Financial Research Papers - November 2011

Fiscal responses to the economic downturn in Eastern Europe in 2010-11

With special attention paid to unorthodox measures

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Abstract

An economic downturn boosts demand for fiscal rebalancing. It can come either in the form of increased revenues or as spending cuts. Extra revenues can be generated in two major ways: 1) increasing traditional forms of taxes or 2) hitherto unknown, or unorthodox revenue raising, special taxes and levies. Latter was especially dominant in the case of Hungary.

We discuss Hungarian special taxes in three separate groups: 1) the bank levy, 2) the special taxes on retail and energy companies and 3) the telecom taxes. Then we address a new phenomenon, the fat tax. In each cases we attempt to take account of similar measures taken by other governments.

Keywords— Economic crisis; Fiscal policy; Special taxes; Bank levy; Windfall tax; Fat tax

JEL— E62, H25, H12

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EXECUTIVE SUMMARY

1. The economic downturn has boosted **demand for fiscal rebalancing** either in the form of increased revenues or spending cuts. Extra revenues can be generated in two major ways: 1) increasing traditional forms of taxes or 2) hitherto unknown, or unorthodox revenue raising, special taxes and levies.

2. We discuss Hungarian special taxes in three separate groups: 1) the bank levy, 2) the special taxes on retail and energy companies and 3) the telecom taxes.

3. According to IMF there are three major ways to impose **bank levy**:

   3.1. ***Financial Stability Contribution* – FSC**: *Direct tax based on the banks' balance sheets*. It is meant to stabilize the future financial system in one of two ways: 1) directly by setting up a financial stability fund or 2) indirectly by strengthening current national budgets. The second form satisfies fiscal needs effectively while its stabilizing effect is doubtful due to the time mismatch between the collection of the revenue and the possible future needs.

   3.2. ***Financial Activities Tax* – FAT**: Directed at the banks' profits and the bonuses of bank employees in Europe – France and the United Kingdom have introduced this tax for a limited period at first – with the UK pondering permanence. Politically tempting form of taxation because it resonates with broader electoral sentiment. In fiscal terms, however, its effects are unpredictable. It may cause the narrowing of the tax base or it may be avoided by means of regulatory arbitrage.

   3.3. ***Financial Transaction Tax* – FTT**: Directed not at banks but certain types of financial transactions deemed *risky*. The IMF wouldn't write off FTT as a source of revenue but falls short of recommending it for the present for multiple reasons.

4. **The European Union is considering the FTT** arguing that it decreases volatility and noise trading as well as eliminating the bias towards financial services (as opposed to the real economy) caused by the financial sector having been exempt form VAT. According to its proponents it may also divert investment into the real economy with slower returns. The debate is whether the revenues should go into national accounts (British and French standpoint) or a Europe-wide fund (German) and spent accordingly.

4.1. The successful Swedish example of saving its banks in the 90s deserves a mention because it had served as an example for similar moves in 2010. (The Swedes have imposed a solidarity tax on their banks as early as 2009.) The example is all the more relevant because Sweden has experimented with the FTT, the transactional tax in the 90s, but did not introduce it this time due to negative experience.

4.2. Global (and even European) consensus is lacking with regards to the bank levy – leaving room for regulatory arbitrage in case of its introduction, thus threatening its effectiveness.

5. Special tax on **telecommunication** companies have been introduced in three European countries: in France (March 2009), Spain (September 2009) and finally in Hungary. This type of tax is against European regulation.

6. We could not find examples on special taxes imposed on energy and retail companies in Europe during this period – and even in the not so distant past. It is more characteristic to raise revenues by increasing traditional taxes' rates. This, however, can only distinguish according to the size of companies, not according to ownership or nationality of the owner – as opposed to the Hungarian example of retail tax that is semi-openly targeted at companies in foreign ownership.

7. On the risk of contagion of unorthodox measures – The example of the "fat tax" demonstrates how fiscal need can find a way to justify entering uncharted territories – and how the example then becomes too tempting to resist and a point of reference for governments in similar situations.

INTRODUCTION

Fiscal measures

The economic downturn has boosted **demand for more fiscal revenues**: its two major directions are

1) increasing traditional forms of taxes (income taxes, corporate and personal and VAT) or
2) unorthodox revenue raising, special taxes and levies (solidarity tax as well as new tax forms with behavioural justification in the shape of excise duties levied on certain food groups such as the fat tax introduced in Denmark and Hungary).

Expenditure cuts can take three directions – depending on how much governments wish to utilise Keynesian manipulation of demand.

3) Cutting public services, freezing payrolls, firing civil servants and the introduction of hiring stops.
4) Cutting welfare expenditures in the shape of narrowing the circle of recipients for entitlements or lowering benefit payments.
5) Comprehensive structural reforms like the pension reform – no immediate savings.

The first two moves offer immediate drop in expenditures but fail to address the underlying structural problems.

Special taxes in Hungary

Discussed in three groups:

1) Bank levy – Introduced in more than a dozen countries since the 2008 financial crisis. Each country has chosen a combination of the three major varieties: FSC, FAT or FTT. Differences persist in whether the country had to bail out its banks (Hungary did not) and in the utilisation of the revenue (going into stability funds or funding current fiscal deficits).

2) Telecom taxes – Among the Hungarian special taxes this is the only one that is against EU regulations thus deserving special attention. French and Spanish telecom taxes are earmarked to fund state media outlets recently seeing a drop in revenues due to previous regulation banning paid advertisements on them. The Hungarian telecom tax is meant to generate fiscal revenues.
3) Special taxes on retail and energy companies – not explicitly against EU regulations but still raise questions through the preferential treatment of national champions to be created in the Hungarian retail industry.

BANK LEVY

The IMF proposed two possible solutions on the financing of bank bailouts in its paper in April 2010 (commissioned by the G-20).

1) *Financial Stability Contribution - FSC*

Direct bank tax based on banks' balance sheets. The revenues could finance a bank stability fund designed to provide financial stability in the future. After its introduction it would be desirable to gradually apply different rates according to the risk of individual financial institutions. (IMF 2010)

2) *Financial Activities Tax - FAT*

A tax levied on the sum of profits and remuneration of financial institutions. Politically tempting given the strong electoral support for such a tax despite its unpopularity among banking professionals. Latter may lead to a the narrowing the taxable base if financial institutions choose to realise their profits abroad or exploit regulatory loopholes for paying out bonuses. Revenues on FAT are thus doubtful.

One advantage of this type of tax is that it eliminates the benefits the financial services have enjoyed so far by being exempt from VAT – argues the IMF. This, however, is partially true for all types of bank levy. (See more on the subject in the paper released by the European commission describing how the tax system has provided the incentives driving economic actors into debt-financing as opposed to financing through savings through tax exemptions on debt service not applicable for savings. (Hemmelgarn – Nicodeme 2010)) According to the IMF "since value added is simply the sum of profits and wages, a FAT would bear the same relationship to an FTT as the VAT does to a turnover tax—a FAT in effect taxes net transactions of financial institutions, whereas an FTT taxes gross transactions." (IMF, 2010: 19)

3) *Financial Transaction Tax - FTT*

Indirect tax targeting certain types of financial transactions (as opposed to financial institutions). Its benefit is the possibility to target risky transactions but not all transactions are risky – a blanket transaction tax would thus miss the point of stabilizing an overly volatile market. Categorization in a constantly changing environment is going to be an overwhelming regulatory task. Another possible technical difficulty is the collection of the tax.

The most serious disadvantage of this type of tax, however, would be the perverse incentives and unintended consequences that arise from the categorisation itself.

The IMF does not explicitly recommend this tax – designed essentially according to the 1936 proposal of JM Keynes and the Tobin-tax on forex transaction – even though it does not exclude it either in the future. According to the IMF this tax would miss the real cause of the crisis and that it would eventually be paid by banks' customers. (IMF, 2010:17)

Nouriel Roubini warned that any new financial regulation or levy must be global in nature in order to have an effect. (2010) By June 2010, however, it became obvious that bank levy will not be global and countries will insist on their individual solutions. Most ardent opponents of the global tax are countries with a large share of corporate tax coming from financial services, like Canada (26%) and the United Kingdom (20.9%).

Country	Period	Contributions as percentage of corporate tax income	As percentage of total tax revenues
Argentine	2006-2008	6,0%	1,0%
Australia	FY 2007	15,0%	2,8%
Brazil	2006-2008	15,4%	1,8%
South Africa	2007-2008 FY	13,7%	3,5%
US	2006-2007 FY	**18,2%**	**1,9%**
UK	2006-2008 FY	**20,9%**	**1,9%**
France	2006-2008	18,0%	1,9%
Canada	2006-2007	23,5%	2,6%
Korea	2006-2008	17,7%	3,0%
Mexico	2006-2008	11,2%	3,1%
Italy	2006-2008	**26,3%**	**1,7%**
Turkey	2006-2008	23,6%	2,1%
Unweighted average		17,5%	2,3%

Table 1: Share of financial services in corporate tax revenues (left) and contribution to all government revenues (right) between 2006-2008, Source: IMF, 2010

According to the IMF these revenues must be used towards future financial stability and the steps must be part of broader measures. It suggests that for many countries provisioning for approximately 2-4% of GDP would suffice.

Revenues raised by the Hungarian bank levy are large compared to the size of the economy. The rate and introduction of the Hungarian bank levy is all the more striking because there was no bail-out of banks (unlike in Germany or the UK). Hungarian banks had to contribute EUR 695 million (HUF 200 billion) in 2011 and the proceeds went into public deficit reduction – as opposed to a financial stability fund as seen in the case of Sweden. In fact, it was Hungary that introduced the first such bank levy not serving the cause of future bank stability.

Unlike the other special taxes, the bank levy is planned to be permanent in Hungary.

Bank levy in comparison

Sweden has introduced its bank levy in 2009. It was 0.036% of the balance sheet of its banks meant to reduce risk taking in the financial sector. Its proceeds went into a special bank stability fund until it reaches the size of 2.5% of the Swedish GDP.

Targeting a certain size of the bank stability fund has emerged elsewhere: the US TARP fund[1] was planned to be financed by the bank levy until it sees its expenditures covered. Germany is also planning to reach a certain size of GDP before removing the levy.

The Swedish model is exemplary in more than one aspect. Sweden had to bail out its bank in the 1990s and the program (creating a "bad bank") is widely considered successful. Its 2009 "stability fee" to be paid by banks has been on lawmakers' mind all over the Western world when creating their own blend of bank levy in and after 2009.[2]

The United Kingdom has introduced its bank levy in 2011 and targeted banks above a certain size. Followed by similar moves in France and Germany in order to avoid large scale reallocation of capital within Europe. (The United Kingdom had to save its banks in 2008.) In 2009 the UK has introduced a one-off FAT tax – 50% Bank Payroll Tax on bonuses. Latter was discontinued in 2010 but the British government is considering its reintroduction in 2011.

The **German** bank levy would be levied according to the risk of the institutions. The aim of the German levy is to create a dedicated restructuring fund (Restrukturierungsfonds handled by a federal authority, Bundesanstalt für Finanzmarktstabilisierung) to be drawn upon in the event of financial crisis, whereas the proceeds of the United Kingdom levy and the French

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[1] Troubled Asset Relief Program created in 2008 to bail out ailing carmakers and financial institutions.

[2] Source: Swedish Bank Fee Sets Example for America, The New York Times, January 2010 http://www.nytimes.com/2010/01/22/business/global/22levy.html

levy will feed into general revenues. [3] When the German stability fund reaches the size of 70 billion euros, its scale would be renegotiated.

The United Kingdom and Germany have adopted a similar approach[4], taking into account total equity and liabilities subject to certain exceptions, e.g., for minimum regulatory capital. By contrast, the French bank levy is based on minimum regulatory capital.

France has introduced a one-off bonus tax in 2009 (50% over EUR 27500) and an FSC-type tax from January 2011.[5]

Slovakia would impose a 0.4% levy on commercial banks' liabilities regardless of the state of the debate about the EU-wide bank levy in 2012. The revenues would not go into the general budget but would be saved on a special account to deal with future financial emergencies. Note that all Slovakian bank levy plans can be subject to change after the general elections in early 2012. Robert Fico, the leader of opposition party Smer has already expressed his plans to increase the tax considerably in case of his election victory. That scale would pale the Hungarian bank levy in comparison.

Slovenia introduced bank levy in 2011 based on the banks' balance sheets. Banks with considerable corporate lending are exempt from the levy.

A balance sheet-based bank levy has been on the agenda in **Croatia** as well until banks have agreed to a cut of interest rates instead in February 2011. The Croatian prime minister has

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[3] Source: German Bank Levy - Federal Government Issues Restructuring Fund Regulation, Cleary Gottlieb report, March 2011 http://www.cgsh.com/files/News/781734aa-5598-4635-884e-6e29297de9b9/Presentation/NewsAttachment/1d667420-70d9-4db6-8b99-70baeb8cb54d/CGSH%20Alert%20-%20German%20Bank%20Levy.pdf

[4] Source: Bundesrat committee approves German bank levy, Reuters, June 2011 http://uk.reuters.com/article/2011/06/01/uk-germany-banks-levy-idUKTRE7506J420110601

[5] Source: Bank Levies in the UK, France and Germany: A Comparison of the New Levies on Banks Sullivan & Cromwell, May 2011 http://www.sullcrom.com/Bank-Levies-in-the-UK-France-and-Germany-05-06-2011/

actually threatened by a bank levy of "Hungarian proportions" to tame its 90% foreign-owned banks.[6]

The **Polish** bank levy is expected to be moderate and triggered little resistance from the banks. The expected revenue of EUR 380 million (1.5 bn zloty) is merely EUR 10 per person – next to 38 euros in Britain and 69.5 euros in Hungary.

Austria is going to introduce a bank levy in 2011. The levy is moderate compared to the Hungarian tax. Up to a balance sheet of EUR 1 billion there is no levy; between 1 and 20 billion it is 0.055%, and over 20 billion the Austrian levy is 0.085%.[7]

The **Dutch** bank levy is forecast to reap EUR 300 million in public revenue from 2012, which is earmarked to fund a cut of stamp duty on real estate transactions – in order to revive the housing market.

The idea of a **Danish** bank levy has been dropped in September 2011 although the left wing winner of the elections had proposed it during campaign.[8]

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[6] Source: Die Bankensteuer macht im Osten Schule, Die Presse, September 2010 http://diepresse.com/home/wirtschaft/eastconomist/593219/Die-Bankensteuer-macht-im-Osten-Schule?from=rss

[7] Source: Terjed a bankadó Európában - Ausztria is határozott időre tervez, Világgazdaság, 19 January 2011 http://www.vilaggazdasag.hu/gazdasag/adozas/terjed-a-bankado-europaban-ausztria-is-hatarozott-idore-tervez-338609

[8] Source: Denmark's New Government Boosts Investments to Fight Crisis, Bloomberg, October 2011 http://www.bloomberg.com/news/2011-10-03/denmark-s-new-cabinet-to-ease-immigration.html

Country	Type	Year	Rate	Revenue, 2011	Utilisation
Sweden	FSC	2009	0.036% of balance sheet	EUR 250 million (2009)	Stability fund
UK	FSC, FAT	2011	0.075% (2011) 0.088% (2012)[9]	GBP 2 bn	Budget revenue
Germany	FSC	2011	Investment banks higher than commercial ones	EUR 1.2-1.3 bn	Stability fund
France	FSC, FAT FTT planned	2011	0.25%	EUR 500 million	Stability fund
Austria	FSC	2011	Up to EUR 1 bn balance sheet 0% Between EUR 1 and 20 bn 0.055% Above 20 bn 0.085%	EUR 500 million	Budget revenue
Poland	FSC	2011		500-700 million zloty per annum (EUR 380 million)	Deposit guarantee fund
Hungary	FSC	2010	Under HUF 50 bn tax base 0.15% Above 50 bn 0.53%[10]	EUR 700 million	Budget revenue
Netherlands	FSC	2012		EUR 300 million	
Slovakia*	FSC	2012	0.4% of banks' liabilities which can be approx. 8% of their profits[11]	EUR 50 million (in 2012)	Stability fund
Slovenia	FSC	2011	0.1% of balance sheet	EUR 5 million	
Croatia	FSC	Off the agenda (Feb 2011)	Based on balance sheet	N/A	Budget revenue
Denmark	N/A	Off the agenda (Oct 2011)	N/A	N/A	N/A

* Slovakia's bank levy is under reconsideration and may change under the new government to be elected in 2012.

Table 2: Proposals and implementations of bank levy in Europe, their type, scale and the utilisation of the revenue, Source: Own research

[9] Increased from 0.078% in November 2011 in order to keep revenues unchanged. Source: Osborne Increases U.K. Bank-Levy Rate, Keeps Revenue Target, Bloomberg, November 2011 http://www.bloomberg.com/news/2011-11-29/osborne-increases-bank-levy-rate-to-0-088-versus-0-075-.html

[10] The Hungarian bank levy is not exclusive to banks and financial institutions. Insurance companies, funds and other financial services are also affected.

[11] Source: Cabinet approves special bank levy, New Europe Online, 25 September 2011 http://www.neurope.eu/article/cabinet-approves-special-bank-levy

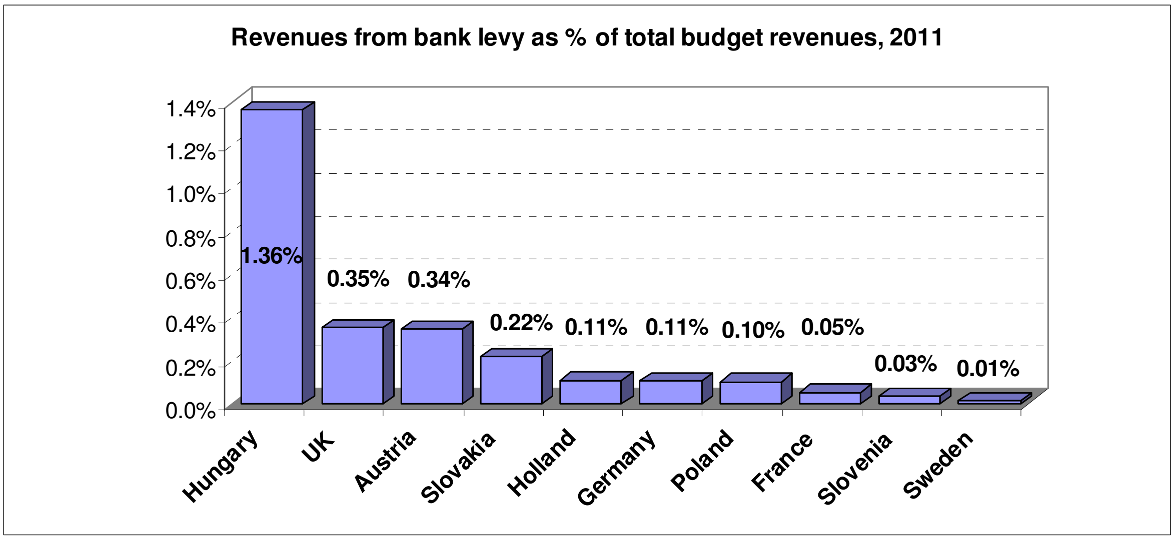

Chart 1. Revenues from the bank levy as a percentage of all budget revenues, 2011, Source: IMF, WEO data and own research

The European bank levy

The three countries proposing the Europe-wide tax have settled for the FTT, the form of levy targeting financial transactions that was least preferred by the 2010 IMF report.[12] The new budget including the bank levy comes into force in 2014.

The European proposal would cover all transactions regardless of risk, including bonds, securities, forex (excluding spot trading) and derivatives, both regulated and OTC products. The tax would be set by the member states with a minimum of 0.01% for derivatives and 0.1% for other financial transactions. Financial institutions are broadly defined to avoid evasion through qualification. Collection would be executed by national tax authorities.

[12] The European Commission introduced its proposal for the budget between 2014-2020 on the 29th of June 2011. In the previous cycle (2007-13) countries contributed 1.12% of their GNP. The Commission proposed to bring down that ration to 1.05% and top up the difference from increased EU-wide taxes – most obvious target being the revenue coming from the FTT. Source: Európai bankadó és ÁFA is szerepel a 2014-2020-as EU-költségvetésben http://www.euractiv.hu/gazdasag/hirek/europai-bankado-es-afa-is-szerepel-a-2014-2020-as-eu-kltsegvetesben-003443 EurActiv, 30 June 2011

The main argument for a Europe-wide FTT was that the VAT exemption of financial activities had distorted the investment market to prefer financial markets as opposed to real investments.

A report produced by the European Commission examining whether the European tax climate has contributed to the escalation of the crisis has found that the tax system has not only favoured home-ownership (driving up demand and thus house prices) but incentivised debt-financed infrastructure investment for corporations relative to other sources through tax credits given on interest payments but not on development form own sources. It has eventually led to housing bubbles and leveraging practices that put companies at risk during a downturn. (Hemmelgarn – Nicodeme 2010). The proposal for a European bank levy would also aim to eliminate such incentives by creating new ones.

The utilization of the tax revenue has divided the member states. Germany and France preferred the collection and usage of the income on the national level – as opposed to a Europe-wide stability fund.

The third dividing factor was whether to collect the revenue in a stability fund (Germany) or enriching annual national budgets (French, British standpoint).

The FTT is to serve three purposes:

1) To stabilize the financial markets by reducing the volume and frequency of speculative transactions and technical trading.
2) Massive income without distorting the structure of the real economy.
3) Make banks contribute to the cost of recovering of financial stability.

The original argument for the Tobin tax proposed that it would also increase the effectiveness of national monetary policies by counteracting the effect of the international flow of hot money.

The Tobin tax is also appealing to national governments by making national tax policies possible. Among its appeal are furthermore the decrease of technical trading and thus, hopefully, that of volatility. It is also meant to incentivise investors for long-term, real investments as opposed to quick, passive, VAT-free income through financial services.

The most tempting feature of the tax is, however, the revenue it raises by upsetting no large groups of the electorate.

Reasons against the FTT are:

1) Decreasing the effectiveness of markets by decreasing liquidity. The argument that an FTT would reduce market price volatility may be faulty since this is not always true in either theory (thinning of markets and lack of liquidity can increase volatility) or practice (the empirical evidence suggests that transactions taxes either do not affect price volatility or increase it).
2) Making it harder to raise capital.
3) Decrease investments.

Moreover, international cooperation would be crucial given the scale of capital movements and the complexity of cross-border financial institutions.

Of the three types of bank levy, the FTT is most likely to be passed on to costumers. Its future implementation should, however, not be dismissed based solely on administrative basis, said the IMF.

The Swedish experience of the 90s could also be informative. Introducing the FTT back then had the unintended result of the financial services (and thus capital) relocating to London. The Swedes have thus not repeated this element of the 90s bank bail out in 2009.

SECTORAL LEVY AND WINDFALL TAXES

A The telecom tax

Special tax on telecommunication companies have been introduced in three European countries: in France (March 2009), Spain (September 2009) and finally in Hungary.

In both the Spanish and French cases it was earmarked to finance a shortfall in the financing of state owned media outlets that have priorly seen their incomes dwindling after a ban on paid advertisement in state media. The taxation of telecommunication companies is, however, regulated by the European Union. According to the EC directive tax can be levied upon telecommunication companies *"only to cover certain administrative and regulatory costs (mainly authorisations and regulatory functions) and should be objective, transparent and proportionate."* [13]

The telecom taxes are therefore under attack before the European Court. In terms of proportionate budget revenue, Hungary has the most to lose (EUR 200 million expected from it in 2011) while the French and Spanish cases have more political relevance within the EU. They are also in a more advanced phase of the enquiry (started in March 2011) and Hungary was merely pointing at the two big member states when introducing the special tax. National legislation can only be overwritten by the European Court.

	Spain	**France**	**Hungary**
Rate	0.9%	0.9%	0 - 6.5%
Tax base	Gross income	Income above EUR 5 million	Income Up to HUF 100 million: 0% Up to HUF 500 million: 2.5% Up to HUF 500 billion: 4.5% Above HUF 500 billion 6.5%

Table 3. Telecom tax in Europe – Tax base and applicable rates

In France an estimated 400 million euros were collected from this tax in 2009.[14] (France Telecom was among the most affected – also hit by its exposure to Northern African

[13] Source: · Az Európai Parlament és a tanács 2002/20/EK irányelve (7 March 2002) az elektronikus hírközlő hálózatok és az elektronikus hírközlési szolgáltatások engedélyezéséről

[14] Tax and Africa weigh on France Telecom, Financial Times 3 May 2011 http://www.ft.com/cms/s/0/945fe48c-755c-11e0-8492-00144feabdc0.html#axzz1ZcU9Vxqw

countries in upheaval and a recent European Court decision to return approximately USD 1.5 billion received from the government in tax breaks and subsidies over the years.[15])

The Spanish revenue from the telecom tax is an estimated EUR 230 million a year.[16]

The *Hungarian* telecom tax appears to be the highest – both in terms of tax rate and revenue-to-budget ratio.

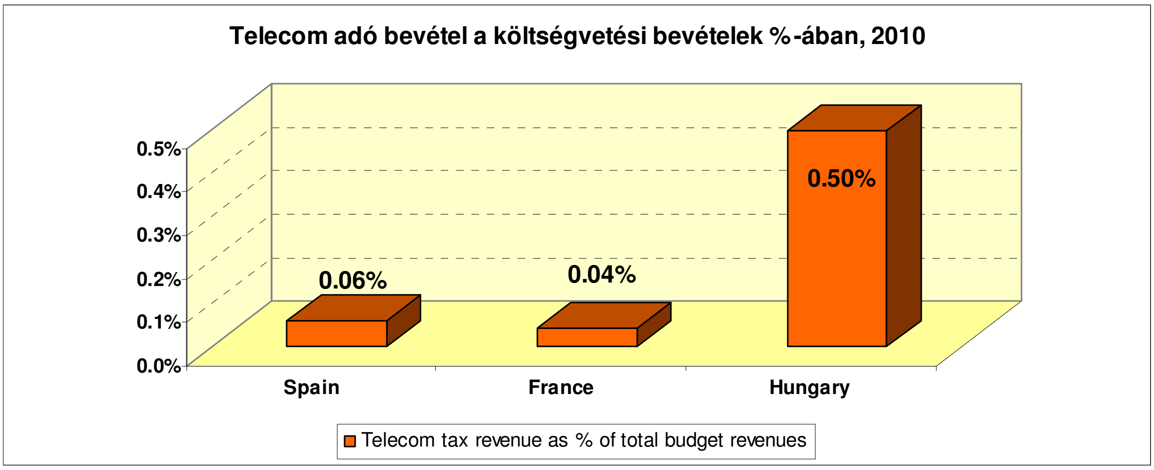

Chart 2. Telecom tax revenues as % of total revenues, Source: IMF and own research

2010	Spain	France	Hungary
Budget revenues (bn EUR)	380	958	44
Telecom tax revenue as % of total budget revenues	**0.06%**	**0.04%**	**0.50%**
Telecom tax revenue (bn EUR)	0.23	0.40	0.218

Table 4. Telecom tax revenues as % of total tax revenues, Source: IMF

[15] France Telecom May Lose Appeal Over $1.55 Billion in Tax-Break Subsidies, Bloomberg 8 September 2011 http://www.bloomberg.com/news/2011-09-08/france-telecom-may-lose-appeal-over-eu1-1-billion-in-subsidies.html

Digital Agenda: Commission refers France and Spain to Court over 'telecoms taxes' 14 March 2011 http://europa.eu/rapid/pressReleasesAction.do?reference=IP/11/309&format=HTML&aged=1&language=EN&guiLanguage=fr

[16] EU steps up telecom tax action on France, others, Dow Jones Newswires 14 March 2011 http://www.totaltele.com/view.aspx?ID=463225

B Special tax on retail and energy companies

The two tax types share certain characteristics: They were imposed on company turnover – as opposed to profits, in order to avoid tax evasion and both were introduced retroactively. Both taxes hit foreign-owned companies most. (The biggest Hungarian retail chains were unaffected due to fragmented ownership forms. According to unofficial remarks and discussion minutes, however, the clear intention of the lawmakers was tilting the playing field toward Hungarian-owned retailers.)[17]

	Billion HUF	
Budget revenues, 2010	12095	
Telecom tax revenues	61	0.50%
Special tax on energy sector	70	0.58%
Special tax on retail sector	30	0.25%

Table 5. The Hungarian special taxes as % of all 2010 budget revenues, Source: own research

C International examples of windfall taxation

In 1997 the incoming British Labour government had imposed a windfall tax on privatised utilities. The tax was claimed to be on "the excess profits of the privatised utilities" in Labour's election manifesto. It was widely held that the privatisation of many state-owned assets by the previous Conservative government were at prices too low. The tax produced an estimated one-off revenue of GBP 5 billion, which was meant to fund the *New Deal*, a welfare-to-work program that sought to tackle long term unemployment. In the words of Gordon Brown the "reform of the welfare state — and the programme to move the unemployed from welfare to work — is funded by a new and one-off tax on the excess profits of the privatised utilities."[18]

[17] http://www.trademagazin.hu/piaci-hirek/kulonado-es-gazdasagi-valsag-nem-zart-jo-evet-tavaly-a-spar-es-az-auchan.html

[18] Budget speech delivered on 2 July 1997.

This form of windfall tax was thus paid by national champions – as opposed to foreign-owned companies.[19] Since 1997 there was no windfall tax in the UK – although there were attempts and calls for it.

In 2008, after the bankruptcy of the biggest UK mortgage lender, Northern Rock there were calls for a windfall tax on banks to fund similar government efforts – but the Labour government decided for nationalisation instead. Also in 2008 there were calls for another windfall tax on energy companies – but it was not followed through.

In March 2011, the Conservative British Chancellor of the Exchequer, George Osborne announced a levy increase on energy companies – a rise on the supplementary charge to North Sea oil and gas producers from 20% to 32%. He said the tax increase was needed to fund his cut of the duty on petrol. Osborne said the levy would raise about GBP 2 billion but independent experts have put the number closer to GBP 10 billion. According to Osborne the industry will not be able to pass on the extra cost because the price of oil is set internationally.

North Sea oil and gas accounts for a big share of the UK's economic output. At least 500 000 people are employed in the sector generating GBP 6.5 billion from corporation tax and revenue tax in 2010.[20] Reserves in the North Sea have been, however, gradually running out. In the past five years the UK has become a net importer of fossil fuels as the enormous oil and gas fields have been depleted. One way out of the problem would be the application of costly, new engineering techniques and advances in seismic geology to exploit remaining reserves, but the extra levy may halt companies from introducing profitable, new exploration forms. Their share prices were instantly hit and Centrica decided soon afterwards to leave idle the UK's biggest gas field, South Morecambe, because the tax rise means extraction is simply not worth its while. The firm calculated that when other energy taxes are taken into account, the 2011 increase of levy

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[19] An incomplete list: BAA, British Energy, British Gas, British Telecom, National Power, Northern Ireland Electricity, Powergen, Scottish Hydro, Scottish Power, Scottish Railtrack, regional power suppliers, water utilities.

[20] Oil giants warn that Osborne's windfall tax could hit North Sea exploration, The Guardian, 27 March 2011 http://www.guardian.co.uk/business/2011/mar/27/fuel-duty-windfall-tax-chancellor

lifted the total tax rate for the South Morecambe field from 75% to 81%. Similarly, Norwegian energy giant Statoil plans to curb the development of its North Sea fields.[21]

In September 2011 a one-off windfall tax on UK nuclear power plants was called for after they were unintentionally left exempt from a Europe-wide carbon tax targeting non-renewable energy generation. The „extra profits" nuclear plants can thus make should be taken away – says the argument with the revenue earmarked on low-income households' energy subsidies – making the new levy called for by the Liberal Democrats, the junior UK coalition partner doubly justified.[22]

The relevance of the levy for our purposes that it hits a French national champion, EDF especially heavy since it owns eight and operates six of Britain's nuclear plants. The tax would be introduced in 2013 with an estimated revenue of 200 million pounds.

A similar nuclear tax has been proposed in Germany but the reason is not any "extra profit" nuclear generators earn under the European carbon tax regime but the strong anti-nuclear sentiment in Germany. The proposal comes from the junior coalition partner, the FDP and it is meant to punish any extension from the originally planned nuclear phase-out in Germany.[23]

Two further examples for windfall tax came from Greece (on most profitable enterprises according to their 2009 results, extended until 2013 – as part of the austerity measures demanded by the IMF[24]) and the US. The special levy on American pharmaceutical companies was designed to cover extended lifespan and the resulting higher medical costs

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[21] A taxing problem in the North Sea , The Telegraph, 2 June 2011
http://www.telegraph.co.uk/comment/telegraph-view/8553452/A-taxing-problem-in-the-North-Sea.html
Oil firms 'rethink investment' after £2bn tax hike, BBC, 29 March 2011 http://www.bbc.co.uk/news/uk-scotland-scotland-business-12887877

[22] U.K. Needs Windfall Tax on Nuclear Plants, Coalition Party Says, Bloomberg, 20 September 2011
http://www.bloomberg.com/news/2011-09-20/u-k-needs-windfall-tax-on-nuclear-plants-coalition-party-says.html

[23] Merkel Standing by Nuclear Windfall Tax, FDP Coalition Lawmaker Breil Says, Bloomberg, 26 August 2010
http://www.bloomberg.com/news/2010-08-26/merkel-standing-by-nuclear-windfall-tax-fdp-coalition-lawmaker-breil-says.html

[24] Greece: Financial services report, Economist Intelligence Unit, 18 January 2011 http://www.eiu.com

and it was proposed by Nancy Pelosi in 2009 during the Obamacare debate. It has not been introduced.

These taxes are either part of a domestic political game or means to raise extra revenues for the government. They are also rich in unintended consequences.

Special levy on energy companies is a favoured tool all over Europe but rarely capable of taxing foreign-owned companies only. There is no European directive on the taxation of energy utilities.

D Pharmaceutical industry

Among the Hungarian special taxes features the reduction of state subsidies to drugs and medicines. According to the Széll Kálmán Plan, "*Hungarian taxpayers no longer subsidise the extra profit of big pharmaceutical companies*". It entails the reduction of the price-subsidies of certain medications while making sure it would not be paid for by the customers.[25] It works through an increase of a previously existing levy that required pharmaceutical companies to repay 12% of the subsidies they were given by the national health insurance fund (imposed in 2007). The repayment was now increased to 20%.

We have found two more examples of special contribution of pharmaceutical companies in Eastern Europe. The Romanian government has replaced an ineffective special levy with a new form of tax in 2011. According to the 2010 tax regime, pharmaceutical companies operating in Romania were subject to a 5-11% levy (retroactively to beginning 2010) with the estimated revenue of EUR 119 million. This, however, has failed to collect the desired revenue and was therefore replaced by a new regime. It requires paying the difference between the national health insurer's forecast and the actual drug consumption in Romania – split between pharmaceutical companies according their market share. [26]

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[25] Page 27 of the Széll Kálmán Plan

[26] Claw back tax to be changed in Romania, 7 July 2011 http://www.ceepharma.com/106926/Claw-back-tax-to-be-changed-in-Romania.shtml Romanian government approves new version of claw-back tax, September 2011 http://www.ceepharma.com/110912/Romanian-government-approves-new-version-of-claw-back-tax.shtml

In Poland, the change in the VAT affects the revenues of the pharmaceutical industries. The increased VAT of 23% from January 2011 to 2013 affects medications as well. The price of subsidised medication is, however, still regulated and thus the rise of the VAT must be covered by the companies.[27]

[27] Poland: VAT Changes Affecting the Pharmaceutical Sector, Cameron McKenna, 19 January 2011 http://www.mondaq.com/article.asp?articleid=120678

FAT TAX

Among the unorthodox tax measures, taxes aimed at behavioural change generally meet the lowest degree of taxpayer resistance. Arguments against paternalistic government mostly escape the attention of the majority of voters who find it hard to argue against a tax measure brought "in their own interest". Behavioural taxes like the fat tax is thus a good candidate for raising revenue – similarly to parking fines, speeding tickets, security-related measures and the already established excise duty on tobacco and alcohol. Their effectiveness in manipulating behaviour (or reducing medical bills) may be empirically low or non-existent, the revenue is still (and therefore) certain and temptingly large.

Fat tax is a revenue form based on the perceived health-damaging effect of certain food groups – according to present science and common wisdom. It may be waged according to the sugar-, salt-, caffeine- and fat content of certain products, or based on a constantly changing and adjustable classification of food products. The lawmaker may also introduce special exemptions and tax breaks on food types considered part of their national culture or products manufactured by local companies or other politically supported entities. The manipulation of the new duty thus enables the governments to enter a new area of seemingly inexhaustible revenues and legally backed market manipulation.

The Hungarian fat tax was introduced in September 2011 and targets sugary drinks, energy drinks, sweets, snacks and certain types of flavour enhancement. It was originally targeted on fast food chains (and consequently coined "hamburger tax") but the original target group later became exempt. The fat tax is not based on the sugar-, salt-, etc. content of products but is instead based on total quantities of specifically targeted products – giving a huge task to legislation, enforcement and manufacturers as well, who are already adjusting recipes to avoid the extra tax. It is also obvious that once the bureaucracy is in place constant adjustment of the products and the targeted food types is to be expected, while new product groups will be an obvious target for raising new revenues in the future. The annual readjustment of the tax is also required to maintain the desired revenue level.

International examples of "fat tax"

The United Kingdom is the most obese country in the EU and thus has the longest history of considering some form of fat tax. The situation is similar in the US (fat tax having been debated on and off since 1994), but the introduction seems still remote due to bigger suspicion of government paternalism in the public debate.

A tax justified by inflated healthcare cost may attack either food or waistlines – the latter inducing an even bigger intrusion in the individual's life through taxes levied based on medical fitness or variance from the government-imposed waistline standard (as seen in the Japanese example).

When studying a certain example of fat tax, it is also worth watching whether the collected revenue is earmarked for its supposed destination (funding healthcare) or does it only indirectly by enriching the budget. Japan and Denmark have introduced fat taxes that directly fund health insurance while the Hungarian tax is only a general budget income. Hungary is also far less affected by clinical obesity than either the US or the UK – and so are Denmark and Japan.

The Danish fat tax was introduced in October 2011 and it is based on the sugar and fat content of food products. Estimated government revenue is 2.2 billion Danish krone going directly in the health insurance fund.[28]

Japan introduced a special form of "fat tax" in 2008.[29] According to the Japanese example, employees are incentivised through their corporate employers (or local councils) to lose weight and get back in shape for the annual measurement. It is then charged on the company if its employees are found having gained weight to support the employee's weight loss. If a

[28] Fat Tax in Denmark Agreed, Agriculture and Food, 22 June 2011 http://www.agricultureandfood.co.uk/Current_issues/Danish_Matters/2011/June/Fat_tax_in_Denmark_agreed.aspx http://www.telegraph.co.uk/health/healthnews/8796522/Denmark-taxes-fatty-products.html

[29] Source: Fat in Japan? You're breaking the law. 10 November 2009 http://www.globalpost.com/dispatch/japan/091109/fat-japan-youre-breaking-the-law

corporate target is not met, the company has to contribute an extra to the national health service. The target is to decrease medical bills on what they call “metabo” syndrome, a symptom group widely associated with obesity, including high blood pressure, high cholesterol level and diabetes. Since Japan is one of the least obese countries in the world, the extra revenues may instead fund the medical bill of the world’s most rapidly ageing population.

Fat taxes targeting food groups are very regressive. They penalise the lowest income groups hardest because of two reasons: 1) food is strongly represented in their consumption basket and 2) the sugar- or alcohol content is constant in a product regardless of whether it is targeted at low income groups or marketed as luxury item – and thus the levied tax would be nominally the same on both items. (A similar fat tax was debated, but the idea dropped in Romania for the same reasons.)

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