmented landscape within which FMIs collaborate and compete. This is complemented by a clear topology of links between Issuer CSDs and Investor CSDs, as documented by ECSDA on 7 November 2012 in respect of CSD regulation (Commission Proposal (2012)73).

The links that already exist between CCPs and CSDs are, in many cases, mature and support the central model. Consideration has been given to the mix of domestic and cross border FMI entities as well as to the existing relationships and eligible direct and relay links between CCPs and CSDs operating relevant securities settlement systems.

Recognising the possibility that EU FTT would require an "EU issuance" database that potentially maps NNA codes with ISINs, we have identified those CSDs that are members of the Association of National Numbering Agencies and have NNA responsibilities within the 11 PMS. The NNA capabilities within a number of the CSDs supporting the 11 PMS should benefit the central model.

Our observation concerning FMI is, therefore, while it is a potential asset to leverage from in the context of EU FTT, it has considerable variety by geography, functionality, operating model and asset class and therefore presents a complex environment into which to deploy collection methods.

7.3 Assessment of the leverage potential for EU FTT collection on existing and future transaction reporting

Approach

We have evaluated potential EU FTT transaction reporting requirements against existing transaction reporting requirements of the MiFID I and EMIR directives, as well as any future improvement arising from MiFID II reporting.

Having identified 34 subjects envisaged to be reportable to facilitate EU FTT collection and enforcement, we analysed them against transaction reporting requirements under MiFID I and EMIR. Each subject was scored in terms of how well that area is covered by the particular regulation.

Scoring scale:

	Good coverage	Some reporting changes required
	Medium coverage	Significant reporting and data collection changes required
	No coverage	Major changes required, incl. new data exchange mechanisms

As a result, the "Current overall" column shows a colour-coded interpretation of the subject gap between existing requirements and envisaged EU FTT reporting requirements, where the current coverage is interpreted as the best score out of MiFID and EMIR.

Further improvement points were awarded where MiFID II reporting requirements are expected to narrow the gap, therefore creating the "Future overall" rating. The extent of improvement is represented by +/++.

Results

	Coverage				
Field/Subject Name	**MiFID**	**EMIR**	**Current overall**	**+MiFID II**	**Future Overall**
EU FTT Specific Reporting Subjects					
Reporting firm identification					
Instrument identification (e.g. UPI)					
Derivative instrument descriptors					
Instrument type/classification				+	
Instrument issue place					
Transaction buy/sell					
Transaction trade type					
Transaction quantity					
Transaction price					
Transaction (notional) consideration					
Transaction currency					
Transaction capacity					
Transaction date and time					
Transaction status (new/modify/cancel)				+	
Counterparty identification					
Counterparty country of authorisation					
Counterparty place of registration					
Counterparty branch location					
Determined counterparty PMS of establishment					
Client identification				++	
Client country of authorisation					
Client place of registration					
Client branch location					
Determined client PMS of establishment					
Intermediary chain - counterparty identifications					
Intermediary chain - counterparty trading capacities					
Intermediary chain - deemed PMSs of establishment					
FTT amount/rate					
FTT exemption reason					
FTT payment date					
FTT PMS recipient					
Technical Reporting Subjects					
Transaction report matching reference				++	
Transaction report status				+	
Submitting entity details (if reporting on behalf)					
Average					

Conclusion on trade reporting

While existing reporting requirements provide good coverage of basic instrument, trade and counterparty information, effort will be required to facilitate reporting of intermediaries along the trade chain, their determined PMSs of establishment as well FTT payment information.

Furthermore, there is a real concern that some of the reportable data may not be readily available and additional inter-counterparty information exchange and cooperation mechanisms will need to be established ahead of reporting. This is particularly applicable to information on the ultimate client and along the intermediary chain.

MiFID II/R will likely bring substantial improvement on the availability of ultimate client information; however, gaps will still exist with respect to the establishing the client's deemed PMS of establishment.

It should also be noted that the successful determination of all client and intermediary information along the chain is dependent on full participation of all intermediaries. This applies to PMS, other EU as well as non-EU jurisdictions.

Conclusion on EU market and infrastructure

Having regard to our high level review of current market structure and the trend of future regulation, our observations are as follows:

1. Although it might be thought that future EU regulations over the 2014-2017 period (EMIR, MiFID II/R, CSDR, Liikanen etc) will provide a more consistent framework from which to build harmonized collection models, historical evidence confirms that markets will evolve dynamically in response to both client demand and regulatory and competitive pressure. In practice, there are significant market uncertainties that surround how trading venues, sizes, patterns and transaction flows will evolve ahead of regulation and technological advances. It will prove challenging to propose collection models while the "future state" for trading across the EU remains highly fluid and uncertain.

2. The majority of transactions in cash equities and exchange traded derivatives take place in such a way that the other side of the transaction, e.g. the other counterparty to the CCP transaction, is unknown to the first counterparty (cfr. table p. 44). Whilst other asset classes suffer less from this issue, the general trend towards centralisation will only increase the problem over time. As a separate point, the counterparties to CCPs are often not required to identify and distinguish own account transactions and transactions on behalf of ultimate investor. The design of the CCP arrangement means that there is no inherent need for the ultimate investor to be identified for credit risk purposes, since this is assumed by the CCP. However over time, we expect trade venues, both lit and dark, will be challenged to provide acceptable levels of transparency as to the identity of counterparties or ultimate investors/sources of funds.

3. Concentration of transaction processing in certain asset classes provides an opportunity to consider the centralised collection methods, as an identified

number of infrastructure firms process many taxable transactions. This provides an opportunity to promote industry standards and risk mitigation procedures, where data is reconciled with public bodies such as national competent authorities or other sources of legal entity data. However, it should be noted that at many points within the infrastructure the transactions processed are net transactions (often with a big gap between gross taxable transactions and net) and the counterparty data will often be with regard to financial intermediaries who are, for instance, exchange or clearing members, and not the taxable beneficial owners.

4. It follows that the challenge of deploying a central collection method within the current construct of market infrastructure participants (even against a static commercial and regulatory background) is significant.

8. Pros and cons of potential EU FTT collection approaches

8.1 Introduction

As explained in Section 6, a series of four potential collection approaches have been identified, ranging from a self-administered model where all FIs calculate, pay and report their own taxes to a model in which a limited number of authorised providers pay and report EU FTT (and potentially calculate liability too). This section of the report sets out the key features of these collection models and identifies potential advantages, drawbacks and challenges associated with each approach. It also takes into account the analysis of the key topics in Section 7.

8.2 Self-administered approach

Under this model EU FTT would be paid by each FI liable to FTT.

Potential advantages of a self-administered model are described below.

- Access to (pre-netted) information. The FIs liable to FTT will have access to information on their gross transactions which may not be available to, for example, central clearing and settlement infrastructure operators as a result of netting before settlement.

- Ability to support operation of intermediary relief and avoid potential multiple charges to FTT for the same transaction. If the fact that tax has been paid can be flagged by the first financial intermediary in a chain of intermediaries involved in a single transaction, this will support claims by subsequent intermediaries in that chain for intermediary relief.

- Comprehensive coverage. A self-administered model is in principle open to all FIs liable to FTT in respect of all in-scope financial transactions, whether OTC or exchange traded, whether or not centrally cleared/settled, intragroup or third party.

- Limited co-operation and co-ordination needed. This system also requires the least amount of industry dialogue and collaboration and therefore has the benefit of less co-ordination needed, at least to establish the system.

Drawbacks and challenges with a self-administered model include the following.

- Lack of validation for tax authorities. Under this model PMSs would have no aggregation/validation of EU FTT payable by the multiplicity of EU FTT payers, and would only be able to enforce compliance at the level of the individual FI. The collection system would contain no cross checks of its own to support compliance by FIs. That raises particular problems in relation to non-PMS FIs because of the lack of audit possibilities.

- Lack of any governance mechanism supporting certainty that the correct EU FTT is being paid. A self-administered collection model would contain no support or infrastructure to help FIs comply unless market providers emerge

to provide such services. This is particularly an issue in relation to the EU FTT support needs of FIs outside the PMSs.

- Prone to variation across FI/market participants. Differing interpretations of potential EU FTT liability would be likely with no third or central party involved in calculating or validating EU FTT collection. This would result in a potential destabilising of markets as a result of different market participants taking a different view.

- Joint and several liability risk. Given the lack of validation mechanisms from a collection model involving interaction with other FIs, this approach would carry significant joint and several liability risk for the FIs involved in taxable transactions.

- Geographic coverage. Although the model is likely to be easily understood by FIs globally i.e. it is their own responsibility to complete and collect tax, this model provides no inbuilt mechanisms to support and encourage compliant behaviour. All other models have such inbuilt features which will make it easier for FIs outside the EU FTT zone to comply.

8.3 Delegated collection approach

This approach could be used as a variant of the self-administered model or could be integrated in a central collection model, in which FIs liable to EU FTT would be able to transfer their payment and reporting obligations to another FI (or other service provider), along with any payment and reporting obligations they have themselves accepted from other FIs.

The principle of the delegation model is the transfer of collection and/or reporting responsibilities to another entity. This is most valuable for situations where:

- FIs are not in a position to collect EU FTT for lack of infrastructure to do so:

- where an FI may not have the information necessary to determine EU FTT liability; or:

- The FI does not have direct access to the central collection functionality, if any.

As such, the delegation model would essentially start with putting the responsibility on the FI receiving or initiating the purchase or sale or entering into a derivative but would make it possible to delegate this responsibility. PMSs could force or limit delegation for all or certain asset classes and qualifying delegates could be limited to FIs established in the EU FTT zone or in a country that has entered into some type of agreement with the EU FTT country or the EU (such as an Inter-Governmental Agreement).

With this approach, intermediaries involved are free to accept such responsibility for which they would need to receive the relevant data. Delegation will enable a degree of flexibility and allow the market to determine where best to concentrate the burden of calculation, reporting and payment. Thus, a delegation approach may also be suggested as a framework for accommodating the necessary flexibility countries may

want to deploy and it might equally be used to address certain enforceability challenges. Compared to self administration, asset managers and wealth managers are likely to favour this type of approach since they would typically outsource many functions concerned with the trade itself to the brokers they use to execute trades. It is also possible to consider delegation not as a separate model, but a design principle in other models to allow prescribed flexibility in the application of collection systems.

Potential benefits of a delegation model are described below:

- More flexible than a self-administered model. The possibility of delegating EU FTT collection responsibility to another FI would allow some flexibility (e.g. in relation to parties without the capacity to operate a self-administered model).

- Allowing accessibility, particularly for those FIs outside of the EU FTT zone. A delegated system might have the effect of directing EU FTT collection towards FIs located in the FTT zone. For instance, for trades undertaken between an EU FTT FI and a non-EU FTT FI, the non-EU FTT FI might chose to delegate to the EU FTT FI.

- Checks and balances involving market participants already interacting with each other. Parties and intermediaries in relation to a transaction will already deal with the next intermediary or other FI in the "chain" of transactions or intermediaries in relation to a single transaction, and delegation of reporting requirements to that person could be a source of data validation which could build certainty over EU FTT (and potential joint and several) liability.

Drawbacks and challenges with a delegation collection model include the following:

- Fundamental design challenges. The precise design of delegation would need to be thought trough so as to incentivise this model.

- Workability of a delegation model for tax payments made on settlement date EU FTT payment is required. Post trade processing of EUFTT may take longer than with self administration since information would be needed from third parties, this puts time pressure on getting accurate tax payments made in a timely fashion.

- Lack of clarity and certainty over EU FTT obligations. With a choice of whether or not to delegate collection obligations, there would be a degree of uncertainty for PMSs and potentially for FIs over who in fact is responsible. Complex audit trails would be needed to overcome this difficulty.

- Contractual bi-lateral requirements. Although this would be legal delegation proscribed in a Directive, we would envisage a contractual infrastructure would need to be built to support and maintain collection for those aspects not fully covered by the Directive.

- More prone to variation across FI/market participants compared to self-assessment. Delegating EU FTT responsibility could lead to additional variations across countries with certain FIs/intermediaries delegating responsibility and others not doing so. Unless delegation obligations (and consequences) were clearly set out in legislation, this could add significantly to operational and joint and several liability risk.

- Data privacy. This approach could require an FI to transfer not only its own data but also that of third parties for whom it has accepted delegated collection responsibilities. The necessary permissions for such transfers would need to be considered.

8.4 Central clearing or settlement approach

This model entails collection and payment of EU FTT under centralised clearing and settlement infrastructures. The clearest market comparison for this is the CREST system for UK SDRT. While many EU FTT chargeable transactions do not have central clearing and settlement (e.g. fund units in most markets, modification of derivatives) that would not preclude building on a CCP/CSD model for overall FTT compliance; for instance, CREST is used for SDRT compliance where no depository action is needed, apart from SDRT (e.g. so called "own account transfers").[10] In addition, the CREST system offers an SDRT assessment service called whereby trades Stamp Assessed Trades (SATs) can be sent for SDRT collection purposes when those trades are netted or settled outside CREST.

Potential advantages of a central clearing and settlement model are described below:

- Commercial incentive to comply. Even if "delivery versus payment" is not technically dependent upon tax being paid, there is a behavioural effect (as experienced in the UK) that results in an expectation of SDRT being accounted for in the CSD process.

- Central clearing is an increasing trend. In the US and Europe there is an established trend for centralisation of clearing, with many asset classes moving to this model. Therefore the scope for this model to cover transactions potentially liable to EU FTT is only likely to increase.

- Tax processing as part of central clearing/settlement could be relatively low cost. From a FI perspective, once the system build is complete, the central collection of the tax payment results in a simpler process with fewer additional steps (compared with the creation of an independent new utility, for instance). The low costs of collection of SDRT from the UK tax authority's perspective offers similar potential for PMSs, although SDRT's design is very different from EU FTT.

- PMS and Market confidence. The experience of SDRT in the UK is that a central collection system can give confidence to FIs that all market participants are subject to the same procedures, minimising potential market distortions. The CCP/CSDs could act as a transmission mechanism to the wider EU FTT taxpayer landscape by issuing central instructions,

[10] Under the CREST system, as with other CSD systems, FIs will typically hold shares as custodian for a third party beneficial owner. Where two different beneficial owners buy and sell shares, but both use the same custodian bank, typically this will be within one "omnibus" account at CREST. Apart from SDRT, CREST does not need to be notified where transfers are made within the same omnibus account. Such transfers are called "own account transfers". However, such transactions are notified to CREST solely so that CREST collects tax on these transactions together with those transactions that do require settlement at the depository.

standard templates etc. From a PMS perspective having data concentrated at CCP/CSD would facilitate audits and data analytic processes.

- Certification of trading platforms. A central collection model may provide for the opportunity to consider the introduction of "certified trading patforms", i.e. platforms that are certified by tax authorities of PMS (assuming algorithms are in place that ensure a proper identification of both tax liability and tax payment).

Drawbacks and challenges with a central clearing and settlement model include the following:

- Limited to EU FTT zone central clearing and settlement. It is hard to conceive that the central clearing and settlement model for EU FTT could be replicated outside the EU and possibly not even outside the EU FTT zone. If the EU FTT central clearers and settlement systems did embed EU FTT, at the very least their operating cost base would increase and this would put them at a competitive disadvantage. So, even where it may be technically feasible to impose EU FTT collection on central clearing (via CCPs) or settlement mechanisms such as CSDs, consideration would be needed as to the commercial consequences and the potential impact on European capital markets and the operational risks the CSDs would have to assume in collection with the EU FTT collection. Even within the EU FTT zone, there will be specialist asset classes (e.g. composite indices, CFDs or structured, illiquid or non-fungible asset classes) within the scope of EU FTT where market arrangements will likely remain over –the-counter (OTC) and therefore not warrant centralized clearing. However, as the introduction of the Stamp Assessed Trades services in the UK indicates, a central collection model operated by a CSD, may be designed such that it can handle transactions not settled through the CSD. It should even be possible to extend the scope of the EU FTT processing functionality to securities not eligible for deposit into the CSD. It is important to note in this connection that the degree of controls and validation of the EU FTT instructions will reduce in these cases.

- Cost to implement. The systems architecture between market participants and CCPs and CSDs involves many complex automated processes and the cost to reconfigure all of the many systems, front to back, to embed EU FTT within clearing and settlement will be significant. Therefore the cost and time to build is likely to exceed the self-administered and delegation models.

- The central party function may just be a "post box" and not add value. Although a central party is involved in some collection models, such arrangements can be little more than a central utility facilitating self-administration, relying completely on the input and information received from financial intermediaries involved. An example would be the Italian CSD role in Italian FTT collection. In order to justify the extra cost to build and to provide the confidence in the system which the CCP/CSD model potentially offers, there will need to be some design features of this model which adds value to the process of tax collection. These could include:

    - a provision to absolve market participants of joint and several liability if they use CCP/CSD tax collection,

- European Commission/PMS approval of tax rules engines thereby reducing tax risk (although many FIs will continue to have to use their own rules engines),

- central tax staff housed within CCP/CSD to facilitate compliance and provide central liaison with PMS on technical issues, and

- some degree of data matching/reconciliation.

- Netting. CCPs and CSDs transact on a net basis. As an example of the problems this causes, local custodians will typically settle on a net basis for their global custody clients. UK SDRT has dealt with this kind of problem with its "SDAS" solution as described in Section 4.

- Data transfer. A system of transferring data would need to be established. This may range from a full data set transferred to the CCP/CSD through to a flagging system used to tax trades in certain ways which, in effect, is an abridged data set. Data privacy issues would need to be solved for a system involving transfers of data to third parties.

8.5 New utility approach

The new utility model would involve a service offered by a series of authorised providers to pay and report EU FTT, and perhaps calculate primary liability since the utility would have access to detailed data. An equivalent model exists in regulatory reporting, for instance, with Trade Repositories under EMIR; indeed the new utility could be an augmentation of an existing transaction reporting utility. The service would be offered to all FIs potentially liable to EU FTT. The utility could have a tax rules engine which could be validated by PMS.

The utility would require FIs to submit data to it using standard templates. The utility model could have global accessibility by having national/regional facilities and resources outside the EU. As a potential incentive for compliance, FIs supplying data to the utility could be exempted from joint and several liability on the condition of supplying accurate data.

Potential advantages of a new utility model are described below:

- Facilitation of compliance. A new utility offers the potential for matching and aggregation of data which could support compliance by FIs (by providing validation of EU FTT liability) as well as audit by PMSs (which would be able to interact with a relatively small number of organisations with high volumes of data). Additionally, if PMSs approve the rules engines then the key compliance risk would then lie with the provision of accurate data, not with rule interpretation. Having a database of FIs that participate in the central utility model could itself support compliance as it might become market convention to trade only with FIs that have a utility identification number, perhaps using the outputs from the Legal Entity Identifier project.

- Cost/benefit analysis. Most FIs will continue to build their own tax rules engines in order to calculate EU FTT. The utility model will result in additional costs over and above this and being separate from the cash flows

on the transactions themselves will create additional operating costs. However, these costs could be justified if the overall system provides benefits to the compliance environment such as consistency across markets and reduced risk of audit or joint and several liability risk.

- Leverage of existing and future transaction reporting. FIs are used to daily reporting of their trades (normally, within a few minutes to trading venues) which are then "enriched" to form transaction reports (normally, end of day to market regulators). This is an increasing requirement globally (e.g. through Dodd-Frank, EMIR and MiFID). If EU FTT compliance could be aligned with daily reporting this could add efficiency gains, and even though EU FTT design will clearly require extra data fields to be created and populated this may be an easier task than to create a new reporting engine specifically for EU FTT. (See Section 7 above where we consider the scale of this gap).

- Market standardization. Given the formidable challenges for FIs in establishing their primary liability and the likelihood of increased uncertainty as the rules get transposed into local market practices and legal systems, any central utility which could provide objective determination without liability has the potential to offer consistency, reducing risk for market participants and helping to facilitate more stable markets. Similarly, managing data reporting with standard templates would reduce complexity and market uncertainty compared to other models where reporting of EU FTT within the system would otherwise become very fragmented. (Individual FIs would remain principally liable for their own EU FTT calculation, but if the utility had its own rules engine too, this would allow a reconciliation to take place and discrepancies identified).

- Global accessibility. The burden of EU FTT compliance becomes even greater outside the EU where the framework of the Directive becomes harder to understand, since it draws upon EU financial market regulation. However, most markets have daily transaction reporting and are using the trade warehouse concept. Adding EU FTT to an existing business process, such as transaction reporting will facilitate compliance. However we note that very few businesses that offer transaction reporting services do so on a global, comprehensive basis.

- Comprehensive product coverage. Unlike the CCP/CSD model, the utility could be applied across all products/asset classes and therefore will be able to process tax collection across all categories.

Drawbacks and challenges with a new utility model include the following:

- Feasibility of data matching. It remains to be seen whether data matching is feasible for the volumes and range of asset classes covered by EU FTT. Although compared to the CSD/CCP model, a new utility is arguably in a better position to cope with complex rules, given it will have gross data, the lack of primary rule simplication will still be a considerable challenge.

- Multiple data input points. Although the utility would carry out the EU FTT calculation process, it will only be able to do this based on data obtained from FIs involved in the transaction. To avoid imposing extensive reporting obligations on FIs not already involved in this volume of transaction reporting, it will be necessary to build in flexibility for financial

intermediaries to be able to report on behalf of other FIs involved in a chain of transactions or intermediaries in relation to a single transaction.

- Economic model. The funding of building the utility or series of utilities needs to be considered. There are key questions over whether the build cost of a new utility might exceed the value that would add, bearing in mind that many FIs would themselves wish to build rules engines to inform front office pricing on EU FTT and reconcile their own calculation with the calculation made by the utility. At this stage, it is also difficult to predict who might take on operation of such utilities or how a competitive market would be established so that FIs can choose a utility that best suits their circumstances.

- Competent authority framework. A new utility is potentially facilitated by the existing regulatory competent authority frameworks, under which local financial regulators have direct or indirect access to transaction data (e.g. Approved Reporting Mechanisms under MiFID). It is not obvious how such competent authority networks could be leveraged for EU FTT by PMS tax authorities beyond the PMS themselves.

- Wide scope of the proposed EU FTT. Certain transaction types that are subject to the proposed EU FTT have little current or prospective trade or transaction reporting (e.g. intragroup transactions) or requirements which are less extensive than EU FTT (e.g. in relation to collateral), as a result of which the opportunity to leverage certain types of existing reporting through the utility model may be limited. Outside the EU, the transaction reporting environment varies significantly. Even within the EU, the scope of the proposed EU FTT will require a more comprehensive set of data to be reported and the rules engine will be more complicated than at present. These features mean that the build cost on top of existing transaction reporting will be significant.

- Timescale. The utility model would only be desirable if it can deliver a robust, strategic solution to the EU FTT collection challenge. Commensurate with the ambition to design, build and test such a model globally comes with an increased timescale to deliver, which would be expected to be longer than for other models.

- Confidentiality concerns. Data privacy legislation may constrain the ability of FIs to pass taxpayer confidential information to third parties, including a new utility.

- Access to cash. If the utility is not a FI it may not be able to collect the EU FTT once it has determined the EU FTT primary liability because it would not have access to cash accounts which it can debit. This means that the actual payment of the tax would be more complicated.

8.6 General market reaction to collection approaches for EU FTT

Although we have conducted a range of interviews with market participants this section should not be seen as an authoritative and exhaustive statement of industry views. It is based upon the 50 or so FIs we have informally consulted with during our

study. The views across these FIs about the viability and desirability of particular collection models varies, but general trends can be identified. As mentioned in Section 2 participation in this study should not be seen as implicit or explicit support for the EU FTT itself.

Smaller financial institutions, funds and asset managers, particularly those with outsourced business models, are likely to look to existing providers of operational support services (transfer agents, broker/dealers, custodians) to take on any new EU FTT payment and reporting tasks for them. This suggests that they want to be offered the possibility to delegate their EU FTT compliance obligations to an agent. Furthermore, many FIs do not have direct market access to CSDs/CCPs and do not have the existing functionality to connect systems to these institutions.[11]

Almost irrespective of the type of collection model, banks, especially those that are broker/dealers will need to build and deploy large scale systems and processes to deal with EU FTT. Their existing solutions for Italian and French FTT are "tactical" i.e. not built into the core systems architecture and the imposition of EU FTT would in most cases necessitate a strategic solution to upgrade systems and processes in order to ensure their systems can cope robustly with high levels of transactions in an STP environment. Therefore broker/dealers will need to:

- Establish strong front office solutions for EU FTT pricing, and
- Ensure they have capability to reconcile EU FTT costs with their trading transactions

A significant amount of EU FTT capability would need to be built irrespective of the collection mechanism chosen. So for these types of FI, the principal task of liability calculation would be undertaken at firm level and therefore centralisation of collection does not alleviate the cost or complexity of this task.

Notwithstanding this, banks and broker/dealers are generally likely to prefer central collection methods if the potential additional build costs can be outweighed by reduced risks and market standardisation.

Infrastructure providers are likely to be particularly concerned that the data they hold for current processes is increasingly netted and inadequate for the task of calculating and reporting on EU FTT. As well as having only net data, CSDs and CCPs will typically not have the beneficial ownership data required for FTT purposes. There is an increasing disconnect between the transactions which infrastructure process and the legal beneficial owner transactions which are the source of primary liability. If central

[11] For example, the French FTT rules determine that as long as there are two (or less) intermediaries between the accountable party (for French FTT purposes) and Euroclear France, the FTT collection process must go through Euroclear France. However, if there are more than 2 intermediaries involved: (i) the accountable party (for French FTT purposes) must send its declarations and pay the FTT directly to the French tax authorities (collection through self-assessment), or alternatively (ii) the accountable party is allowed to declare and pay the tax through an Euroclear France member to whom it provides directly or indirectly the relevant information (collection through delegation). If the latter option is chosen, the given Accountable Party must inform the French tax authorities of this option through a dedicated declaration. This declaration is valid for one year and is considered implicity renewed (if not expressly repealed). The tax declaration process will follow the standard procedure as of any other accountable party declaring through a Euroclear France member. No specific tax audit will be performed by Euroclear France on the existence of this declaration. As such, the above mentioned rules for French FTT collection illustrate how a combination a centralized approach to collection can involve both collection through self-assessment and delegation as to allow flexibility.

infrastructure is considered an appropriate place to house EU FTT collection, then the remoteness of infrastructure to the end client is a significant challenge. Notwithstanding this, the UK SDRT collection mechanism operated by Euroclear UK & Ireland does show potential as a model for infrastructure based tax collection.

Given the fragmented nature of Europe's financial market infrastructure (resulting in a number of options for centralised approaches to EU FTT collection), one can conclude that market infrastructure entities will necessarily have to work together with no single existing entity or group of entities having all the requisite components in place to provide the full coverage necessary for the collection of EU FTT.

9. Mitigating certain collection challenges

9.1 Introduction

Although there are also some fundamental changes which would improve collection, such as rule simplification and elimination of the counterparty rule, etc, these would entail significant changes to the primary rules, which might occur for other reasons than to facilitate tax collectionIt is not in our terms of reference to suggest major changes to the primary rules in order to improve tax collection.

However, in the course of our analysis we have also identified certain tactical opportunities. These opportunities, which are described below, may represent partial solutions to some of the challenges we have listed in Section 4 above and may not require significant changes to the draft EU FTT Directive.

9.2 Gross vs net (Challenge 4)

Introduction

We specifically listed in Section 4 the fact that taxing gross transactions is a challenge because financial markets have many processes which occur on net transactions.

The availability of gross data tends to reduce along the path to central functions such as clearing, settlement and custody. As a result this is a particular problem for centralised collection methods. Local FTT regimes, such as the UK's SDRT, have faced such challenges and we have examined their experience as follows.

How does UK Stamp Duty Reserve Tax "SDRT" cope with transaction netting?

Where a large number of securities transactions are entered into on a daily basis between the same parties, it is common for these trades to be netted off before they are settled in "CREST" (CREST is the UK's central securities depository). Although Euroclear UK & Ireland has until recently acted as a netting agent in the UK, in the last several years market participants have increasingly opted to net trades outside of CREST. Where such netting is occurring, CREST (which receives only the net settlement instructions) is unable to accurately handle SDRT collection and reporting since, while SDRT is due on gross transfers (strictly, the tax is payable in respect of each agreement to transfer chargeable securities), CREST would only be 'seeing' net transfers.

Concerned that netting of trades outside CREST could be causing under-reporting and under-payment of SDRT, HMRC consulted with the market for a solution which would provide greater assurance to HMRC that SDRT was being correctly assessed and reported. The result of that consultation was that Euroclear UK & Ireland has introduced from June 2014 a new interface over which gross trades are sent to CREST for SDRT assessment, reporting and payment. Such trades can still be netted outside CREST and sent for settlement (on a netted basis) in CREST: the (net) settlement is instructed separately from the (gross) 'stamp duty assessment service' ('SDAS') reporting.

Initially SDAS will be for trades using CCP settlement netting models, since these currently make up most of the netting occurring outside of CREST. When SDAS goes

live (expected to be June 2014), HMRC will require financial institutions using CCP settlement netting to report their gross transactions in chargeable securities using SDAS. However, HMRC is aware of other post-trade aggregation and netting models which do not involve the aggregation or netting process being undertaken by a CCP. HMRC is planning further consultation and development work to enable financial institutions using such other models to report gross trades by means of SDAS. Certain transaction types, such as stock loans, will be outside the scope of SDAS and trades in SDRT-exempt securities (such as most bonds) should not be sent via SDAS to avoid SDRT being assessed and collected where in fact no tax is due.

SDAS data flows and reconciliation

In SDAS, gross trades on a one-for-one basis - Stamp Assessed Trades ('SATs') – are bundled into files and sent over the new interface to CREST. The SATs are assessed for SDRT in CREST: where SDRT is payable, Stamp Payment Transactions ('STPs') are generated to collect the tax (as is the case currently for gross trades settled and reported in CREST). The settlement instructions (which could be on a net or gross basis) are sent separately to CREST. To avoid any element of SDRT double-charging, the settlement instructions needs to be marked with a special Transaction Stamp Status ('TSS') flag - "No SDRT liability or Irish Exempt, Net/Aggregate Transaction or Assessed Elsewhere" - which is introduced to ensure SDRT is assessed and paid only in respect of the SATs and not also in respect of the separate settlement instructions.

Since both the SATs and settlement instructions must be sent to CREST for correct SDRT assessment to take place, CREST seeks to reconcile each SAT with each settlement instruction that carries the special TSS exempt flag. Specifically, the net stock quantities of SATs and settlement instructions are put forward for reconciliation where the Participant ID, Member Account ID, ISIN, Intended Settlement Date and Dealing Capacity match.

HMRC receives overnight reports of settlement instructions, SATs and STPs as well as reports of any failed reconciliation daily from the intended settlement date until it is archived 60 days later. In any event, any failure to reconcile does not affect the SDRT assessment or settlement functions in CREST: SDRT assessment, settlement and reconciliation will run independently of each other.

Existing SDRT functionality

SDAS applies in addition to the existing SDRT functionality in CREST. Consequently, trades which are sent to CREST on a gross settlement basis with no SDAS reporting continue to be assessed for SDRT in CREST in exactly the same way as was the case before. Further, non-settling own account transfers remain available for participants who use CREST to report and pay SDRT where there is no relevant settling transaction. Note that, in any event, CREST does not perform detailed reconciliation of trades to compare SDRT paid with what 'should' be paid according to the SDRT legislation. For example, if participants incorrectly report a trade by flagging it as exempt from SDRT when in fact SDRT is payable, CREST generally accepts the trade as exempt (even though, as a matter of SDRT law, SDRT is payable) and whichever participant is the 'accountable person' for SDRT purposes remains responsible for identifying the error (e.g. through its own internal reconciliation procedures) and reporting and paying the tax due to HMRC.

Implications for proposed EU FTT

The SDAS example indicates that the practical experience of a gross transaction tax system is that it struggles to keep up with market developments and the desire of market participants to do their own netting and avoid the additional costs of sending instructions and executing gross transactions.

However, it also shows that with careful planning and close co-operation with industry participants, workable solutions can be developed over time to continue to support robust tax collection.

9.3 Intermediary Relief (Challenge 9)

Introduction

The draft EU FTT Directive contains a limited form of intermediary relief (Article 10 (2)). However, as explained in Section 4, … the wording of that relief will make it difficult to apply in practice.. The principal difficulty is that each FI has to establish, for each of its markets and for each of its third party relationships, whether it is "acting on behalf of another FI?". One issue that this faces is the different market practices for intermediaries: the wording is most clearly appropriate for pure agency relationships but this is less appropriate for other intermediary models like "riskless principal".

Under the current wording, it will be difficult in practice to run the relief operationally. This section considers whether there are changes to the intermediary relief which could simplify its operation.

Alternatives to intermediary relief

The practical operation in conjunction with the counterparty principle is likely to be a challenge. Brokers and other FIs intervening in a sales transaction in practice often act as undisclosed agents or as principals vis-à-vis their counterparties whilst the securities are not their own. The intermediary relief is applicable in those circumstances where the financial institution acts for the account of another financial institution. The relief is likely to be ineffective to eliminate the cascading effect. Because a financial transaction is often settled through a chain of intermediaries, the effective rate of FTT will thus likely be significantly higher than the headline rate in spite of the intermediary relief unless the notion "intermediary" is clarified such that FIs are not subject to FTT when the securities involved in the transaction are not treated as their own and that the profits or losses resulting from the transaction are not their own either.

Alternatively, the rules could simply provide that FIs are only liable to FTT when they are either (i) receiving an instruction to buy or sell securities from a person/entity that is not an FI or, (ii) when they are acting as a buyer/seller. Here again, it is key for FIs that are acting as an intermediary are not treated as buyers or sellers even when they are not disclosing their underlying customers. The difference between this suggestion and the intermediary relief contained in the current draft of article 10(2) is that no relief must be invoked and that each FI can determine its EU FTT liability without

having regard at the next or previous FI in the chain. Regard must only be had at the FIs own status when it acts as a buyer or seller or at the status of its client when the client is not an FI. The compatibility of such a mechanism with the counterparty principle must be considered.

Because the buyer/seller or the first intervening FI will be at the bottom of the chain of intermediaries, it would be best placed to verify whether or not the buyer/seller is exempt. It should then be able to pass on the information regarding the EU FTT status of the transaction by way of a transaction flag or otherwise up to the central collection mechanism or on a tax return. That transaction flag would be determined by the status of the buyer/seller and would not change throughout the chain subject to the need for verifying the application of the counterparty principle as laid down in article 4(1)(f). The application of that principle and ensuring that this information reaches the first FI in the chain is a challenge that will complicate the operation of this process, as previously mentioned.

The disadvantage of using a first FI rule whereby subsequent FIs can claim an exemption is that it may be challenging in theory to combine this rule with a central FTT collection mechanism because there are likely to be many instances where the first FI does not have direct access to the collection mechanism. In the case of the UK SDRT that does, however, not seem to a real problem, in particular because CREST now also permits non settling instructions to be sent for SDRT purposes only.

The question can be raised whether "reversing the picking order" to make the last FI liable for the payment of EU FTT instead of the first intermediary would be a good alternative to intermediary relief. The advantage of such rule would mainly be the fact that the last FI in the chain is more likely to be directly connected to the FTT collection mechanism. This is however usually not true in practice because the last intermediary is often not involved in the trading chain but merely acts as a custodian and would under the current proposal not be liable to EU FTT. It seems not a good a idea to change this because the FI would generally not be able to independently determine whether EU FTT is due or not. The FI could however be made accountable for EU FTT relevant instructions it inputs into the FTT collection mechanisms but this should not be linked to the intermediary relief issue.

Although other models of intermediary relief are possible, the practical problems associated with operating intermediary relief may only be adequately dealt with through entity exemptions. However, we would regard this as a major change to the primary rules, notably as this might substantially erode the tax base.

9.4 Global enforcement and the issuance principle (Challenge 13)

Introduction

The fact that the proposed EU FTT Directive includes an "issuance" principle, gives EU FTT a global reach, just like some domestic FTTs currently in place, for example the UK SDRT. With this global reach comes the need to ensure global collection and enforcement.

How does SDRT cope with collection for non UK transactions?

As a matter of law, SDRT has global reach in the sense that SDRT arises on agreements to transfer 'chargeable securities' – broadly, shares and certain other securities (such as convertible bonds) issued by UK companies or issued by non-UK companies but registered on a UK register or paired with UK securities – irrespective of the place of that agreement. Although a purchaser, wherever located, is liable to pay the tax, in practice enforceability becomes harder where UK shares are traded outside the UK. Although total compliance will not be achieved in practice, there is a mechanism that tends to encourage non-UK entities to pay SDRT, namely the concept of 'accountable person' (typically a broker, custodian or other financial intermediary acting for the purchaser or, in some cases, the seller), linked to the fact that the vast majority of UK-issued shares in publicly-traded companies ultimately will be held through CREST, means that a UK-based broker or custodian (even if this is a UK subsidiary or branch of a non-UK financial intermediary) will generally be involved in settling a trade and will therefore seek either payment of SDRT or a declaration that a specific exemption applies.

In addition there is a 'higher rate' SDRT regime (1.5%) for transfers of chargeable securities to non-UK clearance services or depositary receipt systems (however, we note that this 1.5% charge is the subject of current legal challenge – previous CJEU and UK court decisions have ruled that the charge is unlawful in relation to new issues, but, subject to legal challenge, HMRC continues to collect the tax on transfers of existing securities).

Installing a similar mechanism for EU FTT

Lessons can be drawn from the UK SDRT example, as EU FTT faces the same challenge in relation to financial transactions entered into by non-PMS FIs involving financial instruments issued within the EU FTT zone (i.e. coming within the scope of EU FTT by virtue of the 'issuance principle').

A potential solution for situations where PMS clearance services or depositary receipt systems are involved, is to require these systems to have the obligation of collecting the tax. In other situations, for example in case of a non-PMS CSD settling PMS issued securities that are cross listed or settling a trade in PMS issued securities on its own books for two of its non-PMS members, trades could remain outside the given PMS' enforcement net in case no specific measure are taken.

Higher rate or bilateral collection agreements

As part of EU FTT enforcement mechanisms, one could consider introducing a system similar to the UK SDRT (provided the existing and potential legal challenges can be overcome) with a higher rate to be applied every time PMS issued securities are transferred to a non-PMS clearance services or depositary receipt system.

Mitigation of such higher rate could then be organised by allowing non-PMS or non-EU clearance services or depositary receipt systems to enter into bilateral agreements in which the agree to set-up a proper system for EU FTT collection itself (i.e. outside the EU FTT zone) and to ensure proper EU FTT collection and its corresponding payment. In return, the given financial transaction or transfer of securities should not face the detriment of the higher rate (only the standard EU FTT rate being applied).

In general (apart from the rate mitigation suggestion), offering insitutions outside a given jurisdiction the possibility to engage in voluntary compliance (assuming certain non-domestic tax collection responsibilities) via a system of bilateral agreements is not new to the tax world. For example, for purposes of the US 'Qualified Intermediary' (QI) system, financial institutions outside the U.S. can assume US tax responsibilities after having entered into an agreement with the IRS (after which the responsibilities it carries out will be subject to recurring review and audited).

9.5 'Counterparty' identification (Challenge 3)

The need for counterparty identification has been further developed and touched upon in Section 7 both from a markets perspective (7.1) and from a regulatory reporting point of view (7.3).

Unlike other transaction taxes, the proposed EU FTT is in many case affected by the identity of the counterparty. For instance, non-EU FTT FI's may be brought into tax if their counterparty is an EU FTT zone person, EUFTT zone FI's need to identify counterparties if they are responsible for paying their counterparty's EU FTT, etc.

However, in many parts of the financial markets, particularly Regulated Markets and MTFs, the legal counterparty is the CCP. If PMSs want to adopt an interpretation of the draft EU FTT Directive which requires an FI to "look through" the CCP to the other counterparty of the CCP, then this function could only be performed by the CCP. Both pre and post trade, the FIs are not identified to each other but the CCP is in a position to match the trades. So, particularly for cash equities and exchange traded derivatives it would make sense to utilise CCP/CSDs to facilitate EU FTT collection, if this "look through" principle is to be retained.

However utilising CCPs/CSDs in this way is not without difficulties. For instance, pre trade, FIs will need to know whether their trades are going to be with an EU FTT chargeable FI or not to ensure correct pricing, This as a key market issue separate from collection per se. The netting issue for which a solution has been found for CSDs post trade (CREST SDAS above) would need to be considered pre trade and a solution developed. Also since FI's who are members of exchanges are often acting as executing brokers and may be able to take advantage of intermediary relief, and may not be "parties to the transaction" further complicating the question of counterparty identification.

Nothwithstanding these difficulties, exchanges, CCPs and CSDs seem to offer opportunities to match data on both sides of a transaction and this could be valuable for the counterparty rule and for other EUFTT purposes like joint and several liability.

10. A comparative analysis of collection models: towards an overall system

This section is a summary of the detailed analysis we have undertaken to consider the *relative* merits of the theoretical collection models. It also indicates a way forward for an overall system as a basis for further analysis. We have organised our analysis by asset class.

The methodology has been:

- Firstly, establish a list of evaluation criteria to test the models (recognizing this is not a full list of relevant criteria),
- secondly, consider and analyse a range of collection approaches,
- thirdly, test the collection approaches against the evaluation criteria for different asset classes, and
- finally, provide an overall assessment of the conclusions from the testing.

Our approach in this section should not be seen as a scientific method, it is really a framework through which we have organized our thinking and the observations made by market participants.

In determining the outcomes of this process we have judged each outcome as follows:

Relative to other models:

- Many potential barriers with limited potential options to overcome them.
- Limited potential to achieve desired outcome.
- Obstacles are on balance, highly material.

Relative to other models:

- Some potential barriers with some potential options to overcome them.
- Partially meets desired outcome.
- Obstacles remain but are less material.

Relative to other models:

- Few barriers and where barriers exist there are potential options to overcome them.
- Meets or almost meets desired outcome.

Analysis not applicable.

Clearly the proposed Directive covers many potential asset classes and within asset classes there will be variations of taxable transactions.

In our work we have tended to focus upon the most widely applicable asset classes: namely cash equities, fixed income, cleared derivatives and uncleared derivatives. However, even within these categories there will be EU FTT taxable transactions which may result in a different assessment for each criterion, so, for instance collateral transfers in fixed income, stock lending in cash equities or contract variation in derivatives.

Our analysis below concentrates upon the basic common commercial transactions and not these important variations.

In addition, we recognise that there are many other asset classes such as ETFs, fund units, intra group transactions that are not addressed by the analysis in the table below. In the course of our work, though, we have been mindful of the breadth of the proposed Directive and that different asset classes present different challenges. Much of that is reflected in the analysis in the rest of the report.

The below table considers how each of the theoretical collection models stack up against the four chosen asset classes against a range of criteria. We will not explain the criteria here since they are hopefully largely reflected in the "challenges" section 4 above.

The below table re-presents the data from the previous table but does so in a form which more readily shows both:

- which model looks most viable for an asset class, and
- which model looks most viable across asset classes.

In this respect the subsequent table gives a sense of how much harmonisation is feasible against a range of asset classes.

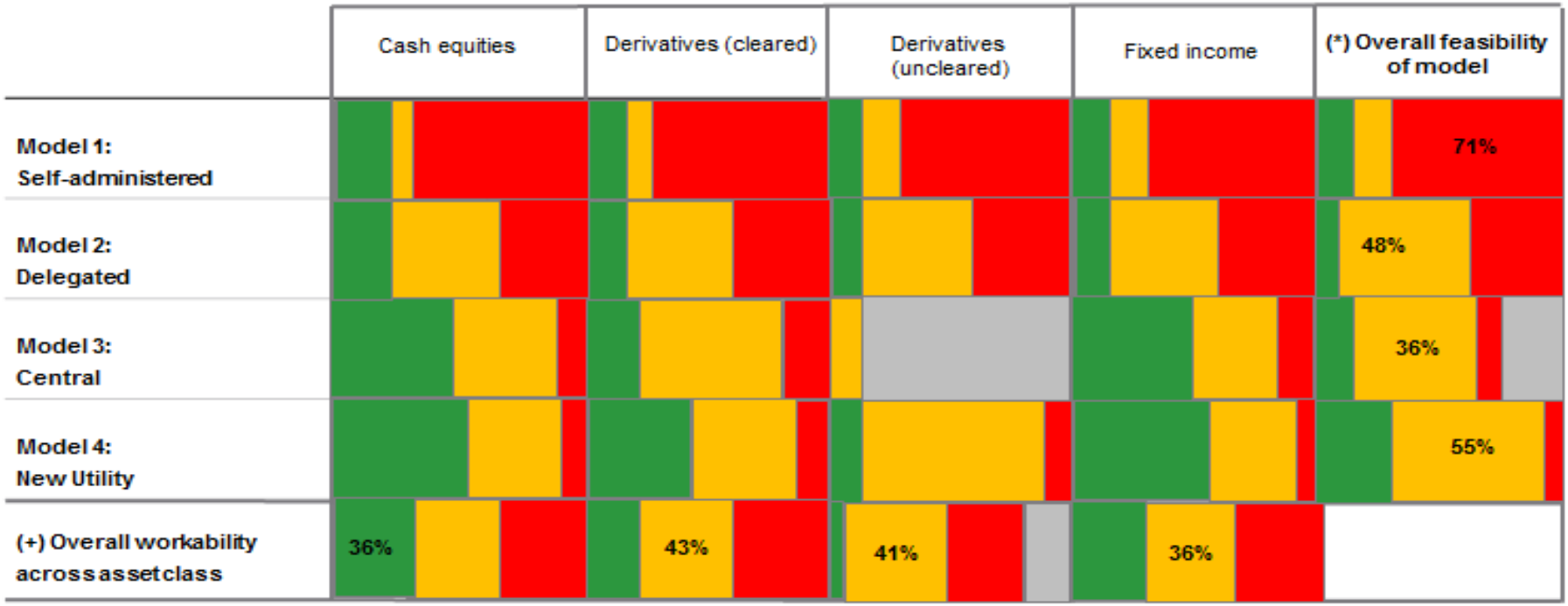
Comparison of models against design principles

	Model 1 Self-administered				Model 2 Delegated				Model 3 Central				Model 4 New Utility			
	A	B	C	D	A	B	C	D	A	B	C	D	A	B	C	D
DP1 - Alignment with data processes and reporting																
DP2 – Operational risk mitigation																
DP3 - In-built capacity to reduce tax risk																
DP4 - Alignment with cash flows																
DP5 – Minimisation of collection and reporting points																
DP6 – Harmonisation across geography, asset classes and execution venues	not materially model or asset class dependent															
DP7 - Maximisation of process automation																
DP8 - Global accessibility																
DP9 – Alignment with current market practices																
DP10 – Simplicity and clarity of collection procedures	not materially model or asset class dependent															

Key
A – cash equities B – derivatives (cleared) C – derivatives (bilateral/uncleared) D – fixed income (OTC)

Assumptions
- Model 3 assumes the use of a CSD for cash equities, CCP or trade repository for cleared derivatives and a CSD/ICSD for fixed income. Bilateral derivatives do not clear via a CSD or CCP as in their nature are uncleared.

Comparison of models – overall feasibility



(*) This column reflects the feasibility of each model as a whole when considering that the model would need to operate across all four asset classes. The percentages reflect the majority percentage for each model.

(+) This column reflects the capacity of any given model to work for each asset class. The percentages reflect the majority percentage for each model.

10.1 Relative collection model assessment across asset classes

Our assessment of this data can be explained as follows:

Cash equities

The facts we are envisaging for cash equities are listed equities, traded on PMS exchanges utilizing CCPs and cleared through PMS CSDs. In such markets direct market access is typically confined to broker dealers who act using various models such as pure agency, riskless principal and proprietary trading.

Trade venues vary and include multi-lateral trading facilities, dark pools and other regulated market structures. The buyers and sellers in this market will include pension schemes, hedge funds, UCITS funds and private investors.

The project to rationalize cross border settlement of securities, Target 2 Securities, is an important feature to bear in mind.

Turning to the models for collection, if cash equities tax was self-administered, then, given that broker/dealers and buyers and sellers all have banking arrangements to facilitate cash equity settlement, those arrangements could be used to pay EU FTT. However payment arrangements are currently often configured to occur within the CSD Delivery Versus Payment process. Therefore not using the same process to pay the tax as one used to settle the transaction is relatively inefficient.

Under a self-administered model for cash equities, there would be relatively more operational risk since there would be no external systems to support counterparty reconciliation, nothing to help manage joint and several liability risk and there would be a general concern that the treatment of an FI's transactions may prove to be out of line with other market participants. Without any check on their systems until a tax audit, there is potential for significant tax risk to accumulate.

Similar considerations are behind our assessment of "red" for the categories of "auditability", "alignment with reporting regimes" and "capacity to standardize market practices". While self-administration is of course globally available, by providing no support to facilitate compliance, we would regard it poorly when it comes to "global accessibility".

If the delegation model is in use for cash equities, then in general, we don’t see a great deal of difference between self-administration and delegation, against these criteria.

Because broker/dealers and custodians would probably be taking on more collection tasks under this model, there would be fewer participants operating EU FTT collection and greater visibility between participants on EU FTT treatments being adopted. This would be a positive result from a market standardization perspective and increases the auditability of the system from a PMS perspective. There would be better potential to manage joint and several liability, particularly for the person to whom delegation has happened.

However, the effective use of delegation may depend on the circumstances (either within a PMS or more globally).

When we consider centralization and how effective that might be for cash equities, we are entirely relying on a hypothesis – the functionality of the central function is as yet unknown. Notwithstanding that, we can foresee benefits of centralization even for limited centralization, as exhibited by CREST. CREST gives us evidence that market practice can be standardised through a CSD tax collection process, it can have reconciliation features and is auditable. This is the case at least when the chargeable transaction is instructed for settlement. In case of transactions that are settled or netted outside the central collection mechanism, the possibilities for audit and reconciliation will be more limited.

Having the EU FTT due as part of the DVP process can result in settlement breaks but the daily occurrence of exceptions allows quick remediation of any errors. We would grade this form of centralization low in terms of operational risk.

It is, though, not going to be available for EU FTT processing outside the EU FTT zone; hence it is "red" for global accessibility. It may be possible to develop a central collection mechanism that provides for access for all FIs wherever they are established. Alternatively, it could be envisaged that non FTT zone FIs access the collection mechanism indirectly by using an agent with direct access to the collection mechanism.

Fixed income

Turning to fixed income securities, the trading model for fixed income is more bilateral and often transacted with voice brokerage. However, the settlement and custody structures are similar to cash equities and as a result we do not grade fixed income any differently with regard to the criteria we have used. However, it should be noted that fixed income transactions are often not simple purchases and sales. Unlike cash equities, they are far more widely used to provide liquidity (via repos) and collateral. Depending upon the legal form of such contracts, they are subject to EU FTT. We have not considered in any detail the collection criteria for the models for fixed income transactions in these contexts. We would also note that while transaction taxes are common in cash equity markets they are not common in fixed income. Therefore the overall change programme to embed EU FTT collection will be a greater challenge than for cash equities.

Derivatives

With regard to derivatives, these present very different characteristics for the collection models.

Firstly, even after Emir, many derivatives remain uncleared and not traded on exchange platforms and therefore centralization is much more limited and only exhibited at the trade reporting level.

Secondly, there are limited cash flows at the inception of a derivative, normally only the initial margin is posted.

Thirdly, the taxable events within a derivative context may well happen very frequently, not on the derivative itself, but on the underlying collateral movements.

Finally, derivatives often have executing and clearing brokers but do not have central securities depositaries, so for centralization we are assuming using the CCP or the Trade Repository as possible FTT collecting agents.

So, for both cleared and uncleared derivatives, we see the same kind of limitations of the self-assessment model as we do for cash equities and fixed income.

Indeed, given the common practice to have derivative brokerage functions in the market, the delegation model provides similar collection benefits as we see for cash equities and fixed income.

The distinction between cleared and uncleared derivatives starts to become clearer when we consider central models. For uncleared derivatives, there is no central function, beyond reporting, that could be leveraged. Although uncleared derivatives have to be reported under Emir, given the lack of a central clearing function and a lack of market standardization in these products, we would envisage that a new utility function would find it harder to deliver benefits of auditability, market standardization and reconciliations compared to other asset classes. As with fixed income, derivatives are not normally subject to transaction taxes and therefore there will be greater challenges in embedding EU FTT collection.

10.2 Assessing costs for the models

Introduction

With respect to collection and reporting, and ignoring the broader commercial implications of EU FTT and the actual cost of the tax, there are two major sources of cost:

- set-up costs: the costs of implementing technology and processes to collect and report the tax; and:
- running costs: any maintenance and incremental cost of collecting and reporting the tax, once EU FTT is in force.

Cost would be incurred both by market participants and tax authorities. Both will be keen to contain costs.

The tax authorities will want to:

- maximise the yield from the tax; and:
- ensure the collection model itself does not have undesirable incremental effects on the competitiveness of FIs operating in their jurisdictions.

The market participants will want to minimise additional infrastructure, transaction and headcount costs.

FI costs to implement will vary considerably across different categories of FI. Of the costs incurred it will be difficult to separate out costs which are purely for collection and reporting from the overall implementation of the tax itself. The drivers for cost for FI's from EU FTT include the following elements:

Set-up costs for individual FIs

In broad terms there are two categories of set up costs for individual FIs with regard to the proposed EU FTT, firstly, ensuring the the organisation has the right data for EU FTT purposes and then reconfiguring the systems and processes to use that data in order to calculate EU FTT and deal with payment requirements.

i. With regard to the first category as explained in Section 4 there are several unique data requirements, but we shall focus upon one, counterparty data, as an example. It will be necessary to undertake a client repapering exercise. A large FI will typically have tens / hundreds of thousands of corporate and institutional clients and potentially millions of individual clients. In order to operate EU FTT it will be necessary to correctly categorise each client according to its EU FTT status. This kind of "re-papering" exercise is somewhat akin to the process many FI's have undertaken to comply with the US Foreign Account Tax Compliance Act and will now need to do for the OECD Common Reporting Standard ('CRS'). However, there is limited synergy between the data needed for these purposes and EU FTT. Large FI's when dealing with this exercise for FATCA have either:

- attempted to re-utilise existing client data (a high cost approach due to the need for internal resources) or,
- contacted all clients specifically for these purposes (a lower cost approach which passes risk and efforts to customers).

In our experience the repapering of client database for FATCA for a large global FI typically has cost upwards of €10m - €50m depending upon the approach taken. This category of cost was not incurred for IFTT, FFTT or SDRT.

ii. Systems/IT build. In order to operate the proposed EU FTT we would anticipate large FI's would need to embed the proposed EU FTT in their core systems and processes. This has not typically been the case for IFTT and FFTT where tax calculation and reporting has typically been "offline". Given the complexity of the financial markets and the intricate rules of EU FTT coupled with the lack of a broad based market maker exemption, FI's will not be able to relegate EU FTT to a post trade process. The FI will need to ensure all relevant front office systems are reconfigured for the proposed EU FTT and, depending upon the collection method, the proposed EU FTT will need to be built into IT interfaces with counterparties and financial infrastructure. There will be a wide range of processes and sub-processes that will need the proposed EU FTT coding, ranging from payments, credit control, treasury, settlement, product control and finance. This kind of project is broadly equivalent to cost basis reporting in the US or flat tax in Germany ("Abgeltungssteuer"). Both of these taxes required detailed business process mapping and detailed business requirements specification. For the German Flat Tax, which has largely fallen upon custody bank to implement, these banks have typically spent €100m on the programme to implement it.

Organisational change

The proposed EU FTT implementation will require large FI's to undertake global change management programmes in the same way as they have done for regulatory change such as Emir or CRD IV. Such change programmes are needed for issues like EU FTT that:

- affect many business units,
- require central co-ordination and governance to ensure consistent implementation.

These types of programmes typically require:

- training of staff,
- internal and external communication,
- detailed programme management and commissioning of IT projects,
- interfaces with other "in flight" change programmes.

Examples of such global programmes for large FI's have often exceeded €50m and in some cases even€300m. The design of EU FTT and its wide scope and impact of EU

FTT and its wide scope and impact on the business would normally require large FI's to take this approach, whereas a tax like IFTT, FFTT or SDRT is much narrower and cheaper to handle for FI's.

Running costs for individual FIs

FI's we have consulted cannot cost an unknown model which has many uncertainties and variables

We can, though, list the types of cost category which will typically be included in running a tax like the proposed EU FTT:

- Customer reference database management: The daily processes on on-boarding and changing customer reference data for changes in circumstances would need to include EU FTT. Whilst, in principle, these processes occur regularly and therefore adding additional requirements to customer reference data management should not be too burdensome, the consequences of failure to update records quickly will be far more direct and financial. So, for instance, whilst taking 3 months to update a change of address for a customer might result in mis-directed mail, failure to update an address for EU FTT may result in the wrong charge for EU FTT. As a result FI's may not be able to simply widen the scope of an existing process, they may need to reconsider whether existing processes are sufficiently robust to deal with a totally different type of risk and consequence.

-Payments and payment instructions. A collection system which involves the transfer of data to third parties via electronic secure messages will incur transaction charges and therefore a system which reduces the volume of messages needed contains costs. Similarly, if the data is already being transferred to a third party can be re used for EU FTT purposes, that contains incremental cost.

-Reconciliations, errors and exception management. Typically we would expect a small team to be needed for each FI to deal with off line issues which will inevitably occur even where a high rate of straight through processing can be achieved. Where primary rules are too factually dependent, where there are many local market variations and payment regulations are complex, then will be a much greater need for large FIs to devote dedicated staff to handle EUFTT.

-New product on boarding and other business changes. Changes to product lines, legal entity booking models, operational and commercial changes and regulatory driven changes will all potentially affect EUFTT processes and will need to be handled. The final design and scope of EUFTT will determine how costly it is to run ongoing routine business changes with containable costs associated with EUFTT.

Relative cost profile for each collection model

The above types of cost which will be incurred by FIs for set up and running of EU FTT will be altered by the overall collection model. Just as individual FIs have provided us limited guidance on cost for them as institutions, we have limited information from which to draw upon to estimate costs for an overall collection model.

However, we are able to make some preliminary general observations about the likely relative costs of the models.

Because of the design of EU FTT, which requires a lot of unique data to be considered by each taxpayer against a set of intricate rules, the burden of this must really fall upon the liable person.

In a self-administered model, each FI will need to build rules engines, manage their own data and remit their own taxes. As discussed above, FIs will need to also establish new reference databases and support front offices in pricing of EU FTT, pre trade. Relative to other existing transaction taxes we would judge the burden of building and operating EU FTT to be "high".

Where delegation takes place, many FIs will see the direct cost of building and operating a tax collection system fall away dramatically. However, the person to whom administration has been delegated will have a much bigger build and operate cost which will then be recharged one way or another. Generally speaking there is likely to be little aggregate cost difference between self-administration and delegation, except where economies of scale can be realized by providers of delegation services. Such economies need to be balanced against the cost of increased data being transferred in a delegated model.

Central models, both involving a CCP/CSD or a new utility, may well prove to have additional costs compared with the self-administration/delegation model. The tax calculation processes, data management etc. will continue to take place at an FI level, in addition the step of tax collection/reporting is undertaken centrally. So the issue then becomes whether those additional costs of centralization are justified by the benefits? And what is the economic model to incur and recoup those costs?

How much the methods of centralized tax collection will cost will be a function of, inter alia:

- how much systems work is required to either adapt and configure existing systems, or build new systems,
- how much of the gross detailed transaction data is transferred centrally and how complex the central processing of that data will be (for example, the SDRT flagging system is simple, whereas the systems build to match data between counterparties for EU FTT is likely to be very complex), and
- how much the existing and future work to support connectivity with CSDs/CCPs or Trade Depositories/ARMs can be leveraged for EU FTT purposes.

In essence, the build cost will depend largely on what functions are to be undertaken by the central collecting agent. If a central collection utility is required to perform a full range of functions against the scope of the proposed Directive, then the cost to design, build and deploy will be very substantial.

The answers to these and other relevant questions are subject to the final shape of the Directive and the design of the chosen collection systems.

Our rough assessment of the relative costs of each model can be illustrated in the below table:

	Model 1	Model 2	Model 3	Model 4
	Self-administered	**Delegated**	**Central**	**New Utility**
Set-up costs				
▪ FIs	High	Low to V. High	Medium to High	Medium to High
▪ Infrastructure	N/A`	N/A	V. High	V. High
▪ PMS	Low	Low	V. High	V. High
Operating costs				
▪ FIs	High	Low to High	Medium	Medium
▪ Infrastructure	N/A	N/A	Low	Low to Medium
▪ PMS	High	High	Low to Medium	Low to Medium

The overall economics of a collection system from a PMS perspective will require an assessment of inter alia,

- The direct costs it will need to incur
- The likely compliance performance of the system, for example, what is the likely size of the "tax gap" and
- The impact of the chosen collection system on the domestic financial services industry.

Taking each system in turn we would offer the following observations:

- Self-assessment system. From a PMS perspective the most comparable tax from a cost/resources point of view is probably value added tax. Under a self-assessment basis the costs of the tax authorities will be predominantly applied in risk assessing and potentially auditing individual institutions. Due to the nature of the proposed EU FTT as with VAT the most effective risk assessment or audit techniques are likely to require data analytic tools to be deployed. Given the variety and sophistication of IT systems within the financial industry, PMS would themselves need to invest in a range of data tools and specialists to ensure audit procedures are effective. The self-assessment system is also likely to throw up the most disputes between taxpayers and PMS as to the correct liability on transactions. We would therefore anticipate that this system is likely to require the most PMS resources on dispute resolution and litigation considering that 'standardization' of application of the EU FTT rules would likely require a significant number of years.
- Under a delegation model similar IT and data analytics resources and tools would be needed, albeit that it would be focused upon a smaller number of larger institutions, typically broker/dealers, custodians and asset servicers. Due to the scope of the proposed tax and the complexity of the financial landscape we would not envisage the tax authority resources required to be materially reduced from a self-assessment model. On the one hand there will be a degree of efficiency gains through a reduced number of material collecting agents, this will facilitate more a targeted, risk-based audit

approach. On the other hand the delegation model itself will need on-going governance from PMS authorizing FIs to be collecting agents and there will an onus on PMS to ensure collecting agents are operating EU FTT correctly.

- Under centralization models the operating costs could be substantially lower for PMS if the system can become largely self-regulating. Set-up costs can be very high for PMS depending (i) on the contribution they have to make at inception and (ii) the level of cost sharing that is possible with infrastructure (participating in any centralised collection).

- Under central models PMS resources are most likely to focus upon:

  - Technical matters which the central system can then cascade through to market participants

  - Risk based audits of FIs to ensure that the data being processed by the centralized collection method is complete, accurate and correctly classified for EU FTT

  - Identifying situations where the central collection system does not process taxable activity at all.

  The number of disputes surrounding FTT in such an environment is likely to be lower, albeit probably of much higher value, since by design a specific interpretation is more likely to have been consistently applied across users of the central collection model.

10.3 Comparison of models' relative feasibility

Our overall high level conclusions on each model, taking into account the challenges, asset class variations, EU market structure, input from FIs, regulation, cost etc is as follows:

Self-Administration

Our overall interpretation of the above suggests to us at least one fairly clear conclusion: self administration as an overall collection model is the least desirable outcome. However, self-administration has the benefit of clarity i.e. all actors know they are responsible for their own tax. It will likely result in market based solutions to assist compliance, such as IT software provision and database solutions. However, these solutions are necessarily going to be uncoordinated, and unlikely to be comprehensive across markets, particularly outside of the EU. This model provides PMS the least apparatus to influence the compliance environment and therefore little support to ensure the right amount of tax is collected. Notwithstanding this, self-administration is likely to have to have a place in a final FTT collection system in order to:

- allow FIs that cannot access other models a "last resort" method of compliance and;

- allow all FIs the capacity to deal with certain transactions that other collection models have no intrinsic advantage in dealing with. In particular, intragroup transactions and intragroup risk transfer arrangements.

A delegated model

The possibility of being able to delegate FTT compliance and collection obligations to an agent or upper-tier FI has significant advantages for certain classes of FIs compared to other models. This could apply to FIs that:

- are too small to build their own infrastructure to comply with EU FTT,
- are outside the EU FTT zone, and taxable because of the FTT status of their counterparty, who could have the option to require their counterparty (or agent) to account for tax on their behalf, and
- want to use existing commercial arrangements such as asset servicing, custody or transfer agency for FTT compliance.

Delegation offers wider advantages as follows:

- A delegation model offers cost advantages compared to self-administration, since it could leverage existing business practices and will likely result in a reduced number of FIs who can process the tax in high volumes at low unit costs.
- In addition for many FIs the CCP/CSD model is not viable since they do not have direct market access to such institutions. Such institutions will often have outsourced transaction reporting, often to their broker-dealers and therefore would not have direct day to day dealings with regard to transaction reporting.

A CCP/CSD model

The CCP/CSD model offers potential advantages over the delegated model:

- The CSD model operated by Euroclear UK & Ireland has shown that for a relatively simple tax a CSD collection model can be cost effective, particularly from a PMS perspective.
- Centralization offers a "transmission mechanism" of standard market practice and this should reduce risk.
- Centralization (at a CCP level) offers the possibility to match net data between counterparties, this would be far more difficult for a new utility to achieve using regulatory reporting based EU FTT data.
- Centralization offers an opportunity to access aggregated data which can facilitate PMS tax audit procedures. However, the major drawbacks for this model are:
    i. its lack of global reach (albeit that non PMS FIs could access PMS CSDs)
    ii. the significance of the data quality challenge (especially net data and limited data on counterparty etc.) – this issue could potentially be addressed by the development of a functionality that enables the capturing of gross transactions by way of non-settled declarative instructions

iii. the build costs are likely to be significant and the time to deliver will exceed the self-administration and delegation models.

The new utility model

So our tentative conclusion is that except for discrete areas, perhapscash equities, the CCP/CSD model of Central Collection is not per se the most generic and beneficial form of centralization. At the same time, it is fair to say that the issue is probably more about the role that should be given to the central collection entity than about whether a CCP/CSD or rather a new utility should operate the central collection mechanism.

The new utility model has the same types of centralization benefits that the CCP/CSD model has but it has less exposure to the significant problems with that model in so far as:

- The new utility model is not self-limiting geographically. Whilst the CCP/CSD model may face certain obstacles outside the EU FTT zone, this model could be a structured contractual model which is less likely to require the endorsement and co-operation of non-EU zone regulators and authorities.

- The new utility model may be able to utilise already existing gross data sources in the form of regulatory reporting.

- The CCP/CSD model makes little sense for certain asset classes or for certain trades which remain OTC and uncleared.

Having said this, we would envisage certain CCPs/CSDs to want to operate as EU FTT utilities, leveraging their position within markets. To the extent this occurs, there will be little difference between the two models of centralization. With both methods of centralization it is an open question as to how much data needs to be supplied to the central point, whether simply the output of a rules engine at FI level (represented by "flags") or highly detailed, gross transaction data (which the central point could apply a calculation logic to in order to compute tax liability).

10.4 Towards an overall system

Partial overlaps exist in relation to these approaches to collection of EU FTT which we have initially outlined (self-administered collection, delegation of collection responsibilities, collection via central clearing or settlement, collection via a new utility) and some of the distinctions to be drawn between these approaches require a more detailed assessment.

As market participants appear to express the preference for some sort of 'centralized' approach or functionality in relation to EU FTT collection, we have tried to identify in more detail what level of 'centralized collection functionality' that can be considered feasible given the challenges identified.

Further analysis carried out suggests that the main question to be answered may not necessarily be who will be performing a given central function. The central issue to be dealt with is broader than a choice between collection via central clearing or settlement on the one hand and collection via a new utility on the other hand.

To be more precise, in relation to 'centralized collection functionality', it seems that the 2 basic options are:

- a centralized collection model with limited central functionality (i.e. centralized collection via transaction flagging), where EU FTT liability is determined at the broker/dealer level ('liable person') and with the logic to be built centrally only having to be able to read the flags and not the full transaction data; and:

- a centralized collection model with expanded central functionality (centralized collection via data transfer), based on centralizing all (or several) data required to determine EU FTT liability and to contain (and run) a central FTT logic on those data to determine EU FTT liability centrally, with (data regarding) every chargeable transfer to be sent to a central system.

As will be clear from our report, there are many issues to address in deploying a collection system, and indicating a possible approach does not suggest these issues can be easily solved or indeed that they can be solved at all. The overall systems which seem most worthy of further investigation are, either:

- a centralized system based upon limited data flagging of taxable/non taxable transactions potentially leveraging existing infrastructure for inputting settlement instructions (in particular when a CSD would be mandated to operate the system). The extent of the flagging will in turn determine what functions central collection mechanisms may be able to perform beyond pure mechanical collection.

  or

- a centralized system based upon regulatory reporting, utilizing the gross data across asset classes.

These centralized systems need not be directly accessed by all taxpaying FIs. Many FIs may elect to use an authorized method of delegation to a FI that may either have a different function (such as a broker/dealer or custodian) or be within the EU FTT zone. Such institutions would access the central utility "behind the scenes" to facilitate EU FTT collection.

As a fall back, self-administration will always need to be an option.

In any event, the effectiveness of collection would be improved by key changes in primary rules to simplify collection processes. Clarity and granularity of collection procedures is also a requirement of effective collection.

Should the CREST collection model for SDRT be replicated for EU FTT collection purposes?

A number of domestic systems have used a centralised approach to reporting and payment collection, typically using the facilities of a CSD. While such an approach may offer various opportunities and various advantages, this does not mean that merely copying an existing centralised approach will be a relatively simple way forward. Typically, existing centralised mechanisms operated through a CSD (e.g. CREST in respect of UK SDRT) offer functionality which is geared towards the relevant domestic taxes. To the extent that such taxes are more limited in scope than FTT, the functionality on offer will be more limited than would be required for FTT.

Taking UK SDRT as a comparative example, APPENDIX 2 compares key operational aspects of the SDRT and EU FTT regimes and highlights (i) the differences between the regimes, (ii) how difficult it would be in practice to bridge the gaps and (iii) how easy it would be to implement a potential solution.

To better understand why there would be substantial challenges to implement reporting and payment collection mechanisms for EU FTT based largely on the reporting and payment collection mechanisms currently in place for SDRT, it is important to acknowledge that EU FTT (if introduced in line with the proposed Directive) would have a number of fundamental legal differences from SDRT:

- EU FTT would apply to a much wider spread of asset classes (e.g. it would cover all derivative contracts) than those covered by SDRT (which in practice primarily applies to shares).
- EU FTT would include a residence basis in addition to an issuance basis whereas SDRT has only an issuance basis.
- EU FTT would be targeted specifically at financial institutions: these would be the persons liable to EU FTT. By contrast, a financial institution is only liable to SDRT if it is the purchaser. Although SDRT has a concept of 'accountable person' - typically a financial intermediary (e.g. broker or custodian) acting for a purchaser - who is legally required to report and pay the SDRT, the accountable person has a right to recover tax paid from the purchaser and, in certain circumstances where the accountable person is unable to so recover, the obligation to account is relieved.
- Further, consistent with being targeted specifically at financial institutions, EU FTT currently offers only a limited form of intermediary relief (which is based on specific transaction facts and circumstances) whereas SDRT is essentially an end-investor tax with a broad intermediary relief (which is entity-based) for brokers and other securities dealers.

Of all these fundamental differences, the two differences that present the greatest challenge to simply replicating for EU FTT the current CREST-based SDRT reporting and payment collection functionality are:

(1) Wider spread of asset classes

Although existing CSD/CCP infrastructure could be adapted or built up to facilitate centralised reporting and payment collection in relation to shares

and certain other centrally-cleared or centrally-settled assets (e.g. bonds), there is no existing central infrastructure in relation to some of the asset classes within the scope of EU FTT (e.g. most derivative contracts traded OTC).

(2) Inclusion of a residency basis

CREST copes well with SDRT arising only on an issuance basis. It is a relatively straightforward process to ensure a UK-issued chargeable security is flagged appropriately in CREST such that any transfers of that security effected through CREST would (subject to any reliefs or exemptions claimed) be liable to 0.5% SDRT. Consistent with SDRT arising only on an issuance basis, CREST currently offers no functionality to collect SDRT based on residency. In contrast, any FTT infrastructure would require provision to collect FTT based on residence (in addition to tax collected on an issuance basis).

Even where a domestic system points the way to a potential solution for an issue arising under FTT, there will still be significant, possibly substantial, challenges in realising that solution in the context of FTT. By way of examples:- The new Stamp Duty Assessment Service ('SDAS') in CREST addresses potential under-reporting and under-payment of SDRT in relation to netted trades. However, SDAS is initially limited to trades using CCP settlement netting models. In the context of FTT, potentially a significantly greater level of provision would be required given the wider spread of asset classes within the scope of FTT.

In conclusion, copying from, or even being guided by, the centralised approach of a domestic system would not be a straightforward exercise and in any event would require significant or substantial changes to address specific features of FTT (most notably the wider spread of asset classes within the scope of FTT and the inclusion of a residence basis).

Appendix 1 - Overview of key features of existing national FTTs: Belgium, France, Italy, Switzerland, United Kingdom

The table below summarises certain key features of five existing national FTTs. It covers for each of the taxes:

- their scope;
- the approach adopted to collection; and
- an assessment (drawing on publicly available information) of:

a) the level of revenues raised;

b) relative compliance/enforcement costs to taxpayers, infrastructure providers and tax authorities; and

c) key compliance risks

	Belgium	France	Italy	Switzerland	United Kingdom
Type of collection system	**First financial intermediary (self-administered)**	**Mixed centralised/first financial intermediary (self-administered) system**	**Mixed centralised/first financial intermediary (self-administered) system**	**First financial intermediary (self-administered)**	**Centralised system**
Scope					
Taxable event	Sales and purchases of 'Publicly' tradable securities (actual listing is not required), and repurchases of accumulating shares of certain corporate investment funds if the transaction, if the transaction is done through a Belgian financial intermediary and is executed in Belgium.	Tax is due on transfer of legal ownership of listed equities of large companies established in France, similar instruments and depository receipts provided that the underlying securities are French equities; on cancelled high frequency trading orders where the high frequency trading is carried out in France; oncredit default swaps on sovereign debt . Writing and sales of derivatives out of scope of tax.	The transfer of legal ownership of equities/equity derivatives of a company resident in Italy. Modification of derivatives.	Tax is due on legal transfer of ownership of equities and bonds if one of the parties is a Swiss securities dealer.	0.5% charge applies to agreements (electronic, oral, written or otherwise) to transfer 'chargeable securities' for consideration in money or money's worth. If agreement is conditional when made, tax only arises if and when agreement becomes unconditional Higher (1.5%) charge for certain transfers of 'chargeable securities' to clearance services or depositary receipt systems

	Belgium	France	Italy	Switzerland	United Kingdom
Type of collection system	**First financial intermediary (self-administered)**	**Mixed centralised/first financial intermediary (self-administered) system**	**Mixed centralised/first financial intermediary (self-administered) system**	**First financial intermediary (self-administered)**	**Centralised system**
					'Chargeable securities' include shares and other securities (e.g. Debt instruments): (i) Issued by a UK-incorporated company; (ii) Issued by a non-UK company but registered on a register kept in the UK; or (iii) (shares only) issued by a non-UK company but 'paired' with shares issued by a UK-incorporated company ('paired' means that the non-UK and UK shares can only be dealt with as a single unit) (NB Separate, much older tax - stamp duty - can apply to paper-based transfers of shares)
Payment due date	Last working day of the month, following that during which the transaction took place.	FTT reporting and payment is due to the CSD by the 5th day of the following month (in case of reporting via the CSD), tax declaration and payment is due before the 25th day of the following month by the CSD/taxpayer to the French tax authorities.	16th day of the following month - monthly F24 return or bank transfer – paid at the same time.	Form 9 return due 30 days after end of quarter in which transaction took place.	For transfers effected through CREST, SDRT is collected on earlier of settlement (typically T+3) or T+10 business days (effectively T+14) For transfers effected outside CREST, SDRT must be reported and paid to HMRC by 7th day of month following month in which agreement to transfer was made (or, if agreement was conditional, became

	Belgium	France	Italy	Switzerland	United Kingdom
Type of collection system	**First financial intermediary (self-administered)**	**Mixed centralised/first financial intermediary (self-administered) system**	**Mixed centralised/first financial intermediary (self-administered) system**	**First financial intermediary (self-administered)**	**Centralised system**
					unconditional) (Where stamp duty, rather than SDRT, is the applicable tax – i.e. written transfer instruments – the relevant transfer instrument must be presented along with payment to HMRC within 30 days of execution to avoid interest and penalties.)
Exemptions	Transactions involving most Belgian government debt securities, commercial paper and certificates of deposit issued under the Law of July 22, 1991, shares issues by institutional and private equity funds, short term debt instruments by the National Bank of Belgium. Transaction not involving a Belgian professional intermediary Transactions not executed in Belgium. Transactions done for their own account by non-resident, Belgian financial institutions as defined by law, pension funds and investment funds.	Defined market-making activities for financial intermediaries. Primary issuance. Temporary sales. Intra-group transactions. Restructuring transactions (e.g. mergers/De-mergers). Acquisition by employee investment schemes. Liquidity agreement concluded by the issuer. Exemption of CSDs and clearing houses. No exemption based on regulatory status (as based on transactions).	On a transaction by transaction basis (e.g. inheritance or gift, corporate actions etc.). Defined market making activities for financial intermediaries (proprietary trading is not excluded from IFTT, there is an intermediary relief available where the broker acts as riskless principal). Primary issuance of shares.	Professional brokers are exempt if trading shares for their proprietary trading account. However, registration with SFTA is a pre-requisite. Primary issuance of shares and bonds as well as "grey market" (i.e. until payment date of newly issued securities). A catalogue of exempted parties applies (such as e.g. Swiss and foreign CIVs, foreign states, foreign social security funds, foreign listed companies and their foreign subsidiaries). All derivative trading instruments such as options, swaps, swaptions, futures. Repo and securities lending transactions (as they are seen as collateralised loans rather than transfer of taxable securities).	'Recognised intermediaries' (brokers and other securities dealers) who have been recognised directly by HMRC or indirectly through membership of certain markets are exempt on purchases on own account. Stock lending and repos. Most debt instruments (NB exemption does not apply where there are certain equity like characteristics e.g. convertible into shares or interest rate is higher than a commercial rate). Most cash-settled derivatives - e.g. CFDs, swaps - are exempt (but derivatives which are capable of being physically settled, such as some options, are not exempt). Purchases by charities. In Budget 2013 it was announced that stamp duty

	Belgium	France	Italy	Switzerland	United Kingdom
Type of collection system	**First financial intermediary (self-administered)**	**Mixed centralised/first financial intermediary (self-administered) system**	**Mixed centralised/first financial intermediary (self-administered) system**	**First financial intermediary (self-administered)**	**Centralised system**
					would be abolished on AIM shares.
Method of collection					
Tax collector	Financial intermediaries self assess and administer the taxes they are liable for	Collected via executing broker if present, or via custodian if not. Where the CSD holding the issuance account is in France, securities dealers and their clients must (or in some cases may opt to) submit FTT declarations and tax payments to the Central Securities Depository (CSD), Euroclear, who submit to the tax authorities. Otherwise collected directly by tax authority.	Collected via financial intermediary closest to the client or directly from purchaser if no FI present. Tax may additionally be collected from further intermediaries in chain if in black listed jurisdiction unless paid through Italian or white-listed jurisdiction branch or via Italian tax rep. Securities dealers can appoint the CSD (Monte-Titoli) to submit FTT declarations and pay the tax to authorities; Monte-Titoli can also calculate payment advice.	Securities dealers i.e. banks, bank-like FIs. Both sides of the transaction are taxed therefore the securities dealer will remit half of the tax for the purchaser, and the second half for the seller.	Shares are held in the Central Securities Depository (CREST). Brokers send electronic settlement instructions to CREST detailing which securities are being traded. CREST then settles the transaction. For transfers effected through CREST, settlement instruction will include a number of inputs relevant to SDRT reporting and payment. Generally, both reporting and payment of SDRT will be processed automatically through CREST (settlement instruction information is transmitted to HMRC and payment is collected within the CREST system). Off-market transactions made outside of CREST, tax should be calculated, reported and paid directly to HMRC.

	Belgium	France	Italy	Switzerland	United Kingdom
Type of collection system	**First financial intermediary (self-administered)**	**Mixed centralised/first financial intermediary (self-administered) system**	**Mixed centralised/first financial intermediary (self-administered) system**	**First financial intermediary (self-administered)**	**Centralised system**
Liable person	The Belgian professional intermediary acting for the buyer or the sellor	Investment service provider i.e. executing broker or custodian closest to the purchaser), regardless of location. Practicalities exist for entities located outside of the EU in determining whether they are considered as ISPs. Indeed, the French definition of ISP derives from MiFID Directive, to which EU FIs are generally used, while this is not the case for non-EU (particularly U.S.) entities. Issues remain in relation to transactions between ISPs.	Purchasers and sellers (see below). For equity IFTT: the ultimate purchaser For Derivative IFTT: Both counterparties Since intermediary exemption is only available to white-listed intermediaries, double taxation could occur	Purchasers and sellers The Swiss securities dealer is liable to tax. However, this is split evenly between counterparties unless they have exemption status.	Purchaser is ultimately liable. However, a financial intermediary (typically a broker or custodian) may be the 'accountable person', that is the person required in the first instance to report the charge and pay the tax to HMRC (such an accountable person has a right to recover the tax paid from the purchaser).
Who pays the tax: (e.g. purchaser, seller or both)	Purchaser and sellers The professional intermediary is the debtor of the tax, and has an obligation to provide a certificate to the taxpayer containing information with regard to the transaction and the amount of tax which will be due on the day after the execution of an order[12]. The tax agency then audits those that are judged to have a high risk of non-compliance.	Executing Investment Service Provider (ISP), of the purchaser regardless of location. Custodian Bank if no ISP. Identification of taxpayer in relation to transactions between ISPs is difficult. The market practice has developed a standard contractual framework in order to secure the determination of the taxpayer. Despite this contractual arrangement, some technical and commercial	Purchaser (and seller in the case of derivatives) is ultimately liable Financial intermediaries closest to the liable party are required to collect tax. Collection can be delegated to Monte Titoli (CSD). Final purchaser if no financial intermediary is involved Clearing broker where involved in the execution of the order (derivatives)	Purchasers and sellers As Swiss securities dealer liable to remit tax, tax pass through to non-exempt party is common.	SDRT must be reported and paid by the 'accountable person', albeit the accountable person will then recover the tax paid from the purchaser (if the purchaser itself is not the accountable person)

[12] The intermediary has to keep a copy of the certificate or include the information in a day to day listing for a period of 6 years.

	Belgium	France	Italy	Switzerland	United Kingdom
Type of collection system	**First financial intermediary (self-administered)**	**Mixed centralised/first financial intermediary (self-administered) system**	**Mixed centralised/first financial intermediary (self-administered) system**	**First financial intermediary (self-administered)**	**Centralised system**
		issues remain for taxpayer determination.			
Reporting liability	Purchasers and sellers Financial intermediaries are required to maintain records of their transactions that are subject to the tax, declare the transactions in a monthly tax return and pay the **self-assessed** tax at the same time when the tax return is filed.	ISP or custodian. Pursuant to Article 235 ter ZD, VI and VII of the FTC, the person that is responsible for collecting and reporting the tax can differ from the legal taxpayer. Reporting and payment required on a monthly basis.	Financial intermediaries who collected the tax or purchasers (in the case where no financial intermediary applied the tax) Annual return (but monthly payment) – due by 31 March 2014 for transactions occurred during March – December 2013 for Equity IFTT and HFT IFTT and September – December 2013 for Derivative IFTT	Swiss securities dealers Swiss securities dealers are required to register all transactions and remit transfer taxes on trades closed between themselves and other parties. Dealers must also maintain a trading journal. All trades must be filed in this journal three working days after the transaction has been signed at the latest. This serves as the basis for the tax remittance to the tax authorities.	The 'accountable person' is required to report (and pay) any SDRT liability. There are penalties for failure to report correctly in good time (and interest on late payment).
Obligation to maintain a register	Intermediary provides certificate to taxpayer confirming how much tax is due and nature of transaction. Intermediaries should keep a copy of the certificate.	Euroclear- if FI member of Euroclear - to maintain a set of accounts specific to the taxable transaction; issue an annual report on the controls put in place for the tax authorities. If the taxpayer reports directly to the FTA (and not through Euroclear), the taxpayer should keep a record of all transactions.	Financial Intermediaries who collected the tax or purchasers (in the case where no financial intermediary applied the tax), except for individuals.	Securities dealer must maintain one register of transactions including exempted transactions – must be entered in register within 3 days after transaction conclusion.	

	Belgium	France	Italy	Switzerland	United Kingdom
Type of collection system	**First financial intermediary (self-administered)**	**Mixed centralised/first financial intermediary (self-administered) system**	**Mixed centralised/first financial intermediary (self-administered) system**	**First financial intermediary (self-administered)**	**Centralised system**
Tax Revenues Raised					
Total Tax Revenue	EUR 236.3 m – 2008 EUR 140.8 m – 2009 EUR 130 m – 2008 – 2012 average	EUR 690 m - 2013 EUR 702 m – 2014 (estimated)	EUR 159 m – 2013 On Equity and High Frequency Trading, March –Sept, and Derivatives, Sept (Italian Ministry of Finance)	CHF 1,472 m - 2009 CHF 1,417 m - 2010 CHF 1,312 m - 2011 CHF 1,107 m – 2012 (of which 200m francs from foreign shares: IRSC, 2013)	Share transfers: electronic and paper based (£bn) 2008-09 £3.2bn 2009-10 £3.0bn 2010-11 £3.0bn 2011-12 £2.8bn 2012-13 £2.2bn
% Total Tax Revenue	0.27% - 2008 0.17% - 2009 0.20% - 2008 – 2012 average	0.07% - 2013 (of 2012) 0.08% - 2014 (of 2012) *Latest figures: Total tax revenue in 2012 EUR 920bn (OECD)	0.02% - 2014 (of 2012) *Latest figures: Total tax revenue in 2012 EUR 920bn (OECD)	4.7% - 2010 (of CHF 46,347 m^) ^ Federal tax revenues	Share transfers: electronic and paper based (% Total Tax Revenue) 2008-09 0.73% 2009-10 0.74% 2010-11 0.66% 2011-12 0.60% 2012-13 0.48%

	Belgium	France	Italy	Switzerland	United Kingdom
Type of collection system	**First financial intermediary (self-administered)**	**Mixed centralised/first financial intermediary (self-administered) system**	**Mixed centralised/first financial intermediary (self-administered) system**	**First financial intermediary (self-administered)**	**Centralised system**
% Gross Domestic Product	0.07% - 2008 0.04% - 2009 0.05% - 2008 – 2012 average	0.03% - 2013 0.03% - 2014 (estimated)	0.01% - 2013	0.4% - 2010 (of CHF 546,245 m)	Share transfers: electronic and paper based (% GDP) 2008-09 0.22% 2009-10 0.21% 2010-11 0.20% 2011-12 0.18% 2012-13 0.14%
Compliance Levels					
	The administrative burden for taxpayers is estimated to be low (Brondolo 2011). However, there is no publicly available information with regard to the cost of collection, tax authority compliance activity and the administrative burden on taxpayers or others.	No publicly available data on compliance levels exists. French government expected EUR 1.6 bn of revenue for 2013 (but EUR 1bn was budgeted), but only EUR 690m has been collected. The estimated revenues for 2014 amount to EUR 702 m	No publicly available data on compliance levels exists. Revenue raised, EUR 15 m, is a fraction of the EUR 1 bn revenue targets. Collection of derivatives tax especially low.	The Swiss stamp tax is thought to have low compliance and administrative costs, and high compliance rates, although no precise estimates are available (Brondolo, 2011).	No publicly available data on compliance levels is available. Nonetheless, compliance rate is generally considered to be very high. In 2012 the SDRT tax gap was estimated to be £200 million or 3% of tax due (HMRC, 2013).

	Belgium	France	Italy	Switzerland	United Kingdom
Type of collection system	**First financial intermediary (self-administered)**	**Mixed centralised/first financial intermediary (self-administered) system**	**Mixed centralised/first financial intermediary (self-administered) system**	**First financial intermediary (self-administered)**	**Centralised system**
Compliance costs					
Taxpayers	Low (see 3.1.1)	High (see 3.2.1)	High (see 3.3.1)	Low (see 3.4.1)	Low (see 3.5.1)
Infra-structure	Low (see 3.1.2)	High (see 3.2.2)	Medium(see 3.3.2)	Low (see 3.4.2)	Low (see 3.5.2)
Tax authority	High/Medium (see 3.1.3)	Medium (see 3.2.3)	Medium (see 3.3.3)	Low (see 3.4.3)	Low (see 3.5.3)
Compliance risks					
Under-reporting	High risk due to tax's self-assessed nature Timing issues: Tax is not due at time of taxable event. Reliant on professionalism of intermediaries, who are the debtors of the tax, and reliability of the audit process.	Lower risk than self-reported, due to central clearinghouse (Euroclear France). FFTT reporting model is operationally complex and the underreporting risks this poses would need to be fully assessed in light of first year experience	High risk due to self-assessed nature Timing issues: Tax is not due at time of taxable event. Reliant on IFFT Register compliance Audit process and frequency is unclear Many uncertainties involving black listed intermediaries.	High risk due to tax's self-assessed nature, but collaborative design has helped to minimise taxpayer reporting errors and boost compliance (Brondolo, 2011) Timing issues: Tax is not due at time of taxable event. Reliant on reliability of Securities Dealers' trading journals as well as reliability of audit process	Lower risk than self-reported, due to central CSD (CREST). No timing issues as tax is remitted at settlement

	Belgium	France	Italy	Switzerland	United Kingdom
Type of collection system	**First financial intermediary (self-administered)**	**Mixed centralised/first financial intermediary (self-administered) system**	**Mixed centralised/first financial intermediary (self-administered) system**	**First financial intermediary (self-administered)**	**Centralised system**
Cross-border	Belgian tax applies in countries where there is no authority to audit.	FFTT applies in countries where there is no authority to audit.	Italian tax applies in countries where there is no authority to audit. A higher rate applies in regulated markets which are not white listed.	Swiss tax applies in countries where there is no authority to audit. However, since the onus of levying the transaction tax is on the Swiss securities dealer, there is a low risk of non-compliance.	UK Stamp duty reserve tax applies in countries where there is no authority to audit.
Additional commentary	Only covers transactions in Belgium. Proposals exist to include transactions executed outside of Belgium on account of Belgian residents.	Applied to net transactions. Significant obligations in terms of taxpayers and CSD reporting. It is implied that the taxpayer and CSD reporting cost is re-charged in the value chain.	Equity IFTT applied to net transactions settled on the same trading day. Practical difficulties in identifying in–scope products, on-market vs. OTC, derivative modifications New (mainly manual) system and practicalities yet to be clarified		Low administration costs, penalties for non-compliance and CREST participants can be audited upon notice. Tax may not able to be calculated (or audited) unless transaction amounts are input through CREST (e.g. net figures provided).

Appendix 2 - From UK SDRT collection to EU FTT collection: A gap analysis

Category	Relevant SDRT elements	Relevant FTT elements	How different is FTT from SDRT in this aspect?	How difficult would it be to bridge the gap (e.g., adapt or build upon existing reporting/payment infrastructure?	What is a potential solution and how easy is it to implement?
Asset classes	SDRT applies to 'chargeable securities' – broadly UK shares and certain other securities which have equity-like characteristics (such as convertible bonds). Due to the more limited range of asset classes within its scope, SDRT can be collected largely through	FTT has much wider spread of asset classes, including derivative contracts. This will present substantial payment and collection infrastructure issues.	Substantially different. FTT would apply to a number of asset classes which are not within the scope of SDRT.	Substantially difficult. Although existing infrastructure could be adapted or built up to facilitate reporting and payment in relation to shares and certain other centrally-cleared instruments (e.g. bonds), there is no existing central infrastructure in relation to some of the asset classes within the scope of FTT.	The range of asset classes within the scope of FTT could be reduced, but this would require amendment of core provisions of the draft Directive. Built the creation of a specific FTT only instruction format within existing infrastructure
Issuance and residency	SDRT is issuance-based only: 'chargeable securities' includes securities issued by UK companies and also by non-UK companies where the securities are registered on a UK register or (for non-UK shares in limited circumstances) paired with UK shares	FTT has a wider scope, including a residency basis in addition to an issuance basis. While CREST is able to cope easily with SDRT on an issuance basis, any FTT infrastructure would need significantly greater provision to capture trades taxable by virtue of residency	Substantially different. Whereas SDRT is issuance-based, FTT will also apply additionally on a residency basis.	Substantially difficult. Where central infrastructure currently exists for certain asset classes within the scope of FTT, it would be substantially easier to build reporting and payment mechanisms based on the issuance basis alone. Inclusion of a residency basis presents substantial challenges in terms of adapting or building upon existing infrastructure.	The residency basis could be removed, leaving FTT to apply solely on an issuance basis, but this would require amendment of core provisions of the draft Directive.

Category	Relevant SDRT elements	Relevant FTT elements	How different is FTT from SDRT in this aspect?	How difficult would it be to bridge the gap (e.g., adapt or build upon existing reporting/payment infrastructure?	What is a potential solution and how easy is it to implement?
Capacity to deliver automation of reporting and collection	SDRT collection is largely achieved through CREST with a high degree of automation alongside transaction settlement. HMRC has facilities to receive manual reporting and payments outside of CREST.	For FTT, automation capacity is significantly reduced due to I) a number of primary rules being facts and circumstances based and therefore difficult to automate ii) a number of asset classes for FTT are not part of transaction automation processes (e.g. intragroup transactions) iii) Existing reference data (e.g. on place of listing of instruments) is not sufficient to deal with EUFTT definitions.	Substantially different. For FTT, manual reporting and payment would be expected to play a larger role compared to SDRT.	Substantially difficult. Substantial resources and infrastructures changes need to deliver a robust, automated EUFTT collection system	Simplification of primary rules and reduction in data requirements, particularly in counterparty classification.
Tax position of intermediaries	Recognised Intermediary ('RI') relief exempts securities dealers (who have been recognised as such) from SDRT on purchases made in a principal capacity (i.e. either for their own account or when acting as riskless principal) of almost all publicly-listed securities. In CREST, RI relief from SDRT is applied automatically based on account-level flags and markers.	FTT is specifically targeted at a broad range of financial institutions. Intermediaries do not have an entity exemption, therefore the article 10(2) exemption is facts and circumstances based.	Substantially different. FTT is specifically targeted at financial institutions and has a form of intermediary relief that exempts certain transactions	Substantially difficult. Presumably any FTT-specific infrastructure would seek to replicate the effect of the CREST dealing capacity indicator to track intermediary capacity, but this will be a substantial challenge particularly where there is no central reporting or payment collection infrastructure.	A broader version of intermediary relief (adopting at least some of SDRT RI relief) could be introduced, but this would require amendment of core provisions of the draft Directive.

Category	Relevant SDRT elements	Relevant FTT elements	How different is FTT from SDRT in this aspect?	How difficult would it be to bridge the gap (e.g., adapt or build upon existing reporting/payment infrastructure?	What is a potential solution and how easy is it to implement?
Payment time	For transfers through CREST, in practice SDRT is collected in CREST upon settlement at T+3 working days. (Strictly the law requires payment at the earlier of (i) T+10 working days and (ii) settlement date.) Note that the standard settlement cycle for UK securities transactions is planned to reduce to T+2 working days in October 2014.	FTT is intended to be collected at the time of the transaction (i.e. T) where the transaction is carried out electronically. In all other (i.e. non-electronic) cases, FTT must be paid within T+3 working days.	Significantly different. For electronic trades, FTT would be collected at T, whereas SDRT is collected at T+3 (with a move to T+2 in October 2014).	Substantially difficult. In practice, currently it would be impossible to collect FTT at T.	Moving the payment date for FTT so as to align with the relevant local standard securities settlement cycle (e.g. T+3) would be a straightforward solution, requiring an arguably minor amendment to the proposed Directive.
Capacity to deal with netting	SDRT is chargeable on a gross basis. HMRC concerns over under-reporting of SDRT in relation to netted trades has led to the introduction of the Stamp Duty Assessment Service ('SDAS') in CREST. However, initially SDAS will be limited to trades using CCP settlement netting models (since these currently make up most of the netting occurring outside of CREST). Consultation will take place on extending SDAS to other netting models in due course.	FTT is also chargeable on a gross basis.	No significant difference. Both SDRT and FTT are chargeable on a gross basis	Significantly difficult. FTT reporting and payment collection mechanisms will need to make at least a similar level of provision to SDAS. Potentially a significantly greater level of provision would be required given the wider spread of asset classes within the scope of FTT.	A reporting and payment collection mechanism based on SDAS could be introduced for FTT, albeit the collection mechanism may have limited possibility to validate SDAS instructions. Although this would involve significant infrastructure challenges, it would not require any amendment of the proposed Directive.

Category	Relevant SDRT elements	Relevant FTT elements	How different is FTT from SDRT in this aspect?	How difficult would it be to bridge the gap (e.g., adapt or build upon existing reporting/payment infrastructure?	What is a potential solution and how easy is it to implement?
Liable persons	The purchaser (whether a financial intermediary or not) is always liable for SDRT. However, a financial intermediary (e.g. a broker or a custodian) typically would be the 'accountable person', that is the person required by law to report and pay any SDRT on behalf of the purchaser. The accountable person has a legal right to recover payment of the SDRT from the purchaser. If, having taken all reasonable steps without success, the accountable person cannot recover from the purchaser the SDRT paid, the accountable person is relieved of its obligation to account for the tax	FTT includes provision for joint and several liability. Financial institutions are liable to FTT, although the proposed Directive permits Participating Member States to make provision for persons other than financial institutions to be jointly and severally liable for FTT.	Substantially different. FTT is specifically targeted at financial institutions but includes provision for joint and several liability.	Significantly difficult. Experience of Hong Kong Stamp Duty (which has joint and several liability for the seller and purchaser of securities) shows that joint and several liability can be made to work effectively for securities settled or cleared centrally (in the case of Hong Kong, this takes place through CCASS). However, building the necessary reporting and payment infrastructure will be a substantial challenge, particularly in relation to those asset classes within the scope of FTT for which there is no current central infrastructure.	The system used for Hong Kong Stamp Duty could be used as the basis for a FTT-specific system. The wider range of asset classes within the scope of FTT would involve significant infrastructure challenges. However, it would not require any amendment of the proposed Directive.
Extraterritorial aspects	SDRT has a mandatory, global reach in respect of agreements to transfer chargeable securities. Although a purchaser, wherever located, is liable to pay the tax, in practice enforceability becomes harder where UK securities are traded outside the UK. However, the concept of 'accountable person', linked to the fact that the vast majority of UK-issued shares in publicly-traded companies ultimately will be held through CREST, means that a UK-based broker or custodian (even if this is a UK	FTT has mandatory, global reach too but currently contains no inherent mechanisms to promote compliance in situations where enforceability will be harder in practice (e.g. transactions in non-PMS securities brought within the FTT charge by virtue of the residency basis and transactions in PMS securities settled in a non-PMS or outside the EU).	Substantially different. FTT lacks mechanisms equivalent to the SDRT 'accountable person' concept or the SDRT 'higher rate' (1.5%) regime.	Substantially difficult. The residency basis within FTT presents substantial infrastructure challenges in respect of transactions in non-PMS securities. The introduction of a 'higher rate' FTT regime for transactions in PMS securities settled in a non-PMS or outside the EU would present substantial infrastructure challenges, particularly in relation to those asset classes within the scope of FTT for which there is no current central infrastructure.	A concept similar to that of 'accountable person' could be introduced for FTT. There is a range of possibilities for a FTT-specific 'accountable person' concept, e.g. a group member or affiliate within the EU. If the residency basis were removed from FTT (such that only the issuance basis applied), this solution would be significantly, rather than substantially, difficult since there would be a much greater likelihood of an EU-based financial intermediary being

Category	Relevant SDRT elements	Relevant FTT elements	How different is FTT from SDRT in this aspect?	How difficult would it be to bridge the gap (e.g., adapt or build upon existing reporting/payment infrastructure?	What is a potential solution and how easy is it to implement?
	subsidiary or branch of a non-UK financial intermediary) will generally be involved in settling a trade and will therefore generally seek either payment of SDRT or a declaration that a specific exemption applies. Further, there is a 'higher rate' (1.5%) SDRT regime for transfers of chargeable securities to non-UK clearance services or depositary receipt systems (note that this 1.5% charge is the subject of current legal challenge: previous CJEU and UK court decisions have ruled that the charge is unlawful in relation to new issues, but, subject to legal challenge, HMRC continue to collect the tax on transfers of existing securities).				present. The introduction of a 'higher rate' FTT regime for entry into non-EU clearance services and depositary receipt systems would seem to require substantial amendment of both the proposed Directive and the existing Capital Duty Directive.

Appendix 3 - Considerations regarding a standardized FTT return

1. Introduction: Information required for determining FTT liability

Under Article 11 of the initial EU FTT proposal, the FTT return, which is to be submitted by the tenth day of the month following the month during which the FTT became chargeable, is supposed to set out all the information needed to calculate the FTT that has become chargeable during the relevant one month period including the total of the transactions taxed at each rate.

Taking this into account, the appropriate starting point for the determination of the content of the FTT tax return would appear to be to list the information required to calculate the chargeable FTT, as detailed below.

1.1 FTT Liability rules

The following elements can be identified as potentially relevant in determining FTT liability:

- the identification of financial instruments which are the subject of the relevant financial transaction, in order to determine whether they must be treated as issued in the EU FTT zone;
- the identification of the type of the relevant financial transaction, to determine whether it is in scope;
- information regarding any non-PMS FI which is a party to the relevant financial transaction, to determine whether it must be treated as established in the EU FTT zone;
- the identification of the other party or parties to the relevant financial transaction, to verify whether these include an FI;
- information regarding the FI(s) party to the relevant financial transaction, to determine whether it (they) must be treated as established in the EU FTT zone;
- the capacity in which each FI (party to the relevant financial transaction) is acting, to determine (if necessary) which FI is liable to pay FTT;
- (if necessary) the identification of the PMS in which the FI liable to pay FTT must be treated as established, to determine the collecting tax authorities;
- the identification of specific party, transaction or counterparty characteristics necessary to determine the applicability of an exemption;
- the consideration (notional amount or other) for the relevant financial transaction, to determine the taxable amount of the FTT;
- the applicable rate, to determine the FTT chargeable;

- the moment at which the relevant financial transaction occurs, to determine when the FTT becomes chargeable; and

- the date of payment of the chargeable FTT, to determine whether late payment penalties and interest apply.

1.2 Gathering of FTT liability data

For the sake of completeness, we should point out that depending on the chosen model of FTT collection, all the information required to calculate the chargeable FTT need not necessarily be reported in a formal tax return: under a delegation model part of the information could be included in separate reporting performed by the delegating FI; in a model linked to central clearing/settlement or to a new utility, the required information could be included in the instructions/inputs fed into the clearing/settlement system or the utility. The central system would need to send information to the tax authorities.

2. Key elements of a standardized FTT return format

Further to the above, we would envisage the FTT tax return having the basic content set out in the following sub-sections, with certain additions applying depending on the chosen model of FTT collection (see section 8.3).

In view of maximizing the harmonization and cost-efficiency of FTT collection with respect to what will be numerous covered transactions, we would envisage FTT tax returns being filed electronically. Ideally, this electronic filing would be made through a common portal created at the level of the EU FTT zone, to which all PMS would have access. Alternatively, it could be made through a portal in the PMS of establishment of the declarant, which would then forward a copy to each PMS for which the tax return shows chargeable FTT (this option would be somewhat similar to the current intra-EU VAT refund process).

We note that the choice of portal need not affect the audit process for FTT, which could either be carried out exclusively by the PMS of establishment of the declarant, or by another PMS relying on assistance from the PMS of establishment of the declarant under the EU administrative cooperation and mutual assistance directives.

2.1 General and taxpayer identification data

General information

- Period covered: month and year

- Return version number[13]

[13] The various possible establishment criteria for FIs are set out in Article 4(1), a) to g). The identification of the applicable criterion for each transaction included in the tax return would enable (ideally automatic) identification of the PMS of collection.

Details of declarant

- Legal identity
  - i. Name
  - ii. Address
  - iii. National identification number (or unique Legal Entity Identifier reference number if available)
- Establishment[14]
  - iv. PMS of establishment
  - v. Applicable criterion
  - vi. If counterparty is applicable criterion (article 4(1)(f)), details of counterparty
    - 1) Name
    - 2) Address
    - 3) National identification number (or unique Legal Entity Identifier reference number if available)
    - 4) Establishment
      - a) Applicable criterion
      - b) PMS of establishment
- Capacity of involvement: in own name and for own account, or in the name or for the account of another FI
- Representative
  - vii. Name
  - viii. Function
  - ix. Address if different to that of declarant
  - x. Telephone
  - xi. Email
- Date
- Signature

[14] The various possible transaction types are set out in Article 2(2). The identification of the applicable type for each transaction included in the return would enable (ideally automatic) determination of the applicable FTT rate (which will depend on the PMS of collection, assuming the potential for rate differentiation as provided for in article 9(2) is retained.

2.2 FTT liability data

Details of financial transactions

- Financial instrument Cusip code (or other identifier if not available)
- Issuer CSD code (if available)
- Transaction type[15]
- Occurrence date
- EUR (or EUR equivalent amount of) consideration or notional amount

FTT Liability

- Chargeable transactions
    i. Applicable tax rate: higher rate or lower rate16
    ii. PMS of collection
    iii. Chargeable FTT
    iv. Payment date
- Exempt transactions: ground for exemption[17]

Recapitulative fields

- FTT chargeable at higher rate
- FTT chargeable at lower rate
- Amount of exempt transactions

[15] Corrections to previously declared transactions could either be processed through the filing of a corrective return for the relevant period, or through the entry of a negative amount as a taxable basis in the return for a later period. The second option would at first sight appear preferable from an efficiency perspective.

[16] The higher rate refers to that set by PMS pursuant to Article 9(2)(a) and the lower rate refers to that set by PMS pursuant to Article 9(2)(b).

[17] The various possible grounds for exemption are set out in Article 3 and Article 10(2).

3. Application under the potential FTT collection approaches

The final format of the FTT return will ultimately be impacted by the chosen collection approach.

The following sub-sections detail how the standardized FTT return format set out in section 2 above, would be applied under each of the theoretical collection models proposed in section 6 above.

3.1 Approach 1: Self-administered - Standardized FTT return

Under Approach 1 ('Self-administered') as set out in sub-section 6.2 above, all FIs determine, pay and report FTT due from them under the proposed Directive.

We anticipate that the tax return format proposed in section 9.2 would be directly applicable to a self-administered FTT collection approach. In case of contractual delegation, which is likely to be applied in the market, the 'Representative' section would be completed with the contractual delegate's details.

In case of electronic filing, which we advocate, the transactions reportable in each monthly tax return should be electronically uploadable into the return. Alternatively, in case of manual returns, a trading journal similar to the one kept by Swiss securities dealers (who are responsible for collecting and reporting Swiss transaction tax) could be envisaged. The collection and reporting system under approach 1 would thus be fairly similar to the Swiss transaction tax regime described in section 3.

Finally, as previously highlighted, the application of the intermediary exemption laid down in article 10 (2) may require disclosure of information to preceding FIs in a transaction chain, in order to allow completion of the 'Details of counterparty ' section in the FTT returns filed by the various FIs.

3.2 Approach 2: Delegation of collection responsibilities - 'Expanded' standardized FTT return

As described in section 6.3., approach 2 is a variant of the self-administered model, the key differentiator being a transfer of collection responsibilities which is legally recognised by a Directive or implementing measures, to another FI or potentially to another specialised service provider.

From an FTT return filing perspective, the proposed standardized FTT return could be used in a similar way as under approach 1, with the delegated FI filing the FTT return on behalf of the delegating FI (as indicated in a specific 'delegation' field).

The delegating FI would in such case not be required to file a separate FTT return nor to perform separate reporting, subject to the following conditions:

- an audit trail requirement establishing by whom FTT collection/reporting has been assumed for any given transaction,
- the exclusion of certain FI types from assuming FTT collection delegation responsibilities, and
- the obligation for FIs to accept delegation responsibilities if certain information requirements are met.

For the sake of completeness, we note that the delegated FI would file separate FTT returns in respect of its own chargeable FTT transactions.

3.3 Approach 3 and 4: Central collection (with limited or expanded) functionality - No FTT return

As previously explained in section 6.4, a central FTT collection approach would require each FI involved in a transaction which might be liable for FTT (or its appointed agent), to provide the central party (CSD, CCP or new utility) with information (by way of a transaction flag) to indicate what FTT (if any) is due to which PMS. The CCP/CSD would then act as collecting/paying agent for the FIs.

FIs liable for FTT would not be required to file separate FTT returns.

Finally, aggregated FTT reporting by the relevant CCP/CSD or new utility could be envisaged, again similarly to the reporting by CREST in respect of UK SDRT c.q. by Euroclear France in respect of French FTT (possibly including an annual report for audit purposes, as compiled by Euroclear France for the French tax authorities).