The bank levies in Slovakia and in other EU countries[1]

Bankové odvody v SR a v EÚ

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Abstract

In the light of the crises many EU countries have already introduced their own levies on bank borrowing with the aim of reducing risk in the financial sector. But these levies vary significantly between the countries, especially regarding the tax base. Some of them have been introduced as taxes funding general budget, others as regulatory levies arising to a fund separated from the general budget. It can be stated that the bank levies have economically significant effect on banks funding choices. It is estimated that the banks increased their equity-asset ratio by 1-1.5 % on average in response to levies. The paper deals with the taxation of the banking sector via bank levies, pointing to the diversity of bank levies and future arrangements.

Key words: taxation of financial sector, bank levy, banking union

JEL Classification: H20, G21,G28

Introduction

Excessive risk taking by financial institutions is regarded as the main cause of the global financial crises in 2007-2008. Prior to the crisis, the banks invested mainly in mortgage-backed securities (the risk of which was underestimated), while at the same time they were relying on the short-term borrowing for funding.

The banking crises are expensive. They may involve large fiscal costs, because a significant amount of public funds is required for stabilization of the banking sector. To avoid a collapse of the entire financial system, governments intervened by providing the banks credit loans, long guarantees or a new capital. During the recent financial crises, the fiscal costs of bank recapitalization and assets relief (in the period 2008-2013) reached 4.9 % of GDP and government guarantees reached 6.5 % of GDP in 2012. Therefore, the G-20 asked the IMF, to prepare a report that studies the scope of special taxes on banks in order to raise a fair and

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substantial contribution from the financial sector. Subsequently, 15 countries in the EU introduced some sort of bank levy. [6].

The objective of the bank levy is to raise revenue to cover the fiscal cost of banking crises and thus to compensate the governments and taxpayer for provision of guaranties as well as to internalize externalities (like Pigovian tax) associated with government guaranties.

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1. The taxation of the financial sector in the EU

The European Commission enforces taxation of the financial sector not only because the financial sector was the main cause of the financial and economic crisis and it could therefore contribute via increased or new taxes to fiscal consolidation after crisis, but also because the taxation of the financial sector could complement basic regulatory measures designed to increase the efficiency and stability of financial markets and reduce their volatility. It must be taken into consideration also the fact that the financial sector - selected financial services are exempt from VAT in the EU. In this way, taxation of the financial sector could ensure higher tax fairness.

At the EU level, there are discussed two concepts of taxation: the Financial Transaction Tax (FTT, also known as a Tobin tax[2]) and the Financial Activities Tax (FAT). These two instruments represent two different approaches to taxation. While the FTT is a turnover tax on financial transactions, the FAT is a profit and remuneration based tax[3].

Many EU countries prefer imposing a national special bank levy/tax over a common financial transaction tax. On the other hand, the European Union as a whole enforces the introduction of a common tax on financial transactions[4]. The tax would be a sort of generalised Tobin tax, which would be levied on a broader set of financial transactions than foreign currency transactions alone, as originally proposed by Tobin.

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[2] TOBIN, J., 1978. A Proposal for International Monetary Reform. In *Eastern Economic Journal,* Volume 4 (Issue 3-4), p. 153-159.

[3] European Commission, 2010. Financial Sector Taxation, Working paper No.25, 2010.

[4] FTT would be applied to all financial transactions in particular those carried out on organised markets such as the trade of equity, bonds, derivatives, currencies, etc.

On 28 September 2011, the European Commission made a Proposal for a Council directive on adopting FTT in the European Union [3]. According to the original plans a new tax should be applied from 2014, with an EU-wide tax rate of 0.1% on bond and equity transactions and of 0.01% on derivative transactions between financial firms.

Many EU countries are of the opinion that the “new tax” can help to ensure that the financial sector will more fairly and significantly contribute to the public budget revenues in order to provide additional source of income and to help in creating the stable and efficient financial sector.

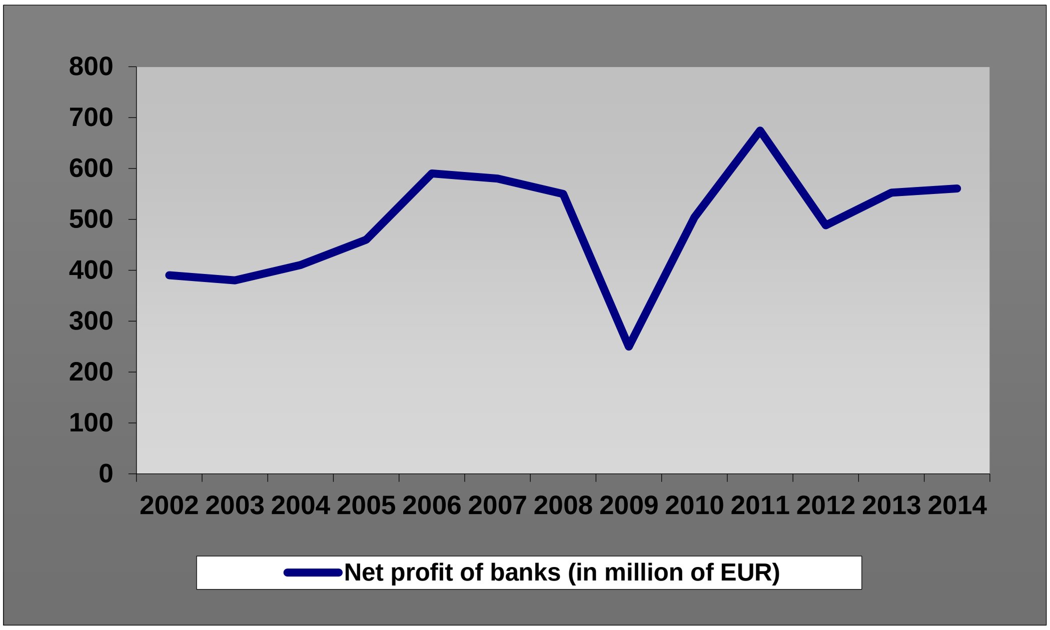
In June 2010, the IMF has presented a report [5] on possibilities for taxing the financial sector. IMF proposes taxation of financial sector as the compensation for the financial sector exempt from VAT. On the other side, the IMF is against the financial transaction tax (known as the Tobin tax) and proposes taxation, which would simulate the VAT and which does not burden the financial sector - the financial activities tax (FAT).

2. The taxation of the banking sector in Slovakia

The banking sector in Slovakia is highly profitable. It wasn’t influenced by the crises in such negative way as the banking sectors in western European countries. Although there was a drop in the net profits in 2009 more than 50 % compared to 2008, the net profit of the Slovak banks reached the pre-crisis level already in 2010 and in 2011 there was a year-to-year increase in profit of 34 % comparing to 2010.

Graph 2

Net profit of banks and branches of foreign banks in Slovakia (in million euros)



Source: Data from Financial Stability Reports for 2003-2014. National Bank of Slovakia, www.nbs.sk

In 2012, the net profit of banks fell up to 27 % in comparison with 2011. The main reason for a decline in the banks' profitability was the introduction of the bank levies (bank taxes) in 2012. Since 2013, the profitability of the Slovak banks is rising slightly, but at a slower pace as it was in the period 2010-2011. It was influenced mainly by a decline in the interest rates of retail loans and increase of the cost of credit risk.

Since 2012, Slovakia has joined the states that have introduced a special bank tax (levy), with the aim to gain resources which could be used for fiscal consolidation[5]. In 2012, approximately 170 million euros was collected from special levies paid by the Slovak banks and more than 500 million euros was collected until August, 2014.

Table 1 **Bank tax (levy) launched in Slovakia in 2012**

	(Initial) Bank tax since January 1, 2012	**(Increased) Bank tax since September 1, 2012**	**Special (extra) bank tax only in 2012**
Rate	0.4 %	0.4 %	0.1 %
Tax base	Liabilities - own equity – protected deposits	Liabilities - own equity	Liabilities - own equity
Expected yield	EUR 100 million per year	EUR 200 million per year	50 million in 2012

Source: Laznia, M. (2012).

[5] According to the Act No. 384/2011 Coll. on specific levy for selected financial institutions

The bank tax in Slovakia is levied at the rate of 0.4 % (table 1)[6], which is the highest among EU countries (the average European rate is some of 0.05 %) except Hungary. According to the act on specific levy for selected financial institutions if the total amount of the bank levy in Slovakia exceeds 500 million euros, the rate of bank levy drops to 0.2 %. The statutory condition was fulfilled in July 2014 and since 2015 the tax rate will decrease to 0.2 %.

3. The taxation of the banking sector in the EU countries

It should be noted that the introduction of the bank taxes or levies has already been realized in several EU countries. Over the period 2009-2012, fourteen countries in the EU adopted the bank levies. The states mostly used argument that the bank tax will generate funds for coverage of any future financial crisis. The states use different options for the calculation of the tax basis on which the bank tax is levied - it can be an asset of the bank, bank liability, respectively bank profits and bonuses.

The first state, which introduced the bank tax in 2009, was Sweden. The bank liabilities are taxed at 0.036 % tax rate. Introduction of tax levy was justified by the fact that the imposed tax creates a financial reserve for a crisis and also encourages banks to increase the amount of own funds (equity, reserves and retained earnings) at the expense of borrowed funds. Financial resources from the bank tax are concentrated in a special fund.

The most common design of bank levy was introduced in 11 countries (Austria, Belgium, Cyprus, Germany, Netherlands, Latvia, Portugal, Romania, Slovakia, Sweden and the UK) and it taxes some measure of bank liabilities. But despite the similar features, the levies vary between the countries:

- The most of the levies fall on total liabilities net of costumer deposits that are guaranteed under a deposit insurance scheme, but some countries include insured deposits in the levy base (e.g. Cyprus).
- The most levies threat short-term and long-term liabilities symmetrically, but two countries apply a reduced rate to liabilities with maturity exceeding one year (the Netherlands and UK).

[6] Since September 2012, the Slovak banks paid “increased” bank tax of 0.4 % from broadened tax base including protected deposits (till September 2012 protected deposits were excluded form the tax base) and “extra” bank tax of 0.1 % from the same tax base (it was paid only in 2012).

- The most countries apply flat tax rate, but four countries have progressive rate structure, where small banks are taxes at lower rates than large banks or are not taxed at all (Austria, Germany, Netherlands and the UK).
- The UK has several provisions which narrow the taxable base.

On the other side, three countries (France, Hungary and Slovenia) implemented bank levies that are quite different from the levies in other 11 EU countries, mentioned above. In France, the taxable base is the minimum amount of capital necessary to comply with regulatory requirements. In Hungary, it was implemented the bank tax levied on total assets net of inter-bank lending and in Slovenia total assets are taxed.

Table 2

National bank levies/taxes in EU countries

	Tax rate	**Tax Base**	**Date of implementation**
Sweden	0.036 % (during 2009 and 2010 reduced to 0,018 %)	Liabilities minus own equity and subordinate debt	30.9.2009
Hungary	0.15 % from a tax base up to HUF 50 bln 0.53 % from a tax base exceeding HUF 50 bln	Hungarian bank assets minus domestic interbank loans and securities issued by other domestic credit institutions	27.9.2010
Belgium	0.15 % in 2010, 0.13 % in 2013, 0.08 % from 2014	Bank deposits of households and other insured products	2010
Germany	0.02 % from a tax base up to EUR 10 bln 0.03 % from a tax base between EUR 10 bln -100 bln 0.04 % from a tax base above EUR 100 bln 0.02 % - 0.06 % since 2013	Relevant liabilities of German banks minus customers deposits and other liabilities toward non-banks equity capital	1.1.2011
France	0.25 % from EUR 0.5 billion of minimal own funds requirement 0.50 % since 2013	Minimal amount of own funds (risk-weighted assets)	1.1.2011
Austria	0.055 % from a tax base between EUR 1 bln – 20 bln 0.085 % from a tax base above EUR 20 bln 0.013 % of the tax base of derivatives	Liabilities of Austrian banks minus nominal capital and reserves and assured bank deposits + financial derivatives	1.1.2011
Denmark	0.02 % from liabilities	Insured deposits and securities	2011
UK	0.075 % (for short-term funding) in 2011, 0.088 % in 2012, 0.13 % in 2013, 0.156 % in 2014 0.0375 % (for long-term funding) in 2011, 0.039 % in 2012, 0.065 % in 2013, 0.078 in 2014 - not applied to the first GBP 20 billion of liabilities	Liabilities minus insured bank deposits, tier 1 capital and repo liabilities secured against sovereign debt	1.1.2011
Portugal	0.05 % of total liabilities 0.00015 % of financial derivatives	Total liabilities and notional amount of financial derivatives (except Tier 1 and Tier 2 capital, insured deposits, hedging derivatives and back-to-back derivatives)	1.1.2011
Cyprus	0.095 % (the amount of bank levy will not exceed 20 % of taxable profit) 0.11 % since 2013	Total amount of deposits except interbank deposits btw. the banks operating in Cyprus and deposits made by foreign banks	April 2011
Romania	0.1 %	Total liabilities except of protected deposits	2.6.2011

Slovenia	0.1 %	Total assets	1.8.2011
Slovakia	0.4 % of the tax base 0.2 % since 2015	Total liabilities less the amount of equity (except of protected deposits in Slovakia till 9/2012)	1.1.2012 (changes since 1.9.2012)
Netherlands	0.044 % for short-term non-secured debts 0.022 % for short-term non-secured debts	Total liabilities (except Tier 1 and Tier 2 capital, protected deposits insured deposits)	1.10.2012
Finland	0.125 %	Total amount of risk-weighted assets at year-end	1.1.2013 (until 2015)

Source: According to [7], [8], [9].

In 2014, the European Union has agreed new resolution rules for all EU banks to complete the banking union - The Bank Recovery and Resolution Directive (BRRD), The Single Resolution Mechanism (SRM) and The Directive on Deposit Guarantee Schemes (DDGS). The aim is to prevent future financial crises by pooling responsibility for euro-area banks. Banks will begin paying levies in 2015, initially as part of national schemes, which will be absorbed into the common fund.

According to the BRRD, the Member states should establish in 2015 national resolution fund with a minimum target of 1 % of covered deposits. In the banking union, the national resolution funds set up under the BRRD as of 1 January 2015 will be replaced by the Single Resolution Fund for the banking union as of 1 January 2016. The main factor for determining contributions to the fund starting in 2016 should be the volume of a bank's liabilities apart from state-guaranteed deposits.

Conclusions:

Although Slovakia has introduced the bank levy in 2012 as the 12th country of the European Union, the Slovak banks paid the highest amount of the bank levy in proportion to the amount of assets from all EU countries. After the legal adjustment of the rate of the bank levy in 2015 (from 0.4 % to 0.2 %), Slovakia will still have the highest levy in the euro area, for example, compared to Germany more than three times higher. Since 2015, the Slovak banks will pay also new bank taxes associated with the preparation of the single banking union. The open remains the question of introducing a tax on financial transactions at EU level.

The European Commission enforces taxation of financial sector in order to complement basic regulatory measures designed for increasing the efficiency and stability of financial markets and reducing their volatility. The global nature of financial markets means that there must be international coordination not only in the financial regulation, but also in the additional taxation of the financial sector, although many EU countries prefer imposing national bank taxies over a common financial transaction tax at EU level. An international agreement, at least on basic principles for the taxation of financial institutions, will help reduce the incentive to avoid tax through the relocation and restructuring of financial activities.

While the creating banking union and the harmonisation of bank levy at EU level is generally a positive step to simplify cross-border banking business, it is clear that the new levy will increase the financial burden of banks under existing national levies and it will limit banks' ability to set aside retained earnings to build capital.

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