Abstract

The international integration of factor and commodity markets implies that national authorities are increasingly affected by policy measures of other countries. A policy reform in one country is likely to induce policy reforms in other countries, which in turn affect the welfare in the first country. Given the policy interdependence, each country competes with its social security, redistribution, regulation as well as tax systems for mobile resources.

One widely-analyzed aspect of system competition is capital tax competition. However, the existing literature largely focuses on the issue of tax competition among independent countries. The present analysis extends the literature by considering the efficiency implications of capital taxation in a federal system. Specifically, the following chapters compare three different modes of federal capital taxation.

Chapter 1 introduces the basic capital tax competition model as elaborated by Zodrow and Mieszkowski (1986) and extends it in various ways. First, besides a source-based capital tax the government is allowed to use a labor income tax. Furthermore, the symmetry assumption is dropped in two ways. First, regions are allowed to differ with respect to their factor endowments and, second, they are asymmetric with respect to their preferences for public goods.

Chapter 2 introduces a central level into the basic tax competition model. The rationale for this extension is to analyze whether the inefficiency of decentralized capital taxation can be offset by providing unconditional grants to the regions. The issue is tackled in a federal system with capital taxation at the lower and labor taxation at the upper level of government.

Chapter 3 discusses the efficiency effects of tax coordination. Two forms of tax coordination are considered. First, capital taxation still occurs at the regional level. In this case, tax coordination is modeled as a simultaneous increase in the capital tax rate. Special attention is paid to capital tax coordination among regions with different preferences for public goods. Second, capital taxes are reassigned to a central government. However, the central level is imperfectly informed about regional preferences. Additionally, tax coordination takes place under full and no commitment power by the central government.