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CAN Europe Position

AN EU TAX ON THE PROFITS AND OWNERSHIP OF THE FOSSIL FUEL INDUSTRY

CAN Europe supports a tax on the profits of the fossil fuel industry. It could be a permanent tax, or a temporary tax subjected to extension over time after assessing its impact. In addition to adopting an EU-coordinated tax, the EU should champion a tax on the fossil fuel industry at the global level.[1]

An EU Regulation would ideally be needed to ensure a coordinated introduction of such a tax in all Member States. This would reduce the scope for aggressive tax planning and tax avoidance (profit shifting) within the EU. The solidarity contribution on the fossil fuel industry (enshrined in the 2022 EU Council Regulation on an emergency intervention to address high energy prices) was providing a common frame with minimum common requirements (minimum tax rate, definition of windfall profit, etc) but left room for Member States to design the tax, taking into account national circumstances. Such an approach combining a common frame and national leeway seems a good precedent to build on.

Definition of fossil fuel industry/scope of the tax

We suggest building on the definition already used in EU law (Art. 2 of the 2022 EU Council Regulation on an emergency intervention to address high energy prices), but ask for:

- A lower threshold than 75% of their turnover from economic activities in the field of the extraction, mining, refining of petroleum or manufacturing of coke oven products (for example 51%);
- More fossil fuel-related economic sectors to be covered such as specialized transportation of fossil fuels, storage or sale of energy products derived from fossil fuels.

A very low threshold would end up heavily taxing the profits from non-fossil fuel-related activities - which is not the goal, especially if these activities relate to renewables. Thereby the need to strike the right balance. In order to disincentivise fossil fuels-related activities, the threshold could also be higher to start with and be reduced over time.

[1] For more on the relationship between EU coordination or regulation and international approaches see CAN Europe / New resources for public climate finance and for the Loss and Damage Fund

Tax design

CAN Europe supports in particular **three possible tax designs** for an EU-coordinated tax on the profits and ownership of the fossil fuel industry, which represent various levels of ambition, revenue-raising potential and political feasibility:

- A top-up tax on Member States standard corporate taxes;
- A tax on the excess profit of fossil fuel companies (excess profits preferably defined as return on capital investment above a certain percentage), which could be part of an excess profit tax covering also other or all sectors of the economy; or
- A tax on extreme wealth (see position here) with an additional tax on fossil fuel wealth, i.e. a shareholder pollution top-up tax (taxing ownership of fossil fuel assets, and dividends or transactions of such assets).

The tax base

For a tax on the top of Member States' standard corporate tax rate, the rate could be homogenous across the EU and not related to the level of profits. The tax base could be defined in respective national laws, or based on harmonised principles at the EU level to reduce the risk of profit shifting. Such a top-up tax may be easy to apply by Member States.

For an excess profit tax, the tax could be based on the invested capital approach. The latter considers everything earned above a specified return rate on capital or total assets of a company as excessive and subject to excess profits taxation. Windfall profits come unexpectedly due to external events (like the war in Ukraine in 2022). They are calculated by comparing profits made in a year to profits made on average during a certain period used as a reference period (the EU temporary solidarity contribution used the years 2018-2021 as the reference period). Excess profits include windfall profits but also profits resulting from other structural reasons like monopoly power, patents, network effects etc. Tackling excess rather than only windfall profits based on the return on capital method may be more appropriate for a tax that lasts beyond the exceptional event that generated windfall profits. It would provide greater predictability for tax administrations and fossil fuel companies. If capital investments can be deducted from the company's tax bill, this should be strictly limited to investments in renewable energy and related storage capacity. Excess profits (in the fossil fuel sector and beyond) are a symptom of a non-competitive market and monopolistic positions. They fuel the concentration of wealth and inequality.[2] Therefore, an excess profits tax is also a response to the structural imbalances (excess corporate power) in our economy more generally and could apply beyond the fossil fuel industry. The excess profit tax on the fossil fuel industry could involve higher tax rates based on the polluter pays principle (see below).

A tax on shareholders would be based on the ownership of stock in fossil fuel companies, taxing capital gains and/or dividends and/or transactions of polluting

[2] UNCTAD, Corporate Rent-Seeking, Market Power And Inequality: Time For A Multilateral Trust Buster?, 2018

assets, including fossil fuel companies' share buybacks[3] (companies buying their own shares, which reduces their number, creates scarcity and increases their price). In case a wealth tax is being adopted in the EU, we could demand a higher tax rate on fossil fuel assets. Alternatively, such a tax could potentially precede and pave the way for a more general wealth tax.

The tax rate

The **tax rate** in the EU temporary solidarity contribution was at least 33%. For an excess profits tax inspired by the solidarity contribution, the minimum tax rate could be **higher** than 33% and/or could increase over time potentially up to a 100% tax rate on excess profit. Progressive taxation rates could apply, depending on the level of profits. For example, researchers have been suggesting an additional 20% rate for 'base' excess profits – profits between a rate of return of 10% and 15%; while an additional 40% rate would apply for 'super' excess profits – profits above a rate of return of 15%.

However, in light of the necessity to disincentivise investments in fossil fuel, CAN Europe supports higher tax rates and a lower threshold of return on investment to define excess profits. It is important to connect the tax rate with the tax base as generous exclusions from the tax base mean the high rate applies to a limited scope. For example, Norway applies a high tax rate on profits (78%), but the Norwegian government takes 88% of the investment costs, which is encouraging further extraction and substantially reduces the impact of a high tax rate.

To prevent fossil fuel companies from passing the tax on to energy consumers, we are asking for **flanking measures** such as price caps and other pricing measures aimed at guaranteeing a right to energy for essential needs, while encouraging a reduction in luxury energy use. Solutions may be diverse in different Member States. To prevent the fossil fuel industry from passing the cost of the tax on to workers, specific provisions could be considered to ensure full respect for the right to collective bargaining (cf notably respect of the EU 2022 Directive on adequate minimum wages).

Use of proceeds

The EU Regulation establishing a solidarity contribution provides a good precedent regarding the use of proceeds, as it includes a list of possible uses that notably aim at mitigating the effects of high energy prices on customers (in particular vulnerable households), including by promoting their investments into renewables or energy efficiency investments. Member States could also for example use the proceeds to invest in energy grids and storage. In addition, part of the proceeds of a new tax should be dedicated to international climate finance for adaptation, mitigation and loss and damage.

[3] See The Guardian / Big five oil companies to reward shareholders with record payouts and SOMO / Why share buybacks are bad for the planet and people

➢ **Read more on CAN Europe's [background discussion paper on the EU tax options on the profits and ownership of the fossil fuel industry]**

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