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Choosing the Wrong Box?
Behavioral Frictions and Limits of Tax Advice in Tax Regime Choice

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Abstract: We examine behavioral frictions in entrepreneurs' tax planning when choosing between corporate and partnership taxation under a check-the-box rule. Using German tax return data, we show that only a small fraction of entrepreneurs opt for corporate taxation, despite substantial potential tax savings. A pre-registered incentivized online experiment demonstrates that complexity aversion, status quo bias, and misperception about the corporate tax burden—arising from the interaction of corporate and deferred dividend taxation—help explain the preference for partnership taxation. We further find that these behavioral frictions heighten liquidity risk under the corporate system, particularly in the face of unexpected cash flow needs. Finally, a survey of German tax advisors indicates that tax advice only partially mitigates these frictions. Some advisors misperceive the benefits of corporate taxation, while others anticipate client biases and therefore refrain from recommending the corporate tax system.

Keywords: Check-the-box, Legal Form, Tax Complexity, Tax Misperception, Behavioral Taxation, Tax Advice

JEL Codes: H25 – D91 – D22

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[4] Anonymized preregistration links: https://osf.io/7ryuq/?view_only=7b405bcef4d54c62b563db17d9412bb9 and https://osf.io/mxtsg/?view_only=b7e467fe4f9046d0864dfbe971eda228

1 Introduction

This study examines how behavioral frictions affect entrepreneurs' tax planning under a check-the-box choice between corporate and partnership taxation. To avoid tax distortions in legal form decisions, countries such as France, Germany, and the United States allow partnerships or their partners to elect corporate taxation without changing their legal form (so-called check-the-box rules). Standard tax planning theory (e.g., Scholes et al. 2014) predicts that entrepreneurs will choose the corporate system if it yields a higher after-tax return on investment. However, based on German tax return panel data from 2008 to 2018, only 5.6% of 63,190 entrepreneurs who would benefit from corporate taxation (i.e., are taxed at the top income tax rate) actually choose it (see online Appendix A). Since the rule's introduction in 2008, only about 6,200 entrepreneurs per year have used the option—far below the legislature's expectation of 90,000 annual elections (Federal Council 2007, p. 62). Our conservative back-of-the-envelope calculation suggests that entrepreneurs collectively forgo tax benefits with a present value of at least €381 million per year. This raises a critical question: why do so many entrepreneurs forgo substantial tax savings by choosing partnership taxation?

To investigate this question, we conduct a pre-registered incentivized online experiment with 1,151 participants from Germany. This experiment allows us to examine preferences for partnership versus corporate taxation under controlled conditions. We test four potential behavioral frictions that may explain why entrepreneurs avoid the corporate tax system: (i) complexity aversion and complexity-induced tax misperception, (ii) the disutility of split tax payments, (iii) the use of the partnership tax system as a commitment device against liquidity risk, and (iv) status quo bias.

Our experiment provides causal evidence that the corporate tax system is perceived as more

complex than the partnership system. Since individuals tend to be complexity averse (e.g., Zilker et al. 2020; Umar 2022), this perception increases the attraction of partnership taxation. Specifically, we find that both *corporate tax rate complexity* and *corporate tax time complexity* increase participants' preference for the partnership system. *Corporate tax rate complexity* refers to the need to calculate a combined burden from corporate income and dividend taxes while considering their interdependence—since a corporate tax reduces the base for dividend taxation. *Corporate tax time complexity* arises because dividend taxation is deferred until profit distribution, while partnership profits are taxed immediately. We also find that corporate tax complexity leads to a misperception of the overall tax burden, which in turn affects tax preferences. When confronted with *corporate tax rate complexity*, individuals often overestimate the tax burden by applying simple heuristics—such as summing corporate and dividend tax rates without accounting for their interdependence. These kinds of mistakes reinforce the preference for partnership taxation. In contrast, *corporate tax time complexity* causes individuals to neglect the deferral of dividend taxation, thus underestimating the true tax burden and reducing their preference for partnership taxation.

Based on prospect theory (Kahneman and Tversky 1979) and the concept of hedonic editing (Thaler 1985), we hypothesize that entrepreneurs may perceive two separate tax payments under the corporate tax system (corporate and dividend tax) as more painful than a single tax payment under the partnership system—even with the same total tax burden. This framing effect should reduce the preference for the corporate tax system. However, our experimental results do not support this hypothesis. The split structure of tax payments under the corporate system does not significantly affect the choice between corporate and partnership taxation.

Entrepreneurs often rely on business liquidity to finance personal consumption. If they fail to fully account for future dividend taxes, this can lead to lower earnings retention under the corporate

system, resulting in higher liquidity costs in the event of an unexpected private cash flow need (liquidity shock). If entrepreneurs are aware of this behavioral bias, opting for partnership taxation can, in theory, serve as a commitment device to reduce such risks. Our experimental results confirm that both the likelihood and size of liquidity costs rise under corporate taxation; however, these risks do not significantly influence tax system choice.

We also find strong evidence that experience with the partnership tax system significantly increases the likelihood of sticking with it—even when switching to the corporate tax system would be economically beneficial. In the experiment, the likelihood of choosing the partnership system rises by 20 percentage points when participants have experience with only that system, compared to those who previously encountered both systems. This behavior is consistent with *status quo bias*, the tendency to prefer familiar options and avoid change, even when an alternative may offer equal or greater benefits (e.g., Samuelson and Zeckhauser 1988).

In sum, our experiment shows that behavioral frictions can significantly affect tax decisions when choosing between corporate and partnership taxation under a check-the-box rule.

Since entrepreneurs typically rely on professional tax advice, one might expect advisors to correct their biases. To test this assumption, we surveyed 292 certified German tax advisors. The firms represented in the sample report median annual revenues between €0.75 million and €1.5 million and employ a median of 18 staff members. The surveyed tax advisors primarily advise small and medium-sized enterprises (SMEs), which are the main target group of the German check-the-box rule (section 34a of the German income tax code). More than half of the advisors have already recommended opting for the corporate tax system to a client at least once.

We presented the advisors with a hypothetical scenario in which a client considers electing corporate taxation under the check-the-box rule. The scenario clearly favored the corporate tax

system financially, making a recommendation in its favor the expected response. However, only 49.3% of advisors recommended it. Among those who did not, 42.9% gave responses reflecting a misperception of the corporate tax benefit, suggesting that many advisors fail to recognize its economic advantage. This is surprising, given the qualifications of German tax advisors.[2] Some explained they refrained from recommending corporate taxation because they anticipated clients' behavioral biases, especially the tendency to underestimate or forget future dividend taxation, potentially causing the liquidity shortfalls also observed in our experiment. As one advisor noted: "It should be borne in mind that clients are happy to take the immediate advantages but forget the future disadvantages (dividend taxation), and nasty surprises are then inevitable." This suggests that advisors consider client biases and, to preserve relationships, avoid strategies that might backfire under biased decision-making. Finally, several advisors cited the rule's complexity and associated compliance costs. In sum, these findings suggest that many tax advisors fail to debias their clients, as they are constrained by either their own misperceptions or their expectations of client behavior.

This study makes the following contributions. First, it contributes to the literature on the effect of taxes on the choice of legal form (e.g., Guenther 1992; Ayers et al. 1996; Mackie-Mason and Gordon 1997; Omer et al. 2000; Hodder et al. 2003; Goolsbee 2004; Elschner 2013; Utke 2019). While research emphasizes that differences in after-tax income drive legal form decisions, our findings show that tax misperception, complexity aversion, and status quo bias also shape the choice of corporate versus partnership taxation.

Second, despite the economic relevance of partnerships, tax research has focused on corporate tax planning by large firms, while tax planning among SMEs-—especially partnerships-—remains

[2]German tax advisors must hold a relevant university degree (typically eight semesters plus two years of practical experience; three years if less than eight semesters) or equivalent vocational training with substantial experience (six to eight years) in income and corporate tax matters (Blaufus et al. 2017).

understudied (Hess et al. 2024). We address this gap by examining entrepreneurs operating sole proprietorships or partnerships, thereby complementing research on corporate tax planning (Hanlon and Heitzman 2010). We also contribute to the growing literature on bounded rationality in tax planning (Graham et al. 2017; Hanlon et al. 2022; Blaufus et al. 2022a). To our knowledge, this is the first study to demonstrate the impact of behavioral frictions on the choice between partnership and corporate taxation. These frictions can significantly undermine tax policy goals. For example, the German check-the-box rule aimed to eliminate tax distortions in legal form choice. We show that it did not achieve this—and that aligning effective tax rates alone does not ensure tax neutrality.

Third, we contribute to research on the effects of tax complexity on decision-making (Zwick 2021; Armstrong and Glaeser 2023; Amberger et al. 2024; Euler et al. 2024; Giese et al. 2024). We show that corporate tax complexity prevents many taxpayers from choosing the optimal tax system. Like Zwick (2021), we focus on complexity-induced behavioral frictions in tax planning. However, using an experiment, we provide causal evidence that specific components of tax complexity drive misperception and complexity aversion. While we confirm Zwick's finding that tax advisors vary widely in sophistication—and thus so does their advice—our survey reveals an additional mechanism: they anticipate clients' behavioral biases and refrain from recommending the financially superior tax choice because of concerns about these biases.

2 Theoretical Background and Hypothesis Development

2.1 Corporate Tax Benefit

To examine the determinants of the choice between the partnership and the corporate tax system, we start with a simple rational choice model. An entrepreneur can choose at $t = 0$ whether the

pre-tax profit is taxed in the following T periods as a partnership (the pass-through principle) or as a corporation (double taxation). In the case of partnership taxation, all profits—regardless of whether they are retained or distributed—are attributed to the entrepreneur and taxed at the income tax rate t_p. In contrast, under the corporate tax system (retained) profits are taxed at t_c and additionally taxed at t_d when distributed to the entrepreneur. By retaining (parts of) the profit, the entrepreneur can defer the payment of the dividend tax. If $t_p > t_c$, the tax deferral can result in a tax benefit that depends on the firm's return on equity r (i.e., interest on retained earnings) and the investment period T. If the pre-tax profit P is retained and invested at a rate of return r, the future value after T years under the partnership tax system is given by:

$$FV_p = P(1 - t_p)[1 + r(1 - t_p)]^T. \tag{1}$$

In the case of corporate taxation, the following future value results in $t = T$:

$$FV_c = P(1 - t_c)[1 + r(1 - t_c)]^T(1 - t_d). \tag{2}$$

An entrepreneur will choose the corporate tax system if $FV_c > FV_p$. The advantage of opting for the corporate tax system as a German entrepreneur can be illustrated with a simple example, which we also used in our survey of tax advisors (see Section 5): *Suppose a sole proprietor with unlimited tax liability earns annual profits of around €500,000 with only minor fluctuations. He plans to retain all profits over the next five years to invest in expansion, expecting a 6% annual return (before taxes). In addition, he has rental income of about €300,000 per year.*

In this example, the corporate tax benefit amounts to €16,434 (in present value terms: €13,971). More generally, when applying the top tax rates for German partnership and corporate taxation,[3]

[3] As in many countries, Germany's corporate tax rate is a combination of federal and local taxes. Our calculations follow Section 34a of the German Income Tax Code, which prescribes a nominal corporate tax rate of 29.8%, including the solidarity surcharge (for periods from 2008 to 2023). However, since part of the retained earnings must be withdrawn to pay taxes, the effective corporate tax rate on retained earnings increases to $t_c = 36.20\%$. We assume a

we always obtain a positive corporate tax benefit (defined as $FV_c - FV_p$) if the annual pre-tax rate of return exceeds 1.45%—assuming, for example, an investment period of six years.[4]

In sum, for entrepreneurs subject to the top marginal income tax rate who intend to retain their profits opting for corporate taxation typically results in significant benefits. However, as outlined in the introduction, most entrepreneurs in Germany refrain from choosing corporate taxation under the check-the-box rule, thereby forgoing substantial tax savings (see online Appendix A.3.1). To better understand this discrepancy, we analyze potential behavioral frictions that may influence the choice between partnership and corporate taxation.

2.2 Corporate Tax Rate Complexity

Research increasingly shows that individuals are boundedly rational (Simon 1959). Blaufus et al. (2022a) summarize this research and propose a *Behavioral Taxpayer Response Model*, which suggests that subjective perceptions of the tax burden drive tax decisions. In the tax context, bounded rationality can produce decisions that deviate from the optimal choice on account of the characteristics of the tax information, the decision environment, and decision-maker traits.

Tax complexity and timing are key factors shaping the perception of the tax burden. Research shows that tax complexity affects the correct use of marginal tax rates, the accuracy of effective tax rate forecasts by managers and analysts, and the likelihood of erroneous investment decisions (Rupert and Wright 1998; Rupert et al. 2003; Boylan and Frischmann 2006; Bratten et al. 2017; Graham et al. 2017; Heinemann-Heile et al. 2025). We expect tax complexity to also influence the

dividend tax rate of $t_d = 18.51\%$, reflecting a reduced effective rate due to a statutory tax base adjustment (the nominal rate is 26.38%). The top personal income tax rate, including the solidarity surcharge, is $t_p = 47.5\%$. When earnings are distributed, the effective corporate tax burden becomes $t_c + t_d(1 - t_c) = 48.01\%$, which exceeds the top personal income tax rate. Thus, a corporate tax benefit only arises if profits are retained and reinvested.

[4]Six years correspond to the lower bound of entrepreneurs' investment periods based on tax return data; see Online Appendix A.3.1.

use of the check-the-box rule, as calculating the effective tax rate for corporations is harder than for partnerships. Unlike the partnership tax rate, the corporate rate combines income and dividend taxes. The corporate rate applies to pre-tax profits, while the dividend tax is levied on after-tax profits, i.e. $t_{corp} = t_c + t_d(1 - t_c)$. Thus, differing tax bases preclude simply adding both rates.

To reduce their cognitive effort when making complex decisions, individuals apply two approaches. First, many use simple heuristics (Tversky and Kahneman 1974). When calculating the corporate tax burden, they may thus neglect the different tax bases and simply add the nominal dividend and corporate income tax rates. This would lead to an overestimation of the corporate tax burden, which in turn would reduce the probability of opting for corporate taxation.

Second, entrepreneurs may avoid the more complex option altogether and choose the partnership tax system to reduce cognitive effort. Research provides evidence for complexity aversion. Differences in option complexity affect the choice between risky and safe options (Zilker et al. 2020) and between different savings plans (Sonsino and Mandelbaum 2001), and differences in the complexity of news titles affect how investors allocate their attention across news (Umar 2022).

Both lines of reasoning suggest that corporate tax rate complexity reduces the attractiveness of the corporate tax system. The first effect is indirect: tax rate complexity increases the probability of overestimating the corporate tax burden and thus decreases the likelihood of choosing to pay the corporate tax. The second effect is direct: entrepreneurs avoid complexity and thus the more complex corporate tax system. Thus, we formulate our first set of hypotheses as follows:

Hypothesis 1a *Corporate tax rate complexity has an indirect positive effect on choosing the partnership tax system, mediated by overestimating the corporate tax burden.*

Hypothesis 1b *Corporate tax rate complexity has a direct positive effect on choosing the partnership tax system.*

2.3 Corporate Tax Time Complexity

According to the *Behavioral Taxpayer Response Model*, the timing of taxation is another important characteristic of the tax system that affects the perception of the subjective tax burden and thus affects taxpayer behavior, for example, withholding decisions (Bobek et al. 2007), spending (Chambers and Spencer 2008), risk-taking (Falsetta and Tuttle 2011; Falsetta et al. 2013), and savings (Blaufus et al. 2025).

The partnership and corporate tax systems also differ in tax timing. Under the corporate system, entrepreneurs can defer dividend tax payments by retaining profits, while, in partnerships, taxes are due immediately when profits are earned, regardless of retention. We refer to this difference as *tax time complexity*, which can lead to a misperception of the corporate tax burden and influence the choice of system. Research shows that individuals often ignore or underweight deferred taxes due to myopia, confirmation bias, or anchoring to pre-tax wealth, leading to suboptimal saving, production, and risk allocation (Blaufus and Milde 2021; Stinson et al. 2021; Cuccia et al. 2022; Blaufus et al. 2022b). If entrepreneurs underestimate or ignore deferred dividend taxes, they will underestimate the corporate tax burden and thus be more likely to opt for the corporate tax system.

However, the tax deferral also increases the complexity of the corporate tax system. Blaufus and Milde (2021) show that deferred taxation is perceived as significantly more complex than economically equivalent immediate taxation. Thus, if entrepreneurs aim at avoiding this *tax time complexity*, they may prefer partnership taxation.

In sum, there are two opposing effects. On the one hand, increased tax time complexity (switching from immediate to deferred dividend taxation) increases the probability of underestimating the corporate tax burden and reduces the probability of choosing partnership taxation (indirect negative

effect). On the other, if entrepreneurs are complexity-averse, it may directly increase the likelihood of choosing partnership taxation. The total effect depends on which mechanism dominates. We state the next set of hypotheses accordingly:

Hypothesis 2b *Corporate tax time complexity has an indirect negative effect on choosing the partnership tax system, mediated by underestimating the corporate tax burden.*

Hypothesis 2b *Corporate tax time complexity has a positive direct effect on choosing the partnership tax system.*

Hypothesis 2b *There is an ambiguous total effect of corporate tax time complexity on choosing the partnership tax system.*

2.4 Disutility of Split Tax Payments in the Corporate Tax System

According to prospect theory, entrepreneurs evaluate profits and losses asymmetrically (Kahneman and Tversky 1979). In the loss domain, the value function is convex, implying diminishing sensitivity: two separate losses reduce utility more than a single loss of the same total magnitude. Based on this principle, Thaler (1985) proposes a hedonic editing framework, in which individuals mentally organize multiple outcomes to maximize perceived utility—for example, by integrating two losses into a single one to reduce the overall psychological impact.

Applied to our context of choosing between partnership and corporate taxation, this suggests that making two separate payments under the corporate system (corporate tax and dividend tax) leads to a greater perceived loss than paying the same total amount once, as in the partnership system. All else equal, this should increase the preference for the partnership system.

Hypothesis 3 *The presence of two separate tax payments under the corporate tax system increases the likelihood of choosing the partnership tax system.*

2.5 Partnership Taxation as a Commitment Device against Liquidity Risk

For entrepreneurs with small and medium-sized companies, their business typically serves as the primary source of financing for personal consumption. Thus, they act both as producers making investment decisions for their business and as households making consumption decisions aimed at maximizing lifetime utility (e.g., Chen et al. 2010). To optimize consumption allocation, they must manage business liquidity so that the marginal utility in period t equals the discounted expected marginal utility in period $t + 1$ (e.g., Browning and Lusardi 1996).

However, managing liquidity over the business life cycle is more complex under a corporate tax system, due to its high tax time complexity (see Section 2.3). Entrepreneurs must anticipate the additional dividend tax on future withdrawals, necessitating higher retained earnings than under partnership taxation. Research shows that they often fail to increase their retained earnings enough to fully offset this additional burden (Blaufus and Milde 2021). Compounding this issue, they face a higher risk of liquidity constraints in the event of unexpected consumption needs—such as divorce or caregiving responsibilities. For example, suppose an entrepreneur retains €10,000 under both tax systems, neglecting the additional dividend tax in the corporate case. If unexpected needs of €10,000 arise, the full amount is available under partnership taxation; under corporate taxation, dividend tax reduces the accessible amount to below €10,000. The resulting shortfall may then require external financing, which imposes additional costs.

If entrepreneurs anticipate their own behavioral constraints and the resulting increase in liquidity risk under the corporate tax system, they may prefer partnership taxation in light of potential future liquidity shocks. Research shows that individuals aware of their behavioral constraints are more likely to use commitment devices (e.g., Cobb-Clark et al. 2024). Choosing partnership taxation

may serve as such a commitment device, helping entrepreneurs prepare for future liquidity shocks. In sum, we formulate the following hypotheses:

Hypothesis 4a *In the presence of potential future liquidity shocks, entrepreneurs face a higher risk of liquidity constraints under the corporate than the partnership tax system.*

Hypothesis 4b *The presence of potential future liquidity shocks increases the likelihood of choosing the partnership tax system.*

2.6 Status Quo Bias

The choice between the partnership and corporate tax systems may also be influenced by a status quo bias, the tendency of individuals to prefer the current state of affairs and avoid change, even when an alternative may offer equal or greater benefits (e.g., Samuelson and Zeckhauser 1988). Providing a check-the-box option for entrepreneurs previously taxed under the partnership system suggests that their experience has been limited to that system. The corporate tax system is presented to them as a new option, requiring an affirmative decision to switch. Consistent with status quo bias, entrepreneurs may prefer to remain in the familiar partnership system—because switching requires overcoming psychological inertia and entails uncertainty. Thus, status quo bias may contribute to under-adoption of the corporate tax system, even when it is favorable.

Hypothesis 5 *Having experience with only the partnership tax system increases the likelihood of choosing the partnership tax system.*

3 Method, Data, and Procedure

3.1 Data and Participants

To investigate our hypotheses, we conduct a large pre-registered and incentivized online experiment. In the experiment, participants were asked to choose a tax system as part of an business life cycle. Participants were recruited from the German online access panel Bilendi & respondi.[5] The experiment was programmed with oTree (Chen et al. 2016). We present a translation of the instructions and screenshots of the experiments in the online appendix.

A total of 1,151 participants were randomly assigned to nine treatments (see Section 3.2). They were selected according to crossed quotas (gender × age) based on the distribution of company founders in Germany in 2020 (KfW 2022a,b). This quota was intended to proxy for the demographic structure of individuals typically facing the choice between the two tax systems early in the entrepreneurial life cycle. The final sample was comprised of 39.0% women and 61.0% men; 19.7% of participants were ages 18–24, 27.8% ages 25–34, 26.8% ages 35–44, 17.0% ages 45–54, and 8.7% ages 55–64. Descriptive statistics regarding participants' sociodemographic characteristics are provided in Appendix A. On average, participants received total compensation of €9.55 (SD 6.02). The median time required to complete the experiment and questionnaire was 34.7 minutes, resulting in a median hourly wage of €16.51, with a minimum of €4.00 and a maximum of €58.13.

3.2 Experimental Design and Treatments

Participants completed five independent rounds. In each, they performed a task over five business periods in which they determined how much of each period's profit (in ECU, an experimental

[5] Bilendi & respondi (2.5 million users) holds a certification for market, opinion, and social research (ISO 20252). Many studies in accounting have used Bilendi & respondi to recruit participants for experimental research (e.g., Maske et al. 2021; Maske and Sohn 2023; Blaufus et al. 2025).

currency) should be retained and how much of the resulting reserves should be released. Profits were independently determined each period from a discrete uniform distribution ranging from 0 to 6,000 ECU (in increments of 1,000) and were identical for all participants. Thus, profits were uncertain, and participants were informed only of the possible profit levels and that each was equally likely.[6] The distributed profit, minus taxes if applicable, plus released reserves, represents the entrepreneur's consumption and corresponds to the payout for a given period.

The first round was a training round without any taxes, which did not affect final compensation. The second round was also conducted without taxes, followed by rounds three and four, which differed only in their respective tax treatments (except for the *No Experience* treatment; see below). In one, profits were subject to partnership taxation; in the other, to corporate taxation (round order was randomized). In the fifth round, participants chose a tax system before performing the task. Participants who selected "indifferent" were randomly assigned to one of the two systems.

In both tax systems, the effective tax rate was identical at 47.5%. To incentivize saving, we follow the experimental paradigm of Blaufus and Milde (2021), informing participants that only one of the 20 periods (four rounds * five periods) would be randomly selected for their compensation. This approach allows us to simulate real-world profit accumulation decisions and encourages participants to distribute their payouts equally over time. For instance, if no reserves were built and the profit in a given period was 0 ECU, a randomly selected payout from that period would result in no variable compensation for the participant.

To obtain reliable data for our analysis, we implemented the following design elements: (1) At the start of each round, participants received detailed instructions on the procedure and, if applicable,

[6] Although profits are uncertain during the task, this uncertainty does not affect tax system choice. An additional treatment with known future profits shows no effect on this choice (see online Appendix B.1), suggesting that income uncertainty does not systematically bias preferences toward partnership taxation.

the tax rules (see online Appendix C). (2) A training round ensured participants understood the task. (3) Participants completed three comprehension tests—one on the procedure before the training round and one each on the tax rules of the respective tax system before rounds 3 and 4. (4) An attention check and an honesty test were included to confirm participant engagement. Only those who answered all comprehension questions correctly[7] and passed both checks were allowed to participate. Additionally, we excluded speeders—defined as the fastest 1%—to eliminate responses likely given without sufficient care.[8] The experimental treatments are described below. A summary of the treatment manipulations is provided in Table 1.

[Insert Table 1 about here]

3.2.1 Corporate Tax Rate and Tax Time Complexity (H1 and H2)

To test Hypotheses 1a-1b and 2b-2b, we use a 2x2 between-participants design with two levels of tax rate complexity and two levels of tax time complexity. The effective tax burden is held constant at 47.5% across treatments and tax systems. Tax rate complexity is manipulated by varying the dividend tax base. Under low tax rate complexity (*Low Tax Rate Complexity*), the tax burden is easily computed by adding the corporate and dividend tax rates (30% + 17.5%), while under high tax rate complexity (*High Tax Rate Complexity*), the corporate tax reduces the dividend tax base (30% + 25%(1 - 30%)). Tax time complexity is manipulated by varying whether dividend taxation is deferred (*High Tax Time complexity*) or not (*Low Tax Time complexity*); see examples in the instructions (online Appendix C). Reserves do not earn interest in any treatment, ensuring economic equivalence between tax systems and allowing us to isolate the effects of tax complexity

[7] Each question could be answered incorrectly only once.

[8] Across all treatments, 32.5% of participants failed the comprehension test and 5.4% failed the attention or honesty check. The observed completion rate aligns with typical rates in life cycle experiments (e.g., Bachmann et al. 2023).

from other factors.[9]

3.2.2 Disutility of Split Tax Payments (H3)

To test Hypothesis 3—whether the presence of two separate tax payments under the corporate tax system increases the likelihood of choosing the partnership tax system—we designed a treatment that isolates the effect of split tax payments (*One vs. Two Taxes*). This treatment builds on the *Low Tax Rate Complexity & Low Tax Time Complexity* treatment but includes two adjustments to exclude potential tax misperception. This is important because, even in the *Low Tax Rate Complexity & Low Tax Time Complexity* treatment—despite low corporate tax complexity—we observe significant misperception: participants systematically underestimate the corporate tax burden ($p < 0.001$; see Section 3.3 for details on measurement). First, we removed information necessary for the full 2×2 design (see Section 3.2.1) but not required in this specific treatment—such as the "not deductible" labels on tax bases. Second, we explicitly displayed the aggregated tax burden when two separate taxes were applied (30% + 17.5% = 47.5%).

3.2.3 Liquidity Risk (H4)

To test Hypotheses 4a and 4a—whether the risk of liquidity constraints is higher under corporate taxation in the presence of potential future liquidity shocks and whether such shocks increase the preference for the partnership system—we introduced two additional treatments that closely follow the *High Tax Rate Complexity & High Tax Time Complexity* treatment (see Section 3.2.1). In contrast to the previous treatments, participants had to meet a minimum payout threshold of 600 ECU [1,200 ECU] in periods with [without] taxes. If this threshold was not reached, a penalty

[9] We examined whether dropout rates differed systematically across the four treatments (*dropout bias*). A Pearson chi-squared test comparing completion rates——including failures on comprehension, attention, and honesty checks as well as speeders——revealed no significant differences ($p = 0.343$). In addition, a joint chi-squared test based on a multinomial logit model confirmed that sociodemographic characteristics listed in Panel B of Table A2 were balanced across treatments ($p = 0.689$).

equal to the shortfall was imposed, further reducing the participant's payout for that period. The penalty reflects the liquidity costs associated with failing to retain sufficient earnings, such as the need to take out a short-term loan in response to unexpected consumption shocks.

The two treatments differ only in the structure of the consumption shock. In *Liquidity No Shock*, the minimum payout remains constant across all periods. In contrast, *Liquidity Shock* introduces a one-time increase in the minimum payout to three times the usual level in one of the periods between 2 and 4.[10] Participants knew this but not the exact period in which the shock would occur.[11]

3.2.4 Status Quo Bias (H5)

To examine whether experience with only the partnership tax system influences participants' choices, we implemented two additional treatments. While earlier treatments excluded a corporate tax benefit to isolate behavioral responses to structural features of the tax systems, testing for status quo bias requires a different setup. Here we introduce a corporate tax benefit—via interest on retained earnings—to ensure that the corporate tax system is objectively superior. This allows us to detect deviations from the optimal choice due to participants sticking with the familiar option.

The *Experience* treatment is identical to the *High Tax Rate Complexity & High Tax Time Complexity* condition, except that retained earnings accrue interest at a rate of 20% per period.[12] In the *No Experience* treatment, only the partnership tax system was available in rounds 3 and 4 before the choice between corporate and partnership taxation in the final round.[13]

[10] All minimum payouts were calibrated to ensure that penalties could be avoided with appropriate planning.

[11] A Pearson chi^2 test revealed no systematic differences in dropout rates across treatments (p = 0.155). A joint test using a multinomial logit model confirmed that sociodemographic characteristics listed in Table A4 were balanced (p = 0.529).

[12] The high interest rate ensures that the corporate tax benefit is salient, given that it increases with the return on retained earnings when $t_c < t_p$.

[13] A Pearson chi^2 test showed no differences in dropout rates across treatments (p = 0.768). A joint test using a multinomial logit model confirmed that sociodemographic characteristics listed in Table A5 were balanced (p = 0.812).

3.3 Variable Measurement

To investigate the predicted effects on the preferences for partnership taxation, we use the variable *Choice Part* as the dependent variable. *Choice Part* is equal to one if the partnership system is chosen and zero if the corporate system is chosen or if the participant is indifferent between the two. For the mediation analyses (H1 and H2), we use also *Overestimate* and *Underestimate* as dependent variables. After rounds 3 and 4, we asked the participants about the effective tax rate of the tax system in the current round. To incentivize this question, we randomly paid out 15 times €50 among all participants with correct answers. *Overestimate* (*Underestimate*) is one if the participant entered a tax rate higher (lower) than 47.5% [+/- 0.5 percentage points tolerance]. In addition, for the two liquidity treatments (H4), we consider two further dependent variables: *Liquidity Cost Probability*, which indicates whether a liquidity shortfall occurred (i.e., whether the participant was penalized), and *Liquidity Cost Amount*, which measures the monetary value of the penalty in a given round. We use our treatment variables as independent variables. These are binary variables that equal one if the observation belongs to the respective treatment and zero otherwise.

To control for socio-demographic factors, we include the following variables: gender (*Male*), age (*Age*), net income (*Income*), single household (*Single Household*), education (*University Degree*), tax knowledge (*Tax Knowledge*), cognitive ability (*Cognitive Ability*), loss aversion (*Loss-averse*), the preference for prepayment (*Preference for Prepayment*), and tax aversion (*Tax Aversion*). Definitions and descriptive statistics for these controls are provided in Appendix A.

4 Empirical Results and Discussion

4.1 Corporate Tax Rate Complexity (H1)

Before proceeding with the analysis, we first examine whether the corporate tax system is perceived as more complex than the partnership system, as higher perceived complexity may trigger complexity aversion and tax misperception, biasing choices toward the partnership system. To assess the baseline perception of tax complexity, we conducted an additional survey in which participants were randomly assigned to evaluate either the corporate or partnership tax system (hereinafter referred to as the evaluation survey).[14] Each participant received only the relevant tax information and rated perceived complexity on a scale from 1 (very simple) to 9 (very complicated) without making a decision. In contrast to the main experiment, this setting allowed us to measure perceived complexity in isolation—unbiased by potential complexity spillovers from the broader experimental setting or learning effects. Results confirm our expectation: the corporate tax system was rated as significantly more complex than the partnership system (see Panel B in Table 2).

[Insert Table 2 about here]

We next test whether our manipulation of corporate tax rate complexity altered perceived complexity. In the evaluation survey, participants were randomly assigned to either the high or low complexity condition. We find that perceived complexity was significantly higher in the high tax rate complexity group than in the low complexity group (see Panel B in Table 2).

With these perceptions in place, we now examine the effect of tax rate complexity on tax system

[14]The evaluation survey was conducted via Bilendi & respondi in Germany, using the same sampling quotas as in the main study. Participants from the main experiment were excluded. In total, 362 participants completed the survey. The median time required to complete it was 5.4 minutes, resulting in a median hourly wage of €13.23. Descriptive statistics are reported in Panel A of Table 2 (for the dependent variable) and Table A6 (for sociodemographic characteristics). The full instructions and questionnaire are provided in online Appendix G.

choice in our main experiment. Panel C of Table 2 shows that increasing tax rate complexity increases the probability of preferring the partnership tax system by 17.8%-points, which is significant, as shown by the OLS regression results in Panel D.[15] To examine the extent to which this effect is driven by tax misperception, we conduct mediation analyses. Here, choosing the partnership system serves as the outcome variable, tax rate complexity as the predictor, and the overestimation of the corporate tax burden as the mediating variable. The results of this analysis are presented in Figure 1a. We find a significant positive effect of increasing tax rate complexity on the probability of overestimating the corporate tax burden. One reason for this is that participants simply added the nominal tax rates (9.3% of our participants) and thus estimated the average tax burden to be (30% + 25% =) 55%. Corporate tax rate overestimation also has a significant positive effect on the probability of preferring the partnership. In line with Hypothesis 1a, this results in a significant positive indirect effect on *Choice Part*. Figure 1a also shows a significant positive direct effect of tax rate complexity on the preference for the partnership system, supporting Hypothesis 1b and indicating complexity aversion. In sum, we find a significant positive total effect.

[Insert Figure 1 about here]

4.2 Corporate Tax Time Complexity (H2)

As a first step, we again examine whether our manipulation of tax time complexity affects perceived tax complexity. Results from the evaluation survey show that dividend tax deferral (*High Tax Time Complexity*) led to significantly higher perceived complexity than the condition without deferral

[15] We rely on OLS regressions to analyze our dichotomous dependent variable for two main reasons. First, recent methodological research suggests that linear approaches are not only valid but can outperform nonlinear models like logistic regression for estimating treatment effects on binary outcomes (e.g., Angrist and Pischke 2009; Gomila 2021). Second, t-tests are well suited for testing directional hypotheses, as they are based on two-tailed distributions. In contrast, standard methods for binary outcomes—such as logistic regression or chi-square tests—typically rely on one-tailed distributions, limiting their use for directional testing. Our approach aligns with recent practice in accounting research (e.g., Hageman et al. 2023; Bourveau et al. 2025).

(*Low Tax Time Complexity*). The difference is statistically significant (see Panel B in Table 2).

We next analyze how tax time complexity affects participants' choices. Panel A of Table 2 shows that tax time complexity increases the probability of preferring the partnership from 29.6% to 38.2%, which is significant, as shown by the OLS regression results in Panel B. We again conduct a mediation analysis to provide information on the extent to which the total effect can be explained by the indirect (Hypothesis 2b) and direct (Hypothesis 2b) effects (see Figure 1b). Consistent with our theoretical predictions, we find that dividend tax deferral increases the probability of underestimating the corporate tax burden. This in turn has a negative effect on the choice for partnership taxation. In line with Hypothesis 2b, we find a significant negative indirect effect of tax time complexity on preferences for partnership taxation. We also find a significant positive direct effect (Hypothesis 2b), as participants act complexity averse. The total effect is also significantly positive, as predicted by Hypothesis 2b. Finally, the OLS regression shows no significant interaction between *High Tax Rate Complexity* and *High Tax Time Complexity* on *Choice Part*, indicating that combining both complexities does not amplify complexity aversion.

4.3 Disutility of Split Tax Payments (H3)

To test whether the structure of the tax burden affects participants' preferences, we examine whether the presence of two separate tax payments under the corporate system increases the likelihood of choosing the partnership system, as predicted by prospect theory and Hypothesis 3.

In the treatment *One vs. Two Taxes*, the two tax systems differ solely in the number of taxes. Our evaluation survey confirms that perceived complexity does not differ between the conditions (see Panel B in Table 3). Moreover, as intended, there are no differences in the perception of effective tax rates between the one-tax and two-tax treatments ($p = 0.804$, paired t-test), indicating that the

manipulation successfully isolates the effect of split tax payments while holding complexity and tax perception constant. Panel C of Table 3 shows no clear preference for either system, which is further supported by the insignificant binomial probability test reported in Panel D. We conclude that the number of taxes does not influence the choice of legal form, and we therefore find no significant support for Hypothesis 3.

[Insert Table 3 about here]

4.4 Liquidity Risk (H4)

We now examine the effect of a liquidity shock on the choice between partnership and corporate taxation. As a first step, we analyze whether a future liquidity shock leads to a higher risk of liquidity shortfalls—and thus higher liquidity costs—under the corporate tax system compared to the partnership system (Hypothesis 4a).

Panel A of Table 4 shows that the probability of incurring liquidity costs due to a liquidity shock (*Liquidity Cost Probability*) increases under both tax systems. For the partnership, this probability rises from 21.0% to 37.0%, an increase of 16.0 percentage points. For the corporation, it increases from 25.9% to 56.3%, corresponding to a 30.4 percentage point increase—almost twice as much. A similar pattern emerges for the amount of liquidity costs (*Liquidity Cost Amount*). The OLS regression results in Panel B confirm that the differential impact of the liquidity shock between the partnership and the corporation is statistically significant, both for the probability and the amount of liquidity costs. These findings support Hypothesis 4a.

[Insert Table 4 about here]

Nevertheless, as shown in the last two columns of Panel B, we find no support for Hypothesis 4b: the liquidity shock does not significantly increase the probability of preferring the partnership

system. Our analyses suggest that this is due to the continued dominance of perceived complexity in driving preferences for the partnership. After their decision, participants were asked whether their choice of the partnership was motivated by the desire to avoid an additional tax burden in case of a high minimum payout (= shock). However, only 23.2% cited this as a reason, making it the least frequently cited reason. This indicates limited support for the idea that the partnership system is used as a self-commitment device against liquidity risk. In contrast, the complexity of the corporate tax was the most frequently cited reason, with 66.1% of participants mentioning it.

4.5 Status Quo Bias (H5)

Panel A of Table 5 shows that, without prior experience with the corporate tax system, 52.4% of participants choose the partnership system, compared to only 32.8% among those with prior corporate tax experience. The OLS regression results in Panel B confirm this pattern: experience reduces the probability of preferring the partnership by 20.7 percentage points (p = 0.001), supporting Hypothesis 5. The results reveal a status quo bias driven by inertia: familiarity anchors decisions and reduces the propensity to switch—even when the corporate tax system is economically superior.[16]

[Insert Table 5 about here]

[16]Since the *Experience* treatment includes a corporate tax benefit, we also examined to what extent the benefit itself influences participants' choices. To do so, we added a second treatment in which the corporate tax benefit is implemented via a reduced corporate tax rate and compared both conditions to the otherwise identical *High Tax Rate Complexity & High Tax Time Complexity* treatment without a benefit. We find that the presence of a corporate tax benefit significantly decreases the likelihood of choosing the partnership system—by 13.6 percentage points when the benefit is based on interest and by 23.9 percentage points when implemented via a lower corporate tax rate. This indicates that the monetary advantage of corporate taxation plays a meaningful role in participants' decisions. However, even with a substantial corporate tax benefit, due to a reduced corporate tax rate, only 65% of participants choose the corporate tax system, highlighting again the role of behavioral frictions in tax system choice. A detailed analysis of this effect is provided in online Appendix B.2.

4.6 Discussion

The experiment provides causal evidence that behavioral frictions—such as complexity aversion, complexity-induced misperception of the corporate tax burden, and status quo bias—influence the choice between the corporate and partnership tax systems. Specifically, it shows that corporate tax rate and tax time complexity increase the preference for partnership taxation. Moreover, we find that the choice between the partnership and corporate tax systems is influenced by a significant status quo bias. In contrast, the experiment does not support the notion that the disutility of split tax payments (corporate tax and dividend tax) under the corporate system influences decision-making. Nor do we find that the partnership tax system serves as a commitment device against liquidity risk. However, consistent with theoretical predictions, we find that entrepreneurs face a higher risk of liquidity constraints under corporate taxation compared to partnership taxation. Yet most participants appear unaware of this, which may explain why it does not influence their choice.

While the experimental setting isolates behavioral frictions at the individual level, real-world entrepreneurs typically operate under different conditions. (1) They are often better informed about tax issues and more engaged in tax planning due to higher incomes. To test whether such real-world characteristics moderate behavioral responses, we re-estimate our models (untabulated) including interaction terms with tax knowledge (*Tax Knowledge*) and income level (*Income*). However, we find no significant interactions, suggesting that neither factor systematically alters the behavioral effects we observe. (2) In practice, compliance costs may affect the decision to switch tax systems. While this is a potential concern, we consider it an unlikely factor in our context. According to the legislature, the costs of applying the German check-the-box rule were expected to be very low—around €22 per application (Federal Council 2007, p. 62). While this estimate may seem

far too low, both practitioner interviews and tax advisor survey responses (see Section 5) suggest that compliance costs are not the main barrier. (3) In the real world, entrepreneurs are typically hire tax advisors. These advisors could help mitigate behavioral biases. At the same time, they might anticipate behavioral constraints, such as clients' difficulty in managing liquidity under the corporate tax system, and thus steer clients toward the partnership system. In cases like this, the partnership system could still function as a de facto commitment device, albeit indirectly through advisors' recommendations. To explore this possibility, we surveyed tax advisors; the design and results are presented in the next section.

5 Survey of Tax Advisors

In 2020, we conducted a survey of certified German tax advisors in cooperation with a German business magazine. A total of 292 tax advisors answered questions on consulting practice and tax knowledge of the German check-the box rule; a translation of the questionnaire is provided in the online Appendix F. Panel A of Table 6 provides an overview of the survey sample. Most respondents primarily advise self-employed individuals and SMEs; 73.3% indicated these groups comprise their main client base. The median annual revenue of the tax consulting firms was between €0.75 and €1.5 million, with a median of 18 employees per firm. Moreover, 55% of respondents had recommended the corporate tax system under the check-the-box rule to a client at least once.

[Insert Table 6 about here]

Among other things, we presented the tax advisors with the example case introduced in Section 2.1, which illustrates the corporate tax benefit. In this scenario, the client asks whether they should opt for corporate taxation.[17] Recall that the corporate tax benefit in this example amounts

[17] In the original German question, we refer to the specific section and ask: Your client asks you whether you would

to €16,434, which makes opting for the corporate tax system the preferable option. Advisors responded on a five-point Likert scale from 1 (definitely not) to 5 (definitely).

Despite the significant corporate tax benefit, we find that 23.0% of tax advisors would not recommend the option (checking one or two in the question). Only 49.3% would recommend using the option, while 27.7% were indifferent. To better understand the reasons for not recommending the favorable option, we also asked respondents to provide an open-ended explanation for their recommendation. The stated reasons were categorized by 10 independent research assistants with expertise in tax law, based on a predefined set of coding criteria. Each response was coded twice, at a one-week interval, to ensure reliability.[18] The criteria were developed in advance by two of the authors (see Table 7). A response was assigned to a category if more than half of the 10 research assistants independently classified it as such. The proportion of responses assigned to each category is reported in the last column.

[Insert Table 7 about here]

Among those who would not recommend opting for the corporate taxation, we found misperception of the corporate tax benefit in 42.9% of the reported reasons; i.e., these respondents did not realize the present value benefit of opting for the corporate tax system. We find that an additional 36.7% of tax advisors mentioned liquidity-related concerns as a reason for not recommending the application of the check-the-box rule. This is noteworthy, as our experimental evidence suggests that anticipated liquidity shocks do not significantly affect the preference for corporate taxation. One possible explanation is that tax advisors anticipate potential liquidity risks and fear being blamed

recommend submitting an application for preferential treatment of retained profits in accordance with Sec. 34a EStG.

[18] A second round of coding was essential, as many of the advisors' responses were vague or ambiguous. Despite these challenges, the average intra-coder agreement reached 89.5%, indicating a high level of coding consistency. To assess inter-coder reliability, we calculated the average agreement with the majority decision for each category and statement, which resulted in a comparable value of 89.2%, suggesting a substantial level of consensus across coders.

by clients if financial constraints arise due to dividend taxation. Moreover, 6.1% of responses were categorized as expressing concerns that clients might "forget" about the deferred taxation of future withdrawals—providing a further indication that advisors factor in potentially irrational or short-sighted client behavior. In addition, 12.2% mentioned consulting and compliance costs as the reason.[19]

To examine the determinants of nonrecommendation, we conducted an OLS regression with *Non-recommendation* (dummy equal to one if advisors answered one or two to the question mentioned above) as the dependent variable and several determinants (see Panel B in Table 6). These include *Tax Expertise* (number of correct answers out of 24 knowledge questions on the German tax system), *Experience* (dummy equal to one if the advisor applied the check-the-box rule for at least one client in the past five years), *Client Group SMEs* (dummy equal to one if most of their revenue comes from self-employed clients and SMEs), *Tax Firm Employees* (number of employees), and *Revenue* (categorical variable capturing firm revenue). In line with prior results regarding the heterogeneity in the quality of tax advice (Zwick 2021), we find that advisors with lower tax expertise ($p = 0.006$) and less consulting experience ($p = 0.005$) were more likely to advise against switching to the corporate tax system, despite its economic advantage.

6 Conclusion

Why do many entrepreneurs forgo tax savings when choosing between the partnership and corporate tax systems under a check-the-box rule? This study presents experimental and survey evidence indicating that behavioral frictions largely drive this choice.

[19]The high level of complexity of the German check-the-box rule (Section 34a) is also reflected in the numerous German-language publications (Wagner and Zeller 2011). As a result, many German economists called for the abolition of the option shortly after its introduction (Knirsch et al. 2008).

Our experiment shows that both corporate tax rate complexity and tax time complexity shift preferences toward the partnership system, driven by overestimation of the corporate tax burden and general complexity aversion. Moreover, we find that a status quo bias strongly influences the choice: participants who lack experience with the corporate tax system are more likely to stick with the familiar partnership system, even when switching would benefit them financially. Although we also document higher potential liquidity constraints under the corporate tax system in the presence of liquidity shocks, these constraints are, on average, not anticipated by our participants and therefore do not influence their choices. While one might expect tax advisors to correct misperceptions, our survey reveals that they do not necessarily do so. Some advisors themselves misjudge the corporate tax benefit. Others anticipate clients' behavioral tendencies—such as misperceiving deferred taxes, which may lead to liquidity constraints—and strategically align their advice with clients' likely reactions rather than purely financial considerations. As a result, professional advice does not universally lead to optimal outcomes.

From a theoretical perspective, our study supports the *Behavioral Taxpayer Response Model*, particularly its core assumption that actual choices depend on the *subjective* tax burden. This subjective burden systematically deviates from the objective one due to bounded rationality. Our results emphasize that tax information characteristics—such as tax complexity and timing—as well as behavioral traits—such as status quo bias and complexity aversion—significantly shape tax decisions. Our findings also refine the model's prediction that information intermediaries can mitigate subjective misperception. We show that this moderating role is limited: some tax advisors also misperceive the economic benefits of complex tax rules, while others adjust their advice in anticipation of their clients' behavioral frictions. Put differently, advisors sometimes fail to correct biased decision-making. Future research should examine the strategic behavior of tax advisors in

the presence of client biases, particularly to what extent they recognize and deliberately adapt to client misperceptions (e.g., Hatfield et al. 2008).

Our findings have practical implications for both taxpayers and policymakers. Entrepreneurs may incur substantial financial losses by forgoing tax benefits due to tax misperception. Improving tax advice——through standardized tax comparison tools and behavioral training for advisors——could help bridge the gap between policy intent and taxpayer behavior.

For policymakers, our findings suggest that achieving tax neutrality between corporate and partnership taxation requires more than aligning effective tax rates. Behavioral frictions can undermine the intended neutrality of tax policy—even when systems are theoretically equivalent. Policymakers must therefore consider complexity aversion and status quo preferences when designing tax rules. In response to persistently low uptake of the corporate tax option, the German legislature simplified the check-the-box rules and increased the associated corporate tax benefit in 2024. While these adjustments address structural barriers, it remains unclear whether they can overcome the behavioral obstacles identified here. To fully realize policy objectives, additional behavioral interventions may be needed—particularly at key decision points. These could include pre-filled tax burden comparisons in digital application portals, simplified interactive calculators, or targeted materials provided during the early stages of startups. Such measures may help reduce tax misperception, support more informed decisions, and enhance the effectiveness of tax policy.

As with any empirical study, ours has limitations. While our experiment allows for causal inference and reveals underlying behavioral frictions, the generalizability of our findings may be shaped by institutional features of the German tax system. Its complexity is considerable—as documented in cross-country tax complexity indices (Hoppe et al. 2023). Notably, the behavioral impact of individual tax rules, such as the check-the-box option, may depend not only on the

design of the rule itself but also on the broader complexity of the surrounding tax environment. Experimental evidence by Abeler and Jäger (2015), for example, shows that taxpayers underreact to changes in tax incentives when embedded in more complex systems. This suggests that the effectiveness of tax instruments may be moderated by the overall complexity of the tax system, something future research could explore across institutional settings.

At the same time, our experiment isolates core features of the legal form choice—namely, double taxation of corporations versus single-level taxation of partnerships. This abstraction supports the broader relevance of our results for systems that share this fundamental structure, independent of specific national implementations.

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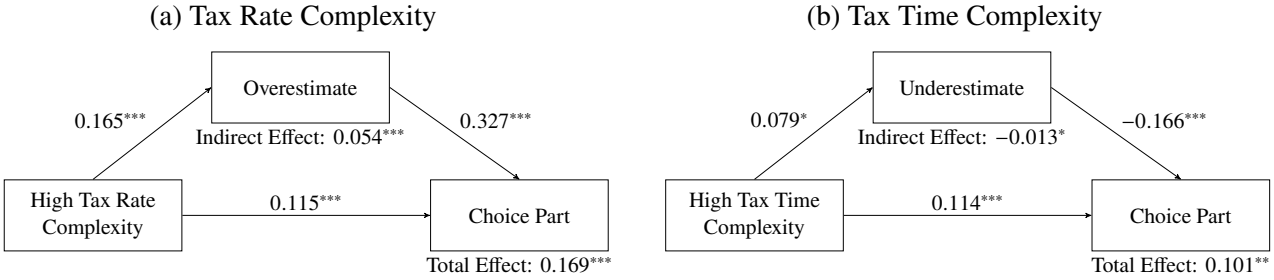
FIGURES

Figure 1: Mediation Analyses (H1 and H2)



This figure presents results from two mediation analyses that examine the extent to which the effect of tax complexity on tax system choice is mediated by tax misperceptions (H1 and H2). The mediation models display direct and indirect paths through which the treatments—*Tax Rate Complexity* and *Tax Time Complexity*—affect the likelihood of preferring the partnership tax system (*Choice Part*) relative to the low complexity conditions, with *Overestimate* and *Underestimate* serving as mediators. The path analysis is conducted by estimating a generalized structural equation model, including the control variables *Male*, *Age*, *Income*, *Single Household*, *University Degree*, *Tax Knowledge*, *Cognitive Ability*, *Loss-averse*, *Preference for Prepayment*, and *Tax Aversion* as covariates. ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively.

TABLES

TABLE 1
Overview of Treatments

Treatment	TRC[a]	TTC[b]	Experience[c]	CTB[d]	Liquidity Risk[e]	Liquidity Shock[f]	n
H1 & H2							
High TRC & High TTC	High	High	Yes	No	No	No	125
Low TRC & High TTC	Low	High	Yes	No	No	No	121
High TRC & Low TTC	High	Low	Yes	No	No	No	123
Low TRC & Low TTC	Low	Low	Yes	No	No	No	120
H3							
One vs. Two Taxes	Low[g]	Low[g]	Yes	No	No	No	130
H4							
Liquidity No Shock	High	High	Yes	No	Yes	No	143
Liquidity Shock	High	High	Yes	No	Yes	Yes	135
H5							
Experience	High	High	Yes	Yes	No	No	128
No Experience	High	High	No	Yes	No	No	126
Total							1,151

Across all treatments, the total tax rates for the partnership and the corporation are identical at 47.5%; that is, there is no tax rate differential between the two regimes.

[a] *Corporate Tax Rate Complexity* (TRC): Under low complexity, the effective tax burden is 30% + 17.5%. Under high complexity, the corporate tax reduces the dividend tax base (30% + 25%(1 – 30%)).

[b] *Corporate Tax Time Complexity* (TTC): High complexity allows deferral of dividend taxation; under low complexity, dividends are taxed immediately.

[c] *Experience*: In the *No Experience* condition, participants were exposed solely to the partnership tax system prior to making a choice between the partnership and corporate tax systems; those in the *Experience* condition encountered both systems before deciding.

[d] *Corporate Tax Benefit* (CTB): Present when retained earnings earn 20% interest, making the corporate regime financially superior; absent at 0% interest, where both regimes are financially equivalent.

[e] *Liquidity Risk*: Introduces a minimum payout requirement per period; penalties apply if thresholds are not met.

[f] *Liquidity Shock*: One randomly selected period required a substantially higher payout to simulate unexpected cash needs.

[g] In contrast to the *Low TRC & Low TTC* treatment, we made two adjustments to exclude tax misperceptions. First, we removed unnecessary information (e.g., "not deductible" labels on tax bases). Second, we additionally displayed the aggregated tax burden across both taxes when two taxes were present.

TABLE 2
Results Hypotheses 1 and 2

Panel A: Perceived Tax Complexity (Evaluation Survey)

Treatment Manipulation	Mean	SD	Min	p50	Max	n
Partnership vs. Corporation						
Partnership	5.54	2.44	1.00	5.00	9.00	52
Corporation	6.69	2.20	1.00	7.00	9.00	209
Corporate Tax Rate Complexity						
High	7.04	1.93	1.00	8.00	9.00	104
Low	6.35	2.40	1.00	7.00	9.00	105
Corporate Tax Time Complexity						
High	7.09	1.83	2.00	8.00	9.00	103
Low	6.31	2.45	1.00	7.00	9.00	106

Panel A reports descriptive statistics for perceived tax complexity, measured on a scale from 1 ("very simple") to 9 ("very complicated"). Perceptions were elicited in a separate survey, independent of the main experiment.

Panel B: Tests of Mean Differences (Evaluation Survey)

Test	Difference	df	t-statistic	p-value
Effect of *Partnership* on *Perceived Tax Complexity*	-1.16	259	3.32	< 0.001
Effect of *Corporate Tax Rate Complexity* on *Perceived Tax Complexity*	0.69	207	2.28	0.023
Effect of *Corporate Tax Time Complexity* on *Perceived Tax Complexity*	0.78	207	2.60	0.010

Panel B reports the results of independent-samples t-tests. The dependent variable is perceived tax complexity, measured on a scale from 1 ("very simple") to 9 ("very complicated"). All p-values are two-tailed.

Panel C: Descriptive Statistics – Mean Values by Tax Complexity Treatment (Main Experiment)

	Choice			Corporate Tax Rate Misperception		
	Partnership (*Choice Part*)	Corporation	Indifferent	Overestimate	Underestimate	n
Corporate Tax Rate Complexity						
High	0.427	0.355	0.218	0.278	0.621	248
Low	0.249	0.407	0.344	0.112	0.656	241
Corporate Tax Time Complexity						
High	0.382	0.407	0.211	0.203	0.671	246
Low	0.296	0.354	0.350	0.189	0.605	243

Panel C presents descriptive statistics on participants' final-round choices between the two tax systems (Partnership vs. Corporation) and their corporate tax rate misperceptions. *Overestimate* (*Underestimate*) equals one if a participant reported a tax rate more than 0.5 percentage points above (below) the true rate of 47.5%, based on elicitation questions following rounds three and four.

Panel D: OLS Regression with *Choice Part* as the Dependent Variable (Main Experiment)

	Predicted Sign	Coef.	Robust Std. Err.	p−value
Intercept	+/-	0.279	0.111	0.012
Corporate Tax Rate Complexity	+ (H1a, H1b)	0.182	0.059	0.002
Corporate Tax Time Complexity	+/- (H2c)	0.112	0.055	0.042
Corporate Tax Rate Complexity x *Corporate Tax Time Complexity*		-0.027	0.085	0.747
Controls				YES
Adjusted R^2 (%)				6.31
n				489

Panel D reports results from an OLS regression using robust standard errors; all p-values are two-tailed. *Choice Part* is one if the partnership system is chosen. Our control variables are *Male*, *Age*, *Income*, *Single Household*, *University Degree*, *Tax Knowledge*, *Cognitive Ability*, *Loss-averse*, *Preference for Prepayment*, and *Tax Aversion*. These variables are defined in Appendix A.

TABLE 3
Results Hypothesis 3

Panel A: Perceived Tax Complexity (Evaluation Survey)

Treatment	Mean	SD	Min	p50	Max	n
One Tax	5.69	2.70	1.00	6.00	9.00	52
Two Taxes	5.37	2.38	1.00	5.00	9.00	52

Panel A reports descriptive statistics for perceived tax complexity, measured on a scale from 1 ("very simple") to 9 ("very complicated"). Perceptions were elicited in a separate survey, independent of the main experiment.

Panel B: Tests of Mean Differences (Evaluation Survey)

Test	Difference	df	t-statistic	p-value
Effect of *Two Taxes* on *Perceived Tax Complexity*	-0.32	102	-0.66	0.514

Panel B reports the result of an independent-sample *t*-tests. The dependent variable is perceived tax complexity, measured on a scale from 1 ("very simple") to 9 ("very complicated"). The *p*-value is two-tailed.

Panel C: Descriptive Statistics – Mean (Main Experiment)

Treatment	Partnership (*Choice Part*)	Corporation	Indifferent	n
One vs. Two Taxes	0.169	0.146	0.685	130

Panel C presents descriptive statistics on participants' final-round choices between the two tax systems (Partnership vs. Corporation).

Panel D: Test of Significance of Difference Using Binomial Probability Test (Main Experiment)

Is the proportion of participants choosing the corporation significantly different from those choosing the partnership?	p = 0.755 (two-sided)

Panel D reports the result of a binomial probability test examining whether the proportion of participants choosing the corporation differs significantly from those choosing the partnership. Participants who were indifferent between the two tax systems were excluded from the statistical test.

TABLE 4
Results Hypothesis 4

Panel A: Descriptive Statistics – Means across Treatments

Treatment	Choice			Liquidity Cost				n
	Partnership (*Choice Part*)	Corporation	Indifferent	Probability		Amount		
				Part.	Corp.	Part.	Corp.	
Liquidity No Shock	0.399	0.357	0.245	0.210	0.259	18.0	21.3	143
Liquidity Shock	0.415	0.326	0.259	0.370	0.563	68.4	99.5	135

Panel B: OLS Regression

		Δ Liquidity Cost Probability		Δ Liquidity Cost Amount		Choice Part	
	Predicted Sign	Coef.	p−value	Coef.	p−value	Coef.	p−value
Intercept	+/-	0.198	0.181	5.87	0.805	0.619	< 0.001
Liquidity Shock	+ (H4)	0.135	0.022	27.99	0.006	0.005	0.928
Controls			YES		YES		YES
Adjusted R^2 (%)			2.05		0.45		0.93
n			278		278		278

Panel A presents descriptive statistics on participants' final-round choices and liquidity cost between the two tax systems (Partnership vs. Corporation). Panel B reports results from an OLS regression using robust standard errors; all p-values are two-tailed. *Choice Part* is one if the partnership system is chosen. *Liquidity Cost Probability* indicates whether a participant incurred a liquidity shortfall (i.e., received a penalty) under a given tax system. *Liquidity Cost Amount* measures the corresponding monetary penalty in ECU within that tax system. Δ *Liquidity Cost Probability* and Δ *Liquidity Cost Amount* capture the difference in each measure between the corporate and the partnership tax system (Corporation minus Partnership). Our control variables are *Male*, *Age*, *Income*, *Single Household*, *University Degree*, *Tax Knowledge*, *Cognitive Ability*, *Loss-averse*, *Preference for Prepayment*, and *Tax Aversion*. These variables are defined in Appendix A.

TABLE 5
Results Hypothesis 5

Panel A: Descriptive Statistics – Means across Treatments

Treatment	Partnership (*Choice Part*)	Corporation	Indifferent	n
Experience	0.328	0.484	0.188	128
No Experience	0.524	0.349	0.127	126

Panel B: OLS Regression with *Choice Part* as the Dependent Variable

	Predicted Sign	Coef.	Robust Std. Err.	p−value
Intercept	+/-	0.207	0.062	0.001
No Experience	+ (H5)	0.207	0.062	0.001
Controls				YES
Adjusted R^2 (%)				4.40
n				254

Panel A presents descriptive statistics on participants' final-round choices between the two tax systems (Partnership vs. Corporation). Panel B reports results from an OLS regression using robust standard errors; all p-values are two-tailed. *Choice Part* is one if the partnership system is chosen. Our control variables are *Male*, *Age*, *Income*, *Single Household*, *University Degree*, *Tax Knowledge*, *Cognitive Ability*, *Loss-averse*, *Preference for Prepayment*, and *Tax Aversion*. These variables are defined in Appendix A.

TABLE 6
Survey of Tax Advisors

Panel A: Descriptive Statistics

Variable	Mean	SD	Min	p50	Max
Tax Expertise	0.826	0.117	0.417	0.854	1.000
Experience	0.548	0.499	0.000	1.000	1.000
Client Group Private Individuals	0.146	0.113	0.000	0.100	0.800
Client Group SMEs	0.733	0.182	0.100	0.800	1.000
Client Group Large Firms	0.120	0.173	0.000	0.050	0.850
Tax Firm Employees	58.40	166.5	0.000	18.00	1,745
Revenue < *€400K*	0.096	0.295	0.000	0.000	1.000
€400K ≤ *Revenue* < *€750K*	0.168	0.374	0.000	0.000	1.000
€750K ≤ *Revenue* < *€1.5M*	0.267	0.443	0.000	0.000	1.000
Revenue ≥ *€1.5M*	0.469	0.500	0.000	0.000	1.000

Panel B: OLS Regression with *Non-recommendation* as the Dependent Variable

	Coef.	Robust Std. Err.	p−value
Intercept	0.972	0.213	<0.001
Tax Expertise	−0.598	0.217	0.006
Experience	−0.137	0.049	0.005
Client Group SMEs	−0.002	0.001	0.265
Tax Firm Employees	−0.000	0.000	0.685
€400K ≤ *Revenue* < *€750K*	−0.132	0.094	0.159
€750K ≤ *Revenue* < *€1.5M*	−0.104	0.090	0.248
Revenue ≥ *€1.5M*	−0.002	0.088	0.986
Controls			YES
Adjusted R^2 (%)			5.74
n			292

This table presents descriptive statistics from the survey of tax professionals. *Non-recommendation* is a binary variable equal to one if the tax professional selected option 1 or 2 on a five-point Likert scale ranging from 1 ("definitely not recommending") to 5 ("definitely recommending") in response to the recommendation question, indicating that they would not advise the client to opt for the more beneficial corporate tax treatment under the check-the-box rule. *Tax Expertise* is measured as the proportion of correct answers to 24 knowledge questions about the German tax system. *Experience* is a binary variable equal to one if the tax professional has filed an application for corporate taxation under the check-the-box rule (Section 34a of the German Income Tax Code) on behalf of at least one client within the past five years. The *Client Group* variable equals one if the client group (private individuals, SMEs, or large firms) accounts for the largest share of the firm's revenues. *Tax Firm Employees* captures the total number of employees working in the tax firm. *Revenue* is a categorical variable with four groups: less than €400K, €400K to < €750K, €750K to < €1.5M, and greater than €1.5M.

TABLE 7
Coding Categories for Open-Ended Responses

Category	Definition	Share Coded
(1) Tax Misperception	The advisor fails to recognize the tax advantage of applying Section 34a of the German income tax code in the given scenario (i.e., the tax rate disadvantage is smaller than the interest advantage).	42.86%
(2) Liquidity Risk due to Unplanned Withdrawals	The advisor refers to liquidity risks resulting from the mandatory subsequent taxation of unexpected (over-)withdrawals; taxation may occur at an inconvenient time (e.g., increased consumption needs, lower profits).	36.73%
(3) Client Myopia	The advisor stresses that clients might "forget" about the deferred taxation of future withdrawals.	6.12%
(4) Uncertainty About Future Tax Rates	The advisor emphasizes the uncertainty of future tax rates (e.g., due to legislative changes or income fluctuations).	2.04%
(5) Compliance and Advisory Costs	The advisor highlights the high administrative burden and the increased monitoring effort associated with the complexity of Section 34a EStG.	12.24%
(6) None of the Above Categories	–	6.12%

This table shows the categories used to code the open-ended responses, based on a predefined set of coding criteria developed by two of the authors. A response was assigned to a category if more than half of the ten independent research assistants classified it accordingly. The column "Share Coded" indicates the percentage of responses assigned to each category.

Appendix

A Control Variables

A.1 Definition

TABLE A1
Control Variables and Definitions

Variable Name	Definition
Male	Dummy variable equal to one if the participant is male.
Age	The age of the participant.
Income	Categorical variable of household net income after taxes and social insurance contributions: less than €1,700, €1,700-€3,599, and €3,600 or more.
Single Household	Dummy variable equal to one if the participant lives in a single household.
University Degree	Dummy variable equal to one if the participant has at least a university degree.
Tax Knowledge	Individual tax knowledge, as indicated by the participants on a scale from 1 (”no knowledge at all”) to 9 (”tax expert/professional”).
Cognitive Ability	Dummy variable equal to one if the participant correctly answers all questions on the simple three-item cognitive reflection test of Frederick (2005).
Loss-averse	Dummy variable equal to one if the participant is (strongly) loss-averse (degree of loss aversion following Karle et al. (2015) > 1.8).
Preference for Prepayment	Based on Patrick and Park (2006), we asked the participants to imagine that they plan a one-week vacation trip to the Caribbean in six months. They were then informed that the purchase would cost €1,200 and that they have two options for financing this cost: (1) in six monthly payments of €200 starting six months before the planned vacation or (2) in six monthly payments of €200 for six months after the planned vacation. The binary variable *Preference for Prepayment* equals one if the payments are chosen before the planned vacation.
Tax Aversion	Dummy variable equal to one if the participant prefers a tax-free bond to a less favorable taxable bond (Sussman and Olivola 2011).

A.2 Descriptive Statistics

TABLE A2

Descriptive Statistics - Means across Treatments (H1 and H2)

Panel A: Dependent Variables

	Choice			Corporate Tax Rate Misperception		
	Partnership (*Choice Part*)	**Corporation**	**Indifferent**	**Overestimate**	**Underestimate**	**n**
Treatment						
High TRC & High TTC	0.464	0.384	0.152	0.304	0.624	125
Low TRC & High TTC	0.298	0.430	0.273	0.099	0.719	121
High TRC & Low TTC	0.390	0.325	0.285	0.252	0.618	123
Low TRC & Low TTC	0.200	0.383	0.417	0.125	0.592	120

Panel B: Controls

		Treatments			
	All	High TRC High TTC	Low TRC High TTC	High TRC Low TTC	Low TRC Low TTC
Male	0.616	0.664	0.620	0.569	0.608
Age	36.52	35.5	37.2	37.5	35.9
Income €1,700 and less	0.176	0.184	0.165	0.195	0.158
Income €1,700 - €3,599	0.399	0.384	0.397	0.447	0.367
Income €3,600+	0.425	0.432	0.438	0.358	0.475
Single Household	0.252	0.232	0.281	0.301	0.192
University Degree	0.556	0.512	0.587	0.593	0.533
Tax Knowledge	0.452	0.464	0.496	0.439	0.408
Cognitive Ability	0.368	0.352	0.430	0.341	0.350
Loss-averse	0.452	0.432	0.537	0.407	0.433
Preference for Prepayment	0.808	0.808	0.785	0.854	0.783
Tax Aversion	0.669	0.648	0.636	0.740	0.650
Observations	489	125	121	123	120

Panel A presents descriptive statistics on participants' final-round choices between the two tax systems and their corporate tax rate misperceptions. *Overestimate* (*Underestimate*) equals one if a participant reported a tax rate more than 0.5 percentage points above (below) the true rate of 47.5%, based on elicitation questions following rounds three and four. TRC (TTC) is the corporate tax rate (time) complexity. Panel B contains the means of our control variables (defined in Section A.1) across treatments.

TABLE A3
Descriptive Statistics - Means (H3)

	One vs. Two Taxes
Male	0.608
Age	36.94
Income €1,700 and less	0.092
Income €1,700 - €3,599	0.385
Income €3,600+	0.523
Single Household	0.208
University Degree	0.492
Tax Knowledge	0.577
Cognitive Ability	0.377
Loss-averse	0.446
Preference for Prepayment	0.731
Tax Aversion	0.700
Observations	130

Notes: This table contains the means of our control variables (defined in Section A.1).

TABLE A4
Descriptive Statistics - Means across Treatments (H4)

		Treatments	
	All	Liquidity No Shock	Liquidity Shock
Male	0.633	0.643	0.622
Age	37.67	37.93	37.40
Income €1,700 and less	0.122	0.112	0.133
Income €1,700 - €3,599	0.331	0.301	0.363
Income €3,600+	0.547	0.587	0.504
Single Household	0.252	0.210	0.296
University Degree	0.525	0.524	0.526
Tax Knowledge	0.493	0.510	0.474
Cognitive Ability	0.421	0.378	0.467
Loss-averse	0.475	0.462	0.489
Preference for Prepayment	0.766	0.727	0.807
Tax Aversion	0.741	0.755	0.726
Observations	278	143	135

Notes: This table contains the means of our control variables (defined in Section A.1) across treatments.

TABLE A5
Descriptive Statistics - Means across Treatments (H5)

		Treatments	
	All	Experience	No Experience
Male	0.610	0.594	0.627
Age	37.14	37.51	36.76
Income €1,700 and less	0.193	0.203	0.183
Income €1,700 - €3,599	0.398	0.398	0.397
Income €3,600+	0.409	0.398	0.421
Single Household	0.244	0.281	0.206
University Degree	0.606	0.594	0.619
Tax Knowledge	0.480	0.445	0.516
Cognitive Ability	0.354	0.391	0.317
Loss-averse	0.449	0.375	0.524
Preference for Prepayment	0.780	0.727	0.833
Tax Aversion	0.720	0.703	0.738
Observations	254	128	126

Notes: This table contains the means of our control variables (defined in Section A.1) across treatments.

TABLE A6
Evaluation Survey

Panel A: Hypotheses H1 and H2

		Treatments				
	All	High TRC High TTC	Low TRC High TTC	High TRC Low TTC	Low TRC Low TTC	Partnership
Male	0.628	0.627	0.635	0.642	0.604	0.635
Age	37.51	37.41	37.52	37.70	37.90	36.99
Income €1,700 and less	0.146	0.196	0.154	0.094	0.151	0.135
Income €1,700 - €3,599	0.441	0.471	0.346	0.453	0.491	0.442
Income €3,600+	0.414	0.333	0.5	0.453	0.358	0.423
University Degree	0.421	0.294	0.442	0.396	0.566	0.404
Tax Knowledge	0.582	0.686	0.538	0.585	0.642	0.462
Observations	261	51	52	53	53	52

Panel B: Hypothesis 3

		One vs. Two Taxes	
Treatment	All	Corporation	Partnership
Male	0.635	0.635	0.635
Age	37.13	36.42	37.83
Income €1,700 and less	0.221	0.269	0.173
Income €1,700 - €3,599	0.385	0.385	0.385
Income €3,600+	0.394	0.346	0.442
University Degree	0.490	0.462	0.519
Tax Knowledge	0.538	0.500	0.577
Observations	104	52	52

Notes: These tables contain the means of our control variables (defined in Section A.1) across treatments. TRC (TTC) is the tax rate (time) complexity.

Online Appendix to:

Choosing the Wrong Box? Behavioral Frictions and Limits of Tax Advice in Tax Regime Choice

This appendix contains the analysis of tax return data (Section A), analyses of additional experimental treatments (Section B), the experimental instructions (Section C), screenshots of oTree (Section D), the experimental questionnaire (Section E), the questionnaire of the survey of tax advisors (Section F), and the questionnaire of the evaluation survey (Section G). The presented experimental procedures and questions were originally written in German and translated into English. We show information that is identical across treatments and experiments, and show specific treatment manipulations in square brackets and indicate when information differs across the treatments.

A Analysis of Tax Return Data

A.1 Data

To empirically analyze how many taxpayers opt for corporate taxation under the German check-the-box rule, and to study the determinants of this choice, we use the German Taxpayer Panel, an administrative dataset provided by the Federal Statistical Office of Germany. The Taxpayer Panel is based on all individual income tax returns in Germany. The unit of observation is the taxpayer, i.e., either a single individual or a couple filing jointly. Taxpayers are included in the panel if at least two consecutive years of data are available for the taxpayer. The data contains detailed tax return information on each taxpayer such as sources of income, special expenses, taxable income, and tax liability. In addition, some socio-demographic information such as age, gender, marital status and number of children is included.

We use a 5% stratified random sample of the Taxpayer Panel that covers the years from 2005, three years prior to the introduction of the German check-the-box rule, to 2018. Our sample (unbalanced panel) includes, on average, 728,449 observations per year representing a weighted sample of 6,268,582 entrepreneurs in Germany. We restrict our sample to those taxpayers who are entitled to use the check-the-box rule. These are entrepreneurs with positive income either from business, agriculture and forestry, or self-employment.[1]

To obtain a balanced panel dataset for our study on the determinants of tax system choice, we excluded observations that lacked complete data for our regression analysis in at least one year of the observation period (2008 to 2018).[2] Our balanced sample thus includes 336,525 observations per year representing a weighted sample on 3,094,225 entrepreneurs.

A.2 Variable Measurement and Estimation Strategy

A.2.1 Variable Measurement

The dependent variable *Choice Part* is a dummy variable that equals one for each year in which the taxpayer did not opt to tax retained earnings according to the corporate tax system.

To examine the determinants of the check-the-box choice, we include a set of tax case characteristics and taxpayer characteristics. A detailed overview of all variable definitions is provided in Table 1. As tax case variables, we control for the marginal income tax rate (*MTR*), since opting for corporate taxation is only beneficial above certain thresholds and becomes increasingly attractive as the MTR rises. We also include a measure of MTR instability (*MTR Risk*) to capture the risk that a declining MTR may eliminate the corporate tax benefit. Further, we consider current profit levels (*Profit*) as the size of the tax benefit scales with taxable income, and include two risk measures: *Profit Uncertainty* and *Loss Probability*, which capture income volatility and the likelihood of future losses. Finally, we include a proxy for tax compliance costs (*Compliance Costs*) to capture potential

[1] In case of partnerships, we further check for a minimum current profit of €10,000 (according to Sec. 34a (1) S. 3 of the German income tax code).

[2] This includes all taxpayers from the federal state North Rhine-Westphalia, as there are missings in the Taxpayer Panel due to data delivery problems at the federal statistical office of North Rhine-Westphalia in the years from 2008 to 2010.

administrative burdens associated with opting for corporate taxation.

As taxpayer characteristics, we include a measure of prior use of the check-the-box rule (*Experience*), which may reduce perceived uncertainty and increase the likelihood of choosing the corporate regime. We also include a proxy for tax system familiarity (*Tax Literacy*) based on the use of various tax planning items. To account for household-related factors that may influence liquidity needs and planning behavior, we control for whether the taxpayer has children (*Children*), is married and files jointly (*Joint*), and the taxpayer's age (*Age*). Taxpayers with children may be more likely to face unexpected consumption needs, increasing the likelihood of early profit withdrawals and thus reducing the attractiveness of the corporate tax system. Joint taxation may reduce this pressure due to income pooling within the household, potentially increasing the willingness to retain earnings. Age serves as a proxy for the expected investment horizon: older taxpayers may have a shorter remaining planning period, reducing the expected benefit from deferring taxes under the corporate regime. Definitions of all variables can be found in Table 1. Summary statistics of the variables used in our balanced panel are provided in Table 2.

TABLE 1
Variables and Definitions

Panel A: Tax Case Characteristics

Variable Name	Definition
MTR44.31 & MTR47.5	Binary variables indicating whether the taxpayer is in one of the two highest tax brackets of the German income tax schedule, where the marginal income tax rate (MTR) is 44.31% and 47.5%, respectively.
MTR Risk	Dummy variable that equals one if the MTR has declined in at least one of the previous three years.
Profit	Sum of profits eligible for using the check-the-box rule.
Profit Uncertainty	Dummy variable equal to one if the profit has declined in at least one of the previous three years.
Loss Probability	Number of losses within the previous three years.
Compliance Costs	Dummy variable equals one if the taxpayer earns income from agriculture and forestry or self-employment (e.g., lawyers or physicians). These taxpayers typically determine their tax base using either cash-based accounting (self-employment) or estimated average revenues (agriculture and forestry). Opting for corporate taxation requires switching to accrual-based accounting, which is costlier. Blaufus and Hoffmann (2020) estimate that cash-based accounting reduces external compliance costs of small firms by about 30%. Since these taxpayers are not obliged to use accrual-based accounting, most would need to switch accounting methods if they opt for corporate taxation. In contrast, business income earners are generally required to use accrual-based accounting, except for small sole proprietorships with profits below €60,000 and sales below €600,000.

Panel B: Taxpayer Characteristics

Variable Name	Definition
Experience	Dummy variable that equals one in all years after the first time opting for the corporate tax system.
Tax Literacy	Dummy variable that equals one if the taxpayer filed more than nine specific tax items in the past three years. These items reflect the use of optional tax planning opportunities and serve as a proxy for tax familiarity. They include: donations, income from capital investments, tax relief for household-related services, tax relief for cultural assets, tax relief for estate used for own residential purposes, loss carrybacks tax planning, add-on taxes, added foreign tax, added foreign withholding tax, tax-exempt income according to double taxation agreements.
Children	Dummy variable indicating whether the taxpayer has children.
Joint	Dummy variable indicating whether the taxpayer is married and uses joint filing.
Age	Reported age of the taxpayer.

TABLE 2
Descriptive Statistics

Variable	Mean	SD	p25	p50	p75
Choice Part	0.992	0.090	1.000	1.000	1.000
MTR44.31	0.491	0.500	0.000	0.000	1.000
MTR47.5	0.094	0.292	0.000	0.000	0.000
Compliance Costs	0.488	0.500	0.000	0.000	1.000
Loss Probability	0.155	0.489	0.000	0.000	0.000
Profit (tEUR)	171.375	784.193	14.974	66.474	192.000
MTR Risk	0.303	0.459	0.000	0.000	1.000
Profit Uncertainty	0.677	0.468	0.000	1.000	1.000
Experience	0.015	0.120	0.000	0.000	0.000
Tax Literacy	0.015	0.121	0.000	0.000	0.000
Children	0.517	0.500	0.000	1.000	1.000
Joint	0.677	0.468	0.000	1.000	1.000
Age	52.390	11.297	45.000	52.000	60.000
Observations	3,701,776				

This table presents descriptive statistics for all variables used in our regression analysis (balanced sample). All variables are defined in Section A.2.1.

A.2.2 Estimation Strategy

To examine the determinants of the check-the-box choice, we estimate the following random effects logistic panel regression with clustered standard errors at the participant level.[3]

$$\begin{aligned} ChoicePart_{i,t} = \alpha &+ \beta_1 \cdot MTR42_{i,t} + \beta_2 \cdot MTR45_{i,t} + \beta_3 \cdot ComplianceCosts_{i,t} + \\ &\beta_4 \cdot LossProbability_{i,t} + \beta_5 \cdot Profit_{i,t} + \beta_6 \cdot MTR\ Risk_{i,t} + \\ &\beta_7 \cdot ProfitUncertainty_{i,t} + \beta_8 \cdot Experience_{i,t} + \beta_9 \cdot TaxLiteracy_{i,t} + \\ &\beta_{10} \cdot Children_{i,t} + \beta_{11} \cdot Joint_{i,t} + \beta_{12} \cdot Age_{i,t} + \epsilon_{i,t} + u_i \end{aligned} \tag{1}$$

[3] In addition, to test whether our findings are affected by unobservable (time-invariant) factors, we also conduct a logistic panel regression with fixed effects. The results (untabulated) remain qualitatively unchanged.

A.3 Empirical Results

A.3.1 Adoption of the Corporate Tax Option and Forgone Tax Benefits

Based on our unbalanced panel, Table 3 presents the number of taxpayers opting for the corporate tax system each year, as well as the average percentage of profit to which the option was applied. The results reveal that even in the top tax bracket, the option is used surprisingly rarely; only 5.6% of potential applicants choose 8.2% of potential profits to be taxed according to the corporate tax system. Since the introduction of the check-the-box rule in 2008, only just over 6,200 entrepreneurs have made use of the option per year which is far below the legislator's expectation of 90,000 applications per year (Federal Council 2007, p. 62). Moreover, the low number of entrepreneurs opting for the corporate tax system cannot be attributed to a lack of awareness. In fact, both the number of applicants and the share of profits taxed under the corporate regime have declined over time.

To measure how much tax benefit taxpayers forgo by not opting for the corporate tax system, we adopt a conservative approach by restricting our analysis to entrepreneurs of commercial companies, as they do not incur additional compliance costs from accrual-based accounting. For these taxpayers, we first identify the total amount of income subject to the 47.5% top marginal income tax rate, since at this rate, opting for the corporate tax system becomes advantageous even for very short investment periods— typically between one and two years, depending on the rate of return. Then we determine the amount of business profits that is not taxed according to the corporate tax system. We find that every year, business income in the amount of between €15.6 billion and €30.0 billion is subject to partnership tax rates although taxpayers could have opted for the advantageous corporate tax system. Next, we approximate the average investment period for the retained earnings. Of the €49.8 billion retained profits that are taxed according to the corporate tax system since 2008, only €8.4 billion has been taxed again as dividend until 2018 (the end of our observation period). These were retained in the company for an average of 5.6 years. To obtain a lower-bound estimate, we assume that all profits are distributed as dividends in the year 2019 (the year after our observation

Table 3: Use of the German Check-the-box Rule per year

Marginal Income Tax Rate	**< 44.31%**	**44.31%**	**47.5%**	$\sum$
Average Taxpayers 2008 to 2018				
Potential users	4,218,127	766,706	63,190	5,048,023
Actual users	143	2,511	3,567	6,221
	0.0%	0.3%	5.6%	0.1%
Average Profits 2008 to 2018				
Potential profits (mEUR)	78,643	81,723	52,815	213,180
Used profits (mEUR)	3	199	4,323	4,525
	0.0%	0.2%	8,2%	2,1%

Notes: This table shows the average annual number of taxpayers that opted for corporate taxation according to the German check-the box rule (Sec. 34a German income tax code) and the average percentage of profit for which the option was used. The numbers are based on all data available in the TPP from 2008 to 2018 (unbalanced panel).

period ends). In this case, we obtain an average investment period of six years. Using the six-year investment period would imply that the entrepreneurs forgo tax benefits with a total present value of at least €381 million per year if we assume an average investment return of 6%.

A.3.2 Determinants of the Corporate Tax Choice

The results of the regression according to equation (1) based on our balanced panel are presented in Table 4. Regarding tax case characteristics, we find that entrepreneurs in one of the two top-income tax brackets (*MTR44.31* and *MTR47.5*) are significantly less likely to choose the partnership tax system ($p < 0.01$). On average, the probability of choosing the partnership tax system is 8.2 [2.1] percentage points lower for taxpayers with a MTR of 47.5% [44.31%]. It also makes a difference whether the entrepreneur is subject to a marginal tax rate of 44.31% or 47.5%. The probability of choosing the partnership tax system is significantly lower for taxpayers that are subject to a marginal income tax rate of 47.5% versus 44.31% ($p < 0.01$). Interestingly, *MTR Risk* has no effect on the choice of the tax system, while *Profit Uncertainty* does. In addition, a higher profit reduces the probability to choose the partnership tax system and *Loss Probability* increases the probability of choosing the partnership tax system. Finally, compliance costs associated with choosing the corporate tax system significantly increase the probability to choose the partnership tax system.

TABLE 4
Random-Effects Logistic Regression Results

	(1) Logit Choice Part	(2) Average Marginal Effects Choice Part
MTR44.3	-5.311***	-0.0208***
	(0.142)	(0.000859)
MTR47.5	-7.491***	-0.0816***
	(0.154)	(0.00393)
Compliance Costs	3.734***	0.00749***
	(0.0736)	(0.000154)
Loss Probability	0.297***	0.000767***
	(0.0409)	(0.000107)
Profit	-0.000145***	-0.000000***
	(0.000024)	(0.000000)
MTR Risk	-0.0187	-0.000036
	(0.0358)	(0.000092)
Profit Uncertainty	0.197***	0.000508***
	(0.0248)	(0.000064)
Experience	-1.559***	-0.00561***
	(0.0572)	(0.000334)
Tax Literacy	-0.369***	-0.00104***
	(0.0845)	(0.000287)
Children	0.160***	0.000416***
	(0.0495)	(0.000130)
Joint	-0.608***	-0.00149***
	(0.0532)	(0.000125)
Age	0.0963***	0.000249***
	(0.00377)	(0.00001)
Constant	10.763***	
	(0.206)	
Chi-Square	9,807.733***	9,807.733***
Observations	3,701,766	3,701,766
Wald-Test (p-value)		
MTR47.5 = MTR44.3	0.000	0.000

Notes: This table shows the results of the random-effects logistic estimation using the dependent variable Corporation (balanced sample). All variables are defined in Table 7 in the Appendix. Model (1) provides coefficients of random-effects logistic estimation and Model (2) provides average marginal effects (AMEs). Robust clustered standard errors are in parentheses. ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively.

Regarding individual taxpayer characteristics, we find that experience with corporate taxation and tax literacy reduce the probability to choose the partnership taxation. Furthermore, also *Children*, *Joint*, and *Age* are significant determinants and have the expected sign.

B Additional Experimental Analyses

B.1 Uncertainty

Future business income is uncertain. While income uncertainty does not depend on the choice of the tax system, it may affect that choice. Uncertainty increases the complexity of the decision environment and thus increases background complexity.[4] According to the *Behavioral Taxpayer Response Model* (Blaufus et al. 2022), background complexity is another important determinant of tax misperception (e.g., Ackermann et al. 2013; Abeler and Jäger 2015). Thus, uncertainty may strengthen corporate tax misperception and should increase the preference for taxation under partnership rules rather than corporate taxation.

To investigate if income uncertainty influences the choice of the tax system, we carried out an additional treatment that removes business income uncertainty with 123 participants (*Deterministic*).[5] This treatment was identical to the *High TRC & High TTC* treatment in all respects, including the tax complexity structure and the absence of a corporate tax benefit. The only difference was the treatment of business income uncertainty: while participants in the *High TRC & High TTC* treatment were informed only about the distribution of potential profits in each period, participants in the new treatment were informed about the exact sequence of profits they would receive in each future period before making their tax system choice. Panel A of Table 5 reports descriptive statistics for the two treatments.

To examine the effect of income uncertainty on tax system choice, we compared participants' decisions across treatments (see Panel B of Table 5). The results show no effect of business income uncertainty on the probability of choosing the partnership tax system.

[4] In this vein, uncertainty is used as one component of complexity measures (e.g., Hoppe et al. 2023).

[5] We recruited participants for this experiment through the survey platform Bilendi & respondi. On average, participants received total compensation of €10.54 (SD 8.72). The median time required to complete the experiment and questionnaire was 34.8 minutes, resulting in a median hourly wage of €18.17. All participants were 18 years or older and were native speakers of German. The majority of participants were male (61.8%), and the mean age of participants was 36.1 years (SD 11.4).

TABLE 5

Panel A: Descriptive Statistics – Means across Treatments

Treatment	Partnership (*Choice Part*)	Corporation	Indifferent	n
Uncertain[a]	0.464	0.384	0.152	125
Deterministic	0.447	0.374	0.179	123

Panel B: OLS Regression with *Choice Part* as the Dependent Variable

	Predicted Sign	Coef.	Robust Std. Err.	p−value
Intercept	+/-	0.738	0.176	< 0.001
Uncertain[a]	+	0.006	0.064	0.927
Controls				YES
Adjusted R^2 (%)				1.13
n				248

Panel A presents descriptive statistics on participants' final-round choices between the two tax systems (Partnership vs. Corporation). Panel B reports results from an OLS regression using robust standard errors; all p-values are two-tailed. *Choice Part* is one if the partnership system is chosen. Our control variables are *Male*, *Age*, *Income*, *Single Household*, *University Degree*, *Tax Knowledge*, *Cognitive Ability*, *Loss-averse*, *Preference for Prepayment*, and *Tax Aversion*. These variables are defined in Appendix A.1 of the main manuscript.

[a] This treatment is the same as *High TRC & High TTC*.

B.2 Corporate Tax Benefit

To test whether a corporate tax benefit increases the probability of choosing the partnership tax system, we use three treatments that differ only in the design of the corporate tax benefit (CTB). In the benchmark treatment, *No CTB*, both tax systems are economically equivalent.[6] In *CTB Interest*,the tax burden under both the corporate and partnership systems is 47.5%. However, because retained earnings earn interest at a rate of 20% per period, the resulting CTB is positive.[7] In *CTB Corp. Tax Rate*, the partnership tax rate remains at 47.5%, whereas the corporate income tax rate is lowered from 30% to 15%, yielding a total corporate tax burden of 36.25%, calculated as $15\% + 25\% \times (1 - 15\%)$. Next, we compare participants' preference for a partnership tax system between those who receive a corporate tax benefit through interest on retained earnings or a reduced corporate tax benefit and those who do not.

[6]This treatment corresponds exactly to the *High TRC & High TTC* treatment; it was merely renamed here for consistency with the corporate tax benefit framing.

[7]This treatment corresponds exactly to the *No Experience* treatment.

TABLE 6
Results Hypothesis 1

Panel A: Descriptive Statistics – Means across Treatments

Treatment	Partnership (*Choice Part*)	Corporation	Indifferent	n
No CTB[a]	0.464	0.384	0.152	125
CTB Interest[b]	0.328	0.484	0.188	128
CTB Corp. Tax Rate	0.225	0.651	0.124	129

Panel B: OLS Regression with *Choice Part* as the Dependent Variable

	Predicted Sign	Coef.	Robust Std. Err.	p−value
Intercept	+/-	0.685	0.133	< 0.001
CTB Interest[b]	- (H1a)	−0.133	0.061	0.031
CTB Tax Rate	- (H1b)	−0.223	0.057	< 0.001
Controls				YES
Adjusted R^2 (%)				6.58
n				382

Panel A presents descriptive statistics on participants' final-round choices between the two tax systems (Partnership vs. Corporation). Panel B reports results from an OLS regression using robust standard errors; all p-values are two-tailed. *Choice Part* is one if the partnership system is chosen. *No CTB*, *CTB Interest*, and *CTB Corp. Tax Rate* indicate treatment assignment and differ only in the corporate tax benefit (CTB): none (systems economically equivalent), interest on retained earnings, or a reduced corporate tax rate (30% to 15%). Our control variables are *Male*, *Age*, *Income*, *Single Household*, *University Degree*, *Tax Knowledge*, *Cognitive Ability*, *Loss-averse*, *Preference for Prepayment*, and *Tax Aversion*. These variables are defined in Appendix A.1 of the main manuscript.

[a] This treatment is the same as *High TRC & High TTC*.

[b] This treatment is the same as *No Experience*.

Panel A of Table 6 shows that the choice of the partnership tax system decreases in the presence of a corporate tax benefit (CTB). While 46.4% choose the partnership in the absence of a CTB, this share drops to 32.8% with an interest-based CTB and to 22.5% when the CTB is implemented via a reduced corporate tax rate. The OLS regression results in Panel B confirm that this relationship is statistically significant. Thus, the monetary corporate tax benefit has a significant impact on the choice between both tax systems. However, even in the treatment with a substantial CTB resulting from a reduced corporate tax rate, only 65% of participants choose the corporate tax system. This underscores the impact of behavioral frictions on the decision-making process between the two tax regimes in a check-the-box scenario.

C Experimental Instructions

C.1 Welcome Page

Welcome to our Study

Thank you for participating in this study. Before the study begins, please read the following carefully.

1. Procedure and Duration

In this study you have to make some economic decisions. Furthermore, there are some questions regarding socio-demographic characteristics (e.g. age). Please answer all questions carefully and pay attention to the attention check questions, which are designed to sharpen your attention. In total, the study should take about 40 minutes.

2. Purpose of this Research Study

This study examines consumption and investment behavior as part of a scientific research project.

3. Compensation

You will receive a fixed compensation of €4.00 for completing the study. In addition, you will receive a variable compensation. The amount depends on your decisions and luck. In the following instructions, you will learn how your decisions can influence your variable compensation. The average variable compensation is around €5.20. The total average compensation in this study is therefore €9.20.

Please note the following: We attach great importance to you conscientiously completing the task in this study and answering the questions honestly. Therefore, we will pay you an appropriate compensation. We will not pay any compensation in the following cases:

- **You do not read the instructions carefully.**
- **You do not read the questions carefully or answer not conscientiously.**

Participation in this study is completely voluntary. If you stop the study in between, you will not be penalized, but you will not receive any compensation either.

4. Benefit of the Study

This study will help the researchers involved to learn more about human behavior in the context of corporate activities. We hope that in the future, firms and lawmakers will benefit from this study through a better understanding of investment behavior.

5. Confidentiality

The information you provide will be kept strictly confidential. Only the project manager and his or her staff will have access to the raw data. Anonymized data from this study may be shared with qualified researchers or research institutions when deemed appropriate in accordance with academic association, journal, or university policies. All reports from this study will be at an aggregate level and/or with individual information anonymized or disguised so that participants cannot be identified.

6. Declaration of Consent

By clicking on *Next* you confirm that you have read the points above and that you agree to participate in the study.

C.1.1 Instructions Training Round

Structure of the Study

The study consists of several comprehension tests, a training round, four decision rounds, and a subsequent questionnaire. Both the training round and the four decision rounds include five periods each.

You earn a profit in each period. The profits are given in a fictitious currency, which we call "ECU". 1,000 ECU correspond to €2.50. Your actual compensation is calculated at the end of the study from the "earned ECU" and is then converted into Euros.

Below you will receive instructions that apply to the training round as well as the subsequent decision rounds.

Training round

1. The Situation:

A decision round always contains 5 periods. In each of the 5 periods you earn a profit (see point 2). Your task is to decide how much of the profit of one period you want to put aside for future periods (= building up of reserves). Reserves can be released in subsequent periods as you wish (= release of reserves).

[All treatments except *CTB Interest*: The profit less the building up of reserves plus the release of reserves is called the payout:

payout = profit - build up of reserve + reserve release]

[Treatment *CTB Interest*: You receive interest on the reserves in each period. The profit plus interest less the building up of reserves plus the release of reserves is called the payout:

payout = profit + interest - build up of reserve + reserve release]

[Treatments *Liquidity (No) Shock*: In each period, a minimum payout of ECU 1200 must generally be achieved. [only in the shock treatment: In the second to fourth round, however, it can amount to ECU 3600 once.] The amount of the minimum payout will be announced at the beginning of each period. If the minimum payout is not reached, you must pay a penalty, which is calculated as follows:

penalty = minimum payout - payout

The profit less the building up of reserves and any penalty plus the release of reserves is called the payout:

payout = profit - build up of reserve + reserve release - penalty

Example: The minimum payout is 1,200 ECU, but your profit is only 1,000 ECU. No reserves have been built up or released. In this case, you will incur a penalty of 200 ECU, meaning the payout will be 800 ECU.]

2. Your Profit:

Treatments with uncertain income: The following table shows you the amount of profit you can earn in one period. You cannot influence the amount of profit yourself. For each period your profit

is determined randomly according to the following table. This means that the profit can vary from period to period. Note that the probability for each possible profit is the same.

Profit	Probability
0 ECU	1/7 (≈ 14.29%)
1,000 ECU	1/7 (≈ 14.29%)
2,000 ECU	1/7 (≈ 14.29%)
3,000 ECU	1/7 (≈ 14.29%)
4,000 ECU	1/7 (≈ 14.29%)
5,000 ECU	1/7 (≈ 14.29%)
6,000 ECU	1/7 (≈ 14.29%)

[Treatment with certain income: The following table shows you how much the profits are in each period of the training round.

Period	Profit
1	3,000 ECU
2	6,000 ECU
3	0 ECU
4	4,000 ECU
5	2,000 ECU

]

3. Build up and Release of Reserves:

In the first 4 of the total 5 periods, you have the possibility to build up reserves from the profit of a period. The payout in the respective period is reduced accordingly by the built reserve. The built reserves are added to a reserve account. [Treatment *CTB Interest*: The interest on the reserves in this study is 20% per period.]

You can release the reserves in your reserve account in any period in any amount. When you release reserves, this increases the payout in the period accordingly. In the last period of each decision round (period 5), you can no longer build up reserves. Instead, all reserves built up to that

point in the reserve account and not yet released in previous periods are automatically paid out in the last period.

4. Your Compensation:

Your compensation in this experiment is based on the payout of a randomly drawn period from the four decision rounds. You will receive details after the training round. The training round is not relevant for the payout and only serves to make you more familiar with the structure and content of the study.

5. Training Round:

After you have answered the comprehension questions, a training round will start. This is designed to make you more familiar with the structure and content of the study before the actual study begins. After the training round, you will receive further instructions.

Comprehension Test

Question 1: How many periods are included in the training round and the 4 subsequent decision rounds?

- □ 1
- □ 3
- □ 5

Question 2: Which of the following statements about the profit in a given period is correct?

- □ The profit can range between 0 ECU and 6000 ECU.
- □ The profit can range between 1000 ECU and 5000 ECU.
- □ The profit is the same in every period.

Question 3: Which of the following statements about reserves is correct?

- ☐ All reserves in the reserve account are automatically released in the fifth (i.e., final) period of a round.
- ☐ You can build reserves in all 5 periods of a round.
- ☐ Reserves are never released.

Question 4: Which formula determines the payout in a given period?

- ☐ Payout = Profit [Treatment CTB Interest: + interest] [Treatments Liquidity (No) Shock: - penalty]
- ☐ Payout = Profit [Treatment CTB Interest: + interest] - Reserve Allocation [Treatments Liquidity (No) Shock: - penalty]
- ☐ Payout = Profit [Treatment CTB Interest: + interest] - Reserve Allocation + Reserve Release [Treatments Liquidity (No) Shock: - penalty]

Question 5: Which of the following statements about reserves is correct?

- ☐ You do not receive interest on reserves.
- ☐ The reserves earn 20% interest per period in this study.

[Treatments *Liquidity (No) Shock*:]

Question 6: Which of the following statements about the minimum payout is correct?

- ☐ The minimum payout is always 1200 ECU.
- ☐ The minimum payout is generally 1200 ECU. In rounds two through four, however, it may be 3600 ECU once.
- ☐ The minimum payout is generally 1200 ECU. In rounds one, three, and five, however, it may be 1800 ECU once.

C.2 Instructions - Decision Round 1

Instructions - Decision Round 1

After you have become more familiar with the structure and content of the study in the training round, the actual study now begins. You will receive further information on this in the following. There are four decision rounds in total. Each of the four decision rounds contains five periods (20 periods in total). All four decision rounds are identical to the training round. If there are any changes, you will receive further information before the corresponding round.

This first decision round is completely identical to the training round, so you do not need any further information about the process. However, your decisions are now relevant for the compensation at the end of the study. You will receive further information on this on the next screen.

Your Compensation

1. Fixed Compensation:

You will receive a fixed compensation of €4.00.

2. Variable Compensation:

You will also receive a variable compensation. The variable compensation is based on the payout of a randomly drawn period of all four decision rounds. Each period is drawn with equal probability. Consequently, only the payout of one of the 20 periods is remunerated! The payout of the randomly drawn period will be converted into Euro and paid to you as variable remuneration. 1000 ECU correspond to €2.50.

Comprehension Test

Question 1: Which of the following statements regarding variable compensation at the end of the study is correct?

- □ The average payout for all periods is paid at the end of the study.
- □ The average payout of the last decision round is paid at the end of the study.
- □ The payout from one of the 20 periods is paid at the end of the study.

C.3 Instructions - Decision Round 2

[In this decision round, the partnership tax system is shown. In the experiment, however, it was random which of the two tax systems appeared in this round.]

Instructions - Decision Round 2

Below you will find more information about this decision round.

1. This Decision Round:

The following decision round is identical in its procedure to the training round. However, your profit is now subject to taxation. All taxes paid by you and the other participants in this study are used to finance the conducting of this study and further research projects. You will find more information on taxation below.

2. Payout:

Due to the taxation of profits, the payout is now as follows:

Payout = profit [Treatment *CTB Interest*: + interest] - taxes - reserve accumulation + reserve release [Treatments *Liquidity (No) Shock*: - penalty]

[Treatments *Liquidity (No) Shock*: In the following decision round, a minimum payout of ECU 600 must now generally be achieved. [only treatment *Liquidity Shock*: In the second to fourth round, however, it can now amount to ECU 1800 once.]

3. Taxation of Profits:

Your profit [Treatment *CTB Interest*: plus interest] will be taxed in the following decision round as follows:

Tax A:

You pay **Tax A1** of 47.50%. For any tax, the following applies: tax payment = tax rate * tax base.

The tax base for Tax A is the profit. The build up of reserves does not reduce this tax base, and the release of reserves does not increase this tax base.

Example: Your profit is 500 ECU and you build up a reserve in the amount of 200 ECU.

Tax A

Tax base for Tax A:

Profit:	500 ECU
- Built up reserve:	not deductible
Tax base:	500 ECU

Calculation of Tax A:

Tax base for Tax A * Tax rate for Tax A = 500 ECU * 47.50% = 237 ECU

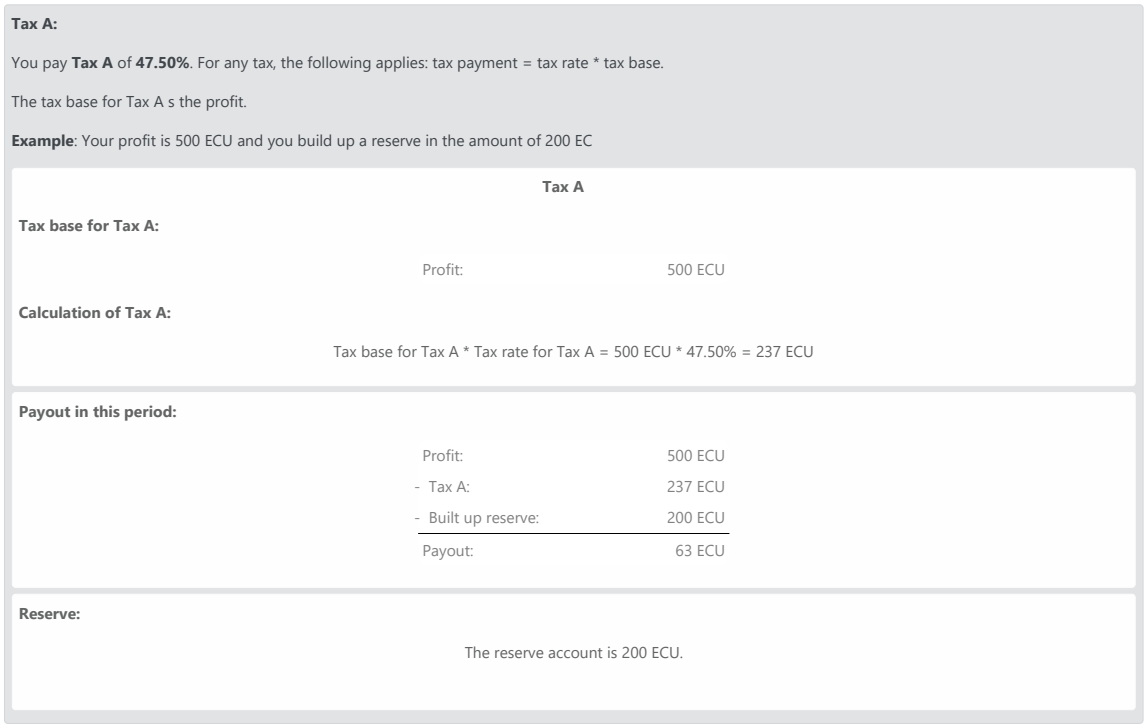
Payout in this period:

Profit:	500 ECU
- Tax A (47.5%):	237 ECU
- Built up reserve:	200 ECU
Payout:	63 ECU

Reserve:

The reserve account is 200 ECU. A later release of the reserve does not increase the tax base A and, accordingly, does not result in any additional tax payment.

[*One vs. Two Taxes*]



Tax A:

You pay **Tax A** of **47.50%**. For any tax, the following applies: tax payment = tax rate * tax base.

The tax base for Tax A s the profit.

Example: Your profit is 500 ECU and you build up a reserve in the amount of 200 EC

Tax A

Tax base for Tax A:

Profit:	500 ECU

Calculation of Tax A:

Tax base for Tax A * Tax rate for Tax A = 500 ECU * 47.50% = 237 ECU

Payout in this period:

Profit:	500 ECU
- Tax A:	237 ECU
- Built up reserve:	200 ECU
Payout:	63 ECU

Reserve:

The reserve account is 200 ECU.

Comprehension Test

Question 1: What is the tax rate for **Tax A**?

- ☐ 15.00%
- ☐ 30.00%
- ☐ 47.50%

[Except in treatment *One vs. Two Taxes*:]

Question 2: Which of the following statements about the **creation of reserves** is correct?

- ☐ Creating reserves does not reduce the tax base for Tax A.
- ☐ Creating reserves reduces the tax base for Tax A.

[Except in treatment *One vs. Two Taxes*:]

Question 3: Which of the following statements about the **release of reserves** is correct?

- ☐ The released reserves do not increase the tax base for Tax A.
- ☐ The released reserves increase the tax base for Tax A.

C.4 Instructions - Decision Round 3

Instructions - Decision Round 3

Below you will find more information about this decision round.

1. This Decision Round:

The following decision round is identical in its procedure to the training round. However, your profit is again subject to taxation. All taxes paid by you and the other participants in this study are used to finance the conducting of this study and further research projects. However, the taxation differs from the last decision round. You will find more information on taxation below.

2. Payout:

Due to the taxation of profits, the payout is now as follows:

Payout = profit [Treatment *CTB Interest*: + interest] - taxes - reserve accumulation + reserve release [Treatments *Liquidity (No) Shock*: - penalty]

[Treatments *Liquidity (No) Shock*: In the following decision round, a minimum payout of ECU 600 must now generally be achieved. [only treatment *Liquidity Shock*: In the second to fourth round, however, it can now amount to ECU 1800 once.]

3. Taxation of Profits:

Your profit [Treatment *CTB Interest*: plus interest] will be taxed in the following decision round as follows:

[*High TTC & High TRC*:]

Tax B1 and Tax B2:

There are two taxes (Tax B1 and Tax B2). For any tax, the following applies: tax payment = tax rate * tax base.
You pay **Tax B1** at the rate of 30.00%. The tax base for Tax B1 is the profit. The build up of reserves does not reduce this tax base, and the release of reserves does not increase this tax base.
You also pay a second **Tax B2** at the rate of 25.00%. The tax base for Tax B2 is the profit **less** the Tax B1 and the built up reserve and **plus** the released reserve.

Example: Your profit is 500 ECU and you build up a reserve in the amount of 200 ECU.

Tax B1

Tax base for Tax B1:

Profit:	500 ECU
- Built up reserve:	not deductible
Tax base:	500 ECU

Calculation of Tax B1:

Tax base for Tax B1 * Tax rate for Tax B1 = 500 ECU * 30.00% = 150 ECU

Tax B2

Tax base for Tax B2:

Profit:	500 ECU
- Tax B1:	150 ECU
- Built up reserve:	200 ECU
Tax base:	150 ECU

Calculation of Tax B2:

Tax base for Tax B2 * Tax rate for Tax B2 = 150 ECU * 25.00% = 37 ECU

Payout in this period:

Profit:	500 ECU
- Tax B1:	150 ECU
- Tax B2:	37 ECU
- Built up reserve:	200 ECU
Payout:	113 ECU

Reserve:

The reserve account is 200 ECU. A later release of the reserve increases the tax base of Tax B2 and results in a tax payment of: 200 ECU * 25.00 % = 50 ECU.

[*High TTC & Low TRC*:]

Tax B1 and Tax B2:

There are two taxes (Tax B1 and Tax B2). For any tax, the following applies: tax payment = tax rate * tax base.
You pay **Tax B1** at the rate of 30.00%. The tax base for Tax B1 is the profit. The build up of reserves does not reduce this tax base, and the release of reserves does not increase this tax base.
You also pay a second **Tax B2** at the rate of 25.00%. The tax base for Tax B2 is the profit **less** the Tax B1. The built up reserve does not reduce the tax base.

Example: Your profit is 500 ECU and you build up a reserve in the amount of 200 ECU.

Tax B1

Tax base for Tax B1:

Profit:	500 ECU
- Built up reserve:	not deductible
Tax base:	500 ECU

Calculation of Tax B1:

Tax base for Tax B1 * Tax rate for Tax B1 = 500 ECU * 30.00% = 150 ECU

Tax B2

Tax base for Tax B2:

Profit:	500 ECU
- Tax B1:	150 ECU
- Built up reserve:	not deductible
Tax base:	350 ECU

Calculation of Tax B2:

Tax base for Tax B2 * Tax rate for Tax B2 = 350 ECU * 25.00% = 87 ECU

Payout in this period:

Profit:	500 ECU
- Tax B1:	150 ECU
- Tax B2:	87 ECU
- Built up reserve:	200 ECU
Payout:	63 ECU

Reserve:

The reserve account is 200 ECU. A later release of the reserve does not increase the tax base B2 and, accordingly, does not result in any additional tax payment.

[*Low TTC & High TRC*:]

Tax B1 and Tax B2:

There are two taxes (Tax B1 and Tax B2). For any tax, the following applies: tax payment = tax rate * tax base.
You pay **Tax B1** at the rate of 30.00%. The tax base for Tax B1 is the profit. The build up of reserves does not reduce this tax base, and the release of reserves does not increase this tax base.
You also pay a second **Tax B2** at the rate of 17.50%. The tax base for Tax B2 is the profit **less** the built up reserve and **plus** the released reserve. The Tax B1 does not reduce the tax base.

Example: Your profit is 500 ECU and you build up a reserve in the amount of 200 ECU.

Tax B1

Tax base for Tax B1:

Profit:	500 ECU
- Built up reserve:	not deductible
Tax base:	500 ECU

Calculation of Tax B1:

Tax base for Tax B1 * Tax rate for Tax B1 = 500 ECU * 30.00% = 150 ECU

Tax B2

Tax base for Tax B2:

Profit:	500 ECU
- Tax B1:	not deductible
- Built up reserve:	200 ECU
Tax base:	300 ECU

Calculation of Tax B2:

Tax base for Tax B2 * Tax rate for Tax B2 = 300 ECU * 17.50% = 52 ECU

Payout in this period:

Profit:	500 ECU
- Tax B1:	150 ECU
- Tax B2:	52 ECU
- Built up reserve:	200 ECU
Payout:	98 ECU

Reserve:

The reserve account is 200 ECU. A later release of the reserve increases the tax base of Tax B2 and results in a tax payment of: 200 ECU * 17.50 % = 35 ECU.

[*Low TTC & Low TRC*:]

Tax B1 and Tax B2:

There are two taxes (Tax B1 and Tax B2). For any tax, the following applies: tax payment = tax rate * tax base.
You pay **Tax B1** at the rate of 30.00%. The tax base for Tax B1 is the profit. The build up of reserves does not reduce this tax base, and the release of reserves does not increase this tax base.
You also pay a second **Tax B2** at the rate of 17.50%. The tax base for Tax B2 is the profit. The built up reserve an the Tax B1 do not reduce the tax base.

Example: Your profit is 500 ECU and you build up a reserve in the amount of 200 ECU.

Tax B1

Tax base for Tax B1:

Profit:	500 ECU
- Built up reserve:	not deductible
Tax base:	500 ECU

Calculation of Tax B1:

Tax base for Tax B1 * Tax rate for Tax B1 = 500 ECU * 30.00% = 150 ECU

Tax B2

Tax base for Tax B2:

Profit:	500 ECU
- Tax B1:	not deductible
- Built up reserve:	not deductible
Tax base:	500 ECU

Calculation of Tax B2:

Tax base for Tax B2 * Tax rate for Tax B2 = 500 ECU * 17.50% = 87 ECU

Payout in this period:

Profit:	500 ECU
- Tax B1:	150 ECU
- Tax B2:	87 ECU
- Built up reserve:	200 ECU
Payout:	63 ECU

Reserve:

The reserve account is 200 ECU. A later release of the reserve does not increase the tax base B2 and, accordingly, does not result in any additional tax payment.

[*One vs. Two Taxes*]

Tax A1 and Tax A2:

You pay **Tax A1** of 30.00% and **Tax A2** of 17.50%. You therefore pay a **total tax** of **47.5%.** For any tax, the following applies: tax payment = tax rate * tax base. The tax base for Tax A1 and Tax A2 is the profit.

Example: Your profit is 500 ECU and you build up a reserve in the amount of 200 ECU.

Tax A1 and Tax A2

Tax bases for Tax A1 and Tax A2:

Profit:	500 ECU

Calculation of Tax A1:

Tax base for Tax A1 * Tax rate for Tax A1 = 500 ECU * 30.00% = 150 ECU

Calculation of Tax A2:

Tax base for Tax A2 * Tax rate for Tax A2 = 500 ECU * 17.50% = 87 ECU

Payout in this period:

Profit:	500 ECU
- Tax A1:	150 ECU
- Tax A2:	87 ECU
- Built up reserve:	200 ECU
Payout:	63 ECU

Reserve:

The reserve account is 200 ECU.

Comprehension Test

[Questions 1 to 6 except in treatment *One vs. Two Taxes*:]

Question 1: What is the tax rate for **Tax B1**?

- ☐ 15.00%
- ☐ 30.00%
- ☐ 47.50%

Question 2: Which of the following statements about the **creation of reserves** is correct with respect to **Tax B1**?

- ☐ Creating reserves does not reduce the tax base for Tax B1.
- ☐ Creating reserves reduces the tax base for Tax B1.

Question 3: What is the tax rate for **Tax B2**?

- □ 17.50%
- □ 25.00%
- □ 47.50%

Question 4: Which of the following statements about **Tax B1** is correct with respect to **Tax B2**?

- □ Tax B1 reduces the tax base for Tax B2.
- □ Tax B1 does not reduce the tax base for Tax B2.

Question 5: Which of the following statements about the **creation of reserves** is correct with respect to **Tax B2**?

- □ Created reserves reduce the tax base for Tax B2.
- □ Created reserves do not reduce the tax base for Tax B2.

Question 6: Which of the following statements about the **release of reserves** is correct with respect to **Tax B2**?

- □ Released reserves do not increase the tax base for Tax B2.
- □ Released reserves increase the tax base for Tax B2.

[Treatment *One vs. Two Taxes*:]

Question 1: How much tax do you pay in total on your profits (**Tax B1 + Tax B2**)?

- □ 15.00%
- □ 30.00%
- □ 47.50%

C.5 Instructions - Decision Round 4

Instructions - Decision Round 4

Below you will find more information about this decision round.

1. This Decision Round:

The following and final decision round is identical in procedure to the previous two decision rounds. However, at the beginning of this decision round you have to decide between the two different taxation options from the last two decision rounds. All taxes paid by you and the other participants in this study are used to finance the conducting of this study and further research projects.

2. Taxation of Profits:

You now have two taxation options (A and B) for the taxation of the profit.

Here again is an overview of the two taxation options:

Taxation option A (as in decision round 2):

You pay Tax A at the rate of 47.50%. For any tax, the following applies: tax payment = tax rate * tax base.

The tax base for **Tax A** is the profit [Treatment *CTB Interest*: plus interest]. The build up of reserves does not reduce this tax base, and the release of reserves does not increase this tax base.

Taxation option B (as in decision round 3):

There are two taxes (Tax B1 and Tax B2). For any tax, the following applies: tax payment = tax rate * tax base.

You pay **Tax B1** at the rate of 30.00% [*CTB Corp. Tax Rate*: 15.00%].

The tax base for Tax B1 is the profit. The build up of reserves does not reduce this tax base, and the release of reserves does not increase this tax base.

[*High TRC & High TTC*:] You also pay a second **Tax B2** at the rate of 25.00%. The tax base for Tax B2 is the profit [Treatment *CTB Interest*: plus interest] **less** the Tax B1 and the built up reserve and **plus** the released reserve.

[*High TRC & Low TTC*:] You also pay a second **Tax B2** at the rate of 25.00%. The tax base for

Tax B2 is the profit **less** the Tax B1. The built up reserve does not reduce the tax base.

[*Low TRC & High TTC*:] You also pay a second **Tax B2** at the rate of 17.50%. The tax base for Tax B2 is the profit **less** the built up reserve **plus** the released reserve. The Tax B1 does not reduce the tax base.

[*Low TRC & Low TTC*:] You also pay a second **Tax B2** at the rate of 17.50%. The tax base for Tax B2 is the profit. The built up reserve and the Tax B1 do not reduce the tax base.

D Screenshots

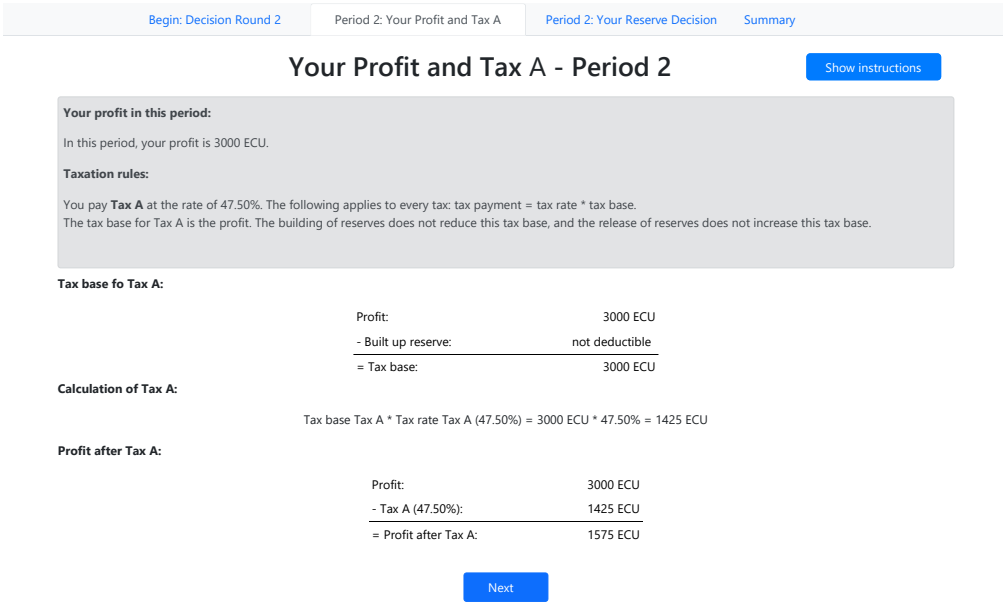


Figure A1: Decision Round - Profit and Tax - Partnership

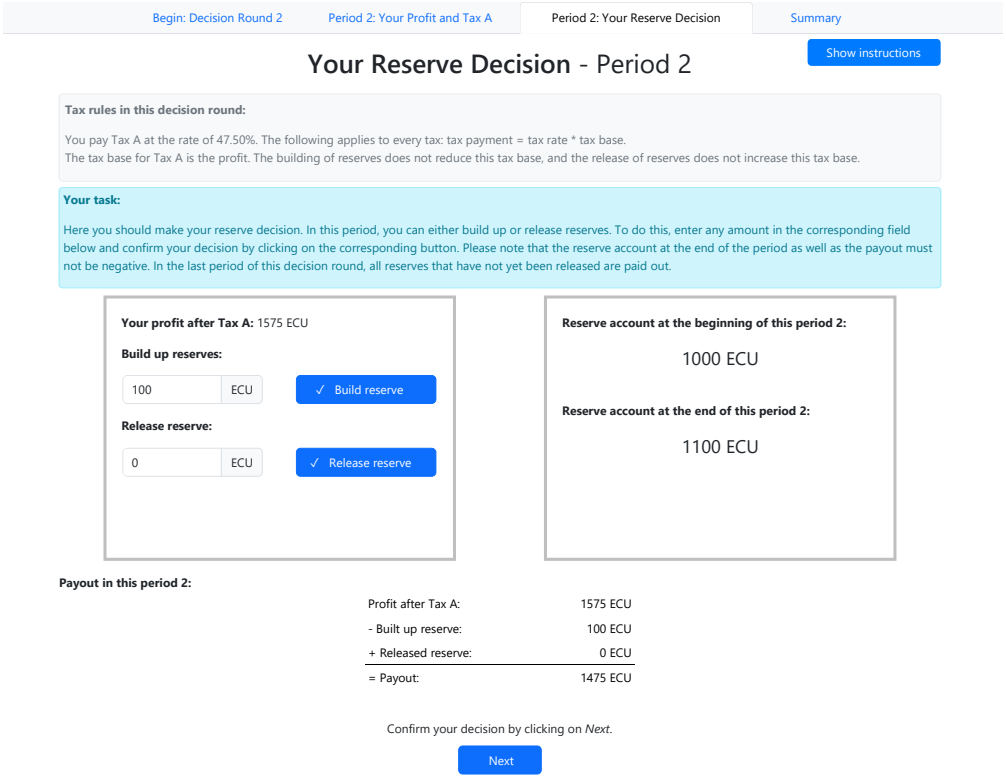


Figure A2: Decision Round - Reserve Decision - Partnership

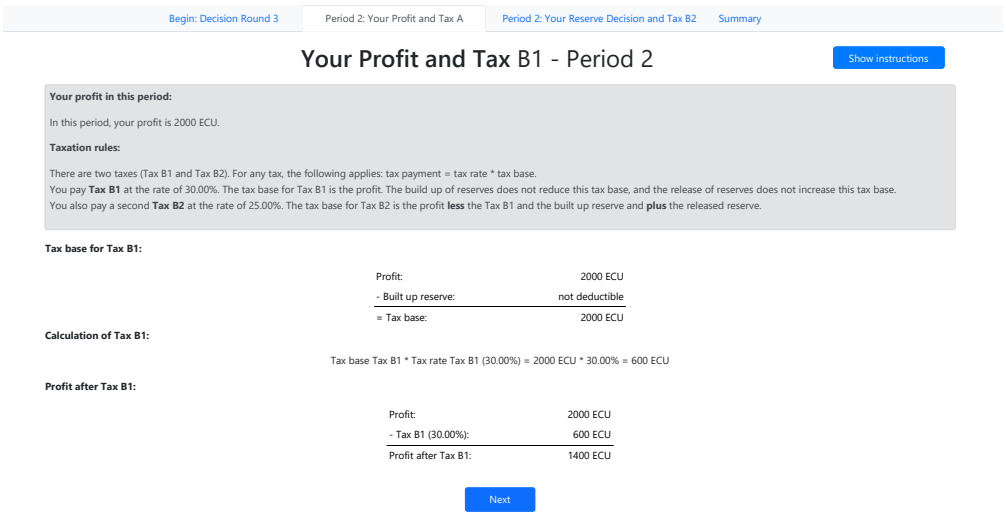


Figure A3: Decision Round - Profit and Tax - Corporation

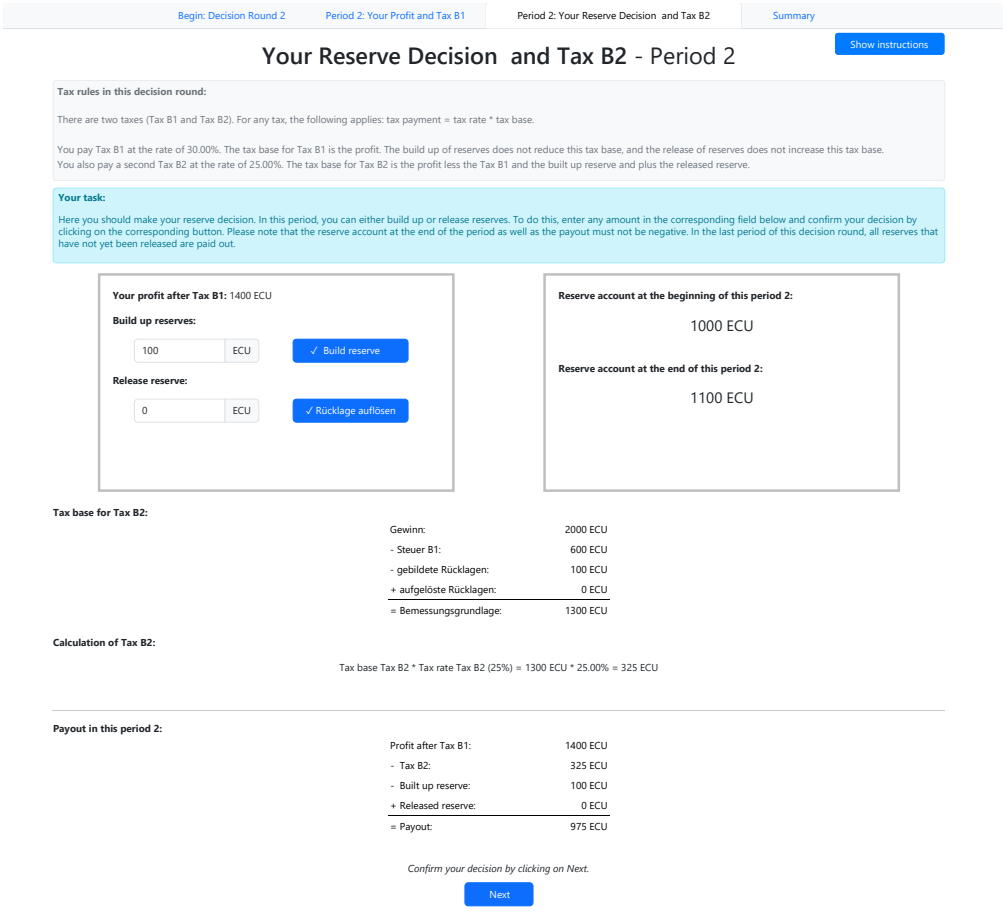


Figure A4: Decision Round - Reserve Decision - Corporation

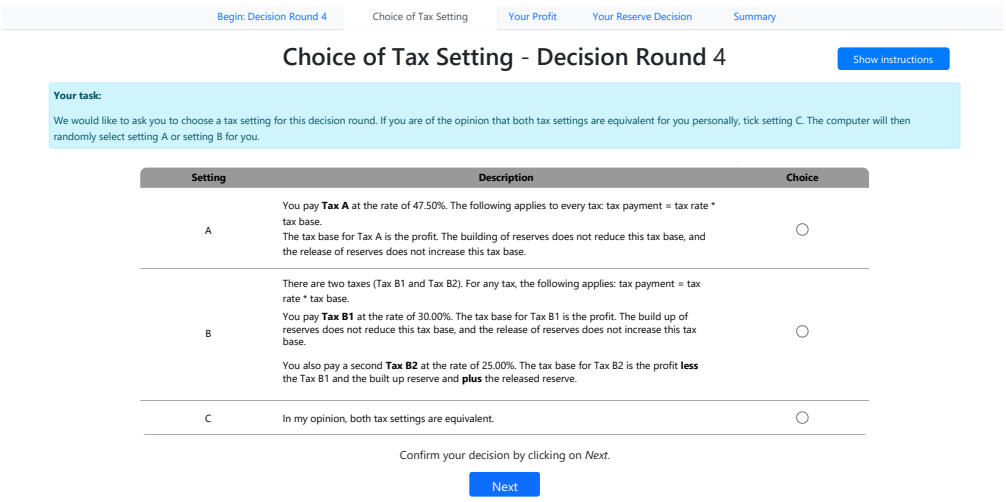


Figure A5: Choice of Tax Setting

E Experimental Questionnaire

E.1 Questions before the Experiment

Question 1: Are you female, male or non-binary?

- ☐ female
- ☐ male
- ☐ non-binary

Question 2: In which year were you born (e.g. 1962)?

☐

Question 3: How do you rate yourself personally: Are you generally a person who is willing to take risks or do you try to avoid taking risks?

not at all willing to take risks ☐—☐—☐—☐—☐—☐—☐—☐—☐—☐—☐ very willing to take risks

Question 4: How would you rate your own tax law knowledge?

no knowledge at all ☐—☐—☐—☐—☐—☐—☐—☐—☐—☐—☐ tax expert/consultant

E.2 Questions after Decision Rounds 2 and 3

If you think back again to the decisions made in this round:

Question 1: How uncertain did you feel about your decision-making situation regarding the payoffs in this decision round?

not at all uncertain ☐—☐—☐—☐—☐—☐—☐—☐—☐—☐—☐ Very uncertain

Question 2: To what extent does the distribution of payoffs across all 5 periods correspond to your initial expectation?

not at all □—□—□—□—□—□—□—□—□—□—□ fully

Question 3: How complicated did you find the taxation of earnings in this decision round?

very simple □—□—□—□—□—□—□—□—□—□—□ very complicated

Question 4: How burdened did you feel by taxes in this decision round?

not burdened at all □—□—□—□—□—□—□—□—□—□—□ very burdened

Question 5: In your opinion, what was the total average tax burden on earnings (Tax A) [Corporation: (Tax A1 and Tax A2)] in this decision round (in %)?

You can earn **more money** with this question. Among the best answers we give away a total of 10 times 50 €.

Only after decision round 2:

Question 6: This question is to check your attention. Please click here on the last answer option (= perfect).

not at all □—□—□—□—□—□—□—□—□—□—□ perfect

E.3 Question after the choice of the tax system

Question 1: Why did you choose this taxation option? (Multiple answers possible)

- ☐ The other system is too complicated for me.
- ☐ Because of the lower total tax burden in this system.
- ☐ I don't want to pay taxes twice.
- ☐ I want to take advantage of the fact that I do not have to pay a tax until the reserve is released.
- ☐ I would like to avoid being charged with an additional tax in case of a small profit.
- ☐ I feel I will earn more with this taxation option.
- ☐ None of the above reasons.

E.4 Questions after the Experiment

Question 1: How old are you?

Question 2: What kind of employment are you in?

- ☐ Pupil
- ☐ University student
- ☐ Employee
- ☐ Public official
- ☐ Freelancer
- ☐ Homemaker
- ☐ Unemployed/job-seeking
- ☐ No longer working (e.g. retired)

Question 3: What is your highest educational qualification?

- □ Secondary modern school qualification (Hauptschule?)
- □ Secondary school certificate
- □ High-school diploma
- □ University of Applied Sciences degree
- □ University degree
- □ Dual university degree
- □ Doctorate

Question 4: What is your marital status?

- □ married/ long-term relationship
- □ single
- □ divorced/widowed

Question 5: How many people are in your household?

- □ 1
- □ 2
- □ 3
- □ 4
- □ 5 or more

Question 6: What is your monthly net household income?

Monthly net household income is the sum of the monthly net incomes of all household members. The monthly net household income is calculated from the gross household income earned (all household income from employment, from assets, from public and non-public transfer payments) less taxes, contributions to health, nursing care, unemployment and statutory pension insurance. A (private) household is defined as any group of persons living together and forming an economic unit (multi-person households).

- □ < €1,300
- □ €1,300 - €1,700
- □ €1,700 - €2,600
- □ €2,600 - €3,600
- □ €3,600 - €5,000
- □ > €5,000

Question 7: Now please imagine that you are planning a one-week vacation trip to the Caribbean in six months. This trip will cost €1,200. You have two options for financing this cost. Which of the following options would you choose?

- □ Six monthly payments of €200 each during the six months before the planned vacation.
- □ Six monthly payments of €200 each during the six months after the planned vacation.

Question 8: How important is it to you personally to save taxes?

not at all important □—□—□—□—□—□—□—□—□—□ very important

Question 9: Imagine that you have just inherited some money that you are planning to invest. You are deciding between two different bond options. Both have the same risk and 10-year maturities. The first bond is expected to pay €401 per year, but you will also be taxed €100 on these earnings each year. The second bond's return is lower, €300 per year, but it will not be taxed. Which bond would you invest in?

- □ I would put my money in the first bond.
- □ I would put my money in the second bond.

Question 10: To what extent do you agree with the following statement: When I buy a larger thing (e.g. TV, fridge, sofa, etc.), I avoid taking out a loan, even though it is interest-free, in order not to be additionally burdened by the repayments of a loan in difficult financial situations (e.g. unemployment or short-time work)?

do not agree at all □—□—□—□—□—□—□—□—□ fully agree

Question 11: Do you agree with the following statements?

	do not agree at all					fully agree
I generally view change as something negative.	☐	☐	☐	☐	☐	☐
I'll take a routine day over a day full of unexpected events any day.	☐	☐	☐	☐	☐	☐
I'd rather do the same familiar things than try new and different things.	☐	☐	☐	☐	☐	☐
Whenever a set routine is established in my life, I look for ways to change it.	☐	☐	☐	☐	☐	☐
I'd rather be bored than surprised.	☐	☐	☐	☐	☐	☐
Plan changes seem to me to be very troublesome.	☐	☐	☐	☐	☐	☐
I often feel a little uncomfortable even with changes that could potentially improve my life.	☐	☐	☐	☐	☐	☐
When someone pushes me to change something, I tend to resist it, even if I think the change might ultimately benefit me.	☐	☐	☐	☐	☐	☐
Sometimes I find myself avoiding change even though I know it's good for me.	☐	☐	☐	☐	☐	☐
Once I make plans, I probably won't change them.	☐	☐	☐	☐	☐	☐

Question 12: A bat and a ball cost 22 €. The bat costs 20 €more than the ball. How much does the ball cost?

Question 13: If it takes 5 machines 5 minutes to make 5 widgets, how long would it take 100 machines to make 100 widgets?

Question 14: In a lake, there is a patch of lily pads. Every day, the patch doubles in size. If it takes 48 days for the patch to cover the entire lake, how long would it take for the patch to cover half of the lake?

E.5 Risk and Loss Aversion

In the following two tasks you can earn more money. In a total of 12 decisions, you always have to choose between a safe amount and a lottery. After you have made all the decisions, one of the 12 decisions will be randomly determined for your payout.

Decision 1 to 6

- **Lottery:** You will receive 400 ECU with a probability of 50% and nothing otherwise.
- **Safe payment:** Safe payoff, which increases with each decision.

Please tick in each case whether you choose the lottery or the safe payment.

Decision	Lotteries (probability 50% / 50%)			Safe payment
1	400 ECU (profit) with 50% probability 0 ECU otherwise	□	□	40 ECU (profit) safe
2	400 ECU (profit) with 50% probability 0 ECU otherwise	□	□	80 ECU (profit) safe
3	400 ECU (profit) with 50% probability 0 ECU otherwise	□	□	120 ECU (profit) safe
4	400 ECU (profit) with 50% probability 0 ECU otherwise	□	□	160 ECU (profit) safe
5	400 ECU (profit) with 50% probability 0 ECU otherwise	□	□	200 ECU (profit) safe
6	400 ECU (profit) with 50% probability 0 ECU otherwise	□	□	240 ECU (profit) safe

Decision 7 to 12

- **Lottery:** With a probability of 33.3%, you will receive 400 ECU. However, with a probability of 66.7% you lose money. The amount of the possible loss increases with each decision.
- **Safe payment:** Safe payoff of 0 ECU.

Decision	Lotteries (probability 33.3% / 66.7%)			Safe payment
7	400 ECU (profit) with 33.3% probability - 40 (loss) ECU otherwise	□	□	0 ECU safe
8	400 ECU (profit) with 33.3% probability - 80 (loss) ECU otherwise	□	□	0 ECU safe
9	400 ECU (profit) with 33.3% probability - 120 (loss) ECU otherwise	□	□	0 ECU safe
10	400 ECU (profit) with 33.3% probability - 200 (loss) ECU otherwise	□	□	0 ECU safe
11	400 ECU (profit) with 33.3% probability - 280 (loss) ECU otherwise	□	□	0 ECU safe
12	400 ECU (profit) with 33.3% probability - 400 (loss) ECU otherwise	□	□	0 ECU safe

F Questionnaire: Survey of Tax Advisors (extract)

F.1 Statistical data

Question 1: At how many locations is your company/law firm represented?

Question 2: How many professionals does your company/law firm employ in total?

Question 3: How many employees does your company/law firm employ in total?

Question 4: Revenue 2019

- ☐ up to €400k
- ☐ €401k to €750k
- ☐ €751k to €1.5 million
- ☐ more than €1.5 million

Question 5: With which of the following client groups does your law firm generate the most revenue? (firm revenue share in %)

private persons

self-employed persons and SMEs

large companies

F.2 Tax Expertise Questions

Question 1: When was the so-called banking secrecy lifted?

- □ January 1, 2017
- □ May 15, 2017
- □ June 25, 2017
- □ December 31, 2017

Question 2: Which statement about tax refunds and tax liabilities (possibly as inheritance liabilities) is correct in regard to inheritance tax?

- □ Tax refund claims and tax debts of the year of death are part of the taxable acquisition.
- □ Tax refund claims and tax debts of the year of death are not part of the taxable acquisition.
- □ Only tax refund claims of the year of death are part of the taxable acquisition.
- □ Only tax debts of the year of death are deductible as inheritance liabilities.

Question 3: The VAT assessment for 2017 is dated June 18, 2018. When is the payment due at the earliest?

- □ June 21, 2018
- □ July 18, 2018
- □ July 21, 2018
- □ July 23, 2018

Question 4: A taxpayer made negligent incorrect declarations in the tax return. What is the maximum possible fine?

- □ €500
- □ €5,000
- □ €25,000
- □ €50,000

Question 5: How many years must Germans who move to a low-tax country have been subject to unlimited tax liability before the extended limited tax liability applies?

- □ 3 years
- □ 4 years
- □ 5 years
- □ 8 years

Question 6: A taxpayer owes multiple amounts to the tax office and pays €500 every Monday. Which statement is correct?

- □ The taxpayer can specify the purpose of payment.
- □ Without specification, payment is first applied to VAT, then fines and interest.
- □ Without specification, payment is first applied to income tax, then fines and interest.
- □ Without specification, payment is applied to fines, payroll tax, then late fees.

Question 7: An appeal decision lacks a legal remedy instruction. What is the filing deadline according to the Fiscal Court Code?

- □ 1 month
- □ 6 months
- □ 1 year
- □ Unlimited

Question 8: When a partial business is contributed to a corporation, the assets can be transferred at book value if the fair value of other consideration does not exceed:

- □ €125,000
- □ €250,000
- □ €500,000
- □ €750,000

Question 9: What must be considered with the interest barrier rule? The interest income from special investment funds is reduced by:

- □ Negative capital income
- □ Foreign taxes
- □ Direct costs
- □ Deemed distributions

Question 10: From which income level does the extended limited income tax liability apply?

- □ €16,500/year
- □ €24,000/year
- □ €30,500/year
- □ €32,800/year

Question 11: What must an employer record in the payroll account?

- □ The capital letter U under §41(1) sentence 5 EStG
- □ Wages separated by cash and in-kind benefits
- □ Tax-free allowances and tips
- □ Lump-sum taxed payments under §40c EStG

Question 12: According to §46 EStG, what is the hardship allowance if other non-wage income amounts to €625 per year?

- □ €175
- □ €195
- □ €410
- □ €625

Question 13: A civil servant retires in 2023 with annual pension payments of €31,600. What percentage of this is the tax-exempt portion?

- □ 15.2%
- □ 13.6%
- □ 11.8%
- □ 10.9%

Question 14: An attic home office is recognized for tax purposes. Which statements are correct?

- □ Areas with a ceiling height under 1m do not count as living space.
- □ Areas with a height between 0.8m and 1.8m count 50% toward living space.
- □ Areas from 2m height count fully as living space.
- □ Areas count only from 2.2m ceiling height.

Question 15: What is added back to business income at 25% if applicable?

- □ Prepayment penalties
- □ Cash discounts
- □ Commitment fees
- □ Discounts

Question 16: Under which inheritance tax class are spouses of stepchildren taxed?

- □ II (like in-laws)
- □ I (like stepchildren)
- □ II (like stepparents)
- □ III (other)

Question 17: What must a receipt for business meals include for the expense to be deductible?

- □ Tips
- □ Names of participants
- □ Occasion of the meal
- □ Addresses of participants

Question 18: Which types of businesses are exempt from trade tax?

- □ Guarantee banks exempt from corporate tax
- □ Inland fishing (non-corporate)
- □ State-run lottery companies
- □ Short-term care homes, 70% subsidized by social services

Question 19: An architect gifts a paperweight to her assistant. What is the maximum tax-deductible cost?

- □ €35 incl. VAT
- □ €35 plus VAT
- □ Depends on whether 7% or 19% VAT applies
- □ €60 incl. VAT

Question 20: Which of the following services are VAT-exempt?

- ☐ Amusement park operations
- ☐ Pet food sales in a zoo
- ☐ German Youth Hostel Association services
- ☐ Preparation of study materials by professional authors

Question 21: What was the per diem meal allowance for a business trip to Hong Kong in 2019?

- ☐ €74
- ☐ €79
- ☐ €93
- ☐ €115

Question 22: How far in advance must the tax authority notify a taxpayer of an external audit?

- ☐ One week
- ☐ Two weeks
- ☐ Three weeks
- ☐ Depends on business size

Question 23: Recurring income is deemed received in the prior year if it is paid "shortly after" year-end. What does "shortly after" mean?

- ☐ 5 days
- ☐ 7 days
- ☐ 10 days
- ☐ Up to 12 days if the 10th day falls on a weekend

Question 24: What was the capitalization rate for 2018 under the simplified earnings value method?

- ☐ 4.5% plus base interest rate
- ☐ 11.25%
- ☐ 13.75%
- ☐ 14.80%

F.3 Question About Sec. 34a EStG

Your client, a sole proprietor with unlimited tax liability (single), earns annual business profits of approximately €500,000 with only minor year-to-year fluctuations. He plans to retain all profits in the company for the next five years to invest in expansion. He expects a return on these investments of 6% p.a. (before taxes). In addition to business income, your client has rental income of about €300,000 per year. His business is located in a municipality with a local business tax multiplier (Hebesatz) of 400%.

Your client asks you whether you would recommend submitting an application for preferential treatment of retained profits in accordance with Sec. 34a EStG.

What recommendation would you give your client?

1: Never submit an application according to Sec. 34a EStG

5: In any case, submit an application according to Sec. 34a EStG

1 □—□—□—□—□ 5

For how many clients have you filed an application for the preferential treatment of retained earnings according to Sec. 34a EStG in the past five years?

- □ none
- □ 1–2
- □ 3–5
- □ 5–10
- □ 10–20
- □ more than 20

G Evaluation Survey

G.1 Questions before the Experiment

Question 1: Are you female, male or non-binary?

- ☐ female
- ☐ male
- ☐ non-binary

Question 2: How old are you?

[ ]

Question 3: This question is designed to test your attention. Please click on the third answer "true".

- ☐ neither
- ☐ false
- ☐ true
- ☐ no answer

Question 4: How would you rate your own tax law knowledge?

no knowledge at all ☐—☐—☐—☐—☐—☐—☐—☐—☐—☐—☐ tax expert/consultant

G.2 Instructions

G.2.1 Procedure of the study

In this study, we ask you to answer a few questions about a fictional tax system. On the next screen, you will receive a description of this tax system. This will be followed by a comprehension check to ensure that the key aspects of the tax system have been understood correctly.

Important:

You may only proceed with the study if all questions in the comprehension check are answered

correctly.
If one or more questions are repeatedly answered incorrectly, the study cannot be continued. In this case, your participation will end, and you will not receive any compensation.
Note: You can access the instructions at any time throughout the study by clicking on *Show instructions* in the top right-hand corner.

G.2.2 Tax Rules and Comprehension Test

Imagine you are an entrepreneur and make a profit. This profit is subject to taxation.
As an entrepreneur, you also have the opportunity to use part of the profit as a reserve for future years. This means that this part is not distributed in the current year. The payout in the current year is reduced accordingly.
In later years, these reserves can be released and paid out again. Please note that payouts from reserves are also taxable under certain circumstances.
You can find out exactly how profits and reserves are taxed later on this page.
Read the tax rules carefully before answering the comprehension questions on the next page.
Participants were presented with the same tax rules as in our main experiment. Specifically, the rules for the corporate tax system corresponded to those used in the treatments *High TTC & High TRC*, *High TTC & Low TRC*, *Low TTC & High TRC*, *Low TTC & Low TRC*, and *One vs. Two Taxes* (see Section C.4). The rules for the two partnership tax systems (*Baseline* and *One vs. Two Taxes*) were identical to those described in Section C.3.
The comprehension test that followed was also identical to the one used in the main experiment.

G.3 Task

Please refer to the previously described tax system and answer the following question. If you have any questions, you can revisit the instructions at any time by clicking “Show Instructions” in the top right corner.
You can earn additional money with this question. Among all correct answers, we will randomly select 5 participants to receive a bonus of €50 each.
Assume that your business generates a profit this year, which you fully transfer into a reserve for the next year. The reserve does not earn any interest. Next year, you dissolve the reserve entirely and pay out the full amount to yourself.

Question 1: What do you estimate to be the average total tax burden on this profit over the two years combined (in %)?

G.4 Question about the Tax System

Question 1: How complicated did you find the tax system described?

very simple □—□—□—□—□—□—□—□—□—□ very complicated

G.5 Questions after the Experiment

Question 1: What is your highest educational qualification?

- □ Secondary modern school qualification (Hauptschule?)
- □ Secondary school certificate
- □ High-school diploma
- □ University of Applied Sciences degree
- □ University degree
- □ Dual university degree
- □ Doctorate

Question 2: What is your marital status?

- □ married/ long-term relationship
- □ single
- □ divorced/widowed

Question 3: What is your monthly net household income?

Monthly net household income is the sum of the monthly net incomes of all household members. The monthly net household income is calculated from the gross household income earned (all household income from employment, from assets, from public and non-public transfer payments) less taxes, contributions to health, nursing care, unemployment and statutory pension insurance. A (private) household is defined as any group of persons living together and forming an economic unit (multi-person households).

- □ < €1,300
- □ €1,300 - €1,700
- □ €1,700 - €2,600
- □ €2,600 - €3,600
- □ €3,600 - €5,000
- □ > €5,000

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