Inside the revolving door: Campaign finance, lobbying meetings and public contracts. An investigation for Argentina

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Motivation I - Little money

Tullock's puzzle: Why is there so little money in US politics?

In 1972, total campaign spending in federal elections was about $200 million and total federal spending was $400 bilion. In 2000, total campaign spending was around $3 billion while total federal government spending was around $2 trillion. The Federal government awarded $134 billion in defense contracts in 2000 while defense contracting firms and indviduals associated with those firms donated only around $13.2 million. In sum, value of policy much larger than campaign contributions.

What about Argentina?

In 2007, the national government awarded $886 million in all public contracts whereas the total amount of campaign contributions *by all firms and individuals* were $15 million. The figures for 2013 were $1.62 billion and $18 milion, respectively

Motivation II - Informal connections

- How do IGs influence politics and policies in Argentina?

Figure: The day McDonalds Argentina ran out of ketchup

- Delays in DJAI; problem was solved within a day or two when the then chief of cabinet took notice of the situation.

Channels of influence

"In Argentina there are two ways to exert influence: one, more traditional, through formal meetings and opinion leaders, and another, directly related to electoral campaigns and the amount of *under-the-table* contributions in exchange of future favors" [Unnamed lobbist source. Link: La Nacion]

Motivation III - Policy relevance

Changes in political finance regime

There were three major reforms to the regime of political finance in Argentina in the last 15 years: the first was aimed at formalizing the mixed system of political finance (2002); the second sought to increase transparency and accountability (2007) and the third prohibited contributions from firms and other legal persons (2009). Little to no evidence as to how these changes impact on several outcomes.

Regulation of lobby activity

There is currently a draft for a project bill regulating the activity of interest groups. It is familiarly known as the project of "Ley de Lobby" although the official project merely extends on the current practice of recording hearings of interests.

Related literature

- Long-standing literature on campaign contributions and roll-call voting [Green and Krasno (1988), Palda and Palda (1998), Ansolabehere et al (2003), Stratmann (2005)]
- Electoral competition with special interest groups $\longrightarrow$ Baron (1994), Grossman & Helpman (1992, 1996, 2001)
- Beyond campaign finance $\longrightarrow$ political connections and the revolving door [Vidal, Draca & Fons-Rosen (2012), Acemoglu et al (2016)]
- Timing of political influence $\longrightarrow$ You (2014) states that around 50% of lobbying activity in the US takes the form ex-post lobbying –i.e after Congressional vote.
  - Our focus is on executive rather than legislative lobbying –extensive evidence that roll-call voting in Argentina is highly partisan [Jones (2001), Jones, Wang and Micozzi (2009)].

What we do

- Build a theoretical model where IGs decide on the optimal allocation between ex-ante and ex-post contributions aiming to obtain the highest share of public contracts awarded by the government
- Test (partially) some of the theoretical implications regarding the size and direction of effects and the relationships between both channels of influence
- Test for a given tender process whether competition in lobbying and contributions increases the probability of getting a contract (to do list)

Set up: general features and (non)strategic players

- Election game between two candidates, $k = A, B$.
- A wins the election with probability P; B with $1 - P$.
- **Candidates:** differ in their campaign promises on a total expenditure $V^k > 0$ on public contracts, if they take office.
- **Voters:** a priori, they are indifferent between both candidates, but they can be influenced by information revealed during the campaign.
- **Interest groups (IGs):** compete with each other for the highest share of $V^k > 0$ of the winning candidate.

  To this end, each IG can make monetary contributions:

  - *before* the election: **campaign contributions,** $C_i \geq 0$.
  - *after* the election: **lobbying contributions,** $L_i \geq 0$.

Set up: contributions

- Through **campaign contributions**, the IGs try to induce voters in favor of their favorite candidate.

  To model this: consider two IGs, $i = 1, 2$, and an endogenous joint probability $P(C_1, C_2)$ such that:

  $\Rightarrow$ If the IGs have **aligned-preferences:**

  $\frac{\partial P(\cdot)}{\partial C_i} > 0$, $\frac{\partial^2 P(\cdot)}{\partial C_i^2} < 0$, $i = 1, 2$, if A is preferred over B, or
  $\frac{\partial P(\cdot)}{\partial C_i} < 0$, $\frac{\partial^2 P(\cdot)}{\partial C_i^2} > 0$, the other way around.

  $\Rightarrow$ If the IGs have **opposite-preferences**:

  $\frac{\partial P(\cdot)}{\partial C_i} > 0$, $\frac{\partial P(\cdot)}{\partial C_j} < 0$, $\frac{\partial^2 P(\cdot)}{\partial C_i^2} < 0$, $\frac{\partial^2 P(\cdot)}{\partial C_j^2} > 0$ for $i \neq j$, if i supports A, while j supports B.

Set up: contributions (cont)

- Through both **campaign and lobbying contributions**, the IGs compete with each other for the highest share of V^k.

  To model this: the share that i gets from its contributions to the (wining) candidate k:

$$\alpha^k = \frac{\text{i's total contributions to candidate k}}{\text{total contributions to candidate k}}$$

Example: if A takes office and both IGs have contributed to his campaign: $\alpha^A = \frac{L_i^A + C_i}{L_i^A + L_j^A + C_i + C_j}$. *But, if only i did it:* $\alpha^A = \frac{L_i^A + C_i}{L_i^A + L_j^A + C_i}$.

In this context:

- C_i and C_j can constitute an externality ex-post the election.
- C_i and L_i to a winning candidate are substitutes intertemp.

Set up: timing

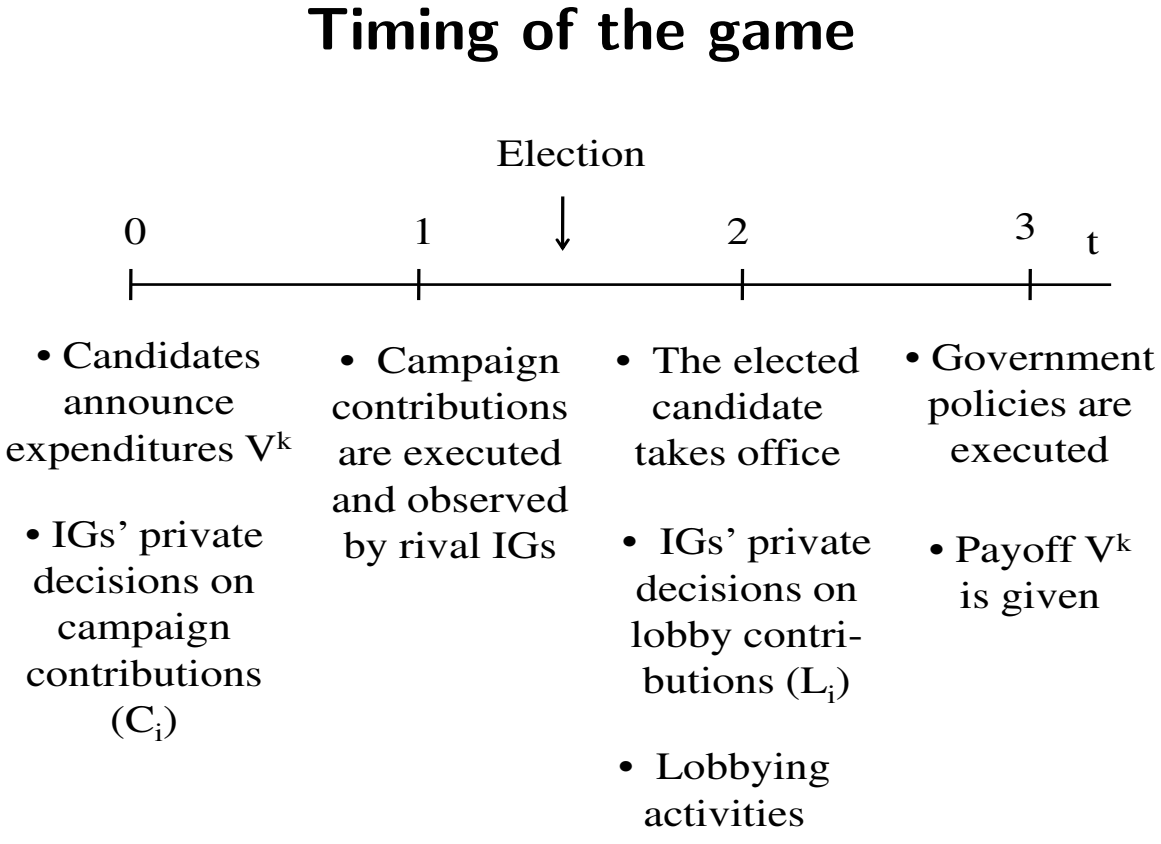


Figure: Time-structure of the model

Set up: the IG's two-periods decision problem

- In this context, the IG i's two-periods problem is:

$$\begin{cases} \max_{C_i} \; U_i^{EA} = P(C_i, C_j)\left(\alpha^A V^A - L_i^A\right) + (1 - P(C_i, C_j))\left(\alpha^B V^B - L_i^B\right) - C_i \\ st : L_i^k \in arg\max_{L_i^k} \; U_i^{EP} = \left[\alpha^A(L_i, L_j|\overline{C}_i, \overline{C}_j)\; V^A - L_i^A\right] I \; + \\ \qquad\qquad \left[\alpha^B(L_i, L_j|\overline{C}_i, \overline{C}_j)\; V^B - L_i^B\right](1 - I) \end{cases}$$

(Where $I = 1$ if candidate A takes office, and $I = 0$ if candidate B does it.)

- Solving procedure:
  - Ex-post problem $\longrightarrow$ how much lobby to exert after the election given a rival IG that also lobbies and given C_i and C_j.
  - Ex-ante problem $\longrightarrow$ how much campaign contribution to make given the ex-post (lobbying) optimal behavior.

The Aligned-preferences game

- The IGs have aligned-preferences for candidate A iff $V^A > V^B$
  $\rightarrow$ Hence, any contribution go to candidate A.
- Assume: $P(C_i, C_j) = 1 - \frac{1}{2}e^{-2(C_i+C_j)}$.

Proposition 1 (Ex-post interior solution)

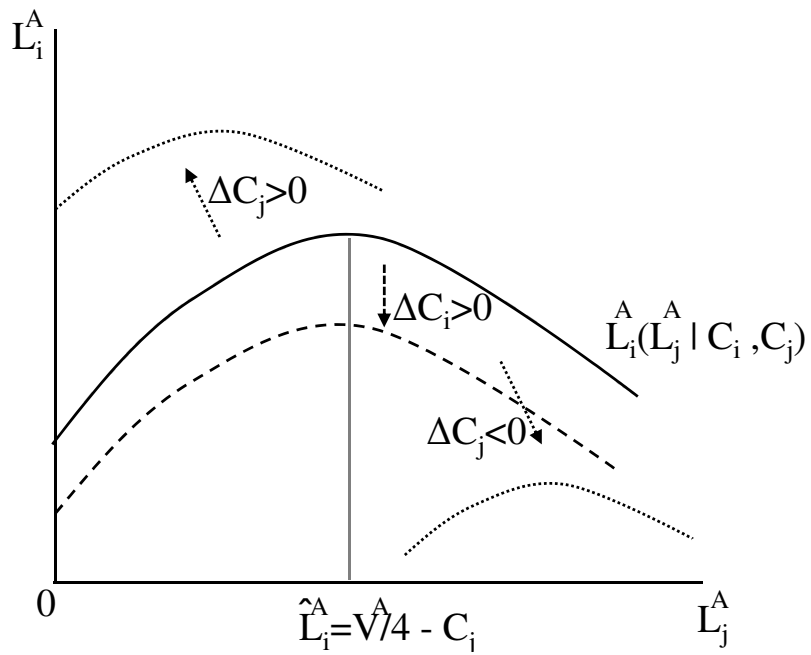
Ex-post lobbying is increasing in the total expenditure V^k, and if the ex-ante supported candidate A:

(i) takes office: ex-ante and ex-post contributions are perfect substitutes: $L_i^A + C_i^A = \frac{1}{4}V^A$, for: $i = 1, 2$.

(ii) does not takes office: $L_i^B = \frac{1}{4}V^B$, for: $i = 1, 2$.

In both cases, competition for V leads to equal shares, $\alpha^A = \alpha^B = \frac{1}{2}$.

(i) Lobbying optimal strategy

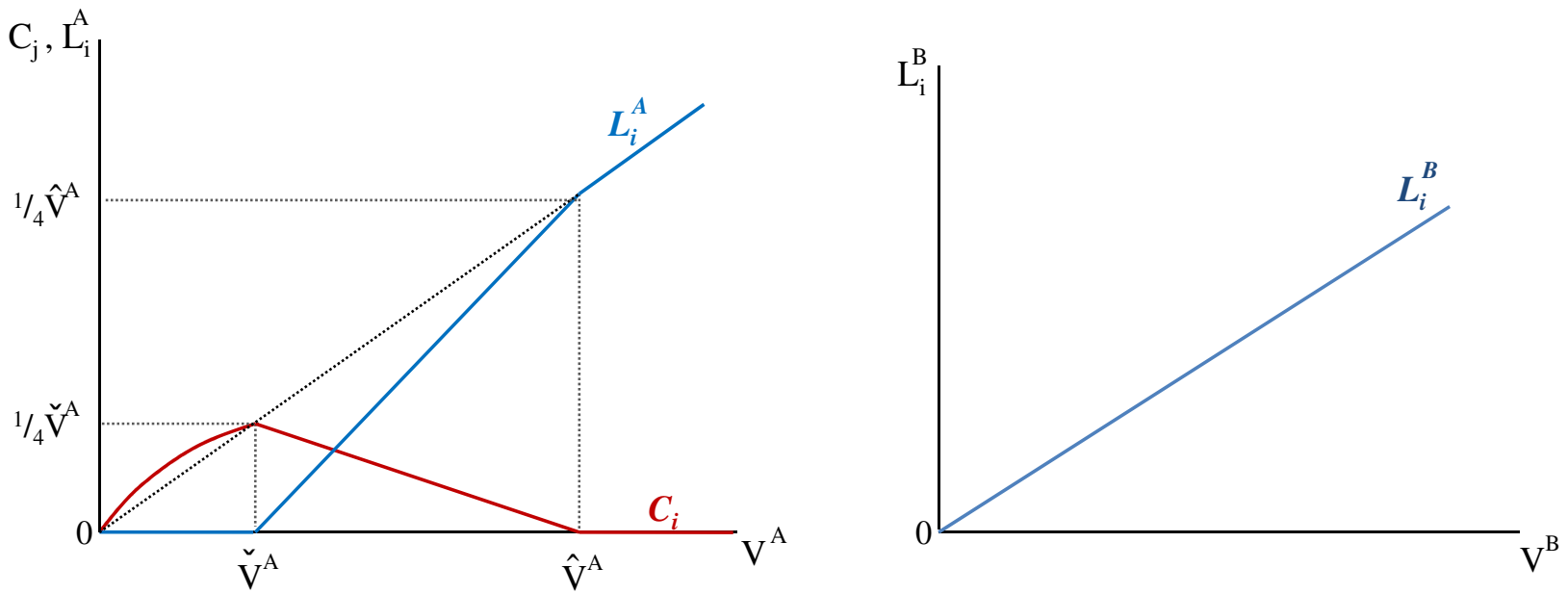


The Aligned-preferences game (cont.)

Proposition 2' (Ex-ante equilibrium when A takes office)

- For low values of V^A: *"to maximize P and not to fight after elections"* is a dominant strategy for both IGs.
- For high values of V^A: *"to fight for V^A after elections at the risk of a lower P"* is a dominant strategy for both IGs.

Optimal contributive behavior



The Aligned-preferences game (cont.)

To remember:

- **Campaign contributions** can be a useful instrument to bias the likelihood of winning for a given candidate.

  (Possible extension: in a game where V^k is endogenous, candidates might find it optimal to coordinate low V^k promises...)

- **Lobbying**, instead, is (almost) a total waste of resources, since competition leads to equal shares of V for both IGs.

- However, as the total expenditure V increases, the IG inevitably fall into a lobbying fight.

- Hence, the IGs may find it optimal to coordinate their strategies –especially, lobbying (e.g., they can improve their results by defining a mechanism by which they commit to reduce lobbying to a minimum).

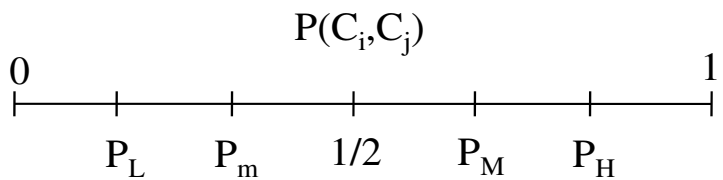
The opposite-preferences game

Considering: $U_i = P\left(\alpha^A V^A - L_i^A\right) + (1-P)\left(\alpha^B \theta_i V^B - L_i^B\right) - C_i$

The IGs have opposite-preferences iff $\theta_i < \frac{V^A}{V^B} < \theta_j$.

- Assuming $\theta_i = 1 < \frac{V^A}{V^B} < \theta_j = \theta \ \rightarrow$ Any contribution of i go to candidate A, and any of j go to that of B.
- Therefore, to increase P, the IG i has to contribute more than its rival. Otherwise, there is an increase in $1 - P$.
- Assume the following joint probability distribution $P(C_i, C_j)$:

	$C_i = 0$	$C_i > 0$
$C_j = 0$	$1/2$	P_H
$C_j > 0$	P_L	P_M $1/2$ P_m



Opposite-preferences vis-á-vis aligned-preferences

Aligned-preferences

I Lobbying is increasing in V^k.

II If the supported candidate (A) takes office, ex-ante and ex-post contributions are perfect substitutes.

III Equal shares of V across IGs and election outcomes: $\alpha^A = \alpha^B = 1/2$.

IV For low V^A: $C_i = C_j > 0 \Rightarrow$ campaign contributions affect P and offset lobbying.

For high V^A: $C_i = C_j = 0$.

In between: point II holds.

Opposite-preferences

I Lobbying is increasing in V^k.

II For the IG whose supported candidate takes office, ex-ante and ex-post contributions are perfect substitutes.

For the rival IG: lobbying is the unique tool to compete ex-post.

III Equal shares of V across IGs if A takes office: $\alpha^A = 1/2$.

Asymmetric shares of V across IGs if B takes office: $\alpha^B < 1/2$.

IV Always: $C_i, C_j > 0 \Rightarrow$ campaign contributions affect P iff $C_i \neq C_j$.

(If high, campaign contributions can offset lobbying.)

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Data: Main databases

- Data compiled from several sources leads to three main datasets all at the individual level of observation for the period 2003-2015
  - Data on campaign contributions $\longrightarrow$ over 46000 individual-level campaign contributions for National elections [Sources: Cámára Nacional Electoral, Poder Ciudadano's Dinero y Política project and la Ruta Electoral project]
  - Data on hearings of interest ("audiencias de interés") $\longrightarrow$ nearly 70000 records of official hearings between members of the executive and individuals representing themselves/an organized interest
    [Source: Registro Nacional de Audiencias de Interés]
  - Data on public procurement contracts $\longrightarrow$ including individual and firms participating in public procurement contracts comprising purchases of goods and services and public works
    [Source: Automatic Scrapping from Boletin Oficial Nacional]

Data: Dictionary databases

- AFIP adminstrative records (padrón de contribuyentes) $\longrightarrow$ over 4.6 million records containing names and IDs (CUIT number) for both natural and legal persons. activity codes for 480000 legal entities

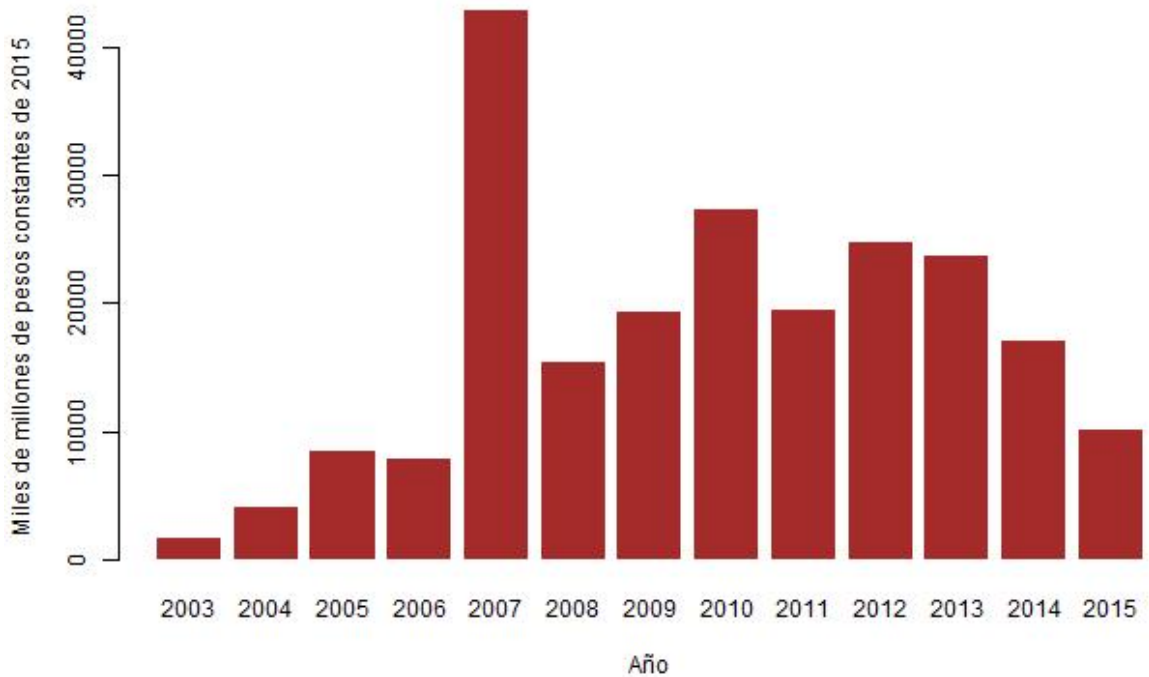
- Registered legal entities and authorities (Inspección General de Justicia) $\longrightarrow$ over 1.2 million records containing CUIT and membership type (partner, director, etc)

Matching IDs

- Common unique identifier in all databases $\longrightarrow$ CUIT number.
  - Many missing data on CUIT –this is mostly a problem for both public contract and hearings of interest data.
  - The original raw data on public contracts available from the Boletín Oficial contained only about 15% of CUIT data –contract was awarded to firm/person "ABC" and if CUIT was missing, no certain way of knowing how "ABC" is!
  - When "cuit" is missing, we followed two procedures:
    - Manual recovery of "cuit" data $\longrightarrow$
    - String-matching (matching based on "name") against our dictionary databases.
    - Exact-string matching
    - Fuzzy-string matching algorithm based on "optimal string alignment" (minimal Levenshtein distance)

Descriptive

Figure: Public tender contracts awarded (up to $1 million 2015 pesos)



Descriptive (cont.)

Table: Distribution of public tender contracts - By firm/person and of contracts awarded

of contracts	firms/persons	%
1 a 5	11409	0.838650397
6 a 20	1552	0.114084093
21 a 50	450	0.033078506
51 a 100	132	0.009703029
more than 100	61	0.004483975
Total	13604	1

Empirical strategy

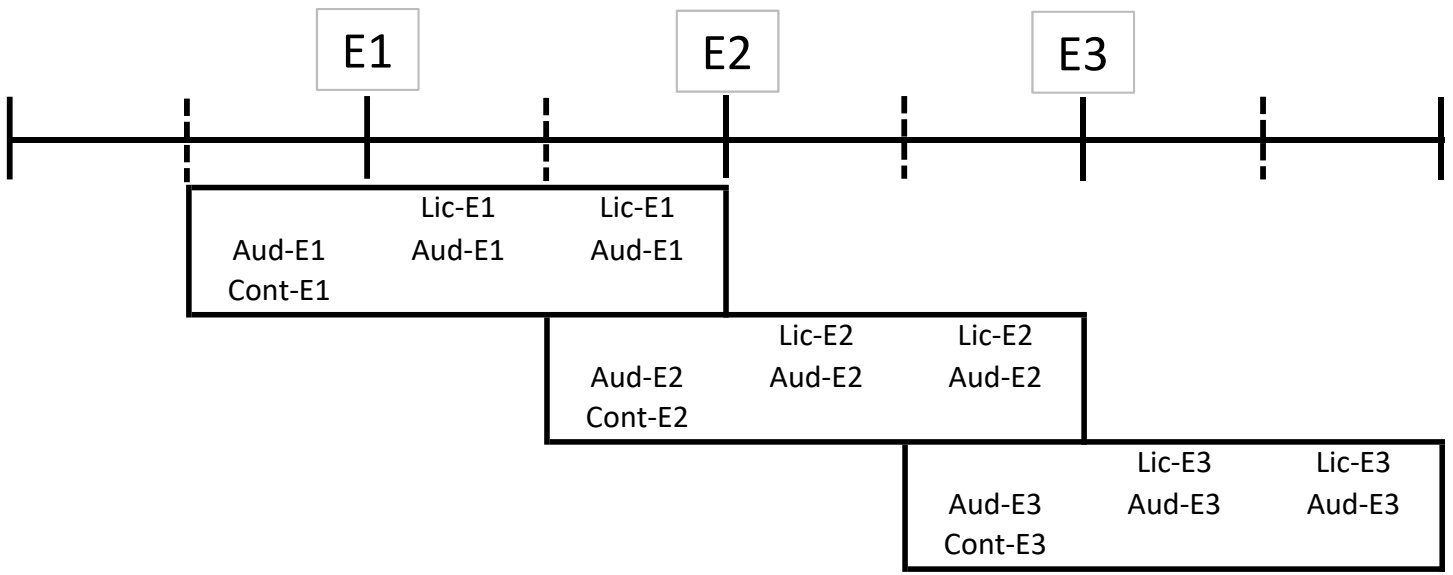
- We are to perform two types of analysis.

$$Y_i = \sum_{h=0}^{H} y_{i,t+h} = \alpha + \beta C_{i,E} + \gamma \sum_{h=0}^{H} \omega_{t+h} L_{i,t+h} + \epsilon_i \qquad (1)$$

- we use only information on actors who obtained a positive amount of public procurement contracts, so that β and γ will reflect just the existence of correlations with the dependent variable; we expect both coefficients to be positive.

Timing and assignment

Figure: Assignment of political influence activities - National elections, public audiences and campaign contributions



Results

Table: Contract amount and probability of winning contract - Pooled

	Pooled OLS				Pooled Probit			
	ln_monto				win			
audiencia	1.65***	1.66***			0.79***	0.79***		
audiencias			0.50***	0.50***			0.43***	0.43***
contributed	0.52***		0.55***		0.24*		0.25*	
incumbent		0.12		0.31		0.71		0.72
others		0.58***		0.58***		0.19		0.19
Obs	47036	47036	47036	47036	50176	50176	50176	50176
R-sq	0.98	0.98	0.98	0.98				

*** $p < 0.01$, ** $p < 0.05$, $*p < 0.1$

Results (cont.)

Table: Contract amount and probability of winning contract - RE

	Random effects				Probit random effects			
	ln_monto				win			
audiencia	0.47***	0.47***			0.88***	0.88***		
audiencias			0.21***	0.21***			0.42***	0.41***
contributed	-0.14		-0.14		0.19		0.19	
incumbent		-0.35		-0.32		0.93		0.95
others		-0.1182		-0.12		0.1124		0.1072
Observations	40839	40839	40839	40839	43842	43842	43842	43842
Number of $id_c uit$	5711	5711	5711	5711	6142	6142	6142	6142

*** $p < 0.01$, ** $p < 0.05$, $*p < 0.1$

Conclusions

- Political influence game where IG decide on two types of influence, campaign contributions and lobbying contributions where both are subsitutes intertemporally
- Preliminary evidence shows that lobbying (both having had and the number of audiences) prior to the award of contracts are associated with greater amounts of contracts and greater probability of getting contracts.
- Campaing contributions seem to also be correlated albeit only in the pooled models; in fact when separating between incumbents and challengers, contributions seem to be relevant only for challengers! [incumbents likely rely on other channels]