FACTSHEET

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Taxing Excess Profits

How can Austria identify and skim off excess profits of energy companies?

Summary

The Austrian Chamber of Labour (AK) and the Austrian Trade Union Federation (ÖGB) present a concrete model for taxing excess profits in the energy sector at 60% to 90%. There should be an immediate and full deduction for investments in renewable energy sources. The model is limited to the period from 2022 to 2024. From the estimated *annual* excess profits of about €4 billion to €5 billion in the period of validity, the AK-ÖGB model would deduct €1 billion to €1.5 billion for investments in renewables and skim off another €1.5 billion to €2.2 billion per year to finance anti-inflation measures.

Record inflation in Austria

According to the current WIFO forecast from June 2022, the average inflation rate in 2022 will be 7.8% – an upward revision as part of the autumn forecast is likely. This is the highest level since 1975. **The bulk of the inflation comes from the energy sector**. Energy companies are not only passing on imported price increases, but also driving up prices by increasing their profit margins, especially on electricity and fuel. In other words, the enormous excess profits for many energy companies are the flip side of the social costs to the population and the costly relief measures that taxpayers must finance.

Therefore, many European countries have been discussing for some time the introduction of windfall or excess profit taxes in the energy sector. Countries such as Romania, Italy, Spain, Hungary, and the United Kingdom have already implemented different models of taxation. Intensive debates are taking place in other countries such as Belgium and Germany. Most recently, the Czech government announced its intention to introduce a windfall tax on energy companies.

Figure 1: Countries with windfall or excess profits taxes

In Austria, after Chancellor **Nehammer**, also Vice-Chancellor **Kogler** has recently expressed support for the introduction of a windfall tax.

- *“Windfall profits in companies with state participation belong to the people and not to the companies alone.”*

  Austrian Chancellor Karl Nehammer in the Tiroler Tageszeitung on 5 May.

- *“My point is that we must come up with a feasible and constitutional proposal. And that’s not as easy as some people imagine who are just yelling and calling out for a windfall tax. We must be very precise about how we construct it.”*

  Austrian Vice-Chancellor Werner Kogler at ORF “Sommergespräch” on 15 August

AK and ÖGB now present a concrete model on how to implement such a tax.

Objective: the windfall tax should skim off part of the excess profits to finance anti-inflationary measures (such as for an energy price cap for households), while leaving sufficient leeway and incentive for the expansion of renewable energy sources, which is necessary to achieve climate goals.

The starting point for the windfall tax is record inflation in Austria, three-quarters of which is driven by rising energy prices, according to the Austrian Institute of Economic Research (WIFO). These, in turn, are largely based on the increased profit margins of energy companies – partly due to war-related distortions in the electricity market, and partly due to the exploitation of market power, e.g., in the petroleum industry. The energy companies are (at least partly) causally responsible for the record inflation and the associated economic costs. A temporary tax contribution by the sector to finance government aid programmes thus appears to be **constitutionally well justifiable** – like the Austrian bank levy in the wake of the financial crisis. Anyone who insinuates that the measure is arbitrary, and that other successful companies or sectors would also be "threatened" if it is introduced overlooks the factual justification of the excess profit tax by the economic crisis caused by record inflation.

Windfall tax – the model

The **taxable** entities are domestic energy companies. Based on the Italian model, these are mainly companies that:

- extract, produce, store, transport, supply, or trade natural gas, biomethane, liquified natural gas or other gases for the purpose of energy use
- generate[1], transmit, supply or trade electricity
- produce, store, supply, or trade crude oil
- produce, store, supply, or trade petroleum products

As in other European countries, the focus is on the level of the individual company and no group-approach is chosen. In the Austrian case a group-approach would have been interesting because OMV (Austrian Mineral Oil Administration Stock Company), Austria's biggest energy company, has large excess profits abroad. Nevertheless, the conventional single entity-approach is to be preferred as it promises more legal certainty and faster implementation.

There is a de minimis limit for micro-enterprises with turnover of up to €1 million.

The **object of taxation** (tax base) are the excess profits. These are the profits of the respective year compared to the reference profit (average of profits 2019 to 2021).[2]

The earnings base is **EBITDA**, i.e., **earnings before interest, taxes, depreciation, and amortization.** The advantage of this indicator is that it is strongly oriented to the operating business and thus best reflects the companies' excess profits. Distortions, e.g., due to the revaluation of investments, can be minimised.

Investments in renewable energy sources such as photovoltaic plants and wind turbines, attributed to a domestic operation or a permanent establishment in Austria may be deducted from excess profits. This corresponds to a kind of **super-deduction for renewables**, which, unlike the usual depreciation for wear and tear, are not spread over time, but are immediately deductible at 100% of the acquisition cost in the year of purchase.

[1] Exemptions for own use apply in accordance with § 2 Electricity Tax Act.

[2] To avoid distortions, an adjustment of profits is to be made in the case of reorganizations based on spin-off or merger balance sheets.

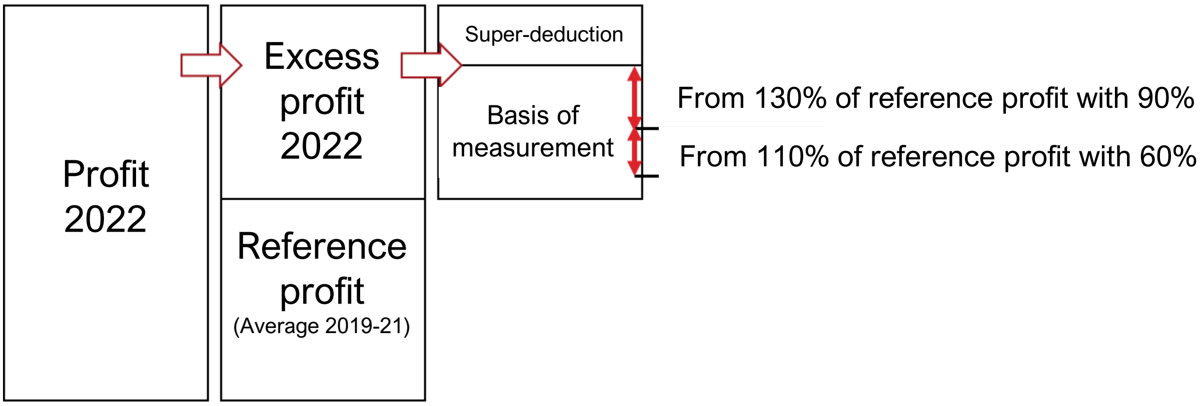
The **tax rate** is as follows: Percentage of profit from

- 110% of the reference profit: 60%
- 130% of the reference profit: 90%

To avoid double taxation, the windfall tax is deductible from income or corporation tax.

The de minimis limit of 10% ensures that, in addition to “normal profits”, a certain increase in profits is not subject to the windfall tax.

Figure 2: Schematic representation of how it works



The excess profit tax – like the “bank levy” – should be structured as a special levy, independent of the corporate income tax. This provides greater flexibility in design. Tax revenue shall exclusively flow to the federal government, responsible for financing the bulk of anti-inflation measures.

The tax is levied based on **declarations** made by taxable entities. The declaration could be made when drawing up the annual financial statements. This usually occurs in September of the following year. In the case of listed groups, where the financial statements are available earlier due to the annual general meetings being held in spring, the declaration can be made earlier.

Since excess profits in the energy sector can be expected to endure for several years (given no major geopolitical changes or changes in the design of energy markets), the **term** of the windfall tax should cover the years **2022 to 2024**. If the windfall tax is adopted in 2022, the recognition of excess profits in 2022 does not constitute a retroactive effect according to the Austrian’s Constitutional Court case law.

Numerical framework

The current market situation is associated with a high degree of uncertainty. This also applies to forecasts of the incidence of a windfall tax. However, based on the balance sheets and analysts' estimates for the largest energy companies (in particular Verbund and OMV), orders of magnitude can certainly be determined.

Figure 3: Expected revenue from an excess profit tax for Austria

in € billion	2022	2023	2024
Excess profits	4.2	5.3	4.0
Super-deduction renewables	1.3	1.3	1.3
Revenue from excess profit tax (gross)	2.1	3.0	2.0

Source: Own calculations based on company balance sheets and analysts' estimates

Excess profits of €4 billion to a good €5 billion are expected in the period under review. This is somewhat more conservative than the European Energy Agency's estimate[3].

Of this €4 to €5 billion, the AK-ÖGB model would

- deduct €1 to €1.5 billion for investment in renewables,
- €2 to €3 billion would be skimmed off, of which €1.5 to €2.2 billion would remain to finance the anti-inflation measures after deduction of the loss of corporation tax revenue.

These **revenues are urgently needed in budgetary terms**, as not only tax revenues but also government spending is at record levels. Austria is expecting a structural budget deficit of 3% to 3.5% of GDP for 2022. According to EU fiscal rules – which have been suspended – 0.5% would be permissible. The expectation that the situation would improve in 2023 is deceptive. In view of the foreseeable further increases in energy prices, it is to be expected that the anti-inflationary measures will not only have to be extended, but even expanded. It is negligent to pretend that the state has unlimited financial resources and that no counter-financing measures for the aid packages are necessary.

The sometimes discussed "**special dividends"** are no alternative to the windfall tax because these are only in prospect at Verbund and TIWAG and, in overall, are expected to generate significantly lower revenues. In the case of OMV, the state is a minority shareholder and cannot arrange for a special dividend. If it were agreed, it would mainly benefit private shareholders. In the case of smaller electricity or petroleum companies, ownership is purely private. In terms of equal skimming off of excess profits, the windfall tax is the more effective and fairer solution.

[3] The European Energy Agency has estimated that excess profits in the energy sector of the EU states will hit €200 billion. If this order of magnitude is applied to Austria with its EU-GDP share, this suggests excess profits of €5 to €6 billion.