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► **To cite this version:**

Lisa Kastner. Delayed Industry Capture: A Lobbying Analysis of the EU Financial Transaction Tax. 2015. hal-02385476

**HAL Id: hal-02385476**

**<https://sciencespo.hal.science/hal-02385476>**

Submitted on 28 Nov 2019

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## Delayed Industry Capture

### *A Lobbying Analysis of the EU Financial Transaction Tax*

*Author: Lisa Kastner*

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In January 2013, eleven euro zone states, including France, Germany, and Italy, decided to introduce a Financial Transaction Tax (FTT) with the goal of making the financial sector contribute to the cost of economic recovery after the 2008 financial crisis as well as creating disincentives for speculative trading.[1]

At first sight, the case of the EU FTT shows all signs of drastic “industry capture,” whereby financial sector groups dominate the policy process. The initial Commission proposal of September 2011 included a broad-based FTT, with very few exemptions.[2] However, as a consequence of massive industry lobbying, exacerbating differences among member states during subsequent negotiations, the Commission proposal was considerably watered-down. The initial start date for an FTT of January 2014 had to be repeatedly postponed.[3] There is wide-spread agreement among financial experts, market participants, and academics that the final version of the FTT will differ substantially from the initial proposal, resembling a narrow tax with many exemptions for various financial instruments. Despite continued statements of support for an FTT by heads of state and government as well as finance ministers of participating member states renewing their political commitment to an FTT, market participants are now anticipating a start date of January 2017.[4]

From the beginning, the financial sector rallied its troops against the proposed reform. Ahead of a G20 Summit in Cannes in November 2011, the Global Financial Market Association (GFMA), which speaks for the leading financial firms, sent an open letter to policymakers, urging them “to reject any FTT proposal that might be raised and discussed at the upcoming G20 Finance Ministers and Leaders meetings.”[5] Financial industry groups were unified in their opposition with “nobody in the industry in favor of an FTT.”[6] While industry groups have been largely successful in watering down the Commission proposal as well as in their advocacy for various exemptions, a closer look at the different stages of the policy cycle reveals a different picture about lobbying success. Industry’s initial attempts to block legislative action in the early phases of agenda-setting clearly failed. Despite investing massive resources into lobbying and despite their unified opposition, EU-based financial sector groups were not able to exercise influence over the agenda-setting phase of regulatory reform.

This raises questions about constraints on “regulatory capture” theories, whereby industry interests are said

to have dominated the financial reform process.[7] If the financial industry lobby was able to massively water-down the proposed FTT during negotiations, why was it not more successful in preventing the political decision to introduce an FTT among eleven member states during the agenda-setting stage? I will show that interest groups dynamics changed in the aftermath of the financial crisis, with financial industry groups temporarily losing their privileged access to the policymaking process, even with regard to core matters to their interests, such as taxation.

## Policy Debate and Lobbying Camps

In light of the political pressure from key member states and strong public support of an FTT, the Commission announced its proposal for an EU-wide FTT in June 2011 for financing the EU budget. The proposal identifies such a tax as base for a new own resource system giving extra room for maneuver to national governments and contributing to general budgetary consolidation efforts.[8] In September 2011, then, the Commission presented a first draft Directive for an EU-wide FTT. After the Commission proposal was met with resistance from some member states, notably the UK, the Netherlands, and Sweden, a sub-group of eleven member states, led by France and Germany, decided to proceed with the implementation of a transaction tax via the so-called “enhanced cooperation” procedure, which binds only participating member states to introduce the tax. The Commission adopted a new proposal for a Council Directive in February 2013, proposing enhanced cooperation for an FTT.

The political debate about an EU FTT was the subject of vocal and wide-spread campaigns by civil society activists. Pro-tax campaigns, promoting a small tax on the financial sector with its revenue attributed to public finances as well as global development assistance, mobilized to pressure policymakers. When the financial crisis hit, these groups were well-prepared. A network of development NGOs had been campaigning for a “Tobin tax” on currency trading for decades, since the idea first gained political traction as part of the anti-globalization movement in the 1990s to raise money for developing countries.[9] In September 2009, right after the crisis, several NGOs sent a letter to the G20 urging heads of state and government to implement an international FTT “to pay for the cost of the crisis in the north,” “to assist countries in the South to meet their development objectives,” and to “contribute to a reduction in speculation.”[10] By late 2009 to early 2010, groups supporting an FTT became more organized. Several national campaigns in support of an FTT—dubbed a “Robin Hood Tax,” spanning not only currency transactions but all sorts of financial instruments—were initiated by civil society groups, which were successful in gathering wide-spread political support in Germany, Italy, and the UK. Campaign groups promoted a tax with 50 percent of the revenue spent domestically and 50 percent spent internationally.[11] When prospects for the introduction of a global or EU-wide tax faded, groups mobilized for an FTT via enhanced cooperation with revenues to be shared between international development, member states, and the EU institutions.

Conversely, and unsurprisingly, tremendous opposition to the FTT proposal came from the banking industry. From the very beginning, financial industry groups were unified in their opposition to an FTT. In the words of one lobbyist, “all [...] financial institutions agreed that we completely disagree.”[12] The day the Commission presented its proposal for the introduction of an EU-wide FTT in September 2011, the *Financial Times* headline read: “Business attacks transaction tax plan.” According to the article, “the proposal has been fiercely resisted by financial and business interests in Europe, pointing to a fierce political battle that lies

ahead.”[13] After it had become clear that eleven member states were going ahead with its implementation and the likelihood of legislative success increased, industry groups intensified their lobbying against the legislative proposal to implement an FTT.[14] The proposal was subsequently substantially watered down during negotiations among the eleven participating member states, which started in February 2013. It now seems likely that the draft Directive will end up as a narrow-based FTT, similar to the UK Stamp Duty Reserve Tax, a 0.5 percent tax covering only share transactions.

Despite the industry’s success in watering-down the proposed FTT, the decision to introduce a policy directed at penalizing the financial sector speaks to the inability of industry groups to affect the policy agenda in line with their preferences. At the same time, the civil society campaigns in favor of an FTT were successful in channeling widespread public support and influencing the initial agenda-setting phase. Peter Wahl, the German campaign leader, concluded about the proposed Directive that, “for civil society the process is nevertheless a great success by now.”[15] How can we explain the initial failure of industry groups to derail an EU-FTT, despite their unified opposition?

## Industry Lobbying in the Post-Crisis Financial Regulatory Environment

In the post-crisis context, heads of states and governments, and notably French president Nicolas Sarkozy and German chancellor Angela Merkel, became interested in the FTT as a populist policy measure to appease public opinion. Increased public attention on financial reform made the regulatory dialogue also less conducive to private sector influence. In those early phases of the reform, financial industry groups, faced with adverse public opinion, were not successful in vetoing policy change. In the midst of the financial crisis, the dialogue among policymakers and private sector groups was generally more adversarial than it had reportedly been during pre-crisis times. Expressing frustration about heightened public attention regarding the proposed FTT, one industry lobbyist complained that it was “difficult to have reasonable discussions if it becomes so much politicized.” The context for regulatory debate had noticeably changed for private sector groups and the mood-swing in public opinion was clearly felt by industry lobbyists. As this industry representative complained: “If there are behaviors which should be prohibited, let’s prohibit them. But pretending to introduce a tax to regulate is an argument which uses the fact that there is a political opinion shared by citizens that banks are bad.” Public outrage and de-legitimization of the industry was clearly felt by financial sector lobbyists who perceived the FTT as retribution for wrongdoings that led to the crisis. In the words of one interviewee: “We are the ones to be punished.”[16]

Increased public attention to the regulatory reform process was accompanied by divisions among policymakers and the private sector. One important way in which the regulatory environment had changed was that policymakers started to call industry groups’ expertise into question. Public attention to financial debates had clearly weakened incentives for elected officials and politicians to openly heed demands coming from the financial sector. Wolfgang Schäuble, the German finance minister, for example, dismissed arguments from the opposing camp in November 2011: “The objections made by some who claim it would mean a substantial drop in employment and in the economy generally seem to rest on exaggerated and sharply challenged projections—and, more important, ignore the potential of such a tax to stabilize currency markets in a way to boost rather than damage the real economy.”[17]

Statements of industry lobbyists in Brussels and London corroborate a story that their influence on the

particular content of the proposed FTT prior to the publication of the Commission's first draft Directive in September 2011 was rather limited. Before the financial crisis, industry groups were used to exchanging information with Commission officials at early stages of the legislative process, even before the publication of draft Directives. After the financial crisis, industry lobbyists had temporarily lost their privileged access to the policymaking process. One industry representative complained that, apart from the Commission's public consultation between February and April 2011, there had been no pre-legislative discussion among financial industry groups and Commission officials before the publication of the first FTT draft proposal in September 2011. In the perception of another industry representative, the Commission worked on the draft Directive "in complete isolation, not with the industry." And this industry lobbyist reported that information exchange was difficult; he felt the Commission was "shying away" from working with industry groups. Other commentaries from financial lobbyists confirm that despite "a lot of talk about the lobbying machine of the financial sector working its magic," it was "difficult to have constructive discussions" with the European Commission and the European Parliament on the FTT. Financial sector participants were generally frustrated by the policy process and their inability to exert influence. One interviewee stated that his association was "having a very tough time" when trying to engage in discussions with policymakers about the FTT.[18]

In the post-crisis context, industry groups realized that their arguments seemed to matter less to policymakers. For industry lobbyists who reported having meetings with Algirdas Šemeta, the Commissioner for Taxation and Customs Union, Audit, and Anti-Fraud, as well as with Commission officials, discussions "did not have a significant impact on the direction the Commission was traveling." One disgruntled lobbyist reported that the Commission was generally "dismissive" about industry concerns. Another industry representative reported: "I know that the financial sector has spoken of its frustration that the Commission has such entrenched views. [...] To all the complaining the financial sector is doing, it is kind of irrelevant to them." In his view the Commission proposals did not reflect any interaction with industry. This explains why industry representatives were irritated when they read the first Commission draft. Private sector lobbyists reported that they thought the Commission draft, once proposed, was "that bad, you have to restart from scratch," that "not a single measure [was] acceptable," that it did not "accurately reflect how the financial markets work," and that the design of the tax was "fundamentally flawed." Taken together, then, there is good evidence that the financial industry was not able to exercise effective influence over the agenda-setting phase of the regulatory policy process.[19]

Changes to the post-crisis financial regulatory environment also forced financial industry groups to adapt their lobbying strategies. From the beginning, financial industry groups saw their advocacy efforts directed at blocking or vetoing any legislative proposal regarding an FTT largely curtailed. This industry representative complained that financial sector groups "couldn't do anything for political reasons," saying that in the context of the crisis they "were not in a position to take action" to affect policy decisions. Aware of the potentially negative consequences for their reputation, financial sector groups did, for example, employ only limited "outside lobbying strategies," whereby interest groups go beyond the legislative arena to lobby policymakers with media activity or the mobilization of grassroots. In the context of huge bailout costs using taxpayer's money, the financial services industry was facing serious reputational problems, and saw itself deprived of the usual lobbying repertoire, as one financial lobbyist reported: "It is very difficult for the banking sector for example to go all out and oppose an FTT when they are beneficiaries of government bailouts [...]. The financial sector has found it very difficult to publicly articulate their opposition to the FTT without seeming to be just serving their own interest. [...] the financial services sector has such a bad

reputation.” Private sector groups refrained, for instance, from publishing position papers opposed to the FTT in order to avoid negative publicity.[20]

## Conclusion

Taken together, then, there is good evidence against the proposition that EU-based financial industry groups exercised effective influence over the agenda-setting phase of financial reform. Regarding the policy decision to introduce an EU FTT, industry groups did not fare very well in the early stages of the policy cycle and saw themselves deprived of their full lobbying repertoire. Industry complained about a lack of consultation and subsequently perceived proposed regulatory reform extremely negatively. These findings based on anecdotal evidence from interviews with industry lobbyists in the aftermath of the crisis suggest that the direct leverage of financial industry groups over the agenda-setting phase of the policymaking process was more constrained than before the crisis.

Furthermore, these findings suggest that scholarly work on financial regulatory politics would benefit from more nuanced understanding of the traditional capture narrative. EU financial industry groups have been largely unsuccessful in their attempts to block regulatory change during agenda-setting, although they had bitterly opposed an FTT from the beginning. The political decision to introduce an FTT among a sub-group of EU member states, with support of the European Commission and the European Parliament, was a major success for the mobilized civil society coalition. It remains to be seen how much the FTT proposal will be watered down during the technical discussions taking place in Council working groups at the time of writing. Latest reform proposals indicate that reformers prefer a scaled-down version of the tax, thereby giving up on structural changes. The FTT is therefore likely to miss the mark of effectively raising revenue and tackling speculative trading. Pro-reform groups, so it seems, have only been able to delay financial industry capture, not to prevent it.

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[1] Council decision 22 January 2013 authorizing enhanced cooperation in the area of financial transaction tax (2013/52/EU).

[2] According to the proposal, the tax would be levied on all financial transactions between financial institutions when at least one party to the transaction is located in the EU (“residence principle”). The proposal included a harmonized minimum 0.1% tax rate on shares and bonds and of 0.01% on derivatives with revenues generated being shared between the EU and member states. To avoid individual citizens being negatively affected, the scope of the proposal excluded most consumer products, such as insurance contracts, mortgage lending and consumer credit. The Commission estimated that the tax would raise between €57 billion every year (European Commission, “Press Release – Financial Transaction Tax: Making the Financial Sector Pay Its Fair Share,” 2011, available at: [http://europa.eu/rapid/press-release\\_IP-](http://europa.eu/rapid/press-release_IP-)

11-1085\_en.htm?locale=en.)

- [3] Hubert Zimmermann, "EU-11 Als Globale Avantgarde?: Die Verhandlungen Um Eine Finanztransaktionssteuer," 2014, [http://edoc.vifapol.de/opus/volltexte/2014/5394/pdf/GGS\\_2014\\_02\\_de.pdf](http://edoc.vifapol.de/opus/volltexte/2014/5394/pdf/GGS_2014_02_de.pdf).
- [4] KPMG UK, "European Financial Transaction Tax," 6 August 2015, <http://www.kpmg.com/uk/en/services/tax/corporatetax/pages/european-financial-transaction-tax.aspx>.
- [5] GFMA, "GFMA Submits Letter to G20 Finance Ministers in Opposition to the Financial Transaction Tax," 2011, <http://www.gfma.org/correspondence/item.aspx?id=49>.
- [6] Interview with financial industry representative, London, 18 June 2013.
- [7] For a more detailed discussion of regulatory capture see Stefano Pagliari, *Making Good Financial Regulation: Towards a Policy Response to Regulatory Capture*, International Centre for Financial Regulation (Guildford, Surrey: Grosvenor House Publishing Ltd., 2012).
- [8] Communication from the European Commission, "A Budget for Europe 2020."
- [9] James Brassett, *Cosmopolitanism and Global Financial Reform: A Pragmatic Approach to the Tobin Tax*, 1 edition (Milton Park, Abingdon, Oxon ; New York: Routledge, 2013).
- [10] WEED, "International Financial Transaction Tax on the Pittsburgh Agenda," 2009, [http://www.globaleverantwortung.at/images/doku/g20\\_pittsburgh\\_financialtransactiontax\\_sept09.pdf](http://www.globaleverantwortung.at/images/doku/g20_pittsburgh_financialtransactiontax_sept09.pdf).
- [11] Interview with NGO representative, London, 12 June 2013.
- [12] Interview with industry representative, Brussels, 22 May 2013.
- [13] "Business Attacks Transaction Tax Plan." *Financial Times*, 28 September 2011, <http://www.ft.com/intl/cms/s/0/f9d2188a-e9ec-11e0-a149-00144feab49a.html#axzz2NnsvMIJ>.
- [14] Interview with Commission official, Brussels, 12 May 2013.
- [15] Peter Wahl, "The European Civil Society Campaign on the Financial Transaction Tax," Working Paper for the Global Labour University project "Combating Inequality," Geneva, 2014, [http://www.global-labour-university.org/fileadmin/GLU\\_Working\\_Papers/GLU\\_WP\\_No.20.pdf](http://www.global-labour-university.org/fileadmin/GLU_Working_Papers/GLU_WP_No.20.pdf).
- [16] This section is based on interviews with industry lobbyists conducted in Brussels and London in May and June 2013.
- [17] "Archbishop of Canterbury Rowan Williams Calls for New Tax on Bankers," *The Telegraph*, 1 November 2011, <http://www.telegraph.co.uk/news/religion/8863794/Archbishop-of-Canterbury-Rowan-Williams-calls-for-new-tax-on-bankers.html>.

[18] This section is based on interviews with industry lobbyists conducted in Brussels and London in May and June 2013.

[19] Ibid.

[20] Ibid.

## About this Publication



**Author:** [Lisa Kastner](#)

**Published:** November 2, 2015

**Topics:** [Business and Global Markets](#), [Debt Crisis and Financial Regulation](#)

**Tags:** [Economic & Financial Policy](#), [Eurozone](#)

**Type:** [Transatlantic Perspectives](#)

**Program:** [Business & Economics Program](#)

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