Abstract

In this article we consider the issue of debt governance within the context of sustainable development and economic growth. Although a lot have been made towards improving global financial stability after the recent crisis, the risks remain high as new threats emerge, and the global financial system is still unable to respond to them adequately. Today the key forum to confront increasing risks and promote viable governance is a group of major economies - G20. It is G20 that has done important steps towards global stability, and is expected to take the initiative for further improvements. Having considered the banking regulation innovations from the perspective of financial security and inclusiveness, we come to conclusion that the system is not yet sufficiently sustainable. The other idea we come up with is that implementation of financial transaction tax as a tool to discourage excessive speculation without impeding other economic activities seems to be socially responsible measure working for financial stability at the same time. Finally, we also assume that steadily increasing governmental debt of the leading economies presents a serious challenge to global financial stability and to sustainable growth, and should be dealt with accordingly. Otherwise, the world economic system appears to become very fragile and unsustainable under the burden of financial imbalances and emerging risks.

Vladimir Zuev, Elena Ostrovskaya, Ekaterina Frolova[1]

Debt Governance and Sustainable Development Goals

Introduction

On September 25, 2015, world leaders of the 193 UN Member States adopted the 15-year program, entitled "Transforming Our World: 2030 Agenda for Sustainable Development", containing 17 Sustainable Development Goals (SDGs) and 169 targets[2]. In 2016 the G20, as a group of leading economies and a key forum to promote the SDG Agenda, adopted the G20 Action Plan on the 2030 Agenda for Sustainable Development, in which G20 members committed to contribute to its implementation through "collective and individual efforts, at home and abroad" with a "focus on sectors and themes of the Agenda where the G20 has comparative advantage and can add value as a global forum for economic cooperation".[3]

Since the start of the Agenda implementation, the G20 has placed global sustainable development at the center of its activities[4]. However, so far no country has achieved sustainable development in its economic, financial, social or environmental dimensions. The next few years will be critical for an early action on some selected areas of special relevance to reach the SDGs for the G20 countries. In this article, we want to treat the issue of financial stability as a key factor for the SDGs implementation.

The waves of financial instability are mounting all across the vast space on the ocean of the global economy. Which segment of the world economy will be the next one to confront a new financial tsunami and to which extent national and global regulators are ready to sustain the future shocks? Many new initiatives were launched recently to enforce the global financial supervision and governance. However, the risks remain high. New threats emerge and the world economy remains far from being resilient enough to the likely shocks arising from growing financial imbalances. To navigate successfully on the choppy waters the ship has to be either well equipped for the navigation, or alternatively leave the troubled area for safe waters.

---

[1] Authors work at the National Research University "Higher School of Economics", their study was supported by the World Economy and World Politics Faculty and is planned to be published in the International Organizations Research Journal.

[2] Sustainable Development Solutions Network. http://unsdsn.org/news/2015/11/10/sdsn-g20-declaration-for-action/

[3] G20 Action Plan on the 2030 Agenda for Sustainable Development https://www.g20.org/Content/DE/_Anlagen/G7_G20/2016-09-08-g20-agenda-action-plan.html?nn=2068780

[4] Declaration for the G20 Summit in Antalya, Turkey, November 2015. http://unsdsn.org/wp-content/uploads/2015/11/151111-SDSN-G20-declaration-FINAL.pdf

Recently the IMF published a report on a global non-financial sector debt (IMF, 2016). The figures demonstrate a fast rise in the public and private sector debts, reaching new highs by the year 2017. So far, regulators made a lot to lessen financial risks arising from the banking sector, though the new parameters of the system still need a lot of improvement, especially from the point of reaching inclusiveness. The record levels of non- financial sector debt represent in our view a new serious challenge for the SDGs. Governments have to take care more of their own debts rather than to help financial and non- financial institutions out of the public budgets by further increasing indebtedness levels. A correct assessment of the new risks is needed to secure the system and make it sustainable at a time.

We firstly make an assessment upon the banking regulation innovations from the perspective of financial security and inclusiveness. The conclusion is that it is not yet sufficiently sustainable. Then we pass on to disclose the remaining deficits of the regulative system, discovering emerging new risks for stability and growth from the non- financial sector, arriving to suggest more arguments for the introduction of the adequate regulative response. Otherwise, the system appears to become very fragile and unsustainable.

Dealing with the Banks Debts

The global financial crisis revealed a systemic deficit of financial regulation at the global level of all financial institutions, banks among them above all. This came as the result of the long process of the "diffusion of power in favor of private actors" in the financial sector[5]. The insufficient regulation at the global level made the system extremely unstable and risky. The uncontrolled exponential growth of the financial sector and its rapid globalization has led to the equally rapid increase in endogenous challenges. Some of the main risks, that we would like to outline to assess the challenges to the global economic governance, were the following:

- Overleveraged banks provided too many credits, which lead to financial bubbles, real estate and derivatives bubbles including;
- Banks risk management strategies occurred to be wrong;
- Too much speculation activity. Bankers losing interest to credit real sector companies, comparing high incomes from speculations and modest incomes from the real sector investments;
- Too much self- generosity and exorbitant bonuses policy;

Looking at the list, we can see that most the risks originated from banking. Normally banks are supposed to stimulate growth, but many risks resulted from banking activities. In general, we can conclude that financial sector lost an adequate connection to industries. The important intermediator link between the banking sector and the real sector was gone.

The core element of the financial governance is the banking regulation. In theory, banking services should provide an important link between the financial and the real sector to secure economic growth. In reality, the banking sector has become in itself a source of risks multiplication, including active speculative activities, resulting in financial "bubbles", increasing the gap between the real and the financial sector. Banks unsecured operations started to threaten growth instead of stimulating it. The intermediator link between the banks and the real sector becomes less vital to the banks. Financial sector in itself comes as a focus of the banking activities. This sector begins to live its own life. That has become a challenge for regulators to bring banks back closer to producers in order to stimulate economic growth again. As banks appear the key contributors to financial instability, the big question is how to diminish that risk.

Banks are the cornerstone of financial stability. If they are at risk, if they are too big to fail, the governments jump in to save banks by budgetary allocations in order to protect customers. In doing so they help banks with the money of the same customers - taxpayers',

[5] Underhill G., Zhang X. Setting the Rules: Private Power, Political Underpinnings, and Legitimacy in Global Monetary and Financial Governance. International Affairs 84: 3 (2008). P. 535–554

which socially is unfair. It contradicts the principle of inclusiveness and seems to be not in line with the Sustainable development goals of the G 20.

Speculative operations are the source of highest risks, but simultaneously – the origin of biggest profit margin for the banks. Thus, it seems unrealistic to separate speculative investment from crediting activities. Banks always will be tempted to be involved in risky operations in search of high returns. The already undertaken measures at the global and national level to favor upgraded capital requirements, extensive monitoring and making stress tests are all necessary, but they are not enough guarantees from banks' insolvencies.

Another aspect of the issue is that most of the risks had a global origin but are dealt with on a national level. The system was largely uncontrolled at the global level. Financial markets became long ago transnational, while the regulation and supervision remained mostly national. Because of these gaps, the system became either self-regulated, or poor regulated, which had been promoted by liberalization of financial markets by states, using liberalization as a tool to attract investment[6]. For this reason, the need for the global financial governance was felt more than ever. The attempts to create an independent system of global supervision encounter the opposition from nation-states and from the banking community. Being interested in 'carte blanche', they are not supporting so much setting up the system of global financial governance.

A better global financial governance means among all, setting up a coherent system of legitimate institutions; using adequate and effective instruments of regulation; relying on efficient methods of monitoring and control over the financial networks, ensuring that the interest of the people remains safeguarded with these measures in place. In this study, we try to analyze most important of these aspects to provide the ground for the assessment of the emerging system's inclusive function.

Many scholars do support a stronger international regulation[7]. What kind of regulation do we need and what should be regulated?

Theoretical concepts of the global governance are well developed by many scholars. The link between formal and informal institutions is represented by the concepts of major informal institutions (like G8 and G 20) governing either through multilateral formal organizations[8], or against them[9], or without them[10]. The authors of this study advance another vision of this link, presuming that within the last decade an emerging system of interlinks of different institutions can be defined similar to the orchestra of players, each of them having its own partita (music sheet) making a coordinated effort to play a tune of the financial stability. The reason for the new concept comes clear from the logic of the following argument. Having analyzed the scope and the substance of the regulative activities of formal and informal international organizations, and having studied the way all the institutions interact, we can conclude that a larger part of the financial regulation has been initiated at the global level, strengthening the global financial governance during the post-crisis decade and making it sound as an orchestra.

Selecting Proper Instruments to Assure Inclusive and Sustainable Growth

The starting point in making the system of financial regulation more efficiently targeted to inclusive and sustainable growth is a necessity for a greater and more reliable accountability

[6]Tsingou, E. 2003, 'Transnational policy communities and financial governance: the role of private actors in derivatives regulation', p.8. http.: warwick.ac.uk/2009/1/WRAP_Tsingou_wp11103.pdf

[7] Paul James and Heikki Patomäk (2006), Globalizing Finance and the New Economy: A Critical Introduction. In Globalization and economy, vol. 2, Globalizing Finance and the New Economy. Eds. Paul James and Heikki Patomäki. London: Sage Publications.

[8] Kokotsis E. (1999) *Keeping international commitments: compliance, credibility and the G7, 1988-1995* (New York, Garland)

[9] Kirton J (2004) Multilateral organizations and G8 governance: a framework for analysis in Kirton J and others Making Global Economic Governance Effective. Ashgate 2010.

[10] Bayne N. (2000) *Hanging in there: the G7 and the G8 Summit in Maturity and Renewal* (Andershot, Ashgate)

of banks. Regulations regarding capital requirements for banks came into effect in all 27 jurisdictions that are members of the Basel Committee on Banking Supervision. Due respect of these provisions by the banks enhances a more reliable system, but this is not enough. The Basel III prescriptions, even if applied in full, are insufficient to build an effective system of control over the banking sector[11].

Among the deficits in the existing mechanism is the fact that banks use internal models to calculate capital requirements, lack of disclosure, insufficient minimum leverage ratio[12]. Another difficulty is the growing discrepancy in national approaches to Basel implementation. Basel IV framework could provide solutions to these issues. The Bank of International Settlements (BIS) tries to catch up with these deficits advancing different solutions.[13]. The Basel Committee also does a lot on adopting standards and recommending best practice in banking supervision. The Financial Stability Board encourages the adherence by all jurisdictions to regulatory and supervisory standards on information exchange[14]. The Economic Stability Council pushed forward the introduction of the International Financial Reporting Standards (IFRS). This is particularly important, as national states are reluctant to transfer their powers to global regulators[15]. ESC's tasks to simplify and improve international standards of financial reporting and harmonize financial listing standards were conducted in cooperation with the International Accounting Standards Board (IASB) as well as with national institutes.

As CRA had responsibility for the economic crisis, as they had not assessed in an adequate way the risks on the markets, and as they had not averted investors about these risks, many brokers are interested themselves to use alternative practices of the risk calculation. They are looking for the best practices other than reliance on the CRA to secure their investments, compared to the past[16]. International Organization of Securities Commissions formulated standards for financial operations that go far beyond the securities trading. For instance, on December 2015 they published an overview of the best practices for the market intermediaries in the assessment of creditworthiness and the usage of external credit ratings[17]. The report provided recommendations to national regulators to use the best practices in the supervision over market agents. Using these practices intermediaries should assess credit risks' alternatively to Credit rating agencies (CRA). Thus, the introduction of a more reliable system means more sustainability.

The Basel Committee on Banking Supervision, IOSCO and IAIS are implementing the jointly developed General principles of operation for financial markets supervision bodies, which consist in the respect of four principles: transparency, financial stability, ability to pay and operational responsibility. The main ambition of this policy is to integrate the norms into national legal systems and ensure stability on global financial markets. Common principles help creating a common vision of solutions and on this basis to move forward with the introduction of the regulative norms, which in their turn facilitate reaching the goal of sustainable growth.

The process of creation of new packages of regulations by the global institutions is systematic and consistent. For example, in January 2016 the next set of changes in requirements

---

[11] Gros D. (2013) The problems of Basel principles usage in the EU. Banking union with a sovereign virus: The self-serving treatment of sovereign debt. Intereconomics, Springer, Heidelberg, Vol. 48, Iss. 2, pp. 93-97.

[12] Basel 4 - emerging from the mist? KPMG, September 2013. URL: https:/.kpmg.com/ID/en/IssuesAndInsights/ArticlesPublications/Documents/Basel4-Emerging-from-the-Mist.pdf

[13] Revisions to the Standardized Approach for credit risk - second consultative document. Bank for international settlements. December 2015. URL: http://www.bis.org/bcbs/publ/d347.pdf

[14] FSB, "Promoting global adherence to international cooperation and information exchange standards", 10 March 2010. Available at: http://www.financialstabilityboard.org/publications/r_100310.pdf.

[15] Baxter L. G., Exploring the WFO Option for Global Banking Regulation, in: Globalization & Governance. pp. 113-124. Laurence Boulle - ed., Syber Ink 2011.

[16]Paudyn B. (2013) Credit rating agencies and the sovereign debt crisis: performing the politics of creditworthiness through risk and uncertainty. Review of International Political Economy, 20 (4). pp. 788-818.

[17] Market Intermediary Business Continuity and Recovery Planning. OICU-IOSCO. December 2015. URL: https://www.iosco.org/library/pubdocs/pdf/IOSCOPD523.pdf

for banks regarding market risks revaluation was adopted; in February 2016 appeared two more documents - the Guide to Anti-Money Laundering and Recommendations on Account Opening Procedure [18]. And so it goes on. This regularity, continuity and consistency, generated at a global level within the last decade, provides for a solid base to avoid erratic and conflicting national legislative activities, which is where and how the new sound international financial order might be set up.

There are many other issues to be tackled in order reach SDGs, such as "too big to fail", or "shadow banking system"[19]. They all lie within the competence of international institutions[20]. 'Too big to fail' banks is a special case for social responsibility and inclusiveness. In this particular case, an international regulative response to the issue is very important.

There is a pressure on different financial institutions to take more responsibility over their activities. In the year, 2013 a methodology to identify global systemically important insurance companies (G-SIICs) and updated technique of revealing global systemically important banks (G-SIBs) were published. On this basis the list of G-SIBs was composed (it included 28 G-SIBs) and an initial list of G-SIICs is compiled and is updated annually starting from November 2014. Financial institutions included in these two lists are obliged to meet higher requirements and fall under more rigorous supervision. Plans for the settlement of insolvency were developed for them. The liquidity adequacy requirements for 28 G-SIBs were also developed and in most cases, the G-SIBs increased capital before the deadlines. Additional stringent requirements for liquidity adequacy start to apply to G-SIBs since 2016 with the gradual full introduction until 2019.

Late in 2014, FSB put forward an initiative increasing big banks' accountability in order to upgrade the risk absorption role of the global banking system[21]. The proposal was to oblige the global, systemically important banks (G-SIBs) to have additional reserve assets so that the losses are not shifted on to taxpayers' shoulders in case of emergency. On November 11, 2015, following a quantitative impact assessment the Financial Stability Board finalized total loss absorbing capacity (TLAC) minimal requirements for G-SIBs. Although the initiative was endorsed by the G20 summit, the implementation mechanisms are still to be detailed at a national level. Nevertheless, this move goes in the right direction – banks should bear the larger part of responsibility by themselves to cover eventual risks.

On October 12, 2016, the standard for Internationally active banks (both G-SIBs and non-G-SIBs) on TLAC holding was published by FSB according to which banks must deduct their TLAC holdings that do not otherwise qualify as regulatory capital from their own Tier 2 capital. This reduces a significant source of contagion in the banking system. The standard also reflects changes to Basel III specifying how G-SIBs must consider TLAC requirement when calculating their regulatory capital buffers.[22]

In 2015, the Financial Stability Board launched a peer review on the implementation of policy framework for financial stability risks posed by non-bank financial entities ("other shadow banking entities")[23]. The objective of the review was to evaluate the progress made by jurisdictions in implementing the principles to reduce the importance of the shadow banking set

---

[18] Basel Committee on Banking Supervision. Bank for International Settlements. URL: https://www.bis.org/bcbs/

[19] FSB includes in this category, among others, money market funds (MMFs), structured finance vehicles, broker-dealers, finance companies, financial holding companies, hedge funds and other investment funds. For more details, see A Police Framework for Strengthening Oversight and Regulation of Shadow Banking Entities and a Policy Framework for Addressing Shadow Banking Risks in Security Lending and Repos. Financial Stability Board. URL: http://www.fsb.org/wp-content/uploads/c_130129y.pdf

[20] Tobias A. (2014). Financial stability policies for shadow banking. Staff Report, Federal Reserve Bank of New York. No. 664, p.9.

[21] Bruno V., Song Shin H. Cross-Border Banking and Global Liquidity //Bank for international settlements. August 2014. URL: http://www.bis.org/publ/work458.pdf

[22] TLAC Holdings. Financial Stability Board. 12 October 2016. http://www.fsb.org/2016/10/tlac-holdings/

[23] FSB launches and invites feedback on its Peer Review on implementation of the FSB policy framework for shadow banking entities. http://www.fsb.org/2015/07/

out in the framework. The peer review appears as another instrument to build up a more reliable system. In accordance with the provisions of the Charter of the FSB, the member countries are obliged to proceed periodically the Financial Sector Assessment Program (FSAP) of the IMF and World Bank. They have to present the country surveys, which contain evaluation of the degree of implementation of international standards. The work to provide these reports builds up compliance.

One of the problems is that most of the global institutions decisions are recommendatory. Although a relatively high level of compliance appears as an extraordinary feature of the global financial governance[24]. Expanding controlling functions of the international institutions and the obligation of the national and international actors to make regular reports on their activities help substantially to increase the influence of internationally acknowledged norms. Thus, the global institutions set up a certain standard of the financial regulation. More than that, they enforce this regulative framework for financial institutions in a soft way. For example, if the financial institutions concerned do not fully comply with the provisions of the Basel III (liquidity coverage ratio or the net funding ratio) they may be not allowed an access to the major stock exchange platforms. In this way a stimulus to respect the new international prescriptions is created. Although many bankers claim they are not ready to fulfill the recommendations describing them as too tough, nevertheless, the adopted global standards find their way for implementation by most countries despite the grudging on the part of the banking community. Therefore, it is crucial that the chosen global standard should work for inclusive and sustainable growth.

Another instrument of financial governance is introducing sanctions based on the stress tests. Conduction of stress tests on a regular basis is a novation in global governance. Terms of reference of the stress tests, undertaken by the FSB, stipulate an issuance of a warning, if non-compliance is revealed for the first time. An inclusion of a member-state or its banking institutions in "grey" and "black" lists in case of the repeated non-compliances entails imposition of sanctions by the Financial Stability Board. Thus, the members of FSB are involved in the formulation of general rules, norms and procedures, selecting proper instruments of implementation, providing for supervisory and controlling functions, thus assuring the compliance with the adopted recommendations. November 2015 the FSB published the first report on the *Implementation and effects of the G20 financial regulatory reforms.* Implementation of the Basel III reforms for the bank capital and liquidity requirements went ahead of schedule[25].

Summing up the overview of the adopted instruments, we can conclude that a vast number of new measures appear: monitoring procedures, checks and stress tests, new standards of reporting and accounting, new risk-management techniques and exchange of best practices, new capital requirements, etc. What is missing?

There are two big problems still unresolved. Market speculations remain very attractive for the banks. If so, the risk of building up dangerous financial bubbles continues to stand high. If so, banks safe position could be questioned one day or another. If so, chances are high that the necessity to provide liquidity for the banks could be on the governmental agenda again. However, as in the past, there is no fund financed by the bankers themselves to rescue banks in case of necessity. A rational solution appears to be evident.

Financial Transaction Tax – Inclusiveness, Social responsibility and Financial Stability

Is the current contribution from the financial sector to the financial stability for the majority of customers fair enough? The ongoing reforms since the outbreak of the global

---

[24] Brummer C., Soft Law and the International Financial System: Rule Making in the 21st Century. (2012). New York: Cabmridge University Press.

[25] I*mplementation and effects of the G20 financial regulatory reforms.* Report of the Financial Stability Board to G20 Leaders. FSB, 2015. http://fsb.org/wp-content/uploads/Report-on-implementation-and-effects-of-reforms-final

financial crisis do not solve one key problem, namely enormous cost to rescue the financial sector financed to a large extent by governments and the tax payer and the absence of a fair contribution from the financial sector.

Our study aims to outline the necessity to undertake concrete policy measures by the regulators to meet the global financial stability challenges, having in mind social responsibility target at a time. If we think about the market instruments, taxation is the first thing to come to our mind. It could serve two goals: discourage speculation and provide a source of financing a Fund to rescue banks in trouble at the expense of the banks. Thus, it serves well the inclusive and sustainable criteria.

The discussion on introduction of various forms of financial tax has a long history. Back in the 1936 J. Keynes wrote: 'The introduction of a substantial Government transfer tax on all transactions [on Stock Exchanges] might prove the most serviceable reform available with a view to mitigating the predominance of speculation over enterprise in the United States'[26]

The regulatory system needs adequate mechanisms to discourage excessive speculating activity. The Basel III provides for stronger capital requirements, assuring more responsibility by the banks, but does little to reduce speculation. Speculation continues to flourish with redundant money in the financial sector and reduced finance for the real sector economy.

Back in the year 2009, Paul Krugman published an article under titled "Let's make banking boring again"[27]. He argued, that the banking industry emerged from Depression in the USA was tightly regulated. Banks served as intermediators. Banking was boring. After 1980, however, many of the regulations on banks were lifted, and banking became exciting again. That was the moment when speculation activity became great. Debts began rising rapidly, and the financial industry exploded in size. Krugman suggested to separate investment banking from a traditional one. The ongoing structural measures to introduce limitations on banking such as the U.S. Volcker rule, the U.K.'s Vickers ring-fence, and the EU's Liikanen proposal, which envisage creating functional separation of operations, all advanced as a reaction to the inadequate management of the excessively risky speculative investments by deposit taking banks.

Our assumption is that it is more difficult to undertake the separation of speculative operations from deposit-credit activities of the banks with an appropriate control, than to introduce a proper taxation on speculative activities. Even if it occurs to be possible, than those speculative activities will be switched to the shadow banking system, which in its turn is still harder to control.

The global institutions are trying to catch up. The Basel committee on Banking Supervision published a new standard revising the prudential treatment of banks' investments in the equity of funds within the Basel capital framework (to take effect from 2017), which is to be applied to banks' equity investments in all funds (e.g. hedge funds, managed funds and investment funds)[28]. Still it is extremely difficult to make banks reduce their speculative activities and thus lessen the risks to the financial system. Why not let the banks do their job themselves, creating substantial buffers outside of their books at the expense of the same banking community?

One of the most suitable tools for this role seems to be the Financial Transaction Tax (FTT). Many analysts share that point of view[29]. Still the critical mass of arguments for its implementation has not been accumulated so far. FTT is a fee charged on financial institutions

[26] J.M. Keynes, General Theory of Employment, Interest and Money, Harcourt Brace, New York (1936), 1961, pp.159–60.

[27] P. Krugman Making Banking Boring. The New York Times. April 9, 2009

[28] Revised policy framework for banks' equity investments in funds issued by the Basel Committee. 13 December 2013. http://www.bis.org/press/p131213.htm

[29] Baker D. The Benefits of a Financial Transaction Tax. Washington, DC, 2008.Center for Economic and Policy Research; The need for a tax on financial trading. New York Times, January 28, 2016. URL: http://www.nytimes.com/2016/01/28/opinion/the-need-for-a-tax-on-financial-trading.html;

for certain financial operations they carry out. This may concern stocks, bonds, shares, derivatives etc. The taxing modes may vary - by residence of the investor or of the issuer, or by the asset's origin. It is essential that the place of the operation does not matter which decreases the attractiveness of offshore jurisdictions with regard to this type of operations.

The common argument stopping countries from introduction of FTT is the risk the turnover of the financial sector reduces and a number of financial institutions flee to non-taxed destinations. However, the tax rate is so minimum, to really divert businesses from being registered in the country-origin and to make a visible impact on their activities. The FTT mostly does not exceed a few tenths (or even hundredths) of a percent of the operation amount. The tax is possible to split between the seller and the buyer. Among the other negative consequences of the introduction of FTT - a likely a reduction in investment. Some experts dispute the very idea to tax such operations[30]. The use of the FTT can lead to a contraction not only in speculative trade, but also in transactions made by brokers with non- speculative purposes. An increased cost of operations added concern for the governments as they assume investors might be less willing to buy state bonds due to a new taxation. Traders and investors may also move overseas in case the tax is introduced in their country. Although as mentioned above the country of operation is not critical for the collection of the tax, bankers may find loopholes.

The additional funds from the FTT received by the state or by an international organization (if the Fund is governed globally, which in our opinion is the preferable option) are primarily referred as an advantage of this regulation. Such a tax could have empowered the G-20 (or the IMF) with the necessary financial resources to move forward faster with reforms of the global financial sector. For example, the US Congress proposing the introduction of FTT estimates getting $180 billion only from the US banks during the period 2015 to 2023 (See Figure 1). The global tax could yield much more.

Figure 1. Budget revenues from a tax on financial transactions in the US

(Billions of dollars)	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2014-2018	2014-2023
Change in Revenues	0	12	18	19	20	21	21	22	23	24	68	180

Source: Congressional Budget Office. Staff of the Joint Committee of Taxation. November 2013. URL: https://www.cbo.gov/budget-options/2013/44855

Another important theoretical point is that apart from money-raising arguments, the FTT comes as an appropriate market tool to lower down incentives for excessive speculation. It is unrealistic to expect that the use of the FTT will dramatically reduce the number of short-term and high-speculative securities trading, as the rate of the tax is minimum at an initial stage of its introduction. However, the motivation for speculative activities might be, at least a bit reduced. That would be a very important sign for the bankers. FTT has significant advantages over other taxes on financial activities as it is relatively easy feasible and difficult to avoid. For the brokers specializing in high-frequency trade, for example, it is technically difficult to conduct operations from a different place but their respective countries because computer proximity to the Stock Exchange is critical.

Still another argument is that the FTT reducing systemic risks contributes to sustainable economic growth. At the time of growth, the volume of the rescue Funds and thus the ability of safeguarding financial stability will be in a steady increase. Justifying the introduction of the tax J. Tobin pointed out another positive effect of the FTT on the economy. If a decrease in speculation activity occurs with a lowering down of the excessive profit margins, it makes financial sector less attractive for active, intelligent and educated professionals. This could mean

[30] French financial transaction tax on equity securities. Latest developments and practical implications for the market. PricewaterhouseCoopers. August 2012. URL: http://www.pwc.be/en/financial-services-newsalert/2012/landwell-fftt-pdf-aug-2012.pdf

that non-financial services sector like medicine, or industries and science will get new arrivals of talented people and therefore a greater focus on industrial growth will happen.

Beyond these effects, the FTT could be vital because of its deep-rooted substantial effects, which are of special importance to mention with regard to this study. This way of taxation could contribute to a more equitable income distribution and a slowdown in disproportional wealth concentration. As described in the works of Thomas Picketty, the problem is standing high on the global agenda[31]. Research shows that levying FTT has a progressive effect. Roughly, 3/4 of its collection assumed by the taxpayers in the highest income quintile and more than 40 percent falls on the top 1 percent[32]. One major step to socialize the FTT mechanism could be the introduction of smart accountability systems. In particular, in case of provision of special conditions for the pension funds accountability, exemptions for small companies and companies engaged in socially responsible activities.

Finally, a crucial influence is that the bankers themselves and not the taxpayers would bear financial responsibility to save financial institutions in trouble at the time of a crisis, shifting the burden of the emergency bailouts away from the taxpayers, thus assuming their due part of the social responsibility for financial regulation.

While the debate goes on, deficits of the practical implementation of the idea remain. In 2011, the EU member states - Austria, Belgium, France, Germany, Italy and Spain among them, have put forward the idea of a common FTT for the European Union. December 2012, the European Parliament voted for the proposal supported by eleven EU members. In January 2013, the Council of the European Union approved the introduction of the FTT. That was a very significant first move to implement the FTT globally. The EU soft power impact of example played an important role in respect to many other initiatives. It could be the case this time as well. The bank support fund created with the FTT disbursements could become a clever instrument to assure financial stability. The EU Council considered the introduction of FTT not to put the burden for bailouts again on the taxpayers as was during the global financial crisis of 2008. Taxpayers' money helped to bail out financial sector. FTT on the banking system appear to be a fair way to assure a socially more just financial regulation. Once created in the EU, other countries might wish to follow and to have such an instrument as well.

Still divergences remain even at the top political level on how to make use of it in a more effective way. In May 2014, ten out of the initial eleven participating member states (except Slovenia) agreed to seek a tax on equities and derivatives by 2016. December 2015 Estonia decided to stay apart considering that the cost of tax collecting will surpass the revenues. Which, according to our calculus, is not the case. Nevertheless, on 16 March 2016, the Republic of Estonia has completed the formalities required to leave the enhanced co-operation on FTT. The FTT issue came to a standstill in the EU Council. The ECOFIN decided that work would continue during the second half of 2016 between the remaining ten participants. Concerns arose over cost efficiency of FTT collection. February 2017, German Finance Minister Wolfgang Schaeuble said that implementation of the proposed European financial transaction tax was hindered by increasing demands for exemptions.[33]

Setting up a common EU system for taxation of financial transactions is a method of ensuring the banks make a fair contribution to compensate the cost of getting out of the crisis, since these banks received substantial amounts of governmental support. Deadline to implement the agreement was shifted several times. The United Kingdom as in many other cases makes

[31] Thomas Piketty, Capital in the 21st century. Harvard University Press, 2014

[32] Burman L., Gale W. and others. Financial transaction taxes in theory and practice. Urban Institute & Brookings Institute. June 2015. URL: http://www.taxpolicycenter.org/PDF/2000287-Financial-Transaction-Taxes-in-Theory-and-Practice

[33] Bloomberg. 21 February 2017. Schaeuble Sees Financial Transaction Tax Riddled With Holes. https://www.bloomberg.com/news/articles/2017-02-21/schaeuble-sees-financial-transaction-tax-riddled-with-exemptions

clear to use special protective measures in case of a damage to its market[34]. The UK in general was not so much against the tax in principle. The country thought it would never work unless the tax was levied globally by the G20. The authors of this article share this view to a certain extent without over exaggerating the negative effect that London as financial center would lose out to New York or Singapore.

Taking into consideration the remaining lack of unity on the issue, the EU so far is undermining introduction of the FTT in the rest of the world. The opposite is also true: in case of adoption of the tax in the EU, the critical mass necessary for its transformation into a truly global instrument of regulation could be formed.

The idea of the introduction of the FTT at a global level was raised by the G20 in 2008 and received the support of majority of member-states at that time. It was unfortunate that in 2010 at the summit in Toronto the proposal was shelved. It was a surprise as currently 16 of the 20 members of the G20 use different types of taxes with similar effects to FTT. The most widespread types of taxes close to the FTT are a tax on large companies' shares trade, the EU tax on short sales and sovereign credit default swaps (CDRs), or taxes aimed at high-frequency trade (for example, in France it is a tax on cancelled orders, in Italy – a tax on modified orders). Globally more than 30 countries use different variations of the FTT applying the rate of 0.1 to 0.5%. Among those applying different variations of financial taxes - United Kingdom, France, Belgium, Greece, Hong Kong, Switzerland, Australia, and South Korea.

In order to respect the social justice principle the FTT mechanism provides exemptions for different categories of persons and institutions in different countries. For example, in Italy the tax on transactions with shares of national companies and derivatives is not applied to companies operating in socially meaningful and ethical spheres[35]. Introduction of the taxation of the financial operations in a selective way should be an additional tool while thinking about socializing of the regulative financial environment.

The current UK FTT regime did not lead investors to escape the country because it is not related to the investor's residence, as was the case with the Swedish tax[36]. Thus, unification of those taxes could have been convenient for everybody[37]. Unification of taxes makes the argument of an additional burden with the introduction of the FTT for financial institutions irrelevant. Though this argument seems to be irrelevant anyway, as the rate of taxation is very small. In all the states that have adopted variations of FTT as well as in most other countries (e.g. in the EU) support for the tax by the civil society is high. The tax has a strong backing by the expert community: there have been numerous actions in support of the FTT involving prominent economists[38]. Politicians have to take that in to account.

German position, holding in 2017 the G20 Presidency, can be critical to push forward the idea again.

A tax in one country or in a small group of countries will be not efficient enough. It could only bring a solid and visible effect, if introduced at a global level. Thus, a global institution could and should provide an appropriate platform for such an initiative. The G20 is one of the options as the adequate global format to introduce such a tax. Though so far, the idea was rejected. It will benefit the G20, upgrade financial stability and socialize the global governance institutions, as they do not enjoy much of the public support. Surprisingly, the idea is not among the top priorities in the global agenda, although the cost is low for the stakeholders,

---

[34] Maurice E. EU Financial Transaction Tax on life support. EU Observer. December 8, 2015. URL: https://euobserver.com/economic/131435

[35] Hemmelgarn T., Nicodeme G. and others. Financial transaction taxes in the European Union. European Commission taxation papers. Working paper №62 – 2015.

[36] Seely, Antony (2014) The Tobin tax: Recent developments. Library of the House of Commons. 15 May, 2014

[37] Hemmelgarn T., Nicodeme G. and others. Financial transaction taxes in the European Union. European Commission taxation papers. Working paper №62 – 2015.

[38] 1000 Economists Tell G20: Support a Robin Hood Tax. April 12, 2011. URL: http://robinhoodtax.org.uk/1000-economists-tell-g20-support-robin-hood-tax

because of the low rate of the tax proposed. This paper strongly supports the idea to favor the introduction of the financial transaction tax. The authors want to increase the public and governmental awareness of the necessity of such a measure.

Transposition of the FTT at a regional and at the global level is a prerequisite for the soother acceptance of the tax. The cases of Estonia and Sweden demonstrate that the introduction of the tax on a unilateral basis by a small country alone may be not efficient. Most of the studies reveal that a FTT with a broad (global) tax base provides greater revenues[39] and greater effects. The necessary synergies appear at the global level much easily.

The most relevant measure to assure financial stability among the other ones is to introduce a tax on financial institutions' speculative operations and to establish a rescue fund for banks at their own expense. Our argument is that this measure combines lower risks for financial system with social justice and inclusiveness, which is the focal point.

To socialize efficiently the impact of the FTT introduction it is critical to define exact patterns how to spend the funds raised by the states at the times of the absence of the necessity for the bank assistance. We do not have crisis all the time. Thus, the Fund could be used for some other purposes if there is no financial crisis. The EU countries experience demonstrates that it is possible to proclaim "far reaching" goals, such as using the new funds to grant aid to the poorest countries. A way of spending could be financing growth enhancing projects and formation of an international "safety cushion" for the banks, which would be the incentive for their readiness to follow the initiative. In our view, it could be much easier to gain supporters of the idea of the FTT introduction within the banking community, had it been announced that the Basel 3 norms on capital requirements could be not applicable in full for countries, which had created the fund for assistance to the banks in trouble. Creating the fund means banks could have more flexibility in their credit policies, as the Fund since becoming operational could provide a necessary assistance and at the expense of the banks themselves. In this case, one could expect a positive effect on banking community leaders to stimulate them to accept the taxation.

Using a financial transaction tax as a tool to discourage excessive speculation without hampering any other activity seems to be socially responsible measure working for financial stability at the same time.

Debt: do not use it widely

Financial globalization and fast growing debt levels mean that crises can spread far more quickly and widely, contributing to financial shocks. These are detrimental to global economic growth and resilience, presenting a major challenge for the SDGs implementation. According to the *IMF Fiscal Monitor,* published in October 2016 [40], the global debt of non-financial sector has reached an unprecedentedly high level of 225% of the world GDP. Two thirds of the global debt consist of private sector liabilities, which becomes a point of additional concern. As soon as the government makes the decision to help national corporations at time of financial trouble by launching bailouts, private debt turns into public debt and ads up substantially to the levels of governmental indebtedness, which was the case at the aftermath of the 2007-09 global crisis.

Emerging markets' nonfinancial corporate debt surpassed the $26 trillion mark in the first half of 2016, according to the Institute for International Finance. In its turn, the corporate debt level of most nonfinancial companies in emerging economies rose from $4 trillion in 2004 to $18 trillion in 2014.[41]

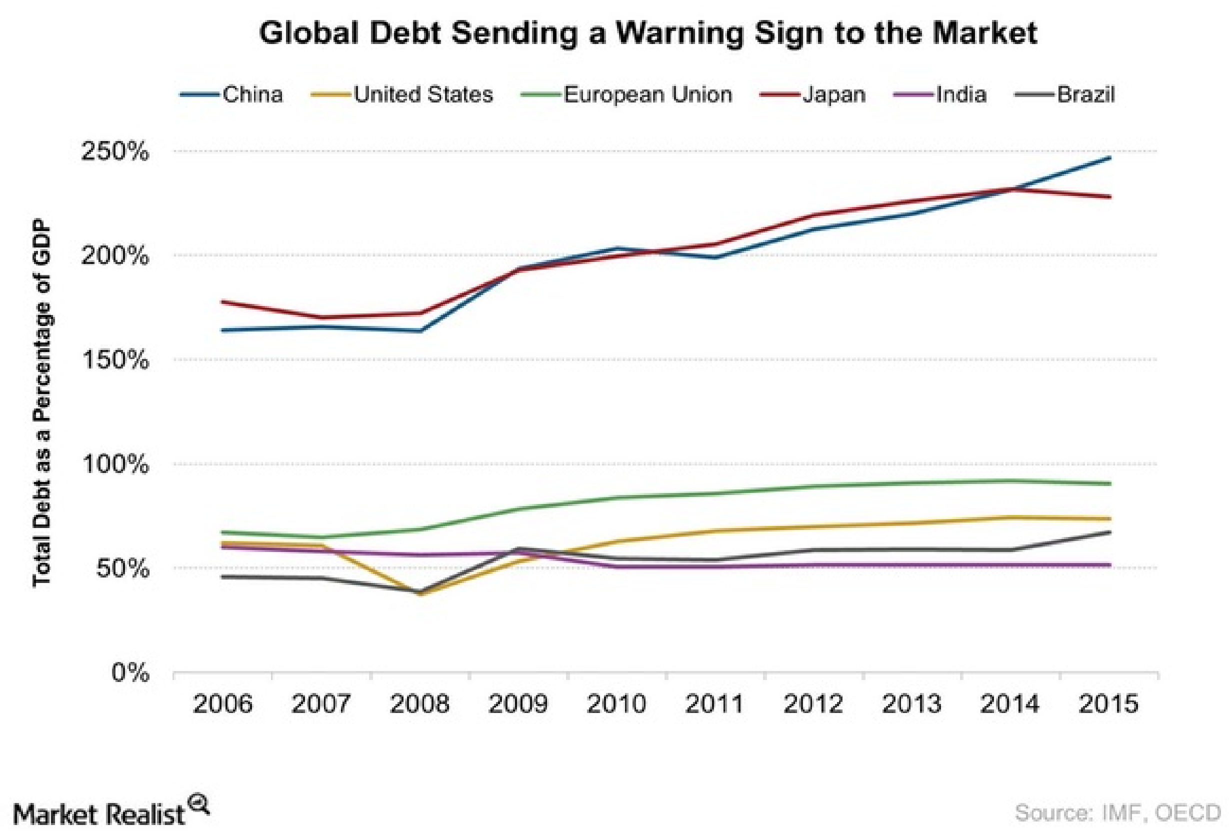
[39] Schaefer D. Fiscal and economic impacts of a limited financial transactions tax. Deutsches Institut fuer Wirtschaftsforschung. Berlin, 2015.

[40] International Monetary Fund (IMF). 2016. Fiscal Monitor: Debt—Use It Wisely. Washington, October.

[41] International Monetary Fund, Global Financial Stability Report—Fostering Stability in a Low-Growth, Low-Rate Era (Washington, October 2016).

Demand for emerging market debt can be explained by higher yields at this destination and low and or even negative bond yields in developed economies. The Brexit was another important factor to stream the investment flows out of the developed economies. International investors have put more than $18 billion into dollar-denominated emerging market bond funds since the United Kingdom voted in favor of a Brexit. China and Saudi Arabia are the leading countries - issuers of debt. That large corporate debt could be considered as an additional pressure on the governmental finance. In case of low economic activity, if a government is to help national corporations, the debt burden will only be in further increase. Billionaire investor George Soros has expressed concern about China's increasing new credit. The rise in new credit suggests that the government is prioritizing growth instead of controlling debt. Stocks and bonds maintain a positive correlation especially when investors are unsure about the prospects of stocks.

Graph 1.



Thus, we have all the reasons to consider the levels of non-financial sector debts jointly, public and private. Excessive private debt is widely considered as a potential risk to economic stability and growth. On the other hand, there is another concern that a private deleveraging process could stifle the delicate economic recovery.

Surprisingly enough, little attention is paid to government debt, which amounts to the remaining one third of the global debt. While increasing control is exercised over private sector's and banks' borrowings (see part 1 and 2 of the article), there is virtually no regulation of government debt. Indeed, the regulation aimed at prevention of bankruptcy among individuals, firms and banks becomes more advanced and rigid. On the contrary, governments are almost free in their borrowing: no limits, no regulation, no control. Most experts until recently, while assessing the risks of the global financial stability, took into consideration all types of the debt, except the sovereign debt. Does it mean we don't have to worry about the ability of the states to repay their appropriate debts? The cases of Greece, Ireland, Portugal and other countries during the recent global financial crisis demonstrated that the risks are high and real. Even bigger countries, like Italy, can't feel safe enough against financial stability risks. Let us look at it the other way. If a government is over-indebted, cuts in public budgets and vital services are inevitable, which means a sacrifice to human well-being and long-term growth prospects. More than this. In a globalized world, one country's over-indebtedness can surely have spillover effects on regional or even global markets, as the recent Greek financial crisis demonstrated[42].

We try to summarize the arguments in favor of regulation of government debt:

1) Excessive levels of government debt might stifle economic growth.

Central banks across developed economies are putting more money into their respective economies in the form of quantitative easing (QE). Governments across the world are issuing more debt to fund their fiscal deficit. By issuing debt, they are aiming to increase their fiscal stimulus and accelerate economic activity to boost economic growth. While implementing stimulating fiscal policy, popular with countries during crisis and post crisis period, governments overwhelmingly resort to debt financing. Some experts consider increase in government debt to be an incentive for economic recovery and growth. Particularly, econometric models presented in the work of Jordà, Schularick, and Taylor suggest *"that fiscal policy can significantly reduce the output cost of a financial crisis, provided that fiscal buffers are available prior to the crisis".*[43]

However, having become excessive, government debt turns into an obstacle to economic growth. Three groups of economists have independently shown that high government debt negatively affects long-term economic growth. The general explanation for this negative correlation is the following: when government debt exceeds a certain threshold, private investment activity tends to go down due to lower value of government guarantees trust to government, which ultimately lowers future profits and leaves no space for future growth. According to empirical studies across advanced economies, the worst effects occur when government debt to GDP ratio reaches the level of 90%. Studies by Manmohan Kumar, Jaejoon Woo (IMF)[44] and by Carmen Reinhart, Vincent Reinhart, Kenneth Rogoff (National Bureau of Economic Research) [45] have illustrated that once a country's government reached higher-debt status, the economy tended to experience slowdown in economic growth. The third study was carried out by Stephen Cecchetti, Madhusudan Mohanty, and Fabrizio Zampolli (the Bank for International Settlements), who found about the same negative effects on economic growth from high government debt. [46]

Despite being challenged by some experts, for instance, Ugo Panizza and Andrea F. Presbitero (UNCTAD)[47], as questionable, the idea of potential harm to economic growth from overleveraged governments gains popularity in international economic community.

2) Excessive levels of government debt might cause a potential harm to global financial stability.

Numbers speak volume. If we look at the scale of government debt compared to GDP, an alarming trend of rapid increase catches the eye (see the Graph 1 below).

---

42 Motoko Aizawa, Macroeconomics and sovereign debt. 30 November, 2016. https://www.boell.de/en/2016/11/30/macroeconomics-and-sovereign-debt?dimension1=ds_g20_en

43 Jordà, O., M. Schularick, and A. M. Taylor. 2016. Sovereigns versus Banks: Credit, Crises, and Consequences. Journal of the European Economic Association, 14 (1), p. 45–79.

44 Manmohan S. Kumar and Jaejoon Woo (2010) Public Debt and Growth. IMF Working Papers, WP/10/174.

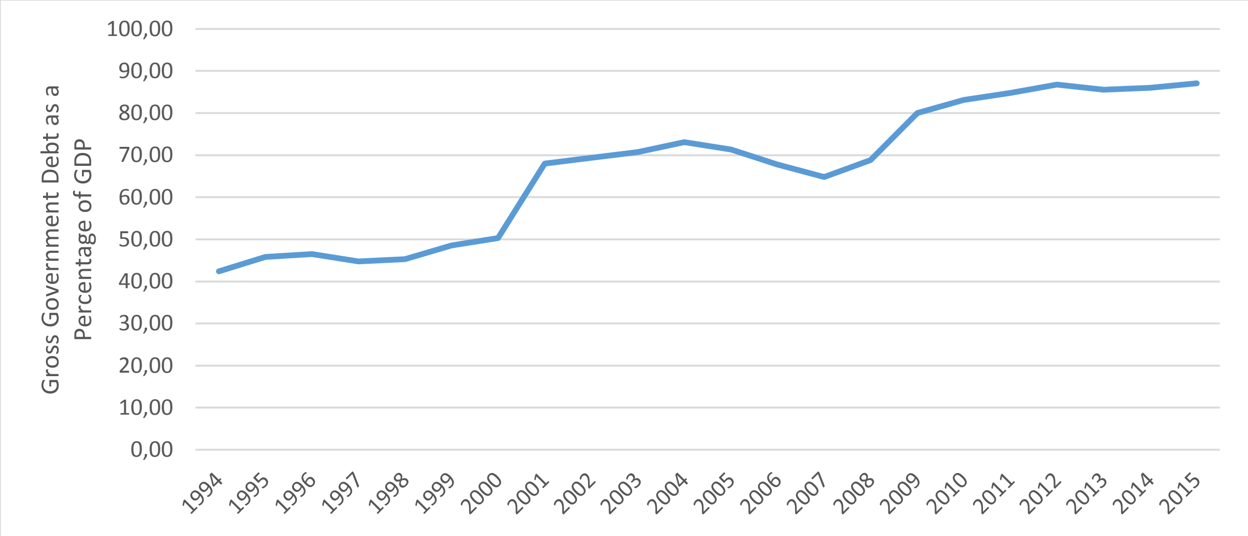
45 Reinhart, C. M., V. R. Reinhart, and K. S. Rogoff. 2012. "Public Debt Overhangs: Advanced-Economy Episodes since 1800." *Journal of Economic Perspectives* 26 (3): 69–86.

46 Cecchetti, S. G., M. S. Mohanty, and F. Zampolli. 2011. The Real Effects of Debt." BIS WorkingPaper 352, Bank for International Settlements, Basel.

47 Ugo Panizza, Andrea F. Presbitero. 2014. Public Debt and Economic Growth: Is There a Causal Effect? Journal of Macroeconomics, 41, p.21-41.

Graph 2.

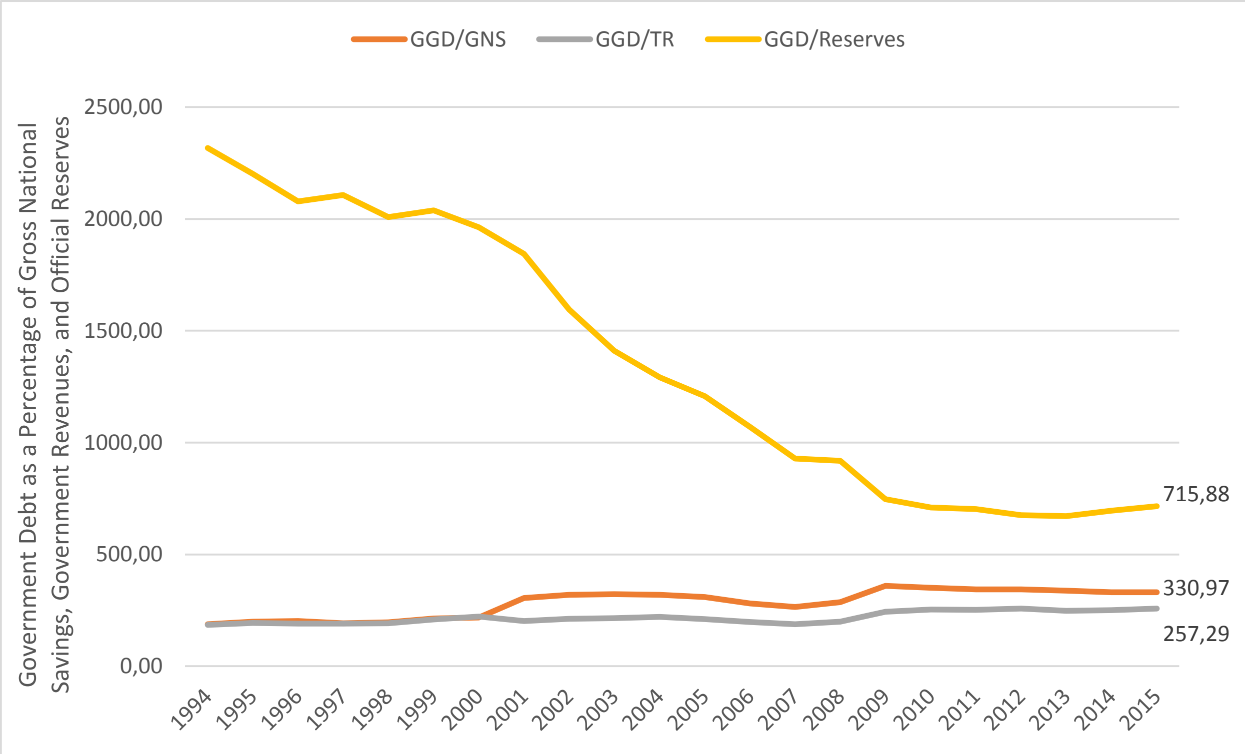
Gross Government Debt to GDP Ratio for G20 countries



Source: calculated by authors according to IMF Data

However, comparison with GDP doesn't provide the complete picture of the issue as the whole value of GDP couldn't be spent on the debt repayment. In principle, one could use government debt to GDP ratios to certain judgments about the situation, but this approach ignores the asset side of the balance sheet, which is crucial for adequate evaluation of repayment capacity. And it is the capacity to pay back debt to be most important in terms of sustainable growth. An alternative is to compare government debt to some other indicators, such as gross national savings, total revenues of central government. As we can see from the Graph 3, government debt in G20 dramatically exceeds government revenues and national savings, and the trend is still upward. Situation is different if we look at government debt to official reserves ratio which decreased substantially during economically prosperous period of 2000-2006, but started to grow again after the recent financial crisis.

Graph 3.



Source: calculated by authors according to IMF Data

Taking into account the government debt at extremely high levels in major economies we can speak about a threat to global financial stability. Governments as lenders of last resort are expected not just to provide public goods and confront the economic cycle, but also to provide financial assistance in the form of loans to banks and non-financial sector in the aftermath of financial shocks. If systematically important banks and companies face a risk of bankruptcy again, it is the government to help them. But who will help governments one by one facing the risk of default?

Obviously, international financial institutions with IMF at the top form a kind of a financial buffer that plays crucial part in case of emergencies. Despite being criticized for insufficient efficiency and agility, IMF managed to help countries in need during the recent financial crisis. Nevertheless, it is obvious that the Fund's resources measured in billions are incompatible with the global government debt measured in trillions (see the Table below), and in case of global government debt crisis it can't be expected to assure the financial stability in the world. After the financial crisis of 2007-2008, the global financial system has undergone several reforms aimed at improving its stability and enhancing the effectiveness. But even though established institutions are accumulating financial resources and new institutions are being developed, the capacity of the global financial system still doesn't respond to the exponentially increasing risks.

Table 2.

Government debt to IMF resources ratio (total value of SDRs)

Year	1994	1996	1998	2000	2001	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Ratio	4746	5882	3860	4582	6162	7511	8711	9141	9338	10020	11541	12747	7181	8068	8383	8465	8734	8366

Source: calculated by authors according to IMF and World Bank Data

3) Excessive levels of government debt confront with the idea of sustainable and inclusive economic growth.

According to the 2030 Agenda for Sustainable Development, the G20 countries take a firm stand to *"ensure that no one is left behind in our efforts to eradicate poverty, achieve sustainable development and build an inclusive and sustainable future for all"*[48]. Still, continuously increasing government borrowing at the expense of future development does not conform to the goal of sustainable growth declared by G20. Additionally, it contradicts with the idea of inclusiveness that implies considering interests of all groups of population/people/citizens, because, ultimately, citizens are to pay for government debt restructuring. Indeed, if governments are bankrupt, citizens would suffer most again, like in case of banks' crisis. Socially responsible global financial governance should take into consideration the seriousness of the governmental debt issue in a similar manner it treated the bank's resilience issue.

That being said, a need for control over government borrowing turns out to be an important objective. The pioneer in this direction is the European Union that has already taken some steps in building government debt regulation. These are introduction of the Maastricht criteria, implementation of the budget coordination mechanism, development of stability and convergence programs. We consider that such kind of practice should be taken by the G20 countries, which present approximately 86% of global GDP and 87% of global government debt.[49] One of the meaningful solution might be the introduction of agreement, if not equivalent, but comparable to Basel Agreements in banking that have already proved their effectiveness.

Today international institutions explore ways to ensure responsible lending and borrowing by G20 governments and their sovereign wealth funds. As suggested by Motoko Aizawa, responsible lending, in accordance with 2012 UNCTAD Principles on Promoting Responsible Sovereign Lending and Borrowing and the 2011 EURODAD Responsible Finance Charter, could protect not only debtor but also creditor nations whose loans would not be regard as "illegitimate", leading to calls for debt cancellation.[50]

However, in our point of view, achieving responsible lending and borrowing by individual governments is not very much realistic. Imagine a government in desperate need for funds that will refuse a gracious offer from an outside lender to provide the necessary finance…Convincing lenders that they have to be more responsible is also illusionary. By nature of the activity, they are willing to get back their money and profits anyway. You do not have to convince them or to guide them by any type of codex. The only thing that matters - high level of risk awareness is required. The more the lenders realize much higher risks of the present situation of high debt global levels, the more prudent they will be in their lending policies.

Additionally, in terms of the Sustainable Development Goals, it is reasonable to assess whether a country's debt payments are preventing the financing of human and environmental needs. Already existing IMF-World Bank Debt Sustainability Framework should be broadened and applied to advanced and emerging economies, not only to low-income states as it is now. The extremely high levels of their debt endanger the global financial stability.

We consider that G20 should also make a significant contribution towards increasing public awareness of risks that come from high debt levels for both developed and developing countries. The most critical indicator for investors is trust. Once investors lose their trust, they stop giving money. Consequently, the more people, thankfully to G20's effort, will be aware of risks, the more rational and efficient will be their investment activity.

Lack of monitoring is another issue G20 could try to tackle. Who will control states in their insane borrowings policies? The need is there for the introduction of comprehensive public debt workout mechanism, based upon the early warning system of global financial supervision.

---

[48] G20 Action Plan on the 2030 Agenda for Sustainable Development
https://www.b20germany.org/fileadmin/user_upload/G20_Action_Plan_on_the_2030_Agenda_for_Sustainable_Development.pdf

[49] Calculated by authors according to IMF Data.

[50] Motoko Aizawa, Macroeconomics and sovereign debt. 30 November, 2016.
https://www.boell.de/en/2016/11/30/macroeconomics-and-sovereign-debt?dimension1=ds_g20_en

Conclusion

Rapidly growing debt levels in the age of financial globalization, both private and public, both banking and non-financial sector can become real hazard to global financial stability as any crisis is expected to spread far more quickly and widely, contributing to financial shocks around the world. Being detrimental to global economic growth and resilience, that presents a major challenge for the SDGs implementation.

It would be incorrect to say that the issue is not being considered. It is. But the way it is considered is too “narrow’ in comparison with potential consequences. So, the problem requires much broader consideration: at the global, not a group of countries, level; with enough attention paid to both private and public debts. Requirements for the bank’s capital were largely upgraded but no major fund exists to help them with their own money that could have been achieved with the introduction of the FTT at the G20 level. On the other hand, there is a similar fund for the governments, which is the IMF, but the amount of the resources available lag far behind the rapidly growing public and non-financial sector debt levels.

After the start of the global financial crisis, public debt in advanced economies and some systematically important emerging economies rose rapidly, which presents a real treat to the global financial stability and economic development. Governments tend to borrow unlimitedly but this can’t continue endlessly.

Much more attention of economists and policy makers should be drawn to the issue due to its high relevance. In a globalized world, if major economies fail under the burden of public debt, there will be no adequate response and assistance from the international financial institutions. Then there will break out a real economic chaos, compared to which the global financial crisis will be regard as a kind of “slight instability”.