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Misconduct

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## ABSTRACT

We document that firms with powerful political representation on the two U.S. congressional committees that oversee the Securities and Exchange Commission (SEC) are less likely to face regulatory enforcement against corporate financial misconduct relative to other firms. Conditional on receiving an SEC enforcement action, the same firms also receive materially smaller monetary penalties. We establish causality using plausibly exogenous shocks to firms' political representation on these congressional committees based on committee turnover cases and firm headquarters location changes. Our findings are consistent with politician concern about voters' adverse reactions to the effects of financial misconduct by local firms: for politicians serving on one of these two committees and running for reelection, an SEC enforcement action against a constituent firm is negatively associated with the likelihood that the politician is subsequently reelected.

**Keywords:** Political Economy; Corporate Governance; SEC Investigation; Senate Committee on Banking, Housing, and Urban Affairs; House Committee on Financial Services; AAER; Elections

**JEL Codes:** G34; M42; M48

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## ABSTRACT

We document that firms with powerful political representation on the two U.S. congressional committees that oversee the Securities and Exchange Commission (SEC) are less likely to face regulatory enforcement against corporate financial misconduct relative to other firms. Conditional on receiving an SEC enforcement action, the same firms also receive materially smaller monetary penalties. We establish causality using plausibly exogenous shocks to firms' political representation on these congressional committees based on committee turnover cases and firm headquarters location changes. Our findings are consistent with politician concern about voters' adverse reactions to the effects of financial misconduct by local firms: for politicians serving on one of these two committees and running for reelection, an SEC enforcement action against a constituent firm is negatively associated with the likelihood that the politician is subsequently reelected.

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## 1. Introduction

A number of high profile corporate failures in recent years have led investors, media commentators, and academics to question the quality of regulatory oversight by the Securities and Exchange Commission (SEC). Some scholars argue that corporate failures occur because the SEC is “captured” by the very firms they are charged with regulating, consistent with capture theory (Stigler, 1971; Laffont and Tirole, 1991). Recent studies find support for this argument; commonly used proxies for capture theory such as corporate political connections, lobbying, and political contributions are associated with a reduced likelihood of SEC enforcement actions against firms (e.g., Correia, 2014). Our objective in this paper is to examine a largely unexplored source of influence over the SEC’s regulatory efforts: politicians that serve on congressional committees with SEC oversight responsibilities. Our study complements prior research on the determinants of SEC enforcement actions and penalties by examining a distinct *channel* through which the SEC can be influenced as well as the consequences of enforcement actions on politician reelection campaign outcomes.

Congressional committees serve as one of the key mechanisms through which the United States Congress shapes government policy and governs corporate behavior. Congress divides and delegates tasks to committees that have specialized legislative and regulatory oversight responsibilities. As our research setting, we exploit the fact that amongst all congressional committees, only two have oversight of the SEC: the U.S. Senate Committee on Banking, Housing, and Urban Affairs and the U.S. House of Representatives Financial Services Committee (hereafter “influential committees”).

Research in political economics provides two explanations for why influential committee members have incentives to seek to influence SEC enforcement activity against financial misconduct: capture theory (Stigler, 1971; Laffont and Tirole, 1991) and congressional rational choice theory (Fenno, 1973; Mayhew, 2004). First, capture theory suggests that interest groups or

firms with high-stakes interest in achieving a particular regulatory outcome can undertake a concentrated effort to influence regulators and politicians. In contrast, individuals and other stakeholders that may be only marginally affected by the regulatory outcomes will either ignore the outcome or are unwilling or unable to coordinate their efforts. Recent studies by Yu and Yu (2011) and Correia (2014) find evidence that the likelihood that a firm faces SEC regulatory enforcement is negatively linked to the tools used for proxy for regulatory capture such as lobbying, political connections, and contributions.

Second, congressional rational choice theory (Fenno, 1973; Mayhew, 2004) can also explain why politicians serving on influential committees have incentives to pressure the SEC. Because politicians' primary goal is to get reelected, they will seek to prevent events that decrease the probability of reelection success. If corporate financial misconduct in an influential committee member's constituency adversely affects voter perceptions about the politician's effectiveness on an influential committee, which in turn adversely affects the likelihood that the member will win the reelection, then the theory implies that influential committee members have incentives to avoid or dampen the effects of SEC enforcement efforts against constituent firms.

An important advantage of focusing on politicians serving on influential committees is that only those politicians have the *capability* to influence the SEC because of the jurisdictional power assigned to them from Congress. The relation between congressional committees and regulatory agencies can be viewed as a principal-agent problem. Politicians can incentivize regulatory agencies under their jurisdiction to act in the politicians' interests via monitoring and disciplining mechanisms such as congressional oversight and budget appropriations (Weingast and Moran, 1983; Weingast, 1984) and the threat of dismissal for the regulator's leadership (Shotts and Wiseman, 2010). Empirical evidence provides support for congressional control theory (e.g., Faith et al. 1982;

Weingast and Moran, 1983; Hunter and Nelson, 1995).<sup>1</sup>

Despite the arguments above, there are at least three reasons why it is not obvious that firms with influential committee representation will have a lower likelihood of facing SEC enforcement actions against financial misconduct relative to other firms. First, politicians trade off the benefits of supporting transgressing firms (such as the receipt of future political contributions and support) against the costs of being identified as supporters of transgressing firms and the adverse effects on reelection prospects. Second, if allegations of corporate financial misconduct are publicly revealed prior to an enforcement action, it is likely to be politically difficult for a politician to argue against a regulatory investigation. Third, politicians likely also consider broader reputational effects from the perspective of future post-congressional employment opportunities such as ambassadorships, federal executive positions, or non-executive corporate board directorships (Parker, 2005). Given these conflicting arguments, the effect of influential committee politician representation on SEC enforcement actions against constituent firms is an empirical question.

Using a panel dataset of 17,017 firm-year observations over the 2001 to 2010 period that links publicly listed firms with state-level Senate and district-level House congressional representation data, we find evidence that the power of a constituent firm's influential committee representation is negatively related to the likelihood that the firm will face SEC enforcement for financial misconduct. In economic terms, a one standard deviation increase in a firm's influential

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<sup>1</sup> Anecdotal comments by former SEC Chairman Arthur Levitt further illustrate the power of congressional committees over regulators:

*"...the congressional committee that oversees the SEC that has a chokehold on the existence of the SEC, that can block SEC funding, that can block SEC rulemaking, that can create a constant pressure in terms of hearings and challenges and public statements, that can absolutely make life miserable for the commission." And "[The politicians] kept the heat on me by telephone calls, by letters, by congressional hearings, and ultimately by threatening the funding of the agency by threatening its very existence. I mean, we were at that point struggling [to receive] the same compensation as other financial regulators... and certain members of this committee suggested to me that getting that pay parity was out of the question while we were proceeding with this issue. So we were really being held, well, an attempt was made to hold us captive." (<http://www.pbs.org/wgbh/pages/frontline/shows/regulation/interviews/levitt.html>)*

committee representation is associated with an 18% lower probability of receiving a financial misconduct-related Accounting and Auditing Enforcement Release (AAER), relative to other firms.

We also examine and find that the power of a firm's influential committee representation is negatively associated with the magnitude of regulatory penalties issued against a transgressing firm, relative to other transgressing firms. In economic terms, a one standard deviation increase in the power of a firm's influential committee representation is associated with a reduction of \$1.3 million in financial misconduct-related regulatory penalties. Overall, our baseline results provide evidence of a channel through which the SEC's enforcement efforts can be influenced: firms' representation in the constituencies of influential committee members.

In order to establish identification, we exploit multiple plausibly exogenous shocks to constituent firms' committee representation. Our first identification strategy exploits two sets of politician departures from influential committees that reduce certain state and congressional district level political influence over the SEC. Our second identification strategy uses firm headquarters location changes to capture changes in firms' influential committee representation. We also undertake a falsification test using departures of powerful politicians serving on *other* important congressional committees that have no jurisdiction over the SEC to rule out the possibility that our findings are influenced by unobserved omitted variables that affect firm incentives to engage in financial misconduct (for instance, state- or district-level economic downturns).

In sum, our findings provide causal evidence that politicians serving on influential committees act as a channel through which the likelihood of SEC enforcement actions and penalties conditional on an enforcement action can be affected. Furthermore, our results are also consistent with congressional rational choice theory; in other words, politicians appear to have reelection-related incentives to limit SEC enforcement and penalties that are distinct and incremental to incentives attributable to traditional proxies to measure political capture including political connections (e.g., Chaney et al. 2010; Guedhami et al. 2014), political contributions (Correia, 2014),

and lobbying (Yu and Yu, 2011).

Next, to further understand why politicians may seek to interfere in the SEC's enforcement activities against their consistent firms, we examine the consequences of SEC enforcement actions for politicians using outcomes from reelection campaigns. Voters are likely to care about SEC enforcement against a local firm if it disproportionately affects their employment stability and/or personal wealth through equity investments in the local firm. For a sample of incumbent influential committee members who undertake a reelection campaign, the issuance of an SEC enforcement action against a constituent firm in the two years leading up to a reelection is associated with a 9% higher probability that the politician loses the reelection campaign. Importantly, the findings do *not* hold for politicians that do not serve on influential committees but are more pronounced when the transgressing firm is large or when the financial misconduct is more severe.

Our findings complement those in a concurrent working paper by Heese (2015). He shows that firms are less likely to face an SEC enforcement action during presidential election years in politically important states. His results indicate that, on an *ex ante* basis, the SEC is likely to refrain from enforcement in periods when voters have power to punish politicians. Our results complement his study by showing that, *ex post*, SEC enforcement actions are linked to a higher likelihood of politician turnover. It is important to note that we are able to identify the *direct* link between enforcement actions and politician turnover; our turnover results hold only for the sample of politicians serving on influential committees.

Our study makes a number of contributions. First, we contribute to a broader stream of research that examines determinants of the SEC's enforcement efforts and penalties (Dechow et al. 1996, 2011; Beneish, 1999; Erickson et al. 2006; Karpoff et al. 2008; Armstrong et al. 2010; Johnson et al. 2009; Kedia and Rajgopal, 2011; and Files, 2012), and specifically, to studies examining political economy related determinants of SEC enforcement actions (Yu and Yu, 2011; Correia, 2014). Our study complements these papers by providing evidence of a specific *channel* through



which politicians' influence on SEC occurs and documenting that a career-based incentive can explain this influence. An important contribution of our findings is that politicians' reputational-related incentives appear to have distinct and incremental explanatory power to capture-related incentives.

Second and relatedly, to the best of our knowledge we are one of the first to provide evidence of a consequence of SEC enforcement for politicians by showing that, *ex post*, regulatory enforcement actions by the SEC are linked to adverse effects on politician reelection outcomes. This finding contributes to a stream of literature examining the consequences of regulatory enforcement of financial statement for firm value (Dechow et al. 1996; Hung et al. 2015), executives (Karpoff et al. 2008), and directors (Srinivasan, 2005).

Third, our study also contributes to a multi-disciplinary literature examining links between U.S. congressional committee representation and constituent firms.<sup>2</sup> Our paper is most closely related to studies that specifically examine how congressional committee representation affects regulatory actions against constituent firms such as the likelihood that individuals and corporate constituents face IRS tax audits (e.g., Hunter and Nelson, 1995; Young et al. 2001) and the outcome of deceptive trade practice reviews by the FTC (e.g., Faith et al. 1982; Weingast and Moran, 1983). Our findings build on this work by providing insights about congressional influence over an important regulator – the SEC. In addition, while prior studies examining regulatory actions against constituent firms provide evidence that is largely associational in nature, we exploit multiple plausibly exogenous shocks to firms' influential committee representation to allow causal inferences.

Finally, our research is likely to be of interest to regulators and policy makers. From a policy viewpoint, our findings help increase our understanding of the set of political frictions as a result of

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<sup>2</sup> Prior studies have examined the influence of congressional committee representation on the allocations of government-controlled economic benefits in the form of distributions (Atlas et al. 1995; Levitt and Poterba, 1999), the Financial Accounting Standards Board's accounting rule amendments (Ramanna, 2008), firms' investing activities (Cohen et al. 2011; Wellman, 2017), the allocation of government contracts to corporations (Tahoun, 2014), and bank risk-taking behavior (Kostovetsky, 2015).

representation on certain congressional committees for the enforcement of financial reporting practices.

We proceed as follows. The next section describes the data and methodology. Section 3 presents descriptive evidence and the main results. In Section 4, we discuss the link between regulatory enforcement and election outcomes. Section 5 contains robustness analyses. We conclude in Section 6.

## **2. Data, Political Power Variables, and Methodology**

In this section we describe the data sources and procedure used to generate our sample. We then discuss the construction of key variables and outline the methodology used in empirical tests.

### **2.1 Data**

We collect U.S. Congressional member and electoral district data for the 2001 to 2010 period from multiple sources: MIT Professor Charles Stewart's website, the U.S. Census Bureau based on the 2000 U.S. Census and from the University of Missouri Census Data Center. All data is publicly available.

The sample window covers the 106<sup>th</sup> Congress to the 111<sup>th</sup> Congress. We identify each politician's state and/or district of representation and the duration of service in the House or the Senate, committee membership assignments, committee membership appointment dates and service period, and party affiliation. The data also allows us to identify the duration of each politician's service on a committee (in years), which allows us to determine committee seniority. We focus on the politicians who serve on the two committees responsible for SEC oversight: the Senate Committee on Banking, Housing, and Urban Affairs, and the House Financial Services Committee.<sup>3</sup>

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<sup>3</sup> The composition of each committee manifests as a result of committee assignments at the start of each Congress. Committee assignment decisions depend on a large number of factors including the number of vacancies on a given committee, the political needs of each party assigning members to committees, the number of members competing for a committee assignment, views on specific issues, seniority, party loyalty, and rules on the number and types of

Senators represent an entire state whereas House representatives represent roughly equally populated electoral districts within a state.

Next, we link committee members with firms headquartered in their constituencies. While this is relatively straightforward for the members in the Senate because senators represent the entire state, it is less straightforward for those serving in the House of Representatives because each member of the House only represents a district within a state. In order to accurately capture the relation between firms and corresponding House representatives, we explicitly require firms to be headquartered in a House influential committee member's district. In untabulated analyses, we find that our results are qualitatively similar if we 1) link House influential committee members with firms located within a 20-mile radius of the member's district boundaries based on the ZIP Code of the firm's headquarters;<sup>4</sup> or 2) if we link firms and House influential committee members based on state location, rather than district location.

We merge these data with firm-specific financial data from Compustat, Compact Disclosure, CRSP, political connection data from BoardEx, political contribution data from the Federal Election Commission, lobbying data from the Center for Responsive Politics, and auditor data from Audit Analytics. We identify SEC investigations into financial misconduct between 2001 and December 2013 using Accounting and Auditing Enforcement Release (AAERs) data as discussed in Karpoff et al. (2008) and Dechow et al. (2011). We identify all cases that involve financial misstatement and focus on the year that the AAER is issued in order to accurately capture the outcomes of regulatory scrutiny. Our AAER sample includes all cases alleging earnings-estimate improprieties, financial

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assignments that each member may hold (Smith, Roberts, and Vander Wielen, 2013). The GOP and Democratic parties and each chamber also have specific rules and restrictions on the number and type of committee assignments that each politician can hold.

<sup>4</sup> We use 20 miles because a recent 2009 U.S. Department of Transportation report (<http://nhts.ornl.gov/2009/pub/stt.pdf>) notes that this is the average commuting distance. As commuting distances are likely to be highly heterogeneous across the U.S., we check alternative distance specifications up to 50 miles and find qualitatively similar results.

misrepresentation, or failure to adhere to U.S. Generally Accepted Accounting Principles (GAAP).<sup>5</sup>

We impose a number of data restrictions on our sample. First, we remove utility firms and financial services firms (SIC codes between 4900 and 4999; and between 6000 and 6900) because of different accounting requirements for these firms that may cause error in the measurement of important control variables such as financial reporting quality. Results from untabulated tests indicate that our findings are qualitatively similar if we include these firms. Second, we remove all firms with foreign headquarters because of the unclear link between those firms and U.S. politicians. Third, we drop all firms audited by Arthur Andersen during the sample period because of increased regulatory scrutiny against those firms around Arthur Andersen's collapse. Fourth, we remove all firms that are not audited by one of the "Big 6" auditing firms because of differences in the propensity of SEC enforcement action for firms audited by the Big 6 versus Non-Big 6 auditors (Lennox and Pittman, 2010).<sup>6</sup> After these restrictions, our sample consists of 17,017 firm-year observations, representing 2,641 unique firms.<sup>7</sup> We identify 360 AAERs issued to unique firms during our sample period.

## **2.2 Measures of Political Power on Influential Committees**

We use three proxies to capture the power of a firm's influential committee representation. Each proxy is calculated at the firm-year level. Our primary tests aggregate a firm's Senate and House influential committee representation because we do not a priori expect different effects between the influential committees. In sensitivity tests discussed below, we find that our primary

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<sup>5</sup> Although SEC regulatory efforts span a broad set of activities, we focus on financial misconduct because the revelation of an AAER is a major event for an investigated firm. For instance, Feroz et al. (1991) document abnormal cumulative average returns (CARs) of -6% over the two-day window around the disclosure of an SEC accounting investigation, even when the accounting transgression was reported earlier.

<sup>6</sup> The Big 6 are BDO Seidman, Deloitte, Ernst & Young, Grant Thornton, KPMG, and PricewaterhouseCoopers. The clients audited by the Big 6 represent 97.4% of aggregate total assets for all Compustat firms over our sample period. Our results are qualitatively similar if we include Arthur Andersen clients and/or Non-Big 6 audited clients in our sample.

<sup>7</sup> An important issue for our study is the link between firm headquarters location and influential committee representation. A limitation of using Compustat to correctly identify firm location is that we can only obtain the current (i.e., non-historical) firm location data, which may result in biased estimates. In order to overcome this limitation, we obtain annual firm-year headquarters location details from Audit Analytics. In addition, our results are robust to the removal of firms that change headquarters during our sample period.

results are qualitatively similar when using separate proxies for the House and Senate committees. A key determinant of committee power is committee seniority (Levitt and Poterba, 1999; Cohen et al. 2011). Senior committee members determine a committee's actions and agenda and oversee regulatory bodies under their jurisdiction. Thus, our first firm-level proxy for influential committee power is the aggregate years of influential committee member service (*Total\_Seniority*).

This firm-level measure is easily illustrated using an example: Books-A-Million Inc. (NASDAQ: BAMM) is headquartered in Alabama's 6<sup>th</sup> congressional district. In 2004, Alabama had one representative on the Senate Committee on Banking, Housing, and Urban Affairs – Richard C. Shelby (D-AL) – who had served on the committee for 17 years. Alabama also had two representatives on the House's Financial Services Committee: Spencer Bachus (R-AL), who was the 6<sup>th</sup> congressional district representative, and Artur Davis (D-AL), who was the 7<sup>th</sup> congressional district representative. Bachus and Davis had served on the House committee for six years and one year respectively as of 2004. The value of *Total\_Seniority* applied to Books-A-Million for 2004 represents the aggregate years of service for Shelby and Bachus only ( $17 + 6 = 23$ ). Davis is not included in the seniority count as the firm is neither in Davis' congressional district.

Our second proxy for an influential committee member's political power is a continuous yearly variable for the total number of influential committee members (*Committee\_Num*) that represent a firm. This variable captures the possibility that committee influence may stem from "power in numbers" – a greater volume of representation on influential committees can result in more cohesive influence over SEC actions.

A possible limitation of the *Total\_Seniority* measure is that it imperfectly captures differences in the strength of a firm's political representation on influential committees. For instance, firm A with two judiciary committee members of 10 years and 11 years (i.e., a total of 21) is treated the same as firm B with two committee members of 20 years and 1 year. It may be the case that firm B's senior member is more likely to be able to influence antitrust outcomes than either of firm A's

members. In order to address this issue, our third proxy to measure influential committee representation is an indicator variable set to one when a firm is located in a state and/or district for which a Senator and/or Representative is in the top quartile of influential committee member seniority for that year, and zero otherwise (*Seniority\_Dum*).

### 2.3 Methodology

We begin by investigating whether the power of a firm's representation on influential committees affects the likelihood that the firm receives an AAER for accounting misconduct. We estimate the following logit model:

$$Enforcement_{i,t} = \alpha + \beta_1 * Seniority_{i,t} + \beta_X * Controls_{i,t} + \zeta_{i,t} \quad (1)$$

where  $Enforcement_{i,t}$  is an indicator variable set to one for detected fraudulent financial misconduct cases against firm  $i$  in year  $t$  based on the SEC's issuance of an AAER and set to zero otherwise.  $Seniority_{i,t}$  represents one of three measures of influential committee representation: *Total\_Seniority*, *Committee\_Num*, or *Seniority\_Dum*.

$Controls_{i,t}$  is a vector of control variables which have been shown to be associated with accounting misconduct, including a litigation risk indicator variable (*Litigation Risk*), log of total assets (*Size*), long-term debt divided by total assets (*Leverage*), market-to-book ratio (*MtB*), scaled earnings (*Profit*), an indicator variable to capture recent debt or equity issuances (*Issuance*), the standard deviation of operating cash flows over the past five years (*Stdev\_Cashflow*), the standard deviation of total sales over the past five years (*Stdev\_Sales*), the operating cycle (*Oper\_Cycle*), and financial reporting quality (*FRQ*). We also control for the total stock ownership by institutional investors (*Inst\_Own*), the log of the number of analysts that cover the firm (*Analyst\_Following*), and the log distance in miles between the firm's headquarters and the nearest SEC regional office (*Distance\_to\_SEC*) based on Kedia and Rajgopal (2011). In addition, we control for multiple auditor-related variables that can affect the likelihood of financial misconduct: the auditor's city-level industry expertise (*Auditor\_Share*), the number of years that the auditor has been retained

(*Auditor\_Tenure*), the log number of clients of the firm's auditor office (*Office\_Size*), and whether the firm received a going concern opinion in the prior year (*GC\_Dummy*).

Importantly, we also include controls for the possibility that committee member behavior is influenced by other connections to constituent firms. First, following prior work (e.g., Faccio et al. 2006; Chaney et al. 2011; Guedhami et al. 2014), we control for political connections based on a committee members' previous employment experience at the firm in an executive or director capacity (*Political\_Connection*). We find that 402 unique sample firms are professionally connected with 376 unique politicians during the sample period. Second, we control for the firm's logged monetary political contribution (*Political\_Contribution*) via PAC contributions and logged SEC lobbying expenditures (*Lobby\_SEC*). All variables are defined in the Appendix.

We control for time-invariant state or industry effects by including state and Fama-French industry fixed effects. We also include year and auditor fixed effects. Standard errors are adjusted for heteroscedasticity using a Huber-White Sandwich estimator and clustered by firm. In untabulated sensitivity tests, we check that our results are robust if we: 1) use OLS rather than a logit specification to address concerns about an incidental parameter problem; and 2) cluster standard errors by state.

## **2.4 Summary Statistics**

Table 1 displays descriptive information about influential committees. The House (Senate) committees we examine have an average of 69 (21) members during our sample period, representing 29 (21) states. Thus, conditional on a state having representation on a committee, each state has an average representation on the House (Senate) committee of about 2 (1) members. Politicians serving on the House (Senate) influential committee have an average tenure of approximately 3.6 (6.9) years, with a maximum tenure of 19 (29) years. Next, we tabulate states with representation in the top (bottom) quartile of influential committee power over the sample period based on the number of consecutive years of service on a committee. Influential committee power does not appear to be

exclusively driven by the largest or most populated states, such as New York, California, or Texas. Rather, committee power appears to be spread across a large cross-section of states. The states with the longest representation on the Senate committee are Connecticut (10 years), Alabama (10 years), Utah (8 years), and Maryland (8 years). Only two states (Alaska and Maine) have no representation on influential committees during our sample period (representing 22 firm-year observations).

Table 2 presents descriptive statistics. Panel A present the mean, median, and standard deviation for each variable used in the multivariate tests. We begin with the three-abovementioned proxies of committee power based on state-level values (500 state-year observations based on 50 states multiplied by the 10-year sample period). The average aggregate seniority of a state's influential committee representation is approximately 8.8 years, with a median of 6 years. Each state has an average of about 0.4 representative across the influential committees. In addition, approximately 26% of states have a committee member in the top seniority quartile across both influential committees. We also present seniority measures for the firm-level full sample of 17,017 observations. While quite similar, the differences in the state-level and firm-level seniority measure values are mechanically driven by the uneven distribution of sample firms across states and districts.

Across the full sample, we find that *Enforcement* has a mean value of 0.021, indicating that 2.1% of sample firm-year observations are subject to SEC enforcement action. We find that roughly 17% of firm-year observations have political connections, while on average each firm makes political contributions of about \$466,000 annually and spends \$140,000 to lobby the SEC. Approximately 32.8% of sample observations are in industries classified as having a high risk of litigation. The average (median) total assets is \$3,303 (\$407) million, while the median leverage is 11.3% and the median market-to-book ratio is 2.041. The median profitability (using ROA) is 3.3% and the average occurrence of firms issuing security is 44%. Sample firms have median institutional ownership of 62.3%, are followed by about 15 analysts, and the average auditor tenure is about 9.8 years.

In Table 2 Panel B, we present differences between means for the full sample after



partitioning by firms that are subject to enforcement actions for financial misconduct and those that are not. In summary, we find some weak evidence that influential committee representation differs across the enforcement/non-enforcement groups. In addition, enforcement firms are more connected and make more political contributions. We observe that there is no statistical difference in total seniority of the committee between the two groups of firms. We do find that the number of influential committee representatives is significantly larger for firms with enforcement actions relative to other firms, which highlights the need to control for other firm-specific factors that examine enforcement actions. Further, we find that firms with enforcement actions have significantly greater political connections and political contributions, are larger in size and have more institutional ownership and analyst following. These results are largely consistent with the evidence in prior studies examining SEC enforcement actions.

### **3. Multivariate Results**

In Section 3.1 we discuss results from our primary tests examining the effects of influential committee representation on SEC enforcement actions against constituent firms. Section 3.2 and 3.3 present results using two identification strategies. Section 3.4 presents results from falsification tests. We document the effects of influential committee membership on regulatory penalties in Section 3.5.

#### **3.1 Influential Committees and Financial Misconduct Enforcement Actions**

In Table 3 we present results from multivariate tests examining whether political representation on influential committees is associated with financial misconduct-related regulatory enforcement actions. Columns 1-3 present coefficient estimates from tests of equation (1). Column 1 shows that firms with more powerful influential committee representation are significantly *less* likely to receive financial misconduct-related AAERs. More specifically, the coefficient on *Total\_Seniority* is negative and statistically significant at the 1% level ( $|z\text{-statistic}| > 2.60$ ). The marginal effect (presented in brackets) suggests that a one standard deviation increase in *Total\_Seniority* is

associated with an 18% decrease in the probability that a firm will receive an AAER, relative to firms in other constituencies. The evidence in columns 2 and 3 provides similar inferences when we use alternative measures of influential committee power (i.e., *Committee\_Num* and *Seniority\_Dum* respectively). The effects are statistically significant at the 5% level. For instance, the marginal effect for the test using *Committee\_Num* indicates that a one-politician increase in influential committee membership is associated with an 8.5% decrease in the probability that constituent firms will receive an AAER. Coefficients for control variables are largely consistent with prior studies. Note that we also observe that our results are robust to the inclusion of variables to proxy for the effects of political capture: lobbying, contributions, and political connections (e.g., Yu and Yu, 2010; Correia, 2014). The implication of this finding is that our results are consistent with congressional rational choice theory and suggests that influential committee membership is an explicit channel through which SEC regulatory efforts against financial misconduct can be influenced. In the following section, we undertake a number of tests to provide evidence about the causality of our findings.

### **3.2 Identification Using Influential Committee Member Turnover**

In the following two sections, we examine two distinct plausibly exogenous shocks to firms' powerful representation on influential committees to address causality. In this section, we examine the effects of plausibly exogenous departures of politicians from influential committees on the change in the likelihood that firms in the departing politician's jurisdictions face SEC enforcement efforts. We highlight that we only examine certain departure cases as not all departure cases are likely to be exogenous.

In order to satisfy the exclusion restriction, we require that the reason for a committee turnover event (the independent variable) does not also directly cause subsequent period SEC enforcement action in the departing politician's constituency (the dependent variable). We undertake two tests using turnover cases are possibly satisfy the exclusion restriction: 1) departures due to committee transfers that typically occur after a reelection victory at the start of each new Congress;

and 2) departures because of death or illness. In contrast, an example of a turnover case that is *unlikely* to satisfy the exclusion restriction is turnover due to election defeat: it is possible that poor underlying state or district economic conditions affect both reelection outcomes and a firm's probability of survival, which in turn influences antitrust review outcomes.<sup>8</sup>

First, turnover from influential committee politician transfers to other congressional committees are unlikely to be systematically and directly linked to enforcement actions because prior studies document that committee transfers occurs for a number of different reasons, including the desire for increased power or prestige, interest in helping shape public policy in areas outside of the jurisdiction of the judiciary committee, which may stem from a politician's pre-Congress work experience or education, and the opportunity to more easily obtain federal funding or develop economic interests relevant to a subset of the constituency (Fenno, 1973; Bullock, 1976).

Furthermore, as noted in Footnote (5), the timing of a transfer is often out of the control of the politician requesting the transfer because of the large number of factors and rules affecting transfer decisions. Thus, a critical characteristic of committee transfers that reaffirms our argument that transfers are plausibly exogenous is that the timing of a actual transfer is largely uncorrelated with the timing of a politician's desire to transfer committees. We also include committee departures that occur due to politician death as these are likely to be exogenous and in additional tests, check that our results hold when just using the death cases to identify turnover shocks.

There are 112 influential committee turnover events during our sample window (29 Senators and 83 Representatives). We use LexisNexis and Google.com to identify the reason for each turnover case. Of the 112 influential committee turnover events during our sample window, 46 cases (41%)

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<sup>8</sup> Another example of a turnover case that we cannot clearly identify as exogenous is that of Senator Phil Gramm (R-TX), who announced his retirement from the Senate in 2002. Gramm was the chairman of the Senate Committee on Banking, Housing, and Urban Affairs between 1999 and 2001. In December 2000, Gramm cosponsored a bill favorable to Enron Corp that exempted energy commodity trading from government regulation and public disclosure. Furthermore, Gramm's spouse, Wendy Gramm was an Enron board director between 1993 and Enron's collapse in 2001.

occur because of committee transfers or death. These are the treatment cases in our turnover tests. Of these 46 cases, 9 (20%) represent senior committee members and 37 (80%) represent non-senior members. There are 615 firms in the jurisdictions of these 46 turnover cases. The remaining 66 politician departure cases (59%) represent turnover for some other reason. These include departures due to election losses, for non-elected public or private sector positions, or because of retirement. We do not treat these 66 cases as plausibly exogenous turnover event cases in our tests.

The minimum loss in a firm's influential committee seniority representation is 1 year and the maximum loss is 34 years. The median loss is 10.5 years and the top quartile is 20 years. Of the sample cases, 9 (3 Senators and 6 Representatives) depart while their seniority is in the top quartile of committee seniority.

We use propensity score matching to identify a set of control group firms that do not experience turnover shocks to their influential committee representation, with matching occurring in the year prior to committee member turnover. Treatment firms experience the loss of a powerful influential committee member during our sample window, while control firms are in other states that do not experience a shock to their influential committee representation in the same year, or in the two preceding and subsequent years.<sup>9</sup> All treatment cases are coded such that year 0 represents the year of the loss of a powerful influential committee member. We match firms based on *Firm Size*, *FRQ*, *ROA*, *Leverage*, *MtB*, *Analyst\_Following*, *Inst\_Own*, *State\_Unemployment\_Rate*, *State\_GDP\_Growth*, and Fama-French industries, with no replacement, and with a caliper of 0.1%. We estimate the following changes specification using a logit model:

$$\Delta Enforcement_{i,t} = \alpha + \beta_1 * Senior\_Drop_{i,t} + \beta_X * \Delta Controls_{i,t} + \zeta_{i,t} \quad (2)$$

where  $\Delta Enforcement_{i,t}$  is an indicator variable set to one when firm  $i$  receives an AAER in year  $t+1$  or  $t+2$ , and does not receive an AAER in year  $t-1$  or  $t-2$ , and set to zero otherwise. Year  $t$  is the year

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<sup>9</sup> Our results are unaffected if we use the following conditions to identify possible control firms: firms in states 1) with no change to their influential committee membership; 2) with no change to their senior influential committee membership; or 3) with no influential committee membership in the year of turnover.

in which the influential committee member turnover occurs. We partition the 46 committee member turnover cases based on whether the departing member is a senior or junior member. The congressional committee tenure process implies that senior committee members have greater authority over committee affairs relative to less senior committee members. *Senior\_Drop<sub>i,t</sub>* is an indicator variable set to one if a firm experiences the exogenous loss of a powerful influential committee member in year *t*, and zero otherwise. We denote “powerful” committee members as those in the top quartile of committee seniority at the time of turnover. The matching process yields 109 firms in the constituencies of senior committee members that depart from influential committees and 109 similar firms that do not experience influential committee membership changes in the same year or the two-year window prior to or following the turnover year.

We also estimate a specification in which we examine the effects of committee member turnover of non-senior influential committee members. In this specification, we replace *Senior\_Drop* with *Non-Senior\_Drop*, an indicator variable set to one for firms that experience turnover of influential committee representatives who are not in the top quartile of committee seniority, and set to zero otherwise. The matching sample consists of 500 firms in the constituencies of non-senior committee member that depart from influential committees and 500 matched firms in other constituents that do not experience influential committee departures in the same year or the two-year window surrounding the turnover year.

We address the possibility that some politician departures (due to committee transfers) may not be exogenous. For instance, it is possible that politicians hoping to switch committees attempt to delay the filing of enforcement actions against constituent firms, as such actions may harm their reelection and committee transfer prospects. In order to address this possibility, we replicate our tests using a subsample of politician turnover events that occur because of death.<sup>10</sup> There are 44 sample

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<sup>10</sup> The three deaths are Congresswoman Julia Carson, Congressman Paul Gillmor, and Congresswoman Stephanie Jones.

firms in the constituencies of these three politician death cases. We compare SEC enforcement actions against these firms (treatment firms) to a matched sample of firms in other states that do not experience committee turnover in the same year (control firms), using the same matching criteria discussed above. The matching process yields 80 firms, representing 40 treatment firms and 40 control firms. We reestimate Equation (2) after replacing *Senior\_Drop* with a new indicator variable called *Death\_Drop*, which is set to 1 for firms in a constituency affected by one of the three influential committee member deaths, and set to 0 otherwise.

$\Delta Controls_{i,t}$  represents the change form of a vector of control variables similar to those in equation (1), all measured as the difference between  $t-1$  and  $t+1$ , where  $t$  represent the shock year. We drop variables that do not vary in the pre and post periods for the sample firms: *Political\_Connection*, *Litigation\_Risk*, and *Distance\_to\_SEC*. All specifications include state, industry, auditor, and year fixed effects. Our results are robust to using matched-firm-pair fixed effects instead of state fixed effects. Standard errors are adjusted for heteroscedasticity using a Huber-White Sandwich estimator and clustered by firm.

Table 4 presents coefficients from estimations of equation (2). In column 1, the evidence indicates that firms that experience decreases in senior influential committee representation are significantly more likely to subsequently receive AAERs relative to similar firms that do not experience committee membership changes. The marginal effect suggests that the loss of a *senior* influential committee member results in a 40% increase in the probability that constituent firms will subsequently be subject to financial misconduct-related enforcement action, relative to a matched sample of firms with no changes to their influential committee representation. Column 2 presents results from tests of the effect of *non-senior* committee member turnover on the likelihood that the SEC issues an AAER against financial misconduct. The coefficient on *Non-Senior\_Drop* is positive but statistically insignificant. Thus, the loss of a non-powerful influential committee member does not appear to have a statistically significant effect on financial misconduct-related enforcement

actions against constituent firms. This is consistent with prior work that suggests that congressional committee influence is concentrated amongst senior committee members (e.g., Levitt and Poterba, 1999). The evidence in column 2 also serves as a falsification test: if some omitted variable drives both influential committee politician turnover and AAERs, then the omitted variable must affect turnover for all committee members, but simultaneously only affect AAER likelihood for firms that experience the loss of a powerful influential committee member.

The results in column 3 indicate that death-related politician turnover is positively and significantly associated (at the 5% level). We highlight that the results in column 3, using a much smaller set of turnover cases, are consistent with the results using the politician turnover sample in column 1 that relies on senior member turnover cases due to transfers to more prestigious opportunities.<sup>11</sup> Finally, our findings are also robust to a number of sensitivity tests.<sup>12</sup>

### **3.3 Identification Using Firm Headquarters Relocations**

Our second identification strategy exploits firms' headquarters location changes. Headquarters changes affect the state in which a firm is located (and thus a firm's representation in both the House and Senate), which mechanically affects the strength of the firm's influential committee representation. This shock to influential committee representation is plausibly exogenous because it is unlikely that a firm's decision to change headquarters location also drives SEC enforcement actions against financial misconduct, implying that using headquarters changes likely satisfies the exclusion restriction. We identify 78 unique firms in our sample that change their

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<sup>11</sup> We further note that although the death turnover cases include non-senior politicians, these turnover cases are possibly more exogenous than the tests using all turnover cases in columns 1 and 2.

<sup>12</sup> First, we consider committee appointments. The tenure system means that newly appointed committee members are the most junior members on a committee and thus have the least amount of power on the committee. Un-tabulated analyses indicate that the addition of a committee member to an influential committee has a positive but statistically insignificant effect on the likelihood of AAER issuances. Second, our results are qualitatively similar if we replicate our tests after including firm-level fixed-effects (and removing industry and state fixed-effects). Third, the results are qualitatively similar when we control for governance characteristics over the 2001 to 2007 period using firm-specific governance characteristics based on the G-Index (Gompers et al. 2003). Finally, to rule out potential state-specific confounding factors, we compare the firms from the shock states to themselves, i.e., firms from the same states when they do not experience committee member turnover.

headquarters location.<sup>13</sup> Among these cases, 39 (38) firms experience an increase (decrease) in *Total\_Seniority*. One firm experiences no change in total seniority. The average increase (decrease) in *Total\_Seniority* for the respective groups is 14.28 years (14.97) years. The maximum increase (decrease) in *Total\_Seniority* around a headquarter change is 57 (48) years.

We use propensity score matching to identify a set of control group firms in other states that do not switch headquarters locations in the same year, or in the two preceding or subsequent years. We match in the year prior to the headquarters location switch and based on *Firm Size*, *FRQ*, *ROA*, *Leverage*, *MtB*, *Analyst\_Following*, *Inst\_Own*, *State\_Unemployment\_Rate*, *State\_GDP\_Growth*, and Fama-French industries, with no replacement, and with a caliper of 0.1%. The matching sample yields 78 treatment firms and 78 control sample firms using a 1 to 1 match. We estimate the following changes specification using an ordered logit model:

$$\Delta Enforcement\_HQChange = \alpha + \beta_1 * HQChange + \beta_2 * \Delta Total\_Seniority + \beta_3 * HQChange * \Delta Total Seniority + \beta_x * \Delta Controls + \zeta \quad (3)$$

Where  $\Delta Enforcement\_HQChange$  is an ordinal categorical variable set to one if a firm receives an AAER for financial misconduct in  $t+1$  or  $t+2$  but not in  $t-1$  or  $t-2$ ; set to 0 if a firm does not receive an AAER for financial misconduct in any of  $t-1$ ,  $t-2$ ,  $t+1$ , or  $t+2$ ; set to negative one if a firm only receives an AAER for financial misconduct in  $t-1$  or  $t-2$  but not in  $t+1$  or  $t+2$ , where  $t$  is the year of the change in the headquarters location.  $HQChange$  is an indicator variable set to one for treatment firms (i.e., those that change their headquarters location) and set to zero for control sample firms.  $\Delta Total\_Seniority$  is the change in the value of *Total\_Seniority* from year  $t-1$  to  $t+1$ . The interaction term captures the effect of a change in headquarters location on SEC enforcement actions that is incremental to the effect of influential committee seniority changes. All specifications include state, industry, auditor, and year fixed effects. Our results are robust to using matched-firm-pair fixed

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<sup>13</sup> We use Compact Disclosure to identify accurate headquarter locations and changes. This data is only available for the period from 2000 to 2006.



effects instead of state fixed effects. Standard errors are adjusted for heteroscedasticity using a Huber-White Sandwich estimator and clustered by firm.<sup>14</sup>

Table 5 presents coefficients from an estimation of equation (3). The evidence indicates that for firms that move headquarters locations, the change in influential committee representation is negatively related to the likelihood that the firms subsequently receive AAERs, relative to similar firms that do not change their headquarters locations. In column 1, the coefficient on *HQChange* is positive but insignificant, suggesting that on average, firm headquarters changes do not affect the likelihood of SEC enforcement for financial misconduct. We find that  $\Delta Total\_Seniority$  is negatively associated with the likelihood of facing SEC enforcement, consistent with the main results. The marginal effect indicates that a one-year increase in committee seniority is associated with a 1.8% decrease in the probability of receiving an AAER. The interaction term *HQChange* \*  $\Delta Total\_Seniority$  is negative and significant, indicating there is an incremental effect from headquarter changes on the likelihood of facing an SEC enforcement action. Economically, for firms that change their location, the marginal effect estimates indicate that a one-year increase in the seniority of a firm's influential committee representation is associated with an average reduction in the probability of facing an SEC enforcement action by 9%, relative to firms that do not change their headquarters location. In sum, the evidence is consistent with a causal relation between influential committee representation and SEC enforcement actions against constituent firms.

### **3.4 Falsification Test: Representation on Other Powerful Congressional Committees**

It is conceivable that our sample of politician turnover cases and SEC enforcement action likelihood are driven by some other unobserved factor such as changes in state level economic conditions (i.e., an omitted variable problem). To alleviate this possibility, we undertake a series of falsification tests using changes in representation on the most powerful congressional committees

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<sup>14</sup> In untabulated tests, we find that empirical results are robust to: 1) using Ordinary Least Squares to address the incident parameter problem; and 2) clustering standard errors at the state-level.

that have no jurisdiction over the SEC (i.e., powerful committees other than influential committees). We identify the ten most powerful unrelated Senate and House committees from Edwards and Stewart (2006).<sup>15</sup> We create measures of committee power that are similar to the previously defined measures, but based on the power of a firm's political representation on these alternative powerful committees. We re-estimate equation (2) after replacing the *Senior\_Drop* and *Non-Senior\_Drop* variables with these new variables: *Senior\_Drop\_OtherComm* and *Non-Senior\_Drop\_OtherComm*. We match each firm that experiences the turnover of a senior/non-senior non-relevant committee politician with a firm in another state that also has representation on one of the ten alternative committees but does not experience a shock to the committee representation. We use the same matching variables as previously discussed. For tests using senior and non-senior committee member turnover on other powerful committees that do not have congressional jurisdiction over the SEC, the matched sample yields 7,000 and 9,972 firm-year observations respectively.

Table 6 presents regression results. Coefficients on both *Senior\_Drop\_OtherComm* and *Non-Senior\_Drop\_OtherComm* in columns 1 and 2 respectively are statistically insignificant. In other words, the loss of a powerful politician (or a relatively less powerful politician) from a non-influential congressional committee does not appear to change the likelihood of financial reporting enforcement actions against the politician's constituent firms. These findings indicate that it is unlikely that our results are driven by the set of omitted variables that also drive senior committee member turnover.

### **3.5 Influential Committees and Financial Misconduct Enforcement Penalties**

Next, we investigate whether the influential committee representation affects penalties for constituent firms subject to SEC investigations against financial misconduct. For each of the 360

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<sup>15</sup> The committees are as follows. Senate: Finance, Veterans Affairs, Appropriations, Rules, Armed Services, Foreign Relations, Intelligence, Judiciary, Budget, and Commerce. House: Ways and Means, Appropriations, Energy and Commerce, Rules, International Relations, Armed Services, Intelligence, Judiciary, Homeland Security, and Transportation and Infrastructure. In untabulated tests, we find similar results to those presented if we use the top 3 or top 5 (instead of top 10) most powerful other committees.

AAERs during our sample period, we use the SEC's regulatory filings, court verdicts, LexisNexis, and Google.com to identify the scope of the alleged financial misconduct and subsequent regulatory penalties by the SEC or the Department of Justice (DOJ) on the transgressor firm and/or employees.<sup>16</sup> We exclude 25 ongoing investigations from our tests, as well as another 69 cases because of the difficulty in accurately mapping the assessed penalty with the scale of the financial manipulation.<sup>17</sup> For the remaining 266 cases, the mean aggregate income or profit manipulation is approximately \$19.8 million and ranges from \$76,000 to \$15 billion. Our findings are qualitatively similar if we remove the largest and smallest penalty cases. Firms with influential committee representation in the top quartile of seniority report an average earnings manipulation of \$13.7 million compared to \$21.4 million for all other cases. The difference is statistically significant at the 5% level. The regulatory penalties issued against these firms and/or their employees ranges between \$0 and \$2.25 billion with an average of \$11.7 million.<sup>18</sup> Firms with influential committee representation in the top seniority quartile report an average penalty of \$7.7 million compared to \$13 million for all other cases. The difference is statistically significant at the 5% level. In almost all the cases, the SEC also issues a "cease and desist" notification against the firm. In four cases, the SEC simply drops the enforcement investigation against the firms. In roughly 13% (35 cases) of the 266 misconduct cases, employees receive jail sentences, ranging from several months up to 286 years (aggregated at the firm level). In the vast majority of cases that do not result in incarceration, the SEC imposes bans against convicted employees from subsequently serving as an executive or a

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<sup>16</sup> Karpoff et al. (2008) undertake a comprehensive analysis of the consequences of financial misconduct for employees. Our analysis aggregates the consequences of financial misconduct across penalties issued to both firms and employees.

<sup>17</sup> For example, in the SEC's case against Dynegy Inc., the SEC "found that Dynegy violated federal securities laws by improperly disguising [a] \$300 million loan as cash flow from operations on its financial statements, thereby misleading investors about the level of its energy trading activity." Our results are robust to including these non-income or sales manipulation related cases and either excluding the control variable that captures the amount of the manipulation amount (which is defined as total manipulation in income) or using a crude dollar value of manipulation in all income and non-income accounts to capture the amount of manipulation.

<sup>18</sup> We exclude amounts paid as a result of class action lawsuits by investors as such payments are separate to penalties issued as a result of SEC enforcement actions.

director of a public company and/or suspends professional licenses. Bans range from one year to life. We estimate the following multivariate specification to examine the effect of influential committee representation on penalties assessed for financial misconduct:

$$Penalty_{i,t} = \alpha + \beta_1 * Seniority_{i,t} + \beta_X * Controls_{i,t} + \zeta_{i,t} \quad (4)$$

where  $Penalty_{i,t}$  is a continuous variable capturing the log monetary value of the aggregate penalty imposed by the SEC or Department of Justice (DOJ) on the firm and/or employees.  $Seniority_{i,t}$  is one of the three measures of seniority as previously defined.  $Controls_{i,t}$  is a vector of controls, including *Political\_Connection*, *Political\_Contribution*, *Lobby\_SEC*, the log dollar value of the net profit misstatement alleged by the SEC (*MisconductSeverity*), *Litigation\_Risk*, *Size*, *Leverage*, *MtB*, *Profit*, *Inst\_Own*, *Analyst\_Following*, and *Distance\_to\_SEC* as previously defined. We also include state, industry, auditor, and year fixed effects.<sup>19</sup>

We present multivariate test results in Table 7. Overall, the evidence indicates that the SEC imposes lower monetary penalties for financial misconduct by firms located in areas served by powerful influential committee representation, relative to financial misconduct by firms in other states. The results are robust across all three measures of committee power: *Total\_Seniority*, *Committee\_Num*, and *Seniority\_Dum*. In economic terms, for a firm issued with an AAER, we find that a one standard deviation increase in their influential committee *Total\_Seniority* is associated with a reduced penalty of approximately \$1.3 million. This amount holds after controlling for a number of determinants of the magnitude of the penalty assessed, including the alleged amount of income manipulation and firm size. In addition, the evidence in column 4 suggesting that the effect of committee power is more pronounced in the severity of the manipulation. Importantly, our results are robust to the inclusion of variables that capture the presence of political connections via prior monetary contributions and lobbying.

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<sup>19</sup> It is possible that a state's influential committee representation changes between the issuance of an AAER and the date that a trial outcome or settlement is determined. Our results are unaffected if we use political representation at the time of the AAER or the time that the penalty is imposed.

#### **4. Financial Misconduct and Influential Committee Member Election Outcomes**

The findings in Section 3 are consistent with congressional rational choice theory and provide causal evidence about a channel through which SEC enforcement decisions can be influenced. In particular, politicians serving on influential committees have incentives to limit SEC enforcement against corporate financial misconduct *in their constituencies* because the revelation of financial misconduct by a local firm could adversely affect voter perceptions about the politician and adversely affect reelection prospects.

In this section, we empirically examine whether SEC enforcement actions against local firms affects voter perceptions about their political representatives, as measured by election outcomes. This conjecture implicitly assumes that 1) voters are aware of AAERs against local firms; and 2) care enough to take out their dissatisfaction out on their political representatives. We discuss each of these assumptions next.

There are a number of channels through which voters can learn about SEC enforcement against corporate financial misconduct by a local area firm. First, there is likely to be press coverage about the enforcement action. Local or regional newspapers are especially likely to cover cases of corporate financial misconduct by local corporations. Second, voters who are employees of the transgressing firm are likely to become aware of the misconduct if the transgression is likely to lead to downsizing and layoffs. Third, constituents can learn about the financial misconduct through word of mouth.

There are a number of reasons why voters are likely to care about SEC enforcement against financial misconduct by local area firms. First, as noted above, severe financial misconduct can result in restructuring or bankruptcy. This is likely to affect local voters who are either employed by the transgressing firm or use the firm's products or services. Second, as corporate financial misconduct typically leads to significant investor losses (Feroz et al. 1991; Karpoff et al. 2008), shareholders

may blame politicians and regulators for insufficient regulation or monitoring efforts. Shareholder losses from corporate misconduct by local firms are especially problematic for *local* politicians because recent evidence suggests individual investors tend to overinvest in geographically proximate firms. In particular, Ivkovic and Weisbenner (2005) find individual investors have strong preferences for local investments and Huberman (2001) finds empirical evidence that employees of firms overinvest in the stock of their own employers.<sup>20</sup> Thus, voters may disproportionately experience wealth losses following SEC enforcement against local firms.

Note that the discussion above can apply to *any* politician who serves a constituency in which SEC enforcement action against a local firm occurs and not just politicians serving on influential committees. The extent to which voters penalize influential committee politicians, if at all, is an empirical question. If voters rationally understand that only influential committee members have jurisdiction over financial misconduct regulation, then we should observe that following an SEC enforcement action against a local firm, influential committee members experience a larger effect on their reelection outcome relative to other politicians. On the other hand, if voters do not consider the jurisdictional power and committee responsibilities of their elected politicians with respect to corporate financial misconduct, we would expect to observe similar reelection outcomes following financial misconduct by local firms for all politicians irrespective of their membership in an influential committee.

We conduct empirical tests using a dataset in which the unit of observation is influential committee members in election years (i.e., politician-election year). Elections for politicians in the House of Representatives (Senate) are held every two (six) years. The sample size is 946 politician-reelection years. Of these cases, we use LexisNexis and Google to determine that 34 (4%) result in

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<sup>20</sup> In contrast, outside of the local area, investors are likely to be geographically dispersed. This implies that for any other politician, it is likely that a much smaller proportion of his voter base suffers financial losses from the financial misconduct.

reelection defeat; these are our turnover cases of interest.<sup>21</sup> We estimate the following logit specification:

$$Turnover_{s,t} = \alpha + \beta_1 * Recent\_AAER_{s,t} + \beta_X * Controls_{s,t} + \zeta_{s,t} \quad (5)$$

where  $Turnover_{s,t}$  is an indicator variable set to one if an influential committee politician in state  $s$  loses a reelection campaign in year  $t$ , and set to zero otherwise.  $Recent\_AAER_{s,t}$  is an indicator variable set to one if a firm in state  $s$  has received a AAER for financial misconduct in the prior two years ( $t$  or  $t-1$ ), and set to zero otherwise.  $Controls_{s,t}$  is a vector of variables that have been shown to affect reelection outcomes including the closeness of the reelection result ( $Close\_Reelection$ ), the politician's seniority in Congress ( $Seniority$ ), indicator variables for politician gender ( $Female$ ), party affiliation ( $Democratic$ ), whether the politician is from the same party as the sitting president ( $Presiden\_Same\_Party$ ), and whether the reelection campaign occurs during a presidential election year ( $Presidential\_Election\_Year$ ). We also control for state-level GDP growth ( $State\_GDP\_Growth$ ), and the state-level unemployment rate ( $State\_Unemployment\_Rate$ ). We also include year fixed effects and to mitigate the possibility that the results are driven by time-invariant state characteristics, we include state fixed effects.

We present empirical results in Table 8. In column 1, we present results for the test of Equation (5). The coefficient on  $Recent\_AAER$  is positive and statistically significant at the 5% level, consistent with the notion that SEC enforcement action against a firm in an influential committee's constituency is associated with a *negative* future reelection outcome. In economic terms, an influential committee politician has a 9% higher likelihood of losing a reelection campaign if a firm in the politician's constituency has been subject to an AAER for financial misconduct in the two

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<sup>21</sup> It is possible that influential committee politicians that have an AAER in their jurisdictions anticipate a reelection loss and choose to "retire" rather than run for reelection. As we cannot distinguish between retirement cases that occur for this reason and retirement cases for other unrelated reasons, we do not treat retirement related turnover cases as "reelection loss" cases. This research design choice biases against finding a result and underestimates the magnitude of the link between local corporate financial misconduct and subsequent politician turnover.

years prior to the reelection.<sup>22</sup>

The findings in column 1 do not rule out the possibility that voters penalize *all* elected politicians, i.e., voters do not differentiate between politicians that serve on influential committees and those that do not serve on these committees. To address this issue, we re-estimate Equation (5) for politicians that serve on the top ten most powerful congressional committees that *do not* have jurisdiction over the SEC. We present results in column 2. The coefficient on *Recent\_AAER* is negative but statistically insignificant. This finding suggests that voters only penalize influential committee members even though the effects of local corporate financial misconduct likely affect all voters similarly. The findings in columns 1 and 2 together suggest that voters appear to understand the specific responsibilities of their elected congressional representatives with respect to enforcement actions against financial misconduct and impound this information into their voting decisions.

We also undertake a number of additional cross-sectional tests. First, we split the sample based on the median total assets of the sample cases that receive AAERs. The evidence in columns 3 and 4 indicate that the relation between SEC enforcement efforts prior to a reelection and reelection outcomes are concentrated in the partition for large firms. This is consistent with larger firms having greater visibility and economic footprints in their influential committee representatives' jurisdictions. Second, we examine the effect of the magnitude of the AAER based on whether the firm subsequently files for bankruptcy. The results in columns 5 and 6 indicate that the main effect is concentrated in the cases in which the SEC enforcement outcome is subsequently followed by bankruptcy, consistent with the notion that severe misconduct cases are more likely result in

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<sup>22</sup> A possible question that arises from our findings is that if rational incumbent influential committee members anticipate the increased probability of losing a reelection campaign following an SEC enforcement action against a within-constituency firm, then wouldn't those politicians aggressively act to prevent SEC action against their constituent firms, which in turn should result in zero SEC enforcement actions in their districts/states? In practice, frictions limit a politician's ability to completely prevent the SEC from enforcing misconduct against constituent firms. First, the SEC enforcement action may already be underway before the politician is aware of the event. Second, politicians trade off the adverse effects of within-constituency SEC actions on reelection outcomes with a potentially more adverse effect if revelations of attempting to influence the SEC are publicly disclosed.



employment and investment losses for local voters.

We caveat the findings by noting that, similar to studies in political science examining the determinants of election outcomes and studies examining the consequences of AAERs for firms, managers, and directors, our findings of a relation between within-district enforcement against financial misconduct and reelection outcomes for those constituent firms' elected politicians are associational in nature and should be interpreted accordingly.

Our findings are consistent with prior research that finds politicians (and firms) are aware of events that can be sensitive for voters. For example, Ramanna and Roychowdhury (2010) find evidence that politically connected firms that outsource jobs engage in income-decreasing accruals management prior to the 2004 U.S. elections. They argue that firms want to shield their affiliated candidates from political embarrassment to the extent possible in order to consolidate their relationships with those political candidates. Another study by Piotroski et al. (2015) find that politically affiliated firms in China temporarily suppress negative information releases prior to highly visible political events and this results in an increased number of stock price crashes after the political events when the negative information is released.

## **5. Additional Tests and Robustness Checks**

### **5.1 Effects of House and Senate Subcommittee Membership**

Congressional committees divide their tasks among subcommittees that handle specific areas. The two subcommittees responsible for financial reporting oversight are the Subcommittee on Securities, Insurance, and Investment (Senate) and the Subcommittee on Capital Markets and Government-Sponsored Enterprises (House). We repeat our analyses after partitioning influential committee politicians based on whether they serve on the abovenamed subcommittees or not. We treat influential committee chairpersons and ranking members as ex-officio members of the subcommittees, consistent with committee rules in both the Senate and the House.

Table 9 presents results for tests of Equation (1) after partitioning influential committee members into subcommittee and non-subcommittee groups and identifying these groups by adding “\_Sub” or “\_NonSub” respectively to each seniority measure. The results show that both subcommittee and non-subcommittee representation have a negative and significant effect on the likelihood that constituent firms will face SEC enforcement action. The results are similar across all three seniority measures. F-tests indicate that the subcommittee effect is statistically larger than that for non-subcommittees. A potential explanation for why non-subcommittee membership is important is that all influential committee members (regardless of their subcommittee assignments) have the ability to influence SEC actions, either directly or via relationships with other committee members.

## **5.2 Differential Effects of Senate and House Influential Committees**

In this section, we consider whether our results vary based on whether firms have representation on either the Senate or the House influential committees. One reason to expect a difference between the committees is that the Senate committee is tasked with the responsibility to confirm or deny the president’s recommendations for SEC commissioner appointments and thus may have more influence over the SEC, which in turn affects firm behavior. We calculate three new measures of committee member power based on a state’s representation on the Senate and House committees separately. We then restrict equation (1) to either the Senate or House influential committee power measures instead of the corresponding aggregate committee power measures. We present results in Table 10. The findings across all three measures of committee power indicate that the relation between influential committee representation and enforcement actions is statistically significant for both the committees. F-tests indicate that there is no statistically significant difference between the effect from the Senate and the House influential committees.

## **5.3 Other Robustness Checks**

### **5.3.1 Influential Committee Chairman Representation**

We examine if our results are driven by influential committee chairman representation. Five

unique states have influential committee chairs during our sample period (OH, MA, CT, MD, AL), of which two are in the House and three are in the Senate. We replace *Senior\_Dum* with two indicator variables. The first variable is set to one for firms in influential committee chairman constituencies and set to zero otherwise. The second variable is set to one for firms with non-chairman top quartile representation on an influential committee, and set to zero otherwise. Untabulated results indicate that inferences using both chairman and senior non-chairman representation are statistically significant at conventional levels. In economic terms, the effect is about 25% larger for the chairman relative to senior non-chair representation. We conclude that committee chairmen have the greatest (but not exclusive) ability to influence SEC actions.

### **5.3.2 Differences Between Majority or Minority Party Influential Committee Representation**

We consider whether the effects of influential committee representation on enforcement efforts are affected by whether a politician is affiliated with the majority or minority party in a given Congress. We conduct tests of Equation (1) but replace our seniority variable with two separate variables to capture representation from the majority and minority parties. Untabulated results indicate that the effect for both majority and minority party representation is statistically significant. Results from F-tests indicate the effect of majority party representation is significantly greater than that of minority party representation. These results are consistent with Cohen et al. (2011) who find both committee chairpersons and ranking members have political influence and Mayhew (2004) who suggests that the presence of minority party influence is the outcome of rational behavior: “congressional majorities obviously do not shut out minorities...it would make no sense in doing so; the costs of cutting in minority members are very low, whereas the costs of losing majority control in a cutthroat partisan politics of this kind would be very high”.

### **5.3.3 House of Representatives State Apportionment**

We examine whether our results are driven by states that are disproportionately represented on the House’s Financial Services Committee. This possibility exists because House seats are

apportioned to a state based on the state's population (i.e., each Representative serves an approximately equal number of constituents). In contrast, each state has equal representation in the Senate. Thus, the most populous U.S. states (California, Texas, Florida, New York, Pennsylvania, and Illinois) have the largest number of House seats. Firms located in these six states represent 47.6% of all firms in our sample. Tests excluding each of these five states provide qualitatively similar results to those presented above.

#### **5.3.4 Alternative Identification Methodology to Link Firms and States**

A possible issue for our study is that linking state politician representation with firm headquarters location may not capture politician incentives for geographically diverse firms. In order to address this concern, we use the Garcia and Norli (2012) firm-specific measure of state-level operational dispersion.<sup>23</sup> The measure captures the number of times states are mentioned in a firm's 10-K filing. The greater the number of states mentioned, the greater the dispersion of the firm's operations. The more frequently a given state is mentioned, the greater the expected importance of that state for the firm.<sup>24</sup> The state of a firm's headquarters location represents 64% of the average state name counts across our sample firms. Our tabulated results are robust to two alternate methods to identify the most appropriate state-level Senate and House representation for each sample firm observation: 1) we use a weighted average of influential committee member seniority based on the geographical distribution of operations using all states identified in the 10-K filing; and 2) we determine a firm's committee seniority measures based on the state that has the highest count in the 10-K filing. Note that a limitation of this robustness analysis is that House district-firm links are not identified.

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<sup>23</sup> We thank Diego Garcia and Øyvind Norli for making these data available to us.

<sup>24</sup> For example, in 2006 Boeing Corp. identifies six unique states in its 10-K filing. The firm is headquartered in Illinois and has manufacturing facilities in Washington, South Carolina, Missouri, Kansas, and Oklahoma. However, 50% of all the state mentions are Washington, where Boeing has major manufacturing facilities. Thus, it is possible that Washington's influential committee representatives have incentives to influence potential SEC enforcement action against Boeing.

### **5.3.5 Potential Spillover Effects from Enron and WorldCom Collapses**

In order to rule out the possibility that our results are driven by increased scrutiny against financial reporting following the collapses of Enron and WorldCom, we replicate our tests after removing all observations for 2001, 2002, and 2003. The results from these untabulated tests are qualitatively similar to the reported findings.

### **5.3.6 Business-Friendly States**

We also examine whether politicians who choose to serve on influential committees represent a state or a congressional district in a state that is viewed as “business friendly”. Business-friendly states are likely to attract both higher quality and more successful firms relative to other states, and politicians from those states may be more eager to serve on influential committees. Using Forbes’ annual survey of state-level business environment data between 2005 and 2010, we partition firms into high and low business-friendly state groups.<sup>25</sup> Untabulated tests indicate that our main results are qualitatively similar across both partitions.

## **6. Conclusion**

In this study, we explore whether political representation on the congressional committees that have responsibility for SEC oversight - the U.S. Senate Committee on Banking, Housing, and Urban Affairs and the U.S. House of Representatives Financial Services Committee – is a channel through which politicians can influence the SEC’s regulatory enforcement efforts. We find that when firms are located in jurisdictions served by powerful members of these congressional committees, they are less likely to be subject to SEC enforcement action for financial misconduct and conditional on facing an enforcement action, receive smaller penalties. To draw causal inferences, we exploit multiple distinct shocks to firms’ committee representation using a set of plausibly exogenous politician turnover events as well as firm headquarter changes. One explanation for our findings is

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<sup>25</sup> See <http://www.forbes.com/best-states-for-business/>.

that politicians have incentives to avoid voter discontent as a result of local corporate financial misconduct. Additional tests indicate an SEC enforcement against a constituent firm is negatively associated with the likelihood that a politician wins a subsequent reelection campaign, but only when the politician serves on an SEC-relevant congressional committee.

Our findings are likely to be of interest to regulators, politicians, and firms. Our study highlights the need for future research examining the effects of political influence for firms to consider politician incentives that arise from both political capture as well as politician reelection concerns.

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## Appendix: Variable Definitions

### *Dependent Variables:*

**Enforcement:** An indicator variable set to one if a firm receives an AAER for financial misconduct in the current year, and set to zero otherwise.

**$\Delta$ Enforcement:** An indicator variable set to one if a firm receives an AAER for financial misconduct in  $t+1$  or  $t+2$ , where  $t$  is the year of departure of an influential committee representative, and set to zero otherwise.

**$\Delta$ Enforcement\_HQChange:** An ordinal categorical variable set to one if a firm receives an AAER for financial misconduct in  $t+1$  or  $t+2$  but not in  $t-1$  or  $t-2$ ; set to 0 if a firm does not receive an AAER for financial misconduct in any of  $t-1$ ,  $t-2$ ,  $t+1$ , or  $t+2$ ; set to negative one if a firm only receives an AAER for financial misconduct in  $t-1$  or  $t-2$  but not in  $t+1$  or  $t+2$ , where  $t$  is the year of the change in the headquarters location.

**Penalty\$:** Log of the dollar value monetary penalty imposed by the SEC on a firm and its employees following the issuance of an AAER for financial misconduct.

### *Variables of Interest:*

**Total\_Seniority:** The aggregate tenure (in years) of a firm's total political representation on influential committees, calculated annually.

**Committee\_Num:** A continuous variable capturing a firm's total number of political representatives serving on influential committees, calculated annually.

**Seniority\_Dum:** An indicator variable set to one if a firm has at least one influential committee representative in the top quartile of influential committee tenure, and zero otherwise.

**Senior\_Drop:** An indicator variable set to one for firms in jurisdictions that lose senior representation on influential committees because the politician departs for a more prestigious position, and set to zero otherwise. Senior representation is defined as a politician in the top quartile of influential committee tenure.

**Non-Senior\_Drop:** An indicator variable set to one for firms in jurisdictions that lose non-senior representation on influential committees because the politician departs for a more prestigious position, and set to zero otherwise. Non-senior representation is defined as any politician not in the top quartile of influential committee tenure.

**Death\_Drop:** An indicator variable set to one for firms in jurisdictions that lose influential committee representation because of politician death, and set to zero otherwise.

**HQChange:** An indicator variable set to one for firms that change their headquarters location and set to zero otherwise.

**Senior\_Drop\_OtherComm:** An indicator variable set to one for firms in jurisdictions that lose senior representation on powerful congressional committees other than an influential committee because the politician departs for a more prestigious position, and set to zero otherwise. Senior representation is defined as a politician in the top quartile of influential committee tenure.

**Non-Senior\_Drop\_OtherComm:** An indicator variable set to one for firms in jurisdictions that lose non-senior representation on powerful congressional committees other than an influential committee because the politician departs for a more prestigious position, and set to zero otherwise. Non-senior representation is defined as any politician not in the top quartile of influential committee tenure.

**Recent\_AAER:** An indicator variable set to one if a firm in the politician's state receives an AAER for financial misconduct in the current year or the previous year, and set to zero otherwise.

### *Control Variables:*

**Analyst\_Following:** A firm-year measure defined as the logged average number of analysts covering the firm during the year.

**Auditor\_Share:** A firm-year measure defined as the proportion of the industry audited by the firm's auditor, and measured as the proportion of the total industry assets audited, based on Fama-French industry codes.

**Auditor\_Tenure:** A firm-year measure defined as the number of years that a firm has retained their current auditor.

**Close\_Reelection:** The closeness of the reelection result, measured using the winning margin percentage.

**Democratic:** An indicator variable set to one if the influential committee member is a Democrat, and set to zero otherwise.

**Distance\_to\_SEC:** A firm-year measure of the distance in logged miles between the firm's headquarters ZIP code to the closest SEC regional office.

**Female:** An indicator variable set to one if the influential committee member is female, and set to zero otherwise.

**FRQ:** Unsigned abnormal accruals based on Hribar and Nichols (2007).

**GC\_Dummy:** A firm-year indicator variable set to one if a firm receives a going-concern audit opinion in that year, and set to zero otherwise.

**Inst\_Own:** A firm-year measure defined as the percentage of a firm's common stock owned by institutional investors at year-end.

**Issuance:** A firm-year indicator variable set to one if in the prior three years, a firm has issued long-term debt or stock worth more than ten percent of the prior year's long-term debt or common equity respectively, and set to zero otherwise.

**Leverage:** A firm-year measure defined as a firm's long-term debt scaled by total assets.

**Litigation\_Risk:** A firm-year indicator variable set to one if a firm is in one of the following industries: biotech (SIC codes 2833-2836 and 8731-8734), computer (3570-3577 and 7370-7374), electronics (3600-3674), retail (5200-5961), and set to zero otherwise.

**Lobby\_SEC:** A firm-year measure defined as the amount of a firm's total SEC-related lobbying spending, calculated as  $\text{Log}(1 + \text{total dollar amount of annual SEC-related lobbying spending})$ .

**MisconductSeverity\$:** The logged dollar amount of net profit financial misrepresentation.

**MtB:** A firm-year measure defined as a firm's market value of equity scaled by book value of equity at year-end.

**Office\_Size:** Log of the number of clients of the firm's auditor office.

**Oper\_Cycle:** A firm-year measure defined as  $\text{log}(\text{days in account receivables} + \text{days in inventory})$ .

**Penalty\$:** Conditional on receiving an AAER, the total logged dollar value of the regulatory penalty imposed on a firm and its employees.

**Political\_Connection:** A firm-year indicator variable set to one when a firm is affiliated with an influential committee member based on whether the politician previously served as an executive or director of the firm, and set to zero otherwise.

**Political\_Contribution:** A firm-year measure defined as the total logged dollar value of political contributions.

**President\_Same\_Party:** An indicator variable set to one if the influential committee member is from the same party as the incumbent U.S. president, and set to zero otherwise.

**Presidential\_Election\_Year:** An indicator variable set to one if the reelection case occurs in a presidential election year, and set to zero otherwise.

**Profit:** A firm-year measure defined as earnings before extraordinary items scaled by total assets.

**Size:** A firm-year measure defined as logged total assets.

**State\_GDP\_Growth:** A state-year measure based on the annual GDP growth rate.

**State\_Unemployment\_Rate:** A state-year measure of the year-end state unemployment rate.

**Stdev\_Cashflow:** A firm-year measure defined as the standard deviation of cash flow from operations between  $t-4$  and  $t$ .

**Stdev\_Sales:** A firm-year measure defined as the standard deviation of sales between  $t-4$  and  $t$ .

**Table 1: Influential Committee Descriptive Statistics**

This table presents descriptive statistics about influential committees: the House Financial Services Committee (*House Committee*) and the Senate Committee on Banking, Housing, and Urban Affairs (*Senate Committee*).

**Panel A: Influential Committee Descriptive Statistics**

	House Committee	Senate Committee
Average size (in number of members)	69.25	21.25
Average # of states represented on committee	29.05	20.67
Average # of state representatives	2.28	1.02
Max # of state representatives	11	2
Average politician tenure on committee (in years)	3.62	6.94
Maximum politician seniority on committee (in years)	19.00	29.00

**States with the greatest number of years of representation (and corresponding duration) in the top quartile of influential committee between 2001 and 2010:**

**House Committee:** CA, PA, NY, MA, AL, NC, IL, LA, DE (10 years); VT, IA, OK, (8 years); OK, KS, TX, NE (6 years); IN, OH, NJ (4 years); OR, MN, MO, FL (2 years);

**Senate Committee:** CT, AL (10 years); UT, MD (8 years); SD, TX, RI, (4 years); ID, ID, NE, MA, FL, WY, IN, CO, NY, KY (2 years)

**States with the number of years of representation (and corresponding duration) in the bottom quartile of influential committee between 2001 and 2010:**

**House Committee:** ME, AK (10 years); KY, WI (8 years); MN, MS (6 years); AR, AZ, CO, CT, MI, MO, NH, NJ, NM, SC, TN, UT, WV (4 years); GA, ID, NV, VA, WA (2 years)

**Senate Committee:** ME, AK (10 years); HI, NH, NJ (6 years); DE, FL, GA, MI, MT, NC, OH, PA, TN (4 years); CO, ID, IN, KY, LA, NE, NV, NY, OR, SC, TX, VA, WI (2 years)

States with no representation on influential committees during sample period: AK, ME.

Total # of sample firm-year observations from these states: 22.

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**Table 2: Descriptive Statistics**

This table presents descriptive statistics. Panel A presents mean, median and standard deviation values for variables used in the multivariate tests. Panel B presents t-tests of the differences between mean values for variables after partitioning by firms that receive and those that do not receive SEC enforcement actions for financial misconduct. All variables are defined in the Appendix.

**Panel A: Multivariate Test Variables**

	(1)	(2)	(3)
	Mean	Median	Std. Dev.
<i>State-year Seniority Measures (n = 500)</i>			
Total_Seniority	8.763	6.000	9.981
Committee_Num	0.420	0.000	0.525
Seniority_Dum	0.262	0.000	0.443
<i>Firm-year Seniority Measures (n = 17,017)</i>			
Total_Seniority	10.576	2.000	14.962
Committee_Num	0.906	0.000	0.988
Seniority_Dum	0.271	0.000	0.448
<i>Other Variables (n = 17,017)</i>			
Enforcement	0.021	0.000	0.115
Political_Connection	0.169	0.000	0.375
Political_Contribution (\$)	466,029	0.000	2,481,660
Lobby_SEC (\$)	140,113	0.000	1,538,735
Litigation_Risk	0.328	0.000	0.469
Total Assets (\$Million)	3,303	408	12,118
Size	6.064	6.010	2.039
Leverage	0.167	0.113	0.189
MtB	2.850	2.041	4.073
Profit	-0.010	0.033	0.174
Issuance	0.440	0.000	0.496
Stdev_Cashflow	0.110	0.062	0.167
Stdev_Sales	0.259	0.195	0.224
Oper_Cycle	4.567	4.646	0.810
Inst_Own	0.565	0.623	0.313
Analyst_Following	2.327	2.708	1.452
Distance_to_SEC (miles)	1,771	1,580	1,262
Auditor_Share	0.200	0.214	0.123
Auditor_Tenure	9.845	7.000	8.657
Office_Size	2.717	2.772	1.118
GC_Dummy	0.023	0.000	0.151

**Panel B: T-tests of Differences for Enforcement and No Enforcement Firms**

	(1)	(2)	(3)
	<b>Enforcement</b>	<b>No Enforcement</b>	<b>T-test</b>
Total_Seniority	11.33	10.60	0.62
Committee_Num	2.78	2.25	1.75*
Seniority_Dum	0.275	0.271	0.10
Political_Connection	0.21	0.11	2.66***
Political_Contribution (log)	5.03	3.01	2.51**
Lobby_SEC (log)	0.13	0.05	1.10
Litigation_Risk	0.38	0.33	1.17
Total Assets (\$Million)	7,922	3,226	4.02***
Size	7.61	5.97	7.56***
Leverage	0.184	0.169	0.93
MtB	2.55	2.82	0.77
Profit	-0.005	-0.012	0.75
Issuance	0.41	0.44	0.46
Stdev_Cashflow	0.08	0.11	1.55
Stdev_Sales	0.27	0.26	0.41
Oper_Cycle	4.61	4.57	0.52
Inst_Own	0.69	0.56	4.30***
Analyst_Following	3.09	2.30	5.27***
Distance_to_SEC (miles)	6.81	6.83	0.11
Auditor_Share	0.22	0.20	1.68*
Auditor_Tenure	10.39	9.83	0.65
Office_Size	2.75	2.72	0.25
GC_Dummy	0.029	0.023	0.33

**Table 3: Influential Committee Seniority and Enforcement Against Financial Misconduct**

\*, \*\*, and \*\*\* indicate significance at the 90%, 95%, and 99% confidence level, respectively.

This table presents logit regressions of the likelihood that firms face SEC enforcement for financial misconduct on firms' influential committee representation. The dependent variable, *Enforcement*, is an indicator variable set to one for firms that receive an AAER from the SEC for financial misconduct. The independent variable of interest is one of three proxies for the power of firms' influential committee representation: *Total\_Seniority*, *Committee\_Num*, or *Seniority\_Dum*. All variables are defined in the Appendix. In all regressions, standard errors are Huber-White sandwich estimators and clustered at the firm level, and z-values are in parentheses. We show marginal effect in the bracket. State, industry, year, and auditor fixed effects are included in all regressions.



	(1)	(2)	(3)
	<b>Dependent Variable: Enforcement</b>		
Constant	-7.452*** (-8.11)	-7.611*** (-8.89)	-7.699*** (-8.76)
<b>Total_Seniority</b>	<b>-0.016***[-0.012]</b> <b>(-2.60)</b>	-	-
<b>Committee_Num</b>	-	<b>-0.086**[-0.085]</b> <b>(-2.39)</b>	-
<b>Seniority_Dum</b>	-	-	<b>-0.141**[-0.137]</b> <b>(-2.22)</b>
Political_Connection	-0.652** (-2.11)	-0.660** (-2.19)	-0.655** (-2.15)
Political_Contribution	-0.042** (-2.11)	-0.042** (-2.11)	-0.041** (-2.06)
Lobby_SEC	-0.031 (-1.33)	-0.032 (-1.34)	-0.027 (-1.29)
Litigation_Risk	0.211 (0.50)	0.214 (0.50)	0.200 (0.47)
Size	0.576*** (5.38)	0.577*** (5.39)	0.582*** (5.43)
Leverage	-0.193 (-0.31)	-0.185 (-0.30)	-0.170 (-0.28)
MtB	-0.033* (-1.74)	-0.033* (-1.73)	-0.035* (-1.82)
Profit	0.023 (0.48)	0.023 (0.49)	0.025 (0.53)
Issuance	-0.346 (-1.62)	-0.350* (-1.65)	-0.374* (-1.76)
FRQ	-0.005 (-1.22)	-0.005 (-1.30)	-0.004 (-1.21)
Stdev_Cashflow	1.149* (1.80)	1.139* (1.79)	1.167* (1.82)
Stdev_Sales	0.933* (1.88)	0.929* (1.88)	0.920* (1.86)
Oper_Cycle	0.199* (1.71)	0.193* (1.68)	0.217* (1.81)
Inst_Own	0.964 (1.61)	0.964 (1.61)	0.947 (1.58)
Analyst_Following	-0.093 (-0.60)	-0.098 (-0.63)	-0.087 (-0.56)
Distance_to_SEC	-0.089 (-1.39)	-0.078 (-1.25)	-0.083 (-1.35)
Auditor_Share	-0.987 (-0.80)	-0.941 (-0.76)	-1.048 (-0.86)
Auditor_Tenure	-0.013 (-1.02)	-0.013 (-1.00)	-0.012 (-0.97)
Office_Size	-0.168 (-1.47)	-0.171 (-1.50)	-0.165 (-1.46)
GC_Dummy	0.621 (1.22)	0.612 (1.27)	0.609 (1.31)
State, Industry, Year, and Auditor Fixed Effects	Yes	Yes	Yes
N	17,017	17,017	17,017
Pseudo R <sup>2</sup>	0.141	0.142	0.143

#### **Table 4: Effects of Exogenous Shocks to Influential Committee Seniority on Financial Misconduct Enforcement**

\*, \*\*, and \*\*\* indicate significance at the 90%, 95%, and 99% confidence level, respectively.

This table presents results from matched sample ordered logit regressions of the likelihood that firms face SEC enforcement for financial misconduct around shocks to firms' influential committee representation. The dependent variable in all columns,  $\Delta Enforcement$ , is an indicator variable set to one for firms that receive an AAER from the SEC for financial misconduct in the two years following the turnover of an influential committee representative. The independent variable of interest is *Senior\_Drop*, *Non-Senior\_Drop*, or *Death\_Drop*. *Senior\_Drop* (*Non-Senior\_Drop*) is an indicator variable set to one for firms in jurisdictions that experience the turnover of an influential committee member ranked in the top quartile (non-top quartile) for a more prestigious position, and set to zero otherwise. *Death\_Drop* is an indicator variable set to one for firms in jurisdictions that experience the turnover of an influential committee member because of death, and set to zero otherwise. All other variables are defined in the Appendix. In all regressions, standard errors are Huber-White sandwich estimators and clustered at the firm level, and z-values are in parentheses. We show marginal effect in the bracket. State, industry, year, and auditor fixed effects are included in all regressions.

	(1)	(2)	(3)
	<b>Dependent Variable: ΔEnforcement</b>		
Constant	-4.550*** (-9.61)	-4.882*** (-9.77)	-4.432*** (-5.30)
<b>Senior_Drop</b>	<b>0.405***[0.400]</b> <b>(2.62)</b>	-	-
<b>Non-Senior Drop</b>	-	<b>0.216[0.211]</b> <b>(1.29)</b>	-
<b>Death_Drop</b>	-	-	<b>0.955**[0.946]</b> <b>(2.53)</b>
ΔPolitical_Contribution	-0.050* (-1.81)	-0.052* (-1.84)	-0.055* (-1.88)
ΔLobby_SEC	-0.283 (-1.37)	-0.256 (-1.33)	-0.156 (-1.19)
ΔSize	0.355* (1.88)	0.389* (1.89)	1.056** (2.22)
ΔLeverage	-1.355 (-0.53)	-1.342 (-0.77)	-2.552 (-1.40)
ΔMtB	-0.020 (-1.21)	-0.021 (-1.22)	-0.033 (-0.95)
ΔProfit	0.299 (1.30)	0.312 (1.35)	0.288 (0.72)
ΔIssuance	0.321 (1.11)	0.359 (1.22)	0.055 (0.50)
ΔFRQ	-0.005 (-1.02)	-0.006 (-1.15)	-0.006 (-0.89)
ΔStdev_Cashflow	1.419* (1.89)	1.472* (1.92)	1.377 (1.50)
ΔStdev_Sales	0.822* (1.80)	0.857* (1.90)	1.956 (1.33)
ΔOper_Cycle	0.782* (1.88)	1.023** (2.02)	2.668** (1.82)
ΔInst_Own	0.325 (0.29)	0.330 (0.33)	0.790 (0.89)
ΔAnalyst_Following	-0.110 (-1.02)	-0.125 (-1.12)	-0.079 (-0.56)
ΔAuditor_Share	-1.112 (-1.08)	-1.289 (-1.11)	-0.672 (-0.67)
ΔAuditor_Tenure	-0.018** (-2.30)	-0.017** (-2.20)	-0.222 (-1.26)
ΔOffice_Size	-0.537* (-1.82)	-0.540* (-1.83)	-0.387** (-2.29)
ΔGC_Dummy	0.267 (1.02)	0.256 (1.11)	0.289 (0.78)
State, Industry, Year, and Auditor Fixed Effects	Yes	Yes	Yes
N	218	1,000	80
Pseudo R <sup>2</sup>	0.162	0.135	0.106

### **Table 5: Effects of Firm Location Change on Financial Misconduct Enforcement**

\*, \*\*, and \*\*\* indicate significance at the 90%, 95%, and 99% confidence level, respectively.

This table presents results from a matched sample ordered logit regression of the likelihood that firms face SEC enforcement for financial misconduct around changes to the state in which their headquarters are located. The dependent variable,  $\Delta Enforcement_{HQChange}$ , is an indicator variable set to one for firms that receive an AAER from the SEC for financial misconduct in the two years following a change in their headquarters location. The independent variable of interest is  $HQChange * \Delta Total\_Seniority$ .  $HQChange$  is an indicator variable set to one for firms that change their headquarter locations, and set to zero otherwise.  $\Delta Total\_Seniority$  is a continuous variable measured as the annual change in a firm's  $Total\_Seniority$ . All other variables are defined in the Appendix. Standard errors are Huber-White sandwich estimators and clustered at the firm level, z-values are in parentheses, and marginal effects are in brackets. We show marginal effect in the bracket. State, industry, year, and auditor fixed effects are included in all regressions.

	(1)
	<b>Dependent Variable: ΔEnforcement_HQChange</b>
HQChange	0.505 (1.50)
ΔTotal_Seniority	<b>-0.562** [-0.018]</b> (-2.12)
HQChange * ΔTotal_Seniority	<b>-2.568** [-0.090]</b> (-2.35)
ΔPolitical_Contribution	-0.155 (-1.45)
ΔLobby_SEC	-0.063 (-0.80)
ΔSize	0.035 (1.55)
ΔLeverage	-0.078 (-1.06)
ΔMtB	-0.058 (-1.47)
ΔProfit	0.076 (0.90)
ΔIssuance	-0.552 (-1.60)
ΔFRQ	-0.037 (-0.79)
ΔStdev_Cashflow	1.509 (1.42)
ΔStdev_Sales	1.675* (1.78)
ΔOper_Cycle	0.056 (1.50)
ΔInst_Own	0.090 (1.22)
ΔAnalyst_Following	-0.356 (-1.35)
ΔAuditor_Share	-0.266 (-1.03)
ΔAuditor_Tenure	-0.025 (-1.35)
ΔOffice_Size	-0.060 (-0.77)
ΔGC_Dummy	0.011 (0.30)
State, Industry, Year, and Auditor Fixed Effects	Yes
N	156
Pseudo R <sup>2</sup>	0.238

**Table 6: Falsification Tests Examining the Effects of Political Representation on Other Congressional Committees**

\*, \*\*, and \*\*\* indicate significance at the 90%, 95%, and 99% confidence level, respectively.

This table presents ordered logit regressions of the likelihood that firms face SEC enforcement for financial misconduct on firms' representation on powerful congressional committees that do not have jurisdiction over the SEC. The dependent variable, *Enforcement*, is an indicator variable set to one for firms that receive an AAER from the SEC for financial misconduct. The independent variable of interest is *Senior\_Drop\_OtherComm* or *Non-Senior\_Drop\_OtherComm*. *Senior\_Drop\_OtherComm* (*Non-Senior\_Drop\_OtherComm*) is an indicator variable set to one for firms in jurisdictions that experience the turnover of a politician in the top quartile (non-top quartile) of one of the top 10 most powerful congressional committees other than an influential committee, and set to zero otherwise. All variables are defined in the Appendix. In all regressions, standard errors are Huber-White sandwich estimators and clustered at the firm level, and z-values are in parentheses. State, industry, year, and auditor fixed effects are included in all regressions.

	(1)	(2)
	<b>Dependent Variable: <math>\Delta</math>Enforcement</b>	
Constant	-7.882*** (-8.50)	-7.679*** (-8.39)
<b>Senior_Drop_OtherComm</b>	<b>0.120[0.117]</b> <b>(1.02)</b>	-
<b>Non-Senior_Drop_OtherComm</b>	-	<b>-0.082[-0.078]</b> <b>(-0.92)</b>
$\Delta$ Political_Contribution	-0.053* (-1.86)	-0.052* (-1.82)
$\Delta$ Lobby_SEC	-0.279 (-1.35)	-0.285 (-1.40)
$\Delta$ Size	0.362* (1.88)	0.366* (1.90)
$\Delta$ Leverage	-1.367 (-0.69)	-1.379 (-0.73)
$\Delta$ MtB	-0.022 (-1.28)	-0.023 (-1.34)
$\Delta$ Profit	0.316 (1.29)	0.322 (1.33)
$\Delta$ Issuance	0.355 (1.06)	0.362 (1.09)
$\Delta$ FRQ	-0.006 (-1.06)	-0.007 (-1.22)
$\Delta$ Stdev_Cashflow	1.383* (1.89)	1.422* (1.90)
$\Delta$ Stdev_Sales	0.855* (1.85)	0.832* (1.82)
$\Delta$ Oper_Cycle	1.002** (2.00)	1.106** (2.05)
$\Delta$ Inst_Own	0.326 (0.28)	0.333 (0.35)
$\Delta$ Analyst_Following	-0.122 (-1.03)	-0.125 (-1.11)
$\Delta$ Auditor_Share	-1.120 (-0.99)	-1.220 (-1.12)
$\Delta$ Auditor_Tenure	-0.019** (-2.20)	-0.018* (-2.18)
$\Delta$ Office_Size	-0.550* (-1.88)	-0.542* (-1.80)
$\Delta$ GC_Dummy	0.259 (1.10)	0.250 (1.02)
State, Industry, Year, and Auditor Fixed Effects	Yes	Yes
N	7,000	9,972
Pseudo R <sup>2</sup>	0.055	0.085

**Table 7: Influential Committee Power and Penalties for Financial Misconduct**

\*, \*\*, and \*\*\* indicate significance at the 90%, 95%, and 99% confidence level, respectively.

This table presents logit regressions of the likelihood that firms face SEC enforcement for financial misconduct on firms' influential committee representation. The dependent variable, *Enforcement*, is an indicator variable set to one for firms that receive an AAER from the SEC for financial misconduct. The independent variable of interest is one of three proxies for the power of firms' influential committee representation: *Total\_Seniority*, *Committee\_Num*, or *Seniority\_Dum*. All variables are defined in the Appendix. In all regressions, standard errors are Huber-White sandwich estimators and clustered at the firm level, and z-values are in parentheses. State, industry, year, and auditor fixed effects are included in all regressions.

	(1)	(2)	(3)	(4)
	<b>Dependent Variable: Penalty\$</b>			
Constant	7.822** (2.20)	7.055* (1.88)	7.167** (2.09)	6.892** (2.29)
<b>Total_Seniority</b>	<b>-0.122** (-2.45)</b>	-	-	<b>-0.082* (-1.90)</b>
<b>Committee_Num</b>	-	<b>-0.288** (-2.42)</b>	-	-
<b>Seniority_Dum</b>	-	-	<b>-1.011*** (-2.70)</b>	-
MisconductSeverity\$	0.866*** (3.23)	0.935*** (3.77)	0.990*** (3.81)	0.825*** (3.22)
Total_Seniority*MisconductSeverity\$	-	-	-	-0.007* (-1.89)
Political_Connection	-2.621** (-2.02)	-2.377* (-1.92)	-2.565* (-1.87)	-2.700** (-2.15)
Political_Contribution	-0.101* (-1.78)	-0.105* (-1.75)	-0.103* (-1.73)	-0.091* (-1.71)
Lobby_SEC	-0.500** (-2.23)	-0.425** (-2.18)	-0.415** (-2.11)	-0.489** (-2.31)
Litigation Risk	0.967 (0.88)	1.027 (0.99)	1.045 (1.02)	0.972 (0.99)
Size	0.366 (1.15)	0.422 (1.41)	0.410 (1.01)	0.310 (1.02)
Leverage	-2.122 (-1.02)	-2.145 (-1.09)	-2.111 (-1.05)	-2.233 (-1.01)
MtB	0.156 (1.15)	0.159 (1.16)	0.165 (1.20)	0.167 (1.10)
Inst_Own	1.643* (1.90)	1.276* (1.81)	1.535* (1.90)	1.609* (1.80)
Analyst_Following	0.215 (0.60)	0.232 (0.50)	0.186 (0.50)	0.208 (0.55)
Distance_to_SEC	-0.375 (-1.50)	-0.359 (-1.38)	-0.212 (-1.13)	-0.372 (-1.50)
State, Industry, Auditor, and Year Fixed Effects	Yes	Yes	Yes	Yes
N	266	266	266	266
Adjusted R <sup>2</sup>	0.272	0.273	0.263	0.277



**Table 8: Congressional Committee Member Reelection Outcome and Prior Enforcement Actions in the State**

\*, \*\*, and \*\*\* indicate significance at the 90%, 95%, and 99% confidence level, respectively.

This table presents logit regressions examining whether conditional on undertaking a reelection campaign, the likelihood that a politician loses the reelection campaign is associated with a constituent firm receiving an AAER for financial misconduct in the two years prior to the reelection date. The dependent variable, *Turnover*, is an indicator variable set to one for firms that receive an AAER from the SEC for financial misconduct, and zero otherwise. The independent variable of interest is *Recent\_AAER*, an indicator variable set to one if in the two years prior to the reelection, at least one firm in the politician's district receives an SEC enforcement action for financial misconduct. In columns 1 and 3 to 6 we present result for tests using influential committee politicians' reelection observations. In column 2, we present results for a test using a sample of reelection campaigns for politicians on the ten most powerful unrelated congressional committees. All variables are defined in the Appendix. In all regressions, standard errors are Huber-White sandwich estimators and clustered at the firm level, and z-values are in parentheses. We present marginal effects in brackets. State, industry, year, and auditor fixed effects are included in all regressions.

	(1)	(2)	(3)	(4)	(5)	(6)
	<b>Dependent Variable: Turnover</b>					
	Firms in Influential Committee Politician Constituencies	Firms in Non-Influential Committee Politician Constituencies	AAER firms above median Firm Size	AAER firms below median Firm Size	Bankruptcy follows AAER	Bankruptcy does not follow AAER
<i>Sample:</i>						
Constant	7.556 (0.50)	-9.789*** (-5.59)	-1.356 (-1.05)	8.032 (0.50)	-1.110 (-0.90)	-0.235 (-0.25)
<b>Recent_AAER</b>	<b>0.090**[0.090]</b> <b>(2.20)</b>	<b>-0.035[-0.035]</b> <b>(-0.26)</b>	<b>0.652***[0.650]</b> <b>(2.62)</b>	<b>-0.303[-0.301]</b> <b>(-0.76)</b>	<b>0.950***[0.950]</b> <b>(2.86)</b>	<b>-0.502[-0.501]</b> <b>(-1.32)</b>
Close_Reelection	2.050*** (3.45)	1.822*** (2.88)	2.156*** (3.60)	2.122*** (3.72)	2.055*** (3.62)	2.002*** (3.45)
Seniority	0.042 (0.90)	0.050 (1.20)	0.048 (1.22)	0.045 (1.06)	0.042 (1.00)	0.045 (1.02)
Female	0.533 (1.02)	0.615 (1.30)	0.577 (1.33)	0.611 (1.29)	0.522 (1.15)	0.487 (0.99)
Democratic	-0.393 (-1.06)	-0.455 (-1.24)	-0.366 (-0.89)	-0.455 (-1.26)	-0.350 (-0.99)	-0.351 (-0.92)
President_Same_Party	-0.622 (-1.30)	-0.655 (-1.40)	-0.577 (-1.35)	-0.742 (-1.30)	-0.576 (-1.23)	-0.600 (-1.07)
Presidential_Election_Year	0.104 (0.87)	0.122 (0.95)	0.091 (0.80)	0.120 (0.89)	0.109 (0.96)	0.092 (0.85)
State_GDP_Growth	-13.255** (-2.20)	-14.178** (-2.26)	-14.285** (-2.33)	-15.112** (-2.32)	-13.109** (-2.05)	-13.289** (-2.16)
State_Unemployment_Rate	0.377*** (2.60)	0.345** (2.45)	0.330** (2.30)	0.350*** (2.62)	0.311** (2.32)	0.385*** (2.73)
<i>State and Year Fixed Effects</i>	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>
Observations	946	4,756	946	946	946	946
Pseudo R <sup>2</sup>	0.158	0.143	0.179	0.155	0.180	0.161

**Table 9: Subcommittee Seniority and Enforcement Against Financial Misconduct**

\*, \*\*, and \*\*\* indicate significance at the 90%, 95%, and 99% confidence level, respectively.

This table presents logit regressions of the likelihood that firms face SEC enforcement for financial misconduct on firms' influential subcommittee representation. The dependent variable, *Enforcement*, is an indicator variable set to one for firms that receive an AAER from the SEC for financial misconduct. The independent variable of interest is one of three proxies for the power of firms' influential committee representation: *Total\_Seniority*, *Committee\_Num*, or *Seniority\_Dum*. Each of these three variables of interest are affixed with *\_Sub* (*NonSub*), which captures the power of a firm's representation on SEC-relevant (non-SEC relevant) subcommittees within influential committees. All variables are defined in the Appendix. In all regressions, standard errors are Huber-White sandwich estimators and clustered at the firm level, and z-values are in parentheses. State, industry, year, and auditor fixed effects are included in all regressions.

	(1)	(2)	(3)
	<b>Dependent Variable: Enforcement</b>		
Constant	-7.334*** (-8.11)	-7.255*** (-8.46)	-7.611*** (-8.33)
<b>Total_Seniority_Sub</b>	<b>-0.026**[-0.020]</b> <b>(-2.50)</b>	-	-
<b>Total_Seniority_NonSub</b>	<b>-0.006*[-0.004]</b> <b>(-1.89)</b>	-	-
<b>Committee_Num_Sub</b>	-	<b>-0.138**[-0.122]</b> <b>(-2.37)</b>	-
<b>Committee_Num_NonSub</b>	-	<b>-0.039*[-0.031]</b> <b>(-1.80)</b>	-
<b>Seniority_Dum_Sub</b>	-	-	<b>-0.172**[-0.168]</b> <b>(-2.38)</b>
<b>Seniority_Dum_NonSub</b>	-	-	<b>-0.055*[-0.052]</b> <b>(-1.90)</b>
Political_Connection	-0.633** (-2.16)	-0.639** (-2.20)	-0.632** (-2.19)
Political_Contribution	-0.040** (-2.12)	-0.042** (-2.18)	-0.042** (-2.10)
Lobby_SEC	-0.030 (-1.29)	-0.029 (-1.27)	-0.028 (-1.27)
Litigation Risk	0.221 (0.55)	0.218 (0.46)	0.220 (0.57)
Size	0.560*** (5.31)	0.566*** (5.25)	0.556*** (5.29)
Leverage	-0.182 (-0.35)	-0.172 (-0.33)	-0.166 (-0.27)
MtB	-0.030* (-1.80)	-0.031* (-1.75)	-0.032* (-1.81)
Profit	0.025 (0.50)	0.026 (0.45)	0.026 (0.44)
Issuance	-0.336 (-1.55)	-0.342 (-1.60)	-0.355* (-1.77)
FRQ	-0.004 (-1.20)	-0.004 (-1.13)	-0.004 (-1.33)
Stdev_Cashflow	1.122* (1.81)	1.127* (1.80)	1.172* (1.84)
Stdev_Sales	0.955* (1.90)	0.930* (1.78)	0.935* (1.90)
Oper_Cycle	0.202* (1.80)	0.193* (1.77)	0.206** (1.90)
Inst_Own	0.955 (1.55)	0.950 (1.57)	0.956 (1.60)

Analyst_Following	-0.095 (-0.72)	-0.092 (-0.66)	-0.088 (-0.69)
Distance_to_SEC	-0.090 (-1.33)	-0.082 (-1.22)	-0.080 (-1.29)
Auditor_Share	-0.992 (-0.88)	-0.950 (-0.88)	-0.966 (-0.99)
Auditor_Tenure	-0.015 (-1.11)	-0.014 (-1.05)	-0.013 (-1.01)
Office_Size	-0.177 (-1.50)	-0.163 (-1.49)	-0.166 (-1.37)
GC_Dummy	0.633 (1.21)	0.629 (1.27)	0.619 (1.30)
<i>F-test: Subcommittee = Non-Subcommittee</i>	3.88**	2.81*	2.75*
<i>State, Industry, Year, and Auditor Fixed Effects</i>	Yes	Yes	Yes
N	17,017	17,017	17,017
Pseudo R <sup>2</sup>	0.140	0.141	0.140

**Table 10: House and Senate Influential Committee Seniority and Enforcement Against Financial Misconduct**

\*, \*\*, and \*\*\* indicate significance at the 90%, 95%, and 99% confidence level, respectively.

This table presents logit regressions of the likelihood that firms face SEC enforcement for financial misconduct on firms' House or Senate influential committee representation. The dependent variable, *Enforcement*, is an indicator variable set to one for firms that receive an AAER from the SEC for financial misconduct. The independent variable of interest is one of three proxies for the power of firms' influential committee representation: *Total\_Seniority*, *Committee\_Num*, or *Seniority\_Dum*. Each of these three variables of interest are affixed with *\_House* or *\_Senate*, which captures whether our measures of influential committee representation is measured for the House or Senate influential committees respectively. All variables are defined in the Appendix. In all regressions, standard errors are Huber-White sandwich estimators and clustered at the firm level, and z-values are in parentheses. State, industry, year, and auditor fixed effects are included in all regressions.

	(1)	(2)	(3)
	<b>Dependent Variable: Enforcement</b>		
Constant	-9.233*** (-4.10)	-8.356*** (-5.22)	-7.892*** (-5.11)
<b>Total_Seniority_House</b>	<b>-0.021**[-0.016]</b> <b>(-2.50)</b>	-	-
<b>Total_Seniority_Senate</b>	<b>-0.014**[-0.010]</b> <b>(-2.22)</b>	-	-
<b>Committee_Num_House</b>	-	<b>-0.108**[-0.092]</b> <b>(-2.09)</b>	-
<b>Committee_Num_Senate</b>	-	<b>-0.079**[-0.072]</b> <b>(-2.18)</b>	-
<b>Seniority_Dum_House</b>	-	-	<b>-0.177**[-0.175]</b> <b>(-2.37)</b>
<b>Seniority_Dum_Senate</b>	-	-	<b>-0.109**[-0.108]</b> <b>(-2.33)</b>
Political_Connection	-0.661** (-2.20)	-0.657** (-2.25)	-0.652** (-2.16)
Political_Contribution	-0.040* (-1.90)	-0.043* (-1.91)	-0.041* (-1.88)
Lobby_SEC	-0.029 (-1.22)	-0.026 (-1.21)	-0.028 (-1.30)
Litigation Risk	0.216 (0.66)	0.222 (0.70)	0.219 (0.67)
Size	0.568*** (5.20)	0.572*** (5.29)	0.577*** (5.35)
Leverage	-0.175 (-0.26)	-0.172 (-0.25)	-0.181 (-0.31)
MtB	-0.030* (-1.80)	-0.028* (-1.78)	-0.027* (-1.77)
Profit	0.022 (0.45)	0.023 (0.46)	0.021 (0.46)
Issuance	-0.330 (-1.55)	-0.327 (-1.52)	-0.321 (-1.59)
FRQ	-0.004 (-1.25)	-0.004 (-1.27)	-0.004 (-1.20)
Stdev_Cashflow	1.109* (1.78)	1.122* (1.78)	1.133* (1.80)

Stdev_Sales	0.893*	0.887*	0.892*
	(1.79)	(1.81)	(1.80)
Oper_Cycle	0.206*	0.202*	0.200*
	(1.89)	(1.91)	(1.87)
Inst_Own	0.872	0.897	0.887
	(1.50)	(1.63)	(1.53)
Analyst_Following	-0.085	-0.086	-0.082
	(-0.64)	(-0.71)	(-0.72)
Distance_to_SEC	-0.079	-0.081	-0.081
	(-1.33)	(-1.31)	(-1.26)
Auditor_Share	-0.867	-0.901	-0.883
	(-0.86)	(-0.86)	(-0.87)
Auditor_Tenure	-0.015	-0.017	-0.018
	(-1.22)	(-1.38)	(-1.47)
Office_Size	-0.172	-0.178	-0.180
	(-1.21)	(-1.13)	(-1.13)
GC_Dummy	0.575	0.567	0.607
	(1.20)	(1.29)	(1.28)
<hr/>			
<i>F-test: House Effect = Senate Effect</i>	0.92	0.45	1.20
State, Industry, Year, and Auditor Fixed Effects	Yes	Yes	Yes
N	17,017	17,017	17,017
Pseudo R <sup>2</sup>	0.142	0.141	0.142
<hr/>			