The Effect of Public Disclosure on Politicians’ Outside Earnings: Evidence from Tax Return Data∗

Carina Neisser1,2,3 and Nils Wehrhöfer1

1University of Mannheim
2ZEW Mannheim
3IZA Bonn

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Preliminary Draft! Since this paper relies on very sensitive data, we are not allowed to publish a working paper at the moment.

Abstract

In Germany, politicians are legally permitted to carry out outside activities in addition to their political mandate. However, those members of parliament (MPs) with high outside earnings are discussed controversially. On the one hand, there is a trade off between time spent on parliamentary and outside activities and a potential conflict of interests, but on the other hand high outside earnings can be interpreted as a signal for competence. According to Djankov et. al (2010), 109 countries have some form of disclosure law for MPs. They provide suggestive evidence that public and not necessarily confidential disclosure is associated with better government and perceived lower corruption. Up to now, there is no causal evidence on the effect of public disclosure rules for politicians in a western democracy. This is because of two reasons: The lack of pre-reform (high quality) data and credible identifying variation.

We overcome these two challenges and evaluate two public disclosure laws for German federal MPs that differ in the intensity of transparency. In Germany, members of parliaments’ (MPs) outside activities and corresponding earnings were not observable to voters up to 2007. Starting in July 2007, German federal MPs were forced by law to publish these information in a bracket system top-coded at 7,000€. In 2012/2013 these law was tightened and more brackets were added. Since then outside earnings up to 250,000€are observable. This allows a voter to differentiate between a moderate and a high earning politician.

We exploit these changes in order to identify the causal effects of public disclosure rules on politician’s outside earnings using administrative tax return data. It allows us to observe pre-reform income as well as using unaffected state MP’s as a control group. Our results indicate that the top-censored nature of the reporting scheme have the unintended consequence of raising outside earnings. Stricter laws or more specifically a higher degree of transparency lead to lower outside earnings.

∗Contact: C. Neisser (carina.neisser@zew.de), N. Wehrhöfer (nils.wehrhoefer@gess.uni-mannheim.de). We gratefully acknowledge financial support by MannheimTaxation (MaTax) Science Campus. We thank Max Löffler, Andreas Peichl, Sebastian Sieglisch, Holger Stichnoth and participants at PF Seminar (U Mannheim), ZEW Public Finance 2019, ZEW PE-Workshop 2019 for their helpful comments. Akin Mert and Jakob Schmidhäuser provided excellent research assistance and to the Research Data Lab of the German Federal Statistical Agency, especially Ulrike Gerber, Melanie Scheller, Stefanie Setzer and Stefanie Uhrich for steady support in accessing the data.
In addition, we create a second dataset that consists of the reported outside earnings and activities itself\(^1\). We add demographic characteristics, electoral variables as well as voting statistics to uncover potential mechanism that explain our findings. We provide suggestive evidence that electoral accountability is one of the main explanations.

\(^1\)These two datasets need to be analyzed separately because of data security reasons.