# DECELERATION OF FOREIGN EXCHANGE MARKET: TOBIN TAX AND IMPLEMENTATION

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**Abstract**

Since the collapse of Bretton Woods regime in 1970s, the growth of foreign exchange transactions have become overrun. Numerous amount of money has been invested on foreign currency speculative trade. However, such high level of speculation has caused market volatility and turned into one of the igniter of global economic crises. A Nobel Prize economist, James Tobin, then generated the conceptual regime to tax each speculative foreign transaction. This paper will not only provide the background of foreign transactions and the speculation but also illustrate pros and cons of "Tobin Tax" system including the analysis of its plausible implementation.

**Keywords:** James Tobin, Tobin Tax, Speculative Transactions, Global Financial Crises, Foreign Exchange Market, Currency Speculations, Foreign Exchange Transaction Tax

**บทคัดย่อ**

นับตั้งแต่การล่มสลายของระบบการเงินแบบเบร็ตตัน วูดส์ ในช่วงปี ๑๙๗๐ เป็นต้นมา การเติบโตของการแลกเปลี่ยนเงินตราต่างประเทศก็ตกอยู่ในสภาวะระส่ำระสาย มีการนำเงินเป็นจำนวนมากไปใช้ในการลงทุนเก็งกำไรกับอัตราแลกเปลี่ยน อย่างไรก็ตาม ระดับของการเก็งกำไรที่สูงเช่นนั้นก็ส่งผลให้ตลาดเงินตราเกิดความผันผวนและเป็นหนึ่งในชนวนเหตุที่ทำให้เกิดวิกฤตเศรษฐกิจลุกลามไปทั่วโลก ดังนั้น เจมส์ โทบิน ซึ่งเป็นผู้ได้รับรางวัลโนเบลสาขาเศรษฐศาสตร์ จึงได้เสนอกรอบมาตรการให้มีการจัดเก็บภาษีกับธุรกรรมการแลกเปลี่ยนเงินตราในทุก ๆ ธุรกรรมที่มีลักษณะของการเก็งกำไร บทความนี้นอกจากจะนำเสนอถึงปูมหลังของธุรกรรมการแลกเปลี่ยนเงินตราและการเก็งกำไรกับการแลกเปลี่ยนเงินตราต่างประเทศแล้ว ยังกล่าวถึงข้อดีและข้อเสียของระบบ "ภาษีโทบิน" รวมทั้งการวิเคราะห์การนำระบบภาษีดังกล่าวไปปฏิบัติด้วย

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## INTRODUCTION

After the breakdown of the Bretton Woods system in 1973, foreign exchange transactions have tremendously proliferated. Every day, approximately U.S. $1.2 trillion is currently merchandised on the global foreign currency market.[1] Warnings from many critics assert that an unacceptable level of market volatility resulted from chaotic speculation in the currency markets is one of the most influential factors which caused serious economic problems.[2]

Measure of Taxing 1% on each foreign exchange transactions was initially proposed in 1972 by James Tobin, an American economist, which is later globally recognized as "Tobin tax". He believed that this compulsory measure would at least temporize the monetary volatility that prevails financial markets at present. In the last twenty-five years, the debate over suitability and feasibility to implement Tobin Tax has been elevated by various policy makers and economists. The attraction of Tobin Tax is considerably increased, thanks to many recent and remarkable aftermaths such as European Exchange Rate Mechanism (ERM) crises, the Mexican peso devaluation, and the Asian currency crisis. It is also viewed as a tool to reduce market volatility and strengthen the executive power of national government on supervising its domestic economy.

This paper will begin providing the background of foreign exchange transaction and how currency speculation occurs. Then there will be some discussion about the Tobin Tax regime including its advantages and drawbacks. Finally, the implementation of Tobin Tax will be analyzed.

## BACKGROUND OF FOREIGN EXCHANGE TRANSACTION

In history, the primary value of money was tied with basic form of valuable object like gold. The risk of transaction costs and security of using valuable materials as instrument of trade influenced individuals to create paper note as a substitutable way for transaction.[3] Since they were used as promissory notes to pay the bearer a fixed amount on presentation, actual value was not necessary for these pieces of paper. Private bankers were among the first group who issued such notes. Later, the paper issuance was followed by public sectors.[4] From time to time, note issuers began to attach these notes to a fixed amount of gold which is also known as "mint parity".[5] For example, during the Bretton Woods system, one thirty-fifth of an ounce of gold was set as equivalent to one U.S. dollar, by U.S. government.[6] Due to this policy, U.S. government would trade one thirty-fifth of an ounce of gold with anyone who held a dollar bill. This system of exchanging paper bill for gold is also known as the "gold system".[7]

The modern gold standard is aged for almost two hundred years since the United Kingdom started implementing actual gold standard in the eighteenth century. The commencement of fixed foreign exchange rates was labeled by the gold standard. Because of the equality between exchange rate of each currencies and the ratio of their mint parities, the exchange rates of currencies on the gold standard had been fixed with other gold standard currencies.[8] Therefore, fixed exchange rates were created as a natural result of gold convertibility. When the First World War emerged, most countries suspended the dealing in foreign money on their currencies and

thus ceased the gold standard ideology.[9]

In the middle of the World War I interval, not only the policy on imposing large reparation payments on Germany had been discussed, there was also an agreement among Allied powers on the framework of the post-war international economic system. They concurred with the notion of "competitive devaluation" by imposing highly restrictive tariffs to bar foreign imports and international engagements. As a consequence of these coercive policies, the international trade and monetary system collapsed and scaled down world trade for sixty percent between 1929 and 1932. Because of the breakdown of the international economic order and political instability as domino effect, the conservative extremist groups took an advantage of public tension arisen from economic and political vulnerability as a radical campaign to attack the existing capitalistic dominion.[10]

Hence, after the Second World War, the Allied powers comprehended together that coercive economic policy that was arranged in the repercussion of the First World War was an administrative failure. The close relation between economic instability that impelled the rise of fascism and the occurrence of World War II was believed to be substantive origin of the chaotic conflict among nations. When the war nearly ended in 1944, forty-four Allied countries appointed the delegates to attend the conference arranged in Bretton Woods, New Hampshire with the purpose of establishing a post-war economic regime. The foundation of the International Bank for Reconstruction and Development (World Bank), and the International Monetary Fund (IMF) was the conclusion of such assembly.[11]

Currently, 187 countries have joined the IMF as member nations in the organization. IMF's mission includes promoting global monetary cooperation, ensuring financial stability, facilitate international trade, promote high employment and sustainable economic growth, and reduce poverty.[12] The IMF's General Reserve Account (GRA) is established for collecting a subscription of gold and currency paid by each member.[13] The relative economic status of each member country will designate their subscription rates. Therefore, the GRA got more financial subsidy from affluent countries than from indigent ones. Then, voting rights were allocated to each member states in accordance with their amount subscriptions. In addition, eligibility for IMF loans and allowance for borrowing from IMF were the obtainable privileges which the enrolling countries could enjoy if they wanted to advantage their short-term reserve deficits when their treasury contained insufficient amount of U.S. dollar, causing failure to keep their currency at its pegged exchange rate.[14]

Bretton Woods system at that time relied on the U.S. dollar as its main instrument. An agreement among member states on establishment of a par value for their currency connected to the U.S. dollar was made. They also created a commitment to hold their currency exchange rate within 1% of the par value.[15]

It was around twenty five years that exchange rate remained stable due to the Bretton Woods system of fixed exchange rates. Nevertheless, the downfall of the economic status of the United States created uncertainty on the system among member states. Ultimately, in 1971, representatives from the powerful economic regions considered the proposal of restoring fixed currency parities. The Smithsonian Agreement was then con-

cluded as an equipment to respond to such purpose. By virtue of the Agreement, it did not only depreciate the U.S. dollars by 10% but, by increasing the bandwidth of the floating rates, it also allowed currency to float from 1% to 2.25%. The Smithsonian Agreement was not deemed to be a long-termed strategic plan but it was never renovated. One and a half year later, speculators attacked the U.S. dollar, and even 10% devaluation was not enough to maintain its reasonable range.[16] Therefore, many countries began to launch free floating currency regime. By 1973, free-floating format conquered all main currencies, thus resulting in the collapse of the fixed exchange rates, the mainstay of the Bretton Woods system.

Presently, almost all the major currencies applied free floating system to their currencies whose value is designated neither by governments nor an international organization but by the market[17]. The value of a currency involving other currencies is raised by increase of demand for that currency. On the contrary, a currency is devalued when demand for that currency declines. In brief, "a floating exchange rate is determined by the private market through supply and demand".[18] Trade and investment are among the most influential factors that can illustrate the supply and demand for a state's currencies.[19]

Consequently, the noticeable growth of the demand for a nation's currency will exist when goods and investments from that country are increasingly in demand, causing the accretion of demand for that country's currency. An increase in the value of that nation's currency compared to other currencies is an outcome of such incidence. However, uncertainty still dominates this principle especially in the area of short run foreign currency market. It is very difficult to forecast or explain exchange rate fluctuations, due to many factors, which are also known as "market distortion".[20]

The scale of speculative transactions which has become more widespread since the floating rate system plays a major role in the world monetary system affects the distortion of the foreign currencies market. In a floating rate system, investors can simply bet on the market in the short run because the value of currencies is constantly changing.[21] Global currency transactions trade is massively inflated due to this type of speculation.[22] Statically, after the Bretton Woods system has reached its downfall, which ends the fixed rate system era, there is significant growth of merchantability of foreign currency exchange transaction as mentioned above. $1.23 trillion is estimated to be the value of transactions which are traded per day.[23]

Moreover, eighty-two percents of these transactions, according to the Federal Reserve, are not used to finance international trade and investments; instead, they are mainly used for speculation. In addition, an assessment from the Bank for International Settlements illustrates the domination of "roundtrips" over the majority of these transactions.[24] Roundtrips denote a transaction in which a holder of one currency sells it for another, and then later resells that new currency for an equivalent amount of the old. This high amount of short, round-trip transaction suggests that many transactions are speculative in general.[25]

## PROBLEMS CONCERNING SPECULATIVE TRANSACTIONS

"Speculative bubbles" is the theory asserted by some economic scholars in order to explain the distorted market rate with basic economic essentials.[26] Expectation of currency traders will control the value of a currency in a speculative bubble. If currency traders expect higher price of a currency, the value of such currency will increase. However, the true value of a currency will become more illusive as price of such currency keeps rising. The bubble can overwhelm a currency when a speculative bubble commences. Under this circumstance, traders' aspects tend to be against selling the currency they are possessing although they know that a currency is overvalued. This is because of their expectation for selling it at higher price in future.[27] The psychological trend among the traders is that demand for the currency will remain rising and its value is going to be worth more. Then, although they are literally independent to make their choices, they assume that if they have an attempt to go for other alternative decisions, they will suffer from loss of money. Therefore, when numbers of investors are cemented in these speculative bubbles, the market itself must face difficulty for going back to the right track because most traders cannot resist the market trend.[28]

Market volatility is the crucial result of this "bubbles". The dramatic increase of exchange rate volatility due to the domination of floating system[29] has been featured by some commentators as "excessively volatile". It was almost impossible for any scholars in the 1950s and 1960s to expect the level of such enormous fluctuation in the value of currencies being traded during past few decades. One of the most worrying aspects of this volatility is that these fluctuations seemingly have no basis in market fundamentals.[30]

Market instability and difficulty of designing economic plan are the instant outcome of this volatility due to the unpredictability of main future exchange rate. Generally, for investors who hold foreign assets and liabilities, predictable exchange rates are necessary for them in order that they can participate in profitable economic planning. For example, suppose a Japanese car manufacturer, who wanted to invest in U.S., does not know what the yen to dollar exchange rate will be in six months, much less in six years, it is very difficult to expect the success of the investment in an American manufacturing plant.[31] In addition, risk of foreign exchange resulted from volatile markets can cause diversion of resource usage; far remote from production to hedging instruments. It also bars any business entities from getting together in a productive venture.[32]

Volatile exchange rates can dangerously affect the entire economies including on a macroeconomic level. In 1994, Paul Volker, the chairperson of the Bretton Woods Commission, stated the following remark in its report:

> "Since the early 1970s, long-term growth in the major industrial countries has been cut in half, from about 5 percent to 2.5 percent a year. Although many factors contributed to this decline in different countries at different times, low growth has been an international problem, and the loss of exchange rate discipline has played a part".[33]

Moreover, wide spreading currency crises can be stimulated by volatility in the glo-

bal currency markets. A financial market which is indubitably fluid and innovatively fluctuating can bring about "speculative onslaughts". According to some writers, this kind of predatory investments committed by greedy speculators shall be held responsible for several financial crises. Instead of blaming a country's economic impotence as the root of currency crises, some observers maintain that "self-fulfilling" speculative attacks can be potential sources of many crises. Therefore, although a country's economy is basically healthy, once speculators monetarily assault a currency of that country, it becomes the market trend followed by others and launches a real economic crisis.

One of the most prominent and notable crises which can tangibly exemplify the peril of currency speculative manipulation is when the Thai Baht were under attack which ignited the 1997 Asian Currency Crisis. The unprepared encounter with the massive invasion compulsorily pressured the Thai government to depreciate the baht by eighteen percent on July 2, 1997. Eventually, the crisis rapidly and spreadingly overwhelmed across Southeast Asia following the devaluation of the baht in Thailand. The next casualty is the Philippines where her peso was the next to be under financial constraint and devaluation of peso seemed to be the inevitable solution for the Philippines as well. Afterward, the Malaysian ringgit was the next target of currency speculators, where approximately U.S. $1 billion was vainly spent by the central bank to defend the ringgit prior to its fallen to a thirty-three month low. Last but not least, currency speculators turned their muzzle to Indonesian rupiah. The rupiah was beforehand permitted to float in limited range by Indonesian central bank so as to foster currency stability. Nonetheless, overcome by outer and inner pressure, Bank Indonesia extended the controlled range from 8% to 12%, yet it failed to restrain the fall of rupiah. In order to maintain stability of the currency, 1.4 billion U.S. $ was spent by the Indonesian central bank. Unfortunately, the attempt to defend the currency became a total failure, and later on August 14, 1997, Bank Indonesian removed the intervention bands and authorized the rupiah to float without control. As a result, its value had dropped at an additional 20% within a month. The speculative attack also affected even countries with sturdy economy such as Singapore and Hong Kong. This critical situation opened the way for IMF to activate the safeguards which was used to be instituted after the Mexican currency crisis in 1995. One of the most important actions was the GAB[34]. During such cumbersome stage, 121 billion of U.S. $ had been pledgingly credited to the Philippines, Thailand, Indonesian, and South Korea. Although this IMF urgent allowance was claimed to be a success, IMF was intensely criticized on its defensive response to this economic crisis.[35]

In order to obtain a loan from IMF, a concordance between a member country and the IMF on a mandatory program of national economic policy must be made. IMF lending requires undertakings of certain policy actions from a country as its commitments. This is a design to secure that the resolve of funds' using will be maintained to untangle the balance of payments problems. Doing these would also lead to restoration and creation of pathway to assistance from other financial providers. Once the economic and financial status of the country has returned to normal, the repayment to IMF is made, making other members available to the funds.[36] In addi-

tion, the grantee state is required to initiate economic regulatory agenda that mainly focuses on budget cut and raise of tax and interest rates, which is so-called "IMF Conditionality". Some scholars contend that these kinds of burdensome programs do not facilitate the country as a whole; instead, the common citizens of the recipient countries are subjected to suffer from these programs for the recovery of a minority group of foreign investors. Particularly, their argument concentrates on the distorted conceptualization that the grant of IMF bailouts tends to guard the foreign investors against their risky loan, instead of serving local people. This is because the main theme of utilization of IMF funds of borrowing countries is mainly to avoid default on loans, not to help their own citizens.

During post-Asian crisis, the idea of international financial reformation has been widely acknowledged. The scheme to "adapt the international financial architecture to the twenty-first century" has been mentioned by U.S. president Bill Clinton and "a new Bretton Woods for the new millennium" has become a quote from British Prime Minister Tony Blair. Alan Greenspan, Chairman of the U.S. Federal Reserve, has also pointed that change is needed for the global financial system. A number of authorities have even urged that Bretton Woods-type system of fixed exchange rates should be resurrected or that a global central bank and a global currency should be established. The indication of the need for the international financial system reformation even comes from the one who was believed to gain tremendous benefit from the volatility of the existent system, George Soros. However, although the problems of the existing international financial system are recognized and the reformation of the regime seems to be concurrently agreed to be implemented, the solutions of such missions are still widely debatable.

## THE TOBIN TAX AND ITS PURPOSES

In the 1970s, a notable monetary expert, economist and Nobel Laureate, James Tobin, suggested an idea of taxing on foreign exchange transactions with the following concepts:

"1. The tax would be applied at a uniform ad valorem rate by, at the least, all the key currency countries.
2. It would be administered and collected by each government on all payments by residents within its jurisdiction that involved a spot currency exchange, including, as the case of Eurocurrency transactions, exchange that do not involve the home currency.
3. The proceeds from the tax would be paid into a central fund control by the IMF or the World Bank.
4. Subject perhaps to prior IMF consent, countries could form currency areas within which the tax would not apply. That is, small countries that formally tied their currency to a key currency would not be required to levy the tax on intra-area currency exchange."[37]

The principal goal of Tobin Tax was that speculative races on the major world currencies, which were a partial cause of the downfall of Bretton Woods fixed exchange rate system in the early 1970 and many crises af-

ter, shall be discouraged. Tobin asserted that the runs on speculation were negatively affecting the world economy. Their impact ignited the increase of the exchange rate volatility among the key world currencies, which inevitably became the hindrance of international trade and obstructed the stream of foreign direct investment. More significantly, Tobin stated that the effect of the runs could deter the state authorities from enforcing policies, which aimed to benefit the whole society by longer-term payoffs, without fearful perception of sudden unfriendly backlashes of the financial markets.[38]

To "throw some sand in the well-greased wheels" of the global financial market mechanism and to enhance the mitigation of the domination of speculation over merchantability, according to Tobin's phrase, were the main functions of the Tax. This would work because a one-percent transactions tax, as preliminarily recommended by Tobin, would directly decrease the benefit which speculators normally gain from currency speculation, due to the involvement of "short-term financial round-trip excursions into another currency"[39] with the expectation of gain from each rapid circulation generally an insignificant portion of the majority of borrowed funds put in progress. On the other hand, monetary transactions with higher or longer expectation of profits and with more stability of investment, such as trade of goods and services or foreign direct investment would not be much impacted by the tax. More importantly, since currency speculators were tied up with the tax burden and less exchange volatility to be taken advantage from, they would be vitally defeated, while genuine commodity traders and investors with long-range goal would enjoy more trustable exchange rates as a trade-off for their tax bite.[40]

## TOBIN TAX ADOPTION AND ITS EXPECTED ADVANTAGEOUS OUTCOME

As initially framed by Tobin, 1% of tax on every there-and-back currency transaction shall be levied and the world financial realm would be benefited. This would result in, which is the most important, and the main objective of the Tax, the declination of speculative activity and the deterioration of currency speculation, awakening the rise of foreign exchange market stability.[41]

The reduction of currency speculation was not the only one of the most plausible goals of all the Tax's purported benefits. Moreover, since enforcement of the Tax levy requires speculators, in order to remain profitable, to pay additional rates for each of their bets. Therefore, it will decrease the incentive of this kind of high-return-gamble-alike investments which used to frequently occur among speculators. This phenomenon will then gradually exile most speculators out of world financial empire.[42]

To be more illustrative, the positive outcome of the enforcement of the tax can be exemplified. Suppose ten percent is an interest rate of a given home country and 12 months is investment horizon of a given investor, while one percent is a Tobin Tax rate that is imposed on each roundtrip transactions. As a consequence, in order to make the investment worthy, an investor will have to gain an eleven percent (.11/.99) for reciprocation. Nevertheless, things would become more obvious if the investment horizon were decreased to 1/12 of the year or one month.

As a result, in order to make the investment profitable, investors' compulsorily required return for the investment would apparently jump to twenty-two percent. Definitely, once only one week (1/52 of the year), became the period of investment horizon, the satisfactory rate of return for our model oversea investors would undoubtedly escalate to sixty-two percent. This concept demonstrates that investors with repetitive volatile investing can be heavily penalized at a stunning level by the tax, even at the rates of 1% or less. Furthermore, according to this framework, if the levy rate of the Tax was 0.1% with one day of investment horizon, investing under such condition would not be attractive for investors at all unless their expectable yield was set at 46.5%. Thanks to the factual presumption that, of all foreign transactions, eighty percent is the amount of foreign exchange transactions that occur in seven days or less, then it is foreseeable that the balk of speculative mobility could be seemingly diminished by triggering of this short-term tax; even at the humble rate of 0.1%. Theoretically speaking, the efficiency of the Tax in diminishing speculation and shortening the obese volatility of the market could be upheld.[43]

The next empirical advantage of the Tobin Tax, in addition, is that long-term investment will not or scarcely be impacted by the Tax. In consequence, as the delay of short-term currency speculation trading portion is deliberately maximized, the operation of what has been left in the market remains practically untied from any distortion.[44]

There are other foreseeable betterments of Tobin Tax. One of the most obvious enhancements is the potentiality to collect a considerable amount of gain. Although the tax was originally perceived by Tobin as a mechanism to promote constructive stability in the currency market, the elemental byproduct of the tax, its tax proceeds, is irresistibly adorable. Not only the tax proceeds that become the outgrowth, but also the international societies' perception toward this highly disputatious tax. Even though taxes are always considered by some analysts and scholars as inherent unfavorable factors, there are groups of experts who still insist that national policies of developing countries desirably accept "reasonable" taxes as their components. In addition, an amount of critics similarly maintain that in the aspect of imposing taxes as incentives for encouraging investment, the existence of domestic taxes will cause little or no influence to the executive-level management of the corporate entities whose long-term projects are their favorite.[45]

## THE CASE AGAINST TOBIN TAX

If every coin has two sides, Tobin Tax is not the exception. Not different from other collaborative international initiation, a number of developed nations, particularly the United States, become the loudest oppositions of the Tobin Tax. They oppose that imposing a tax on foreign transaction price will deteriorate the incentive of investment. Tobin Tax is also countered that it will cause negative impact on the foreign exchange market itself. An example of this is that the tax may possibly destabilize the economic balance by getting stuck in the difficulty to differentiate stable, longstanding financial transactions from sloppy, short standing speculative transactions. The argument that the tax will intervene the market and makes it become less efficient, is also asserted by some critics. Nev-

ertheless, the pro-Tobin insists that the foreign exchange merchandise nowadays is not stanchly constructive. Therefore, a development of exchange rate stability would be advantageous for it, thanks to the aftermath of the implementation of the Tobin Tax. An explanation asserted by a commentator points out that after implementation of the Tobin Tax, the determination of exchange rates will still be driven by the market. The role of the Tax is only to increase the efficiency of the exchange rate determination.[46]

Another inevitable and problematic obstacle is enforceability. Let's assume that the implementation of Tobin Tax was occurred at an international forum, then which international institutions should be responsible for monitoring international currency transactions? Capabilities of such organization to evaluate and collect the tax, including its efficiency are also still doubtful. In addition, due to domination of hi-technology in motivating the market of foreign exchange transactions, an establishment of any innovative international mechanisms or a renovation of a current one would not be either facile or low-priced. Each nation, on the other hand, may be able to domestically establish or found the national tax-collecting system and transfer the outcomes to international level for further allocation. With this gateway, however, there are three radical confrontations to undertake. First, since attracting investors, who are willing to enjoy tax haven, is inescapable, countries will bear a weak encouragement to abide by an international agreement regulating the tax. Second, suppose countries do follow the agreement, what international entity should be accountable to obligate the countries' burden to accumulate tax proceeds and what should be the facilitative procedure to do so? Finally, spots where currency transactions are dealt are always various, thus, worldwide enforcement becomes a difficult or even impossible mission.

International cooperation is also essential for implementation of Tobin Tax. This becomes another barrier that may occur along the path of seeking for mutual agreement among international community. The imposition of the tax on international currency transactions requires universal agreements on the terms and conditions of the tax. Since only a few countries and currencies are forums and mediums that most currency transactions are transacted, the tax would paradoxically induce countries to delay acceptation on any international agreements enforcing it. In illustration, if the adoption of an international agreement on the Tobin Tax was widely materialized, most currency traders would tend to be attracted by markets that refrained from imposing the tax; therefore, countries that exempted themselves from the terms of the agreement would be, ridiculously speaking, rewarded.[47]

Problems regarding enforcement could come up in case that a single agreement was to be endorsed by all countries. In reality, the trade of foreign exchange in most countries of this world is already taken place on street corners, in markets that are colored by variety of gray and black shades. For taxing at minimal rates on large transactions, which is the principle of Tobin tax, street corners would not be much impacted.[48]

Some academicians have given advice supporting the use of the automated systems in brokering and in direct interdealer trading, which are becoming more well-known. They asserted that such usage could simplify the tax collection. If the solution of problems of

international agreement could be praticalized, it is reasonable to think that enforcement would be easier for financial transaction taxes compared with an income tax.[49]

## CASE STUDIES FROM COUNTRIES' PRACTICES

The application of taxes and restrictions on capital inflow and outflows, which contains some of the features of Tobin Tax, was implemented by several countries such as some Latin American nations and East Asia. The competency of taxes and manipulations on stream of capital, from the perspective of revenue-raising aptitude, has not been methodically scrutinized. However, in the viewpoint of currency instability, liberality of macroeconomic policy and admissibility of the exchange rate system, such measures have made tangible outcomes, proven by evidence. The Korean administrative has exercised such actions to impose limitation on the flowing activity of the won with purposes to prevent destabilization of exchange sway caused by Korean exporters and to block the accretion of an undesirably bulky external debt load. Chilean authorities have stipulated the limitation on capital inflow to shield the economy from destabilization which was sensitive to arising markets. The influence from these measures yielded the combined capital inflows into multiple countries in Latin American. Compared to the countries where such restrictions were not in place, the nations that restrictively regulated their accessibility to foreign capital market were able to withstand the "tequila shock"[50] of early 1995 less ruggedly.

Japan has also possessed a prolonged experience of securities transaction taxes (有価証券取引税) since 1953.[51] Adjustment has been imposed many times on these taxes for years. They mostly occurred together with the imposition of arrangements on capital gains taxation rates. An expert also analyzed the aftermath of economic conditions affected by the adjustments of stock transaction taxes in various economies which include Japan as well as Hong Kong, Korea and Taiwan. Inconclusiveness was generally bestowed in the study which illustrated that "[o]n average, an increase in tax rate reduces the stock price but has no significant effect on market volatility and market turnover … Overall, the evidence is not consistent with the hypothesis that stock transaction tax can reduce noise trading and volatility". In brief, reduction of market volatility does not appear to be effectively achieved by adjusting transaction costs.[52]

It is also discovered by other scholars that the significant increase of tax revenues was accomplished by Japanese security transaction taxes, partly in short term… "the [tax] generated 4.2% of government general account revenue in Japan in 1988. However, by 1993 this share fell back to 0.96% as most of the speculative trading moved to the trading floors in much less-taxed locations".[53]

In addition, when Japanese security transaction taxes were reduced in 1989, the impact of such reduction was studied by conducting an analysis over the performance of equities contained in the list of the Tokyo Stock Exchange. It revealed that "significant decreases in estimates of the first-order autocorrelation in returns for Japanese stocks listed in Japan, but no changes for Japanese stocks dually listed in the United States as American Depository Receipts (ADRs),

which were not subject to the tax law change. We also find lower price basis between the ADRs and their underlying Japanese stocks. These results are consistent with the hypothesis that a reduction in transaction costs improves the efficiency of the price discovery process". The attribution of this outcome leads to the fact that the activity and higher speed rate of absorption of market data into stock prices are boosted and facilitated by reduced transaction costs.[54]

## PLAUSIBLE AVENUES FOR THE IMPLEMENTATION OF TOBIN TAX

Scholars and stakeholders remark some approaches which are capable of implementing Tobin Tax. One method would be to found an international organization to support implementation and enforcement of the tax on international arena. Most of currency transactions which were subject to assessment of Tobin normally occur within a limited number of industrialized nations. Since stabilization of the foreign exchange is the aim of the tax, its outcome would stimulate the transfer of wealth from restrictively enriched economies of industrialized countries to broader international commonality for further function coping with problems that become world agenda, such as poverty. Consequently, using an international organization as a tool to implement Tobin Tax would enhance emblematical consistency with the impact of the tax because it would lead all countries to not only requirement of international correlations but also representation of economic interdependence.[55]

Numerous avails could be boosted by this approach. When homogeneous implementation would be harmoniously proceeded by an international organization, as a result, it would guarantee that each member nations would be equally treated and potentialize the motivation of many countries to cooperate more in the implementation of the tax. Furthermore, the broader well-founded organizational enforcement and dispute settlement instruments could be utilized by an organization operating under the supervisions of notable international bodies, such as the United Nations or the World Bank. Even though Tobin Tax apostles traditionally appreciate this approach, its plausibility to acquire approval and cooperation from international community is inevitably under impervious obstacle. Furthermore, not only its failure to develop a solution for enforceability has increased the difficulty for practicable implementation, it also demonstrates the uncertainty of placing responsibility to specific organizations for unraveling the enforceability hardship.

Another advisable approach, instead, focuses on administration of national tax system to domestically implement the tax. This track could be got through by innovatively systemizing national taxation and banking regime, tracing any financial transaction which contains international linkage. Effective assessment and collection would then become the aftermath. Later, governmental procedure shall be the mechanism for further contribution of the proceeds to international entities whose mission is to productively manage the fund. Convincingly, countries which mean to participate in this coordination would be likely to follow this path if they walk into the entrance of a multilateral agreement together with other affiliating countries because unilateral imposition of the tax could engage them into a competitively disadvantageous situation. Consequently, entering into a binding agree-

ment by a country for imposing the tax on herself would not likely be possible unless it is assured by other countries that they will also be impartially bound under the same measures regarding the imposition of the tax within their territorial foreign exchange trading arena. In addition, assessment and collection of tax proceeds may be functioned in various channels. For example, the final proceeds can be deducted in order to fulfill the contribution to the international organization "by the administrative costs incurred by the national government in implementing the tax".[56] Countries may possibly expose an anxiety that, with an exclusion of a multilateral agreement in which equal burdens bind all of the parties, more favorable treatment will be veiled on some countries than others.

Domesticalization of Tobin Tax implementation process also comprises of other advantages. Since implementing the tax regime at domestic level mainly relies on institutional mechanisms that are already established, such approach would be more economical than newly establishing of an international organization. This would also increase more effectiveness as a result of making use of countries' own existing expertise, knowledge and other technical tools that they have already become acquainted with. For that reason, manageability of assessment and collection of the tax would be more convenient, leading to the lower possibility rate of tax avoidance committed by investors who use derivative instruments. Moreover, requirement of the mutual agreement on international level for the implementation of the tax will decisively become unnecessary. However, although practicalization of domestic formula maybe more probable, some have raised an argument that practicing this approach will pose a risk for the reason that governments, as a sole implementer of the tax, may be reluctant to grant the tax proceeds to international institutions and tend to reserve the proceeds for their own sake. In order to minimize such riskiness, enforcement of a multilateral agreement which includes provisions governing administration of the tax and dispute settlement might be inevitably essential.

No matter which approaches countries choose to implement, participating in the multilateral agreements is compulsorily fundamental in which expression of definitive intention would likely be made by the parties. The tax imposer countries would be looking for confidence from stakeholders such as international institutions and other binding countries regarding their obligatory fulfillment under the agreement. On the other hand, international organizations which participate in the tax system would expect the obligations under the agreement to be fulfilled by member countries. Therefore, as a result, all relevant stakeholders which are participating countries and international organizations would seek proper use of the tax proceeds and appropriate distribution of the fund received by governments and organizations. At the finish line, accountable and enforceable propositions shall be executed by parties to the obligatory multilateral agreements. If the principal goal of the multilateral agreements leads to an establishment of an upper organization, responsible for distribution of the tax proceeds, a systematic dispute settlement tool of such organization shall also be consorted in the agreements.[57]

## Epilogue

The formation of the conventional inter-

national monetary regime was accidentally heaped rather than deliberately enrooted. Its flawlessness is widely and colossally questionable. Illustration of the international monetary system which has been presented during many crises has affirmed its vulnerability to congenital instability and practice of market falsification.[58] Therefore, the renowned proffer, Tobin Tax, was then proposed by a well-known economist, James Tobin, to stimulate the collection of tax on foreign currency transactions which he personified as "throwing sand" in the wheel of international finance[59], with an aspiration to decelerate distorting and craving transactions on the currency market committed by currency speculators. Finally, although the Tobin Tax may not be the healer-of-all of the global financial difficulty, its ability to initialize the development of more concrete global financial market cannot be overlooked.

## Endnotes

[1]Geoffrey G.B. Brow, *The Tobin Tax: Turning Soros into Plowshares?*, 9 Transnat'l L. & Contemp. Probs. 346, 1998).

[2]*Id.*

[3]*Id.* at 347.

[4]*Id.* at 348.

[5]*Id.*

[6]*Id.*

[7]*Id.*

[8]*Id.*

[9]*Id.* at 349.

[10]*Id.*

[11]Benjamin J. Cohen, Bretton Woods System, http://www.polsci.ucsb.edu/faculty/cohen/inpress/bretton.html.

[12]http://www.imf.org.

[13]Brow, *supra* note 2, at 350.

[14]*Id.*

[15]*Id.* at 351.

[16]*Id.* at 352.

[17]"In reality, many countries have a policy of having their treasury or central bank buys and sells currency when it believes it is necessary to do so to avoid extreme fluctuations in the exchange rate which would otherwise be created by the free market. This policy is known as a managed or dirty float". (*See* http://www.wisegeek.com/what-is-an-exchange-rate-regime.htm).

[18]http://www.investopedia.com/articles/03/020603.asp.

[19]http://www.gocurrency.com/currency-rates.htm.

[20]Brow, *supra* note 2, at 360.

[21]William R. White, *The Tobin Tax: A Solution to Today's International Monetary Instability?*, 1999 Colum. Bus. L. Rev. 368 (1999).

[22]Brow, *supra* note 2, at 361.

[23]White, *supra* note 22, at 365.

[24]*Id.* at 366.

[25]Brow, *supra* note 2, at 362.

[26]*Id.*

[27]http://financial-dictionary.thefreedictionary.com/Speculative+Bubble.

[28]*See* http://www.thetulipomania.com. In the Netherlands during 1600s, a tulip bulb could cost as equal as 12 acres of land.

[29]Brow, *supra* note 2, at 364.

[30]*Id.*

[31]*Id.* at 365.

[32]*Id.*

[33]White, supra note 22, at 367.

[34]The General Arrangement to Borrow (GAB) is credit arrangement made by the IMF and a bunch of member countries including some institutions. In brief, this is simply a stand-by additional fund that these member entities will lend their fund to IMF in case that IMF's main source of financing is not sufficient to fulfill member's needs. (*see* http://www.imf.org/external/np/exr/facts/gabnab.htm).

[35]White, *supra* note 22, at 374.

[36]http://www.imf.org/external/np/exr/facts/crises.htm.

[37]David Felix, *The Tobin Tax Proposal: Background, Issues and Prospects*, 1 (Dept. of Econ., Wash. U., Working Paper No. 191, 1994).

[38]*Id.* at 2.

[39]*Id.*

[40]*Id.*

[41]Amy Youngblood, *Saving the World One Currency at a Time: Implementing the Tobin Tax*, 80 Wash. U. L. Q. 399 (2002).

[42]*Id.*

[43]White, *supra* note 22, at 390.

[44]Youngblood, *supra* note 42, at 400.

[45]*Id.* at 401.

[46]*Id.* at 404.

[47]*Id.* at 405.

[48]Mahbubul Haq et al., The Tobin Tax: coping with financial volatility 67 (1996).

[49]*Id.*

[50]http://www.investopedia.com/terms/t/tequilaeffect.asp.

[51]河野 敏 [Satoshi Kawano],

[Trends and Future Outlook On Relating Tax Securities For Individual Investors], at 5, *available at* http://research-soken.or.jp/inform/gen21/03kawano.pdf.

[52]Steve Youngren & John W. Labuszewski, *Impact of Tobin Taxes*, (October 22, 2010) at 4, *available at* http://www.cmegroup.com/education/files/Tobin-Taxes.pdf.

[53]*Id.*

[54]*Id.*

[55]Youngblood, *supra* note 42, at 406.

[56]*Id.* at 408.

[57]*Id.* at 409.

[58]Brow, *supra* note 2, at 398.

[59]Ben Patterson & Mickal Galliano, *The Feasibility of an International "Tobin Tax"*, at 1, *working paper* for European Parliament, *available at* http://edz.bib.uni-mannheim.de/daten/edz-ma/ep/00/econ107_en.pdf.

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