

The Introduction of Windfall Taxes

During the course of 2022, the UK and the EU introduced their respective versions of a 'Windfall Tax' on Energy and Electricity Firms. The EU proposes to charge a levy on the surplus profits of fossil fuel firms and a levy on the excess revenues made from surging electricity costs. The UK, on the other hand, initially introduced in May 2022 a similar levy that applied to profits made by companies extracting UK oil and gas. In late-2022, this levy was raised to 35% and, simultaneously, an additional levy was also introduced on the excess profits of UK electricity generators.

These governments defended their stance by arguing that the oil and gas majors have recorded exceptional profits in the past two years on the back of soaring oil and natural gas prices that were driven by, in large part, exceptional events. The conflict between Russia and Ukraine, too, pushed up prices further over fears that the conflict will lead to energy shortages.

Households and businesses in these economies have taken a big hit. Apart from the indirect effects of fuel price-linked inflation, households have seen energy bills jump and governments – such as in the UK – have taken steps to subsidize energy bills for households at capped rates (currently proposed caps are at GBP 3,000 per annum per average household). These subsidies are being partly supported by the additional levies being charged on energy and electricity firms.

Although it is early days since the implementation of these proposals, there is some concern that these policies will have 'spillover' effects into other long-term factors including, among others, the development of EU and UK energy security, uncertainty in investment appetite, lack of investment in energy transition, employment and broader economic growth.

Oil and gas companies are, for the most part, concerned about the imposition of such taxes with some questioning the legality of such steps being taken by the Governments (<https://www.reuters.com/markets/commodities/exxon-sues-eu-move-block-new-windfall-tax-oil-companies-ft-2022-12-28/>). Others have also argued that these exceptional taxes may also push up inflation further, given that these proposals dilute the ability (and/or capital) to improve local supply-side energy shortfalls which is essential for long-term price stabilization.

Differences in the way these windfall taxes are being charged also creates uncertainty in the business environment. Individual countries have established their tax rates (in the EU, these range from 25% and upto 80%), tax bases (either sales, selling prices or profits) with various levels that are considered to be a 'windfall' threshold. It is also open to debate as to whether this could create changes in an economy's balance of payments.

The panel aims to engage you with a discussion around these topics. Below are links to articles and news reports that may help you gain some preliminary insight into windfall taxes. Feel free to search other sources to in preparing for your panel discussion:

<https://www.bbc.com/news/business-60295177>

<https://edition.cnn.com/2022/11/17/economy/windfall-tax-nuclear-uk-budget/index.html>

<https://taxfoundation.org/windfall-tax-europe/>

<https://taxfoundation.org/windfall-profits-tax-eu-energy-security/>

<https://www.imf.org/en/Publications/fandd/issues/2022/12/helping-europe-households-Celasun-lakova>

Questions:

1. You are presenting to your colleagues and, based on your understanding of the issues, wish to summarize the key advantages and disadvantages of the 'Windfall Tax' being proposed in Europe. In your opinion, what are the points that you would wish to highlight?
2. Having presented the pros and cons, how would defend your position to the critics of such a levy, who may argue that such extra taxes create potential disincentives for oil companies to invest their profits in new projects to either ease supply or, for that matter, develop newer sources of energy?
3. Should you be in the position of the EU or UK policy makers, what would you consider to be the most significant risks to the adopted policy? In the short and medium term?
4. What kinds of checks and balances would you think it necessary to include to ensure that there are no loopholes in the collection of the proposed levies from the companies?
5. What metrics would you consider to be relevant in measuring the success (or failure) of the EU/UK adopted policy? Why?
6. What spillover effects, if any, do you think these policies (either their success or failure) may have for the KSA economy?

Key Competencies covered -

- **Macroeconomics and Public Policy**
- **Medium Term Financial Planning and Sustainable Finance**
- **Leadership, Communication and Decision Making**