PositiveMoney

Options for a windfall tax on banks

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Summary

- A number of European countries, including Italy, Spain and the Czech Republic, are introducing additional taxes on the windfall profits banks are making from higher interest rates.
- A windfall tax in the UK could be expected to raise between **£3bn and £20bn from the profits of the big four banks alone in 2023**, depending on how it is designed.

The public are paying the price of banks' windfall profits

- Banks are receiving tens of billions of pounds of public money due to the way in which the Bank of England currently remunerates central bank reserves.
    - Analysis from BoE deputy governor Sir Paul Tucker suggests that **banks are due to receive £42bn and £33bn in 2023 and 2024** from interest paid on risk-free reserves. The costs of this are ultimately borne by the Treasury.
- Higher interest rates have also enabled banks to charge households and firms more for mortgages and other loans. Banks are making exorbitant profits by not passing these gains onto depositors.
- The UK's big four banks - HSBC, Barclays, Lloyds and Natwest - reported **pre-tax profits of £28.93bn for the first six months of 2023**. This is a nearly 725% increase on the same period in 2020, before rates started rising, and suggests the big four could be on track to make record annual profits of nearly **£60bn this year**.

Option 1: raising the existing surcharge in line with the Energy Profits Levy

- The government introduced a bank profits surcharge in 2015, in recognition of the need for banks to "make a fair contribution in respect of the potential risks they pose to the UK financial system and wider economy." However this surcharge has recently been cut from 8% to 3%.
- Raising the surcharge in line with the 35% Energy Profits Levy imposed on oil and gas companies could be expected to raise around **£20.3bn from the 2023 profits of the big four banks alone**, based on results reported so far - equivalent to around £720 per household.

Option 2: the Thatcher government model

- In 1981, the Thatcher government introduced a 2.5% tax on banks' non-interest bearing deposits. As Thatcher explained in her memoirs: "Naturally, the banks strongly opposed this; but the fact remained that they had made their large profits as a result of our policy of high interest rates rather than because of increased efficiency or better service to the customer."
- The BoE's latest data shows there are around £450bn of non-interest bearing deposits that could be eligible for such a levy today, with around £270bn held by

households and £180bn held by non-financial firms. A 2.5% tax would therefore be expected to raise **more than £11bn** – equivalent to nearly £400 per UK household.

Option 3: the Czech model

- The Czech government has introduced a 60% windfall tax on bank profits exceeding 120% of the 2018-21 average, which will apply for three years from 2023.
- The big four banks in the UK recorded an average pre-tax profit of £25.9bn between 2018 and 2021. Based on the profits reported by the big four banks this year so far, we estimate that replicating the Czech tax could be expected to raise more than **£17.35bn** from these banks' profits in 2023.

Option 4: the Italian model

- The Italian government recently announced a 40% windfall tax on the difference between banks' net interest income (NII) in 2021 and the figure for 2022 or 2023, depending on which is larger.
- In the UK the big four banks' NII was £46.11bn in 2021. Based on their NII for the first half of the year (£30bn), we can estimate a £13.89bn difference in 2021 and 2023 for the big four banks, a 40% levy on which would raise **£5.56bn** - around £200 per UK household.
- The Italian government subsequently watered down its windfall tax, capping it at 0.1% of total bank assets. However, such a cap would still allow around £13bn to be raised in the UK.

What could be done with the proceeds of a windfall tax?

- If a windfall tax raised £20bn a year, as could be expected from options 1 or 3 above, this would be enough to reinstate the £20 universal credit uplift, abolish the two-child benefit cap, provide free school meals to all children and give public sector workers a 10.5% pay rise. Alternatively, it could fund a 2.5% cut to VAT, which would also help reduce inflation.[1]

For further reading, see 'How much coud a windfall tax on banks raise?'

Positive Money is a not-for-profit research and campaigning organisation, working towards reform of the money and banking system to support a fair, democratic and sustainable economy. We are funded by trusts, foundations and small donations.

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[1] Based on the IFS' estimate that a 5% cut to VAT would cost £38bn.