

# **A Feasible Basic Income in Korea: To Promote Freedom, Equality and Sustainable Efficiency**

**Session 1: pages 2-5**

**Session 2: pages 6-18**

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# Objectives

- Real freedom for all
- Equality: Equal right to common wealth
  - Alleviation of inequality and poverty
- Sustainable efficiency
  - Economically sustainable efficiency
    - Means-tested targeted public assistance: efficient in poverty reduction in the short run, but not in the long run
    - Deadweight loss, increasing budget, reduced labor supply, decline of GDP growth
  - Ecologically sustainable
  - Demographically sustainable
    - Fertility rate: 0.78 in 2022 in Korea
    - Declining population and the risk of extinction of rural municipalities

# A feasible plan

- Financially feasible
  - **Fiscally neutral** plan
  - Principle of **reciprocity**: The **right** to basic income requires a **duty** to pay taxes
- Politically feasible
  - NIT-Type Basic Income
    - Easier to sell “differential benefits according to income” than “UBI with flat(or progressive) tax”
    - G. Mankiw: 90% of Harvard undergraduates chose an NIT scheme over a BI scheme with the same redistributive effect
    - Soomi Lee: Public support for UBI is based on their concern for **equality** rather than **unconditionality**
  - Universal EITC: “Make EITC more like a UBI”
    - Regressive employee income deductions in Korea (and Japan): We proposed replacing them with UBI, but faced resistance from working people.
    - Replacing the deductions and the current EITC with a universal EITC on an individual basis
  - Common Wealth Dividends Basic Income

# Effective tax rate, participation tax rate, and effective marginal tax rate

- Effective tax rate incorporates both taxes and transfers(benefits):
  - should be progressive, promoting equality.
  - Negative for low income, and positive and increasing for high income
- Participation tax rate & effective marginal tax rate:
  - Affect work incentives at the extensive and intensive margin
  - High PTRs and EMTRs create work disincentives and restrict freedom to improve one's situation through working
- Participation tax rate =  $1 - \frac{\text{increase in disposable income when working}}{\text{market income when working}}$
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- Effective marginal tax rate =  $1 - \frac{\text{increase in disposable income}}{\text{increase in market income}}$

# Individual-level vs. household-level benefits

- Social welfare provision based on needs:
  - Basic needs for a 4-member family are less than 4 times the basic needs for a 1-member family.
  - Higher benefits per person for smaller household size.
    - Marriage penalty and incentives for family break-up.
  - Higher housing benefits for residents of Seoul and metropolitan cities than for rural residents
- Basic income is based on everyone's equal right to common wealth
  - Basic income can promote marriage and household formation

# Korea's personal income tax

-nominal tax rates: very progressive

| <b>Tax base</b> (after exemptions and deductions) | <b>Tax Rate</b> |
|---|-----------------|
| Up to 14 million won                              | 6%              |
| Over 14 million won and up to 50 million won      | 15%             |
| Over 50 million won and up to 88 million won      | 24%             |
| Over 88 million won and up to 150 million won     | 35%             |
| Over 150 million won and up to 300 million won    | 38%             |
| Over 300 million won and up to 500 million won    | 40%             |
| Over 500 million won and up to 1 billion won      | 42%             |
| Over 1 billion won                                | 45%             |

# Employee income deductions

| Employee income (wages and salaries)          | Deduction Amount  |
|---|---|
| Under 5 million won                           | 70% of total employee income  |
| Over 5 million won and under 15 million won   | 3.5 million won plus 40% of the exceeding amount over 5 million won                               |
| Over 15 million won and under 45 million won  | 7.5 million won plus 15% of the exceeding amount over 15 million won                              |
| Over 45 million won and under 100 million won | 12 million won plus 5% of the exceeding amount over 45 million won                                |
| Over 100 million won                          | 14.75 million won plus 2% of the exceeding amount over 100 million won (capped at 20 million won) |

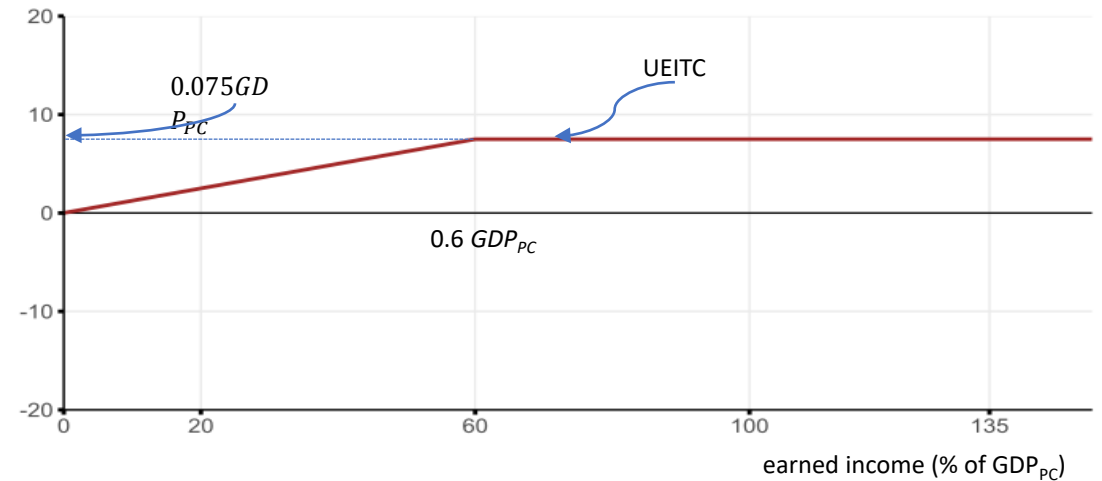
# Large tax reductions for the rich and small EITC benefits for the poor

| Employee income<br>(year-end settlement) |                     | Employee<br>income<br>deduction<br>(A) | Reduced<br>tax<br>due to A<br>(B) | Employee<br>income tax<br>credit (C) | B + C            | EITC<br>payment<br>(D) | B + C + D        |
|--|---------------------|--|-----------------------------------|--------------------------------------|------------------|------------------------|------------------|
| Total wages &<br>salaries (won)          | # of<br>individuals | Average<br>(won)                       | Average<br>(won)                  | Average<br>(won)                     | Average<br>(won) | Average<br>(won)       | Average<br>(won) |
| Total (average)                          | 19,074,871          | 9,371                                  | 1,470                             | 377                                  | 1,848            | 105                    | 1,952            |
| Up to 10 million                         | 2,890,704           | 3,045                                  | 183                               | 16                                   | 199              | 231                    | 430              |
| Up to 15 million                         | 1,431,264           | 6,518                                  | 397                               | 109                                  | 505              | 332                    | 838              |
| Up to 20 million                         | 1,551,944           | 7,889                                  | 655                               | 194                                  | 849              | 191                    | 1,040            |
| Up to 30 million                         | 4,331,915           | 8,927                                  | 1,143                             | 344                                  | 1,487            | 62                     | 1,549            |
| Up to 40 million                         | 2,611,774           | 10,451                                 | 1,546                             | 581                                  | 2,128            | 8                      | 2,136            |
| Up to 45 million                         | 949,555             | 11,614                                 | 1,739                             | 627                                  | 2,366            | 0                      | 2,366            |
| Up to 50 million                         | 795,809             | 12,122                                 | 1,817                             | 640                                  | 2,458            | 0                      | 2,458            |
| Up to 60 million                         | 1,220,521           | 12,487                                 | 1,873                             | 652                                  | 2,525            | 0                      | 2,525            |
| Up to 80 million                         | 1,575,979           | 13,210                                 | 2,666                             | 589                                  | 3,255            | 0                      | 3,255            |
| Up to 100 million                        | 863,500             | 14,179                                 | 3,393                             | 500                                  | 3,893            | 0                      | 3,893            |
| Up to 200 million                        | 754,109             | 15,265                                 | 4,741                             | 499                                  | 5,240            | 0                      | 5,240            |
| Up to 300 million                        | 60,188              | 17,181                                 | 7,030                             | 490                                  | 7,520            | 0                      | 7,520            |
| Up to 500 million                        | 25,362              | 19,686                                 | 9,096                             | 487                                  | 9,583            | 0                      | 9,583            |
| Up to 1 billion                          | 9,393               | 25,309                                 | 13,509                            | 487                                  | 13,995           | 0                      | 13,995           |
| Over 1 billion                           | 2,854               | 49,927                                 | 24,592                            | 495                                  | 25,087           | 0                      | 25,087           |
| Sum(billion)                             |                     | 178,746                                | 28,045                            | 7,196                                | 35,241           | 1,998                  | 37,239           |

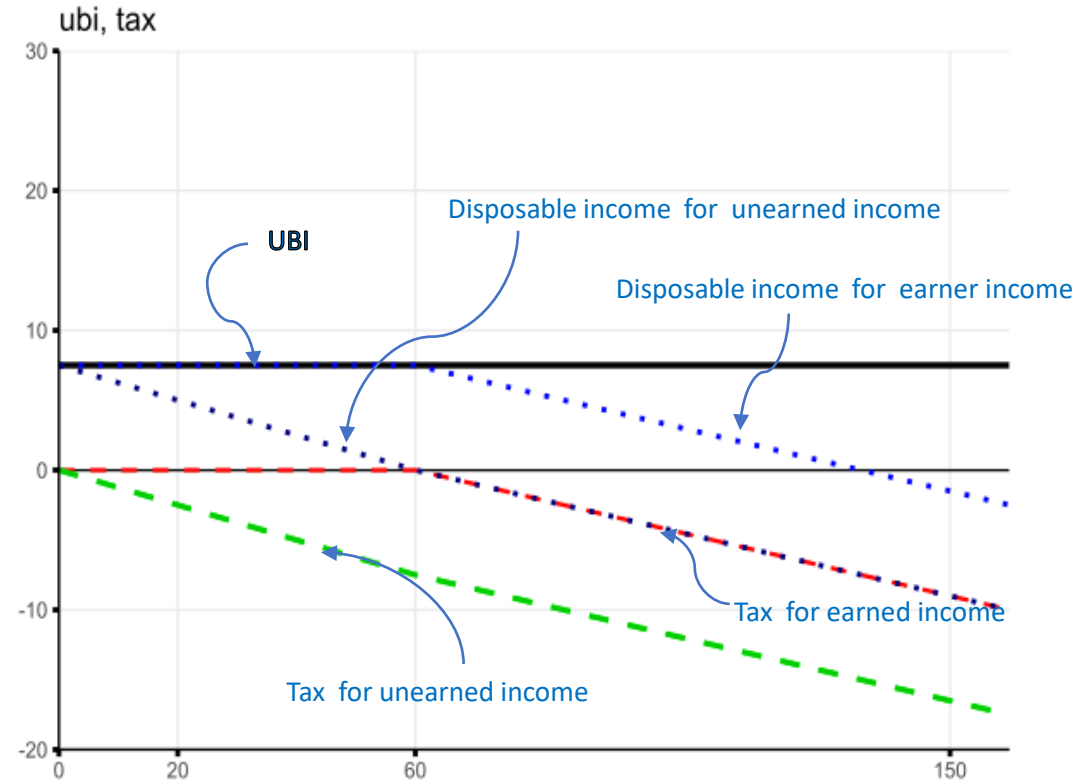
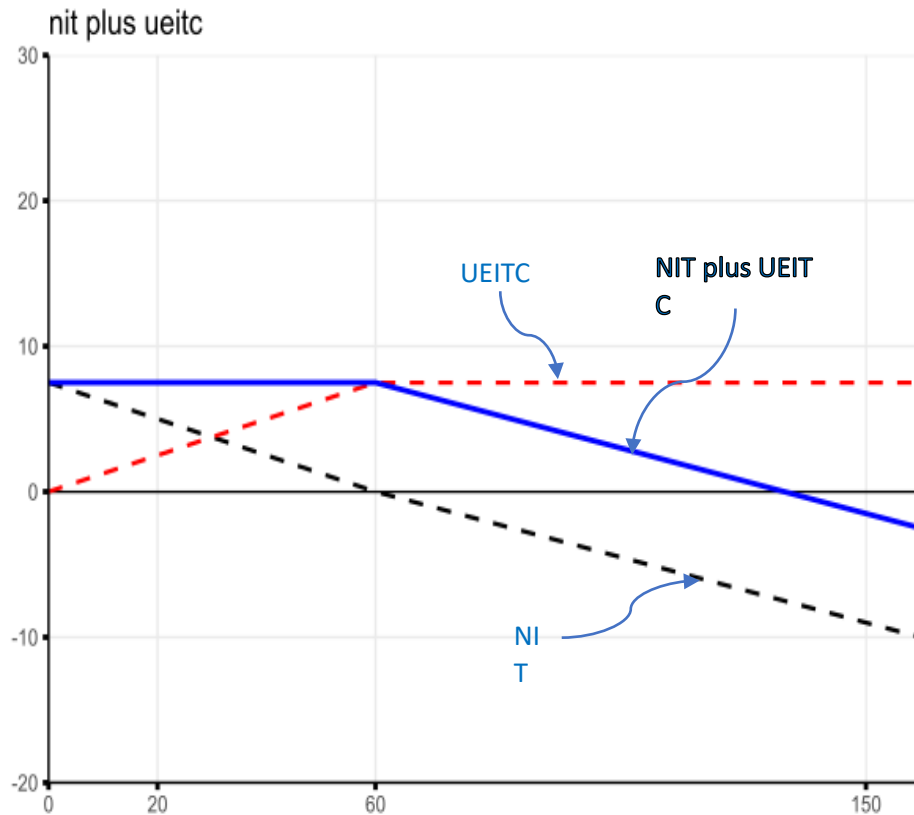


# Our Proposal

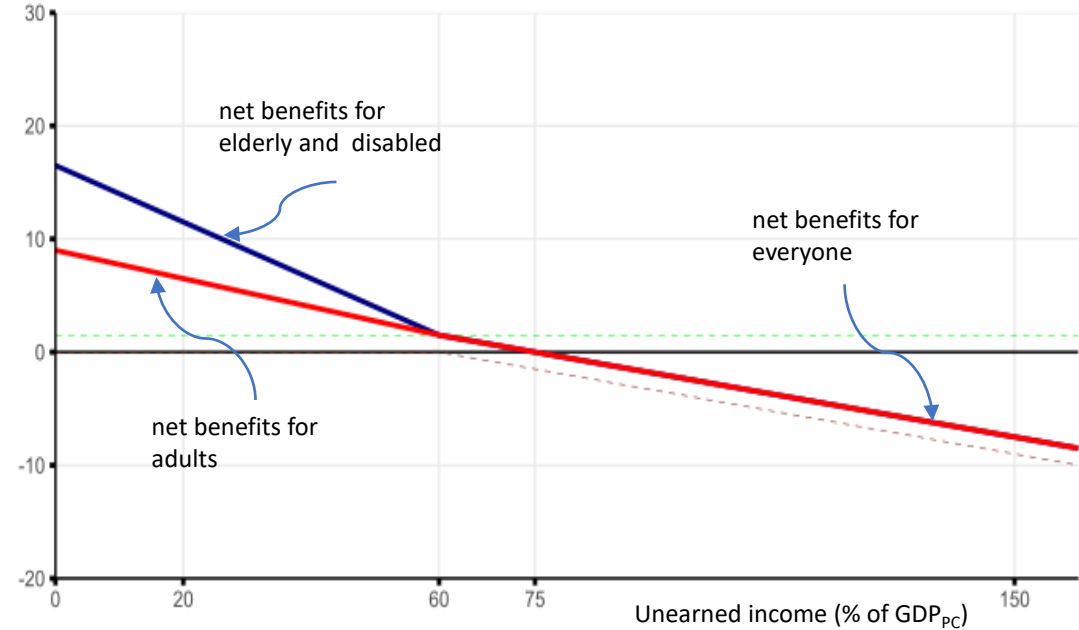
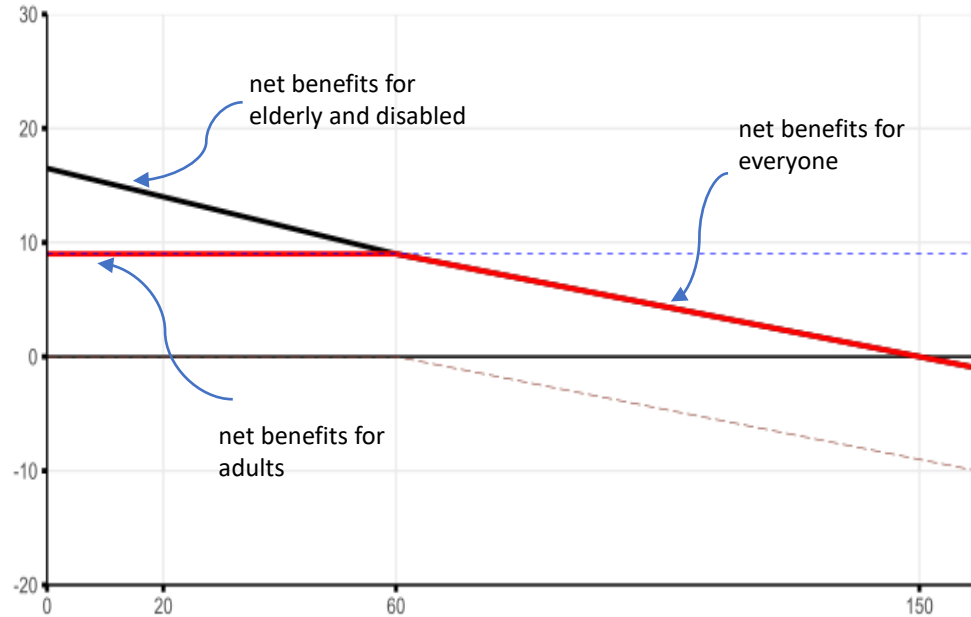
- 1) Common wealth dividend basic income
  - 2) Negative income tax-type basic income
  - 3) Universal earned income tax credit
- Why exclude the non-working?
  - A participation income?



“NIT-type BI plus UEITC” is equivalent to  
“UBI with different tax rates for earned & unearned income”



## Net total benefits for individuals with earned income(left) and unearned income(right)



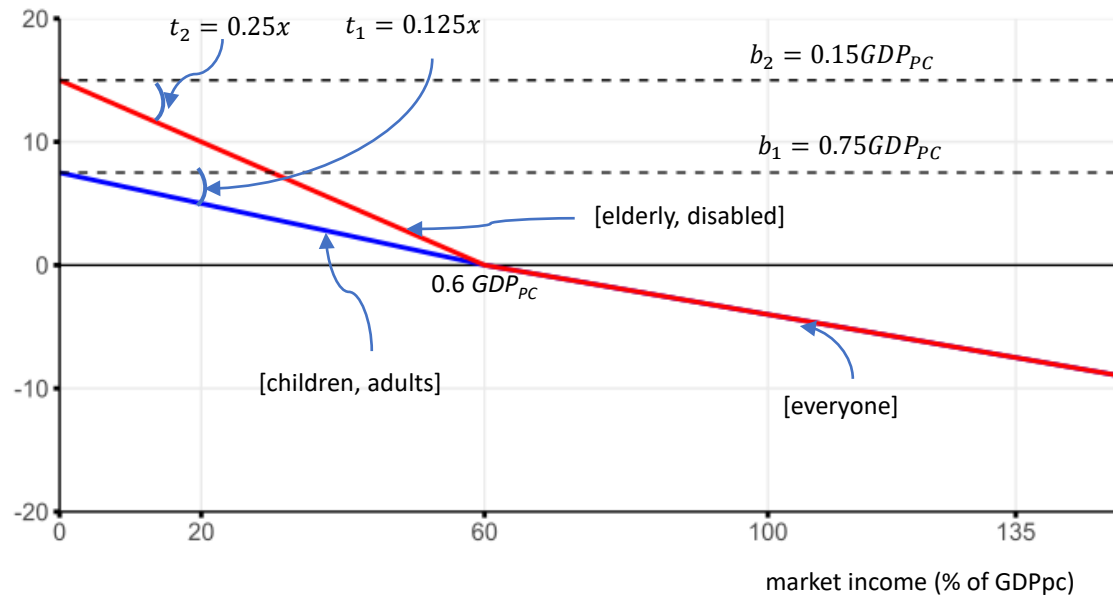
Whether working or not, net benefits are the same for zero income.

-Not a discrimination against the non-working individuals.

Net benefits decrease early and more rapidly for unearned income.

-Equivalent to higher tax rates for unearned income with the same levels of BI.

# Differential levels of basic income, or a single fixed amount of basic income and supplementary benefits for the elderly and disabled?



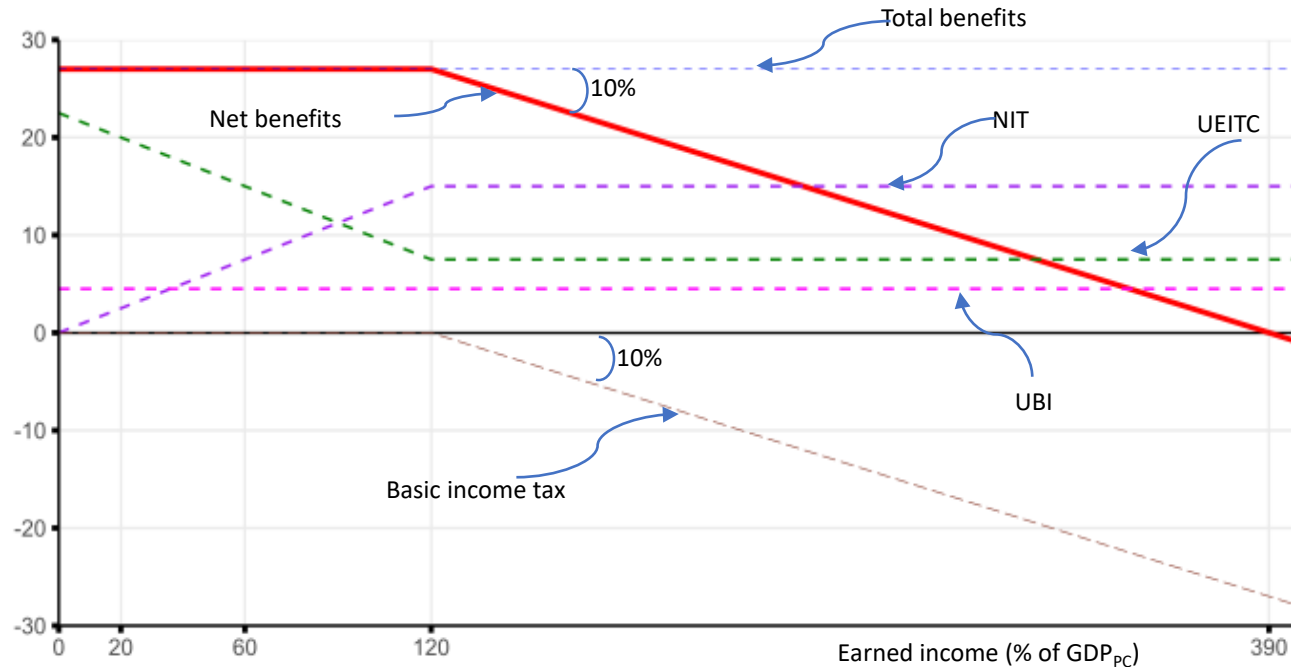
- We would like to get to the higher benefit for everyone.
- Before reaching that level, additional benefits are needed for the elderly and disabled.
- Two ways:
  - 1) Maintaining existing benefits for the elderly and disabled
  - 2) Streamlining and incorporating them as a supplementary NIT-type basic income.

[Figure 5-1] NIT-type basic income payments and basic income tax (unit, % of per capita GDP)

# Why different rates for clawback of benefits and taxing the excess income?

- 1) Considering the existing positive income tax rates
  - 6%, 15% for income below the threshold(break-even) income
  - 24%, 35%, --- 45% for income above the threshold
  - Marginal tax rates for
    - net beneficiaries of NIT-type BI= (6%, 15%) tax base + (12.5%, 25%) comprehensive income
    - net contributors of NIT-type BI= (24%, 35%---45%) tax base + 10% comprehensive income
    - Comprehensive income: No exemptions and deductions, including capital income (including imputed rent) and capital gains
- 2) Fiscal neutrality is possible with a lower tax rate than the clawback rate, because part of the existing public assistance benefits are replaced with NIT-type BI.

# Who claims NIT-type BI for children?



<Figure 5-11> Net benefits for a dual-earner couple with one child(with no income)

NIT-type BI is fixed, not dependent on which parent claims it.

The parents' individual taxes do not depend on children, unlike income deductions.

- Because each individual's benefit and tax are calculated separately.
- Children's NIT-type benefits are taxed(clawed back) if they have capital income, and not included in their parents' taxable income.

# Who claims NIT-type BI for adults with no income?

- Two possible ways
  - 1) Let every adult file annual tax return:
    - Report zero income and claim an NIT-type BI.
    - This assumes that the person will pay taxes when they have income.
    - Over the life course, most people will have years of zero income being net beneficiaries and years of high income being net contributors.
  - 2) Allow the household head to claim adult members with no income as dependents.

# Financial feasibility

Average amount of NIT & UEITC payment budget and increased revenue per person (unit: KRW)

|  |            |
|--|------------|
| nit payment                                    | -1,826,311 |
| nit-bi tax                                     | 1,179,503  |
| reduced public assistance                      | 389,850    |
| increased tax revenue from personal deductions | 267,584    |
| child tax credit                               | 90,449     |
| Child incentive payment                        | 20,223     |
| Balance  | 121,298    |

|   |            |
|---|------------|
| ueitc   | -1,324,227 |
| increased tax revenue from employee income deductions | 758,286    |
| employee income tax credit                            | 252,319    |
| current EITC  | 73,314     |
| Balance   | -240,308   |
| Sum balance   | -119,010   |
| Budget deficit (KRW billion)                          | 6,141      |

Our proposed programs are roughly fiscally neutral.

-Estimated budget deficit is just 0.3% of GDP.



# Distributive effects of our programs and Mayor Oh's 'safety income'

-microsimulation results, using SHFLC data

- Inequality reduction is greater from our programs
- Poverty reduction is greater from Oh's household-level 'safety income'

|                    | Gini coefficient | Poverty rate | Fiscally          |
|--------------------|------------------|--------------|-------------------|
| Current (2021)     | 0.331            | 15.12        |                   |
| Our proposal       | 0.276            | 10.29        | neutral           |
| Oh's safety income | 0.311            | 9.89         | 3% of GDP deficit |

- Oh's safety income:
  - Break-even at 85% of median household income
  - Guaranteed income of 42.5% of median household income
  - Clawback rate of 50%
    - Very high marginal tax rates including existing tax and social insurance contributions
  - Replaces part of existing public assistance benefits, but no additional tax

# NIT, BI, or NIT-type BI?

- NIT:
  - Different levels of guaranteed income and different clawback rates, depending on age and disability
  - Clawback rates are higher than tax rate for excess income
  - Amount of payment or tax is usually determined with annual tax return, with exceptions of quarterly claim.
- BI:
  - UBI with different tax rates for earned & unearned income
  - UBI with progressive income tax (considering the existing positive income tax)