FAWn - Denkanstöße
Beiträge für den offenen Dialog

Leverage Money Tax

A levy on leverage and thus systemic risk as an international financial market tax for stability and to finance a Global Deal

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1. What is money?

The heart of our monetary system is a special kind of money: Legal tender (notes and coins), created from nothing mainly by central banks. This central bank money (as legal tender) in principle is nothing than a "mere scrap of paper" evidencing a promise to get added value at some time in the future. Legal tender is thus a kind of "added value voucher". But there are, in addition to that, much more "scraps of paper", evidencing promises to get legal tender at some time in the future. We name this "leverage money", like debt obligations, bonds, derivatives and the like. "Leverage money" are promises on legal tender and since legal tender can be understood as promises on added value, all "leverage money" is an indirect promise on added value. Thus "leverage money" are indirectly "added value vouchers" as well.

What is a credit? Does credit mean to borrow money? No! A "securitized" credit **is** money. It is leverage money. In principle all liabilities on balance sheets are leverage money. And the overall volume of all forms of money are the "added value gap" of our world.

2. What is the global situation?

One could look to the situation of our "one world" by taking a global business economics viewpoint: Let us regard all the worlds "monetarized economies" as being one large company. Streets, schools, universities, natural resources, production capabilities etc. are the companies' basis to create added value. The world GDP (gross domestic product) defines these companies' overall earnings, its turnover. Currently our world company has almost about 400 million employees. The owners and creditors of the company are rich elites, but for example live insurance- and pension funds or all other kind of institutional investors as well, representing roughly some 800 million further people. These people own all the worlds' financial fortune, intended to finance their (autumn of) live, to get a share in added value. There are today about 5,6 billion people outside the regarded world company!

What happened with this world company the last 40 years? The growth of the companies' debt was all the time higher than the growth of all earnings – the growth of GDP. This has led to the current situation that the overall debt is more than four times the worlds GDP.

What is a debt? Debts – as liabilities – are leverage money. And all leverage money represents (indirectly) promises on added value at some time in the future. And what are interests to be paid? Interests are as well promises on added value. Since interest payments (and dividend payments) grow when the total amount of leverage money grows, a growing share off our world companies' earnings have to be used to cover these payment obligations. This sets the company under high and continuous pressure to reduce costs. The basis for creating added value has thus being reduced and the total sum of wages has been reduced. But this reduces the companies´ potential to create added value. How could then all promises on added value in the future be fulfilled? For some time this "added value gap" has been bridged by more and more public debt – by leverage money – leading to the current dramatic situation of public finance and the financial crisis.

That's why any kind of financing approach for stability, public intervention and a "Grand Design" for balanced economical, ecological and social participation (e.g. a "Global New Deal"), any financing approach that would lead to further indebtedness (which would increase the overall amount of leverage money) can't be a reasonable way out of the disaster.

Instead the system has to be deleveraged "with care" and at the same time assure the 5,6 billion people currently outside to participate fairly by expanding their basis to create added value.

3. Taxing leverage and risk taking

The system has to be deleveraged fairly and balancing!

This could be reached by those adding risk to the system by creating leverage money – a financial product – paying a special financial market tax – a leverage money tax (which would be a product oriented levy, not a transaction tax!). The tax rates could be fixed following the "ability-to-pay-principle". Powerful market participants, usually paying low interest on credits granted to them, should pay higher tax rates than weaker participants that usually have to pay higher interest. This would

- dampen speculative investments,
- stabilize the financial system,
- be an innovative financing instrument.

A leverage money tax of 1 % on average would raise public financial means of 1.000 – 2.000 billion $ a year. If – in addition to that – harmonization of the national assessment bases for taxation is reached, another 1.000 – 2.000 billion $ a year could be raised. These means could give us access to the needed "double dividend" of a) stabilizing the financial crisis and b) providing global funds to co-finance a Global New Deal: The implementation of social and environmental standards as mandatory process and production standards within the WTO!

Then all has to be and will be build up what is needed that the processes to create added value are conforming to all those required environmental and social standards. And if those standards are mandatory WTO-Standards, the WTO will definitively ensure that all processes of creating added value worldwide – and the implementation process itself – do not overshoot our planets environmental capacity. And at the same time it would give a chance for a growth in value added that would have the potential that all promises on added value in the future could be fulfilled. It would be the chance to deleverage the system without harm.

4. A seven point plan

The current world crisis provides a **unique chance** to make a first important step towards a global eco-social market economy, if a pragmatic approach is chosen to solve the complex of problems as a whole. This "7-point plan" to face the global crisis is sketched out in the following:
The financial system is burdened with risk by global actors performing high leveraged business and used to avoid paying appropriate taxes. The principle of tax justice and fairness is turned upside down. Many financial means could be pursued, which do not further burden national budgets or the middle class, if one pushes for harmonization of the tax bases. A leverage money tax would be a reasonable and first step into this direction and a source of innovative financing. We urgently need enough financial

means to ensure that the important eco-social regulations gain acceptance and are implemented in international agreements. Only then will the, for the most part, correctly functioning, though better said, still correctly functioning national social democracies, have an actual chance to survive the process of globalization.
What are the most important cornerstones for this pragmatic and goal-oriented political solution?

1. **Environmental standards**: The window is open to realize a "cap and trade" approach within current negotiations that are in accordance with the Kyoto Protocol and based on equal emission rights per-capital, e.g., the principle of climate justice.

2. **Social standards**: All nation states have agreed upon the basic standards of the ILO that are nevertheless, just as environmental standards, currently being undermined by the framework of the WTO. Child labor and environmental polluting still constitute a competitive advantage in global markets.

3. **World Economy**: Preventing a worldwide recession must entail more than a debt-financed eco-social economic stimulus! Public investments into new energies and environment technologies, education and infrastructure should be part of an implementation process that expands and harmonizes environmental and social standards (as well as its institutional prerequisites). These **process and production standards** must be declared binding within the **WTO**. Only then will there be no more ecological and social dumping for maximization of profit and the global market will become an eco-social market.

4. **Global contract**: How can the full "deal" be agreed upon? The answer is co-financing. For how long have EU countries already benefited from co-financing? New member countries receive funds and in turn they are better able to implement community laws (the Acquis Communautaire). Such an action on a more global scale is the key – **the co-financing of standards**.

5. **Financing**: Where do the means for co-financing come from? The answer: reform of the finance and **tax systems.** The tax systems must also be adjusted. For only through a harmonization of the tax bases can tax evasions be globally stopped effectively.

6. **Balance**: Moreover, to finance implementation and balance processes, funds should be collected through an added value-type tax on all financial products to shore up the speculative leverage businesses as well as to raise funds for balancing processes: A **Leverage Money Tax** would oblige biggest profiteers to pay their fair share and not exclusively place the burden on the middle class and others, who are already handicapped. As compared to the capacities of financial institutions, individuals can not buy in bundles and are thus subject to the higher interest that must be paid for granted credits (a financial product). The profiteers should therefore have a higher tax placed on their "leverage money", e.g., their credits for leveraged investments and speculations. Economically, the less capable actors, such as the middle class, should not be burdened. Through the leverage money tax, a fair tax would be formed that makes that “super bubble” (the money bubble) containable.

7. **Monetary crisis**: Short-termed liquidity bottlenecks as a driver of the global financial crisis including its effects on the real economy must be removed. Central bank money must "circulate" again. To do this the liquidity reserve holding of the financial market actors must be limited. An effective means would be through specifications of a **maximum permissible reserve ratio**. "Surplus" liquidity would then be made available through a "**liquidity circulating fund**".

Details can be found in:

Dirk Solte (2009)
"Global financial system in balance – crisis as opportunity for a sustainable future",
ISBN 978-3-9811715-5-6, Terra Media Verlag, Berlin.

The concept of a leverage money tax has been introduced in the book:
Dirk Solte (2007)
"Weltfinanzsystem am Limit – Einblicke in den "Heiligen Gral" der Globalisierung"
(World financial system at its limits – insights to the „Holy Grail" of globalization)
ISBN 978-3-9811715-2-5, Terra Media Verlag, Berlin

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