Caren Sureth (2002)

Partially Irreversible Investment Decisions and Taxation under Uncertainty: A Real Option Approach

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Abstract:

The paper applies contingent claims analysis in a real option investment model in order to investigate taxation's influence on investor's decisions under uncertainty. The results show the distortion from realistic-type tax systems, allow to identify a tax-induced paradox in option valuation for specific settings and acknowledge the property of investment neutrality of well-known `ideal' tax systems in the context of different degrees of irreversibility. Furthermore, it is clarified that the idea of risk-neutral valuation cannot be adopted by the real option approach in general.