ARTICLE

The Return of Windfall Taxation

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Windfall taxes are not new to the world, but they have assumed a variety of shapes and formats under different names in each country and period. Sometimes, they are designed to be applied on a one-time or temporary basis while, at other times, they coexist with classic forms of income taxation. Sometimes they are imposed on actual profits or net earnings while, at other times, they use alternative tax bases. In one way or another, imposing surtaxes on windfall-like gains has been repeatedly legitimized by society's frustration that well-positioned individuals and firms retain unearned, excessive financial rewards, especially under distorted market or regulatory conditions. With the current global energy and food prices crises, windfall taxes have once again risen to broad popularity. This article examines the historic, economic, and policy rationales for windfall taxation, arguing that lawmakers could use the accumulated experience of the past to go beyond attempts to tax current crisis-driven high returns to ultimately build corporate tax systems that are more progressive.

Keywords: Corporate taxation, windfalls, excess profits, unearned gains, crises, economic theories, normative principles, historical analysis, fiscal progressivity.

1 Introduction

Windfall taxes are a special regulatory tool that are used to regain value for society that was privately captured through means other than the productive application of capital, labour, or ingenuity. Oftentimes, windfalls are associated with abnormal levels of profitability that result from market-spanning distortions, broad legislative failures, or other structurally unfair circumstances including wars and pandemics. As such, taxpayers cannot claim to have invested a particular effort, expertise, or contribution that is deserving of protection against taxation because they do not fully control the processes and actions that create a windfall gain.

In light of the increasing interest in windfall taxes first sparked by Covid-19 and then fortified by the global energy and food prices crises that ensued after Russia invaded Ukraine, this article assesses the theory and practice of taxing above-normal earnings at higher rates. First, it delineates the theoretical foundations of windfall taxation, explaining the meaning of windfalls in relation to other forms of extraordinary profits and the tax policy principles that justify imposing surcharges on specified large amounts. It subsequently presents the most popular tax measures adopted by countries to catch corporate windfalls beginning in the world war period and continuing through today's climate of widespread social unrest. The article concludes that the recent return of windfall taxation might signal a renewed concern with fiscal progressivity, thus providing a unique opportunity to reconsider the broader goals and structure of corporate tax systems.

2 The theory of windfall taxation

Before examining real-world examples of windfall taxes, it is important to understand the fundamentals behind the idea of subjecting increased profit margins to heavier taxation. This part opens with a discussion on what windfalls are and how they might differ from other forms of exceptional private gains. It then considers economic and philosophical theories that provide normative justification for taxing windfalls at higher rates.

2.1 *What are Windfalls?*

In both technical and nontechnical talks about taxation, 'windfall profits' are sometimes used interchangeably with expressions such as 'economic rent', 'economic surplus',

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'abnormal profits', 'excess profits', 'nonroutine profits', 'residual profits', 'super-profits', 'surplus profit', 'extraordinary profits', 'supernormal profits', 'extra-normal profits', 'above-normal profits', and even 'excessive profits'.[1] The specialized literature in economics and law provides no single definition for these terms, but it is common to link them, to different degrees, to anomalous economic phenomena that lead to high levels of profitability. To delimit what might be within and outside the scope of windfall taxes, it is of value to attempt to create a taxonomy of different types of profit.[2]

In a figurative context, a windfall indicates something beneficial yet unearned, meaning an 'unexpected acquisition or advantage' that is connected to luck or chance rather than effort or planning.[3] The common use of the term intertwines with a lack of causality between the actions of the recipient and the acquired benefit while implicitly reflecting a moral judgment about the undeserving nature of the additional income inflow. These elements, however, are not always present in everything that is characterized as a windfall. For example, lottery or gambling winnings are often called windfalls. However, there is no denial that, despite depending on luck, there is some causal link between the act of purchasing a lottery ticket or placing a bet and being awarded a money prize that the winner is entitled to keep.[4] Nevertheless, even in this case, there is an argument to be made that 'winners of lotteries who had minimal active involvement in securing their earnings would not "deserve" their income and could be subject to a higher rate or perhaps a surcharge'.[5]

Concerning corporations, the use of the term windfall to describe some classes of profits typically carries a negative connotation in the sense of excessive profits.[6] As such, corporate windfalls are equated with profiteering, that is, the process by which firms do not obtain gains by engaging in value-creating endeavors. Instead, they are made by manipulating or taking advantage of an impaired social, political, and/or legal context (what economists tend to call rent-seeking behaviour).[7]

The rhetorical appeal of this prohibitive overtone works as a powerful asset in political discourse by means of securing the social acceptability of corrective measures that otherwise could be seen as radical and unjustified. Attaching the word windfall to a tax for which the objective is essentially to return a portion of a company's overall earnings (however defined) to the public creates a scenario that the electorate considers as not only necessary for revenue purposes but also legitimate and fair.[8] However, if the relied upon idea of windfall is perceived as overly subjective, arbitrary, or lacking a compelling reason for action, voters might feel disinclined to support the corresponding tax measure.[9]

In legal doctrine, there are few works dedicated to formulating a more technically objective concept of a windfall. One such work was carried out by legal scholar Eric Kades. He proposed that windfalls should be generally understood as 'economic gains independent of work, planning, or other productive activities that society wishes to reward'.[10] To some extent, this concept overlaps with that of rents used by economists[11] but, as Kades observes, 'not all rents are windfalls'.[12] He exemplifies this with a

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1 A. Christians, *Making Sense of Abnormal, Excess, Non-Routine, Super-Normal, Residual, and Windfall Profits*, 12 Tax & Monop. Focus 16 (2022); R. Boadway, *Tax Policy for a Rent-Rich Economy*, 41 Can. Pub. Pol'y 253 (2015), doi: 10.3138/cpp.2015-044; M. P. Devereux et al., *Taxing Profit in a Global Economy* 23–24 (Oxford University Press 2021).

2 For critiques on the improper use of the labels 'windfall profit' and 'windfall tax', *see* A. Verbruggen, *Windfalls and Other Profits*, 36 Energy Pol'y 3249 (2008), doi: 10.1016/j.enpol.2008.05.032; N. Bock & L. R. Rodriguez, *A Comparison of Windfall Tax Methodologies in Different Fiscal Regimes*, Int'l Petroleum Tech. Conf. (15 Nov. 2011), doi: 10.2523/IPTC-14897-MS (accessed 20 Mar. 2023).

3 *Windfall*, in *Oxford English Dictionary Online* (Oxford University Press 2023) (accessed 1 Apr. 2023). According to etymologists, the term derives from medieval England when commoners were not allowed to cut down trees for their personal consumption but could keep and make whatever use of branches broken or blown down by the wind. W. Morris & M. Morris, *Windfall*, in *Morris Dictionary of Word and Phrase Origins* (Harper & Row 1977).

4 A separate tax-related question is whether the winner should keep the entire amount tax free. Countries in which their tax systems adopt a comprehensive or global approach to taxable income, such as the United States, usually include any windfalls, including those obtained through gambling, betting, lotteries, and other games with prizes, in the personal income tax base. *See* e.g., L. Kreiser & E. Jowitt, *The Taxation of Gambling Winnings in Australia and the United States: A Comparative Study*, 19 Int'l Tax J. 75 (1993) (arguing that, differently from the United States, Australian statutory and case law is uncertain about the taxability of gambling winnings). Others like Canada that lists all possible productive sources of income in the Income Tax Act, might not tax windfalls on the theory that they do not fit a predefined statutory source unless the windfall-generating activity is carried out in the course of a business. *See* Income Tax Folio S3-F9-C1, Lottery Winnings, Miscellaneous Receipts, and Income (and Losses) from Crime, https://www.canada.ca/en/revenue-agency/services/tax/technical-information/income-tax/income-tax-folios-index/series-3-property-investments-savings-plans/series-3-property-investments-savings-plans-folio-9-miscellaneous-payments-receipts/income-tax-folio-s3-f9-c1-lottery-winnings-miscellaneous-receipts-income-losses-crime.html (accessed 20 Apr. 2023).

5 S. M. Sheffrin, *What Role Can Desert Play in Designing Tax Policies?*, 15 Pitt. Tax Rev. 137 at 153 (2017), doi: 10.5195/TAXREVIEW.2017.64.

6 *See* C. Hurt, *The Windfall Myth*, 8 Geo. J.L. & Pub. Pol'y (2010).

7 S. Chakraborty & E. Dabla-Norris, *Rent Seeking*, 53 IMF Staff Papers 28 (2006).

8 Section 2.1 analyses legitimacy and fairness arguments for windfall taxes.

9 *See* e.g., M. Weinzierl, *Popular Acceptance of Inequality Due to Innate Brute Luck and Support for Classical Benefit-Based Taxation*, 155 J. Pub. Econ. 54 (2017), doi: 10.1016/j.jpubeco.2017.09.007.

10 E. Kades, *Windfalls*, 108 Yale L.J. 1489, 1491 (1998), doi: 10.2307/797442.

11 UN, *Handbook on Selected Issues for the Taxation of the Extractive Industries by Developing Countries* (UN 2017), at 423 ('Rents (sometimes called "windfalls") are the financial returns above those a company requires to make the investment profitable'.).

12 Kades, *supra* n. 10, at 1496.

talented athlete whose unique skills in combination with time and effort of practicing, secures an outstanding paycheck.[13] To be sure, the athlete's income can still be subjected to heavier tax rates for progressivity reasons, but the justification in this case is unrelated to an unanticipated and fortunate event.[14]

The economics literature contains different definitions of rents such as those proposed by David Ricardo and Vilfredo Pareto,[15] and authors also make a distinction between pure or true rents, on the one hand, and temporary or quasi-rents, on the other.[16] In their pure form, rents signify returns that exceed the opportunity cost of carrying on an activity or, simply stated, everything above what is needed for an enterprise to remain in operation. Economic theory predicts that rents should be equal to zero under perfect competition as participants would not be able to impose prices higher than marginal costs.[17] Thus understood, economic rents have less to do with whether certain earnings are deserving or could have been anticipated by the beneficiary, though the expression might indicate an underlying macro- or microeconomic problem leading to abnormal profits.[18]

Without the adjective 'abnormal', profits are broadly defined as the difference between revenues (that is, consideration received for the delivery of goods or provision of services) and costs regularly incurred to generate revenues (such as interests, rents, wages, and other business expenses).[19] In principle, any amount that surpasses what is considered a normal return expected by investors could be dubbed an 'abnormal profit' (or extra-normal, supernormal, above-normal, or nonroutine). Depending upon where the threshold of normalcy is established, part of the surplus could still be considered the outcome of planning and effort by the recipient. For example, extraordinary or super profits can be a sign of the presence of monopolistic or quasi-monopolistic actors in the market. However, substantial amounts of earnings can also be attributable to special location or firm-specific features that provide some businesses with a competitive advantage (what economists sometimes call market power) that is not necessarily unfair or objectionable.[20] The latter situation is exemplified by the high frequency of surplus profits in the extractive or energy sectors even when there are no obvious industry- or economy-wide inefficiencies.

One way to view corporate windfalls is as a subcategory of abnormal profits that are specifically related to fortuitous and unforeseen circumstances beyond the company's control. A classic example is a sudden increase in commodity prices due to scarcity, regulatory changes, or other external factors. In this perspective, the risks and investments an oil company undertakes to discover a new oil deposit might produce supernormal returns, but additional revenues from a price hike confer an unexpected bonus.[21] Outside bright-line cases like these, making a distinction between acceptable and unacceptable high profits can be seen as a somewhat arbitrary line-drawing exercise. However, doing so could well be considered as no more arbitrary than current practices of defining categories of income as required by existing tax systems (including the application of tax treaties)[22] that is also an integral part of upcoming reforms debated at the global level.[23]

Given that profits (and, even more so, taxable profits) are not an observable physical manifestation of a natural phenomenon, establishing the boundaries of what is a normal return and what is excessive might always require achieving compromises at the level of politics and principles. To illuminate this process, the next section turns to normative theories of tax policy.

2.2 *Why Tax Windfalls?*

Unexpected gains stemming from exceptional economic situations tend to singularly benefit a few taxpayers.

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[13] *Ibid.*

[14] Yet, the athlete's income-generating talents could be counted within a comprehensive theory of distributive justice as part of what philosopher John Rawls famously referred to as the 'natural lottery'. J. Rawls, *A Theory of Justice* 64 (2d ed., Harvard University Press 1999), ('We may want to adopt a principle which […] mitigates the arbitrary effects of the natural lottery itself'.).

[15] The first author defined rents as 'the excess amount earned by a factor over the sum necessary to induce it to do its work' while the second as 'the excess earnings over the amount necessary to keep the factor in its present occupation'. R. H. Wessel, *A Note on Economic Rent*, 57 Am. Econ. Rev. 1221, 1222 (1967).

[16] Quasi-rents are temporary in the sense that present-day high returns will likely be offset by high marginal costs in the long term. *See* e.g., J. Bankman, M. A. Kane & A. O. Sykes, *Collecting the Rent: The Global Battle to Capture MNE Profits*, 72 Tax L. Rev. 197, 200 (2018); D. Shaviro, *Mobile Intellectual Property and the Shift in International Tax Policy from Determining the Source of Income to Taxing Location-Specific Rents: Part One*, 2020 Sing. J. Legal Stud. 681, at 681–682 (2020), doi: 10.2139/ssrn.3448070.

[17] *See generally* L. Phlips, *The Economics of Price Discrimination* (Cambridge University Press 1983).

[18] *See* W. Griffiths, P. H. Jensen & E. Webster, *What Creates Abnormal Profits?*, 58 Scott. J. Pol. Econ. 323 (2011), doi: 10.1111/j.1467-9485.2011.00549.x; G. Schwerhoff, O. Edenhofer & M. Fleuerbaey, *Taxation of Economic Rents*, 34 J. Econ. Surveys 398 (2020), doi: 10.1111/joes.12340.

[19] R. Griffith & H. Miller, *Taxable Corporate Profits*, 35 Fisc. Stud. 535 (2014), doi: 10.1111/j.1475-5890.2014.12041.x.

[20] *See* L. Kaplow, *On the Relevance of Market Power*, 130 Harv. L. Rev. 1303 (2017); L. Kaplow, *Market Power and Income Taxation*, 13 Am. J. Econ. Pol'y 329 (2021), doi: 10.1257/pol.20200103; K. A. Bamberger & O. Lobel, *Platform Market Power*, 32 Berkely Tech. L.J. 1051 (2017).

[21] UN, *supra* n. 11, at 367.

[22] *See* e.g., D. A. Weisbach, *Line Drawing, Doctrine, and Efficiency in the Tax Law*, 84 Cornell L. Rev. 1627 (1999), doi: 10.2139/ssrn.106728; D. A. Weisbach, *An Efficiency Analysis of Line Drawing in the Tax Law*, 29 J. Legal Stud. 71 (2000), doi: 10.1086/468064.

[23] *See* e.g., T. D. Magalhães & A. Christians, *Rethinking Tax for the Digital Economy After COVID-19*, 11 Harv. Bus. L. Rev. 1 (2021), doi: 10.2139/ssrn.3635907; J. Lammers, *The OECD Concept of User Participation and a More Pragmatic Way to Tax Rent Seeking*, 96 Tax Notes Int'l 611 (2019).

Therefore, it is understandable that windfall taxes might occasionally be perceived as a type of policy based on envy or jealousy that penalizes those who were lucky enough to be in the right place at the right time. To the contrary, their core function, broadly considered, is to capture abnormal and undeserved earnings associated with one or some of the following: Destabilizing macro-events such as wars, pandemics, and crises in general; system-level regulatory imperfections such as a lack of proper or effective legislation; or unjustified enrichment as a result of predatory behaviour including price gouging and other forms of rent seeking.

In normative tax policy terms, windfall taxes are often defended on fairness and efficiency grounds even if, in practice, they might attract criticism based on administrability reasons including complexity and uncertain revenue-generating capacity.[24] As the latter is a pragmatic type of argument that concerns design and enforcement, it will be discussed in the next section in which concrete experiences with windfall taxes are examined. The other two arguments – the first deontological and the other consequentialist[25] – accommodate a variety of reasons for why windfall profits should or could be subject to additional taxes.

Beginning with fairness, surcharges on high-level profit margins have long been advocated as 'a measure that would recognize the so-called ability to pay of corporations more adequately than other profits taxes'.[26] Used in this context, ability to pay reflects a concern with tax equity in its vertical dimension yet specifically encompasses not only individuals (natural persons) but also corporate taxpayers (juridical persons).[27] The origins, meaning, and import of vertical and horizontal equity in the distribution of tax burdens among (physical or corporate) taxpayers have been debated for decades by economists, tax scholars, and philosophers.[28] The two mentioned metrics are also routinely contrasted with the rival theory of taxation based on benefits.[29]

Despite persistent discord among tax theorists, most legal systems appear to accept the notion that taxes should be imposed equally on those that are, economically speaking, equally situated while taking more from those that earn more (usually measured by actual income but theoretically any other tax base could be used for these purposes).[30] With respect to above-normal returns, the ability-to-pay principle might be interpreted according to vertical equity in order to suggest that the business enterprise has an above-normal economic capacity to contribute to society through the payment of taxes.[31]

In scholarship and policy debate, economic capacity to pay taxes is often linked to the concept of 'sacrifice' as reflected in the influential equal-sacrifice principle articulated by the utilitarian philosopher and political economist John Stuart Mill.[32] To the extent sacrifice is understood as welfare loss, a tax system should strive to make taxpayers sustain the same real economic cost as opposed to merely the same monetary value. Accordingly, it is equitable to ask those who earn more to pay additional taxes because they can afford the extra burden – in true economic terms – without diminishing much of their wellbeing. Even under a highly progressive tax scheme, the financially advantaged still retain an abundance, and taking away their last dollars imposes a relatively small loss of welfare compared to the welfare

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[24] Tax policy analysis can be positive (describing the functioning of a tax system without making explicit value judgments) or normative (applying evaluative criteria such as equity, economic efficiency, and administrative capacity). A. Christians, *Introduction to Tax Policy Theory*, SSRN (14 Jun. 2018), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3186791. On theories of taxation more generally, *see* M. Stewart, *Tax and Government in the 21st Century* (Cambridge University Press 2022).

[25] On this distinction, *see* L. Murphy & T. Nagel, *The Myth of Ownership: Taxes and Justice*, 42–45 (Oxford University Press 2002); S. Leviner, *From Deontology to Practical Application: The Vision of a Good Society and the Tax System*, 26 Va. Tax Rev. 405 (2006); B. H. Fried, *Facing Up Scarcity: The Logic and Limits of Nonconsenquentialist Thought* (Oxford University Press 2020), doi: 10.1093/oso/9780198847878.001.0001.

[26] A. G. Buehler, *The Taxation of Corporate Excess Profits in Peace and War Times*, 7 Law & Contemp. Probs. 291, 292 (1940), doi: 10.2307/1189623.

[27] *See* e.g., American Economic Association, *The Taxation of Excess Profits in Great Britain: A Study of the British Excess Profits Duty in Relation to the Problem of Excess Profits Taxation in the United States*, 10 Am. Econ. Rev. 4, 152 (1920).

[28] For the different positions among economists and tax scholars, *see* M. Slade Kendrick, *The Ability-to-Pay Theory of Taxation*, 29 Am. Econ. Rev. 1 (1939); A. G. Buehler, *Ability to Pay*, 1 Tax L. Rev. 243 (1946); P. R. McDaniel & JR. Repetti, *Horizontal and Vertical Equity: The Musgrave/Kaplow Exchange*, 10 Fla. Tax Rev. 607 (1993); A. J. Auerbach & K. A. Hassett, *A New Measure of Horizontal Equity*, 92 Am. Econ. Rev. 1116 (2002), doi: 10.1257/00028280260344650; J. Repetti & D. Ring, *Horizontal Equity Revisited*, 13 Fla. Tax Rev. 135 (2012), doi: 10.5744/ftr.2012.1332; I. K. Lindsay, *Tax Fairness by Convention: A Defense of Horizontal Equity*, 19 Fla Tax Rev. 79 (2016), doi: 10.5744/ftr.2016.1000. For a philosophical perspective, *see* Murphy & Nagel, *supra* n. 25 (arguing that both dimensions of tax equity have no moral value).

[29] *See* e.g., D. T. Krauss, *The Benefit Theory of Taxation*, 11 Tenn. L. Rev. 226 (1932–1933); G. S. Cooper, *The Benefit Theory of Taxation*, 11 Austl. Tax F. 397 (1994); D. G. Duff, *Benefit Taxes and User Fees in Theory and Practice*, 54 U. Toronto L.J. 391 (2004), doi: 10.1353/tlj.2004.0013; J. M. Dodge, *Theories of Tax Justice: Ruminations on the Benefit, Partnership, and Ability-to-Pay Principles*, 58 Tax Law Rev. 399 (2005); M. Weinzierl, *Revisiting the Classical View of Benefit-Based Taxation*, 128 Econ. J. F37 (2018), doi: 10.1111/ecoj.12462; R. Scherf & M. Weinzierl, *Understanding Different Approaches to Benefit-Based Taxation*, 41 Fisc. Stud. 385 (2019), doi: 10.1111/1475-5890.12204; B. H. Fried, *The Case for a Progressive Benefits Tax*, in *Taxation: Philosophical Perspectives* (M. O'Neill & S. Orr eds, Oxford University Press 2018).

[30] *See* e.g., H. Silverson, *Earned Income and Ability to Pay*, 3 Tax L. Rev. 299 (1948); A. Gunnarsson, *Ability to Pay in New Zealand's Tax System*, 27 Victoria U. Wellington L. Rev. 697 (1997), doi: 10.26686/vuwlr.v27i4.6098; S. Utz, *Ability to Pay*, 23 Whittier L. Rev. 867 (2002), doi: 10.1023/A:1024448316675; R. A. de Mooij & L.G.M. Stevens, *Exploring the Future of Ability to Pay in Europe*, 14 EC Tax Rev. 9 (2005), doi: 10.54648/ECTA2005003; C. A. D. Crespo, *The 'Ability to Pay' as a Fundamental Right: Rethinking the Foundations of Tax Law*, 50 Mex. L. Rev. 49 (2010); J. Englisch, *Ability to Pay*, in *Principles of Law: Function, Status and Impact in EU Tax Law* (C. Brokelind ed., IBFD 2014); F. Vanistendael, *Ability to Pay in European Community Law*, 23 EC Tax Rev. 121 (2014), doi: 10.54648/ECTA2014013.

[31] T. S. Adams, *The Taxation of Business*, 11 Nat'l Tax Ass. 185, 191 (1917) ('if we succeed, approximately, in determining what is the normal income and lay the tax upon the net income in excess of that normal return, we have a tax that may permanently endure. It represents, as it were, the share of the state in the "supernormal" success of every business enterprise'.).

[32] J. S. Mill, *Principles of Political Economy with Some of Their Applications to Social Philosophy* 213–214 (S. Nathanson ed., Hackett Publishing 2004).

increases arising for those to whom the collected money is redistributed or on whom it is spent via government-funded public services.[33]

Windfalls provide stronger reasons for progressive taxation, however.[34] Since gains that suddenly accrue to a person or firm do not raise legitimate expectations,[35] taxation imposes no genuine sacrifice or loss for the taxpayer. Perhaps the most appropriate analogy are the justifications provided for heavily taxing inherited wealth.[36] For example, the 1978 Report by the Institute of Fiscal Studies chaired by Nobel Prize-winning economist James Meade proposed an additional tax on gratuitous transfers because '[t]he citizen who by his own effort and enterprise has built up a fortune is considered to deserve better tax treatment than the citizen who, merely as a result of the fortune of birth, owns an equal property'.[37] The legitimacy of such proposals has sometimes been condemned for unduly interfering with private relationships between family members.[38] However, the issue is entirely absent in the case of windfall profits that arise independently of any acumen or special abilities of a company's investors, managers, and workers.

Nevertheless, some economists have questioned the appropriateness of the ability-to-pay theory in dealing with abstract legal persons. Alfred Buehler, for example, argued in 1940 that an excess profits tax could not be justified on ability to pay alone because businesses 'do not possess ability to pay in any personal sense and can only be said to have an impersonal capacity to pay taxes'.[39] For lawyers and courts, the ability-to-pay principle remains relevant for corporate taxation given that, according to the law, juridical persons are recognized as taxpayers with both rights and obligations.[40] This includes the capacity – objectively – to contribute to society by paying taxes in amounts commensurate to a company's level of profitability and financial success.[41]

Either way, 'simply because a corporation itself does not have any ability to pay does not mean a normative justification for the corporate tax on the grounds of fairness does not exist', as Kim Brooks properly notes.[42] This was recognized by Buehler himself who wrote that imposing higher-than-standard rates of tax on high profit ratios was 'from a number of angles, […] more equitable than other forms of profits taxation'.[43] Buehler's recommendation was to target monopolies, especially '[w]here governmental price control is ineffective or impracticable'.[44] This argument has been invoked by many others,[45] but it implies the use of taxation for regulatory purposes rather than redistribution or fairness per se.

A proposal along those lines was put forward by Reuven Avi-Yonah and Lior Frank.[46] In particular, the former has long argued that taxation has three legitimate goals that may or may not overlap depending on the tax and may also change over time. These goals are revenue generation, redistribution, and regulation.[47] When the United States first adopted a corporate tax in 1909, for example, the original intent was to curb monopoly power (thus, to use the regulatory function of taxation), but the tax was ultimately absorbed by the tax system as a permanent revenue source.[48] Defending a return to the corporate tax's roots, Avi-Yonah proposes exempting normal

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[33] This argument relies on the assumption that money has a declining marginal utility, i.e., the more money that an affluent person earns, the less value it brings in terms of welfare enhancement; the opposite is true for the less financially advantaged. *See* e.g., M. S. Stein, *Diminishing Marginal Utility of Income and Progressive Taxation: A Critique of the Uneasy Case*, 12 N. Ill. U. L. Rev. 373 (1992); S. B. Lawsky, *On the Edge: Declining Marginal Utility and Tax Policy*, 85 Minn. L. Rev. 904 (2011).

[34] E. D. Fagan, *Recent and Contemporary Theories of Progressive Taxation*, 46 J. Pol. Econ. 457, 490 (1938), doi: 10.1086/255258. *See also* B. H. Fried, *The Puzzling Case for Proportionate Taxation*, 2 Chapman L. Rev. 157 (1999) (rejecting flat-rate taxes on fairness grounds); B. H. Fried, *Proportionate Taxation as a Fair Division of the Social Surplus: The Strange Career of an Idea*, 19 Econ. & Phi. 211 (2003), doi: 10.1017/S0266267103001135 (refuting libertarian and quasi-libertarian arguments against progressive taxation).

[35] For an argument that legitimate expectations cannot, in any event, be generally invoked to shield market outcomes against redistributive policies, *see* N. Hsieh, *Moral Desert, Fairness and Legitimate Expectations in the Market*, 8 J. Pol. Phil. 91 (2000), doi: 10.1111/1467-9760.00094.

[36] *See* e.g., D. G. Duff, *Taxing Inherited Wealth: A Philosophical Argument*, 6 Can. J. L. & Jurisprudence 3 (1993), doi: 10.1017/S0841820900001788; A. L. Aslott, *Equal Opportunity and Inheritance Taxation*, 121 Harv. L. Rev. 469 (2007); T. Nagel, *Liberal Democracy and Hereditary Inequality*, 63 Tax L. Rev. 113 (2009); J. Bird-Pollan, *The Philosophical Foundations of Wealth Transfer Taxation*, in *Philosophical Foundations of Tax Law* (M. Bhandari ed. Oxford University Press 2017).

[37] Institute for Fiscal Studies, *The Structure and Reform of Direct Taxation: Report of a Committee Chaired by Professor J. E. Meade* 318 (Routledge 1978).

[38] For this debate, *see* A. L. Aslott, *Family Values, Inheritance Law, and Inheritance Taxation*, 63 Tax L. Rev. 123 (2009); L. L. Batchelder, *What Should Society Expect from Heirs? The Case for a Comprehensive Inheritance Tax*, 63 Tax L. Rev. 1 (2009), doi: 10.2139/ssrn.1274466; J. Bird-Pollan, *Death, Taxes, and Property (Rights): Nozick, Libertarianism, and the Estate Tax*, 66 Me. L. Rev. 1 (2013); S. White, *Moral Objections to Inheritance Tax*, in M. O'Neill & S. Orr eds, *supra* n. 36.

[39] Buehler, *supra* n. 26, at 298.

[40] *See* e.g., C. Bardini, *The Ability to Pay in the European Market: An Impossible Sudoku for the ECJ*, 38 Intertax 2 (2010), doi: 10.54648/TAXI2010001.

[41] The authors extend gratitude to Karl Pauwels for this point.

[42] K. Brooks, *Learning to Live with an Imperfect Tax: A Defence of the Corporate Tax*, 36 U.B.C. L. Rev. 621, 631 (2003).

[43] Buehler, *supra* n. 26, at 299.

[44] *Ibid.*

[45] *See* e.g., C. L. Harriss, *Monopoly and the Excess Profits Tax*, 16 Tax Magazine 717 (1938); B. Higgins, *Post-War Tax Policy*, 9 Can. J. Econ. & Pol. Sci. 408 (1943), doi: 10.2307/137254; Boadway, *supra* n. 1; Roosevelt Institute, Balanced Economic Project & Tax Justice Network, *Tax and Monopoly*, 12 Tax Justice Focus Series 2 (2022); D. Kreutzer & D. R. Lee, *On Taxation & Understated Monopoly Profits*, 39 Nat'l Tax J. 241 (1986), doi: 10.1086/NTJ41792177.

[46] R. S. Avi-Yonah & L. Frank, *Antitrust and the Corporate Tax: Why We Need Progressive Corporate Tax Rates*, Tax Notes Int'l 1199 (2020), doi: 10.2139/ssrn.3549006.

[47] R. S. Avi-Yonah, *The Three Goals of Taxation*, 60 Tax L. Rev. (2006), doi: 10.2139/ssrn.796776.

[48] R. S. Avi-Yonah, *Corporations, Society, and the State: A Defense of the Corporate Tax*, 90 Va. Tax Rev. 5 (2004).

returns via 'expensing' (which is economically equivalent to providing annual allowances for the deduction of capital expenditures, that is, the cost of capital)[49] and then applying a sharply high rate of tax (for example, 80%) to incomes above ten billion per year.[50]

The most straightforward argument for taxing windfall profits is that gains arising from brute luck, happenstance, or coincidence can theoretically be safely taxed, even in their entirety (i.e., at a 100% rate) without imposing negative effects on future behaviour.[51] The idea is simple: Shareholders would face no special incentive to divest just because a company was prevented from keeping extra profits that happened to serendipitously arise.[52] If the windfall amounts to economic rent, the tax can also be justified as a progressive measure that reaches capital income.[53] Even so, translating these ideas into the reality of most businesses has not proven to be an easy task as evidenced by the fact that windfall corporate taxes have been more of an exception than the norm. To elucidate on why this is so, the next section analyses the most famous of these taxes that were practiced in various countries at different moments in modern history.

3 The practice of windfall taxation

This part is divided into four sections according to historical and technical features shared by windfall-styled taxes that have been practiced around the world. It begins with the first modern form of windfall taxation that was introduced during the two world wars under the name of excess profits taxes followed by two special types of windfall taxes that, when instituted decades later, raised controversies about their nature as a tax on profits. It then proceeds to explain the workings of a typical windfall tax for the extractive sector known as resource rent tax that has long been used by resource-holding countries as an additional and permanent measure alongside income taxes. The last section examines the more recent windfall taxes arising in the context of the current global energy and prices crises.

3.1 *Wartime Excess Profits Taxes*

Extraordinary stories about bounteous profits reaped by a handful of firms in the course of World War I provided the impetus for the world's first modern forms of windfall corporate taxes to arise. Under the name of excess profits taxes,[54] numerous countries found it appropriate to recapture gains in excess of prewar periods that were seen as a windfall resulting from an exogenous event rather than any individual productive ability or investment decision. Denmark and Sweden, soon followed by the United Kingdom, were pioneers in experimenting with the excess profits tax concept already in 1915.[55] In the years thereafter, most other European countries as well as those outside Europe joined the movement.[56]

Beginning at 50%, the UK excess profits tax soon increased to 60% (in 1916) and then 80% (in 1917), later dropping to 40% (in 1919), and then again rising to 60% (in 1920).[57] In the United States, the first excess profits tax was levied in 1917 with a progressive bracket structure reaching up to 80%.[58] During World War II, the maximum US rate charged on excess profits was as high as 95%.[59] Such a tax was reintroduced in 1950 due to the Korean War with a rate of 30% applied on top of other existing corporate tax rates, amounting to an overall

Notes

[49] This is also known as 'allowance for corporate equity', which is discussed in s. 3.4, *infra*.

[50] R. S. Avi-Yonah, *A New Corporate Tax*, Tax Notes Int'l (2020).

[51] For an extensive efficiency-based discussion, *see* Kades, *supra* n. 10.

[52] Note that, under conditions of tax competition and capital mobility, it is possible that investors move their investments (physically or through artificial means) to low-tax locations. This issue is addressed in the concluding section. *See also* J. E. Dugan & R. A. Zubrow, *The Influence of the Excess Profits Tax on Business Decisions to Invest*, 7 Nat'l Tax J. 242, 250 (1954), doi: 10.1086/NTJ41790003 ('[t]he overwhelming majority of respondents who had to live with EPT [excess profits tax] during the Korean War period stated the tax had *no effect* upon either the level or manner of financing expenditures on new plant and equipment'.).

[53] R. S. Avi-Yonah, *Corporate Taxation to Curb Monopoly Power, A Brief History and Proposal*, Tax & Monop. 9, 11 (2022) ('Economists are almost unanimous in supporting a tax on rents since (a) it does not influence corporate behavior and is therefore efficient, and (b) it falls on capital and is therefore progressive'.).

[54] *See* e.g., Kades, *supra* n. 10 (discussing wartime excess profits tax as a form of windfall taxation); L. V. Faulhaber, *Lost in Translation: Excess Returns and the Search for Substantial Activities*, 25 Fla. Tax Rev. 545 (2022), doi: 10.5744/ftr.2022.2002 (same as previous); A. Christians & T. D. Magalhães, *The Case for Taxing Away Unsustainable Profits*, 91 Geo. Wash. L. Rev. 697 (2023) (same as previous); UN, *supra* n. 11, at 367 ('Windfall profits tax, also referred to as excess profits tax or a cash flow tax, can be profit related'.); S. Hebous, D. Prihardini & N. Vernon, *Excess Profit Taxes: Historical Perspective and Contemporary Relevance*, IMF Notes (2022).

[55] M. Billings & L. Oats, *Innovation and Pragmatism in Tax Design: Excess Profits Duty in the UK during the First World War*, 24 Acctng. Hist. Rev. 83, 86 (2014), doi: 10.1080/21552851.2014.963951.

[56] A. J. Arnold, *'A Paradise for Profiteers'? The Importance and Treatment of Profits During the First World War*, 24 Acct. Hist. Rev. 61, 69 (2014), doi: 10.1080/21552851.2014.963950.

[57] J. R. Tolmie & C. W. Leach, *Excess Profits Taxation*, 7 Can. J. Econ. & Pol. Sci. 350, 361 (1941), doi: 10.2307/137098. *See also* M. J. Daunton, *How to Pay for the War: State, Society and Taxation in Britain 1917–1924*, 109 Eng. Hist. Rev. 882 (1996), doi: 10.1093/ehr/CXI.443.882.

[58] R. R. Reed, *The 'Excess Profits' Tax*, 11 Law. & Banker & S. Bench & B. Rev. 33 (1918); C. C. Plehn, *War Profits and Excess Profits Taxes*, 10 Am. Econ. Rev. 283 (1920).

[59] C. J. Hynning, *The Excess-Profits Tax of 1940—A Critique*, 8 U. Chi. L. Rev. 441 (1940), doi: 10.2307/1597279; L. R. Driver Jr., *The Excess Profits Tax—Proposals for 1941*, Yale L.J. (1941), doi: 10.2307/792380; C. Schoup, *The Concept of Excess Profits under the Revenue Acts of 1940–1942*, 10 Law & Contemp. Probs. 28 (1943), doi: 10.2307/1190024; C. R. Peterson, *The Statutory Evolution of the Excess Profits Tax*, 10 Law & Contemp. Probs. 3 (1943), doi: 10.2307/1190023; J. J. Thorndike, *How to Write Tax Laws and Irritate People: The 1940 Excess Profits Tax*, 175 Tax Notes Int'l 1649 (2022).

rate approximate to 80%.[60] Canada was somewhat a latecomer among developed economies, enacting its first excess profits tax only in 1939, yet rates were anything but modest.[61] In 1940, the Canadian excess profits tax was set at 75%, but it rose to 100% by 1943. Other countries adhered to this trend with some revoking their excess profits tax soon after introduction while others continued to apply it even after economic conditions normalized.[62]

Typically, excess profits taxes adhered to one of two methodologies, specifically the 'average earnings approach' or the 'invested capital approach'.[63] The former compared average earnings during and before the war in order to ascertain the taxable increase for purposes of the excess profits tax. The calculation would thus begin with current-year income but then allow deductions (such as in the form of tax credits) equivalent to prewar profit amounts. The latter approach was to establish a normal return rate beforehand (for example, the 1918 US excess profits tax considered 8% to be a normal expected return on capital invested in tangible assets).[64] Everything earned above the fixed threshold would then be considered excess profits to be subject to a surtax.

Once economic conditions began to stabilize after the ceasefire, most excess profits taxes gradually faced repeal. Overall, these taxes were considered a successful way to legitimately raise revenues with little economic distortion, leading many at the time to support the imposition of surtaxes on corporate profits on a more regular basis.[65]

3.2 *Sui Generis Windfall Taxes*

Windfall taxes have also been employed to address other specific market-distorting occurrences that steeply increased the profitability of certain industries with no socially acceptable justification or even with outright public reproval. Notably, two interesting modern examples include the use of taxation to catch outsize gains arising from deregulation in certain sectors in the United States in the 1980s and the United Kingdom in the 1990s.[66]

In 1973–1974, a major world energy crisis due to petroleum shortages was effectuated by an embargo from the Organization of the Petroleum Exporting Countries (OPEC). In broad strokes, the OPEC refused to sell crude oil to the United States as retaliation for the US Government's economic support of Israel in the Yom Kippur War against Arab states. Oil companies at the time were already extensively criticized for obtaining 'unjustified – and controversial – subsidies'[67] but, with the US Government's decision to decontrol oil prices in response to the OPEC embargo, those companies were expected to additionally 'reap a windfall'.[68]

In anticipation, the Crude Oil Windfall Profit Tax Act of 1980 was passed to catch 'the difference between the former ceiling price of domestic crude oil and the higher market price obtainable upon decontrol'.[69] In the first two years, the applicable rate was 30%, but it was scheduled to decline in each following year until it stabilized at 15% for periods after 1986.[70] The tax base was constructed by reference to the price of the oil barrel instead of traditional net income measurements, therefore, many characterized the tax as a form of excise that would affect not only lucrative firms but also those with minimal profits or even in a loss.[71] Design problems added immoderate administrative and enforcement costs that were not counterbalanced by revenue increases.[72] As a result, the tax did not even last one decade and was abolished in 1988.

Notes

[60] S. Boulton, *The Excess Profits Tax of 1950: A Layman's Outline from the Viewpoint of the Corporate Analyst*, 7 Analyst J. 153 (1950), doi: 10.2469/faj.v7.n2.153; G. R. Donnell, *Excess Profits Tax Minus Its Technicalities*, Acc. Rev. 385 (1951); J. S. Platt & H.M. Mansfield, *The Excess Profits Tax of 1950: The General Rule*, 37 Am. Bar Ass. 234 (1951); George L. Lent, *Excess-Profits Taxation in the United States*, 59 J. Pol. Econ. 481 (1951), doi: 10.1086/257121; A. L. Gitlow, *Wages and the Excess Profits Tax*, 19 South. Econ. J. 95 (1952), doi: 10.2307/1053974.

[61] C. Campbell, *J.L. Ilsley and the Transformation of the Canadian Tax System: 1939–1943*, 61 Canadian Tax J. 633, at 667–68 (2013).

[62] *See* e.g., R. Vosslamber, *Tax Failure: New Zealand's Short-Lived First World War Excess Profits Tax*, 29 Acc. His. Rev. 79 (2019), doi: 10.1080/21552851.2019.1590215; B. S. Yamey, *The Excess Profits Duty in South Africa*, African J. Econ. 263 (1942), doi: 10.1111/j.1813-6982.1942.tb03092.x.

[63] A. Christians & T. D. Magalhães, *It's Time for Pillar 3: A Global Excess Profits Tax for COVID-19 and Beyond*, Tax Notes Int'l 507 (2020), doi: 10.2139/ssrn.3882142; R. S. Avi-Yonah, *COVID-19 and US Tax Policy: What Needs to Change?*, 48 Intertax 790 (2020), doi: 10.2139/ssrn.3584330.

[64] T. S. Adams, *Federal Taxes Upon Income and Excess Profits*, 8 Am. Econ. Ass. 18 (1918); E. Saez & G. Zucman, *The Triumph of Injustice: How the Rich Dodge Taxes and How to Make Them Pay* 33 (2019).

[65] Buehler, *supra* n. 26; Higgins, *supra* n. 45; Faulhaber, *supra* n. 54, at 581 ('Despite this tax being implemented in order to target windfalls from wartime, several legislators pushed to have it become permanent').

[66] Mexico also experimented with an excess profits tax between 1977 and 1979. *See* M. Gillis & C. E. McLure Jr., *Excess Profits Taxation: Post-Mortem on the Mexican Experience*, 32 Nat'l Tax J. 501 (1979), doi: 10.1086/NTJ41862269.

[67] J. J. Thorndike, *The Windfall Profit Tax: Career of a Concept*, Tax Notes (10 Nov. 2005).

[68] D. M. Robinson, *The Misnamed Tax: The Crude Oil Windfall Profits Tax of 1980*, 84 Dick. L. Rev. 589, 682 (1980).

[69] *Ibid.*, at 592.

[70] W. Lee, *The Windfall Profit Tax*, 9 Probate Notes 61, 64 (1983).

[71] *See* B. R. Miller & D. G. Easley, *The Windfall Profit Tax: An Overview*, 12 St. Mary's L.J. 414 (1980); Robinson, *supra* n. 68; D. E. Kinnan, *An Introduction to the Crude Oil Windfall Tax Act of 1980*, 3 W. New Eng. L. Rev. 645 (1981); D. B. Drapkin & Philip K. Verleger Jr., *The Windfall Profit Tax: Origins, Development, Implications*, 22 B.C. L. Rev. 631 (1981); P. Mangum, *Evolution of the Crude Oil Windfall Profit Tax: An Examination of Recent Changes*, 13 St. Mary's. L.J. 767 (1981); J. M. Dow, *The Windfall Profit Tax Exposed*, 14 St. Mary's. L.J. 739 (1983).

[72] Thorndike, *supra* n. 67.

About a decade later, the United Kingdom would also resort to the windfall language to propose a one-off tax on private utilities providers that were considered as having unduly benefited from the privatization that occurred between 1984 and 1996. With a single rate of 23%, the 1997 UK windfall tax was introduced with the goal to recoup part of the initial profits that private actors enjoyed immediately after acquiring state-owned utility companies at what was considered by the public to be too low of a price.[73] Like the 1980 US tax, the UK tax was also accused of not being levied on actual profits, at least not in a traditional sense. The tax used an 'alternative equity value' for its calculation[74] expressed as the excess between the taxpayer's 'value in profit-making terms' and its 'flotation value'.[75] Stated otherwise, determining the tax base consisted in, first, multiplying the average annual profits in a four-year period by nine after the company was privatized (profit-making value) and then subtracting the acquisition price (flotation value).

The newness of this profit measure had repercussions in the United States where a judicial controversy arose as to whether amounts paid by US shareholders under the UK windfall tax were creditable for US income tax purposes.[76] Yet, taxpayers were able to convince the US Supreme Court that, economically, the levy did indeed impact income despite the legislation's express references to value.

3.3 *Resource Rent Taxes*

Resource rent taxes are a typical fiscal instrument present in the tax mix of (developed and developing) resource-rich countries.[77] As part of what is known as a government's 'fiscal take',[78] these taxes are meant to assure that the public will be fairly compensated from the private exploitation of non-renewable resources (normally, upstream extractive activities) given that economic rents and windfalls are common in the sector.[79] Although a permanent measure that exists side-by-side with the traditional corporate income tax, resource rent taxes remain dormant until instigated by a high level of profitability.[80] This means that investors are granted the benefit of tax relief until an exploitation project becomes highly successful. The outcome for governments is that extractive industry profits only generate resource rent tax revenues on an ex-post basis.

In designing a resource rent tax, the key elements to consider are the chosen rate of return on investments above which a rent is deemed to arise; the rate of the tax to be applied on net profits that exceed that return rate; and the specific composition of the tax base. Regarding the last element, different models have been proposed[81] such as those developed by economists E. Cary Brown[82] and Ross Garnaut with Anthony Clunies Ross,[83] as well as the idea of an allowance for corporate equity or corporate capital as proposed by the Institute of Fiscal Studies Capital Taxes Group in 1983 and adopted by countries like Austria, Belgium, Croatia, Italy, and, to some extent, Brazil.[84]

Per the Brown tax (formulated in 1948), interests and other financial costs are non-deductible, but all investment costs are expensed whereas losses are fully refunded. The tax base therefore amounts to gross revenues from sales minus current and capital expenses, i.e., operating costs and money spent to acquire, upgrade, or maintain fixed assets. The Garnaut-Ross model is a more recent

Notes

[73] Finance (No. 2) Act 1997, c. 58 (UK) ('Every company which, on 2 Jul. 1997, was benefitting from a windfall from the flotation of an undertaking whose privatisation involved the imposition of economic regulation shall be charged with a tax (to be known as the "windfall tax") on the amount of that windfall'.).

[74] L. Chennells, *The Windfall Tax*, 18 Fisc. Stud. 3, at 286 (1997), doi: 10.1111/j.1475-5890.1997.tb00264.x.

[75] K. S. Linder, *Hybrid Taxation: The Dual Function and Creditability of the U.K. Windfall Tax*, 65 Tax Law. 429, 433 (2012).

[76] PPL Corp. & Subsidiaries *v.* Commissioner of Internal Revenue (2013). *See also* T. Nuccio, *Substance Over Form: Creditability of the 1997 U.K. Windfall Tax as an Excess Profits Tax Under I.R.C. § 901*, 22 Transnat'l L. & Contemp. Probs. 267 (2013).

[77] UN, *supra* n. 11, at 367 (listing resource rent taxes as one among many profit-based fiscal instruments that, in particular, 'is usually based on gross revenue from the resource development, and allows for certain allowances or deductions'.). *See also* J. M. Otto ed., *Taxation of Mineral Enterprises* (Kluwer 1995); S. Sollund, *Income Tax Regimes in Norway Applicable to Special Business Sectors*, 56 Bull. Int'l Tax'n. 415 (2002); P. Daniel, M. Keen & C. McPherson eds, *The Taxation of Petroleum and Minerals: Principles, Problems and Practice* (Routledge 2010); T. Sarker & E. Whalan, *Reform Issues in Mineral Tax Policy for Economic Development: The Mineral Resource Rent Tax in Australia*, 65 Bull. Int'l Tax'n. 1 (2010); L. Burns, *Resource Rent Taxation*, 18 Asia-Pacific Tax Bull. 312 (2012).

[78] UN, *supra* n. 11, at 471 (defining 'overall fiscal take' as including 'tax, royalty and other revenues that arise as a result of the fiscal terms' and 'fiscal term' as '[s]pecific economic elements relating to extractive industries activities within a particular country including taxation, other payments such as bonuses and royalties, legal framework, and state participation'.).

[79] *Ibid.*, at 423 ('Extractive projects can generate substantial rents. Rents (sometimes called "windfalls") are the financial returns above those a company requires to make the investment profitable'.); C. Michail, *Europe's High Energy Costs: The Case for a Resource Rent Tax*, 108 Tax Notes Int'l 64 (2022) ('RRT [resource rent tax] targets the windfall profits after subtracting relevant costs and a reasonable rate of return (economic rent)'.).

[80] L. Burns, *Income Taxation through the Life Cycle of an Extractive Industries Project*, Asia-Pacific Tax Bull. 401 (2014).

[81] Thomas Baunsgaard, *A Primer on Mineral Taxation*, IMF Working Paper 1/139 (2001); C. Cottarelli, *Fiscal Regimes for Extractive Industries: Design and Implementation*, IMF (15 Aug. 2012); K. Henry et al., *Australia's Future Tax System: Report to the Treasurer – Part 2: Detailed Analysis* 228–230 (2009).

[82] E. C. Brown, *Business-Income Taxation and Investment Incentives*, in *Income, Employment and Public Policy: Essay in Honor of Alvin H. Hansen* (L.A. Metzler et al., W.W. Norton & Co. 1948).

[83] R. Garnaut & A. C. Ross, *Taxation of Mineral Rents* (Clarendon Press 1983).

[84] A. Klemm, *Allowances for Corporate Equity in Practice*, IMF Working Paper (2006); R. Garnaut et al., *Replacing Corporate Income Tax with a Cash Flow Tax*, 53 Austl. Econ. Rev. 463 (2020), doi: 10.1111/1467-8462.12385.

idea that uses a similar tax base, but losses are carried forward indefinitely 'at an interest rate that is judged to correspond appropriately to the return on capital thought to be required ex ante by a mining company in considering an investment'.[85] Finally, the allowance for corporate capital aims to equalize the tax treatment of debt and equity by excluding interest payments and a notional return on equity from the corporate income tax base.[86]

The fact that all cash expenditures are immediately deductible as opposed to depreciated or amortized over time renders the resource rent tax a type of cash-flow tax. It ideally falls on pure economic rents (windfalls included) even if, in practice, other factors might interfere with the final incidence of the tax.[87] Unlike the windfall taxes analysed in previous sections that were initially envisioned as a temporary response to extraordinary events that were expected to dissipate with time, resource rent taxes are often a central and enduring feature of extractive tax regimes.[88] The underlying policy rationale is to capture rents from activities involving oil, gas, and hard minerals whenever those rents arise under the assumption that natural resources are finite and belong to society at large.[89] If well designed and implemented, resource rent taxes are supposed to simultaneously achieve neutrality, efficiency, and equity.[90]

3.4 *Recent Crisis-Driven Windfall Taxes*

World economies were still weakened by the consequences of Covid-19 when a new crisis erupted with the political and military tensions between Russia and Ukraine. The immediate economic consequence for the rest of the world was an extreme price increase for commodities such as oil, coal, and natural gas thereby creating windfalls in the form of extraordinary profits for energy companies. States' first response was to enact a diversified set of fiscal measures to aid households and businesses. With increased government spending, finding additional sources of revenue seemed an inevitable political outcome. However, it was the perceived unfairness that some companies were benefiting from the suffering of everyone else that created momentum for a resurface of windfall-type tax proposals everywhere. On top of that, windfall taxation received the support of multiple international institutions including the United Nations, the Organisation for Economic Co-operation and Development (OECD), the International Monetary Fund (IMF), and the Independent Commission for the Reform of International Corporate Taxation (ICRICT).[91]

Most of these newly introduced taxes have targeted corporate profits, and most have applied exclusively to oil and gas companies, however, there have been various exceptions. Windfall taxes in Canada, Czech Republic, Lithuania, and Spain have also covered banks.[92] Hungary's windfall tax was extended to pharmaceutical companies.[93] Croatia has been applying a windfall tax to any company realizing excessive profits.[94] Colombia has opted for a surcharge within its corporate income tax instead of a standalone new tax.[95] Similarly, Myanmar and Papua New Guinea decided to raise corporate income tax rates.[96]

The UK energy profits levy was styled as a temporary excess profits tax[97] while India created a special additional excise duty to be imposed on domestically produced crude oil and exports of petrol, diesel, and aviation turbine fuel.[98] Proposals in the United States have also

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85 R. Garnaut, *Principles and Practice of Resource Rent Taxation*, 43 Austrl. Econ. Rev. 347, 349 (2010), doi: 10.1111/j.1467-8462.2010.00616.x.

86 J. Mirrlees, *Tax by Design: The Mirrlees Review* 421 (Stuart Adam et al., 2011).

87 B. C. Land, *Resource Rent Taxation—Theory and Evidence*, IMF (2008).

88 N. Vernon & T. Baunsgaard, *Taxing Windfall Profits in the Energy Sector*, IMF Notes (2022).

89 L. Burns, *Taxation of Non-Renewable Natural Resources*, 66 Bull. Int'l Tax'n. 504 (2012).

90 R. Garnaut & A. C. Ross, *Uncertainty, Risk Aversion and the Taxing of Natural Resource Projects*, 85 Econ. J. 338 (1975), doi: 10.2307/2230992; C. Emerson & R. Garnaut, *Mining Leasing Policy: Competitive Bidding and the Resource Rent Tax Given Various Responses to Risk*, 60 Econ. Rec. 133 (1984), doi: 10.1111/j.1475-4932.1984.tb00846.x; R. Garnaut & A. C. Ross, *The Neutrality of the Resource Rent Tax*, 85 Econ. Record 193 (1979), doi: 10.1111/j.1475-4932.1979.tb02221.x.

91 UN, *Press Conference by Secretary-General António Guterres at United Nations Headquarters* (3 Aug. 2022), https://press.un.org/en/2022/sgsm21397.doc.htm (accessed 20 Apr. 2023); OECD, *Economic Outlook – Interim Report: Economic and Social Impacts and Policy Implications of the War in Ukraine* (OECD Publishing 2022); D. Amaglobeli et al., *Fiscal Policy of Mitigating the Social Impact of High Energy and Food Prices*, IMF Note (2022); A. Athanasiou, *Wealth and Windfall Taxes are Needed Globally, Economists Say*, Tax Notes Int'l 1428 (2022) (citing Joseph Stiglitz, co-chair of the ICRICT).

92 W. Hoke, *Spanish Parliament Passes Banking and Energy Windfall Taxe*s, 109 Tax Notes Int'l 123 (2023); J. Robles Santos, *Canada Enacts Inflationary Relief: Cuts Taxes for Small Businesses, Eliminates Federal Student Loan Interest, Imposes New Large Financial Institutions Tax*, IBFD Tax News Service (21 Dec. 2022); E. Burbaitė, *Lithuanian Government Approves Text of Draft Law on Solidarity Tax for Banking Sector*, IBFD Tax News Service (6 Apr. 2023); S. Paez, *Czech Senate Passes Windfall Profits Tax on Energy Companies*, 108 Tax Notes Int'l 1277 (2022).

93 W. Hoke, *Hungary Extends Windfall Tax to Pharmaceutical Sector*, 109 Tax Notes Int'l 109 (2023); G. Erdős and G. Czoboly, *New Legislative Tool for Introducing EU-Wide Windfall Taxes*, 63 European Tax'n. 1 (2023).

94 M. Starčević, *Croatia – Parliament Adopts Extra Profits Tax*, IBFD Tax News Service (19 Dec. 2022).

95 W. Hoke, *Colombian Congress Passes Tax Reform Legislation*, 108 Tax Notes Int'l 1132 (2022).

96 N. Lingbawan, *Myanmar Increases Income Tax Rate for Oil and Gas Sector in Union Tax Law 2022 Amendment*, IBFD Tax News Service (30 Nov. 2022).

97 C. Hennaman, *UK Chancellor Announces 25% Windfall Tax on Oil and Gas Companies*, IBFD Tax News Service (27 May 2022).

98 Indian Ministry of Finance, *Press Release of 1 July 2022*, https://pib.gov.in/PressReleasePage.aspx?PRID=1838455#:~:text=A%20special%20additional%20excise%20duty, imposed%20on%20exports%20of%20ATF.

contemplated excise taxes rather than profit-based taxes such as a special levy on production or import of crude oil under the 'Big Oil Windfall Profits Tax Act'[99] and a special levy on large crude oil producers under the 'Stop Profiting Off Putin's War Act'.[100] In Brazil, the government has attempted to tax the export of crude petroleum oils and bituminous minerals, but the measure has faced legal challenges before local courts.[101] In fact, affected companies have resorted to lawsuits and lobbying against windfall taxes in several jurisdictions.[102]

At the level of the European Union, Member States were required to adopt a uniform approach to windfall taxation pursuant to a 2022 Council Regulation.[103] It authorized the council to adopt extraordinary measures in the case of disruptions to the supply of certain products, especially in the area of energy. Two of the prescribed measures were a temporary solidarity contribution on companies with activities in the crude petroleum, natural gas, coal and refinery sectors and a cap on market revenues of electricity producers. The solidarity contribution is basically a time-limited retroactive tax on excess profits measured by the average-earnings method.[104] Under this tax, profits derived in 2022 and/or 2023 above a 20% increase compared to average yearly taxable profits in the four preceding years are subject to a rate of at least 33%. However, the reference period includes Covid-19 years, raising questions as to whether those profits could be considered normal returns in any reliable sense.[105] Under the second measure, a contribution of at least 90% is to be levied on electricity revenues exceeding a price cap of 180 euros per megawatt hour (MWh).

4 The road ahead

Over the past 100 years, states have accumulated vast experience with various measures designed to tax extra-normal levels of profitability that are often promoted under the banner of 'windfall taxes'. From the theoretical and practical analysis of these measures, a few lessons emerge. First, rent-based taxes are one of the most efficient and fair ways to raise revenues. Second, corporate levies built upon net income measurements appear preferable than other tax bases with an intention to preventing possible disputes (for example, regarding whether amounts paid in one jurisdiction are credible in another). Third, despite the challenges involved in determining normal rates of return, surcharges on outgrown profit margins have been applied or defended throughout modern history in respect to certain industries and even broadly across sectors.

These lessons seem to suggest that progressive corporate taxation might be a viable option for building tax systems that are more equitable while contributing to addressing the growing public concern with the concentration of wealth and power among a few large-size corporations.[106] However, the world is not one unified polity but a fragmented society of states, and the most profitable taxpayers operate as multinational enterprises. Hence, implementing progressive corporate tax regimes would have to cope with the possibility that groups of affiliated entities might split their worldwide income between different jurisdictions in order to avoid higher tax brackets, among other planning strategies of profit shifting. The most workable approach, therefore, would be to make group-level tax progressivity part of the ongoing efforts of the international community to coordinate minimum taxes on the largest multinationals. In any case, political determination among a mass of countries and continuing public support would be key given the inevitable opposition of those for which profits might be affected.

Notes

[99] US Congress, *Bill S. 3802 – Big Oil Windfall Profits Tax Act*, https://www.congress.gov/bill/117th-congress/senate-bill/3802?s=1&r=1.

[100] US Congress, *Bill H.R.7103 – Stop Profiting Off Putin's War Act*, https://www.congress.gov/bill/117th-congress/house-bill/7103.

[101] D. Canen, *Brazil Levies Tax on Crude Petroleum Oil Exports, Resumes Collection of Various Contributions on Fuels*, IBFD Tax News Service (13 Mar. 2023); W. Hoke, *Companies Seek Injunction Action Against Brazil's Crude Oil Export Tax*, 109 Tax Notes Int'l 1520 (2023).

[102] S. Paez, *U.K. Energy Group Lobbies to End Windfall Profits Tax*, 107 Tax Notes Int'l (2022); W. Hoke, *Sabadell and CaixaBank Challenge Spain's Windfall Bank Tax*, 109 Tax Notes Int'l 955 (2023); W. Hoke, *Exxon Lawsuit Claims EU Windfall Tax on Oil Profits Is Illegal*, 109 Tax Notes Int'l 92 (2023).

[103] Regulation (EU) 2022/1854 on an emergency intervention to address high energy prices (6 Oct. 2022), http://data.europa.eu/eli/reg/2022/1854/oj.

[104] *See* K. Nicolay et al., *The Effectiveness and Distributional Consequences of Excess Profit Taxes or Windfall Taxes in Light of the Commission's Recommendation to Member States*, Pol'y Depart. Econ. Sci. & Quality of Life Policies (2023).

[105] F. V. Fernandes, *Windfall Cracks: The Structural Flaws in Taxing Energy Sector Profits*, Int'l Tax Rev. (2022).

[106] Some economists believe this issue would be better addressed by creating an entirely new tax to be imposed on the stock of shares of publicly listed companies. E. Saez & G. Zucman, *A Wealth Tax on Corporations' Stock*, Econ. Pol'y 215 (2022), doi: 10.1093/epolic/eiac026. It is beyond the scope of this article to evaluate this proposal, but it can be noted that political feasibility and compatibility with national laws and tax treaties would be much more difficult to achieve than using existing income tax structures.