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Spain Windfall Levy Case Opens Path to Taxing Sectors Beyond Oil

By Sam Edwards

- Levy aimed at banks, utilities took effect Jan. 1
- Government says first payment raised almost €1.5 billion

A legal battle over the implementation of Spain's new windfall profit tax aimed at banks and energy companies could make it easier to tax other sectors seeing booming profits during an economic downturn.

In the final days of last year, Spain's parliament approved a new tax aimed at raising billions of euros from utilities and banks—two sectors that have seen soaring profits in recent months. It took effect Jan. 1 and is already the subject of several legal challenges by energy company Repsol and associations representing the banks Banco Bilbao Vizcaya Argentaria and Banco de Sabadell, among others.

If the law were able to withstand legal challenges, it would set a precedent as an alternative approach to taxing companies that have enjoyed booming profits, without actually taxing profit, according to several tax professionals. It could also allow authorities to introduce one-off taxes targeting specific sectors benefiting from the results of an economic downturn such as rising oil prices and high interest rates.

The government argues the levy isn't a tax, but rather a nontax contribution—a figure established under Spanish law, normally as a charge levied in exchange for the provision of public services.

"If the courts decide that this figure is not sound, it will act as a defense against future governments passing levies with a quasi-tax nature outside of the tax system," said Ignacio Ucelay, Of Counsel at Baker McKenzie in Madrid.

If the law stands, however, it could establish a precedent for taxing other sectors benefiting from inflation, he added.

Raising Revenue

The levy, which taxes utilities' sales at 1.2% rather than profits, is designed to raise revenue to offset the impact of inflation on households. It also charges banks 4.8% on money they make in interest plus net commission. The tax is due to run for two years, though the government has said it might extend it beyond that.

Since companies can't challenge the tax directly, banking and energy sectors have filed several motions on the form of payment—whereby companies estimate their bill for the year and make an advance payment on predicted profits. AELEC, an association representing utilities, also said it believes the design of the tax itself is discriminatory and unfair because it targets sales not profits.

The introduction of a new way of taxing specific sectors could be an attractive proposal for governments looking to raise revenue in the future, said Alberto Ruiz Ojeda, partner at Cremades & Calvo-Sotelo in Malaga.

The new taxes might have other practical advantages. In comparison with using corporation tax, for example, the temporary windfall levy has the advantage that it doesn't allow companies to offset losses from previous years, for example, Ucelay said.

"These extraordinary windfall taxes are very easy to collect," he said. "In this case, the justification is the special economic context. But later that can become permanent, or simply no one acts to remove it, that's the danger I see," he added.

The new levies were designed in line with the law, said David Valera, a finance ministry spokesman. "We are convinced of their legality and their legal solidity," he said.

Asked about the various legal challenges to the law last month, finance minister Maria Jesús Montero said she was confident that courts would rule in the government's favor.

"We're sure that our tax is just and legal and it falls within our powers," she said during a press conference. "This isn't about using the powers of others or pursuing people, it's about asking for a greater contribution from those better off."

The tax was part of the government's plan for dealing with several years of economic upheaval, Montero added.

"When the government published its tax plan for these difficult years, we always said we were pursuing a strategy of tax justice, in which those with the most, and those who earn the most make a greater contribution to the majority," she said.

Legal Fight Ahead

Several companies and associations representing utilities, energy firms, and banks filed motions in February against the regulations accompanying the law. This followed the first payment of the charge, for an estimated 50% of the total amount due in the year, which the Ministry of Finance said brought in almost €1.5 billion, in line with forecasts.

In its first ruling, the high court rejected a request by energy company Repsol to block the law preemptively, saying that paying the levy wouldn't cause irreparable harm to the oil giant.

Repsol wasn't immediately available for comment.

Two associations representing many of Spain's largest banks, such as Banco Santander, BBVA, and Sabadell, recently filed their own motion against the regulations accompanying the bill, it said last month.

Santander declined to offer additional comment. BBVA and Sabadell didn't respond to a request for comment.

There are other possible ways the law could be challenged in court, said Enrique Beaus, partner and head of the tax law department at Brosetas in Valencia. The levy might violate principles of EU law such as freedom of competition, movement of capitals, and offering services, he said.

“Many of Spain’s laws which have been overturned recently have been rejected for violating EU law,” Beaus said. “In my opinion, this is a strong argument in this case.”

The fact that the tax applies to earnings in 2022 and was only introduced in December last year, could be seen as a violation of the principle of legal certainty, under which companies are able to predict what tax bill they might face, said Patricia Sánchez, counsel in tax for Hogan and Lovells in Madrid.

“This form of creating levies and taxes on the go and affecting the tax year underway creates uncertainty and insecurity that negatively impacts economic activity,” she said.

Spain’s constitutional court said on March 21 it would study the legality of the law underpinning the windfall profit levies. The court accepted a motion challenging the constitutionality of the tax filed by the regional government of Andalusia, which is controlled by the opposition party. The court rejected a request to immediately suspend the levy.

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