How to pay for a Green New Deal: Personal taxes

The UK needs a major programme of investment in order to move our economy beyond fossil fuels, improve our public services and tackle the cost-of-living crisis. This is one of five briefings summarising how that investment can be paid for. To read the other briefings, visit greennewdealgroup.org.

1. Equalise tax rates on income from wealth with those on income from work

Wealth, and the income it generates, is significantly undertaxed in the UK. While income tax is relatively progressive (i.e. higher earners generally pay higher rates), a proportion of the income of the wealthiest people in the country is generated not from employment, but from investments and capital gains. For the top 0.1%, more than half their income is derived from these sources. These are taxed at significantly lower rates.

	Income tax band (2023-24 thresholds)		
	Basic rate (£12,571-£50,270)	**Higher rate (£50,271-£125,140)**	**Additional rate (over £125,140)**
Income tax	20%	40%	45%
National Insurance	10%	2%	2%
Total tax on earnings from employment	30%	42%	47%
Tax on dividends	8.75%	33.75%	39.35%
Capital gains tax	18% on residential property; 10% on other taxable gains.	28% on residential property; 20% on other taxable gains.	

People in the top 1% of incomes (above £125,000) receive an average of £47,000 a year in capital gains in addition to their income. It was reported in February that Rishi Sunak paid tax at an overall rate of just 23% in 2022-23, because most of his £2.23m income was in the form of capital gains.

As well as resulting in the wealthiest paying a lower rate of tax than most people, having different tax rates for different kinds of income also leads to people reorganising their working arrangements to take advantage of this – advantaging those (mainly the wealthy) who can choose to receive their income in the form of dividends or capital gains.

The proposal to tax capital gains at the same rate as earnings is generally popular with the public: 65% believe income from wealth should be taxed either at the same rate as, or a higher rate than, income from work. There is nothing new about this proposal: it was introduced by Nigel Lawson as Conservative chancellor in 1988, and the rates remained aligned until Gordon Brown reduced the rate of capital gains tax in 2008.

Aligning capital gains tax rates with income tax rates would raise between £12 billion and £16 billion a year.

More could be raised if the national insurance advantages from receiving dividends, interest and rents were also addressed. Advani, Hughson and Summers suggest that “if everyone with total remuneration over £100,000 paid the headline tax rate that currently applies to earnings from employment (i.e. 47 per cent) across all forms of taxable income, this would raise up to £23 billion in addition to the revenue from equalizing capital gains tax rates." They note that this figure does not take account of possible changes in behaviour as a result of such a policy, which might reduce the revenue generated.

Richard Murphy suggests that up to £18 billion could be raised by reintroducing an 'investment income surcharge' – an additional tax on income from unearned sources to compensate for the fact that national insurance was not paid on that income. He argues that this surcharge should cover capital gains as well as investment income (excluding pensions), above an allowance of £5,000 a year.

2. Abolish the lower rate of national insurance for high earners.

Employees earning £1,048 to £4,189 a month pay 10% of that income in national insurance (NI) contributions. Above this level of income (just over £50,000 a year), the rate falls to just 2%. This makes NI regressive (i.e. those with higher income pay a lower rate) at the top of the income distribution, and is part of what makes the UK tax system regressive overall.

NI was first introduced in 1911 as a form of insurance, where those contributing could receive sickness or unemployment benefits. Over time, the link between contributions and benefits has been weakened, to the point where NI behaves essentially like another income tax. There is therefore no justification for the lower rate for high earners.

Murphy estimates that abolishing the lower rate of NI for high earners could raise around £12.5 billion a year. If the aim is to make the tax system fairer rather than to raise revenue, this could be used to reduce the overall rate of tax paid by those on lower incomes.

Mythbusting

Myth: *Increasing taxes reduces the overall tax take because high earners leave the country or change their behaviour to avoid paying.*
Reality: This view is based on instinct and anecdote rather than data. It relies on two assumptions: that wealthy people choose where to live based primarily on the tax rate; and that the impact of any outward migration in response to tax reform would outweigh the increased tax revenue generated from those who stay. In reality, there are numerous factors determining a person's choice of where to live, including career, cultural and family ties. A 2022 paper based on data from the UK's reform of the 'non-dom' tax regime found that its impact on migration of the super-rich was close to zero .

Myth: *Higher taxes on capital gains would deter investment.*
Reality: There is no evidence of a correlation between low capital gains taxes and high investment. A 2015 study looking at the 2003 dividend tax cut in the US found no change to wages or corporate investment. Instead, companies tended to respond by increasing payouts to shareholders.

Myth: *National insurance is how we save into our state pension, so no one should have to put in more than they'll take out.*
Reality: The amount of state pension you receive is not linked to the amount you have paid in, and it is not paid from your past contributions. Rather, today's pensions are funded by the NI contributions of today's workers. The government can also top up the NI 'pot' or use any surplus to pay for other things, so it essentially operates like any other tax.

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