The Tax Elasticity of Capital Gains: Evidence from Millions of Housing Sales

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This paper: new evidence on housing CGTs

- Capital gains taxes induce substantial lock-in effects
  - Housing CGT papers usually lack detailed data on individual sales
  - Recent exception: D'Lima (2020) finds strategic timing at one-year mark in ZTRAX

- Exploit several discontinuities in France's tax code
  1. Anniversary dates: tax rate declines stepwise with holding period after year 5

     $\rightarrow$ Strategic timing, rather than liquidity effect
  2. Reform raising the CGT rate more for longer holding periods

     $\rightarrow$ Reduces the liquidity of older properties

- Headline number (DDD): 1 p.p. change in $\tau \implies$ 1%$\downarrow$ in sales volume
  - In long holding period $\times$ non-owner-occupied home cells

Comment #1: what new info comes from the CGT?

- **Housing taxation literature is quickly becoming saturated**
- Many different flavors emphasized elsewhere...
  - Foreign buyer taxes in Canada, HK, SG, Australia, among others
  - Housing affordability and speculation → targeted taxes (e.g. vacancies)
  - Transfer taxes can have muted effects on prices → "liquidity crunch"
- What is the niche for this paper?
  - Holding period thresholds? → No, transfer taxes have these too!
  - Lock-in effects? → No, documented in both CGT and transfer tax regimes
  - **Unique feature here: old vs. new properties**

Housing CGTs vs. transfer taxes

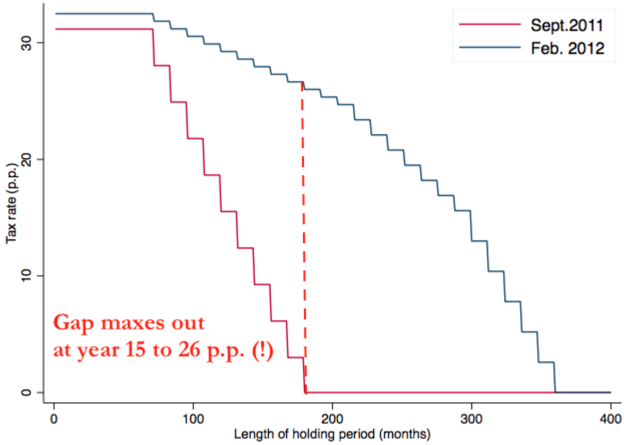
- Each type of tax hits a different market segment
  - Transfer taxes are *ad valorem* $\Longrightarrow$ discourages low cap gain sales
  - CGTs discourage high cap gain sales

- **Bottom line: France CGT reform is unique along two dimensions**
  1. It does not target short-term flips
  2. Lock-in effects large here: tax hike targets properties which have depreciated

- Overall quality of for-sale housing inventory may have improved!
  - Owners of older properties discouraged from realizing the cap gain
  - May decide to keep the property + renovate

CGT rate gap highest for older properties

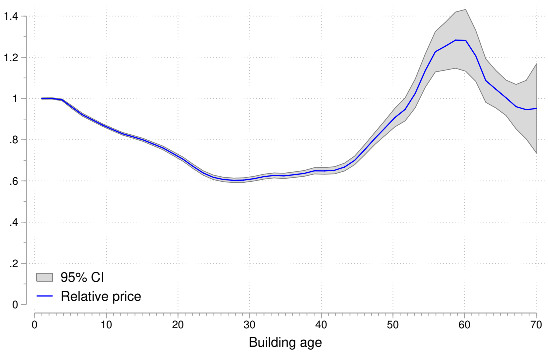
(a) Tax rates by holding period, pre and post-reform



- Long holding period $\implies$ the property is older (mechanical)
- What was the rationale behind this "hump-shape"?
  - Poorly targeted tax if goal is to improve overall affordability
  - Revenue considerations? Cap gain mechanically higher if held for longer

Homes in highly treated group are mostly depreciated

Example: SFHs in Tokyo metro area



Notes: Smoothed mean price relative to a brand new (age = 1) property. Includes all SFHs in the Greater Tokyo metro area. Excluding renovated properties.

- More depreciation in less historically significant locations (identification?)
- Renovations are a normal good, more likely to occur starting around age 15 (esp. in major U.S. metros)
- Depreciation rate slows after age 5 (includes treated group)
- More difficult to offload these properties than newer homes $\Longrightarrow$ lock-in effect will be stronger here

Comment #2: other outcomes besides volume

- Analysis appears a bit incomplete
  - Prices, age vs. holding period, and seller/buyer matches?
  - Sorting? Substitution towards low price momentum areas?
  - Detailed notary records exist for Paris (cf. Cvijanović & Spaenjers 2020)
- **Pricing effects important if want to say anything about redistribution**
  - Theoretically, prices can go up or down (buyer-seller bargaining)
  - Here evidence points to $P \downarrow$: $\Delta \log Q \approx -0.01$, but $\Delta \log(P \cdot Q) \approx -0.013$
- Second homes (taxable) vs. owner-occupied (non-taxable)
  - Mixing the two in the "control" group yields conservative estimates
  - Distinguish using a notion of "permanent address" for paying the tax

Conclusion

- Paper offers convincing evidence of large lock-in effects of housing CGT taxes
- **My take: housing tax literature has a high bar these days**
  - Lock-in, demand, anticipatory effects already documented
  - Contrast CGT with transfer tax along the high vs. low appreciation margin
- Strange nature of this tax helps us say when lock-in effects are likely to be big
  - Equity-efficiency tradeoffs
  - Targeting (implicitly) based on age of the housing stock may be problematic