A Global Financial Tax?

Morris Goldstein assesses the prospects for a global tax on banks to pay for resolving bank failures—and the prospects in Congress for such a tax.

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Steve Weisman: The idea of taxing banks and financial institutions to set up a fund to help stabilize the situation if and when banks fail is gaining currency both internationally and in Congress. This is Steve Weisman at the Peterson Institute for International Economics with Morris Goldstein, senior fellow here at the Institute, leading expert on this approach to financial reform. Morris, thanks for joining me to discuss the latest developments.

Morris Goldstein: Delighted to be here, Steve.

Steve Weisman: Let's talk about the international situation first. The International Monetary Fund and the finance ministers and central bankers meeting in Washington seem to be embracing this idea. What's going on?

Morris Goldstein: They were asked by the G-20 to study this issue of how you would raise funds for an orderly resolution of the financial sector and they've come forth with some recommendations, including two kinds of taxes. One kind of tax is similar to what has been proposed in the United States by the Obama administration, which is essentially a tax on banks' noncore funding. Its tax base is the institution's total liabilities, less its insured deposits and bank capital. That's one measure. A second kind of tax would be on profits and remuneration in the financial sector. That's similar to what we've seen happen in the United Kingdom and France and some other countries. The common element, I think, is a growing recognition that if the financial sector is going to get into difficulties and one is going to have to resolve that—because we can't just let it go on given the cost to the economy—we want the financial sector to pay for that. Not the taxpayer. And these are ways of raising revenue to do that so that the financial sector pays for its own mess.

Steve Weisman: What's been the response of the financial sector?

Morris Goldstein: I think for the most part, they object to it. They would not like to bear the cost of it. They seemed to be less opposed to the first kind of tax—that is a tax on their funding that would go into some resolution fund or into general tax revenue—than the second kind, which is a tax on bonuses and bank profits.

Steve Weisman: What has to happen before this is adopted internationally?

Morris Goldstein: At this stage, I think they're just talking about it. It's already clear that some of the G20 countries are very much in favor and others are much opposed.

Steve Weisman: Which ones are most opposed?

Morris Goldstein: Certainly Canada is opposed and they'll be the next chair [of the G-20]—one of the next chairs, so that's a bit of a problem. The Australians are clearly opposed. The Japanese are opposed.

Steve Weisman: And they argue what? That they haven't had the crisis that other countries have had, so why tax their institutions to protect them against something that they have been wise enough to avoid?

Morris Goldstein: That's right. They say, "We've been prudent and our banks didn't impose costs on the taxpayers, so we don't need this. If you other fellows want to go ahead and do this, that's fine. But don't ask us to play ball. Or they think that if you want to limit any future cost of taxpayer, there are other ways than by imposing higher capital on the banks. That is, they would rather do it via the regulatory structure than via a tax system. Interestingly enough, the proposal gets some support from emerging economies in the G-20, who have a rather different perspective. They're not looking at the proposal so much as a revenue raising measure, but they see it more as a way to change behavior. An example that's often given is that there's a congestion charge for going into Central London. It's not to raise revenue, but it affects behavior of what hours you come in and how you behave. Similarly, the idea with this bank tax would be, since you're going to put a tax on liabilities of banks that are not deposits, then it's going to be more expensive for banks in emerging economies to engage in the kind of large-scale borrowing that has caused so much trouble in the crisis because they would have to pay for it.

Steve Weisman: What's so bad about the idea of the countries that want to do this, doing it on a voluntary basis? If it's not universal, would it still be a good first step?

Morris Goldstein: I think it would. The normal worry of not getting everybody to join in is that activity would move to the low-taxed or no-tax location so that you wouldn't really get the revenue that you thought, because banks would move. However, in this case, it's argued that we already see very big differences across countries in taxation of the financial sector. And we live with that, and banks don't all go to the same place so that we could have this as well. I think it's just somewhat easier if more of the G-20 agreed. But my guess is that we would still see some implementation even if only some of them were in favor.

Steve Weisman: Let's talk about the United States. Congress is now looking at a multilayered bill that would include something like this in the latest version. There are mixed reports about whether it's going to finally stay in the bill. There's a big focus over Republican charges that a fund of this kind is a "bailout" fund that would just set us up for more bailouts.

Morris Goldstein: I think that's really a bogus claim on a number of accounts. First, there is an advantage in setting up a fund ex ante, because if you try and get all the money from the financial sector after the crisis has already happened, you have to tax the survivors, not the people who caused the problem in the first place. If you want to get the people who actually caused the problem and if you want to make the tax higher on those with higher risk, you have to do it ex ante. Second, I think the comment that this is a bailout by the Senate Minority Leader Mitch McConnell and others doesn't make the distinction of where the money comes [from]. This is not money coming from the taxpayer. This is money raised from the financial sector. I think it's perfectly fine to get some of it from a fund that you set up earlier, and the rest you get from the financial sector after the fact. But I think it shouldn't be called a bailout to begin with. I think there are advantages in getting some of it upfront. So I think the Republicans on this are just simply off base.

Steve Weisman: Of course, not all Republicans are opposed to it. In fact, this idea was the product of negotiations with Senator Corker [R-TN], is that right?

Morris Goldstein: I think that is right. The question really is: Will the Obama administration abandon this in the end as the price of getting a deal? I think they were not actually originally the ones who were most in favor of this. I think this proposal came from other places including Sheila Bair, the head of the FDIC [Federal Deposit Insurance Corporation] who thought that for some of the reasons I just outlined, it made sense to have some of the money raised beforehand just as you do with the FDIC Insurance Fund for banks. The Obama administration will say, "Well, this is such an important bill as a package that if we don't get the $50 billion fund beforehand, it's not a make or break issue. Let's give that up to get some Republican support and we'll just have to raise the money after the crisis from the survivors." I would prefer that didn't happen. But if we get a good bill otherwise, I probably would pay it also.

Steve Weisman: When you mentioned congestion pricing, one of the advocates of congestion pricing in New York was Mayor Bloomberg, who wanted everyone to pay a tax who came into Midtown or Downtown Manhattan. But he doesn't seem to be taking the same approach for financial regulation.

Morris Goldstein: The finance industry is claiming they're for reform, but of course, they're sending out an enormous amount of lobbyists and spending a huge amount of money to block various aspects of reform, including some that I think are crucial—OTC [over-the-counter] derivatives, consumer protection and some aspects of discouraging "too big to fail."

Steve Weisman: I think the Obama administration should get credit for this lobbyist stimulus program, don't you?

Morris Goldstein: I do.

Steve Weisman: Thanks, Morris.

Morris Goldstein: Thank you.