Rising Regressivity of the Optimal Capital Tax with the Newborn's Welfare Constraint

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Abstract

In this paper, we provide a three-period model with parent's heterogeneous skills and a welfare constraint for the newborn. Our study is a numerical analysis which shows how the optimal tax system is affected by the planner's weight on the newborn. There are two main findings. One is that a higher guaranteed level of the newborn's welfare makes the optimal capital income tax rate more regressive. The other is that when the Frisch elasticity of labor supply is large, a high planner's weight on the newborns leads to large reduction of the social welfare.