

Properties of Property Taxation

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Abstract

We explore properties of decentralized property taxation in a system of cities with mobile individuals. Fiscal decentralization causes inefficient race to the top taxation because local authorities excessively provide local public goods to attract mobile workers, thereby eroding the tax base of other regions. We evaluate the actual tax structure in Japan and Germany by conducting numerical simulations. Comparing to the observed state, the equilibrium tax rates under the decentralized regime are higher in Japan but lower in Germany. Transition to the decentralized regime from the observed one raises social welfare for both countries by 0.1–1.9%. Centralized taxation can mitigate the inefficiency of the race to the top behavior. Welfare gains from such coordination are, however, limited.

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