The draft Financial Transaction Tax (“FTT”) Directive that the European Commission released in February 2013 can affect businesses in sectors other than financial services, including those in the oil and gas, agribusiness and power production industries that trade commodities, whether as a core revenue generating activity or for hedging purposes.

Although in April 2013, the UK challenged the legality of the legal procedure being used to implement the tax, work is still continuing to define the shape of the tax and there is political will to implement an FTT.

What is the draft FTT Directive about?
The draft FTT Directive taxes most financial transactions undertaken when at least one party to a transaction is a financial institution “established” in an FTT-zone country (see map on page 2). The draft FTT Directive consists of a set of rules that define the specific types of financial transactions that are caught, the types of entities deemed to be a financial institution for the purposes of the tax, when a business is deemed to be established in an FTT country, tax rates, when the tax becomes due and general rules on compliance.

Importantly, a financial institution can include treasury or holding companies or entities which carry out more than a certain proportion of their activities in relation to financial transactions. If the directive is implemented in its current form, this means that financial institutions (as defined) will be liable for FTT if either its counterparty is established in an FTT-zone country or if it trades a financial instrument issued in an FTT – zone country. The draft Directive states that the tax will be implemented on 1 January 2014, but there is a real chance that this date may change, as agreement must still be reached on what the final version of the tax will look like and potentially due to the UK’s legal challenge.

Currently, there are 11 EU Member States that have formally committed to implementing this tax. These countries, including Germany, France, Italy and Spain, are now in the process of negotiating the Directive’s final draft and the draft text of the legislation may change through these negotiations.

How does it affect non-financial institutions?
The draft Directive contains a list of entity types that are deemed to be financial institutions for FTT purposes. These entities will be obliged to account for FTT when they are established in the FTT-zone for the purposes of a financial transaction. Most of the types of businesses on the list are what one would typically consider financial institutions (banks, hedge funds, etc.). However, the Directive could catch non-financial institutions that have subsidiaries or operating units which enter into a significant amount of financial transactions. This could include subsidiaries trading in commodities and engaging in treasury-related activities.

If a business is deemed to be a financial institution, it may be obliged to account for FTT on certain of its activities and meet FTT-related compliance requirements. This could have an effect on a business’s bottom line. Furthermore, even if it is not a financial institution, it should be aware of counterparties who are subject to FTT that could try to push FTT costs onto it. Furthermore, another consideration for businesses that are not in the financial services sector is the position of its treasury function. Depending on the activities of this function, it could be deemed to be a financial institution, with the result being that FTT could be charged on intra-group financial transactions.

Which transactions should commodities traders be concerned about?
The draft Directive subjects a wide range of transactions to FTT. These range from the sale of stocks and bonds to sophisticated derivatives transactions. For those who trade commodities, in-scope financial instruments include (with the notable exception of spot transactions) options, forwards and futures “that must be settled in cash or may be settled in cash at the option of one of the parties.” This catches transactions that may be settled only financially, but also appears to catch commodity trades that can be physically delivered, such as futures.
What should I be doing about FTT?
The first step is to gain an understanding of what the legislation states and to raise awareness of the potential consequences of the legislation internally. Businesses may also consider undertaking an impact analysis project to fully scope the impact of the draft Directive on group entities and financial transactions undertaken, both in financial and operational terms. Also important is to network with relevant industry groups and to make any concerns known to contacts in government who are addressing FTT.

What are my peers doing about FTT?
Awareness of FTT among those outside of the financial services sector has risen significantly since the draft Directive’s release. Businesses outside of the financial sector are at various stages of evaluating the draft Directive. Several clients have pulled an internal team together than includes representatives from areas such as tax, finance, operations, IT, regulatory and those who actually undertake the trading activities to evaluate the legislation to determine what the legislation could mean to their business. Key areas of concern that have arisen include:

- determining whether the draft legislation results in any part of their business being deemed a financial institution;
- understanding the calculation contained in the legislation that relates to whether an entity is to be considered a financial institution;
- identifying potential products and transactions are caught by the legislation;
- obtaining an understanding of how FTT compliance and payment processes and procedures could take place; and
- considering whether any structural or strategic solutions should be implemented now in readiness for the FTT directive.

We anticipate that many businesses will need to address these issues, as well as those unique to their activities. It is important to tackle the challenges proposed by FTT as early as possible to identify how the tax could affect your business, to prepare for the tax to the extent possible and to minimise its effects.

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