Cui and Miao: Taxing Sudden Capital Income Surges

discussed by

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The Paper in a Nutshell

MODEL

- Cont.-time het.-agent model
- Recursive utility with CARA
- Idiosyncratic hyper-exp. capital surges
- Flat capital tax plus extra tax on cap. surges

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Analytically Tractable!

Implementation?

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CALIBRATION

- Realistic cross-sectional wealth distribution
- Large return premium on (private) capital

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- Progressive tax distorts investment less than flat tax
- Capital taxation lowers wealth inequality if used to provide liquidity but raises wealth inequality if revenues are distributed equally

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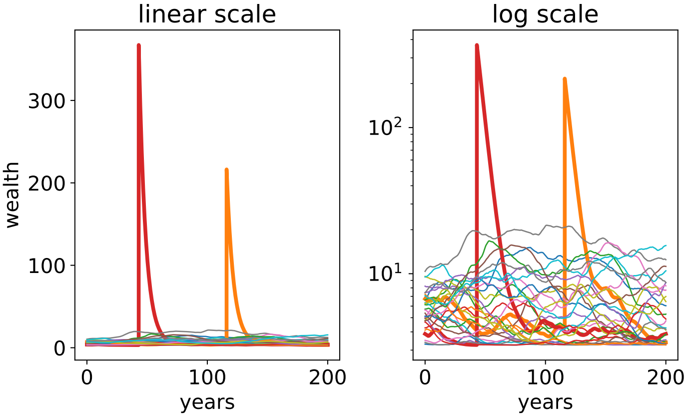
Modelling of Investment Choice?

Consumption Inequality?

Individual Wealth Dynamics in the Model



- The red and the orange experience large capital surges
- Not wealthier before, not much wealthier after several decades

Panel Evidence: How do the Wealthy get Wealthy?

- What about dynamics of individual wealth accumulation?
- The model features
  - constant MPC out of total wealth $\leftarrow$ homothetic preferences
  - equity share falling in wealth $\leftarrow$ CARA utility
- Hubmer et al. (2024): The top 0.1% in Norwegian admin. data ...
  - accumulate their excess wealth through higher saving rates (38%), inheritances (34%), returns (23%) and labor income (5%)
  - have far higher equity share (over 80%) than median (below 10%)

$\Rightarrow$ Be upfront about the fact that the model
  - (over-)emphasizes the role of new fortunes from investment
  - does not capture (potentially) heterogeneous saving rates

Capital Choice: What Drives Capital Surges?

Additional capital-surge tax distorts investment less than higher flat tax.

Why?

Innovation results from saving in private capital as a

- byproduct (like a lottery ticket)
- (ex ante) available equally to everyone
- (ex post) delivering rare huge returns

Making them less huge hardly impacts investment given risk aversion

Plausible?

Capital-surge tax might impact incentives to innovate differently if

- R&D is a separate decision from running ones business
- agents are heterogeneous with respect to (innovation) productivity, as in Guvenen et al. (2024) were wealth tax better than cap.-income tax

Consumption Inequality: Analytically tractable?

Capital taxation reduces wealth inequality if used for liquidity provision but raises wealth inequality if revenues are distributed equally

Why?

Lower precautionary savings from the poor due to higher transfers, among many channels in GE.

So what?

Wealth inequality might go down/up, but consumption inequality might move in the other direction.

$\Rightarrow$ Try to derive moments of consumption distribution analytically!

Taxing Capital Income Jumps: Implementation?

The model features accrual-based extra tax on capital income jumps

However, ...

- even if rapid and large, private equity gains are not jumps, taxing them right away may hinder innovation
- as asset prices fluctuate, optimal capital taxation is based on realization rather than accrual – see Aguiar, Moll, and Scheuer (2024)

Conclusion

- The paper elegantly makes the point that ...
  ... *taxing capital income jumps to fund the government debt can achieve a good balance between efficiency and redistribution*
- Certainly true if capital surges can be thought of as stemming from lottery tickets attached to ordinary private capital investment
- Sensitivity within this model and richer ones as well as empirical work will have to show how important this mechanism is

References I

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