The Tobin Tax: How to Make it Real

Towards a Socially Responsible and Democratic System of Global Governance

Project Report by
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"… what is pragmatically possible is not fixed independently of our imaginations, but is itself shaped by our visions. Self-fulfilling prophecies are powerful forces in history, and while it may be Polyannish to say 'where there is a will there is a way', it is certainly true that without 'will' many 'ways' become impossible."

Erik Olin Wright

Summary

In the 1970's James Tobin proposed a low rate tax on financial transactions of currencies. This tax would make many speculative movements unprofitable and the financial system less volatile and sensitive to daily political news and anticipation of economic policy changes. Consequently, it would create space for more autonomous economic policies of states.

Tobin devised this second-best solution in the absence of realistic possibilities for the best option, namely global unification (single currency, central bank, and elements of economic policy). But he advocated simultaneous steps towards better governance of global economy. Twenty years after Tobin's original proposal, new rationales for the tax have risen: it would yield huge revenues both to the states and the world community; and it is also seen, more and more often, as an invaluable element in restoring democratic values and accountability. Moreover, the endless stream of world financial crises has corroborated Tobin's analysis and strengthened the appeal of his remedy.

This Report develops a new approach to making the Tobin tax real. The major problem has always been the lack of realistic political possibilities. Tobin and his followers have assumed that all major financial centres and most other states would have to consent with the idea before it is workable. We argue that this is not the case.

Hence, it is proposed that the Tobin tax could be realised in two phases: (1) In its first phase, the system would consist of the euro-EU and a group of other countries, or, alternatively, a bigger group of other countries without the EU. However constituted, this grouping should establish an open agreement – any state can join at any time – and a supranational body orchestrating the tax and collecting the revenues of a small underlying transactions tax (10 basis points, at most); much bigger exchange surcharge (1%-3% or even more); and a relatively high tax, perhaps 1%, on domestic-currency lending to non-residents (only to non-residents who are not yet within the tax regime). This arrangement would solve the tax evasion problem and is economically sound.

(2) In the second phase, which should be carried out either when all major financial centres and most other countries have joined the first phase system, or at latest by, say, year 2010, a

universal and uniform Tobin tax at a higher – yet absolutely low – 1% rate would be applied.

This arrangement is politically more realistic than any previous proposal. It would make it possible for a(ny) grouping of countries to proceed quickly without the consent of every state (including such financial centres as London/UK or New York/US), yet it would not compromise the aim of a universal and uniform tax. However, it is devised in such a manner that it would build up pressure for the outsiders to join it, too.

In the fifth chapter, we develop the idea of the Tobin tax organisation (TTO) and its relation to political principles of sovereignty, democracy and justice further. We argue that the Tobin tax regime should be seen as defending some aspects of state sovereignty, yet it also opens up new global political problems of governance.

The organisation that implements and supervises the Tobin tax must be empowered with surveillance capabilities and sanctions. Moreover, in itself, the tax constitutes a form of social control and regulation. The potentially huge revenues – in the second phase, possibly more than USD1 trillion a year – it creates can be used for economic and social purposes that must be determined globally. It thereby revives also the problems of justice and democracy in a new, global context.

We argue for an interim TTO that recognises the validity of the norms and ideals of democracy not by excluding non-democratic states but by giving some powers to a democratically representative and participatory body.

As far as the allocation of revenues is concerned, we make only two modest proposals (besides arguing that the collecting states should get a fair share of the revenues themselves, perhaps a third). The first proposal is to dedicate a relatively small part of the revenues to the UN system. This should give leverage to democratic reforms and prepare for, in the second phase, a more autonomous and democratic UN to take over the TTO (while perhaps leaving the headquarters and some parts of the structure and functions of the TTO intact). Also, it might be desirable to allocate some money for a global political campaign for the Tobin tax.

The second proposal is that it is absolutely crucial that all decisions about revenues will follow public, transparent, fair and democratic procedures, and that the decision-makers are strictly

accountable for their actions both to the member-states and the wider, democratic world republic. Only this will guarantee legitimacy of the decisions of the TTO, and later, possibly, the Economic Security Council of the UN.

Preface

When I first encountered the idea of the Tobin tax a few years ago, it was only a thing on a list of reform proposals, and it sounded rather technical. But it started to come forward more and more often in different contexts. When I first mentioned the Tobin tax in my own texts – in a book review of Martin's and Schumann's "Globalisation Trap" in *Helsingin Sanomat* in August 1997, and later the same autumn in a book on the politics of EMU (with Petri Minkkinen) – it appeared, again, merely as an element on a list of reform proposals. Now I realise that the Tobin tax is a much more interesting and deep idea.

This project was born in early October 1998. Having followed closely the slide of the financial crises in the world economy and the subsequent discussions about what to do, it suddenly appeared that the Tobin tax could be a project where the Network Institute for Global Democratisation, NIGD, and Kepa, Service Centre for Development Cooperation in Finland, could join forces. After intensive discussions with Katarina – my partner in love and politics, collaborator in this project and the co-founder of NIGD – and e-mail discussions with Mika Rönkkö from Kepa, the idea was elaborated, in ten days, into a project proposal.

The original idea was to write a research report on the Tobin tax both in Finnish and English to give substance and credence to a political campaign for it in Finland, orchestrated by Kepa. As can be seen, this happened, but not exactly in the intended way.

The original emphasis on the unilateral actions by Finland has gradually faded away. It was clear from the beginning that a unilateral currency transaction tax would have been more symbolic than real anyway, given that there has been, since the beginning of 1999, a close substitute for the Finnish *markka*, namely *euro*, and also because of more general problems of tax evasion.

However, the deep resistance against the idea at the Bank of Finland and the Treasury, as well as more generally among Finnish economists confirmed not only the general analysis of the role these institutions play everywhere in the world economy, but also that Finland might not, after all, be the place for the

emergence of innovative politics. Not a single person was willing to dirty their hands by writing an expert statement to this Report, despite my persistent efforts, and despite having asked them to write spontaneously whatever they think is appropriate concerning the Finnish currency markets and their taxation. More than once, it was clear that political correctness played a major role in these refusals.

It is true, of course, that in Finland, like in so many other countries, most political parties and their representatives in the Parliament (more than in the Government), NGOs of all kind alongside political movements are endorsing the Tobin tax, some of them enthusiastically. Perhaps this will soon translate into the will of the Government, too, particularly after the March 1999 elections. Either with other Nordic countries or via the EU, Finland could easily play an important role in making an initiative to establish a Tobin tax according to the two phase model this Report discusses.

Yet, looking at things from Nottingham, UK, it was much more encouraging to find enthusiasm for the project elsewhere in the world. Already when designing the project proposal, Katarina vaguely remembered having seen, in *Le Monde,* something about a new, large network advocating the Tobin tax in France. Immediately, I found the web pages of ATTAC (*Association pour une Taxe sur les Transactions financières pour l'Aide aux Citoyens*), that was founded in June 1998. Directly, and with the assistance of Mika Rönkkö who visited Paris at that time and contacted ATTAC, too, we started to discuss possibilities for cooperation. Soon, in early December 1998, I and Katarina – with our new born baby Anna – found ourselves in Paris in the founding meeting of International ATTAC. It is surprisingly easy to get from London to Paris by train, or to Europe, as they would say here in the UK. And a month and a half later we participated, again in Paris, in an expert meeting of international economists discussing the feasibility of the Tobin tax with the Scientific Committee of ATTAC. Some of the authors of the texts often referred to in this Report were there.

Also quite a few researchers in the Anglo-American academic world I contacted were excited about this project, and despite the very short notice, many of them were happy to contribute to this Report. Five of them managed to get their illuminating contributions transmitted in time for the publication

of this Report: Bob Deacon (University of Sheffield, UK, and Stakes, Helsinki, Finland), Adam Harnes (York University, Canada), Manuel Montes (East-West Center, Honolulu, Hawai'i, USA) Ronen Palan (York University, Canada, and University of Sussex, UK) and David Woodward (Catholic Institute for International Relations, UK). In addition, also Christian Chavagneux from Institut d'Etudes Politiques, Paris, France, and editor of the review *L'Economie Politique*, contributed with an expert statement.

Note that throughout the Report, I am using the – politically always so problematic – pronoun 'we'. Since the Advisory Board is not responsible for the main text – although they have commented it – this pronoun should be read to mean either me alone (the conventional distance-taking device in scholarly texts); me and Katarina, who has participated in formulating many of these ideas; or, occasionally, as an open invitation to include also you, the reader, to join the journey: it is up to you to decide whether you are willing to accept this invitation.

I could have never written this Report in such a short time without the invaluable help of Katarina. Many of the ideas and details of Chapter 4 and 5 are in fact developed together with her, and she has conspicuously and meticulously edited and revised the text throughout and many times.

The only Bank of Finland economist that offered readily her help is Katarina's mother, Monica Ahlstedt. We are most thankful to her.

We would also like to thank the Nottingham Trent University for covering the costs of our first journey to Paris, and ATTAC for paying for the second trip in January 1999.

Under the firm leadership of Tuomas Forsberg, and as one of the two host organisations of NIGD, the Finnish Institute for International Affairs has also been kind enough to provide a forum for publishing this first version of the Report as a Working Paper. All comments will be most welcome and helpful for developing this into a full-scale book.

In Nottingham, Monday 22 February 1999,

Heikki Patomäki

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1. Introduction

It seems that globalisation has produced the effects its critics have always feared. In addition to giving rise to growing disparities and alienation in the world, the global economic system has been, since 1997, at the edge of a crisis potentially as severe as that of the Great Depression of the 1930's. In many sites in South-East Asia, Russia and Latin America the picture has been already gloomy enough[1]. In fact, it seems that only the economic centres of Western Europe and, particularly, the United States have thus far remained intact, or have even prospered.

At the heart of this crisis is the volatility, instability and irresponsibility of a global, neo-liberalised financial system. James Tobin's 1970's proposal for a currency transactions tax – a low rate tax on financial transactions involving different currencies – is designed to alleviate these problems and, at the same time, create space for more autonomous economic policies of states.

Despite emphasis on the importance of national autonomy, Tobin's proposal was internationalist and intended to complement other simultaneous steps to be taken toward a better system of governance of global political economy.

This report begins with an analysis of Tobin's original argument and economists' (false) reasons for dismissing it. Secondly, we discuss the reasons for the emergence of wide support for the Tobin tax in the 1990's as well as the nature of that political support. What kinds of new concerns, arguments and points of view are there? The continuous stream of major financial crises is perhaps the most important reason to support the Tobin tax. However, for many actors, the potentially huge revenues stemming from the Tobin tax are seen as equally important in an increasingly globalised and unequal world, where less and less public funds are available for socially and politically useful purposes. For others, the Tobin tax is an element in a wider struggle to find alternatives for neoliberalism, which has not

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[1] In Sub-Saharan Africa, the picture appears even gloomier; there has been a long-term process of decline of economy and degradation of society. The recent turmoil in global financial markets, however, has not had any noteworthy impact on the African conditions, and thus Africa will not be discussed in this Report. Yet, it seems that the neoliberalist Structural Adjustment Programmes have contributed to the implosion of Sub-Saharan Africa. The story of the marginalisation of post-colonial, Sub-Saharan Africa is nicely told in Castells 1998, 70-128, but Gibbon 1996, for instance, is better in explicating the role of Structural Adjustment Programmes in these processes of ill development.

redeemed its promises, but has managed to contribute to unnecessary depression and unemployment, rising inequalities, social destruction and formalisation and ritualisation of democracy.

Thirdly, we tackle some of the major problems of a currency transactions tax. Tax evasion is potentially a serious problem, and also a wide variety of currency substitutes have to be covered. Also a systematic policy to deal with offshore tax havens have to be agreed upon. Yet, the fear of the technical failure of the Tobin tax seems to be greatly exaggerated. When the installation of the tax is seen in processual terms, and the idea of the tax is slightly modified, not all major financial centres have to been within the taxation system from the outset: the tax is still practicable.

Indeed, in a pivotal moment of this report, we propose a two-phases scheme of establishing the Tobin tax regime. In the first, a modified version of the Tobin tax is enacted by a grouping of countries (possibly including the EU). This grouping will establish an agreement open to all states and s supranational body to orchestrate the tax and collect the revenues. In the second phase, when most states and all financial centres are in, a higher, uniform and universal Tobin will be implemented.

At the moment. the United States is opposing the Tobin tax; and the International Monetary Fund and the World Bank are at best likely to remain undecided about it, at worst simply advocating further neoliberalisation. Due to the UK strategy to find competitiveness in the global political economy by means of deregulation and cheap infrastructure/labour, including the City of London, it is likely that also the UK will resist the idea (unless the UK decides to join the EMU). So, for the time being, at least two major financial centres – New York and London – should perhaps be counted out.

Hence, the possibility of implementing the tax on a more unilateral basis is very important. We discuss the potential for the emergence of political will for it from two alternative sources: the European Union and the countries that have been hit hard by recent economic crises, in concert with the "progressivists" (the Nordic countries, Canada, Australia, New Zealand).

Since the ultimate aim must be a uniform global tax, we consequently return to global issues. There are three major issues here. Since sovereign states have exclusive control over their

territory, it seems that they have reasons to oppose the tax. Yet, globalised financial markets seem to have become “sovereign”, too, and in fact, the Tobin tax intends to increase national autonomy (even if in reality this increase might be rather limited). The Tobin tax in fact defends the autonomy of sovereign states against these powerful structures and flows.

Nonetheless, although in practice states will collect the tax, we are also talking about a first global tax of any kind, which opens up a number of new issues concerning authority, democracy and redistribution. On a global level, the issue of tax collection and the allocation of its revenues need to be discussed. There lays also a problem in the division of labour between different organisations. In governing the tax, what should the role of these different organisations – such as the IMF, the World Bank, and the United Nations – be?

Our response to the governance issue is to argue for a UN-based system. However, we heavily emphasise the need to reform the UN prior to granting it this major responsibility. Indeed, the Tobin tax issue is necessarily connected to struggles over the way global governance is organised: either oligarchically (a few rich and powerful dictate the terms for others) or democratically (pluralistic and equal public discourse is combined with representative decision-making). Here, we see the proposal of the Council of Global Governance, CGG, to establish an economic security council of the UN as an interesting possibility. But a reconstructed Economic and Social Council (ECOSOC) of the UN might be even more democratic and functional.

In addition to the main text of this NIGD-project, there are also seven expert statements by the members of the international Advisory Board. These statements, which are not committed to the views expressed in the main text, cover areas from general justification of the Tobin tax to global social policy and a global investment fund. They support, complement and pluralise the main text. They support the text by deepening the analysis or by making the same points from a different angle. They also complement the next, because they cover areas not discussed in the main text. And last but not least, they pluralise the text by bringing in new points of view, sometimes partially contradicting the arguments made in the main text.

2. Tobin's original proposal in an intellectual and political context

In the wake of the partial collapse of the original Bretton Woods system (formally in August 1971), and in response to the volatility of financial markets, James Tobin proposed in 1972 a currency transaction tax[2]. Tobin's basic idea is simple: by implementing a low rate tax on financial transactions involving different currencies, many speculative movements would become unprofitable and the financial system more stable. This would also increase the autonomy of national economic policy makers and, as a by-product, yield revenues to the international community. Yet, the proposal hardly found any supportive, let alone enthusiastic, reception. Tobin himself vivaciously described, in 1996, the fate of his proposal:

> *In 1978, I was emboldened to devote my presidential address to the Eastern Economic Association entirely to it [currency transactions tax]. It did not make much of a ripple. In fact, one might say that it sank like a rock. The community of professional economists simply ignored it. The interest that occasionally arose came from journalists and financial pundits. It was usually triggered by currency crises and died out when the crisis passed from the headlines.*
>
> *The idea was anathema to central bankers. The most recent currency crises led reporters to ask Ottmar Issing, the economic brain of Bundesbank, about the Tobin tax. He replied with some asperity: "Oh, that again. It's the Loch Ness monster, popping up once more!" When I next encountered Issing, whom I like and respect, I said, "Well here I am, the Monster still."*[3]

Unlike the Loch Ness monster, however, James Tobin's proposal has already been publicly visible to anyone interested in it since a quarter of a century. What exactly did Tobin argue in his presidential address to the Eastern Economic Association? Why has the proposal for a currency transactions tax been an

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[2] His 1972 *The Eliot Janeway* lectures were published in Tobin 1974. In 1981, Tobin was awarded the Nobel Prize for "his most outstanding and significant research contribution to the theory of financial markets and their relation to consumption and investment decisions, production, employment and prices".
[3] Tobin 1996, x.

anathema to – and even seen as a Loch Ness monster by – central bankers and players in the global financial markets? And why have professional economists tended to ignore Tobin's proposal?

2.1. The argument

Given the context of the turmoil of the 1970's, it is natural that Tobin started his 7 pages long (or short!) paper by assessing different critical views on the original Bretton Woods system. That system was based on fixed exchange rates to US dollar, which in turn was exchangeable to gold in fixed terms (USD35 per ounce). In the 1950's and 1960's some, such as Robert Triffin, argued for establishing a **world central bank** on the (as such correct) grounds that it is impossible to continue to have all the official reserves of the world in one country's currency – which in turn, was connected to gold – without creating shortages, imbalances and inflationary pressures. There were others who more modestly sought **better and more symmetrical rules of the game** by allowing room for more flexibility for countries to set their own exchange rates. And finally, as a third view, a growing number of economists seemed to be following Milton Friedman in his advocacy of **floating exchange rates**, "determined in private markets without official interventions". For reasons to soon be discussed, those following Friedman's ideas, the monetarists, seemed to be gaining the upper hand in the debate. Echoing Keynes's famous dictum that "the ideas of economists and political philosophers, both when they are right and wrong, are more powerful than is commonly understood"[4], Tobin flattered his fellow economists of their surprising power of making their wishes come true, with some help of historical coincidences and political constellations:

> *By the early 1970's the third view was the dominant one in the economics profession, though not among central bankers and private financiers. And all of a sudden, thanks to Nixon and Connally, we got our wish.*[5]

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[4] Keynes 1961/1936, 383.
[5] Tobin 1978, 153.

Tobin agreed, not uncontroversially, with the monetarists that "floating rates are an improvement on the Bretton Woods system"[6]. But he also argued that the mainstream economics had misconceived the problem. For Tobin, the **essential problem** was – already in the 1970's! – the excessive intercurrency mobility of private financial capital. After the World War II, the world has enjoyed benefits arisen from of the increased world-wide economic integration, yet that integration in itself has been partial and unbalanced. Labour does not move much at all, and even goods move much more sluggishly than fluid funds. Quite independently of whether the world has fixed or floating exchange rates, the problem remains the same:

> *Under either exchange regime the currency exchanges transmit disturbances originating in international financial markets. National economies and national governments are not capable of adjusting to massive movements of funds across the foreign exchanges, without real hardship and without significant sacrifice of the objectives of national economic policy with respect to employment, output, and inflation. [...] speculation on exchange rates, whether its consequences are vast shifts of official assets and debts or large movements of exchange rates themselves, have serious and frequently painful real internal economic consequences.*[7]

Tobin sees alternatives to this situation. He discusses two possibilities: either **unification** of the world or developing more **autonomy** to national central banks and governments. In fact, also the latter is an internationalist and globalist strategy, as will be seen.

The unification of the world would be modelled on federations such as the United States of America, and partially also on the ideals of the European integration. A unified world would have a common currency, common monetary and fiscal policy, and further economic integration. With a common currency, single financial and capital markets, and a single monetary policy, there would be no room for interest arbitrage or

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[6] Ibid., 154. Because of the resulted high volatility and shortening of time-horizons, it has been later argued that fixed exchange rates would have been much better for trade, foreign direct investment and other real economic factors. See Michalos 1997, 12-13. Eichengreen, Tobin and Wyplosz 1996, 163, respond by saying that "the nostalgia for the pre-1971 Bretton Woods System reflects a 'grass is greener' mentality rather than thoughtful analysis".

[7] Tobin, op.cit., 154.

speculation on exchange rate fluctuation that would create "disturbances and painful interregional adjustments"[8].

In the late 1970's, Tobin was quite right in saying that "even for the Common Market countries, the goal [of unification] is still far, far distant"[9]. Twenty years later, however, the goal is not "far distant" anymore, and indeed the prevention of the intra-European speculative turmoil has become one of the objectives of the EMU and the European single currency, **euro**. Perhaps this should make us reassess Tobin's appraisal that world unification is not "a viable option in the foreseeable future, i.e. the twentieth century". After all, the 21st century is about to begin.[10]

Be that as it may, Tobin concluded that the only viable option is to create more room for the autonomy of national governments and central banks. Therefore, he proposed "to throw some sand in the wheels of our excessively efficient international money markets"[11]. Setting an **international uniform tax on all spot conversions of one currency into another**, proportional to the size of transactions, could do this. For instance, a tax of 1% could be equalised by an 8 point difference in the annual yields of Treasury bills or Eurocurrency deposits denominated in dollars or yens. Tobin further argued that this tax would make very short-term financial round-trip excursions particularly expensive. Thus, the currency transactions tax should slow down the volatility and reduce the magnitude of financial flows. Thereby, the autonomy of national governments and central banks would be increased. Also the risk of speculative eruptions with painful real economy consequences would diminish (although not evaporate).

Now, it is important to note that the Tobin tax is an internationalist – or globalist – strategy in at least two accounts. Most importantly, Tobin was very clear in saying that this is only the "second best way out"[12]. World unification would be better. Furthermore, he wanted to urge, simultaneously, the governments to "approach the task of policy coordination with a

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[8] Ibid., 155.
[9] Ibid., 155.
[10] Tobin's claim is now that "it is unrealistic to hope that the major industrial countries can make comparable strides towards political unification in our lifetimes"; in Eichengreen, Tobin & Wyplosz, op.cit., 171.
[11] Tobin op.cit., 154.
[12] Ibid., 155.

longer-range and more global view of their responsibilities"[13]. In fact, he also warned that it is the present system that can very easily create real tendencies for "damaging protectionist and autarkic measures designed to protect economies, at least their political favored sectors, from the consequences of international financial shocks"[14]. Tobin's proposal has therefore nothing to do with nationalism or autarkism; but he argued that inconsiderate and light-minded liberalism, advocating free, deregulated economic flows everywhere, can easily yield conditions for the re-emergence of both.

2.2. Strong opposition by central banks and economists

Given the market orientation and pro-free trade nature of Tobin's proposal, as well as his internationalist stand, why has the tax become an anathema to – even seen as a Loch Ness monster by – central bankers and players in the global financial markets? And why have professional economists tended to ignore and marginalise Tobin's proposal?

Firstly, despite the fact that even central bankers' opinions do change, there seems to be a structural-functionalist reason why there is an "attachment of central bankers to monetarist targets irrespective of exchange rate regimes and the openness of financial markets"[15]. The reason is that the role given to the central banks in the governance of modern, capitalist national economies has to do with, and only with, monetary issues. Given this aim, and the issues at hand in their attempt at everyday problem-solving, they are particularly susceptible to monetarist reasoning: only monetary policy by means of money stock controlling is effective, and even that under very tight constraints; it is the rational expectations and beliefs of the market actors that determine the value of money internally and externally; and the main problem of economic policy is to avoid escalation of inflationary pressures and expectations. To the extent that they accept the monetarist logic in its entirety, logically they must be committed also to the belief in the efficiency of the liberalism of financial flows and freely floating exchange rates.

[13] Ibid., 159.
[14] Ibid., 159.
[15] Ibid., 156.

Most central bankers are economists, and base their practical-political judgements on economic theory. So do most policymakers: since the 1970's, economics has assumed an ever more dominant position in the political life of the West. David Felix's description of the situation in 1978 – and the following years – remains mostly valid as a characterisation of the situation also in the late 1990's, although it is indeed becoming more and more true that "worries over destabilizing financial dynamics" has now overtaken "earlier euphoria over the efficiency gains from liberalisation":

> *In 1978 policy makers were caught up in competitive pressures to deregulate financial and commodity markets, and most mainstream economists, conflating financial with trade liberalization, were egging them on by pointing up alleged efficiency gains from doing both.*[16]

The belief in the superior efficiency of "free markets" explains both the blindness to the problems of financial capital volatility and resistance to reformist proposals such as that of Tobin's (or simply the dismissal of his arguments). In other words, it seems that the dominance of the mainstream economics has been and still is at the heart of the political problem of tackling the adverse consequences of the globalised financial markets. Naturally, the dominance of economics can be seen as a socio-political phenomenon that can be explained – and as such is also transient and changeable, at least in the longer run. But first we should have at least a rough understanding of what is wrong with orthodox economic theory.

Economic theory is based on an **irrealist philosophy**: it denies the existence of social beings and relations,[17] and instead asserts a set of mostly – and in many cases explicitly – untrue or very partial assumptions, which are justified by their instrumental value for enabling simple and parsimonious models that are able to predict certain allegedly important things[18]. These assumptions

[16] Felix 1995a, 4.

[17] For a thorough exposition and critical analysis of the consequences of these moves, see Bhaskar 1986, 224-308, who concludes by arguing that this kind of science "at once naturalises and normalises things and reflects in an endless hall of mirrors the self-image of Bourgeois Man".

[18] This is the standard interpretation of Friedman's, 1969/1953, 515-520, position, widely shared by many economists. Hodgson 1988, 48-50 has shown, however, that Friedman is quick to change his position in the one and the same text: what begins as an instrumentalist assumption, is soon represented as a certain theory about the world. More generally, by

are typically tailored for the building of mathematical and statistical models and using certain areas of mathematics for analysing the properties of these models. This gives economics an exact and scientific appearance. But it is only an appearance. Economics can explain very little[19] and predict hardly anything at all[20]. In fact, it typically misunderstands even the role and nature of mathematical functions. Mathematical functions such as $y = f(x)$ say nothing about what makes y or x, or only that quantitative variations in y is formally, not substantially, related in some way to quantitative variation in x. Moreover, the sign '= ' says nothing about causality. Qualitative analysis of these objects is required to disclose real social and causal relations.[21]

Instead, economists have concentrated on refining the ever more complex mathematical tools at their disposal. Why? Superficially, because they think that this is what science is all about. More fundamentally, because they think that better formal tools help to achieve what economics strives for: ability to predict and control certain things such as amount of production, prices and inflation and employment and income of different "factors or production". But the apparently sophisticated tools do not help:

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changing the status of their fundamental assumptions in this manner, depending on the context and audience, economists are easily able to avoid all criticism (for the true believers and unthoughtful followers, the assumptions form a theory beyond doubt; for other, more suspicious and thoughtful interrogators, they can be represented simply as useful – and hypothetical – assumptions).

[19] What can it explain, then? Well, for instance, the demand/supply-theory of prices seems to be in some respects better explanation of price-formation than the ancient, clumsy labour theory of value, although even the demand/supply-theory falls short of being a real explanation (what are the elements in social, causally efficacious complexes that bring about and constitute "demand" and "supply", and what are the social rules and resources that constitute the conditions for exchange, supply and demand?). Similarily, game theory – which can be counted as a strand of economics – can be also helpful in explaining the typical herd behaviour in financial markets: under the conditions of radical uncertainty and fear of sudden losses, every single actor faces a prisoner's dilemma (PD) kind of a situation: for everybody, it is rational to take their money away from X, but thereby the value of X collapses, and everybody is much worse off than they would have been had they kept their money in X. One crucial difference to the real world story is of course the fact that usually the players in the PD-game of the world financial markets are bailed-out, while it is the outsiders who bear the main burden of the consequences of these losses.

[20] In his systematic and critical study of the background assumptions of economics, Lawson 1997, 14, states bluntly that economics "fares poorly in its own terms; it neither provides particularly accurate forecasts of events nor illustrates the world in which we live. But of equal significance, the whole project is riddled with confusion and incoherence. [...] the failure of the contemporary project to explain, predict or otherwise illuminate is met only with a restricted set of responses: with continuous revisions to certain parts of theories, the collection of ever more data, the development of increasingly sophisticated forms of computer software, and so forth."

[21] See Sayer 1992, 178-180.

economists cannot predict. Outside the public sphere, they are often aware of this themselves, and it is a source of a number of private jokes and anecdotes among qualified economists.[22]

Yet, they are misled by the irrealist philosophy about the sources of this incapability. Instead of tackling the consequences of dealing with open systems and relational, contextual social entities, they continue to sophisticate their formal tools in the vain hope of finally arriving at truly predictive models. The fact that they are able to fit a mathematical/ statistical model to a set of *ex post* empirical data – quantified traces of **past** events and processes – brings some comfort, even if they know that many others can do the same, but with different models. It is much harder to predict the future than the past, and it should be alarming that even the past can be "predicted" in so many ways with economists' tools.

There is one thing that economists can do, however. They can draw ideological and political conclusions on the basis of their models. These ideological conclusions follow logically from their assumptions about the nature of the world. Since mathematical analysis adds nothing to the substantial assumptions of the world, the principle must be: "garbage in,

On the Tobin tax as a bad idea and why it should be supported

Christian Chavagneux

To believe that the Tobin tax may be a helpful instrument to control the erratic behaviour of market forces in the international monetary and financial system is a false economic conception. Nonetheless, it is an idea, which should be supported on an international basis for its political importance. Everyone knows now on what principles the Tobin tax should work, putting "sand in the wheels" of short term speculation while being neutral on long term financial flows serving international investments. Different proposals have suggested various means of applying the tax and proposed a lot of good ideas on the ways its proceeds could be used in the interest of a more efficient and a more equitable world economy. Yet, the introduction of a Tobin tax would face four hurdles, which appear to be impassable.

The first one is well known: such a tax should be put into effect in all the main financial places otherwise those which do not apply it would play as exploiters of the system. But at the moment, no one can see any will coming from New York, London, Frankfurt, Tokyo or Singapore in favour of such a tax.

Secondly, a Tobin tax is no guarantee at all against speculative movements. If a country engaged in a policy mix of monetary and budgetary policies is considered by the financial markets as following the wrong paths, it would entail a speculation based on the bet that the gains of the speculation will be greater than the payment of the tax making speculation still a profitable decision.

[22] For details and systematic analysis of the rhetoric of economics, see McCloskey 1986.

Thirdly, and most importantly, the current complexity of the international monetary and financial system risks rendering the Tobin tax completely inefficient. Until recently, the frontiers separating the different financial institutions were quite clear: banks were making loans, insurance companies proposed insurance policies, etc. Now banks are selling insurance policies and insurance companies buy loans on secondary markets through the process of titration. Institutional frontiers between financial entities tend to disappear.

Until recently, each financial product had its own use: securities were more risky but could bring more money, bonds corresponded to long term financing, etc. Today, bonds are convertible into securities or are bought and sold very quickly. Rapid financial innovations have contributed to the disappearance of functional frontiers between financial products. Finally, until recently, the distinction between financial and non-financial firms was quite obvious. Now, this distinction also tends to disappear with a lot of multinational companies - like General Electric, AT&T or General Motors - building more and more of their results on their financial activities rather than on profits made from selling the goods they produce.

All this complexity and opacity in the financial system makes it very difficult to know where and how international financial flows are moving. Imposing a tax in the foreign exchange markets could then result in a development of other means to make international money circulate. The more powerful financial actors will always find a way not to pay a tax.

There is a final problem, which makes the Tobin tax a bad idea. Even if we imagine that the main state powers of the world economy could be convinced to establish such a tax, nobody could affirm that they would hold this position for long while faced with the conflicting authority of powerful financial actors.

Nonetheless, in spite of all these impediments and obstructions, the Tobin tax is one among different projects, which deserve support – although in my point of view, a more important one would be to fight for the disappearance of tax havens. I see two reasons for this; the first one is to hope to mobilise the largest possible constituency in favour of political authorities against the power of “market forces”. Bringing, in short, democracy against the markets. The second reason is that the tax contributes to fight the liberal idea that the market is the one best mode of social organisation, and that the efficiency of a market economy should open the way for a “market society”.

Now, nobody should believe that the regulation of the financial system would solve all the world’s problems. Most of Africa will still be poor or the world’s environmental problems will not disappear. To give more power to the State against the markets is not enough. Governments should also be persuaded to regulate the world economy in a way that would benefit all the citizens of the world.

garbage out”. Typically, and in most cases only with minor modifications, the models of economics support the thesis of optimal efficiency of free market capitalism[23], quite independently of the specific context under discussion.

Obviously, the suspicion is that this ideology is, indeed, the reason for the hegemony of economics. Typically, and at least

[23] There are some economists and rational choice theorists who have relaxed the property-, ownership- and control assumptions implicit in neoclassical economics, thereby going beyond just studying capitalist market economies (see Elster & Moene 1989; cf. also Bowles & Gintis 1998). But these exceptions have been and are rare.

individually and in the short run, the free markets ideology runs in accordance with the interests of those entitled to make investment decisions in capitalist market economy or have a lot of resources at their disposal.[24]

It should come as no surprise that economics is much better resourced than any other social science, particularly in the US (from where the post-World War II orthodox economics has been exported to most other countries of the world, with the help of the strong, visible hand of the US state and foundations). There is lot of money available for research and university positions, and economists also hold important posts in central banks, ministries, governments and international organisations. With the expansion of the global financial markets, most investment banks started to hire economists only, with huge salaries, despite the fact that economic theory "serves almost no practical function in an investment bank"[25]. On the average, the salaries of economists are much higher than the salaries of historians, cultural theorists, sociologists or political scientists. Economics is thus relatively popular among students, even though its implausible and unappealing assumptions and scholastic technicalities deter many from assuming this profession.

Once developed as a social institution, economics has emerged as a powerful institution on its own. When economists jealously defend their science against outside criticism – which for most economists is by definition misconceived and illegitimate – they have their own cultural capital and positions at stake.

For his realist tenets and unorthodox positions[26], J.M. Keynes was an exception among economists.[27] It is often said that

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[24] Of course further distinctions should be made. Thus, Robert Cox, 1987, 358 et.passim., distinguishes between the interests and ideas of (1) those who control the big corporations and banks operating on a world scale; (2) those who control big nation-based enterprises and industrial groups; and (3) locally based petty capitalists. Monetarism and globalising neo-liberalism are conceptions that are most closely associated with (1), although they can be made consonant with (3), too (e.g. through privatised pension systems, which might be alluring also to better-off public sector employees etc.).

[25] Ormerod 1994, 6.

[26] Typically, Keynes (1961/1936) argued that the basis of economic theory must **be the way things really are**, in the practices of real world actors, not how they logically and ideally should be (in the opinion and assumptions of economists). For instance, a typical and crucial premise in his argument goes like this: "Whether logical or illogical, experience shows that this is in fact how labour behaves" (ibid.,9). This is a great methodological step forward. Yet, taking seriously the idea that the supposed economic "laws" in fact depend upon unique, transitory institutional arrangements, Keynes's own "general theory" – even if

Keynesian economics formed the mainstream for twenty years following World War II. In hindsight, it seems that these twenty years constituted a deviation that faded away quickly. It is not only that historical circumstances changed, but as a movement quite internal to economics itself, Keynesianism was rapidly conflated with models of neoclassical economics and other orthodox assumptions already in the 1950's and 1960's. This development occurred already before the Keynesian doctrine was eventually challenged by rearticulations of the orthodoxy, neo-classical monetarism and the related rational expectations theory.

We are now approaching an answer to the question of why mainstream economists have tended to ignore and marginalise Tobin' proposal for a global tax. James Tobin built his studies on the work of Keynes "and has probably done more to develop Keynesian ideas than any other economist"[28]. In fact, in his proposal, Tobin seems to have followed on Keynes's suggestion for a domestic financial transactions tax[29]. More importantly, it is telling that in one single paragraph of the paper where he proposed a currency transactions tax, Tobin refutes a number of fundamental assumptions of orthodox, "modern" economics:

> *"Whether the market is "efficient" in any deeper economic informational sense is very dubious. In these markets, as in other markets for financial instruments, speculators on future prices is the dominating preoccupation of the participants. In the ideal world of rational expectations, the anthropomorphic personified "market" would base its expectations on informed estimates of equilibrium exchange*

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unorthodox – cannot be seen as anything more than a partially successful attempt to grasp the Western European and Northern American socio-economic and political conditions of the interwar and immediate post-war period.

[27] Just listen to the way Keynes strongly warns against applying irrealist, orthodox economic theory to empirical evidence and practice: "… the characteristics of the special case assumed by the classical theory happen not to be those of the economic society in which we actually live, with the result that its teaching is misleading and disastrous if we attempt to apply it to the facts of experience." Keynes, op.cit., 3. Yet, Unger (1987, 128) is quite right in arguing that Keynes's own "solution was keyed to an intention, a situation, and a narrow set of conjectures".

[28] Pearce 1986, 421.

[29] Keynes was only talking about the internal developments of the US, but in the globalising world, Tobin internationalised his point. "When the capital development of a country becomes a by-product of the activities of a casino, the job is likely to be ill-done. […] It is usually agreed that casinos should, in the public interest, be inaccessible and expensive. And perhaps the same is true for Stock Exchanges. […] The introduction of a substantial Government transfer tax on all transactions might prove the most serviceable reform available, with a view to mitigating the predominance of speculation over enterprise in the United States." Keynes, op.cit., 159-160.

> *rates. Speculation would be the engine that moves actual rates to the equilibrium set. In fact no one has any good basis for estimating the equilibrium dollar-mark parity for 1980 or 1985, to which current rates might be related. That parity depends on a host of incalculables – not just the future paths of the two economies and of the rest of the world, but of the future portfolio preferences of the world's brokers located in London, even when sterling was not involved."*[30]

To sustain the purity of the basic assumptions – and the consequent ideological implications – is the name of the scholastic game of economics[31], and it seems that Tobin has gone against this basic tenet. More precisely, what does he say in this passage? Markets are not necessarily efficient; there are no "rational expectations", only uncertain and ambiguous estimations; future parities and prices are unpredictable; and one could even infer from this passage that the central notion of economics, namely that there is a "unique equilibrium", which is assumed to be Pareto optimal, is nothing but a theoreticians fiction[32]. It is the incalculable real world processes that determine the real prices and parities. No wonder Tobin's proposal for a currency transactions tax has been dismissed by most mainstream economists.

But, we should ask also from a historical perspective, were the mainstream economists right in their anticipation that freely convertible and floating financial markets will lead to global efficiency gains, enhanced stability and greater freedom of action for the states? In the 1970's and early 1980's, it was always possible to claim that any trouble is due to the remnants of the old system or belong quite naturally to the transition phase. Next,

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[30] Tobin 1978, 158-159.

[31] Of course, *internal* criticism is considered to be legitimate, but in most cases the consequent differences are just nuances within the same basic framework. This closed nature of the discourse of economics can be read as an indication of its non-scientific character (after all, as also Karl Popper would have said, both science and open society are constituted by free, critical dialogue and debate).

[32] Tobin would most likely accept the notion that there are multiple equilibria, giving rise to self-fulfilling bubbles and attacks on currencies; and that in an uncertain world a competitive equilibrium is in general **not** a Pareto optimum. However, Tobin might not accept the more radical conclusion of some neo- and post-Keynesian economists (Robinson, Kaldor, Pasinetti, *Journal of Post Keynesian Economics*), that in reality there is no such thing as "equilibrium" (we think that this would be a better starting point for economic theorising). In either case, the assumption that the standard is the existence of a "unique Pareto optimal equilibrium" is false. As a policy guide, this false idea leads to the norm that that everything must be judged in terms of whether it "distorts free markets"; this norm is no more grounded than horoscopes.

let us have a look at some of the events and processes since the mid-1980's.

3. Growing support for Tobin's proposal in the 1990's

Tobin himself claimed that the interest in the currency transactions tax has been "usually triggered by currency crises and died out when the crisis passed from the headlines". Indeed, one reason for the growing support for a global currency transactions tax since the latter half of the 1980's seems to have been the endless stream of financial crises. They seem to have confirmed the relative explanatory and analytical power of Tobin's analysis, particularly in comparison to that of monetarists. For good reasons, following each financial crisis, Tobin's tax has been taken up as a serious alternative. But there have been also other reasons for its growing popularity: attempts at further consolidation and locking-in of the principles of neo-liberalism – such as the establishment of the WTO, amendments of the rules and principles of the IMF, or the negotiations for the Multilateral Agreement on Investments, MAI – have provoked reactions all over the world, and a search for alternatives.

It is also important to understand that since the 1970's, the financial markets have expanded manifold. If Tobin considered the excessive intercurrency mobility of private financial capital to be the essential problem already in 1972-1978, the situation has certainly become much more serious in the 1990's. There has been an exponentially growing number of deregulatory measures and financial innovations, and the consequent exponential growth of the volume of transactions is beyond any fancy dream. By the mid-1980's, the daily turnover on foreign exchange markets world wide had reached USD150 billion, by 1992 about USD1 trillion, and by 1997-98 perhaps nearly USD1.5 trillion[33]. It is not only that these flows – based on a huge accumulation of **private debt** stock[34] and financial assets only valuable in relation to other

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[33] These BIS-based figures are quoted in almost any publication on the topic, but it is hard to verify that they are accurate (if they are, then all transactions are counted, and if they can be counted, they can also be taxed; but more of this later).

[34] "Overall systemic debt burdens within the western economy are no lower today than they were in the Keynesian era of budget-deficiting. The only significant difference is that debt-financed growth within the western economy has become increasingly privatised." Watson 1998, 2. Ultimately, the states, with the IMF, manage this privatised debt-system by bailing out those who fail to pay their debts. Even the World Bank has now acknowledged the crucial nature of huge private debt accumulation. As their chief economist Joseph Stiglitz puts it: "While South Korea, Thailand and Indonesia were heavily criticized for acquiring mountains of debt, the magnitude of debt at LTC M (Long-Term Capital Management) was

financial assets – bear only a weak relationship with the real economy of production and exchange of goods and employment of people. The problem is also that there is no central bank in the world that would be able to control flows of this magnitude.

3.1. The endless stream of financial crises with painful real economy consequences

Already the October 1987 Crash motivated some economists to propose measures to reverse the excessive absorption of human and physical resources in financial speculation. However, the menacing situation was normalised in a few months, and the momentum for these proposals was lost.

When small countries, such as Finland, Norway and Sweden, faced severe monetary difficulties and forced devaluation in the early 1990's, nobody recalled Tobin's proposal. But in September 1992 the speculative runs virtually demolished the EU's Exchange Rate Mechanism. This not only encouraged many Europeans to support the Economic and Monetary Union, EMU – for the single currency will at least stop intra-European speculative movements – but more globalistically made even the free-marketeering *Economist* to observe that "lately, one imagines, a good many government economists have been dusting down their copies of that [Tobin's 1978] article". The determination to establish the EMU even got strengthened after the crisis, but the Tobin tax idea soon faded again.[35]

The 1992 turmoil was quickly followed by the Mexican peso crisis, which started in December 1994. The devaluation announcement evoked panic among Western financial actors, who had invested USD50 billion in Mexican State debentures, shares and IOUs. Instead of the intended 15%, the USD value of Mexican peso fell by 30% in a few days. After 12 January 1995 the Mexican disease began to spread: many other currencies started to loose value rapidly vis à vis the US dollar, German mark and Japanese yen. Operation 'Peso Shield', organised by the White House and the headquarters of the IMF – both located in

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unbelievable". LTCM was a hedge fund that avoided collapse in September 1998 with a 3.5 billion-dollar bailout by 14 firms. "World Bank chief economist cites Asia, LTCM fund problems", *AFP News*, Geneva, 19 Oct 1998.

[35] Cf. Felix op.cit., 4.

Washington, D.C., practically next door to each other – eventually, and in the last minute, saved Mexico from bankruptcy. For many, this amounted to a 'bail-out for speculators', many of whom would otherwise have lost their fortunes.[36] Ordinary Mexicans were left alone to deal with the painful real economic consequences of these panic flows: unemployment, declining real wages and even less public social security. Obviously, it was again time to "dust down" Tobin's article from 1978 – if there was, indeed, any dust on it anymore. For instance, in a paper published in June 1996, Paul Bernd Spahn noted that "recent turbulence in world financial markets has rekindled interest in the so called Tobin tax"[37].

Tobin's article certainly did not get very dusty before the next major crisis, which started in Asia in 1997. In the second half of the year, following Thailand's lead, one Asian economy after another succumbed: currencies dropped, imports slowed, and economic growth sputtered. The Indonesian *rupiah*, for instance, lost 70% of its value relative to the US dollar. Towards the summer of 1998, speculative movements emptied the reserve funds of many countries. As George Soros, the world-known financial speculator, said in his testimony to the US Congress:

> *Some Asian stock markets have suffered worse declines than the Wall Street crash of 1929 and in addition their currencies have also fallen to a fraction of what their value was when they were tied to the US dollar. In Indonesia, for instance, most of the gains in living standards that accumulated during 30 years of Suharto's regime have disappeared.*[38]

In September 1998 it was reported that half of Indonesia is short of food.[39] Furthermore, it started to seem that a generation of Asian families has begun to slip backward into disease, hunger, malnutrition, illiteracy and poverty as a result of the Asian economic crisis that began in the summer of 1997. Millions of workers have already lost their jobs and are slipping back from the middle or working class into poverty in Indonesia, Thailand, South Korea, the Philippines and Malaysia.[40] To save the world as

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[36] This story is told thrillingly by Martin & Schumann 1997, 56-61.
[37] Spahn 1996.
[38] Soros 1998a.
[39] "Half of Indonesia short of food", *Straits Times*, 22 Sep 1998.
[40] "Asians in unhealthy crisis. Financial woes produce ill effects on depressed region's poverty-stricken", *Washington Times*, Sep 25 1998. Note, however, that many of these

a whole from the worst-case scenario, new rescue operations were orchestrated in 1998. IMF was central, for example, to organising a

The Tobin Tax and the East Asian Economic Crisis

Manuel F. Montes

James Tobin's 1971 proposal for a tax on foreign exchange transactions has intrigued for 3 reasons:

(1) by reducing the volume of transactions, the tax might make purely speculative transactions more expensive thereby reducing the volatility of exchange rates,
(2) in a world of characterized by large daily volumes in capital transactions, it might help to safeguard some measure of national independence of monetary policy, and
(3) it could raise enormous public resources for possible application to global concerns.

The proposal remains controversial because of the first and third aspects. In regard to the first aspect, it is not clear, technically and empirically, if reducing the volume of market transactions can hinder or accelerate the convergence of exchange rates to more enduring levels.

In regard to the third aspect, the potential for the raising of large international public funds that can be applied independently of national sovereigns has sparked the almost permanent animosity of the large powers, especially the United States. These objections assume that the tax can be effectively levied; how the tax can be levied in world with feeble political will and myriad ways to evade, including through the use of financial derivatives, is another matter.

In thinking about the role an effective Tobin tax might have played in the East Asian crisis (that began with the devaluation of the Thai baht in 2 July 1997), it is useful to highlight the characteristics of international capital markets which the crisis has exposed.

The most afflicted Asian economies had high savings rates, were vigorous exporters and had robust domestic public finances. External portfolio inflows were unnecessary in financing trade deficits, maintaining growth or securing development, even as these inflows generated enormous domestic wealth for residents that had assets and equity to sell to foreigners. The domestic banking systems of these economies were weakened precisely because their own high savings were being invested domestically into successively poor projects. Into this frenzy, foreign funds jostled in, mostly in short-term mode, enthralled by the potential spectacular speculative returns.

The irony here is that these countries that did not need these funds were precisely being pressured to absorb them, while other countries that might have needed these resources generated little interest from foreign funds. For the recipients, the volume of these external inflows forced monetary authorities to carry

countries had created "free economic zones" and other arrangements on which they based they comparative advantage. Within these zones and social contexts, workers typically lived beyond subsistence level also before the economic crisis – with 12 hours working days and no rights for collective organisation, social security, health, or even control over their own bodies.

out policy contortions (including the sterilization of capital inflows) to prevent the currency from appreciating in order to protect their export industries and to avoid domestic inflation. (Montes and Popov 1999, pp. 2–4.)

What appears in hindsight to after-the-fact experts as a strong peg of currencies to the U.S. dollar actually constitutes a heroic effort at the start of the period on the part of East Asian authorities to prevent currency appreciation and in the period immediately before the crisis as a desperate attempt to prevent depreciation which would have devastated the domestic banking system which by then had borrowed heavily in foreign currencies. (Montes 1998, pp. 20–25.)

The objectors and supporters of the Tobin tax agree on one thing: it will reduce the volume of transactions. The impact of a Tobin tax in terms of reducing the volume of capital flows needs to be estimated and such an evaluation would depend at what rate transactions would be taxed and the extent of international cooperation and enforcement. During the period of capital inflows, a reduction in the volume of such transactions would have been helpful to Asian public authorities. It would have helped to safeguard their scope for monetary policy and reduced the policy contortions they undertook.

A characteristic of “emerging markets” of which those in East Asia are quintessential is that their domestic capital markets are narrow and shallow; if capital markets were already deep and well-developed they would not be progressively “emerging.” This means that for emerging markets portfolio capital flows would either in the mode of inflow (in the period after they are “discovered” by international investors); in the mode of “no (net) flow” after investors have adjusted their portfolios to include investments in these economies; or of “outflow” if, as had happened in Asia; somehow panic and international investment rules demand an immediate reduction in exposure to these markets.

One implication is that even granting for the sake of argument that a reduction in the volume of capital transactions might hinder convergence to equilibrium, national (as opposed to private) potential losses from the tax would not be important during the period of the inflow and there might actually be gains during the period of outflow.

For economies, such as those in East Asia, which must live with the curse of attractiveness to foreign portfolio investors, it would be well to consider implementing among themselves, in a concerted manner, a Tobin tax-like regime**, without waiting for the major powers to cooperate**. They should implement jointly a common tax on foreign exchange transactions; this way they would not be beggaring each other in competing for foreign portfolio funds. In implementing such a tax, they would not be losing competitiveness in regard to capital inflows vis-à-vis other developing countries who elicit minimal interest from portfolio investors anyway. These economies, to the extent that they have placed high priority on developing their real sectors as opposed to their financial services sector, also need not feel compelled to compete with offshore tax havens for foreign funds.

They could either use the tax revenues collected for national purposes or they could place part of it in an international fund to raise their international diplomatic profile. Without the cooperation of the major powers, the question of effectiveness of the levy needs to be faced.

Some national capital controls need to maintained (or restored) to provide the capacity to observe the tax base. As in the case of Chile, for each individual country a Tobin-like tax would have to part of an overall policy stance in managing capital inflows, except that this specific feature would be implemented in concert with other similarly affected countries.

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USD58.35 billion rescue package to South Korea. The speculators were in most cases bailed out, but the area fell into a deep recession. "Some wags began calling the emerging markets 'submerging' markets". "Suddenly, the Asian economic miracle was not so miraculous".[41]

Instead of fading away, this crisis seems to have been ensnaring more and more regions. After Southeast Asia, it was Russia's turn to be hit. Many trends in – and globally, through – Russia had been pointing towards a forthcoming catastrophe. In August 1998, Russia underwent a total financial meltdown and then defaulted on its foreign debt.

In Russia's case, there was no miracle economy to collapse. Rather, the economy had already for years been characterised by declining industrial production and ecological degradation, which led to a catastrophic sinking in human development and life-expectancy for the bulk of the population. The Western "shock therapy" and half-implemented austerity programmes imposed by the IMF, based on the orthodox assumption that a strong currency must be established at any price, contributed to the industrial decline and radical welfare cut-downs.
Moreover, the substitution of Russian consumer goods by Western goods now eagerly sold everywhere and advertised in the totally commercialised mass media, led to a further decline of Russian industry. The outrageous privatisation programme deepened corruption and led to the concentration of the remaining productive capital and assets in a few hands.

It is not difficult to see how the increasingly nervous – after the collapse of the Asian "miracle economies" – global investment banks and the financial sections of multinational corporations came to re-assess Russian prospects/spectres in Summer 1998. The just-in-case initiatives by some were followed by the normal panicking herd behaviour, and the outcome was once again dramatic. Even though the IMF had just begun payments to Russia from one of the largest economic rescue packages in history, the transnational investors – including the

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[41] See Lynch 1998, 103-109.

Russian ones – started to draw their funds away from Russia, 10 August 1998:

> *The rouble collapsed on a Monday morning. The weather in Moscow was unusually good, not too hot and not too cold. Thousands of residents could walk about the city observing the fall of the national currency. Best of all was to stroll about the currency exchange booths. First the rate fell from 6.2 roubles to the dollar to 6.5. By midday the American dollar cost 7.5 roubles; by 1.30pm the price had reached 8.5. After 2pm, it was 9 or 9.5 roubles. By 3pm the banks had run out of money. The currency exchange booths closed one after another 'for technical reasons'.*[42]

In January 1999, the value of Russian rouble was only about ¼ of what it was in July 1998. In 1997, it almost seemed that the deep downfall of GDP (almost 40% between 1992-96), industrial production (almost 60% between 1992-96) and living standards had finally stopped. After the financial meltdown, it started again. GDP fell at least 3% in 1998, and the IMF estimates that it will fall by another 8% in 1999. Industrial production is declining even more rapidly, and the real wages have been diminished by a third in one year only (from November 1997 to November 1998).[43] Starvation has become a real outlook for many Russians in the immediate future; and the collapse of state may be due because what is left of the economy has moved to the black markets or shadow economy.

Although Latin American mutual funds had already lost USD851 million, or 63 percent, of their asset value by September 1998; and although there was a turmoil on the Sao Paulo stock exchange, and some USD1.7 billion quietly leaving the country in one single day in September; many "analysts" still thought in September that Latin America will not fall with Asia and Russia. Nonetheless, Brazil, and perhaps Latin America more generally, was indeed next in line. The Russian debt default – its inability to pay – caused investors to panic and flee many other "emerging markets". By November 1998, Brazilian *real*'s peg to the US dollar was wobbling. Brazil borrowed USD41.5 billion from the IMF to defend the *real* and promises to rein in its budget deficit. But even

[42] Kagarlitsky 1998.
[43] These figures have been taken from (or calculated on the basis of the figures given in) Bank of Finland, "Russian Economy. The Month in Review 12•1998".

with this kind of rescue package, foreign exchange speculators could still smell blood.

After all, global currency transactions were still much more than a USD1 trillion per day in late 1998, after the major crises in Asia and Russia. USD41.5 billion is only less than 4% of this **daily** volume, and no more what in practice could easily leave Brazil in a month. What can that small change do if major investors decide to leave the country, perhaps because the global volume available for short-term investments and speculations is quickly decreasing? Indeed, billions of dollars started again to flee the country, and Brazil was forced to devalue the *real* – not only once, but twice.[44] Eventually, it had to let its currency float, thus renouncing its tie to the US dollar. But the trouble was far from being over.

Unemployment started to rise rapidly and production declined. To meet the IMF requirements, Brazil had to device an "unprecedented" package of budget cuts, social benefits reform and tax increases. The US/IMF advice also mandated astronomously high interest rates. It is widely believed that the combination of the financial meltdown and these recipes will send Brazil deep down into a long recession. Now, Brazil has also the most unequal distribution of income in the world, with the upper 10 percent receiving about half the nation's income, while 43 percent of the people survive on less than USD2 a day. In an unequal society already full of hatred and violence, one can only imagine what the consequences of the bulk of the population dropping under the barest subsistence level will mean for Brazilian social and political fabric.

From the point of view of global financial markets and security of the West, the fear of many economic actors is that Brazil will go the Russian route – i.e. would also have to devalue and default, and thus cause further panic in the financial markets. And since Brazil – as opposed to Russia – is a much bigger factor in the world economy, that would be a serious addition. If Brazil were to default on its debt the rest of Latin America would probably be hit as well. Brazil accounts for one-half of the economy of all South America, so that would then trigger an eruption of a whole new region of the global financial crisis,

[44] See, for instance, "Rio pays for hick's vendetta", *The Guardian*, 16 January 1999.

which would probably bounce back to Asia and elsewhere and probably trigger more currency chaos there.

In February 1999, it is not possible to say whether the partial collapse of Brazil was the last dramatic episode in this economic crisis, or whether it will deepen further and, eventually, turn out to constitute only an event in a long process of the world-wide Great Depression of the turn of the 21st century. On 1 February 1999, the Brazilian currency had depreciated by more than 40% since 12 January, and the *real* continued to slide against the dollar. Also the "first signs of panic among ordinary Brazilians over the currency crisis" appeared namely "heavy withdrawals from bank branches".[45]

Although the future is very uncertain, at least we know that in many parts of Asia, Russia and Latin America, the suffering will continue for a long time; that the global conditions also for many Western firms are meagre; and that political forces favouring radically nationalist, xenophopic and anti-Western solutions may be on the rise[46]. And, perhaps most importantly, the problem of highly volatile, hugely indebted global financial system remains intact.

3.2. The 1990's revival of the Tobin tax

In 1999 the Tobin tax is a political issue like never before. For most, it seems that the first and foremost concern is the stability of financial markets and the prospect of empowerment of more efficient and socially responsible economic policies. In this regard, it is not difficult to see why the Tobin tax in 1999 is more popular an idea than ever. The monetarist economic theory and those advocating financial markets liberalisation had promised more efficiency and stability, as well as more autonomy for the economic policy of states. This did not quite seem to happen. Already before the latest turmoil, many concluded by mid-1990's that foreign exchange markets do always function optimally. "They are marked by excessive, destabilizing volatility".[47] This conclusion is nicely summarised and reinforced by Soros, now strongly backed by the latest round of crises:

[45] "Brazil to Press IMF For Release of Funds", *Financial Times*, 1 February 1999.
[46] About the political reactions against the current governance of global economy, see Patomäki 1999.
[47] Kaul, Grunberg & ul Haq 1996, 3.

> *"The financial crisis that originated in Thailand in 1997 is particularly unnerving because of its scope and severity. We at Soros Fund Management could see a crisis coming and so could others, but the extent of the dislocation took everyone by surprise. A number of latent and seemingly unrelated imbalances were activated and their interaction touched off a process whose results are entirely out of proportion with the ingredients that went into creating it.* ***[...]It is difficult to escape the conclusion that the international financial system itself constituted the main ingredient in the meltdown process****."*[48]

Indeed, there is a need to throw some sand in the wheels of the financial markets. In an editorial letter to the *Washington Post*, Tobin went even further than Soros in claiming that this crisis was produced by the financial system:

> *South Korea and other Asian countries – like Mexico in 1994-95 – are being punished for offenses they did not commit. They have inflation and government budgets under control. They are not sinners, but victims of a flawed international exchange rate system that, under U.S. leadership, gives the mobility of capital priority over all other considerations. It is simply too easy for banks, governments, businesses and speculators to buy and sell huge blocks of a country's currency in panicky moments. Such flows of capital can throw a country literally overnight into a crisis.*[49]

The lesson is, quite clearly, that "the leaders of the global economy need to find ways to make the currency exchange system less volatile, so as to protect innocent bystanders from sudden economic crashes that destroy jobs and income". But there are also other considerations that add to the desirability of the Tobin tax. It is discussed more and more often as an essential element in any more democratic and socially responsible systems of global governance. Hence, it is raised up and proposed as a solution to many problems of world politics and economy. For instance, the Tobin tax is discussed in the well-known and disputed book *When Corporations Rule the World* (1995) by David C. Korten[50]; in the European best-seller *Globalisation Trap* (1996/97), by Hans-Peter Martin and Harald Schumann[51]; and in

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[48] Soros 1998b, in *The London Times*, 30 November 1998. Emphasis by HP.
[49] Tobin 1997, in *The Washington Post*, 21 December 1997.
[50] Korten 1997/1995, 413-416 (translation into Finnish 1997).
[51] Martin & Schumann 1997, 102-106, 290. Original text in German was published in 1996, most translations in European languages in 1997 (in English in 1998).

the widely publicised political book *The Third Way. The Renewal of Social Democracy* (1998) by Anthony Giddens[52], one of the best-known contemporary social theorists and adviser to Tony Blair's government.

Why is the Tobin tax seen as important by these authors and many others? For one thing, Tobin's idea seems to have gained support also because of its huge revenue potential. With the explosion of the magnitude of currency transactions, the potential revenue has become very much larger, too. Tobin himself says that he had proposed this as a by-product of the proposed tax, not as its principal purpose.[53] Yet, it is understandable why many scholars and politicians – for instance François Mitterrand at the World Social Summit in Copenhagen in 1994 – have seen the Tobin tax as a source of huge revenue. After all, 1% of USD1.5 trillion is USD15 billion – a day! (More careful and reasonable calculations will be discussed later on). This is also a part of the argument by Korten, Martin & Schumann, and Giddens: the revenues of the Tobin tax could be of good use in many ways. It could be used to crucially alleviate poverty in the world or to re-organise the debts of the poorest nations; to create stabilising, global investment funds; to establish the basis of global social policy; and to contribute to many other socially useful purposes. A new rationale for the tax has thus risen.

Social Forces Supporting the Tobin Tax

Adam Harnes

At its most basic level, the Tobin tax represents an attempt to (re)regulate the increasingly liberalized global financial system. As such, social forces for and against the tax will largely reflect existing lines of division within current debates surrounding the emergence of a free-market global economy. Potential constituencies concerned with the Tobin tax can be categorized in terms of supporters, opposition and, what can best be described as, the 'swing vote'.

Supporters of the Tobin tax will be found among non-governmental organizations (NGOs) interested in multilateral regulation and economic redistribution (both within and among states) as well as among like-minded political actors within national political parties, the media and national and multilateral bureaucracies. To the extent that the Tobin tax will reduce price volatility and increase the macroeconomic policy autonomy of states, it will be supported by trade unions and social groups favouring expanded social welfare policies and the use of Keynesian

[52] Giddens 1998, 150-151.
[53] Tobin 1996, x.

demand management techniques to reduce unemployment. By helping to reduce volatility and to somewhat stabilize international capital flows, the Tobin tax should also be of interest to NGOs, less developed countries and others concerned with issues of international development; although this case may have to be made more strongly as the perceived benefits of the Tobin tax in this area often emphasize its revenue-generating potential.

Among national bureaucracies, support is likely to be greatest amongst those least connected to the financial community such as departments of industry and human resources. At the multilateral level, organizations such as the International Labour Organization, the United Nations Development Programme and the Commission on Global Governance have already produced reports giving the Tobin tax serious consideration. Finally, given the potential of the Tobin tax to act as a bridgehead for other forms of multilateral regulation and taxation (such as the oft-cited international tax on carbon emissions), environmental NGOs and bureaucracies are also likely to support it.

For all the reasons that these social forces will support the Tobin tax, the financial community and its supporters within national political parties, the media and national and multilateral bureaucracies will oppose it. In the latter case, for example, the International Monetary Fund (IMF) has consistently avoided the Tobin tax in its recent discussions of exchange rate volatility. Moreover, while important, the costs of paying the tax itself will be viewed as a secondary concern compared to its potential impact on macroeconomic policy and multilateral regulation. For the financial community and other supporters of a liberalized global economy, greater macroeconomic policy autonomy is undesirable as it can lead to 'looser' monetary and fiscal policies which they view as eroding investment profits through higher inflation and/or taxation.

In a similar fashion, it is important not to underestimate the extent of opposition based on the Tobin tax's 'demonstration effect' alone. By demonstrating the technical and political viability of international tax and regulatory cooperation, the Tobin tax is viewed by most free market advocates as the 'thin edge of the wedge' towards greater government intervention. This becomes particularly significant when we consider that one of the key ideas underpinning the liberalization thrust is the Thatcherite notion that 'there is no alternative'.

The most significant 'swing voters' concerned with the Tobin tax will be non-financial corporations and broader populations, particularly those within countries housing the major financial centres. While non-financial corporations may have some interest in reduced volatility and greater state autonomy in macroeconomic policy, this may be outweighed by their opposition to the Tobin tax's 'demonstration effect' and the potential for multilateral taxes and regulations that might affect them more directly. At the same time, non-financial corporations are increasingly less subject to volatility risks due to their use of derivatives to hedge foreign exchange exposures.

In terms of broader populations, one of the most significant recent developments is, as Barry Eichengreen argues, that "the traditional distinction between Wall Street, which is likely to oppose the tax, and Main Street, which is likely to support it, may be breaking down" (Eichengreen 1996). As more and more individuals gain a stake in financial markets through their mutual and pension fund savings, it becomes easier for the financial community to universalize their own interests in the eyes of policymakers and, thus, to generate grassroots opposition to the tax.

Finally, while not discussed thus far, a key determinant of support for the Tobin tax stems from the proposed distribution of its projected revenues. Most contentious will be the question of funding (especially direct funding) for multilateral agencies and international development. To the extent that much of the revenues will be collected within the major financial centres, nationalist sentiment, concerns over sovereignty and 'aid fatigue' may make these states unwilling to part with a significant

amount. Building support for the Tobin tax may, therefore, require a strategy of political triage in which proposals for the distribution of revenues are designed with an eye to building support for the tax among swing voters and national governments.

One implication of such a strategy is that revenues may have to be disproportionately allocated to countries which collect the bulk of the tax and to less ambitious multilateral goals such as the U.S. suggestion to create a stabilization fund to build the IMF's lender-of-last-resort capabilities. Another implication is that supporters of the Tobin tax may have to be convinced of its merits solely on the basis of its impact on volatility, macroeconomic policy autonomy and its potential 'demonstration effect'. By pursuing strategically less ambitious goals in the short-term, supporters of the Tobin tax are more likely to achieve broader re-regulatory goals in the medium-term.

References: Barry Eichengreen. (1996) 'The Tobin Tax: What Have We Learned?' in ul Haq et al (eds), *The Tobin Tax: Coping With Financial Volatility*. New York: Oxford University Press

Further reasons for the Tobin tax can be found for instance in an article published in the *Le Monde Diplomatique* in December 1997, written by Ignacio Ramonet[54]. Accoring to Ramonet, here are in fact two closely related problems. First is the one correctly identified by Soros, Tobin and many others: the volatility and magnitude of global financial markets that "is causing **universal insecurity**". But there is another problem as well, namely the **threat to democracy**:

> *"Absolute freedom of movement of capital undermines democracy and we need to introduce machinery to counter its effects. [...] Hundreds of billions of dollars are stashed away out of reach of the tax authorities for the benefit of powerful individuals and financial institutions. [...] The power to levy taxes on unearned income is a sine quo non of democracy."*

Consequently, Ramonet proposes three measures to be taken: closing down the tax havens; increasing taxes on unearned income; and levying a tax on currency transactions. Noteworthily, he also suggested an establishment of an organisation advocating the Tobin tax. As a result, ATTAC (*Association pour une Taxe sur les Transactions financières pour l'Aide aux Citoyens*) was founded in June 1998, and already has hundreds of local working committees and 6000 members in France. ATTAC has quickly become a centre of a transnational network, with official

[54] Ramonet 1997 in *Le Monde Diplomatique*, Décembre 1997.

associations being formed already in Brazil, Canada and Switzerland, and with dozens of other organisations being connected to ATTAC. ATTAC's main focus is on the Tobin tax, but this is only an element in its search for alternatives to such attempts at locking-in neoliberalism as MAI (the Multilateral Agreement on Investments), the NTM (the New Transatlantic Market agreement) and others.

ATTAC has collected world wide information about the current political discussions on the Tobin tax and explicit statements of support for it.[55] The list indicates that there might well be emerging a wide political momentum for the Tobin tax. For instance, recently there have been parliamentary discussions in Australia, Canada, France, New Zealand, and Sweden, among other places. Many political parties, labour unions, and NGOs around the world have expressed – mostly in the mid- and late 1990's – support for the idea.

International organisations such as ILO (International Labour Organisation) and the UNDP (United Nation's Development Programme) have published reports and launched campaigns to support the Tobin tax. An example of a recent initiative by an international organisation is that of the idea to create a World Taxing Organization, with the power to levy a global tax on international financial transactions and to orient the taxing policy of countries. This initiative was launched 12 May 1998 at the 32nd General Assembly of The Interamerican Center for Tax Administration (ICTA). Vito Tanzi, Director of the IMF and a specialist in taxation presented the proposal. "No representative of the 33 countries of the ICTA reacted against the idea". The claim is that this issue is now officially on the table at the IMF.[56]

Mostly in the OECD countries, ATTAC has conducted questionnaires of the opinions of political parties in 25 countries. In all of these countries, there are parties and movements supporting the Tobin tax. Repeated perplexed and uncertain answers to the questions reveal that the idea is still somewhat new and strange. Nonetheless, in a few countries, the parties supporting the Tobin tax and related regulative measures are (already?) in majority. The Greens seem to be in favour almost

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[55] See their WWW-pages at http://attac.org.

[56] About this initiative, see http://www.globalpolicy.org/finance/alternat/glotax2.htm.

universally, and so are some liberal-democratic and many social-democratic and socialist parties.

However, there is no universal line. French and Italian labour unions, for instance, might well have diametrically opposed views, and in many cases the Tobin tax has been raised as a positive alternative in an electoral campaign, but then, once in the government, it has been difficult to incorporate it into the government programme. Thus, the French Socialist Party leader Lionel Jospin supported the Tobin in his campaign, but as Prime Minister he seems to have turned against it, supposedly under pressure from the Ministry of Finance.

Hence, a quick look at the political situation in the late 1990's confirms the Tobin tax is on the global political agenda at the turn of the century. Indeed, it seems that it is gathering momentum behind it. However, although relative ignorance may well play a crucial role in the hesitancy of many – or even most – actors, there is also a persistent opposition against the tax. This opposition is based on two typical arguments against the Tobin tax. As already explained above, the first stems from the fundamentalist attitude towards orthodox economic theory: free markets are optimally efficient and able to adjust themselves. As the Austrian Ministry of Economic Affairs summarises the standard point:

> *From the point of view of the Ministry for Economic Affairs, we do, in general, not support an international tax on foreign exchange dealings as it would contribute to sub-optimal allocation of financial and, as a consequence, of real resources.*[57]

We have already tackled this argument (to the extent that it is possible to do it in a relatively concise Report such as this). As shown, besides fundamentalist belief in the orthodoxy, there seems to be very little to support this view, theoretically, empirically or historically. Indeed, both theoretical reasons and historical lessons support the thesis that there is a strong urgency to "throwing some sand in the wheels of global financial markets" – and to regulate the markets more generally.

However, there is another equally important counter-argument as well. It is often argued that **it is not possible** to establish the Tobin tax because of the tax evasion problem and

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[57] See http://attac.org/ang/index.html.

the lack of political support, and that, furthermore, the Tobin would not lead to the desired effect anyway (it is not effective). These arguments amount to saying that attempts to establish the Tobin tax must be, for various reasons, **futile**. The next section of our Report is devoted to tackling these deep-rooted moves of rhetorics of reaction.[58] In the course of the argument, we also develop the proposal for a currency transactions further, in some detail.

[58] Hirschman (1991) claims that all rhetorical reactions – since the early 19th century until now, to the turn of the 20th and 21st century – against granting equal rights, democratisation and the development of the welfare state can be classified into three categories. The *perversity thesis* maintains that any purposive action to improve some feature only serves to exacerbate the condition one wishes to remedy. The *futility thesis* holds that attempts at social transformation will be unavailing, that they will fail to have the desired effect. Finally, the *jeopardy thesis* argues that the cost of the proposed change or reform is too high as it endangers some previous, precious accomplishment. The criticism against the Tobin tax stemming from the orthodox economic theory can be read most plausibly as the jeopardy thesis ("throwing sand in the wheels of the global financial markets would only threaten the accomplishment of the free markets, which guarantees optimal outcomes"), whereas the worries about 'tax evasion' and 'lack of political will' amount very easily to forms of the futility thesis.

4. Problems of establishing and implementing the currency transactions tax

Even the very cautious 1996 OECD Working Paper on financial deregulation had to acknowledge that deregulation has led to increased risk-taking and destabilising speculations as well as to decreased private saving and higher interest-rates.[59] After the crises of the late 1990's, there is an even more widespread and stronger perception that the deregulated, floating and freely convertible financial markets have not been collectively beneficial in terms of efficiency, stability or autonomy of economic policies of most states[60]. More generally, it now appears that there is no evidence that the floating, deregulated, freely convertible exchange system – or, for that matter, global neoliberalisation – has had any advantages to the real economy.[61] Suddenly, the burden of proof is on the side of those who still believe in the efficiency gains of one-sided and straightforward liberalisation and deregulation. Something must be done to remedy the situation, to reform the global financial markets.

However, it may well be that proposals for reforms such as the Tobin tax are very difficult to establish and implement. Perhaps it is best, all things considered, just to leave things as they are? For instance, we may seriously doubt that the currency transactions tax would be workable, if traders found ways to evade it. And, equally importantly, lack of political will may make it entirely futile even to try to establish and implement the Tobin

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[59] OECD 1996, 7-9. This paper discusses the Tobin tax as a possible solution, but dismisses it on the grounds that the likely effects are controversial, and that "a major stumbling block would appear to be competition between offshore financial centres" (p.12).
[60] Certainly there are many actors who continue to benefit from the system, either directly (in the form of revenues and profits) or indirectly (for instance, because the freely convertible and hugely expanded financial markets seem to serve to compel most states to follow the desired neoliberalist economic policy). But from a global perspective, none of these amount to a collective benefit.
[61] In addition to the endless stream of financial crises, it also seems to be the case that at least for the G7 countries all key economic indicators – growth, inflation, employment, distribution of income, interest rates etc. – have worsened since 1974 as opposed to what they were in the era of the original Bretton Woods system (see Felix 1995b). Of course, economic developments depend upon unique, historical institutional arrangements, and relations of production and exchange have undergone major qualitative changes since the Bretton Woods era. The context is different in many ways. Yet, Felix's point shifts the burden of proof entirely on those who still believe that freely floating and freely convertible financial markets, together with other processes of neoliberalisation, have been and, (tauto)logically must be beneficial in terms of efficiency.

tax. And even if it were possible to establish the Tobin tax, would the tax really accomplish its main task, namely stabilise the markets and prevent speculation? The Tobin tax might even be counter-productive.

The tax evasion problem is, *prima facie*, a serious one. There are two major concerns: financial substitutes for currency transactions, and locational substitutes for contemporary financial centres. The tax must cover all possible substitutes, and financial transactions through tax havens must be systematically penalised in one way or another. But we will argue that the problem is in fact much less alarming than sometimes feared. Also a modified, non-universal system of Tobin taxation can work well, particularly when there is a movement towards a more global and universal system.

No relatively small, uniform currency transactions tax would prevent all speculation from taking place. If the expected profit margins are big enough, as with the emergence of anticipation of a major devaluation, the Tobin tax would play only a relatively small role. Perhaps the Tobin tax is thus futile because it is inefficient when most needed? Yet, the Tobin tax is intended only to “throw sand in the wheels”, not to stop the wheels from rolling. Other arrangements are needed, too, in order to counter the effects of speculative runs and other imbalances.

The argument that there is no point in trying to make the Tobin tax workable because there is not enough **political will** for establishing it is circular. It might well be difficult to organise collective action, and powerful interests might be opposing the realisation of the Tobin tax, yet these are not arguments against the tax itself. At best, these arguments can be seen as careful assessments about what is and is not “realistic” in a given historical situation: given the conditions, we should not waste our energies on this particular project now, but should rather concentrate our energies on other, perhaps related projects for the time being (until, finally, the situation will change).

At worst, the arguments amount to a reactionary judgement favouring passivity almost *a priori*, based on the implicit notion that it is always best to conform with the *status quo* – however rapidly that might be changing, however fluid it might appear to others – because of the firm conviction that ‘there is no alternative’.

That is, the claim about political difficulties might amount to a generalised futility thesis: all attempts at social transformation will be unavailing, for they will always fail to be materialised without the supportive will of the powerful (who in any case always favour *status quo*), and/or because of the general nature of things. Certainly, if you can convince many enough actors that the futility thesis holds also in the case of reforming global financial markets, there will be no political will for the Tobin tax reform!

Our assessment, to be presented and discussed below, of the current situation suggests that the most feasible strategy might be to start with a non-universal equivalent to the Tobin tax. Although this is only a strategy, not an end in itself, we will discuss the technical and political problems related to a non-universal tax regime. Rather sooner than later, this should and will be followed by a uniform global tax; and, yes indeed, it would be best to apply the global tax straight away. Thus, this non-universal tax regime is intended to become universal in two phases.

4.1. The problem of tax evasion: financial and locational substitutes

The problems of tax evasion are practical and technical. If they are used as argument against a tax, the logic must be the following: since X will be able to find ways to evade these taxes, X should not be taxed. But this is fallacious. Given that there is a case for taxing X, the right conclusion should be: X should be taxed, and the loopholes should be closed. Even a stronger conclusion might be possible: creating loopholes should be penalised, too.

One fear in establishing the Tobin tax is that actors in the financial markets, such as investment banks and multinational corporations, will find loopholes and get around the tax by, for instance, means of financial substitutes for currency transactions. To begin with, it is important to note that the present system has not come about by loopholes, but by co-ordinated and orchestrated government actions, even though the deregulatory measures have not always been in accordance with the original

intentions of many states[62]. Now, only when these deregulatory measures have been carried out – always strongly supported by the US and the UK governments, and the IMF – all kinds of fancy financial innovations have become possible (also enabled although not determined by new information technologies).

The meaning and importance of the tax evasion problem are exemplified in four cases. The rate of taxation can be either high or low, and the area of taxation can exclude or include major financial centres. Our argument, to be substantiated below, is summarised in Figure 1.

Figure 1: Four cases of the problem of tax evasion

	Low tax	**High tax**
All major financial centres INSIDE	**No problem**	**More measures and surveillance needed**
Some financial centres OUTSIDE	**Feasible with innovative arrangements**	**Presumably not sustainable in the longer run**

Even though the figure appears non-dynamic, the cases where not all major financial centres are inside the area of taxation are meant to describe the phase of gradual transition from a no-tax situation towards a universal and uniform tax. In the following we will discuss these four cases in further detail.

[62] Out of seven categories of regulatory measures, namely interest rate controls, mandatory reserve requirements, quantitative investment restrictions, capital controls, securities market regulations, restrictions on line-of-business and ownership linkages, and restrictions on foreign bank entry, only in one case deregulation seems to have been carried out because of the direct pressure stemming from the off shores, namely mandatory reserve requirements. OECD, op.cit., 5-7.

4.1.1. A low global tax

Let us suppose that a uniform but low global Tobin tax has been established. Most states, including the EU and other major financial centres, participate, and the rate of taxation has been set for instance at the level of 0.05%. Peter Kenen has scrutinised this case thoroughly and concludes that a globalised Tobin tax is quite easily enforceable.[63] Avoidance efforts over time through asset substitution, offshore booking and the relocating of foreign exchange markets are containable.

The problem here is twofold. On the one hand, the transactions covered by the tax must be defined. Exchanging FIM, or soon euro, to GBP in a Forex office, before travelling to another country, is just one type of currency transaction. Banks' transactions are similar – however typically much more voluminous – although it might take two or three days for them to actually receive the GBP or FIM they have purchased, for various reasons. Nonetheless, these deals are called spot currency transactions: they occur on the spot. Currency transactions are either made on the spot or the result of a future commitment (which, in turn, is definite or optional).

In the financial market, currency transactions are joined by a number of other operations and financial instruments.[64] Many of these are called derivatives. The value of a derivative is derived from an underlying asset. The derivatives can be divided into four groups, namely: outright forwards, swaps, futures and options. Each group then constitutes of several subgroups. The nature and relative significance of these types are explained in Figure 2.

The Tobin tax must not only cover all these, but it must define in detail the actual currency transactions subject to taxation; determine whether it is the buyer or seller who should pay the tax; determine whether it is the dealing or booking site that determines to whom and how and when the tax should be paid; as well as determine whether to adopt a national or market based approach to the taxation.

In the case of spot transactions, the actual currency transactions are quite clear. They are also visible in the case of forward transactions: a counter party is already paying for the

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[63] Kenen 1996.

[64] For an introduction, see for instance Jarrow & Turnbull 1996.

currency he is soon going to get from the other counter party. However, swaps, futures and options are more complicated, for in these cases it is not obviously clear what the (taxable amount of the) currency transaction is. However, a simple principle would be to tax them at the **time for when the actual exchange of currencies occurs**. The price for future or option contracts would thus be taxable (at the moment of purchase of the contract), as would also the transaction itself if it eventually takes place (at the time specified in the contract).

But what does this mean in the case of swaps that seem to cover 40% of all currency transactions? It is clear that the underlying assets of the swaps are subject to taxation. As far as the swaps themselves are concerned, there are two further possibilities: either to suppose that once the underlying asset is taxed, there is no reason for further taxation; or to tax the swap in its nominal value, or some significant part of it (i.e. treat swap as a new spot/forward transaction). The first option would lead to exempting swaps from the tax; and the latter to double taxation and to drastic decline in the volume of swap transactions, since the volume of swap transactions is very sensitive to small cost increase. **This would mean throwing more sand in the wheels of the global financial markets**, and is well in accordance with the idea of the Tobin tax.

Figure 2: Types of currency transactions[65]

Type of Transaction	Nature	Relative significance (1992)
Spot transactions	Currency exchange, settled in less than 3 days (buyer pays now, the purchased currency is delivered almost on the spot)	Almost 50% of all transactions
Outright forward transactions	Currency exchange, settled in 3 or more days (unregulated futures, customized individually)	About 7% of all transactions

[65] Definitions by the authors, the relative significance of different categories based on Table 4.1. in Kenen op.cit, 111. This table discusses only instruments relevant to the Tobin tax.

Swap transactions	Pairing a spot and outright forward transaction, or two forward transactions, and exchanging them or their yields	Nearly 40% of all transactions
Futures	An agreement (standardized and regulated) to sell or buy currencies some time during the contract's expiration period. For this commitment, a margin account for daily settlements with a clearing house to act as collateral is set up to master the risk of failure of either party now.	About 1% of all transactions
Options	An option to buy or sell currencies at a given rate on a given date; for this possibility, a price is paid now (more expensive than a future)	Less than 5% of all transactions

It is not clear whether the revenues would be bigger or smaller this way, for 0.05% of the actual yield differences paid between the counterparts is not that big an amount of money anyway. And, even with 'double taxation', at least some currency swaps would still remain potentially profitable. Hence, it seems that swaps should be treated as no different than spot or forward transactions.

In all cases, the payment of the tax should be split into two: the seller pays half, the buyer pays the other half. It also seems clear to us that the tax should be collected on a national basis.[66] Each bank (or any other economic actor engaging in currency transactions) would collect and consolidate the necessary information on its transactions – those conducted at every dealing site – and pay the corresponding tax to the bank's home country, which is the country where the bank has its headquarters. That is, the booking site should be fixed on a national basis. When the tax is levied on a national basis, banks cannot avoid it by moving their

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[66] A market based system is defined as when the tax due on transactions at each dealing site would be paid to the host country; the country where the dealing site is located, according to Kenen op.cit. Kenen himself prefers the market based system, because it would offer fewer incentives for countries to attract additional tax-free business, and because it would be more favourable to the UK. We do not see these as major advantages. Quite to the contrary, it is not only the case that in our assessment the national system would be more efficient (also with a higher tax), but it certainly suits the political strategy of gradual establishment of the global tax much better.

dealing sites to tax-free locations – to countries, whose governments do not collect the tax.

However, according to Kenen, a major problem of this approach is that a government that wanted to provide a tax-free dealing site could adopt or invoke a legislation to confer confidentiality on individual foreign transactions.[67] A possible response is to **penalise all non-booked transactions**, wherever they occur, and to raise the **tax for transactions involving tax-free countries' currencies** much higher. Given that most countries and all financial centres were within the taxation system, this should not have any adverse consequences; it would simply marginalise, or even better, exclude countries trying to exploit non-taxation in order to break the system.

After the transactions subject to taxation are extensively and well defined, the only remaining problem is the one of countering tax avoidance by substitution in the form of newly created financial instruments.[68] Persuasively, Kenen argues that typically more complex derivatives create more transaction costs for the counter parties and more risks for them. Particularly if the tax is very small, it is unlikely that actors will see the need to invest in the creation of new investments. And if they will, "governments could readily rule that the [financial instrument X] was designed expressively for tax avoidance and could thus treat [the instrument] as a taxable transaction"[69].

However, even in the case of a low global tax, there is a need for a supranational authority for three reasons. Firstly, there must be a body that closely follows developments in the currency markets, (quickly) initiates actions when problems occur, and provides a forum for discussions and decision-making concerning relevant developments in the financial markets and improves the Tobin tax regime. Secondly, there is also a need for a collective

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[67] Ibid., 113.

[68] However, John Grahl from the Business School of the University of London suspects that banks can also hide transactions behind balanced positions. "In practice huge amount of opening and closing of such positions could be going on continuously". Although eventually these positions must become unbalanced (if the money is ever going to be used for something real other than derived currency transactions), this might be an important way of hiding derivative transactions. If this really turns out to be a major problem, either a way must be found to introduce new book-keeping and surveillance systems, or direct capital controls must be re-introduced to back up the Tobin tax. (Grahl at the ATTAC international economists seminar in Paris on 25 January 1999, and in a private e-mail message, 10 February 1999).

[69] Kenen op.cit., 119.

body that sees to that countries really implement the principles and rules of the Tobin tax. This body must be given power to sanction non-complying countries. Finally, it must also be responsible for collecting, with the national authorities, the tax revenues, and allocating them further.

4.1.2. A high global tax

Suppose that the rate of taxation is much higher than 0.05%. It could be 1% like in Tobin's original proposal, or even more, up to 2% or 3%. As Felix and Sau argue, but going beyond their modest proposals, we should also consider taxation at a level that would have more significant macroeconomic and other global ethico-political objectives, by stabilising the financial markets more efficiently, and by collecting more revenues also for global purposes.[70] Suppose further that the administrative arrangements were organised as specified above in the context of a low tax. What difference would a higher tax make? As stated, a higher tax would obviously curb global financial markets much more effectively; it is not impossible that it would make more complicated derivatives disappear totally. It would also create, to use the terminology of economics, "incentives" to innovate substitutes for currency transactions. In other words, also the tax evasion problem would become more severe.

Sometimes the effects of a tax on currency transactions are studied as if the currency transactions were homogeneous.[71] They are not. Thus, there is no singular elasticity of taxation and transaction costs. Spot transactions are very different from many derivatives. A high tax would hit swaps particularly hard (and indirectly their derivatives, such as swaptions), for they are taxed like spot and outright forward transactions, but they are much more sensitive to increased transaction costs.[72]

Now, the standard justification of the existence of swaps – and other derivatives – is that they play a stabilising role, if not collectively, at least for those individual firms who are engaged in

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[70] Felix & Sau 1996, 245.
[71] In Felix 1995a, 199b and Felix & Sau 1996, this impression is created by the assumption that only spot transactions should be taxed. There seems to be no reason for this assumption.
[72] It might be possible to use other measures to tax them, for instance, half of their nominal value.

real economy activities. By using derivatives, firms can hedge against small changes in exchange and interest rate fluctuations, that is, they are able to manage exchange rate changes and secure yield from their economic actions (in fact, banks do this for them, once they have paid a price for banks). This makes the environment of their decisions more predictable and, in principle, enables longer time-horizons.

However, we know that by far most currency transactions are speculative by nature (only much less than 5% are directly related to the real economy). From a firm's point of view, outright forwards, futures and options may be useful, but swaps seem to serve only needs of the financial markets.[73] Speculative markets tend to shorten time-horizons by virtue of the short-term opportunities and volatility they create. We also know that the derivative markets would not exist without radical uncertainty in the currency markets (indeed, instead of any "rational expectations", there must be an abundance of contradictory assessments for these markets to exist in the first place). And when there is radical uncertainty, many actors can take it entirely wrong and, by their collective actions, produce effects that would not otherwise be there. The volatility of financial markets is marked by constant self-fulfilling prophecies.

> *[...] speculators concentrate on how 'the markets' will respond to news, not on basic economic meanings and portents. The hope that transactions taxes will diminish volatility depends on the likelihood that Keynes's speculators have shorter horizons and holding periods than market participants engaged in long-term foreign investment and otherwise oriented towards fundamentals. If so, it is speculators that are more deterred by the tax. It is true that some stabilising transactions might also be discouraged; fundamentalists alert to long-run opportunities created by speculative vagaries would have to pay the tax, too. The judgement that those benign influences are not now so dominant in short runs is based on a presumption that the markets would not be so volatile if they were.*[74]

Thus, the argument about the stabilising nature of such derivatives as swaps (swaptions etc.) seems to be dubious. But would it be possible to separate the wheat from the chaff?

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[73] However, it is true that most derivatives in most contexts do not affect the magnitude of return; only how the return is distributed. Stiglitz 1989, 103, has claimed that many of the new financial innovations have actually made almost everyone worse off – except very few.

[74] Eichengreen, Tobin & Wyplosz 1995, 165.

We do not believe that a 1% – or even 2% – tax would eliminate outright forwards, future or options, and some swaps would be likely to survive as well. But, for the sake of the argument, and very counterfactually, suppose that after the introduction of the tax firms would not have the possibility of securing their yields in foreign currency. Even in this case, there would be substitutes for the derivatives that are now used to manage currency positions. It would be possible to initiate, by public political actions, insurance instruments against exchange rate fluctuations, preferably backed by a global fund derived from the revenues of the Tobin tax.[75] These regulated insurance markets could also be initiated by the actions of the supranational body in charge of the Tobin tax regime. Any insurance against exchange rate fluctuations would be sold only to actors who could demonstrate a connection to real economy activity[76]. This is only a hypothetical possibility; in practice an insurance of this kind could be established, if needed, to complement existing possibilities to secure yields.

Only a substantial – higher – taxation rate could curb the financial markets sufficiently and alleviate the problem of speculation. Also bigger revenues would be desirable for a number of ethico-political reasons. In the absence of persuasive counter-arguments, there thus seems to be a case for a much higher tax than 0.05%. It could be anything between one and three percent.

Offshore

Ronen Palan

The state system has unwittingly created a great number of relatively unregulated juridical spaces in which economic activities can develop more or less without hindrance. Examples of such juridical spaces include the Euromarket or the offshore financial market; the tax havens, of which there were 62 in the last authoritative count (Diamond and Diamond 1998): Export Processing Zones and Free Trade Zones whose number rose from two in the early 1960s to over 800 today, providing

[75] This idea is based on Mann 1998, 3, although she does not discuss it in the context of the Tobin tax.

[76] These types of insurance could be monitored by, for instance, the national guarantee agencies, or by a global organisation serving as a parent organization to the national units. The demonstration of a real economy content of the transaction is no more difficult than to meet the conditions of a car or life insurance.

employment directly to over a million and a half workers world-wide (McMichael 1996). In addition there has been a significant impact of 'flag of convenience' which dominate international maritime fleets, and the extension of the principles of 'flagging out' into other spheres such as aircraft leasing. The Internet is providing opportunities for the extension of similar principles into areas such as gambling, pornography, telecommunication and on-line merchandising.

These fledgling juridical realms are designated as offshore spaces (Palan 1998a; 1998b). Such spaces manifest themselves in three varieties:

1. As territorial enclaves normally located near airports or ports as in the case of the export processing zones.
2. As 'juridical' or virtual enclaves, as in the case of the International Banking Facilities and the 'spontaneous' offshore financial centers.
3. As specialized unregulated jurisdictions, many of which consist of the small islands.

Here I discuss only the offshore financial market and the tax havens. Offshore finance, or what used to be called the Euromarket, is a market unregulated by states which is believed to have emerged in 1958. During the Suez Canal crisis and the ensuing run on the British sterling, the British government imposed restraints on sterling credits to countries engaging in third-party transactions within the sterling area and, in addition, raised the Bank rate to 7 percent.

In response, British banks began actively to solicit dollar deposits to use in trade credits. These transactions in dollars were then considered to be taking place not under the exchange rate regulation, reserve regulation or any other regulations of the British state, hence *de facto* under no regulation at all.

In 1963, the loan market was supplemented by the Eurobond market, which consists of bonds underwritten by an international banking syndicates and not subject to any country's securities laws.

As Eurobanking developed and spread, it became progressively difficult to precisely define its boundaries. Hewson (1982, 406) argues that in addition to Eurobanking, offshore fare cases where:

- 'some attempt is usually made to separate the 'offshore' from the 'onshore' banking activities and the rest of the domestic financial system, either by exchange control, regulation, tax incentives, separate accounting procedures, etc.

- the institutions in the market tend to be classified as non-resident for balance of payments purposes

- transactions in these markets have a significant non-resident component. In some cases transactions are specifically restricted to non-residents, but in others 'resident access' to the market is permitted to varying degrees

- transactions in the offshore market are primarily restricted to foreign currencies

In this broad sense, the term offshore designates the regulatory realm in which certain financial transactions take place. Offshore is not physically separated from onshore and indeed, some types of offshore financial markets can be created quite simply 'if books for foreign to foreign accounts are kept separate from books for domestic financial and capital transactions' (Hanzawa 1991, 284). The offshore

finance market(s) therefore may be thought of as 'fictional' or purely 'juridical spaces' or mere 'booking devices.'

The literature distinguishes among three types of offshore financial centers: the so-called 'spontaneous' offshore sites, such as the UK and Hong Kong; International Banking Facilities (IBF) such as New York and Tokyo; and tax havens. According to the latest census, 62 states are tax havens (Diamond and Diamond 1998). However, these three categories are 'ideal types' as each offshore financial center and tax haven offer their own unique 'bundle' of financial regulations. The spontaneous offshore center of the City of London is so called because, allegedly, it grew up spontaneously. An International Banking Facility (IBF) is a more stringent type of offshore market, in which companies must apply for a license to trade. The first New York IBF was set up on 1st December 1980. In turn, the creation of the New York IBF spawned the creation of the Tokyo in 1984. The Singaporean IBF, known as the Asian Currency market, was established in 1968 when Singapore licensed a branch of the Bank of America to set up a special international department to handle transactions of non-residents.

Tax havens are defined as those economies that have made a deliberate attempt to attract international trade oriented activities by minimization of taxes and reduction or elimination of other restrictions on business (Johns 1983, 20). Typically, these are countries with (1) little or no income or corporate tax, (2) strong bank secrecy laws, (3) good telecommunication links with global markets and,(4) public presentation as a tax haven. The traditional tax haven is used as a central point for handling paperwork and for preparing and processing trade documents. Companies depend on tax havens for passage of title of goods so that these transfers may take place within a minimum of red tape. Companies use tax havens to accumulate dividends, interest and other income.

The Diamonds (1998) estimate the offshore finance stands currently at $5 trillion of investment funds. The offshore financial markets operate through a system of hierarchical and interconnected financial centers: London, New York or Tokyo serve as *primary* centers for world-wide clients and act as international financial intermediaries for their market regions; *booking centers* such as Nassau or the Cayman Islands are used by international banks as the location for 'shell branches' to book both Eurocurrency deposits and international loans; *funding centers* such as Singapore or Panama play the role of inward financial intermediaries, channeling offshore funds from outside their markets towards local uses; and collection centers like Bahrain engage primarily in outward financial intermediation (Park 1982).

Such a hierarchy is testimony to the degree of specialization and interdependence among offshore centers. Supported by their respective states and boasting slightly different packages of legislation, these centers are the platforms upon which an integrated offshore finance system had evolved. In that sense the state system itself is providing the material and legal infrastructure of offshore (Palan & Abbott 1996).

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However, with a higher tax the costs and risks of more complex derivatives – designed perhaps only for tax avoidance – might become much more easily bearable. Even if they are costly and risky themselves, they might become attractive. Moreover, some states might be willing to let the banks and currency exchangers based in their territory get away with the tax, if not *de jure* then *de facto*, in order to create a competitive edge for them. There is thus a need for closer and more thorough surveillance over the market developments and state practices. Yet, these **difficulties are merely practical**. In principle, they do not make any difference to the way the taxation system should operate.

If it appears that widespread tax evasion starts to occur, further regulatory measures might be needed. One possibility is to create a register of legitimate transactions. All legitimate booked transactions also need to be accompanied with a registered and standardised code. Any actor contemplating upon further market innovations that might have to do with currency transactions would have to apply for permission from the supranational body governing the Tobin tax regime for introducing the new instrument. If the body rules that the new financial instrument is a form of currency transaction, it should naturally be subject to the tax. Any illegal transactions, and particularly attempts to innovate illegal substitutes for currency transactions, should be strongly penalised. If necessary, in the last resort, new forms of capital controls must be (re-)introduced to back up the Tobin tax. These capital controls, too, should be governed globally.

4.1.3. A low, non-universal tax

It seems that the real difficulty is in establishing the system of taxation. If most states and all major financial centres have to be in the system from the very beginning, the project can be ruled out on the grounds of political prudence. "The US and the UK will never join". The absence of any major financial centre is

considered to be a major stumbling block for materialising the idea of the James Tobin tax.

Indeed, most analysts have thus far presumed that the system of taxation must be universal and uniform to be workable, including Tobin himself. Still, in 1995, he (with Eichengreen and Wyplosz) claimed that only a universal system of taxation is possible:

> *A transactions tax on purchases and sales of foreign exchange would have to be universal and uniform: it would have to apply to all jurisdictions, and the rate would have to be equalised across markets. Were it imposed unilaterally by one country, that country's forex market would simply move offshore.*[77]

The sceptics are, if possible, even stronger in their judgement. "If any major financial centre does not comply with the regulations then unbalanced foreign exchange positions and foreign exchange transactions will be booked to offshore institutions in that centre."[78] In this light, Garber and Taylor discuss the consequences of a hypothetical unilateral French tax:

> *As market participants seek to avoid the tax, its implementation will immediately push foreign exchange transactions out of Paris either to London or to New York, and the transactions will be booked in those centres. If the French regulators can impose the tax on French bank subsidies abroad, the French banks will be cut out of the foreign exchange business. This is the first main implication. Suppose that on a normal day, the franc foreign exchange market clears with no intervention by the Banque de France – that is, no one approaches the authorities to exchange francs for foreign currency at the lower end of the band, which is, say 3 francs per deutsche mark. Gross values of franc foreign exchange are then unaffected by the tax and no one pays the tax. On days that the Banque de France intervenes, however, some banks must engage in an explicit foreign exchange transaction with the Banque de France in Paris and pay the 1% tax. [...] a transactions tax policy imposed at the national level is equivalent to nothing more than a widening of the band at the edge at which the domestic currency is weakest. This is the second main implication.*[79]

In other words, the claim is that the financial market actors will only operate in taxable jurisdictions if the taxable currency is

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[77] Eichengreen, Tobin & Wyplosz, op.cit., 165.
[78] OECD, op.cit., 12.
[79] Garber & Taylor 1995, 174-175.

marked up by the percentage amount of the tax. Since this burden falls on the central bank, the tax policy equals a depreciation of the taxable county's currency by the tax' percentage rate.

Suppose, however, that the tax level is quite low; that it is not only a single country introducing the tax, but for instance the euro-EU in concert with a grouping of other countries; and that the "regulators" of the authorities of the euro-EU and/or these other countries can indeed impose the tax on all its bank subsidies abroad as well. Would it be possible to introduce the Tobin tax along these lines? Note that Tobin himself recently said in an interview in *Le Monde* that he has been thinking about this possibility a lot, and that he now believes that to start with, it would suffice that 20 countries would introduce the tax.[80] But even in that interview, he seems to be saying that all major financial centres must be included. In the following, we will argue that this is not necessary. The question is how, and with what consequences, could this kind of a non-universal tax be introduced?

First of all, note that there are implicit assumptions at play in the judgements that the tax must be universal and uniform to be workable. Tobin seems to suppose that the taxation would be implemented at the dealing site. However, when the tax is levied at the booking site, on a national basis, banks cannot avoid it by moving their dealing sites to tax-free locations. Remember also that the payment of the tax should be split into two: the seller pays half, the buyer pays the other half. The only tax-avoidance option remaining, as argued by Garber and Taylor, is to transfer all currency transactions to foreign, tax-free banks. But is it reasonable for banks to do so?

It is hard to see why banks would give up exchanging currencies just because of a low-rate tax. Even with a higher tax, the claim that "if the French regulators can impose the tax on French bank subsidies abroad, the French banks will be cut out of the foreign exchange business" sounds dogmatic, based as it is on a strongly abstracting and idealising theory; in the real world, it is not necessarily true. At any rate, it is likely that taxation at the level of 0.05% would not seriously threaten the profitability of currency transactions – after all, at any given transaction they

[80] Tobin 1998, an interview in *Le Monde*, 17 novembre 1998.

would be paying only half of it – and there are also institutional reasons why banks and their real economy customers would continue business as usual, despite the small tax. In fact, the banks make most currency transactions for their own purposes, typically speculatively. Any transaction with a cover higher than 2.5 basis points would remain profitable. Finally, the banks paying the tax know that many of their counter parties pay tax as well, and the prospect is that increasingly the others will do so, too.

Moreover, and as an additional measure this may be crucial, it is also possible and desirable to make the banks residing in tax-free areas pay an equivalent to the Tobin tax. Namely, it is possible to apply a tax to all domestic-currency lending to non-residents, which are not based in the countries that take part in the Tobin tax regime. This would not only discourage speculative sales, regardless of the market in which they are booked, but also solve the major problem of Tobin tax evasion by money-lending to banks based in tax-free areas[81]. Let us go back to the already outmoded example of France:

> *Currency traders wishing to bet against the French franc, to take a concrete example, must obtain francs in order to sell them short. Except for francs made available by the liquidation of existing offshore asset positions, which are by definition limited in amount, these can be obtained only by borrowing from French financial institutions. Hence, the idea of taxing or placing deposit requirement on loans in domestic currency to non-residents.*[82]

This would work exactly the same way for *euro*, *rupiah*, *rouble*, *peso* or *real*, or for any other currency. This tax should also be much higher than the non-universal Tobin tax proper. If the Tobin tax proper is, say, 0.05 %, or 0.1%, the tax on the loans to non-residents could well be 1% or more. This would easily compensate for the loss of the competitive edge of the domestic banks due to the Tobin tax and encourage foreign banks to be more favourable to the extension of the Tobin tax to their respective countries as well.[83] Moreover, it should be easy to

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[81] It is the crux of Garbner's 1996, 134, 140, argument against a non-universal tax that a new division of labour between banks emerge: "The role of banks in the taxed jurisdictions will be to provide cross-border credit to the untaxed banks". But in our scenario, this would be taxed more heavily than currency transactions per se.

[82] Eichengreen, Tobin & Wyplosz, op.cit., 167.

[83] Later, we will argue that this should be complemented by an organised, global political campaign for a global, universal Tobin tax. The revenues of the first phase tax could be used

implement this tax. It can be administered, like the Tobin tax proper, "by adding a few lines of code to banks' computerised trading programmes"; and "compliance could be monitored by periodic inspection of banks' computer records"[84].

Furthermore, to make the small, non-universal tax more effective against speculation, it could be made into a two-tier tax, as proposed by Spahn[85]. Like the European Monetary System before the advent of *euro*, the two-tier Tobin tax would consist of a target rate and an admissible spread or band for any given currency. When the currency is within the band, the low-level underlying currency transaction tax is charged. The exchange surcharge would be applied automatically whenever speculative attacks against currencies occurred, that is, it would be switched on whenever the trading price for a currency passed a predetermined threshold. The exchange surcharge would be much higher, 1% or 2%, possibly 3%, or even more.

Hence, a low, non-universal equivalent to a universal, uniform Tobin tax is not only possible but quite feasible as well. It would be slightly more complicated than Tobin's original proposal, but not much. Furthermore, somewhat like the three phases of constructing the EMU, the universal, global system of currency transaction taxation could be implemented in two phases:

1. In its first phase, the system would consist of the euro-EU and a group of other countries, or a bigger group of other countries without the EU. However constituted, this grouping should establish an open agreement – any state can join at any time – and a supranational body orchestrating the tax and collecting the revenues along the lines proposed above:

    - Small underlying transactions tax (10 basis points, at the most).
    - Much bigger exchange surcharge.
    - A relatively high tax on domestic-currency lending to non-residents (only to non-residents; i.e.

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to subsidise this campaign (for instance, an advertisement campaign addressed both to the customers of the banks and to the citizens of democratic states).

[84] Eichengreen & Wyplosz 1996, 25.

[85] Spahn 1996.

residents of a country which is not yet part of the tax regime).

2. In its second phase, which should be carried out either when all major financial centres and most other countries have joined the first phase system, or at latest by, say, year 2010, a universal and uniform Tobin tax at a relatively high rate would be applied.

This arrangement would make it possible for a grouping of countries to proceed quickly without the consent of every state (including such financial centres as London/UK and New York/US), yet it would not compromise the aim of a universal and uniform tax. The possibility for countries to join the system when they wish makes it possible for a political build-up against those who do not join, or rather, have not joined.

Suppose that this system was started by a small group of countries. Soon other countries join in, and theoretically, it is quite possible to envisage a situation where countries that have been or see themselves as potential objects for financial speculation all join in. Let us assume that the countries, which have joined have done so because they see this as a form of insurance, an insurance against financial speculation. The countries should be willing to pay a price for this insurance: to take the risk that there will perhaps be a small-scale transfer of currency markets, possibly some depreciation of its currency, both due to unilateral implementation of the Tobin tax (as described above). But at most this would be only temporary, if it occurs at all under this two-phases scheme.

Furthermore, let us then assume that the countries within the system globally represent most countries, except the few remaining financial centres. The tax imposing countries would also have the privilege of participating in deciding what to do with the revenues, in addition to keeping a portion of those revenues themselves. Wouldn't all this create a political pressure for the leading financial centres to join in as well?

4.1.4. A high, non-universal tax

Whether in the form of a uniform, high transaction tax, or a two-tier system with a high underlying, basic tax, a high-level non-

universal tax would be presumably hard to manage. Nonetheless, for the sake of the argument, suppose that this kind of tax was introduced by a grouping of countries. What would happen?

In fact, we do not know for sure. There are only likely scenarios, since the future cannot be predicted. A lot depends on the overall, global context – economic fluctuations and turns, political struggles over extending the taxation regime, innovations concerning forms of surveillance, taxation, and capital controls etc. The future might well provide us with new surprises, new coincidences and contingent episodes. For instance, Malaysia is planning to replace the strict capital controls – that it re-introduced in 1998 after the currency crisis – with a unilateral tax on the outflows of capital. In effect, this will be a variation of the unilateral Tobin tax, and there seems to be no reason why it should not work.[86] It might be possible to generalise this experiment to cover all emerging markets in Asia without any major trouble.

Nonetheless, other things being equal, it is likely that multinational corporations and other economic actors would tend to loose interest in bank A if they had to pay an additional 1% or more for their currency transactions via that bank A, in contrast to other options they have. Corporations would turn to banks not paying the tax (note that multinational corporations can all too easily transfer nominal payments within the organisation, particularly if national and international laws allow for this). Most self-serving currency transactions of the tax-paying banks would loose covering, too. Even with additional measures such as tax on domestic-currency lending or some forms of capital controls, at least according to the reasoning of economics, there is a tendency for these banks to loose their forex markets (again, given a context where this is otherwise reasonable and allowed to be possible). Particularly in the longer run, also the revenues from the high tax might therefore turn out to be rather small.

But so what? If the aim is to control speculation, would not this work anyway? Banks based in these countries would perhaps become more national and less concerned with currency speculations (if they survived these changes). A tax on domestic-currency lending would restrict speculations, and so would capital controls and other regulatory measures. At least volatility

[86] "Malesia lieventämässä pääomaliikkeiden sääntelyä", *Helsingin Sanomat*, 26 Jan 1999.

would not be a problem anymore, although side-effects such as shadow street markets for currencies might emerge.

There are, however, global and local mechanisms that might make this strategy quite unsustainable. As Tobin et. al. point out, “in today’s world of high capital mobility, even the minor exercise of policy autonomy can produce major exchange market pressures”[87]. To counteract these pressures, far-reaching regulations and restrictions might be necessary. However, credit rating agencies would immediately react against countries attempting to change course from providing a business climate judged attractive by global standards, as would the IMF.

So, constant attacks against these re-regulated currencies might occur, and certainly countries applying a high Tobin tax would face the strong sanctions and penalties of the global credit system (higher interest rates, more difficulties in getting loans, stricter conditions on loans, attempts at enforcing shock therapy programmes etc.).[88] There might also be indirect effects on the capability of these countries to form an integral part of the global economy. Under these circumstances, the more resistant governments of these countries might be drawn towards more and more nationalistic and autarkic solutions, possibly accompanied by authoritarian domestic measures (because of the need to silence the internal opposition, strongly supported from the outside). Further economic problems would follow. Etc.

Thus, it seems reasonable to expect that the price to be paid for a high, non-universal Tobin tax may be too high, particularly in the longer run. Therefore, in our judgement, this solution may not be sustainable, although there is no certainty about this.

4.2. Is the Tobin tax efficient?

Besides tax evasion, three different efficiency concerns are used as arguments against the Tobin tax. The first is the familiar idea of the orthodox economic theory: any unnecessary distortion of free markets will lead to suboptimal allocation of resources. A currency transaction tax is often seen as such a distortion. Typically, these arguments are based on claims that financial arbitrage (and therefore, also speculation) is stabilising and that

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[87] Eichengreen, Tobin & Wyplosz, op.cit., 162.

[88] For these mechanisms, see Gill 1995a, 1995b.

transaction tax would increase the cost of capital. The reasoning is derived from the neo-classical, orthodox economic theory.[89]

Secondly, and more relevantly, it has also been argued that past attempts at controlling, regulating or curbing financial markets have failed;[90] and that “since Tobin taxes do not exist in practice, there is little empirical evidence to suggest that such taxes would be effective in reducing currency fluctuations”[91].

The argument about failure confuses workability and changes: if the rules and practices are changed, it does not mean that they did not work before (according to criteria X). Rules and arrangements can be dictated, encouraged or forced to change, also by indirect means, and the reasons – whether spontaneous or not – for changing them can be false. Finally, also the criteria X for assessing them can change. Hence, it is not possible to infer from the fact that X has changed that X did not work. They are separate issues.[92]

The Tobin tax has never been tried (except close substitutes in individual countries, such as Chile or Malaysia). It is of course true that since “Tobin taxes do not exist in practice, there is little empirical evidence to suggest that such taxes would be effective”. Something that has never existed can not actually have been (empirically) tested, either. However, the issue is precisely about establishing and testing new rules, practices and arrangements. If their previous non-existence is a conclusive argument against them, certainly they will never be tested!

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[89] Like simple computer programmes, most economists repeat what they are taught to repeat: “Most economists are instinctively sceptical about taxing international financial transactions as a way to enhance the operation of the international monetary system. Union card holders are taught to prize the efficiency of the market and to regard intervention through taxation and controls as welfare reducing. They are trained to anticipate the incentive of market participants to evade taxes and circumvent administrative restrictions.” Eichengreen & Wyplosz 1996, 15. For arguments against this orthodox economic theory position, see the rest of their paper, as well as section 2.2. above.

[90] Without going into the history of capital controls and regulations, let us just mention a counter-example and point to some further evidence. Against all odds, expectations and external pressure, Malaysia’s capital controls and regulations that it reintroduced in 1998, as temporary measures, seem to have been quite successful, at least in terms of trade surplus and currency reserves. “Malesia lieventämässä pääomaliikkeiden sääntelyä”, *Helsingin Sanomat*, 26 Jan 1999. For more systematic evidence for post-1995 use of capital controls, see Eichengreen & Wyplosz, op.cit., 30.

[91] Stotsky 1996 is a representative example of all the standard arguments against the Tobin tax collected together, without any critical reflectivism whatsoever. She even claims that there is no evidence for increased volatility since the 1970’s; free markets are working beautifully. This quote is from p.2.

[92] Stotsky, ibid., does not discuss these changes in any detail. See Helleiner 1994 for a political history of the changes from Bretton Woods to global finance.

Many arguments against the efficiency of the Tobin tax seem to be quite superficial. However, there is doubt about the effectiveness of the Tobin tax, which is based on much more solid reasoning about causes for action. Corporations, and in this context the banks in particular, take into account the cost of their transactions in making their decisions. Now, the claim for the Tobin tax is that it will reduce volatility by making many currency transactions non-profitable. Huge amounts of money are transferred for the sake of winning very small margins, perhaps just one or two basis points (0.01%-0.02%). Particularly by transferring the money quickly back – or elsewhere – for another small margin, the annual yield can still be very high.

The Tobin tax will hit particularly hard these short-term transactions, for the banks have to pay the tax every time currencies are exchanged. A 0.2% tax on a round trip to another currency costs 48% a year if transacted every business day, 10% if every week, 2.4% if every month. “But it is a trivial charge on commodity trade or long-term foreign investments.”[93] Derivatives, in particular, are very sensitive to increased transactions costs. So the **Tobin tax should reduce the volume of transactions** quite considerably – the more, the higher it is – **and thereby also the volatility** of the global financial markets. Table 3 shows basic calculations about the necessary interest yields required to attract investors after the introduction of the Tobin tax.

Table 3[94]: The effect of 1% Tobin tax on short-term transaction, with a home interest rate of 10%

Investment horizon	Required foreign yield to attract investor
One year	**11%**
One month	**22%**
One week	**62%**
One day	**260%**

[93] Tobin 1996, xi.
[94] Constructed on the basis of Frankel 1996, 58.

Despite these cumulative effects, the partially valid doubt about the efficiency of the tax is that in the event of significant speculation and drastic volatility, the tax can and will do nothing. Particularly if the Tobin tax is very low, say 0.05% or 0.1%, it can hardly stop speculators who anticipate devaluation, say, at the level of 15%. Even when the tax is much higher, it is still quite impotent against major changes and outflows

Use of a Tobin Tax to Finance a Global Intervention Fund

David Woodward

The Tobin tax is often proposed to discourage speculative investments in foreign-exchange markets. This potential role is a major reason for the resurgence of interest in the idea following the Asian financial crisis. However, at the rates at which it is normally envisaged (up to about ¼ %), it would have little effect on the sort of exchange-rate speculation which characterised the Asian crisis. This was motivated by the expectation of a substantial step devaluation, which could give rise to major capital gains to speculators over a very short period. A tax of ¼ % on the initial sale of currency, and the same on its subsequent re-purchase, would not be sufficient to deter speculators who anticipated a gain of, say, 25% in a month.

Nonetheless, the Tobin tax could play a major part in the prevention of similar crises in the future, through the appropriate use of the resources it generated. These resources would be unique, in that they would be raised at the global level. They would also be very substantial. Even if the tax deterred 90% of foreign-exchange transactions not related to the real economy, it might raise something in the order of $150bn every year - enough to have financed the “rescue” packages for Korea, Indonesia, Thailand and Mexico put together.

However, simply using the resources to finance “rescue” packages as they operate at present would do little to improve the situation: it might reduce (though not eliminate) the delays in assembling such packages; but it would not prevent the crises from happening, or contribute substantially to reducing their impact. This would require a more fundamental reconsideration of the current approach to such crises.

The fundamental problem is that the mechanisms now available were designed to deal with the very different type of financial crisis, which was typical of the 1980s, e.g. in Latin America and Sub-Saharan Africa - crises which arose primarily from over-borrowing by governments. In Asia, the causes were different: the underlying pressure on the balance of payments and the exchange rate arose from private-sector liabilities, such as corporate debts, inter-bank flows, equity investments and foreign direct investment, and above all from exchange-rate speculation.

This distinction has critically important implications for the response to crises. When a 1980s-style debt crisis strikes, the impact is phased over time, according to the schedule of payments due on the government’s debts (and can be extended further if the government suspends debt-servicing). In an Asian-style crisis, much of the capital involved can leave the country almost instantaneously; and, in the

absence of capital controls, the government has no way of stemming the flow. This gives rise to a sudden and massive reversal of capital flows when the crisis strikes. Dealing with the crisis effectively therefore requires almost instantaneous action, and the immediate provision of financing on a very large scale.

The existing mechanisms have failed to achieve this. Unless the crisis is anticipated (which has not generally been the case), nothing can be done until after it has happened. Then the IMF has to design and negotiate an adjustment programme; to get approval for it from the Executive Board; and to negotiate contributions to the financing from other agencies such as the World Bank and developed-country governments (who then have to go through whatever political and bureaucratic processes of their own might be necessary) before the money can be paid. While this process has been speeding up, it can take some weeks, by which time the crisis will already have had a devastating economic, social and political impact. Even if the crisis is anticipated, there is a serious risk that the arrival of an IMF team to negotiate an adjustment programme will cause a loss of crisis, triggering the very crisis it was trying to prevent.

In addition, the principle of conditionality - that policy changes must be implemented and economic targets met before the money can be paid - further limits the effectiveness of the response. To enforce conditionality, much of the finance potentially available must be held back until the conditions have been fulfilled; and this reduces the amount, which is available at the outset, when it is most needed. Moreover, conditionality reduces the effect of the package in terms of strengthening confidence, because it means that there is no certainty as to whether the later payments will be made at all. This is quite apart from the serious questions which have been raised in many quarters about the appropriateness of the actual policies contained in recent IMF adjustment programmes in Asia.

Another consideration is the socialisation of private sector liabilities. “Rescue” packages take the form of loans to governments. As a result, what starts out as a crisis caused by the reckless borrowing and lending of, and investment by and in, the private sector, ends up with large government debts which have to be repaid by taxpayers. Moreover, by effectively bailing out foreign lenders and investors, there is a serious danger of encouraging them to behave similarly in the future, increasing the risk of future crises - the “moral hazard” problem.

For all these reasons, the current arrangements have proved inadequate to deal effectively with Asian-style financial crises. As a result, much of the damage these crises have done is arguably attributable to their retention; and the likelihood of further crises in the future may well have been increased. If such crises are to be prevented, or dealt with effectively, there needs to be a fundamental reappraisal of the whole way in which the international system responds to actual and potential crises.

The revenues generated by the Tobin tax could play a key role in this process. The main reason for the shortcomings of the current mechanisms described above is that the IMF is the only international institution mandated to deal with balance-of-payments problems. The IMF can only provide resources in response to a crisis in the form of a loan to the government, and only if the loan is subject to conditionality. The Tobin tax could provide a separate pool of resources for use in Asian-style crises, which need not be subject to the same rules.

How might this work? The primary need is not for lending to governments (which in most cases had budget surpluses or very small deficits prior to the crisis), but for support to the foreign exchange reserves, which are depleted by efforts to defend the exchange rate against speculative pressure. This suggests that, for this type of crisis, the present system of loans to governments could be replaced by a Global Intervention Fund, which would support the exchange rates of developing countries against speculative pressure, in much the same way that Central Banks defend the exchange rate (i.e. by using foreign currencies to buy local currency).

Intervention could be triggered automatically when the reserves reach a certain level (say three months of imports); and the only condition required (if any) would be an acceleration of the rate of depreciation of the exchange rate in a crawling-peg system.

This would resolve most of the problems described above. Intervention would be triggered automatically and occur more or less instantaneously, before the crisis had actually occurred. Provided the fund were large enough, this should avert the need for a devaluation - in effect, there would be an absolute guarantee of sufficient resources being provided immediately. Moreover, if the possibility of a step devaluation were thus eliminated, there would be little incentive for speculation, reducing the likelihood that intervention would be required at all. (Accelerating the rate of depreciation in a crawling-peg system would be unlikely to provide a high enough rate of return to encourage speculation - especially if there were a Tobin tax.)

At the same time, since the funds would not be lent to governments, private sector liabilities would not be socialised; and, since intervention operates to prevent devaluation, speculators who sought to precipitate the crisis would be frustrated and penalised rather than rewarded, averting the problem of moral hazard.

The use of funds for intervention rather than for lending to governments would also have financial benefits. In effect, the fund would simply be transferred continuously between currencies, according to the relative pressure on each; and it would always be earning interest (and in principle enough to off-set both inflation and any losses resulting from depreciation). This means that the value of the fund would increase continuously in real terms, even without the $150bn pa provided by the Tobin tax revenues. Once the fund had reached a sufficient size, it would be possible to use part of the subsequent revenues for other priority uses, such as debt cancellation, social development, environmental protection, etc.

Clearly, it would take some time for the fund to reach a sufficient scale to guarantee its ability to prevent crises. However, a hiatus could be avoided by an arrangement with the major developed-country governments to lend money from their own reserves into the fund, the payments on the loans (including interest at a commercial rate) being guaranteed as the first-call on the subsequent revenues of the Tobin tax.

In short, the inadequacy and inappropriateness of the present arrangements for dealing with financial crises are largely responsible for the serious damage done at every level from the poorest Indonesian household to the global economy. Alternatives are available, as are the means of paying for them; and they could easily be put into place, given sufficient political will.

of currencies based on expectation of major devaluations. In other words, when it is most needed, it cannot do its job.

However, a higher tax – at the level of 1% or more – would very likely alter the volume and structure of market in a fundamental way. The daily turnover should decline by 75-80%, and many short-term speculative and derived transactions would disappear. Furthermore, as Frankel further claims, the Tobin tax would make the markets less sensitive to changes in the speculators' expectations (political news etc.) and/or raise the relative amount of real, non-speculative investors in the financial markets. "Either way, by decreasing the role of destabilizing

speculation, the tax would, in this model, result in a lower variance in the exchange rate."[95]

So although attacks against currencies and turbulence more generally would remain possible also after the introduction of the Tobin tax, overall, the markets should be more calm and stable – and leave more space and autonomy for national decision-makers. "The Tobin tax could help to avoid the build up to crisis."[96] Naturally, the relative impotence of the Tobin tax indicates that other global measures and arrangements may be needed, too, to counteract the real economy effects of speculative runs and other instabilities.

4.3. Lack of political will: the US, the UK and the Washington consensus as the problem

There is a way, if there is a will. But is there a will? Indeed, it is difficult to organise global collective action, and powerful interests are opposing the realisation of the Tobin tax. In the global situation of the turn of the century, is it realistic to advocate the Tobin tax?

First of all, to understand the political opposition against the Tobin-tax, let us have a quick look at the re-emergence of global finance in the 1960's. This re-emergence was made possible and encouraged by intentional state actions. Yet, not all states took part in these developments towards financial liberalisation. Only two states, namely Great Britain and the United States, strongly supported the offshore markets in the early years.[97] Britain provided a physical location for these markets (London), whereas the US support was crucial, for it had the power to prevent or alter these processes:

> *US support was equally important because American banks and corporations were a dominant presence in the market in the 1960's. Although it had the power, the United States chose not to prevent them from participating in the market. In fact, by the mid-1960's, U.S. officials*

[95] Ibid., 72.
[96] Griffith-Jones 1996, 144.
[97] The term offshore was probably coined in reference to radio stations, which were quite literally "offshore": broadcasting from vessels situated just outside the territorial waters. By metaphorical extension, euromarkets, tax-havens, free trade zones, and export processing zones started to be designated as "off shores". Offshore markets are, metaphorically and regulatively – but usually not literally – outside the territory of states; yet, these non- or de-regulated spaces are created by states. See Palan 1998, 625-627, et passim.

> *were actively encouraging American banks and corporations to move their operations to the offshore London market.*[98]

Locating the market in London under the auspices of the UK government meant that it could operate free of regulation. The growth of this offshore started to put direct pressure on other states, at least in the form of making the standard capital reserve requirements decreasingly competitive. In the 1970's, the US and the UK initiated a trend towards further financial deregulation and liberalisation. They unleashed "competitive pressures that indirectly encouraged liberalization and deregulation throughout the system"[99]. In many global forums, they also supported directly the political programme of neoliberal globalisation, what was to be known as the Washington consensus. Besides the US and the UK, the main forces behind the Washington consensus have been the Bretton Woods institutions, the World Bank and the IMF (both located in Washington D.C., both close to the White House). And of course the "private sector" itself.

Now, the main ideas of this consensus have been that good economic performance requires liberalised trade, low and stable inflation, and getting prices, including currency prices, right (= at their "unique equilibrium" level). Once the government has dealt with these issues, private markets would allocate resources efficiently and generate growth.[100] In other words, deregulated, liberalised free markets allocate resources optimally, if not distorted by governments.

As a strictly global and universalist conception, it is assumed that this applies to all contexts and markets, including global financial markets. As a restatement of the orthodox economic theory, this conception has justified the reconstruction of the 1920's style global financial system.

However contingent the neoliberalising globalisation has been at times, it has meant reinforcement of the positions of London and New York in the world's financial markets. Currently, New York and London together account for almost half of world's currency transactions. They appear to have high stakes in the struggles over de- and re-regulation – and the Tobin tax. Furthermore, there have been very few signs about changes in

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[98] Helleiner, op.cit., 82.
[99] Ibid., 12.
[100] See Stiglitz 1998.

the positions of the US and the UK. Due to the major crisis and problems of the 1990's, and the emergence of Democratic and Labour Party governments in these countries, the Washington consensus might have been partially and gradually changing towards what some would call a post-Washington consensus. Yet, many of its traditional ingredients seem to have remained intact: monetarist economic policies and furthering global liberalisation and privatisation.[101]

Any given identity and interest is nothing more than frozen politics. Yet the structures sustaining that identity and related interests might be deeply sedimented and not easily changeable. More metaphorically, there might be no heat in sight to melt that frozen entity and turn it into hot politics. Perhaps external forces and historical transformations are needed to produce that heat? So although there is nothing eventual or final in the position of the US and the UK, as well as in that of the Bretton Woods institutions, the Washington consensus seems to be the major obstacle working against the realisation of the Tobin tax and other related reforms and re-regulatory measures.

The media and public sphere in the US in particular, but also to a large extent in the UK, works on the basis of *de facto* filters and systems of framing that in effect function like formal censorship. Few deviations from the (post-) Washington consensus and (softened up version of) neoliberalism based interpretations are possible. The Tobin tax, for instance, is among the practically forbidden topics. Ibrahim Warde, a professor at the University of California at Berkeley, recently checked several million media articles in the US and found that the Tobin tax had been mentioned only seven or eight times.[102] It is also noteworthy that when the US media asks for comments on the world economic crisis, it turns to investment bankers – and sometimes to mainstream, orthodox economists – for they are presumed to be the experts on the world's financial problems. In a sense, they

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[101] But there are signs of criticism, in the midst of continuing calls for further liberalisation and privatisation, cf. ibid., 19, "all too often the dogma of liberalization became an end in itself, not a means to achieving a better financial system". In fact, Stiglitz has taken side for the Tobin tax at least before joining the World Bank; see Stiglitz 1989. Remember also that Giddens op.cit., 150-151, the world-known sociologist, and adviser to the Blair government, advocates the idea of the Tobin tax. Unanticipated changes may always happen, particularly if there is already a basis for them

[102] Ibrahim Warde at the Maison de L'Amérique Latine in Paris, 25 Jan 1999, at a meeting with the public reporting the seminar of international economists on the Tobin tax, organised by the scientific committee of ATTAC.

are, but it is also clear that one should not expect anything but restatements of the orthodoxy from those sources.

This system of silencing all other, different voices is also extended to those international forums that the US dominates. The IMF and the World Bank are *sui generis*, special cases of their own, because of their central and essential position in the Washington consensus.[103] The censorship is more obvious in the case of the UN system. In the 1980's, the Reagan and Thatcher governments systematically attacked the UN system, and eventually they succeeded in making changes in favour of their ideas.[104] The end of the Cold War further consolidated these changes.

Even under these circumstances, the US has been forced to use its direct power to get its will through. Its Secretary General Boutros Boutros-Ghali was removed from office because some of his ideas – including extending the ideals of democracy to international relations[105] – did not quite fit in with the ideas and practices of the Washington consensus. In the late 1990's, and with more formal cooperation with the Bretton Woods institutions, the UN system is now totally dominated by the US, who still refuses to pay its due payments; this functions as a constant threat against any attempt at independent thinking at the UN.

It is telling that the US also suppressed an attempt in 1996 by the UNDP to circulate a volume of expert papers on the Tobin tax.[106] It is equally telling that a high-positioned, long-term UN civil servant explains in late 1998 that "nobody at the UN dares even mention the Tobin tax, particularly because of fear of the anti-UN and anti-Tobin tax sentiments in the US Congress". "But it is good that somebody raises this issue; the initiative must come from the civil society".

So it seems that there is, at the moment, a well-enforced and well-functioning, even if not unambiguous Washington-

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[103] About the World Bank and economics discourse, see George & Sabelli 1994, and Patomäki op.cit. About the IMF and its discourse of economism, see Teivainen 1995. In both cases, already the system of recruitment is a guarantee against unwanted dissidence.
[104] Livingston, 1992, has accurately analysed the Reagan administration's – eventually successful – attempt to remove North-South relations from the international agenda, not least in the UN system.
[105] More than half of Boutros-Ghali's *Agenda for Democratization* was dedicated to "democratization at the international level"; see Boutros-Ghali 1996, 25-51.
[106] Felix 1998,3.

London-New York “consensus”. This hegemonic global voice seems to be the major problem for, and the main obstacle against, materialising the Tobin tax. To a large extent, this is the substance of the lack of political will for the Tobin tax. For this reason alone, it is crucial that it is feasible to implement the Tobin tax in two phases, firstly along modified, non-universal lines. Let us next try to have a look at whom could be the actors initiating and supporting this process.

4.4. The emergence of political will: Europe or the hard-hits?

The US and the UK constitute only about 7% of the world population. Let us next suppose that also the rest of the world might have a say on the desirability of the Tobin tax and related reforms. Obviously, this is not only a matter of a struggle between countries. Large parts of the US and the UK people are excluded from the mainstream politics and society, not to speak of the global financial system; and most of these people take no part whatsoever in formulating the “consensus”. Elsewhere, there are strong social forces supporting the Washington consensus. Globalisation has restructured social spaces and power relations in the world. In fact, the Tobin tax can be also seen as a novel kind of response to the new context and its problems. As such, it may constitute a precedent case.

However, formally, and with the partial exception of the EU, sovereign states are still the decision-makers in world politics, also in systems of multilateral governance. They would also have to establish the Tobin tax regime. Hence, let us phrase the problem in this somewhat traditional way: in the world outside the US and the UK, where 93% of the world population lives, where should we expect the political will for the Tobin tax to emerge most forcefully? In particular, let us consider two, possibly complementary possibilities: the euro-core of the European Union, and the countries that have been hit particularly hard by the recent series of financial crises.

4.4.1. Will the euro-EU take the lead?

The UK is of course a member of the European Union. In a few years time, it might also join the Economic and Monetary Union.[107] That should also have repercussions on the offshore markets of the City of London, and possibly change the UK position in regard to the Tobin tax regime.

But let us start with the European Union as it is. Eleven countries form the EMU, and the euro is emerging as the second – or possibly first? – major currency of the world. On the other hand, with the possible and partial exception of the brief transition period 1999-2001, none of these eleven countries could participate in the Tobin tax regime individually. The European discussions and struggles over the Tobin tax are necessarily tied to the EU politics.

It is often acknowledged that the EMU is ambivalent to the welfare state and regulations of capitalist markets.[108] But in what sense is it ambivalent? On the one hand, it seems to institutionalise the principles of neoliberalisation and the Washington consensus in Europe. "EMU is part of this process in so far as it represents an 'internal' structural adjustment programme for Europe."[109] Yet, it can also be claimed that the EU is "not causing but [only] exacerbating the problems which the European welfare states are facing"[110]. Further, the unification created by the EMU might be necessary for empowering alternative possibilities, as many hope.[111]

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[107] There are thus many simultaneous, partially overlapping and interacting, partially contradictory or coincidental processes going on: history is contingent. Hence, despite the existence of the Washington-London-New York consensus, the UK might be drawn to the European political processes. How likely is that? Risse et.al. 1997, 110-114, argues that deep British beliefs about national identity as something in contrast to Europe, sovereignty, and sterling as a symbol of sovereignty will tend prevent the UK from joining the EMU; whereas Diez, 1998, claims that the official British discourse has always been less separatist and more in line with the European Commission visions of Europe than usually thought. After the Labour Party assumed office in 1997, the Bank of England was granted the right to determine interest rates, that is more autonomy along the lines of *Bundesbank*. This could be taken as a sign to prepare the UK for membership. Further, since the euro was launched on 1 January 1999, there has been a lot of discussion in the UK whether the UK should, after all, join in. See, for instance, "The UK warms to the euro. First poll since launch shows record support", *The Guardian*, 11 February 1999. However, most of these kinds of analyses fail to address the implications of the EMU to the City of London and its offshore position – and the extent to which the City of London takes part in constituting British interests.

[108] See for instance Leander & Guzzini 1997.

[109] Gill 1997, 209.

[110] Leander & Guzzini, op.cit., 160.

[111] For different articulations, see Hettne 1993, and Martin & Schumann, op.cit.

Does the EMU work similarly in the context of establishing the global Tobin tax regime? That is, it is deepening the power of monetarism and neoliberalism in Europe, but also unifying Europe and creating potential for new, more democratic and socially responsible arrangements for global politics? Certainly, there has been more discussion about, and support for the Tobin tax in Europe than in the US. Indeed, many European political actors have favoured the idea, also in the crucial Germany-France axis.[112] Moreover, most European countries have not initiated the liberalisation of capital movements, but rather their governments have often felt compelled to liberalise, even against their original intentions and will. In many cases, alternatives have been actively searched for. The Europeans are also much more used to taxing financial transactions, added value and related items. All in all, there seems to be a background and preparedness to do something about the volatile, over-expanded and crisis-ridden global financial markets.

In this light, consider the Article 73b of the Treaty of the European Union (the Maastricht Treaty). This article seems to make illegal all attempts at regulating global financial markets:

> *1. Within the framework of the provisions set out in this Chapter, all restrictions on the movement of capital between Member States and between Member States and third countries shall be prohibited.*
> *2. Within the framework of the provisions set out in this Chapter, all restrictions on payments between Member States and between Member States and third countries shall be prohibited.*[113]

The Maastricht Treaty takes a strong stand for the freely floating and convertible exchange rate regime and the global, unregulated financial markets. In a sense, it even constitutionalises these

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[112] For years, there have been struggles over getting the Tobin tax on the agenda of the EU. The European Parliament has accepted resolutions mentioning the currency transactions tax at least in 1996 (on Halifax world economic summit, 13 May) and 1997 (on employment, 13 November 1997). However, according to Joachim Denkinger, Economic Adviser of the Green Group in the European Parliament, “the European Union has in recent years shrank back from clearly favouring the Tobin Tax as a means to fight currency volatility (in particular for weaker economies) or to create a worldwide tax base to finance development projects. In a document which the French government (to be considered as the most *progressiste* on the subject in the whole EU) submitted to the informal Council in Vienna (Sept. 98) any reference to the Tobin tax is avoided - only a *clause de sauvegarde financière* in
collaboration with the IMF is mentioned.” E-mail message, via MEP Heidi Hautala, on 19 February 1999. See also section 2.2.

[113] Treaty of the European Union, Article 73b.

principles; the Maastricht Treaty is more difficult to amend than any existing constitution, for any amendment requires unanimity of states. Does this mean that the EU cannot take any initiative towards establishing the Tobin tax before changing the Maastricht Treaty first?

At the time when the Treaty of the European Union was concluded, all the member states were – and still are – committed to Article VI of the Agreement on International Monetary Fund. Section 3 of Article VI ("Controls of capital transfers") states that "members may exercise such controls as are necessary to regulate international capital movements"[114]. The US has been campaigning against this Article[115], and it seems that the EU countries have voluntarily abandoned this right by a collective, quasi-constitutional agreement.

This is not the end of the story, however. The Treaty of the European Union can of course be revised. In our opinion, ultimately this may well turn out to be necessary, but it would take years and may be too long and contingent a process to form a basis for the first phase of the Tobin tax regime. In the shorter run, it is more relevant that it is not necessary that a small, market-friendly transaction tax should be counted as a "restriction" to capital movements. Moreover, Article 73c of the TEU seems to open up exactly this possibility:

> *Whilst endeavouring to achieve the objective of free movement of capital between Member States and third countries to the greatest extent possible and without prejudice to the other Chapters of this Treaty, the Council may, acting by a qualified majority on a proposal from the Commission, adopt measures on the movement of capital to or from third countries involving direct investment - including investment in real estate -, establishment, the provision of financial services or the admission of securities to capital markets.*

The measures needed for the first phase of the Tobin tax regime would seem to fall within this category. In the case of more serious difficulties, it might be possible to go even further without violating the TEU, for the Article 73f enables the Union to take "safeguard measures with regard to third countries for a period not exceeding six months", if, "under exceptional circumstances, movements of capital to or from third countries cause, or threaten

[114] Articles of Agreement of the International Monetary Fund, Article VI, Section 3.
[115] Felix op.cit., 3.

to cause, serious difficulties for the operation of economic and monetary union". Arguably, this is constantly the case with the present global financial system.

In sum, there is nothing in the TEU that would prevent the EU from adopting measures necessary for the first phase of the Tobin tax regime. Even though current interpretations and practices make the TEU support neoliberalist practices and monetarist economic policies, there is also room for alternatives. Even though the TEU may prohibit constant, normal restrictive regulations and capital controls – it is not impossible that some of those might be needed in the longer run to back up the Tobin tax regime – the European Union is indeed Janus-faced and may be put to service of various ideas. Thus, even if the TEU should perhaps be changed, there are already enough degrees of freedom for initiating the Tobin tax regime by the Europeans.

4.4.2. Could the progressivists and the hard-hits initiate the first phase?

Perhaps the strict monetarist vision will prevail in the EU for the time being, and the opposition against the Tobin tax will be too strong for any initiative by the Commission and qualified majority decision-making in the Council to be politically possible. Or perhaps the EU will just be slow in organising any collective action in this regard, while others would like to move forward more quickly. Let us therefore also consider the possibility that the countries hit hard by the 1997-1999 world economic crisis would be interested to hurry up, perhaps following an initiative made by Northern states most likely to actively endorse and advocate the idea.

Firstly, there are countries such as Indonesia, Malaysia, South-Korea, Thailand, Russia, and Brazil that are in deep trouble mainly due to this crisis, both economically and politically. Perhaps we should add Mexico to this list, for it is still bearing the consequences of the 1994-95 crisis, and is threatened by the most recent developments as well. Secondly, there are other states either already experiencing serious problems or immediately threatened by the world economic situation, from Japan, India, China and Hong Kong to many Latin American countries, such as Argentina, Paraguay and Uruguay. And finally, there are those Asian, CIS, Middle Eastern, African and Latin American countries

that are facing almost endless deep economic decline, social implosion, and all too often, political violence. Also some of these countries might see a lot of potential in the Tobin tax – not least because of its revenue potential.

By no means do these countries form a politically coherent group. Japan stands as the second largest national economy in the world, despite recent trouble and negative growth, and has tended to follow the lead of the US, even if at times rather hesitantly. Some less well-off have chosen, with the firm support and pressure from the US, the IMF and USAmerican global media, the recipe of more orthodox measures and obedience to the (post-)Washington consensus; they are led by social forces still believing in the blessedness of neoliberalist globalisation.

Others have decided for, or at least seriously been debating, more nationalistic measures to control capital movements and gain some space for autonomous economic policy more generally. In the cases of Malaysia and Russia, for instance, anti-Western social forces have already influenced the political agenda, albeit in different ways (in Malaysia, economic policy and human rights; in Russia, security policy).

Some countries which are in deep, constant decline are not integrated to the capitalist world-economy for political reasons (in some cases, they are systematically boycotted and excluded); others are totally marginalised in –and even from – it because of political economy processes. There are also major cultural and political cleavages within this rather artificial grouping.

The idea of the Tobin tax might well make a difference in the politics of globalisation. The strict opposition between nationalist and pro-globalisation forces might erode, and new alignments might emerge. Be that as it may, if the first phase of the Tobin tax regime were to be based on the would-be support of the hard-hits, somebody has to take the diplomatic initiative. This initiative must be taken quite independently of any established framework of co-operation.

The Nordic countries, Canada, Australia and New Zealand could well assume this role, for they have the economic resources, technical capabilities and the diplomatic credibility for doing so.[116] Mostly, domestic support for the proposal is already

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[116] It might be objected that this is a very Northern perspective. That is quite correct, but to our knowledge most discussions about the Tobin tax have been in the North (with the important exception of the ul Haq-led UNDP-project), and that might be indicative of the

quite strong, and particularly in the case of the Nordic countries, there is a quest for a new, post-globalisation and post-Cold War identity defined in terms of socially and democratically progressivist ideals[117].

The problem with the idea of spontaneous Nordic action is that they all are, except Norway and Iceland, members of the EU. Since 1999, Finland already participates in the EMU and Sweden may well join in at some point soon as well[118]. Does this limit their room of manoeuvre? In our assessment, it could well be possible for Sweden, Norway and Denmark, perhaps in co-operation with Canada, Australia, New Zealand and/or some other countries, to take the initiative to establish the first phase of the Tobin tax regime. In the transition phase from *markka* to *euro*, Finland could actively support this and participate with its disappearing *markka*, although this would be more or less symbolic (*euro* is already the *de facto* currency for many transactions, and by the time the agreement would enter into force, the Finnish *markka* would not exist anymore).

4.4.3. First steps to be taken

The EU or the other countries taking the initiative – perhaps eventually with the EU – should proceed as follows. First, they should establish an open agreement on the Tobin tax that any state can join at any time. This agreement should define the basic principles and introduce a democratically representative supranational body[119] – perhaps an interim body only, before the responsibilities are handed over to a truly global organisation such as the would-be economic Security Council of the United Nations or a reconstructed ECOSOC[120] – orchestrating the tax, the allowed exchange rate variations, and collecting the revenues.

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motivation and resources for making the initiative. However, we hope we are wrong, and it may well be that these Northern states are not needed for taking the lead in the beginning.

[117] See Patomäki 1999b.

[118] In January 1999, for the first time opinion polls in Sweden show that a majority of Swedes seemed to be in favour of joining the EMU, and the Prime Minister Göran Persson is scheduling a referendum on the issue for late 2000. See “Ruotsi haluaa Emuun kruunun alennusmyynnillä”, *Taloussanomat*, 27 Jan 1999.

[119] The principles of democratic representation in world politics are discussed in Chapter 5.

[120] One possibility is that the administrative and other functions of the body would continue, but its decision-making and accountability should be transferred and subordinated to the economic Security Council or the ECOSOC of the United Nations.

The proposed first phase tax includes the following elements: (i) small underlying transactions tax (a few basis points); (ii) much bigger exchange surcharge; and (iii) a relatively high tax on domestic-currency lending to non-residents not yet within the tax regime.

Secondly, the participating states should work actively – and in concert with non-governmental political actors and movements[121] – aiming to get as many countries to join in as possible already before the taxation is actually implemented for the first time, say, in August 2001 or March 2002. Finally, soon after the tax has been implemented for the first time – not before, since the idea is to guarantee as wide a representation as possible – participants should decide the first tentative principles concerning the allocation of revenues.

4.5. Conclusion

There is a way, and a will may be emerging as well. In this chapter we argued firstly that, as far as the problem of tax evasion is concerned, four cases have to be distinguished. A low, universal tax does not pose any major problems. A higher, universal tax may require more administrative efforts, but is enforceable as well. It is a crucial part of our argument that also a non-universal, relatively low and modified Tobin tax is feasible. This makes it politically possible to initiate the process of establishing a universal, uniform currency transaction tax without the consent of every state, including the US and the UK. Once started, the process should be self-reinforcing in a number of ways: it penalises outsiders; it stabilises insiders' exchange rates; and justifies the right to participation in deciding on the allocation of the revenues. Soon the outsiders should find themselves quite isolated.

In this chapter we have also argued that the Tobin tax is, relatively speaking, efficient. It cannot – and is not intended to – prevent every speculative wave and all ungrounded volatility. But

[121] Burbach et.al. 1997, 21-33, are quite right in saying that the "discontents of globalisation", challenging some of its tenets, are often NGOs and political movements, or sometimes merely disorganised groupings or "underclass linked to crime and violence", rather than political parties aiming at state power. These forces are heterogeneous and often disorganized, and they lack a coherent political ideology. But many of them may well find the Tobin tax an idea worth supportive political actions.

particularly a higher, universal Tobin tax cuts the edges from the global financial markets quite effectively; particularly the most volatile short-term transactions and more complicated derivatives will be curbed quite drastically.

In fact, the lack of political will for the Tobin tax comes down to the special position of the US and the UK in the global financial system, and to the related hegemony of the orthodox economic theory (the Washington “consensus”). Thus, we have also investigated whether it would be politically possible to establish the Tobin tax regime without the US and the UK. And our response is that, yes, it is possible. Either the EU will (or should) take the initiative, or a grouping of the progressivists – the Nordic countries, Canada, Australia, the New Zealand – with the hard-hits of the latest round of the world financial crises. Or perhaps the hard-hits could start it alone. In any case, the first steps to be taken are: to establish the first phase of the Tobin tax regime; to assist in local, national and global struggles over the idea; and to decide about the legitimation and operative principles of the supranational body, including principles for how the revenues should be distributed.

5. Global political issues of the Tobin tax

To conclude our study, we shall tackle a number of unavoidable **global political issues**. Firstly, would sovereign states – or, more deeply, the institution of state sovereignty – allow for the development of an international and global system of taxation? It is true that sovereign states have had monopoly over taxation. Also in the case of the Tobin tax, the states would collect the tax, although in concert with, and under the surveillance of, the supranational body. Obviously, a global system of surveillance and governance is needed, but, as a matter of principle, that will not be different from any of the already existing – or planned – systems of global governance in trade, finance and property rights. In fact, all these regimes, as well as global financial markets, have acquired many properties associated with 'sovereignty'.

There are many ways in which the Tobin tax regime defends sovereign states against the released, and now apparently rampant, transnational forces. However, the best way for most states – and many other political actors as well – to regain control over the transnational forces and flows is to organise collective actions. The Tobin tax regime represents an attempt at such a collective action. But this raises the whole problematic of political theory into a global context: what are the principles of legitimation of collective organisations? How should they be assessed in terms of material benefits and their distribution, rightful authority, justice and democracy? In fact, already the acknowledgement of the power of transnational forces, structures of governance and flows points to the need to discuss these normative fundamentals of politics also in the global context.

Tobin and many of his followers have assumed that the tasks of orchestrating the tax should be given to the IMF; it would also have a role in allocating the revenues, even if it is not, in principle, necessary that it should get any of the revenues for its own purposes. In the following, we shall make an argument for **not** giving the IMF – or the World Bank – this role, and for **not** subordinating the proposed Tobin Tax Organisation to the Bretton Woods institutions.

In short: 1. The two-phase scheme of establishing the Tobin tax regime makes the rationale for Tobin's original proposal disappear (furthermore, the first-phase non-universal tax regime is incompatible with the IMF structure); 2. The Bretton Woods institutions have no specific expertise in international taxation (in fact, they have typically opposed the idea); 3. The economic policies that the IMF has imposed upon countries have contributed to the recent economic crises, and, for the time being, the IMF seems to lack legitimacy for governing the Tobin tax (as acknowledged also by the G7 governments); 4. The fact that the principles of governance of the IMF are by no means democratic contributes to these legitimation problems; and 5. There is a more general and permanent need to pluralise governance structures and open up new democratic possibilities in global governance.

In the first phase of establishing the Tobin tax regime, a new supranational body orchestrating the tax must be founded. Let us call it the Tobin tax organisation, TTO. The TTO should be independent from any existing organisational structure. Given that it will also have a role in collecting and allocating the revenues, the question is: how can we guarantee fair democratic representation in its agenda-setting and decision-making and establish the possibility of accountable, transparent and just outcomes of its proceedings?

When the time for the transition to the second phase approaches, the fate of the TTO has to be decided. Should it remain independent or rather merged with more general systems of governance? We argue that the United Nations has a lot of potential in this regard. But it has to be reformed first. To facilitate these reforms – which should both empower and democratise the UN system, and also prepare it for the second phase of the Tobin tax regime – it will be suggested that the TTO should allocate a share of its revenues to the UN system. Regarding the substance of the UN reforms, we will discuss the proposal of the Commission on Global Governance to establish an economic Security Council; and that of the South Centre to reconstruct the Economic and Social Council, of the UN. Either one could take over the TTO in the second phase.

5.1. Sovereign states and global taxation

The developments of capitalist money economy, modern bureaucracy and sovereign nation-states enabled modern forms of taxation.[122] In the Europe of the 17th and 18th century, taxation became fiscal in the proper sense of the term, for a recognised public domain of finance and expenditure emerged. Moreover, a separate and autonomous field of economy – supposedly following its own laws – was constructed, and constituted by private ownership. Naturally, taxation was the way to underwrite the state's expenses by drawing revenues from the field of economy. However, as Giddens correctly observes, with modernisation,

> *[...] taxation also becomes closely bound up with the surveillance operations of the state. Tax policies come to be used both to monitor and to regulate the distribution and the activities of the population, and participate in the burgeoning of surveillance operations as a whole. Taxes, it has been said, 'are used as tools to increase population (tax burden on bachelors; tax reduction for children), to reduce laziness and to force people to work, to check certain human vices, to influence consumption patterns (particularly conspicuous consumption) and so forth. The education or social goals of such taxes characteristically prevail over the fiscal goals.'"*[123]

There are in fact three noteworthy developments here. Firstly, since state sovereignty was taken to imply **exclusive control** (analogical to ownership) over a territory, modern states have also come to assume monopoly over taxation within their territory. The US government cannot impose a tax on the Japanese, European or even Nicaraguan individuals or firms, however much it would like to, unless they operate within its territory. Secondly, the *de facto* **revenues** of the states have been dependent on taxation, and we may assume that they are jealously guarding their rights in this regard. Finally, taxation has been associated with the **governance of society**, for it has been used to achieving moral and socio-political purposes. Since the development of parliamentarism (late 17th century) and the advent of the notion of people's sovereignty (late 18th century), more democratic procedures for determining these purposes have been established. Finally, the 20th century welfare state

[122] See Weber 1978/1922.
[123] Giddens 1985, 157.

emerged with new ways of spending the revenues on social, egalitarian and democratic purposes.

Taxation is thus a deeply political issue, which cuts across a number of issues: state sovereignty, surveillance, governance and democracy. Is this a problem for the Tobin tax? At the outset, a currency transactions tax appears to be global, and it also creates global revenues, likely to be used for global purposes. Yet, states continue to be sovereign, having, at least in principle, exclusive control over defining their own purposes, and setting the level, means and targets of taxation therein. Is there not a contradiction here?

Firstly, at the turn of the 20th and 21st century, there are good reasons to call into question the supposed monopoly of sovereignty by the state. The idea that sovereignty must be located within the state, in a hierarchical and exclusive manner, was based on certain practical, normative and logical presuppositions, which are now quite outmoded.[124] It is more and more common to acknowledge that many social relations defy any strict and exclusive notion of territorial sovereignty. Importantly, the global financial markets seem to have assumed new forms of agency, autonomy and control over external actors. Latham describes how the re-emergence of the global financial markets and the innovation of new financial instruments (derivatives in particular) in the currency markets opened up a new form of agency for banks and corporations:

> *[...] one of the key elements of the new financial markets is the fluid convertibility of capital. [...] These engines empower participants, but leave clear lines between insiders and outsiders. It also keeps states out via boundaries that emerge from new and evasive practices that are not subject to the reach of the state (e.g. offshore operations). What financial systems and states share is social sovereignty [...].*[125]

Globalisation, not least the globalisation of financial markets, have created and empowered new actors and given rise to new structures. For Latham and many others, these new social

[124] Certain assumptions about the nature of persons, states, legal rules and (deontological) logic (in particular, the requirements of asymmetry, irreflexivity and transitivity), led necessarily to the question as to who/what body is the one that is not tied by any norms but binds other norms; and this agent or body must be territorially somewhere (inside the state). See Patomäki 1992, 84.

[125] Latham (forthcoming).

structures – originally created by some states – appear to be as sovereign and exclusive as states, but non-territorial.[126] These structures are "sovereign" in a sense that they empower actors to operate in autonomous spaces that they have constituted; yet the consequences of these actions forcefully condition actors outside this sphere, not least states. "In today's world of high capital mobility, even the minor exercise of political autonomy can produce major exchange market pressures."[127] Thus, often governments of sovereign states seem to be more forcefully and immediately accountable to these markets than to their parliaments. Where is sovereignty?

From this angle, the Tobin tax can also be read as an **attempt to resurrect aspects of the sovereign power of the state**. As we remember, one of the aims of Tobin's original proposal was indeed to create more space for the autonomy of the nation-state (for their economic policies). It may turn out that the increase in autonomy might in practice turn out to be only modest, depending on the circumstances[128], yet it seems that in the politics of globalisation the Tobin tax regime is, first and foremost, on the side of the sovereign states.

Moreover, the collection of the tax would be carried out at the booking site, on a national basis, and only national authorities can do this. Furthermore, since the implementation of the tax must be resulting from an international agreement, "participating

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[126] A lot of confusion arises from conflating different meanings of 'sovereignty' (there are a multiplicity of moral/juridical in contrast to sociological conceptions of sovereignty; and state sovereignty, in particular, has had internal and external aspects). Cf. Palan, op.cit., 630, who sees offshores "as radical redrawing of [state] sovereignty", not as its erosion.

A modern sovereign is the legal system that defines all the competencies and rules for changing or creating rules; it empowers and constrains. Now, if state A creates, by legislative acts, an offshore for banks and firms based in countries other than A, run by non-A-citizens, it empowers those banks and firms by providing them new opportunities, and constrains other states by making them to loose some of their controls – in the form of regulation and taxation – over those firms. At some point, quantity turns into quality, and suddenly the offshore spaces and related global markets appear as sovereign, instead of states, at least for most states (relations of domination between states still remain as an aspect of these complex realities; witness the relative power of the US in most contexts of multilateral arrangements). The best way for most states in most contexts – and to many other political actors as well – to regain control over these forces is to organise collective actions. The Tobin tax regime represents an attempt at such a collective action.

[127] Eichengreen, Tobin & Wyplosz, op.cit., 162.

[128] In normal conditions, it would create more space against the volatility based on political news etc. But the Tobin tax alone cannot give any guarantees against such crisis as those of 1992-93, 1994-95, and 1997-99, although it can prevent the build up of these crises. See Kaul, Grunberg & ul Haq op.cit., 6.

can be a decision of only sovereign governments"[129]. Although an international body is needed to set the rate of taxation, define taxable transactions, determine exemptions from the tax and undertake monitoring and auditing tasks, as well as collect the revenues from national authorities, the ultimate control and practical implementation would still be at the hands of governments.

This sounds familiar. Although the rules, principles and decisions of international regimes are in practice quite conclusive, it is typically presumed that at least in the last instance, states remain sovereign, thus free to do what they want. Of course, they are free to try to act otherwise, but they have to bear the consequences. Globalisation, and the emergence of offshores, non-territorial spaces, and the mobility of banks and firms, have evoked fears about the reactions of economic actors to any attempt at acting differently from the standard: neoliberalisation. These fears may sometimes be grossly exaggerated, yet many states have faced powerful constraints against spontaneous actions.[130]

Some of the constraints are direct and intentional. Systems of regional and global governance do back up their rules and principles with sanctions. Beside the direct, violence- and security-oriented methods of power (crisis management with the help of armed forces, power-balancing policies, alliance-formation, great power management of collective security etc.), a variety of more sophisticated methods based on surveillance have emerged, data-collection, and supervision. The aim of these methods is always to influence the strategic calculations and cost-benefit-analyses of states by making them visible from a certain perspective.

There are also so called decentralised sanctions, resulting from non-centralised sanctions by few or many, which are about the legitimacy of states. One has to live in accordance with the established rules, norms and practices in order to preserve the highly valued relations. Repeated violations of the rules can lead to tit-for-tat responses, delegitimation and, eventually, to exclusion, either contextually or globally.[131]

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[129] Ibid., 1996, 9.

[130] For a well-known articulation of some of these constraints, see Gill & Law 1993.

[131] For a more complete analysis of these power relations, see Patomäki 1999c.

It is idealism, in the bad sense of the term, to deny the reality of power relations in the world, and to continue to represent the state sovereignty as something actually existing and, in most instances, *de facto*, and always *de jure* inviolable; or as the exclusive, universal normative ideal all should aspire for, no matter what.[132] Hence, although the autonomy of economic policies of states is an important goal, and although sovereign states should also be defended and developed otherwise, complementary political responses to globalisation are needed, too.

From this perspective, we can fully recognise that the Tobin tax regime – as the first global tax regime – would also have deep political implications vis-à-vis authority, surveillance, governance and democracy. Like the IMF and the WTO now, or the planned Multilateral Agreement for Investments, MAI, the body that implements and looks after the Tobin tax must be empowered with surveillance capabilities and sanctions. Moreover, in itself, the tax constitutes a form of social control and regulation. The revenues it creates can be used for **social purposes that must be determined globally**. It thereby revives also the problems of authority, justice and democracy in a new, global context.

5.2. The role of the International Monetary Fund

Tobin assumed in the 1970's that the IMF would orchestrate the tax and that "the tax proceeds could be appropriately paid into the IMF or World Bank".[133] But why did Tobin make this assumption? Apparently, because the tasks of the IMF are perhaps closer to collecting a global tax than the tasks of any other international organisation; and because the World Bank is the other major, global financial institution. But the implicit idea seems to have been to use the IMF as a leverage to enforce a universal regime. Stephanie Griffith-Jones explicates this idea as follows:

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[132] In fact, it has **always** been idealism to represent state sovereignty in this way: it has been a contradictory and counterfactual ideal rather than a blunt description of political realities. Globalisation – in the context of many cultural changes – has only made this more obvious and visible. For different accounts, see Held 1995,73-140; Walker 1993.

[133] Tobin 1978, 159.

> *[...] rules [for the Tobin tax regime] could be established by an international organization, such as the IMF. Indeed, if there was sufficient agreement among the major member countries, it would be possible to amend the IMF Articles of Agreement so that all countries would have to impose a Tobin tax – as Tobin himself suggested.*[134]

But Griffith-Jones goes on to point out that "changing the IMF's Articles is a major exercise", and does not think that it is a good idea to try to implement the tax regime this way.[135]

In fact, the idea of establishing the Tobin tax in two phases makes the idea of using the IMF as a leverage quite unnecessary. In the first phase of our proposal, there is simply no need for the IMF. Moreover, from the point of participants of the Tobin tax regime, the IMF would be likely to be controlled by a management not accepting the rationale for the tax and countries not (yet) belonging to the Tobin tax regime. It does not sound reasonable to incorporate this kind of non-universal system of taxation under the auspices of the IMF.

The real question is whether the TTO should be subordinated to the IMF in the second phase. We will make an argument that it should not. First of all, the IMF does not have the required expertise in international taxation; in fact, it has often been sceptical and critical about the ease of implementation, or more generally, about the idea as such.[136] Secondly, and more importantly, it seems more and more clear to so many actors that the IMF policies have actually contributed to the recent economic crises. Thus the IMF seems to be lacking legitimacy for taking over the TTO.

At present, there is a vivid transnational and international discussion about the need to reform the IMF. However, it remains to be seen whether the IMF will be reformed, and if yes, whether anything more fundamental will change. The direction of the reform proposals is clear, however. Firstly, there is a recognised need to do something about the volatility and rampant nature of the global financial markets. Secondly, the Bretton Woods institutions themselves are understood to lack transparency, accountability and legitimacy – and to be in need of a reform.

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[134] Griffith-Jones, op.cit., 149.
[135] Ibid., 149.
[136] See ibid., 151.

Indeed, in 1998-99, there have been various calls for a new Bretton Woods conference and/or for restructuring the existing Bretton Woods institutions. The French leaders proposed an idea of a new founding conference, "Bretton Woods two". Germany's new Prime Minister Gerhard Schroeder, who endorsed "placing greater controls on international capital and restructuring the global financial system", backed the proposal of the French leaders.[137] However, very few details of these proposals have been revealed —if, indeed, there are any.

Prime Minister Tony Blair and Gordon Brown, Chancellor of Exchequer of the UK, have emphasised that if left intact and uncoordinated, the international financial institutions (the IMF, the World Bank) will be insufficient to prevent future international crisis. They propose not only more co-ordination between the institutions but also a "code of conduct" for the states, a "code of transparency" and new standards for the corporations, and even a "new global regulator".[138] In fact, the substance of these codes, standards and regulations seem to imply further reinforcement of the Washington consensus.[139]

The other set of top-down demands concerns more public accountability and wider participation in international forums and organisations. Wider participation by whom? The answer is, in principle at least: both by states and citizens. The US decided to convene an ad hoc group of 22 "systematically significant economies" to ponder financial reform. Also here, what is noteworthy is the "absence of substantive discussion and the

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[137] "Germany's Schroeder Backs Controls", *The Wall Street Journal*, 1 Oct 1998.

[138] "UK: Monitoring of Global Finance Proposed", *Financial Times*, 1 Oct 1998.

[139] Gordon Brown's explanation of the crisis seems to indicate that most reforms are needed within the states suffering from a crisis (mostly, they are to blame for the crisis): "The current financial crisis originated in national economic policy mistakes in Asia and a destabilising lack of transparency. It grew because of their poorly regulated and often distorted financial sectors. It became global because of insufficient supervision and ineffective risk management in the developed country financial markets. It became a crisis because the initial policy responses were more appropriate to over-extended public sectors whereas the problem was over-exposed private investors. And it has become a human tragedy affecting millions because our social policy approach is still deficient."

Indeed, Gordon's conclusion is telling: "The key challenge is to devise new international rules of the game that, by boosting credibility and investor confidence, help deliver stability and prosperity. Our task is not to weaken support for the IMF and World Bank at a time when the need for surveillance and coordination across the world is more pressing, but to strengthen them by building the operational rules and architecture for the new global financial system." Statement by the Hon. Gordon Brown, Governor of the Fund and Alternate Governor of the Bank for the United Kingdom, at the Joint Annual Discussion of the IMF, can be found at http://www.imf.org/EXTERNAL/AM/1998/ speeches/PR54GBE.pdf.

excessive influence of the IMF management" – as well as underrepresentation of the emerging markets.[140] Yet, this initiative indicates the need to gain legitimacy by making more actors being involved in discussions and, in a more limited way, in agenda-setting (not in decision-making, though).

In his opening speech to the IMF 1998 Annual Meeting, President Bill Clinton made a further gesture towards this direction by arguing that even "the best designed international economic system will fail if it does not give a stake and voice to ordinary citizens". He went on to point out that there is a need to "encourage democratic participation in international organisations".[141]

However, Clinton also makes it clear in his speech that the reason for these initiatives and gestures is the fear that countries may increasingly start to close markets and turn away from neoliberalisation, because of the series of economic crises:

> *Unless the citizens of each nation feel they have a stake in their economy they will resist reforms necessary for recovery. Unless they feel empowered with the tools to master economic change, they will feel the strong temptation to turn inward, to close off their economies to the world. Now, more than ever, that would be a grave mistake. At a moment of financial crisis, a natural inclination is to close borders and retreat behind walls of protectionism. [...] The world economy today needs more trade and more activity of all kinds, not less. That is why when the leaders of APEC meet next month, we must press forward to tear down barriers and liberalise [...].*[142]

The promise is thus that there will be further neoliberalist reforms. Clinton urges governments to "hold fast to policies that are sound and attuned to the realities of the international market place", and endorses support to "the fundamental approach of the IMF". The logic is clear: wider participation is needed for legitimation purposes, but there is no intention to open up neoliberalist policies to democratic politics.

Yet, the Western governments are quite right in addressing the issues of regulation and democratic participation. For good reasons, there is a legitimation problem, and something should

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[140] "Bretton Woods Revisited", *Financial Times*, 21 Dec 1998.
[141] "Remarks by the President to Opening Ceremony of the 1998 International Monetary Fund/World Bank Annual Meeting", The White House Press Release, 6 Oct 1998.
[142] Ibid.

be done. The Bretton Woods institutions seem to have been partially responsible for the economic crisis and thereby of this legitimation problem (if not crisis) of global governance. What is the connection? It seems that once the economic policies of the IMF, in particular, are too obviously unsuccessful, also the principles of governance are called into question. As the founding father of the notion of economic “shock therapy”, Jeffrey Sachs, puts is bluntly, with great hindsight:

> *The International Monetary Fund is currently scoring five out of five – five big rescue packages since mid-1997, and five big failures. [...] The Brazil debacle follows IMF failures in Thailand (August 1997), Indonesia (November 1997), Korea (December 1997), and Russia (August 1998). [...] The IMF is working with the wrong economic model of the world. And as long as it continues to do so, and to remain protected by a hapless G7 that refuses to call the institution to task for its failures, the rest of the world will continue to wake up to financial shocks that undermine living standards in developing countries and that threaten global stability.*[143]

We agree. Furthermore, neither the IMF nor the World Bank are democratic in any measure. They are governed in accordance with orthodox economic theory, and the hegemony of this (false) world-interpretation is materially backed up by the undemocratic principle “one dollar, one vote”. In other words, the governance of the Bretton Woods institutions is based on the unjustified and undemocratic domination of a few Western governments. In none of the top-down reform proposals is there even a hint that this might be seen as a problem.

There is an alternative. Whatever the alignment of countries that will constitute the founding group of the Tobin tax regime, they can start to build a more democratic and socially responsible system of governance on their own. They can do this without compromising the ideas of international cooperation and global responsibilities or without giving up the idea of global free trade. As devised below, the governance principles of the TTO will be more democratic than those of the IMF and the World Bank. The TTO has potential to become an exemplar in the future; the IMF and the World Bank may well represent the past, for they are

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[143] Sachs 1999.

institutions that were created 55 years ago, in the course of the World War II, basically by two countries alone, the US and the UK.

5.3. The Tobin tax organisation (TTO)

Let us continue to assume that the only politically realistic way of establishing the Tobin tax is a two-phase scheme. In the first phase, a new international organisation is needed to set the rate of taxation, define taxable transactions, determine exemptions from the tax and undertake monitoring and auditing tasks, as well as to collect the revenues from national authorities. [144] These are the tasks of the Tobin tax organisation, TTO. The initiators and the first participants will install the TTO and lay down its basic principles. These should include the following:

- Deciding the location of its headquarters (preferably, in the capital of one of the initiators and/or first participants).
- Defining the exact levels of first phase taxes (basic tax, surcharge, and the domestic lending tax).
- Determining the structure and decision-making rules of the TTO (e.g. qualified majority decision-making in the Council of Ministers, with motion-setting rights as well as some budgetary controls and veto-powers to a body representing democratic parliaments and civil society).
- Determining whether there should be any exemption from the tax (preferably none in the beginning).
- Setting the basic methods of surveillance and countering tax evasion, and creating the corresponding administrative functions (this part of the TTO needs to be rapid and relatively autonomous in its actions, even if always 100% accountable; changes in electronic codes and routines of the banks as well as national laws about book-keeping might be needed as well, for it has to be

[144] Considering only the possibility of a universal and uniform tax, Griffith-Jonesop cit., 150-151, argues that it would be useful to complement the operation of an already existing institution (either the IMF, the World Bank or the BIS) "with a small, autonomous intergovernmental global tax commission, in which, for example, proposals for distributing the tax proceeds would be made and discussed. This commission could be established in the context of the UN, but it may need to evoke weighted majority voting… ". In the two-phase scheme, there is no good reason for connections to already existing institutions.

made sure that booking operations are not transferred to tax-free centres).

- Deciding about the support for those members who have difficulties in implementing the rules, and sanctions against those members who turn out not to follow the rules of the regime.

The national authorities will collect the revenues, and transfer them, in accordance with agreed principles, to the TTO. Immediately after the first phase has started, there should be a meeting of the Council of Ministers and the body representing parliaments and civil society where the first, tentative principles and rules of allocating the revenues should be defined.

Two ethico-political issues of organising the TTO are particularly important and delicate. First concerns the structure and decision-making rules. The second is about the allocation of resources. **Democracy** should play a major role in deliberations about the first, while **social justice** seems to be a more important consideration in the latter. But these are interrelated. Let us discuss them in some more detail.

Like other systems of regional and global governance, the TTO will contribute to diversifying the forces and agencies governing the world of the turn of the 20th and 21st century. But, as already pointed out, this trend poses problem to any understanding of democracy. At the heart of democratic theory is the idea of an autonomous political community, which rightly governs itself and determines its own future. In a world of regional and global inter-dependencies and internationalised, shared state powers, these are issues that raise questions concerning the nature of consent and legitimacy, the nature of a constituency, the meaning of representation, and the proper form and scope of political participation. How could democratic ideals in the world of globalised power and inter-dependency relations be worked out?

It is widely acknowledged that there is a democracy deficiency not only in the EU – after all, the only organisation of its kind that has a directly elected parliament – but in the international law and systems of governance more generally.[145] This problem has to be taken seriously when designing the TTO.

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[145] For the best theoretical account thus far, see Held 1995.

The TTO will be responsible and accountable for potentially huge amounts of money. In the second phase, the revenues will be possibly more than a trillion US dollars a year, which is twenty times the GDP of Egypt, ten times that of Finland or Norway, twice that of South Korea or Brazil, or exactly the GDP of the UK in 1995.[146] It is crucial that the decisions made by the TTO will be conceived as legitimate, fair, accountable and, when needed, revisable. That is, they have to be as democratic as possible.

Now, it its important to note that it seems that international law no longer holds to *de facto* approach to statehood and government. Mere military control of state institutions does not suffice. There is a tendency to accept only liberal democratic governments as fully legitimate. Should we thus exclude non-democratic states from the TTO? Even after the “third wave of democratisation”, in a simplest liberal democratic score, a third of states are in no way democracies, and many are at best partial democracies.[147] However, democracy is a contested concept and it is always a process of democratisation rather than a model, in other worlds, there are no absolute yardsticks.[148] Moreover, any norm that operates by total exclusion is problematic.[149] Exclusion would contradict the universality of international law, and the universalist idea that the TTO must be open to all states.

Instead of any exclusion, all states should be included in the TTO. Despite possible deficiencies in the legitimacy of some states, we should assume that they represent their populations and weigh the decision-making powers of them in the TTO

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[146] These GDP figures are taken from World Bank 1997, Table 12, 236.

[147] See Potter 1997, 3-10, et.passim. The category of non-democracies include many economic powers such as China (the fastest growing economy), Singapore (one of the financial centres of the world) and Nigeria (accounting for about one-fifth of the population of Sub-Saharan Africa, with its oil revenues and military predatory state). Also most of the Islamic world is non- or quasi-democratic – although, it should be emphasised, in a simple and formal liberal-democratic score; some of them claim to be different kinds of democracies.

Note also that in Cox’s 1997, 63, assessment, “much of the movement towards democracy noted in recent years must be considered to be what Antonio Gramsci called ‘passive revolution’, i.e. the importing of democratic forms encouraged by external pressures that are embraced by a leading portion of the local populations but without the authentic participation of the local population”. Therefore, this democratising movements is fragile, “lacking a secure base in a participant, articulated civil society”.

[148] See Dryzek 1996.

[149] Crawford & Marks 1998, 78-79. Cf. the similar ethico-political criticism of the model of cosmopolitan democracy in Patomäki, op.cit.

accordingly.[150] The rule should be qualified majority decision-making with secret ballots.

Now, it is possible to recognise the validity of the emerging international legal norm of democracy in less exclusionary ways. Let us suppose that the TTO would have two main bodies, the Council of Ministers and the House of Democracy. The House of Democracy should comprise representatives from those national parliaments whose members are appointed by multi-party elections, and a sample of interested and concerned civil society actors, picked through a screening procedure and lottery.[151] Even though the inclusionary, state-centric Council of Ministers would have a stronger say in decision-making, the House of Democracy should be fully empowered to set motions as well as to have some control over the budget and a qualified veto-power over some of the major decisions of the Council. Perhaps there should also be joint decision-making in certain important areas of the TTO?

The second major issue is the allocation of revenues. First, a word or two on the estimations of the revenues. Naturally, the potential revenue is not easy to estimate. Researchers make different assumptions about, for instance, the elasticity of foreign currency exchange demand, the average pre-tax costs of foreign exchange transactions and the likely amount of tax evasion and exemptions. All the existing estimates are based on a global, uniform tax. It seems reasonable to expect a low, universal 0.05% tax to yield an ample USD 100 billion a year, and a twenty times higher tax, at the level of the recommended 1%, to yield perhaps

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[150] It is a basic democratic ideal that suffrage is based on the equality of human beings, not on their inherited privileges, inherited or acquired possessions, or the power to threaten others. However, also here a compromise with the conventional idea of equality of states is necessary. Hence, the votes of states should be weighted roughly in accordance with the size of the population of these countries, but not arithmetically but rather, say, placing them in three categories and giving them votes from 1 to 3.

[151] All details should not – and cannot – be worked out in this Report in a monological way, but should rather be decided dialogically by the actors. Hence, let us merely illustrate with an example how things could be organised. The House of Democracy could have 600 seats, 350 representing national parliaments, weighed roughly on the population of these countries, and 250 representing civil society actors registered in the member countries (whether NGO's, non-national parties, transnational religious movements or whatever). The civil society actors would have to apply for a seat. In the screening process, they have to demonstrate that they are neither artificial products of, nor directly dependent on, states or private corporations, and that they have a sufficient, spontaneous, popular basis. Also organisations originating in non-democratic state may qualify. Among the qualified civil society actors, there would be a lottery over the seats; and no one actor would be entitled to hold a seat twice in row.

7-11 times more, that is, from USD 700 billion to USD 1.1 trillion a year.[152]

But what about the taxation system in the first phase? Obviously, a lot depends on how many financial centres are included (as defined in terms of national booking sites, not dealing sites, which makes the distribution between countries much more equal). Assuming that, say, one third of the world's currency transactions are directly covered, and a part of the rest partially and indirectly via the domestic-lending tax, a safe bet would perhaps be to assume that the revenues would be around USD 50 billion a year (half of the uniform, universal, very low-level tax). The revenues might also be somewhat less or much more, and, naturally, the more countries join the regime, the higher the revenues will be.

The first major decision about these revenues concerns the national share. There are in fact three considerations here. States have to be compensated for the administrative costs of organising the tax collection. A generous remuneration could also stimulate more enthusiasm in the financial "great powers" to join the regime and implement its rules. Finally, there is a deep-rooted sense of justice that national states possess the products of the activities based in them.[153] This may well be increasingly outmoded in the world of global flows, networks and off shores,[154]

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[152] Michalos op.cit., 25-27, discusses some estimates, but like Felix & Sau 1996, particularly 238-240, he does not really consider taxes higher than 0.25%. Felix & Sau, op.cit., 243, advise against applying higher tax rates on the grounds that "such high rates would disrupt foreign exchange trading so much that exchange rate volatility may not be reduced". Yet, as if to confirm our suspicion that the notion of "distortion" is derived from the questionable notion of "Pareto optimal unique equilibrium", in note 20, p.251, they seem to deny the likelihood of any major "disruptions". Frankel, op.cit., 60, cites Tobin's own estimation of USD 1.5 trillion from a 0.5% tax, but Frankel thinks Tobin is mistaken for number of reasons. Frankel himself claims that under very cautious assumptions, it seems that a 1% tax would yield at least USD 500 billion, but its revenues are more likely to exceed USD 1 trillion a year. There seems to be plenty of room for experimentation with the tax and its level, and the TTO should be flexible enough to quickly adjust to the lessons of these experiments.

[153] As Beitz 1979, 69, has pointed out, "perceptions of international relations have been more thoroughly influenced by the analogy of states and persons than any other device", and the standard conception of person, on which this analogy rests, stems from the liberalist political theory of Hobbes, Locke and others; see also Koskenniemi 1989. Now, the Lockean conception of possessive individualism implies that all the products resulting from the work of a person belong rightly to that person; and in a crucial move, Locke argued that this person can also hire others to work for him, and he still would own the results of that work. By analogy, we may assume that it has been, and still is, a strong moral intuition that all the results of the work occurring within the territory of a state belong to that state (or to the individuals constituting it).

[154] Cf. Castells 1996, 476-477: "The social construction of new dominant forms of space and time develops a meta-network that switches off nonessential functions, subordinate social

yet as a strong moral sense it has real effects in the world, and should be taken into account in all global political arrangements.

Hence, we may want to argue that it is also fair that the states will get a share of the revenues. What, then, would be a fair compensation and share? There is no way of calculating this; it is an issue that needs to be agreed upon. Our suggestion is **one third**, for it is substantial enough, but does not violate the idea that the Tobin tax regime is also a global, collective endeavour.

The second major decision concerns the allocation of the global fund of revenues. There are so many good candidates for spending these resources. It could be used to radically alleviate poverty in the world or to

The Tobin Tax and Global Social Policy

Bob Deacon

The current phase of globalisation has taken place within the context of the dominance of the neo-liberal paradigm. This has resulted in challenges to the capacity of both welfare states in the north and governments in the south to provide for the social protection of their populations.

In terms of the developed and middle income countries globalisation (Deacon, 1997):

- Sets Welfare States in competition with each other. This generates the danger of social dumping, deregulation and a race to the welfare bottom. There are, however, political choices available within each welfare state as to whether it does indeed cut expenditures and loosen labour and other regulations and pursue the race to the welfare bottom, or spend on aspects of social welfare to increase productivity and political and social stability in order to attract investment, or steer a third course and maintain all welfare expenditures funded in ways that do least damage to competitiveness.
- Generates a global discourse within and between global actors on the future of national and supranational social policy. In the emerging 'complex multilateralism' the future for social policy at a national and supranational level is being shaped by a struggle between supranational organizations such as the World Bank and IMF on the one hand and the UN family of agencies on the other.
- Creates a global market in welfare providers. This increased opportunity globalisation generates for providers of welfare services to become global and operate in many countries may contribute to the undermining of national social provision and national regulatory policies. It is clear that the international insurance market is waiting in the wings to sell its products to the less risky

groups and devalued territories. By so doing, infinite social distance is created between this meta-network and most individuals, activities and locales around the world. [...] The new social order, the network society, increasingly appears to most people as a meta-social disorder." Indeed, if this is the more and more common perception of the world, the metaphors and ontological assumptions behind a standard, idealised accounts of state sovereignty must appear increasingly implausible – except perhaps as a nostalgic reaction against the "meta-social disorder".

sections of the population in Europe once the pressures upon pay-roll taxes and the propaganda drip feed of the World Bank begins to create political alliances for reducing public pension commitments. Global markets in social and health service providers (Koivusalo and Ollila 1997) are emerging. The MAI would have facilitated the insertion of such companies into new markets and countries and potentially undermine public welfare provision.

In terms of developing countries and many emerging economies globalisation has:

- Generated severe indebtedness which has undermined the capacity of governments to secure education, health and social protection so that in many countries it is now left to new NGO and bottom up credit initiatives to provide a partial network of coverage for some people.
- Subjected to punishment by international speculators those countries who have through deficit spending attempted to maintain some forms of social protection for the poor such as through basic food subsidies.
- Encouraged the perfectly rational response of selling of country assets including those arising from low labour costs to attract capital at any price and with disregard for emerging global labour, environmental and social standards. Tax havens for TNCs as part of this strategy further undermine the revenue raising capacity of such governments.

We are now witnessing the collapse of the fundamentalist liberal paradigm in the face of the obvious weakness of an unregulated capital market. It is essential that the world moves towards a socially just and socially responsible globalisation which secures a degree of equity both between and within countries. The requirement at this time is for the development at a supranational level, both regionally and globally, of those mechanisms of social policy that are no longer adequate if only existing at national level. The need is for:

- regional and global social redistribution
- regional and global social regulation
- regional and global social empowerment (of poor people and poor countries)

The TOBIN tax fits into this requirement in terms of regulation and redistribution, and, if some of the proceeds were to finance a global court of human and social rights also the need for empowerment. It has been suggested (Kaul and Langmore 1996) that all of the revenue arising from transaction in poor countries should be retained by them but some of the revenues arising from transactions in richer countries should be remitted to a new global spending authority under UN auspices. The positive impact on social welfare north and south would be to:

- Enable the governments of very poor countries to begin to build upon the new networks of civic initiatives for social protection and generalise them across all the population.
- Ensure the meeting of the current OECD:DAC targets of securing basic education and health services as well as water, sanitation and shelter to ALL the world's citizens.
- Shift the balance of power globally back to the UN from the World Bank and the IMF, which in turn would lead to the erosion of the ideology of privatisation and residualisation in public welfare provision.
- Encourage global demand management and an element of global Keynesianism which would have a positive impact on growth globally which in turn is a better

environment within which to continue the struggle to find a north-south compromise on global labour, social and health standards.
- Contribute, through the positive impact all of this would have on egalitarianism within and between countries, to the erosion of all of those public global bads that stem from global inequity. These include international crime and drug running, illegal economic migration, and environmental degradation.

The UK Chancellor of the Exchequer (Brown 1998) had the foresight in late 1998 to argue that if the world were to move towards a better regulated global market place then it would be necessary to agree on a global code of best practice in social policy which "should not be seen in narrow terms as merely creating safety nets". This code is now being drafted within the World Bank but the hope is that other global actors such as the UN, the ILO and others will also own it. It could be an element of the agreements at the Copenhagen plus 5 UN special meeting to be held in Geneva in June 2000. Such a global code will have global resource implications. The TOBIN tax is one way in which some of these resource implications could be met.

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re-organise the debts of the poorest nations; to create stabilising, global investment funds; to establish the basis of global social policy; and to contribute to many other socially useful purposes. But instead of making a monological argument for using the money for this or that purpose – it should be decided dialogically – let us merely suggest two things.

From the beginning of the Tobin tax regime, a slice of the revenues – say USD 1-2 billion a year – should be allocated to the UN basic budget, to rescue it from the constant financial crisis situation, and to give leverage to more democratic reforms than currently considered at the UN headquarters. Some separate support could be given also to other, selected parts of the UN system (UNDP, UNCTAD etc.); and of course, funds for many specific purposes should perhaps be channelled and organised via the UN as well. This would prepare for the more autonomous and democratic UN for taking over the TTO in the second phase

(the transition should perhaps leave the TTO headquarters in their location and parts of the structure and functions of the TTO intact).

Moreover, some funds could also be dedicated to an organised, global political campaign for a global, universal Tobin tax. The revenues of the first phase tax could be used to subsidise this campaign. For instance, in the first year, say USD 500 million could be allocated to an advertisement and publication campaign addressed both to the customers of the banks and to the citizens of democratic states such as the UK and the US. This would possibly include the establishment of more permanent elements of a pluralistic, transnational public sphere: newspapers, on-line publications, virtual TV channels etc.[155]

The support for the UN system would prepare the organisational structure for the second phase. In turn, the political campaign would add on the mounting pressure on the outsiders, although the main pressure should be stemming from the economic incentives built into the regime itself (stability, revenues, decision-making rights etc.).

What about our second proposal on the decision making process of the distribution of the income? Instead of making any further recommendations about the usage of the funds, let us just restate the point that it is absolutely crucial that all the **decisions about the allocation of revenues will follow public, transparent, fair and democratic procedures**, and that the decision-makers are strictly **accountable** for their actions both to the member-states and the wider, democratising world republic. Only if all the relevant participants feel that they are sufficiently involved in determining these decisions on an equitable basis, will they be legitimate in the longer run.

It seems that political problem of allocating and distributing resources gets twisted back to the question of working out democratic ideals in the world of globalising power and interdependence relations. Democratisation does not exhaust issues of social and distributive justice, yet it clearly constitutes an essential ingredient of any just and socially responsible system.[156]

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[155] That is, to create alternatives to the neoliberalist, USAmerican global media.

[156] However, in a deeper perspective, this might be an 'egg-or-hen' problem: many democratic theorists have been painfully aware of the material and distributional preconditions for democratisation. Some classical republicanists and liberalists have envisaged the diffusion of ownership of property among the many as a condition for

5.4. Towards the Second Phase: Economic Security Council or ECOSOC as the Parent Organisation?

When the second phase of the Tobin tax regime approaches, the fate of the TTO has to be decided. Should it remain independent or, rather, be merged with a more all-encompassing system of governance? We shall argue that the United Nations has a lot of potential for becoming the governor of the TTO, yet it has to be reformed first, and we have to acknowledge that this might turn out to be an insurmountable problem.

Before starting, let us make a methodological remark: the following discussion is even more future-oriented and speculative than the previous one (5.3.). The future is radically open, and for a number of reasons it may make this discussion quite futile. But we do not know this yet. In any case, there is a problem of linking the TTO with wider structures of governance in the second phase; and some guidelines for the second phase must be clear from the outset. Therefore, it is important to envisage and assess different possibilities for governance of the future global economy.

First of all, what is the argument for making the UN the governor of the TTO? The United Nations is the only truly universal organisation. Whereas the perspective of the Bretton Woods institutions is necessarily partial, the UN provides, at least in principle, a more representative and holistic viewpoint for discussions and governance. More than the IMF or the World Bank, it has also certain in-built democratic principles. These include the governing principles of the General Assembly (states are equal in decision-making, which is, despite its problems, more democratic than the 'one dollar, one vote' principle) and the universal human rights (human beings are equal and have thereby civic, social and political rights).[157]

Moreover, the UN organs and specialised agencies form the natural basis for developing global welfare functions further; there are no easy substitutes for them. And all things considered, it may

democracy (or republic); whereas other, social-democratic theorists have seen decommodification of labour and fair, transparent and accountable public funding of political activities as a condition for autonomous democratic actions; and some others, calling themselves radical democrats, conceive democratisation to be necessarily linked with vanguard democratisation of organisational relations of production. See Esping-Andersen 1990; Held 1996; and Unger 1998.

[157] For a discussion, see Archibugi 1995; Held 1995, 83-89.

be easier to develop and reform the UN system than to create a network of organisation from scratch (at least we should start with this assumption). Added together, these reasons make a *prima facie* case for the UN to become the governor of the TTO in the second phase of the Tobin tax regime.

The prerequisite is that the UN will be reformed first. In fact, the UN reform has been on the agenda for decades. Some minor reforms have also been carried out, although more far-reaching proposals have remained a dead letter. Now, it is crucial to understand that the substance of the proposed reforms has varied with world political constellations and trends. In the beginning of the 1970's, it was the decolonised Third World that took the initiative with proposals such as the New International Economic Order. Since the early 1980's, neoliberal conservatives have defined the content and direction of attempted UN reforms. Time might be ripe for something else now.

But let us first have a look at the recent developments. In the early 1980's, the Reagan and Thatcher governments launched an attack against the UN. Before the end of the Cold War, they withdrew their support for the UN in number of ways. Gradually, they and their successors started to push for a **financially more accountable UN**. "It is no coincidence that the member states that have done the most to dismantle the welfare state at home, particularly the USA and the UK, have also done most to de-legitimate the claims of the UN to a global role".[158]

After they had managed to change the direction of developments, and particularly after the end of the Cold War, they have concentrated more on using the UN for their own purposes – whenever feasible – and reforming the UN in accordance with their own vision. To summarise, these social forces "are reluctant to concede democratic reform of the UN, and would argued instead for a greater correlation between financial responsibility and influence within the organization – that is, actually **enhancing**, rather than reducing, **the elite privileges** contained in the Charter"[159]. The prevailing argument for this course of action was, and still is, that efficiency and democracy are

[158] Imber 1997, 223.
[159] Ibid., 223.

incompatible and that efficiency should be preferred to democracy.[160]

However, under pressure to democratise the UN, and to make the recent developments look better in the eyes of the world public, the neoliberalising social forces have simultaneously granted limited participation for certain officially recognised NGOs in the UN system; this represents "realistic" democratisation. This development does not challenge the relations of domination within the UN system, or the content of reforms that attempt to make the UN "financially more accountable". Imbalances of the contributions to the UN budget are the means by which reforms are guided. The US and the UK account for 25% and 5% respectively; Japan 12%; and France, Germany and Italy together for 20% of the UN budget.[161]

In 1997, it was quite appropriate to ask whether the "financially more accountable" UN had already passed from being a partially democratic forum to a mere hegemonic instrument.[162] As a report by the South Centre (an inter-governmental organisation having a close relationship with the Group of 77) describes the situation:

> *The history of the UN to date has been marked by the ability of a few powerful countries of the North to exercise an overriding influence on its institutional framework and policy direction, in particular by using the 'financial whip'. With the ending of the Cold War, the resulting lopsided balance of power in the Organization has opened the way for some major powers to embark on more vigorous and systematic efforts to shape the United Nations and specialised agencies even more in line with their own interests, priorities and political preferences.*[163]

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[160] Again, an analogy to the domestic political assault on democracy is apt: the 'ungovernability' thesis launched by the Trilateral Commission – close to the elites of the Western (+ Japan) world – in the mid-1970's claimed that too much public demand upon political systems has led to inflation and indebtness and had begun to make liberal democracies ungovernable; see Crozier et.al. 1975. For an accurate scrutiny of this theory, and a comparison to the rival and rather different neo-leftist 'legitimation crisis' thesis, see Held 1996, 240-253.

[161] The US has used this leverage in the most straightforward manner. The Kassebaum Amendment (1985) of the US Congress provided that the US could pay no more than 20% of the annual budgets of the UN or any of the specialised agencies unless the agency had established a system of weighted voting on budgetary matters. Weighted voting was defined as voting strength proportional to a country's share of the total financial burden of the agency; in other words, as one dollar, one vote. See Kanninen 1995, 41-42.

[162] Imber, op.cit., 225.

[163] South Centre 1997, xv.

It is for this very reason that those who have envisaged reforms for making the UN both stronger and more democratic have been advocating alternative sources of funding to the UN. Almost without exception, this has meant finding the most appropriate form of global taxation. There are suggestions ranging from arms sales and travel taxes to the establishment a UN world lottery and credit card. The Tobin tax is also always mentioned on this list, and often as the most important possibility.

It is our suggestion that the TTO should make, from the beginning, a substantial contribution to the UN budget (perhaps USD 1-2 billion a year, which is about half of the basic, annual budget of the UN). In addition to supporting the UN system as such, without conditions, it should do this also to enable more democratic and socially responsible reforms of the UN; that is, to give help to give a new direction to reforms, and to create a political space and momentum for them.

However, there is no automatic connection between new sources of UN funding and democratic and social reforms of the UN. What would be the likely effects of these revenues? The UN representatives and civil servants should feel more encouraged to think independently and consider different, now prohibited possibilities. A number of projects that are now impossible would be enabled. It could also make a big difference by changing the assessment of political possibilities and thereby changing the way the UN is seen – or, often enough, not seen – in the globalising media and by various political actors.

Yet, even after the substantial TTO contribution, things can continue to move to the direction determined by the neoliberal conservatives. The TTO contribution cannot be conditional on desired political reforms. To be effective and in accordance with its democratic aims, **the TTO allowance cannot work by conditionality** and, in effect, by blackmailing. It has to function more indirectly; but how? In our opinion, contingencies have to be accepted. The best option is to channel funding not only through the basic budget of the UN but also directly to those UN organs and special agencies most in favour of the approach of the TTO and the desired democratic and social reforms. In addition, the member-states of the TTO should push for changes. But there is no guarantee that these will work.

For one thing, all amendments of the UN Charter have to be accepted in the Security Council, whose five permanent

members all have the veto-right: the US, the UK, France, Russia and China. Any of them can stop changes from taking place. Even if a clear, absolute and dedicated majority of both states and world population were in favour of a given proposal for amendments, and even if the bulk of the UN budget came from the TTO, the permanent members of the Security Council could still prevent all changes. This is the heritage of the First and Second World Wars. The globe was divided into re-atomised nation-states, some of which were recognised as "great powers" with distinctive sets of geopolitical interests that, according to the norm, should be respected. These increasingly anachronistic principles of military power politics were built into the UN Charter conception. Nonetheless, following the logic of these principles, the UN can and should do nothing if resisted by any of the great powers nominated in 1945.

Hence, there is no guarantee that the UN can be made more democratic. But it is worth trying. There are in fact at least two possible and desirable scenarios about how things might evolve:

1. The UN will be reformed, and something like an economic Security Council or a reconstructed ECOSOC will emerge, to complement and revise the existing structures and functions of the UN. Consequently, the TTO can be partially merged with, and legally also subordinated to this body.
2. The TTO will turn out to be virtually the economic security council or new ECOSOC for the UN. It might be more a *de facto* than a *de jure* relationship, but for instance many specialised agencies can be linked to it also juridically.

Let us briefly scrutinise these possibilities.

5.4.1. The Economic Security Council of the UN

Following the initiative of Willy Brandt immediately after the fall of the Berlin Wall, Ingvar Carlsson and Sridath Ramphal were invited to co-chair the Commission of Global Governance, a group of 28 state leaders, to suggest ways in which the global community "could better manage its affairs in a new time in human history". The Commission published a Report in 1995 entitled *Our Global*

Neighbourhood.[164] In this Report, the Commission assumed that "so far the UN has not provided a satisfactory forum for practical, well-focused international economic discussion"[165]. Given global interdependencies, there is an urgent need for such a forum:

> *The time is now ripe – indeed overdue – to create a global forum that can provide leadership in economic, social and environmental fields. It would be more broadly based than the G7 or the Bretton Woods institutions, and more effective than the present UN system. While not having authority to make legally binding decisions, it would gain influence through competence and relevance, and acquire the standing in relation to international economic matters that the Security Council has in peace and security matters.*[166]

First and foremost, the economic Security Council would provide a long-term strategic economic policy framework for governments and major international organisations. Its agenda would be defined in terms of comprehensive notion of security; for instance, "shared ecological crises, economic instability, rising unemployment, the problems of transformation in the former Soviet Union, mass poverty, or lack of food security" would constitute the problems it tackles.[167] Nonetheless, the economic Security Council is not intended to be a crisis management forum, but should instead look more generally towards trends in global economy and also take preventive measures.

The economic Security Council would seem to fit well with the idea of governing the currency transactions tax, which is intended to be a preventive measure against global financial fluctuations that have real economy consequences. In fact, the Report also mentions the Tobin tax very positively and urges "the UN and the Bretton Woods institutions to explore the feasibility of such a system in consultation with the regulatory authorities of the leading financial markets"[168]. Although the Report does not specify the relationship between the economic Security Council and the Tobin tax system, we may well assume that the latter would naturally fall within the authority of the former. At least the Report argues that economic Security Council "would also be the

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[164] The Commission on Global Governance 1995.
[165] Ibid., 154.
[166] Ibid., 155.
[167] Ibid., 157.
[168] Ibid., 219.

appropriate forum for studying proposals for financing international public goods by international revenue raising"[169].

So far, so good. However, besides the difficulties of implementing the idea, there are three major problems. Firstly, the proposal of the Commission on Global Governance is based on securitisation of economic, social and ecological issues. This tendency to securitise political issues started in the 1980's but became particularly widespread at the wake of the end of the Cold War. In retrospect, the purpose seems to have been to prioritise these issues by redefining them as matters of security.

It is true that there is a security aspect to many of these issues. However, securitisation as a widespread tendency has to be understood in its specific context: originally it was used both against the Cold War military priorities and practices – to dispel the difference between "high" and "low" politics in international relations – and to defend public policies on socio-economic and ecological issues against the criticism of neoliberal conservatives. Soon it assumed new usages and unintended consequences: military organisations such as NATO started to enlarge their agenda, and the logic of national security and military issues was brought into the fields of socio-economy and ecology.

In the case of the Commission on Global Governance, the logic of securitisation evoked a proposition of a new, complementary Security Council. As its name indicates, Security Council was originally meant to deal with issues of peace, war and military security. Its structure – including veto-powers – was devised in the power political context of 1945. Indeed, the second major problem of the proposal by the Commission is that this may not be the best possible structure for dealing with problems of governing the global political economy of the early 21st century.

In principle, this is acknowledged also by the Commission, but the authors of the Report do not draw any conclusions from this acknowledgement. They argue that the economic Security Council must be small to be "practical and efficient". It would comprise the G7 countries (not Russia, for it would not qualify in terms of its remaining GDP); integration organisations such as the EU, ASEAN and Mercosur; and smaller states to guarantee regional representation. They suggest rotation to guarantee better representation, but apparently the rotation would apply only to

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[169] Ibid., 157-158.

smaller states – as measured by their GDP. In other words, there would be permanent members (G7, EU?) and rotating members. Since decisions would be made by consensus only, all states would have a veto power. And they are very careful in pointing out that "no major new bureaucratic apparatus is being suggested"[170].

This structure might be good for discussions and conducting studies, but not appropriate for governing the Tobin tax. It is not only that it compromises democratic ideals. At least as seriously, it would lack authority and the necessary administrative machine to govern tax itself and allocating the revenues from it. Something stronger and more democratic is needed. It is entirely possible, of course, that the Commission of Global Governance would be willing to revise their proposal in order to take into account the requirements of governing the currency transactions tax. That remains to be seen.

5.4.2. The Economic and Social Council (ECOSOC)

Originally, the UN was placed at the apex of the emerging system of international organisations – including the Bretton Woods institutions. The Economic and Social Council, ECOSOC was designed to be the core of this system. Nominally, the specialised agencies are still subject to co-ordination with the UN via the ECOSOC, and the specialised agencies comprise the IMF and the World Bank. In the UN Charter, the ECOSOC is mandated to deal with economic and social issues in the most comprehensive sense of the term.

The ECOSOC consists of fifty-four Members of the United Nations elected by the General Assembly. Eighteen members are elected each year for a term of three years. A retiring member is eligible for immediate re-election. Each member of the ECOSOC has one representative, and each member has one vote. According to the UN Charter, decisions of the ECOSOC are made by a majority of the members present and voting. Moreover, the ECOSOC may make suitable arrangements for consultation with non-governmental organizations which are concerned with

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[170] Ibid., 156.

matters within its competence. [171] All in all, the ECOSOC seems to be much more democratic than the would-be economic Security Council. It is also empowered to make real decisions.

It thus seems that (i) there already is a substitute for the economic Security Council; (ii) that this body is not restrained by securitisation of socio-economic issues; and (iii) that even more importantly, this body is designed to be in charge of co-ordinating and supervising the entire system of international organisations. Assuming more general democratisation of the UN, would not this be the ideal parent organisation for the TTO? It is not even bound to New York: one of the two bi-annual sessions is held in Europe, in Geneva.

The Commission on Global Governance is of course mostly right in saying "so far the UN has not provided a satisfactory forum for practical, well-focused international economic discussion". They should have only added that the UN has not marginalised the ECOSOC; it has been marginalised by other social forces.[172] Yet, despite its *de facto* weaknesses, there is a lot of potential in the ECOSOC. The revitalisation of ECOSOC seems to have been on the agenda almost constantly.[173]

In its proposal for a strong and democratic United Nations, the South Centre has firmly emphasised that the ECOSOC "requires protection against forced erosion from within, as well as demands for its outright abolition"[174]. In addition to the standard demand to make the ECOSOC the entity envisaged in the UN Charter, they make a number of suggestions about what the ECOSOC would need urgently:[175]

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[171] See Articles 61-72 of the UN Charter.

[172] "Genereous funding has been made available to allow a steady expansion of tasks in the IMF, the World Bank and the WTO, which are considered the most competent institutions whose current working paradigm and governing structures are regarded more favourably. Considerable pressures are exerted to ensure that any remaining activities by the UN in these fields reflect the free market orientation and are supportive of the work of Bretton Woods institutions and theWTO." South Centre, op.cit., 206.

[173] Cf. the situation in the late 1980's, as described by Kanninen op.cit., 81, and in the late 1990's, as illustrated, for instance, by the ECOSOC Press Release 5812, "Managing Risks of Globalization Great Challenge to Modern Times, Secretary-General Tell Economic and Social Council", 3 Feb 1999.

[174] South Centre, op.cit., 226.

[175] Ibid., 167-170.

- An equivalent to a Council of Ministers for long term planning and actions regarding the trends in the global political economy.
- A new, delegated executive body, with more capabilities for implementing the decisions.
- An enhanced secretary with rebuilt independent, analytical capabilities.
- Constant sessions, both to develop early warning capabilities, quick actions, and more serious long-term planning.

All of these reforms would require resources, and perhaps those resources could be provided by the TTO. In any case, it seems to us that these reforms – even if in need of further amendments to make it more compatible with the idea, structure and resources of the TTO – would empower the ECOSOC to govern also the currency transactions tax.

5.4.3. The TTO as the Focal Point of the UN System?

Suppose that, despite all tenacious efforts, it will be politically impossible to either establish an economic Security Council or empower the ECOSOC. Despite all efforts, the UN will remain undemocratic and incapable of handling the Tobin tax and its revenues. Suppose further that the TTO has nonetheless supported the UN with a very substantial allowance for years, and that many of the UN organs, special agencies and projects are funded by the revenues from the currency transactions tax.

By the time of its second phase, the TTO would have become a universal and global organisation, and, at that point, it still continues to fund and organise many UN activities. Suddenly, it may appear that the TTO is the focal point of the whole UN system. Perhaps at that moment many actors realise also that, after all, there is in fact no need to construct new bodies or reconstruct old ones. Against all odds, a bottom-up reform would have managed to change the system of governance of the global political economy.

6. Conclusion: Realism Re-Assessed

Visions about possible and desirable worlds must be based on an analysis of the real world, its interdependent mechanisms, its practices and power structures, its persistent and stubborn nature, its multi-faceted openness and contingencies. A thorough analysis of these may also reveal that a small and modest reform proposal – a small tax on currency transactions – is related to many elements of the current global context.

We started this Report by discussing the original argument for the currency transactions tax. Treasurers, central bankers and economists have tended to ignore or marginalise Tobin's argument, but their orthodoxical reasons for doing so seem to be false. As a well-known dissident economist put it, "the characteristics of the special case assumed by the classical theory happen not to be those of the economic society in which we actually live, with the result that its teaching is misleading and disastrous if we attempt to apply it to the facts of experience". The endless stream of world financial crisis – reaching a climax in 1997-1999 – seem to have confirmed Tobin's original claim that "national economies and national governments are not capable of adjusting to massive movements of funds across the foreign exchanges, without real hardship and without significant sacrifice of the objectives of national economic policy with respect to employment, output, and inflation". In 1999, the Tobin tax is a political issue like never before.

The Tobin tax implies many technical problems: how to monitor the tax, how to prevent tax evasion, how to maximise its efficiency in countering the effects of currency markets volatility, how to make it real in an imperfect world where not all powerful actors are supporting it? Some of these problems are difficult, intellectually and pragmatically. None of them is insurmountable, and the technical problems are mostly resolvable without any great difficulties.

As many others have pointed before us (in different ways), if there is a will, there is a way. The major problem has always been the lack of political will, the absence of global political consent for implementing the tax. In this Report, we have developed a new approach to making the Tobin tax real. Tobin and his followers have assumed that all major financial centres and most other

states would have to consent with the idea before it is workable. We have argued that this is not the case.

Instead, we maintain that the Tobin tax could be realised in two phases. In its first phase, the system should consist of the euro-EU and a group of other countries, or, alternatively, a bigger group of other countries without the EU (those fearing the consequences of the next financial attacks, together with the progressivist Northern states, are the most evident candidates for assuming this role).

However constituted, this grouping should establish an open agreement – any state can join at any time – and a supranational body orchestrating the tax and collecting the revenues of a small underlying transactions tax (10 basis points, at most); much bigger exchange surcharge (1%-3% or even more); and a relatively high tax, perhaps 1%, on domestic-currency lending to non-residents (only to non-residents who are not yet within the tax regime). This arrangement would solve the tax evasion problem and is economically sound.

In the second phase, which should be carried out either when all major financial centres and most other countries have joined the first phase system, or at latest by, say, year 2010, a universal and uniform Tobin tax at a higher – yet absolutely low – 1% rate would be applied.

This arrangement is politically more realistic than any previous proposal. It would make it possible for a(ny) grouping of countries to proceed quickly without the consent of every state (including such financial centres as London/UK or New York/US). Yet it would not compromise the aim of a universal and uniform tax. It is devised in such a manner that it would build up pressure for the outsiders to join it, too.

Having said all this, we must realise that the Tobin tax is more than just another tax. When all the details are thought thoroughly through, it appears that the Tobin tax is bound to expand transformative struggles to many contexts of world politics. The global financial markets have become an established structure; perhaps the Tobin tax is the corresponding activity that will make that structure vulnerable to collective conflict and deliberate revision? Whether intended or not, one of the effects of the Tobin tax seems to be to prevent the privileged factions of the world society from having the monopoly over the means to create the social future on the planet Earth.

Let us therefore presume that what is pragmatically possible is not fixed independently of our imaginations, but is itself shaped by our visions. In this Report, we have proposed a detailed, at times technical, at times political, vision of making the Tobin tax real.

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