QUID PRO QUO? THE SEC OVERSIGHT ENFORCEMENT AND

CORPORATE LOBBYING

by

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This manuscript has been read and accepted for the Graduate Faculty in Business

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ABSTRACT

Quid Pro Quo? The SEC Oversight Enforcement and Corporate Lobbying

by

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Due to the private nature of its internal investigations, research on the SEC oversight enforcement is limited. By distinguishing between enforcement staff' decision to open an investigation (*investigation decision*) and commissioners' authorization of an enforcement action (*enforcement decision*), this study is the first to examine how these two decisions interplay to overcome the political capture while fulfilling the SEC's mission to protect investors. First, I do not find evidence that investigation decision is influenced by firms' political connections, whereas enforcement decision is affected by firms' lobbying efforts. Collectively, my results imply that there exists a misalignment between commissioners' political incentives and the staff' career incentives in the SEC oversight enforcement. My results also suggest that a firm's opportunistic lobbying during an investigation (*reactive lobbying*) is effective in reducing the probability of an SEC enforcement action, while habitual lobbying activities in anticipation of possible adverse events (*proactive lobbying*) do not shield a firm from regulatory scrutiny.

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CHAPTER ONE

Introduction

The oversight enforcement of the Securities and Exchange Commission (SEC) refers to an entire process from a preliminary inquiry to an internal investigation to an enforcement action against firms or individuals charged with securities fraud. Due to resource constraints limiting the capacity to pursue every securities violation, the SEC must exercise discretion in how to prioritize investigation targets and institute enforcement actions.

Research on regulatory oversight is rooted in a view of rational actors seeking to maximize their utility. On the one hand, regulatory capture theory postulates that firms and special-interest groups use money and votes to extract political rent and wield pressure on regulators (e.g., Stigler 1971, Peltzman 1976, Watts and Zimmerman 1978). On the other hand, the human capital hypothesis conjectures that career goals motivate regulators to practice rigorous investigations to demonstrate their competence to future employers (Zheng 2015, Vadenbergh et al. 2020). Although some studies document lax SEC enforcement on politically connected firms (e.g., Correia 2014, Yu and Yu 2012), the extent to which political connections mitigate regulatory interventions remain less explored primarily due to research design challenges. SEC investigations are privately conducted and unobservable to firm outsiders. This issue complicates the interpretations of the empirical association between political lobbying and SEC enforcement; that is, whether it is enforcement staff who are less likely to investigate politically connected firms, thereby resulting in a lower likelihood of enforcement actions or whether it is SEC commissioners who are less prone to authorize enforcement actions against those firms.

Using undisclosed SEC investigations to overcome empirical challenges, I study two

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research questions: first, the effect of habitual lobbying activities on enforcement staff' decision to open an investigation (*investigation decision*) and second, the effect of opportunistic lobbying efforts on commissioners' authorization of an enforcement action (*enforcement decision*). By distinguishing between these two decisions, this paper provides insights into how career and political incentives individually perceived by commissioners and enforcement staff optimize the SEC's oversight enforcement practices.

Although the SEC is responsible for monitoring and bringing charges against firms committing fraudulent misconduct, the SEC is under sustained pressure from its overseers who have ties with politically connected firms. Prior studies identify firms' political connections as frictions that impede the task of the SEC enforcement. If it is true that regulatory capture affects the SEC's enforcement discretion, I expect decreased investigative and enforcement activities directed toward politically connected firms. Such a finding would imply that the SEC is systemically captured by firms' political lobbying.

On the other hand, career incentives may dominate the SEC's regulatory decisions. Building a strong record of diligent work ethics and expertise may motivate regulators to conduct stringent enforcement practices based primarily on the leads and evidentiary fact. Brown et al. (2006) argue that firms with higher litigation risk and regulatory oversight have incentives to acquire political connections. To the extent that political connections signal a fraudulent firm's attempt to circumvent or evade regulatory interventions, I expect an increase in SEC oversight enforcement against politically connected firms.

I collect data on firms' lobbying activities from LobbyView and the Center for Responsive Politics (CRP) from 1998 (the first year the Lobbying Disclosure Act of 1995 required lobbying disclosure) through 2018. Unlike prior studies considering all lobbying

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activities (e.g., Correia 2014, Yu and Yu 2012), I retain lobbying aimed only at the Senate, the House of Representatives, the SEC, the Department of Justice (DOJ), and the Congressional Budget Office (CBO).[1] The existing literature on mechanisms through which firms exert political pressure on the SEC argues that lobbying firms form alliances with members of Congress who use budget appropriations, approvals of chair and commissioner appointments, and congressional hearings to influence the SEC's enforcement practices (Heese et al. 2017, Correia 2014). I collect lobbying activities directed at the DOJ because, under Rule 2 of the SEC's Rules Relating to Investigation, SEC staff frequently communicate and share investigative files with other governmental authorities (Missal et al. 2007). For the SEC's oversight enforcement activities, I obtain raw data on all closed SEC investigations between January 1, 2000 and August 2, 2017 from Blackburne et al. (2020) and Accounting and Auditing Enforcement Releases (AAERs).[2]

To assess the impact of firms' political connections at each stage in the oversight enforcement process, I begin my analyses by examining whether enforcement staff are less likely to initiate a formal investigation against lobbying firms, relative to non-lobbying firms. I do not find evidence that the likelihood of the SEC opening an investigation is statistically associated with a firm's lobbying activities, after controlling for firm characteristics associated with the SEC enforcement and predicted fraud scores derived from a machine learning model (Correia 2014, Bao et al. 2019). Recognizing that insignificant associations may be due to misspecifications or erroneous identification strategy, I conduct a battery of robustness tests to validate my result.

First, I examine the likelihood that a lobbying firm undergoes an investigation as a

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[1] For example, it does not seem plausible that lobbying activities toward the Department of Education is relevant to the SEC oversight enforcement.
[2] Blackburne et al. (2020) obtain undisclosed formal SEC investigation data through the Freedom of Information Act office of the SEC.

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function of *direct lobbying* channel (lobbying toward the SEC, the DOJ, or SEC revolving door lobbyists) and *indirect lobbying* channel (lobbying toward the Senate, the House of Representatives, or the CBO). For the subsample of lobbying firms, I find that neither direct nor indirect lobbying channels are statistically related to the likelihood of an SEC investigation.

I next refine the indirect lobbying channel by looking into lobbying toward SEC-relevant committees in Congress. Mehta and Zhao (2020) identify the Senate Committee on Banking, Housing, and Urban Affairs and House of Representatives Committee on Financial Services as committees with the most influence over the SEC with oversight jurisdiction. They document that congressional influence on the SEC impairs its regulatory effectiveness. Following the same notion, I hypothesize that firms lobbying members of Congress serving in the SEC-relevant committees are less likely to be subject to the SEC oversight enforcement than firms that do not lobby the SEC-relevant committees. The Lobbying Disclosure Act of 1995, however, does not mandate lobbying registrants to disclose the identity of recipients. If such information were available, I could have traced which committee lobbying payment was intended to. As an alternative, I analyze specific issue area codes disclosed in lobbying reports. As the two SEC-relevant committees are primarily concerned with matters related to finance/securities and taxation, I expect that firms lobbying on these issues are likely to contact members serving in the SEC-relevant committees.

The results show positive associations between lobbying issues on finance/securities and budget and the likelihood of an SEC investigation. It is possible that lobbying on sensitive issues involving finance/securities and budget appropriations may have a spillover effect on regulatory monitoring, resulting in a higher likelihood of an SEC investigation. Holzman et al. (2020) document that SEC investigation activities are positively associated with firms' visibility. As

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finance/securities and budgeting are salient issues that draw much attention from media and public scrutiny, firms lobbying on these issues may become more exposed to SEC staff' surveillance activities.

I also run probit regressions with an instrumental variable. Specifically, I use firm-level political risk as an instrument. Hassan et al. (2019) construct the measure using a computational linguistics approach by reading conference calls. Their paper documents that firms with high political risk are more likely to actively lobby and donate to politicians. The IV probit regression does not show a statistical relation between corporate lobbying activities and the probability of an SEC investigation.

Additionally, I substitute three-year lobbying with one-year lobbying activities prior to an onset of an investigation. It is possible that a firm's contemporaneous, newly established political connections exert a stronger influence on the staff' choice of investigation targets than those established in distant periods. The results do not present statistically significant relations.

To address the concern that lobbying firms and non-lobbying firms are systematically different, I construct an entropy-balanced sample using a vector of determinants that prior studies link to the SEC enforcement, as well as macro and micro factors through industry and year matches. The estimated coefficients across almost all specifications do not yield statistical associations between a firm's lobbying activities and the likelihood of the firm undergoing an SEC investigation. Taken together, my validity tests support that SEC staff' investigative activities are conducted based upon the merits of each case regardless of a firm's political profile.

I next examine whether commissioners' enforcement discretion is influenced by firms' opportunistic lobbying efforts. Unlike prior studies that utilize the presence (or expenditure

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level) of lobbying activities prior to enforcement outcomes, my analyses exploit the *percent change* in lobbying expenditures after the onset of an SEC investigation. This research design enables me to draw clearer inferences about the efficacy of corporate lobbying in the midst of an investigation, as I examine how lobbying firms opportunistically respond to an investigation. Results indicate that the increase in corporate lobbying expenditures subsequent to an SEC investigation is negatively associated with an AAER issuance. In terms of economic significance, one standard deviation increase in the percent change in lobbying expenditures corresponds to a 19.3 percent lower likelihood of receiving an AAER relative to the unconditional probability of receiving an AAER in my sample. As SEC investigations span 2.8 years on average in my sample, I also examine two-year percent change in lobbying expenditures. Consistent with previous analysis, I find a negative association between two-year percent change in lobbying expenditures and the likelihood of an AAER issuance. One standard deviation increase in the two-year percent change in lobbying expenditures translates to a 22.7 percent lower likelihood of an AAER issuance.

Following the same identification strategy as in the SEC investigation analyses, I then divide lobbying efforts into direct and indirect lobbying channels. Results are consistent with an indirect channel of lobbying efforts toward Congress, suggesting that firms seeking preferential treatment through congressional lobbying channel are less likely to face an SEC enforcement action. Contrary to my predictions, I generally do not observe statistical associations between direct lobbying efforts toward regulatory bodies and an AAER issuance. One possible explanation for this finding is that the SEC may be concerned about backfire if the public suspects the SEC of steering weaker enforcement practices against firms that lobby the SEC directly (Heese et al. 2017).

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Analyzing the relation between lobbying issues and enforcement decision, I find that the percent change in taxation-related lobbying expenditures is negatively associated with an incident of AAERs. Although I cannot definitively claim that the SEC-relevant committees overseeing taxation issues constitute the influence on commissioners' enforcement decisions, a key finding that a firm's lobbying efforts in seeking congressional influence during an investigation lead to a lower likelihood of an SEC enforcement action remains unchanged.

My study adds an important dimension to the literature on SEC enforcement. Prior research typically treats the SEC oversight enforcement as a centralized process in which investigation/enforcement decision is made uniformly across decision-making groups. However, the staff' investigative practices may not necessarily reflect senior management's political agenda. To the best of my knowledge, this paper is the first to study the misalignment of individual-level incentives between SEC commissioners and enforcement staff, as opposed to prior studies that focus on organization-wide incentives. Notwithstanding career and reputation concerns, commissioners are political appointees and therefore are keenly sensitive to the interests of Congress. As such, they are constrained in their decisions by external political pressures. However, enforcement staff are less susceptible to political pressure and have incentives to optimize investigative activities according to their career concerns. Collectively, my findings suggest that commissioners' political agenda may not be aligned with how enforcement staff shall perform their investigative duties.

This study also contributes to the literature on corporate lobbying. This paper is the first to distinguish between *proactive* and *reactive* lobbying engagement. Proactive lobbying activities relate to whether a firm's habitual lobbying engagement influences the staff' investigation decision, whereas reactive lobbying efforts pertain to a firm's increase in lobbying

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expenditures during an investigation as means to mitigate enforcement risks. While I do not find evidence that proactive lobbying activities curry favor with an SEC investigation, I document that the regulatory relief is more attributable to firms' strategic, reactive lobbying efforts. It is plausible that reactive lobbying efforts implicitly targeting matters related to an ongoing investigation are timelier and more effective in influencing SEC commissioners' enforcement decision.

Background

2.1. SEC oversight enforcement process

Figure 1 illustrates the SEC oversight enforcement process. It begins with a lead of possible existence of federal securities violations obtained from various sources such as external complaints, media reports, whistleblowers, and referrals from other divisions or government agencies. Enforcement staff determines whether it is appropriate to open a Matter Under Inquiry (MUI), which is a preliminary step towards instituting a full investigation.[3] Some considerations used to determine MUIs include, but are not limited to: (1) rules and statues violated; (2) magnitude of the violation; (3) losses and harm to investors; and (4) whether potentially harmed group is vulnerable or at risk. Based on the set of facts enforcement staff gathers, a MUI is either closed or converted to a formal investigation within sixty days. The decision to open an investigation indicates that the suspected violations of securities laws involve serious misconduct and merit an investment of the SEC resources.

During an investigation, the staff acts as an officer of the SEC with a formal order of investigation. The formal order empowers the staff with the authority to subpoena witnesses, administer oaths, and produce documents.[4] Communications between the SEC and individuals involved in an investigation are conducted through a Wells notice in which the staff informs the individuals of specific charges of securities violations and a preliminary determination of enforcement actions. The recipients can provide a written statement setting forth their position

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[3] Since 2009, the Division of Enforcement developed written procedures for review and approval of opening new investigations. The manual is available at www.sec.gov/divisions/enforce.shtml.

[4] Section 19(c) of the Securities Act, Section 21(b) of the Securities Exchange Act, Section 209(b) of the Advisers Act, and Section 42(b) of the Investment Company Act describe the SEC's authority to designate any officer to issue subpoenas and testify under oath.

regarding the subject matter to the staff.

Upon the completion of an investigation, enforcement staff submits an action memorandum with an analysis of the factual and legal foundation to SEC commissioners, seeking an approval of enforcement recommendations. Commissioners then vote on whether to approve or reject the recommendations in a closed meeting.

2.2. Guidelines for reporting lobbying activities

The Lobbying Disclosure Act of 1995 mandates lobby registrants and organizations to register (LD-1) and file lobbying activities report (LD-2) with the Secretary of the Senate and the Clerk of the House of Representatives.[5] Current rules require a lobbying registrant to register and report activities if a total income from a particular client exceeds $3,000 during a quarterly period. An organization is required to register and file reports if the total lobbying expenses exceed $13,000 during a quarterly period.[6] Registration is required within 45 days after a lobbyist is either employed or retained for the initial lobbying contract.

A lobbying registrant files separate lobbying reports for each client, while an organization files a single report covering all in-house lobbying activities for each quarterly reporting period. The lobbying report is required within 20 days after the end of the quarterly period.[7] A registrant is required to file the lobbying report regardless of whether lobbying activities are present during a period, checking "no activity" box on the report even if no

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[5] Under the Lobbying Disclosure Act of 1995, lobbying registrants are defined as entities with one or more lobbyists who act as lobbyists for outside clients. Organizations are those who employ in-house lobbyists. Note that lobbying registrants or organizations with in-house lobbyists are subject to the disclosure requirement, not clients (lobbying firms) which contracts with lobbying registrants. Throughout the paper, politically connected firms are lobbying firms.

[6] The registration thresholds have continued to increase over the past years since the enactment of the Lobbying Disclosure Act. One major amendment was made in 2007 (Honest Leadership and Open Government Act of 2007) in which the period for registration and lobbying activity report changed from a semiannual basis to a quarterly basis.

[7] Each lobbying activity report is assigned a unique identifier after being filed with the Congress. I use these unique identifiers to match lobbying information between LobbyView and CRP.

lobbying activities are carried out.

Hypothesis Development

According to regulatory capture theory, regulatory agencies are charged with responsibilities toward public interest objectives in their early period. As agencies mature, however, they become more concerned about the interests of the industries they regulate and are drawn away from serving the public interests. Stigler (1971) and Peltzman (1976) argue that special-interest groups use money and votes to extract political rent. Watts and Zimmerman (1978) discuss that political connections formed through lobbying and campaign contributions foist pressure on regulators and policy makers.[8] Revolving door lobbyists also play a pivotal role in influencing regulatory bodies (e.g., Bertrand et al. 2014, deHaan et al. 2015). As regulatory authorities are subject to outside checks and controls through congressional hearings, budget appropriations, and appointments approvals, they are likely to refrain from carrying out activities that can aggravate their overseers. In fact, members of Congress spend a significant amount of time and resources intervening with federal regulators on behalf of their constituents (Ohnesorge 2019).

Federal regulatory bodies such as the SEC have considerable discretion in prioritizing firms they investigate, while being subject to comparatively little regulatory accountability (e.g., Solomon and Soltes 2019, Zaring 2016, Barkow 2016). Prior studies document that a firm's

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[8] I focus on corporate lobbying activities and exclude PAC campaign contributions to study the impact of political connections on the SEC oversight enforcement. For lobbying, there is no cap with respect to the amount of lobbying expenditures that can be funded from corporate treasury. In contrast, firms are not allowed to contribute to political campaigns directly. Instead, they form Political Action Committees (PACs) through which executives, employees, and family members contribute voluntarily to support a candidate up to a maximum limit. Therefore, the managers' underlying goal of contributing to PACs can be contaminated (or diluted) by the contributions from employees and family members, which makes it not suitable for my study. In addition, PACs are cyclical, clustered around elections, and location (candidate)-dependent. Given the timing of SEC investigations is random, corporate lobbying is unambiguously a better candidate to study the impact of political connections. Finally, the size of PAC donations is comparatively nine times smaller than that of corporate lobbying (Milyo et al. 2000, Yu and Yu 2012).

political connections influence the way the SEC makes enforcement decisions. Correia (2014) finds that political connections are negatively related to SEC enforcement, as measured by the likelihood of financial restatements and the magnitude of monetary penalties. Yu and Yu (2012) document that lobbying firms evade fraud detection longer. Barkow (2016) postulates that, even if career staff seeks enforcement actions, political appointees convinced by well-connected firms may not move forward with enforcing the law. Heese et al. (2017), however, present a positive association between political connections and the probability of SEC comment letters. They attribute the contrasting findings to a risk of voter backlash when the public becomes aware of egregious regulatory favor rendered to politically connected firms.

On the other hand, human capital hypothesis posits that individuals who develop strong skills and experiences while working at the SEC may conduct stringent enforcement activities to demonstrate their competence to future employers (Zheng 2015). Vandenbergh et al. (2020) argue that the positive reputation of diligent work and expertise incentivizes regulators to perform duties by adhering to enforcement rules and regulations. If a regulator perceives the benefits of growing human capital, the regulator may become motivated to conduct rigorous enforcement practices regardless of firms' political connections.

Extant research relies solely on enforcement outcomes such as AAERs or monetary penalties, assuming that the SEC makes enforcement decisions uniformly across the organization. As I note in Section 2.1, the SEC oversight enforcement is a multi-stage, black box process involving the staff' investigation decision and commissioners' enforcement decision. It is possible that career incentives and political incentives each perceived by commissioners and enforcement staff are not aligned with each other. By taking advantage of undisclosed SEC investigations to distinguish between investigation and enforcement decisions, I take a novel

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approach to evaluating the impact of corporate political connections at each stage in the SEC oversight enforcement.[9]

First, it is unclear *ex ante* whether political connections should be associated with a likelihood of SEC staff' investigation. On the one hand, capitalizing on the notion of regulatory capture, the staff' decision to open an investigation may be influenced by corporate lobbying activities. The political climate lingering at the senior management may pervade the cultural norms on their investigation practices. If the staff share the same sense of the SEC's political agenda and are keen on senior management's political concerns, the political influence may govern the ways the staff select firms for an investigation. It is also possible that the staff receive countermanding or dilutive messages inconsistent with the SEC's code of conduct and ethics from senior management. If so, it implies that there is systemic regulatory capture at the SEC, resulting in a joint effect of the staff' and commissioners' propensity not to institute regulatory interventions against politically connected firms.

On the other hand, career concerns may dominate how enforcement staff decide on the choice of investigation targets. To the staff, building a strong record of due diligence guided by the SEC's enforcement rules of conduct creates an advantage for accessing future career opportunities. In other words, political incentives of senior management may not be aligned with career incentives of staff employees. It is also possible that corporate lobbying signals a fraudulent firm's attempt to circumvent or evade regulatory interventions. Then, enforcement staff may respond by increasing their investigative activities against the lobbying firm.

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[9] Prior studies on political connections and the SEC enforcement do not distinguish between lobbying activities and bribery. Some critics argue that the enforcement benefit discussed in the studies are subject to violations of the federal bribery and corruption statutes. Although it is not the focus of my study, I argue that corporate lobbying and its influence on regulatory outcomes do not constitute bribery, as there is no explicit guarantee of regulatory protection in exchange for lobbying payment. In addition, based on the principal-agent framework suggested by James (2011) and Dal Bo (2006) to illustrate the definition of bribery, I argue that corporate lobbying in the context of the SEC enforcement is not a form of bribery.

There are several reasons as to why commissioners may take a *laissez-faire* approach on staff-level investigations. First, congressional budget justification. The SEC reports and testifies its enforcement metrics during budget appropriations before Congress every year. According to Congressional Budget Justification Annual Performance Plan/Report, investigation volume and timeliness are presented as key performance metrics to justify its budget requests. Velikonja (2016) documents that the SEC overstates its performance statistics to avoid budget cuts and continue enforcing the securities laws. As the chair and commissioners are responsible for securing resources in a sustainable manner, they may support the staff' stringent investigative activities based on the merit of each case rather than influencing the choice of investigative targets. Second, impartial investigations can deter managerial malfeasance. As investigations are a costly process entailing media scrutiny, legal battles, and SEC subpoenas, firms regardless of their political connections may avoid fraudulent misconduct that can trigger regulatory interventions. Lastly, limited attention of SEC commissioners may hinder their involvement in every investigation decision. It would be unpragmatic for commissioners, among many other responsibilities across various divisions within the SEC, to determine which investigation should be opened or dropped. Therefore, I state my first hypothesis (in null form) as follows:

H1: *The SEC's investigation decision is not associated with corporate lobbying activities.*

Prior studies generally find that firms with political connections are less likely to be subject to enforcement actions. However, in the absence of information about the SEC's internal investigations, inferences from prior studies lead to two possible interpretations: (1) enforcement staff are less likely to open internal investigations against politically connected firms, thereby resulting in a lower likelihood of enforcement outcomes, or (2) the staff conduct investigations based on the merit regardless of firms' political ties, but commissioners are less likely to

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authorize enforcement actions against politically connected firms.

Anecdotally, the SEC is under sustained political pressure deriving from budget appropriations, appointment authority, and congressional oversight. Any adverse decisions against politically connected firms can jeopardize funding and resources that support the SEC as well as commissioners' reputation. As such, commissioners may be incentivized to suppress staff-level investigations against lobbying firms, let alone an approval of enforcement actions.

On the other hand, SEC commissioners may balance regulatory capture with political cost. If the public becomes aware of preferential enforcement treatment directed toward politically connected firms, the SEC can face strong criticisms from the public, media, as well as its overseers. This can jeopardize commissioners' future career down the line. As such, the concerns of such backlash may attenuate lenient enforcement practices against firms with political connections. In fact, Heese et al. (2017) find positive associations between political connections and the SEC's periodic filing reviews. Therefore, I state my second hypothesis (in null form) as follows:

H2: *The SEC's enforcement decision is not associated with corporate lobbying efforts.*

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Research Design and Sample Selection

4.1. Research design

I examine the relation between a firm's propensity to engage in lobbying activities and the likelihood of an SEC internal investigation (Hypothesis 1) using the following regression model:

$$\text{SEC\_Investigation}_{i,t+1} = a_0 + a_1 \text{Lobby\_3yr}_{i,t} + a_2 \text{Size}_{i,t} + a_3 \text{BM}_{i,t} + a_4 \text{Leverage}_{i,t} + a_5 \text{Age}_{i,t} + a_6 \text{SP500}_{i,t} + a_7 \text{Analysts}_{i,t} + a_8 \text{DACC}_{i,t} + a_9 \text{Distance}_{i,t} + a_{10} \text{Fraud\_score}_{i,t} + \text{Year\_FE} + \text{Industry\_FE} + \varepsilon \quad (1)$$

SEC_Investigation is an indicator variable set to one if the SEC initiates an internal investigation against a firm in year t+1, and zero if the SEC does not investigate the firm. My main variable of interest in equation (1) is *Lobby_3yr*, an indicator variable set to one if a firm engaged in corporate lobbying activities toward at least one of the contacts (i.e., the Senate, the House of Representative, SEC, DOJ, and CBO) at least once in years t, t-1, and t-2, and zero otherwise. [10] Consistent with my prediction following the framework of regulatory capture (human capital hypothesis), I expect a negative (positive) and significant coefficient on *Lobby_3yr*. I also substitute *Lobby_3yr* with *Lobby_1yr*, an indicator variable set to one if a firm engaged in lobbying activities toward at least one of the five contacts in year t to evaluate short-term lobbying effect.

I follow the stream of research on the SEC enforcement (e.g. Correia 2014 and Yu and Yu 2012) in selecting the vector of controls in equation (1). Specifically, I account for firm size (*MarketCap*), book-to-market (*BM*), financial risk (*Leverage*), firm age (*Age*) and the level of

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[10] Correia (2014) select a five- or three-year window depending on the estimation model for lobbying expenditures. Yu and Yu (2012) define a lobbying firm as a firm engaging in lobbying activities during the sample period (1998-2005).

discretionary accruals (*DACC*). Following Kedia and Rajgopal (2011) on the SEC enforcement preferences, I include the number of analysts' following (*Analysts*), an indicator variable for S&P 500 index (*SP500*) and a distance measure between a firm's headquarter and the closest SEC regional office (or the SEC office conducting an investigation) (*Distance*). Since it is unclear whether politically connected firms are likely to commit misconduct that can trigger an SEC investigation, I control for a firm's fraud risk (*Fraud_score*), a predicted fraud score developed by Bao et al. (2019) using a machine learning model. Finally, to account for macroeconomic and industry-specific factors, I include Fama-French 48 industry and year fixed effects. To accommodate the panel structure of the data, I cluster the standard errors by firm (Petersen 2009). Since the dependent variable is binary, I evaluate the model using a logit estimator. I also verify that the inferences are similar using a linear probability model. To mitigate the possible omitted variable concerns, I re-estimate the equation by substituting industry fixed effects with firm fixed effects. This specification enables me to focus on time-variant factors in the relationship.

I note that there exist various channels through which corporate lobbying influences SEC investigations. Thus, I analyze the likelihood a lobbying firm undergoes an investigation as a function of direct lobbying and indirect lobbying activities. To this end, I modify Equation (1) by substituting *Lobby_3yr* with *Lobby_Contact* to examine how each channel of lobbying activities affects the staff' investigation decision. I consider six alternative definitions of the treatment variable, *Lobby_Contact*:

(1) An indicator variable taking a value of one if lobbying contact is the Senate at least once in years t, t-1, and t-2, zero otherwise (*Lobby_Senate*),

(2) An indicator variable taking a value of one if lobbying contact is the House of Representatives at least once in years t, t-1, and t-2, zero otherwise (*Lobby_House),*

(3) An indicator variable taking a value of one if lobbying contact is the SEC at least once in years t, t-1, and t-2, zero otherwise (*Lobby_SEC*),

(4) An indicator variable taking a value of one if lobbying contact is the DOJ at least once in years t, t-1, and t-2, zero otherwise (*Lobby_DOJ*),

(5) An indicator variable taking a value of one if lobbying contact is the CBO at least once in years t, t-1, and t-2, zero otherwise (*Lobby_Budget*),

(6) An indicator variable taking a value of one if lobbying activities involve SEC revolving door lobbyists at least once in years t, t-1, and t-2, zero otherwise (*Lobby_Revolving*).

I use this approach to distinguish between indirect congressional effect and direct regulator effect on the SEC oversight enforcement.

Mehta and Zhao (2020) identify the Senate Committee on Banking, Housing, and Urban Affairs and House of Representatives Committee on Financial Services as committees with the most influence over the SEC with oversight jurisdiction. Following their notion, I expect that lobbying activities aimed at SEC-relevant committees should induce stronger pressure to the SEC, relative to lobbying activities toward other committees. The Lobbying Disclosure Act, however, does not mandate registrants to disclose the identity of individuals receiving lobbying payment.[11] Ideally, if the names of congressional members were disclosed in the report, I could have traced which committee of Congress lobbying payment was made to.

As an alternative approach, I collect issue area codes lobbyists mark in the reports (e.g.

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[11] Rulemaking petitions for transparent political spending were filed with the SEC in 2011 and 2014 to no avail. Former SEC Chair Mary Jo White was against the idea that the SEC should be involved in politics. In Feb 2019, a new bill was introduced (H.R. 1053) directing the SEC to issue guidance on mandatory political expenditure disclosures by public companies.

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FIN, TAX, or BUD).[12] Based on Mehta and Zhao (2020), the two SEC-relevant committees have jurisdiction on matters related to finance/securities-related issues and taxation. I assume that firms lobbying on these issues are likely to contact members of Congress serving in the SEC-relevant committees, while firms lobbying on natural environment, for example, are more likely to contact members serving in the Senate Committee on Environment and Public Works. As such, I substitute *Lobby_3yr* with *Lobby_Issue*, a proxy for lobbying activities toward SEC-relevant committees. I consider five alternative definitions for *Lobby_Issue*:

(1) An indicator variable taking a value of one if lobbying activities include financial institutions/securities issues (FIN) at least once in years t, t-1, and t-2, zero otherwise (*Lobby_Fin*),

(2) An indicator variable taking a value of one if lobbying activities include taxation/internal revenue code (TAX) at least once in years t, t-1, and t-2, zero otherwise (*Lobby_Tax*),

(3) An indicator variable taking a value of one if lobbying activities include accounting (ACC) at least once in years t, t-1, and t-2, zero otherwise (*Lobby_Acc*),

(4) An indicator variable taking a value of one if lobbying activities include budget/appropriations (BUD) at least once in years t, t-1, and t-2, zero otherwise (*Lobby_Bud*),

(5) An indicator variable taking a value of one if lobbying activities include torts (TOR) at least once in years t, t-1, and t-2, zero otherwise (*Lobby_Tor*),

I select FIN, TAX, and ACC issue codes because members of Congress contacted for these issues are most likely to be members on SEC-relevant committees.[13] I also examine

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[12] There are currently 79 lobby issue area codes available in the system. Registrants indicate lobbying issue codes in a lobbying report.
[13] I do not observe lobbying reports that explicitly mention issues related to SEC's ongoing investigations or regulatory enforcement actions against lobbying firms.

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lobbying activities on budget/appropriations issues (BUD), following prior literature identifying budget appropriations as one of the methods to exert pressure on the SEC. As a falsification test, I consider torts (TOR) issue code. Although congressional members contacted for torts issue may not serve in SEC-relevant committees, it is related with misdemeanors, violations, and litigations. Insignificant estimated coefficients on the variable contribute to mitigating the concern of spurious correlations as an alternative explanation.

Next, I examine the relation between SEC commissioners' enforcement decision and corporate lobbying efforts. After the SEC opens an investigation, a firm may employ various means to reduce the firm's legal liability and the probability of an enforcement action (e.g., cooperation with investigators, remediation efforts, etc.). I speculate that lobbying firms would strategically dedicate more resources to political lobbying during an ongoing investigation to curb the likelihood of an enforcement action (Hypothesis 2). Blackburne et al. (2020) document that corporate insiders become aware of an onset of a formal SEC investigation by showing a spike in insider selling activities around the period. I implement the analysis using the following model using a sample of firms that undergo an SEC investigation:

$$\text{SEC\_Enforcement}_{i,t+n} = a_0 + a_1 \text{Ch\_Lobby}_{i,t} + a_2 \text{Size}_{i,t} + a_3 \text{BM}_{i,t} + a_4 \text{Leverage}_{i,t} + a_5 \text{Age}_{i,t} + a_6 \text{SP500}_{i,t} + a_7 \text{Analysts}_{i,t} + a_8 \text{DACC}_{i,t} + a_9 \text{Distance}_{i,t} + \text{Year\_FE} + \text{Industry\_FE} + \varepsilon \quad (2)$$

SEC_Enforcement is an indicator variable set to one if a firm receives an AAER between the opening and two years after the closing of an investigation, conditional on the firm being investigated by the SEC, and zero otherwise. [14] My treatment variable in equation (2) is *Ch_Lobby*, the percent change in lobbying expenditures from year *t* when the SEC opens an

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[14] The SEC does not provide the nature nor the outcome of investigations (Blackburne et al. 2020). Thus, it is not possible to directly link AAERs to SEC investigations obtained from the SEC. I focus on AAERs issued on dates between the opening date of an investigation and within two years after the closing date of the investigation to ensure the sequential link from an investigation to final enforcement outcomes.

investigation to year *t+1*. Following the prediction of regulatory capture, I expect a negative and significant coefficient on *Ch_Lobby*.

My research design is innovative relative to that from prior literature, as I measure the change in lobbying expenditures upon the initiation of an SEC investigation. The results from this research design help understand how a firm's opportunistic, reactive lobbying efforts are related to an enforcement outcome.[15] In contrast, previous studies exclusively focus on the presence (or expenditure level) of lobbying activities prior to enforcement outcomes due to the private nature of the SEC's internal investigations. In addition, as lobbying activities tend to be persistent, it is difficult to draw causal inferences if I solely examine habitual lobbying activities prior to enforcement outcomes.

Following the same conjecture that lobbying firms can establish political connections through various channels, I substitute *Ch_Lobby* with *Ch_Lobby_Contact* to examine the efficacy of direct and indirect lobbying efforts on the enforcement decision. *Ch_Lobby_Contact* measures the percent change in a firm's lobbying expenditures from year t when the SEC opens an investigation to year t+1 for each contact. This specification allows me to evaluate how various lobbying channels provide lobbying firms with preferential enforcement treatment. I expect negative and significant estimated coefficients for all variables of interest.

I also consider whether a lobbying firm's political ties to SEC-relevant committees affect the enforcement decision. I substitute *Ch_Lobby* with *Ch_Lobby_Issue*, a variable measuring the percent change in a firm's lobbying expenditures from year t when the SEC opens an investigation to year t+1 for each lobbying issue area code.

Considering that an average length of an SEC investigation is 2.8 years (untabulated), I

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[15] Blackburne et al. (2020) argue that the opening of an investigation in unambiguously an important date in the life-cycle of the investigation. I assume a firm is highly motivated to lobby opportunistically around the onset of an investigation.

substitute *Ch_Lobby* with *Ch_Lobby_2yr*, the percent change in a firm's lobbying expenditures in year t when the SEC opens an investigation to the firm's average lobbying expenditures in years t+1 and t+2.[16] This treatment variable would reveal whether a firm's commitment to long-term strategic lobbying efforts for the duration of an SEC investigation induces stronger regulatory favor. In line with previous analyses, I construct *Ch_Lobby_Contact_2yr* and *Ch_Lobby_Issue_2yr* to analogously measure the percent change in lobbying expenditures from year t when the SEC opens an investigation to the average lobbying expenditures in years t+1 and t+2 with respect to each lobbying contact and lobbying issue area code. I expect negative and significant estimated coefficients for all variables of interest.

4.2. Sample Selection

I obtain data for the analyses from the Center for Responsive Politics (CRP), LobbyView (corporate lobbying), the SEC (internal investigations and AAERs), Compustat/CRSP (financial and market data). I begin by collecting from CRP and LobbyView all U.S. firms' lobbying activities from 1998 to 2018. One advantage of LobbyView is that one can run a query for lobbying activities by a firm identifier (GVKEY). LobbyView also makes periodic lobbying report easily accessible. Using a unique lobbying report identifier, I match lobbying information on LobbyView with that from CRP in which I obtain additional lobbying details including lobbyist identities (e.g., SEC revolving door lobbyists) and contacts for lobbying activities. Unlike prior research (Correia 2014, Yu and Yu 2011, Heese et al. 2017) considering all lobbying activities, I retain lobbying activities aimed only at the Senate, the House of Representatives, SEC, DOJ, and CBO. The Lobbying Disclosure Act of 1995 mandates lobby

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[16] Blackburne et al. (2020) find that the average length of SEC investigation is three years.

registrants to file lobbying activities report semiannually and was amended in 2007 to quarterly-basis reports. Thus, I aggregate lobbying activities by firm and year.

Firms generally lobby multiple contacts on multiple issues in each period. However, the lobbying report does not indicate the exact expenditure level for each contact (or issue). Thus, I assign the amount for each contact (or issue) by dividing the total lobbying expenditures by the total number of contacts (issues) disclosed in each lobbying report. This yields a sample of 71,488 firm-year observations with 11,379 lobbying activities. I present the sample selection procedure in Table 2, Panel A. As documented in Table 2, Panel B, between 8 and 21 percent of the sample firms conduct lobbying activities at least once in the past three years. Panel C presents a distribution of the sample lobbying firms by industry. I observe that certain industries display a high concentration of lobbying activities (e.g., utilities) relative to other industries. This is consistent with the prediction of the regulatory capture theory in that certain industries subject to strong regulation and litigation risk have incentives to engage in lobbying activities.

I collect data on SEC investigations from 2000 to 2017 and AAERs from 1999 to 2019. SEC investigations are obtained from filing the requests with the FOIA office at the SEC. The dataset includes information on the identities of firms investigated by the SEC, open and close dates of an investigation, and SEC regional office conducting the investigation. I obtain AAERs from AAER Dataset of University of Southern California. In Panel B, I observe between 1 and 7 percent of the sample firms are investigated internally by the SEC.

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CHAPTER FIVE

Results

5.1.Descriptive Statistics

Table 3 presents descriptive statistics. Starting with the full sample (Panel A), I note that 3.5 percent of firms undergo an SEC investigation at least once between 2000 and 2017. With respect to *Lobby_3yr (Lobby_1yr)*, I find that, on average, 16 (15) percent of firms engage in lobbying activities. For the subsample of lobbying firms, 98 percent of firms contact the Senate or House of Representatives for lobbying activities, while 5 (12) [2] percent of firms lobby the SEC (DOJ) [CBO]. SEC revolving door lobbyists (*Lobby_Revolving*) are involved in approximately 14 percent of lobbying activities. Turning to issue area codes disclosed in lobbying reports, I find that 18, 51, and 3 percent of firms conduct lobbying activities on finance/securities (*Lobby_Fin*), taxation/internal revenue code (*Lobby_Tax*), and accounting (*Lobby_Acc*), respectively. The mean values of *Lobby_Bud* (*Lobby_Tor*) indicates that 43 (7) percent of firms lobby on budgeting/appropriations (torts) issues. Taken together, most frequent lobbying activities in my sample firms are concentrated on taxation and budgeting issues.[17]

For the subsample of firms undergoing an SEC investigation, the mean value of *AAER* indicates that 15 percent of firms receive an enforcement action. Compared to lobbying expenditures in the year when the SEC commences an investigation, lobbying firms increase lobbying expenditures by 19 percent in the following year (*Ch_Lobby*). With respect to the change in lobbying expenditures by contacts, I find that lobbying firms increase lobbying expenditures aimed at the Senate and House of Representatives both by 20 percent (*Ch_Lobby_Senate* and *Ch_Lobby_House*), while they decrease lobbying expenditures toward

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[17] These observations are generally consistent with the evidence in Correia (2014).

the SEC (DOJ) [SEC revolving door lobbyists] by 4 (4) [6] percent. I do not observe the change in lobbying expenditures made to CBO among lobbying firms undergoing an investigation. Of five lobbying issue area codes examined in my analyses, I find that lobbying expenditures on taxation issues (*Ch_Lobby_Tax*) and finance issues (*Ch_Lobby_Fin*) display an increase by 8 percent and 1 percent, respectively, in the following year, whereas lobbying on other issues show negative or no change in expenditures in the subsequent year.

An investigation spans on average 2.84 years until enforcement staff closes the case (untabulated statistic). Thus, I turn to the change in lobbying expenditures for two years ahead after the SEC opens an investigation, lobbying firms increase lobbying expenditures by 29 percent (*Ch_Lobby_2yr*), a 10 percentage point higher relative to one-year change in lobbying expenditures (*Ch_Lobby*). I find that lobbying expenditures toward the Senate and House of Representatives increase by 31 percent and 29 percent, respectively, while lobbying expenditures toward the SEC (DOJ) [SEC revolving door lobbyists] decrease by 3 (4) [3] percent, respectively. With respect to lobbying issues, I observe an increase in expenditures of 3 percent, 11 percent, and 4 percent for finance/securities (*Ch_Lobby_Fin_2yr*), taxation (*Ch_Lobby_Tax_2yr*), and budgeting/appropriations issues (*Ch_Lobby_Bud_2yr*), respectively. However, lobbying firms decrease lobbying expenditures on tort issue by 2 percent.

Next, I compare the characteristics of lobbying (*Lobby_3yr*= 1) and non-lobbying (*Lobby_3yr*= 0) firm-year observations (Table 3, Panel B). I note that lobbying firms are larger (*Size*), undervalued (*BM*), older (Age), and have lower debt obligations (*Leverage*). They are more likely to be listed in S&P 500 index (*SP500*), are followed by more analysts who report quarterly EPS estimates (*Analysts*), and display lower discretionary accruals (*DACC*). The distance measure indicates that lobbying firms and non-lobbying peers are located at a similar

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distance from SEC offices. Using a machine learning approach, I find that lobbying firms score higher for fraud risk (*Fraud_score*).

5.2. The relation between corporate lobbying activities and an SEC investigation

I test whether firms engaging in lobbying activities are less likely to undergo an SEC investigation (Hypothesis 1) using Equation (1). Table 4 presents regression results. Contrary to the prediction following the regulatory capture, the estimated coefficients on *Lobby_3yr* and *Lobby_1yr* are not statistically significant after controlling for firm characteristics associated with the SEC enforcement. However, the estimated coefficient on *Lobby_3yr* is marginally positive when I do not control for *Fraud_score*. The result suggests that fraud risk is a confounding factor to the relationship between lobbying activities and an SEC investigation. Overall, I do not find that either long-term or short-term lobbying activities are associated with the staff' investigation decision. To address correlated omitted variable concern, I re-estimate equation (1) using firm fixed effects in place of the industry fixed effects using an OLS. The analysis yields results consistent to those in the main model, offering additional support for my inferences (untabulated).

To address how different lobbying channels influence the decision on investigation targets, I analyze lobbying activities by lobbying contacts disclosed in the reports. For five out of six specifications, the estimated coefficients on the treatment variables are not statistically significant (Table 5). For lobbying issue area codes, I find that the estimated coefficients on *Lobby_Fin* and *Lobby_Bud* are positive and statistically significant (Table 6).

5.3. The relation between corporate lobbying efforts and an SEC enforcement action

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In this section, I test whether commissioners are less likely to approve an enforcement action against a firm that engages in reactive lobbying efforts during an investigation. Table 7, Panel A presents regression results from estimating equation (2). Consistent with predictions following regulatory capture, the estimated coefficient on *Ch_Lobby* is significantly and negatively associated with the incident of an AAER, suggesting that a firm's reactive lobbying efforts by increasing lobbying expenditures subsequent to an SEC investigation lead to a lower likelihood of an enforcement action.

In terms of economic significance, the marginal effect of *Ch_Lobby* in the fully specified model is -0.0321 (untabulated). The estimated coefficient and sample statistics imply that one standard deviation increase in the percent change of lobbying expenditures corresponds to a 19.3 percent lower likelihood of an AAER issuance, relative to the unconditional probability of receiving an AAER in my sample ($-0.0321*0.9113/0.1517 = -0.193$).

I then consider reactive lobbying efforts based on lobbying contacts to understand how direct and indirect lobbying efforts influence an enforcement decision. Table 7, Panel A presents that only indirect lobbying channels (i.e., lobbying toward the Senate and House of Representatives) are negatively associated with the likelihood of an AAER. In terms of economic significance, one standard deviation increase in the percent change of lobbying expenditures toward the Senate (House of Representatives) corresponds to a 16.8 (22.1) percent lower likelihood of an AAER issuance.

Next, I investigate how a firm's political ties to SEC-relevant committees are related to enforcement decision. Table 7, Panel B presents the results. Column 2 shows that the change in tax-related lobbying expenditures (*Ch_Lobby_Tax*) is negatively associated with the likelihood of an AAER issuance. As a falsification test, I repeat the analysis focusing on torts issue (column

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5). Consistent with my expectations, the estimated coefficient for *Ch_Lobby_Tor* is economically and statistically insignificant.

As an SEC investigation lasts for 2.8 years on average, I re-estimate equation (2), substituting *Ch_Lobby* with variables indicating the percent change in lobbing expenditures for two years ahead after the SEC opens an investigation. Table 8, Panel A presents that *Ch_Lobby_2yr* is negatively associated with an incident of an AAER. In terms of economic significance, the marginal effect of *Ch_Lobby_2yr* in the fully specified model is -0.0334 (untabulated). This indicates that one standard deviation increase in the percent change of lobbying expenditures for two-years ahead during an SEC investigation corresponds to a 22.7 percent lower likelihood of an AAER issuance (-0.0334*1.0290/0.1517= -0.227).

With respect to direct and indirect lobbying channels, the results are generally consistent with those in Table 7, Panel A. Lobbying efforts via the indirect channel for two-years are negatively and significantly related to an AAER issuance. Economically, one standard deviation increase in the percent change of lobbying expenditures toward the Senate (House of Representatives) for two years corresponds to a 18 (25.9) percent lower likelihood of an AAER issuance. Interestingly, I find firms that increase lobbying expenditures directly toward the SEC for two years are more likely to receive an AAER after an investigation.

In Panel B, I re-estimate the analyses using lobbying issue area codes with two-year percent change. The results are consistent with those in Table 7, Panel B. the estimated coefficient for *Ch_Lobby_Tax_2yr* is negatively associated with an incident of an AAER. Collectively, the evidence supports that regulatory capture through reactive lobbying efforts occurs at the SEC's commissioner level.

5.4. Robustness Tests and Additional Analyses

5.4.1. Instrumental variable on SEC investigation analyses

To address the endogeneity of corporate lobbying activities in Hypothesis 1, I run probit regressions with an instrumental variable. Specifically, I use the firm-level political risk as an instrument. Hassan et al. (2019) construct the measure using a computational linguistics approach by reading conference calls on eight topics related to economic policy, environment, health care, security & defense, tax policy, technology & infrastructure, institutions, and trade. Their paper documents that firms with high political risk are more likely to actively lobby and donate to politicians.

I find that a firm's political risk is strongly associated with proactive lobbying activities. In the first stage regression of political risk (*PRisk*) on all explanatory variables (Table 9, column 1), the partial F-statistic of *PRisk* is 209.99. This value indicates that a firm's political risk is highly correlated with the firm's tendency to engage in lobbying activities but is unlikely to be associated with the staff' investigation decision. In column 2, the IV probit regression does not show a statistical relation between proactive lobbying activities and the probability of an SEC investigation.

5.4.2. Entropy balancing

My main analyses use a pooled sample of both lobbying and non-lobbying firms. A potential concern is that the two group of firms are systematically different. I consider entropy balancing approach to address the concern. I construct an entropy-balanced sample using a vector of determinants prior studies links to the SEC enforcement, as well as residual macro and micro factors through industry and year matches. These variables mirror the control variables I use in Equations (1) and (2).

Entropy balancing employs a weighting algorithm that "involve[s] exact balance on the first, second, and possibly higher moments of the covariate distributions in the treatment and the reweighted control sample" (Hainmueller, 2012).[18] I set balance constraints for the covariates at one and the minimum degree for convergence (i.e., tolerance) at 0.015. I present the balance of covariates in Table 10, Panel A. I observe the vector of controls with standardized differences and variance ratios are comparable between lobbying and non-lobbying firms, indicating that the balancing procedure is effective. Re-estimating the equations using the entropy-balanced sample, I find the estimated coefficients on *Lobby_3yr*, *Lobby_Contact*, and *Lobby_Issue* are generally consistent with my main results (Table 10, Panel B).

5.4.3. *The relation between a firm's fraud level and lobbying decision*

Ex ante, it is unclear whether a firm' lobbying decision is correlated with the firm's fraud risk. Hill et al. (2013) discuss the factors that can incentivize a manager to seek political connections, one of them being value enhancing. Corporate lobbying should benefit a firm's value through increasing revenues or, most notably, decreasing firm risk. Similarly, Brown et al. (2006) argue that firms with higher litigation risk and regulatory oversight have incentives to acquire political connections.

If a firm has fraudulent intent (e.g., illegal insider trading or financial misreporting), the firm may have strong motives to organize political activities with a goal of circumventing or evading regulatory interventions. In this case, the decision to conduct lobbying activities reflects lobbying firms' broader strategy to manage enforcement risk. Thus, I posit that firms committing misdemeanors and violations of securities laws may increase lobbying expenditures lest they

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[18] McMullin and Schonberger (2019) find that entropy balancing (EB) is superior to other matching schemes (OLS or propensity score matching) in that EB equalizes higher-order moments of covariate distribution between treatment and control groups and minimizes both type I and type II errors. In addition, EB requires less researcher discretion unlike PSM.

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spur potential SEC investigations. I implement the analysis using the following model:

$$\text{Lobby\_up}_{i,t} = a_0 + a_1 \text{Fraud\_score}_{i,t} + a_2 \text{Size}_{i,t} + a_3 \text{BM}_{i,t} + a_4 \text{Leverage}_{i,t} + a_5 \text{CF}_{i,t} + a_6 \quad (3)$$
$$\text{R\&D}_{i,t} + a_7 \text{HHI}_{i,t} + \text{Year\_FE} + \text{Industry\_FE} + \varepsilon$$

The dependent variable in equations (3) is *Lobby_up*, an indicator variable set to one if a firm increases lobbying expenditures from year t to year t+1, and zero otherwise. If firms have a broader tendency to commit financial misconduct that can trigger an SEC investigation, the firms will allocate more resources on lobbying to seek political protection. I expect a positive and significant estimated coefficient on *Fraud_score*, (i.e., $a_1 > 0$), consistent with a higher likelihood of increasing corporate lobbying activities to evade regulatory intervention. The vector of controls follows prior research on the determinants of corporate lobbying (Hill et al. 2013) for equation (3).

As shown in Table 11, firms with high predicted fraud scores are more likely to increase lobbying expenditures in subsequent periods. In terms of economic significance, the marginal effect of *Fraud_score* implies that one standard deviation increase in a firm's predicted fraud score corresponds to a 5.1 percent higher likelihood of increasing lobbying expenditures in the next period relative to the sample mean (untabulated).

5.4.4. *Administrative proceedings vs. Civil Litigation as a proxy for SEC commissioners' enforcement decision*

In the main analyses, I use AAERs as a proxy for SEC commissioners' enforcement decision. However, it is possible that there are cases in which commissioners are compelled to impose sanctions on politically connected firms whose malfeasance is too evident and too salient (i.e., garnering more media attention). Failure to exercise its authority to charge penalties on those firms will raise the public's concern about the integrity of the SEC. Then, the question becomes whether SEC commissioners have alternative means to provide preferential treatment to

lobbying firms, should there be an enforcement action. To address the question, I offer another proxy for commissioners' enforcement discretion: (1) the decision to institute administrative proceedings (APs) before an administrative law judge and (2) the decision to litigate in federal court. Referred to as *prosecutorial decision*, commissioners' enforcement discretion can entail the type of enforcement forum.

The type of forum through which the SEC brings enforcement actions is an interesting question. The director of Division of Enforcement, Andrew Ceresney, announced in 2014 that the SEC will bring more APs after the Dodd-Frank Act, as the statutory change expanded the SEC's authority, allowing it to enforce regulations against unregistered firms and individuals. *Wall Street Journal* (WSJ) analyzed the outcomes of the SEC's expanded jurisdiction based on the type of forum and reported that defendants are more likely to lose when the SEC litigated them in the APs than when the SEC litigated them in federal court (WSJ, 2014). The article argued that the administrative law judges are biased in favor of the SEC, one that is referred to as taking advantage of a "home court." In academic literature, Velikonja (2018) finds that the study design by WSJ is misleading and that the SEC is less likely to win in cases sued for insider trading and accounting fraud. Choi and Pritchard (2017) report an increase of APs cases and a decrease of litigations in court after the Dodd-Frank Act.

Although these questions are very important, a comprehensive examination is beyond the score of the paper. Nevertheless, I provide a preliminary analysis by investigating which prosecutorial forum the SEC is more likely to take against lobbying firms. Specifically, I evaluate the likelihood that firms engaging in reactive lobbying efforts during an investigation are more likely to be litigated in APs relative to in federal court.

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Table 12 presents the results. In my sample, the SEC brings either APs only or both APs and civil litigations against firms after an investigation. I re-estimate equation (2), substituting *SEC_Enforcement* with *AP_Civil*, an indicator variable set equal to 1 if the SEC litigates a firm in both APs and federal court, and 0 if the SEC brings only APs. I find a negative relation between the change in lobbying expenditures toward the SEC and *AP_Civil*, suggesting that firms engaging in lobbying efforts toward the SEC directly are more likely to settle an enforcement case through APs only.

5.4.5. *Political affiliation of SEC commissioners*

Prior law literature posits that judges' political affiliation plays an important role in predicting lawsuit outcomes (Choi et al. 2015, Epstein et al. 2015). Liberal judges are associated with higher litigation risks to firms than conservative judges. Huang et al. (2019) find that firms headquartered in liberal circuits face a higher likelihood of being sued in class action than those in conservative circuits. Similarly, Republican-leaning judges are inclined to rule in favor of business and corporations (Kang and Shepherd 2015).

SEC commissioners are political appointees by the President and Congress with staggered, five-year terms. Governed by administrative law doctrine, the SEC possess the executive power to administer law enforcement. If federal judges' political characteristics can affect judicial decision-making and lawsuit outcomes, it is possible that commissioners' political affiliation is also associated with the SEC oversight enforcement. Following the same notion, I expect that Republican-leaning (Democratic-leaning) panel of SEC commissioners are less (more) like to authorize an enforcement action against firms.

I first measure the political affiliation for the panel of commissioners each year (*SEC_PA*) by adding together an indicator set to 1 (0) [-1] if the commissioner is identified as Democrat

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(Independent) [Republican]. Then, I re-estimate equation (2) by including *SEC_PA* as an additional explanatory variable. The results find that the estimated coefficients for the change in lobbying expenditures around an SEC investigation remain statistically significant (Table 13). In addition, I observe statistically significant positive associations between *SEC_PA* and *AAER* across all specifications, suggesting that Democratic-learning panel of SEC commissioners are more likely to approve an enforcement action subsequence to an investigation.

5.4.6. *Meetings between SEC Chair and firms under investigation*

Zheng et al. (2019) present another venue of facilitating regulatory capture through meetings with SEC Chair. They argue that politically connected firms or firms under SEC investigations seek out closed-door meetings with SEC Chair as a source of negotiating for and obtaining regulatory favors. They find that firms meeting with SEC Chair receive lower monetary penalties. Similarly, it is also possible that a firm under a formal investigation may ask politicians representing the state where the firm is headquartered in to speak favorably to SEC Chair on behalf of the firm.

As such, I include an indicator variable (*Chair_Firm_Meet*) set to 1 if SEC Chair is scheduled to have a meeting with a firm during a formal investigation. Then I re-estimate equation (2) by including *Chair_Firm_Meet* as an additional explanatory variable. In addition, I re-run equation (2) by including another indicator variable (*Chair_Congress_Meet*) set to 1 if SEC Chair meets members of Congress representing the state where a firm is headquartered in during an investigation. I find consistent, robust results across different specifications, suggesting that the efficacy of reactive lobbying efforts remains considerably material (Table 14).

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CHAPTER SIX

Conclusion

My analyses are rooted in the tension between political incentives and career incentives at the SEC. The implication of the misalignment between the two incentives is that the SEC mitigates political influence from its overseers while satisfying the duty to protect investors. Distinguishing between enforcement staff' investigation decision and commissioners' enforcement decision, I offer two key inferences. First, the preferential treatment deriving from corporate political investment materializes during the final stage in the SEC oversight enforcement when commissioners deliberate the case. Second, the staff exercise due diligence in their stringent investigative activities, targeting firms regardless of their political profile. Collectively, this study supports that the incentive misalignment between commissioner and enforcement staff helps the SEC achieve the conflicting objectives.

In addition, this paper is the first to empirically measure and analyze two different types of lobbying engagement: proactive lobbying activities and reactive lobbying efforts. I present evidence suggesting that reactive lobbying efforts upon the opening of an SEC investigation are effective in mitigating enforcement risk, whereas proactive lobbying activities do not necessarily generate regulatory favor for politically connected firms.

Despite extensive tests, there are some caveats. First, I note that the scope of my analyses is limited by the fact that lobbying reports never explicitly make references to an active SEC investigation. As a matter of fact, lobbying in exchange for enforcement leniency may constitute violations of federal bribery and corruptions statutes. My research design, however, offers a unique setting to empirically evaluate the efficacy of corporate lobbying on the SEC enforcement.

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Other sources of concern are also present. For example, there are confounding factors associated with a firm's choice to engage in lobbying such as an introduction of new bills and lobbying activities conducted by peer firms (Hill et al. 2013). Many firms express their positions on specific bills introduced in Congress by means of lobbying. However, provided that the timing of SEC investigations is exogenous and that lobbying firms must file lobbying activities report every quarter once registered, my analyses are less likely to have concerns of sample selection bias.

Endogeneity may also arise from firms' willingness to cooperate during an investigation. Referred to as Enforcement Cooperation Initiative, the program encourages firms and individuals to cooperate with an investigation in exchange for reduced penalties. Files (2012) finds that firms cooperating with the SEC are less likely to receive sanctions and are rewarded with lower monetary penalties. It is possible that lobbying firms in my sample have received cooperation credit during an investigation, which can possibly lead to the lower likelihood of AAERs. Unfortunately, how comprehensively firms cooperate with an investigation and how the SEC weighs the degree of cooperation are not directly observable to firm outsiders. I relegate the thorough examination of the issue to future research.

My findings inform a wide audience including market participants and practitioners. The evidence adds credence to the efficacy of the SEC's investigations. SEC staff serve the public interest by diligently monitoring and investigating firms regardless of their political connections. My study also highlights the considerations during an enforcement process other than the merits of the case.

Table 1. Variable definitions

Variable Name	Definition	Data Source
SEC_Investigation	An indicator variable set to 1 if the SEC opens an investigation on a firm in year t+1, and 0 if the SEC does not open an investigation on the firm in year t+1.	SEC Edgar
AAER	An indicator variable set to 1 if a firm receives an AAER during or within two years after a formal SEC investigation closes, and 0 if a firm does not receive an AAER during or within two years after a formal SEC investigation closes.	SEC Edgar
Lobby_3yr	An indicator variable set equal to 1 if a firm contacts the Senate, the House of Representatives, the SEC, the DOJ, or Congressional Budget Office for lobbying activities at least once in years t, t-1, or t-2, and 0 otherwise.	CRP and LobbyView
Lobby_1yr	An indicator variable set equal to 1 if a firm contacts the Senate, the House of Representatives, the SEC, the DOJ, or Congressional Budget Office for lobbying activities in year t and 0 otherwise.	CRP and LobbyView
Lobby_Senate	An indicator variable set equal to 1 if a firm contacts the Senate for lobbying activities at least once in years t, t-1, or t-2, and 0 otherwise.	CRP and LobbyView
Lobby_House	An indicator variable set equal to 1 if a firm contacts the House of Representatives for lobbying activities at least once in years t, t-1, or t-2, and 0 otherwise.	CRP and LobbyView
Lobby_SEC	An indicator variable set equal to 1 if a firm contacts the SEC for lobbying activities at least once in years t, t-1, or t-2, and 0 otherwise.	CRP and LobbyView
Lobby_DOJ	An indicator variable set equal to 1 if a firm contacts the DOJ for lobbying activities at least once in years t, t-1, or t-2, and 0 otherwise.	CRP and LobbyView
Lobby_Budget	An indicator variable set equal to 1 if a firm contacts the Congressional Budget Office for lobbying activities at least once in years t, t-1, or t-2, and 0 otherwise.	CRP and LobbyView
Lobby_Revolving	An indicator variable taking a value of one if lobbying activities involved SEC revolving door lobbyists at least once in years t, t-1, and t-2, and 0 otherwise	CRP and LobbyView
Lobby_Fin	An indicator variable set equal to 1 if a firm conducts lobbying activities on financial institutions/securities issues at least once in years t, t-1, or t-2, and 0 otherwise.	CRP and LobbyView
Lobby_Tax	An indicator variable set equal to 1 if a firm conducts lobbying activities on taxation/internal revenue code issues at least once in years t, t-1, or t-2, and 0 otherwise.	CRP and LobbyView

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Lobby_Acc	An indicator variable set equal to 1 if a firm conducts lobbying activities on accounting issues at least once in years t, t-1, or t-2, and 0 otherwise.	**CRP and LobbyView**
Lobby_Bud	An indicator variable set equal to 1 if a firm conducts lobbying activities on budget/appropriations issues at least once in years t, t-1, or t-2, and 0 otherwise.	**CRP and LobbyView**
Lobby_Tor	An indicator variable set equal to 1 if a firm conducts lobbying activities on torts issues at least once in years t, t-1, or t-2, and 0 otherwise.	**CRP and LobbyView**
Ch_Lobby	The percent change in a firm's lobbying expenditures from year t when the SEC opens an investigation to year t+1.	**CRP and LobbyView**
Ch_Lobby_Senate	The percent change in a firm's lobbying expenditures toward the Senate from year t when the SEC opens an investigation to year t+1.	**CRP and LobbyView**
Ch_Lobby_House	The percent change in a firm's lobbying expenditures toward the House of Representatives from year t when the SEC opens an investigation to year t+1.	**CRP and LobbyView**
Ch_Lobby_SEC	The percent change in a firm's lobbying expenditures toward the SEC from year t when the SEC opens an investigation to year t+1.	**CRP and LobbyView**
Ch_Lobby_DOJ	The percent change in a firm's lobbying expenditures toward the DOJ from year t when the SEC opens an investigation to year t+1.	**CRP and LobbyView**
Ch_Lobby_Budget	The percent change in a firm's lobbying expenditures toward the Congressional Budget Office from year t when the SEC opens an investigation to year t+1.	**CRP and LobbyView**
Ch_Lobby_Revolving	The percent change in a firm's lobbying expenditures using SEC revolving door lobbyists from year t when the SEC opens an investigation to year t+1.	**CRP and LobbyView**
Ch_Lobby_Fin	The percent change in a firm's lobbying expenditures on issues related to financial institutions/securities from year t when the SEC opens an investigation to year t+1.	**CRP and LobbyView**
Ch_Lobby_Tax	The percent change in a firm's lobbying expenditures on issues related to taxation/internal revenue code from year t when the SEC opens an investigation to year t+1.	**CRP and LobbyView**
Ch_Lobby_Acc	The percent change in a firm's lobbying expenditures on issues related to accounting from year t when the SEC opens an investigation to year t+1.	**CRP and LobbyView**

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Ch_Lobby_Bud	The percent change in a firm's lobbying expenditures on issues related to budget/appropriations from year t when the SEC opens an investigation to year t+1.	**CRP and LobbyView**
Ch_Lobby_Tor	The percent change in a firm's lobbying expenditures on issues related to torts from year t when the SEC opens an investigation to year t+1.	**CRP and LobbyView**
Ch_Lobby_2yr	The percent change from a firm's lobbying expenditure in year t when the SEC opens an investigation to the firm's average lobbying expenditures in years t+1 and t+2.	**CRP and LobbyView**
Ch_Lobby_Senate_2yr	The percent change from a firm's lobbying expenditures toward the Senate in year t when the SEC opens an investigation to the firm's average lobbying expenditures toward the Senate in years t+1 and t+2.	**CRP and LobbyView**
Ch_Lobby_House_2yr	The percent change from a firm's lobbying expenditures toward the House of Representatives in year t when the SEC opens an investigation to the firm's average lobbying expenditures toward the House of Representatives in years t+1 and t+2.	**CRP and LobbyView**
Ch_Lobby_SEC_2yr	The percent change from a firm's lobbying expenditures toward the SEC in year t when the SEC opens an investigation to the firm's average lobbying expenditures toward the SEC in years t+1 and t+2.	**CRP and LobbyView**
Ch_Lobby_DOJ_2yr	The percent change from a firm's lobbying expenditures toward the DOJ in year t when the SEC opens an investigation to the firm's average lobbying expenditures toward the DOJ in years t+1 and t+2.	**CRP and LobbyView**
Ch_Lobby_Budget_2yr	The percent change from a firm's lobbying expenditures toward the Congressional Budget Office in year t when the SEC opens an investigation to the firm's average lobbying expenditures toward the Congressional Budget Office in years t+1 and t+2.	**CRP and LobbyView**
Ch_Lobby_Revolving_2yr	The percent change from a firm's lobbying expenditures using SEC revolving door lobbyists in year t when the SEC opens an investigation to the firm's average lobbying expenditures using SEC revolving door lobbyists in years t+1 and t+2.	**CRP and LobbyView**
Ch_Lobby_Fin_2yr	The percent change from a firm's lobbying expenditures on issues related to financial institutions/securities in year t when the SEC opens an investigation to the firm's average lobbying expenditures for the same issue code in years t+1 and t+2.	**CRP and LobbyView**

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Ch_Lobby_Tax_2yr	The percent change from a firm's lobbying expenditures on issues related to taxation/internal revenue code in year t when the SEC opens an investigation to the firm's average lobbying expenditures for the same issue code in years t+1 and t+2.	**CRP and LobbyView**
Ch_Lobby_Acc_2yr	The percent change from a firm's lobbying expenditures on issues related to accounting in year t when the SEC opens an investigation to the firm's average lobbying expenditures for the same issue code in years t+1 and t+2.	**CRP and LobbyView**
Ch_Lobby_Bud_2yr	The percent change from a firm's lobbying expenditures on issues related to budget/appropriations in year t when the SEC opens an investigation to the firm's average lobbying expenditures for the same issue code in years t+1 and t+2.	**CRP and LobbyView**
Ch_Lobby_Tor_2yr	The percent change from a firm's lobbying expenditures on issues related to torts in year t when the SEC opens an investigation to the firm's average lobbying expenditures for the same issue code in years t+1 and t+2.	**CRP and LobbyView**
Lobby_up	An indicator variable set equal to 1 if a firm increases lobbying expenditures from year t to year t+1, and 0 otherwise.	**CRP and LobbyView**
Size	The natural logarithm of a firm's market capitalization.	**Compustat**
BM	Book to market ratio (CEQ/PRCC_f*CSHO).	**Compustat**
Leverage	The sum of long-term debt and debt in current liabilities divided by total assets ((DLTT+DLC/AT).	**Compustat**
Age	The number of years from the first date in which a firm appears in Compustat.	**Compustat**
SP500	An indicator variable set equal to 1 if a firm is one of the S&P 500 constituents, and 0 otherwise.	**Compustat**
Analysts	The number of analysts issuing quarterly EPS forecasts during the fiscal year.	**IBES**
DACC	Performance matched discretionary accruals. See Kothari et al. (2005).	**Compustat**
Distance	The natural logarithm of a distance between a firm's headquarter office and the closest SEC regional office (or the SEC regional office conducting an investigation). See Kedia and	**SEC and Compustat**

Rajgopal (2011)

Fraud_score	An accounting fraud prediction metric using machine learning approach	**Bao et al. (2019)**
CF	Operating income before depreciation net of interest expense, income taxes, and common dividends, scaled by total assets ((OIBDP-XINT-TXT-DVC)/AT).	**Compustat**
R&D	The ratio of research and development expenditures to revenues (XRD/REVT).	**Compustat**
HHI	Hirschmann-Herfindahl index, calculated at the two-digit SIC level.	
SEC_PA	The sum of SEC commissioner's political affiliation indicator set to 1 (0) [-1] if the commissioner is identified as Democrat (Independent) [Republican].	**SEC**
PRisk	The standardized average of the transcript-based scores of political risk for a given firm and year	**Hassan et al. (2019)**

Table 2. Sample selection and distribution by year

Panel A. Sample selection

Sample Selection	Investigation Analyses	Enforcement Analyses
Firm-years with matching Compustat, lobbying reports, SEC investigations 1998-2018 excluding non-U.S.firms	217,317	217,317
Less firm-years with missing variables	(80,642)	
Less firm-years with observations in years <1999	(31,917)	
Less firm-years with missing machine-learning Fraud_score	(33,270)	
Final sample for SEC investigation analyses	71,488	
Less firm-years with no lobbying activities	(62,936)	
Less firm-years with no industry variation for logit analyses	(97)	
Final sample for SEC investigation analyses using a subsample of lobbying firms	8,445	
Less firm-years without SEC investigations		(213,642)
Less firm-years with missing variables		(265)
Less firm-years with observations in years <1999		(198)
Less firm-years with no lobbying activities		(2,132)
Less firm-years with no industry variation for logit analyses		(98)
Final sample for SEC enforcement analyses		982

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Panel B. Distribution of firms by year

Year	Firms with sufficient data	Firms lobbying at least once in years t, t-1, or t-2	Proportion of lobbying firms	Firms investigated by the SEC in year t+1	Proportion of firms investigated by the SEC in year t+1
1999	5,437	455	8.37%	118	2.17%
2000	5,240	462	8.82%	89	1.70%
2001	4,830	523	10.83%	95	1.97%
2002	4,524	562	12.42%	259	5.73%
2003	4,387	614	14.00%	220	5.01%
2004	4,332	654	15.10%	261	6.02%
2005	4,146	702	16.93%	271	6.54%
2006	4,066	750	18.45%	160	3.94%
2007	3,988	736	18.46%	158	3.96%
2008	3,755	711	18.93%	129	3.44%
2009	3,553	753	21.19%	154	4.33%
2010	3,477	729	20.97%	111	3.19%
2011	3,420	690	20.18%	126	3.68%
2012	3,385	659	19.47%	118	3.49%
2013	3,412	641	18.79%	98	2.87%
2014	3,463	621	17.93%	65	1.88%
2015	3,111	594	19.09%	55	1.77%
2016	2,962	523	17.66%	4	0.14%
Total	71,488	11,379	15.92%	2,491	3.48%

Panel C. Distribution of firms by industry

	Firms with sufficient data	Firms lobbied in years t, t-1, or t-2	Proportion of lobbying firms
Business Services	9,935	1,030	10.37%
Utilities	1,788	934	52.24%
Pharmaceutical Product	6,324	846	13.38%
Communication	2,446	660	26.98%
Electronic Equipment	4,447	582	13.09%
Transportation	1,642	515	31.36%
Chemicals	1,599	468	29.27%
Petroleum and Natural	3,464	467	13.48%
Medical Equipment	2,975	463	15.56%
Retail	3,405	454	13.33%
Others	33,463	4,960	14.82%
Total	71,488	11,379	15.92%

Table 3. Descriptive statistics

Panel A. Descriptive statistics for a pool sample

Variable	N	Mean	SD	Min	25%	50%	75%	Max
SEC_Investigation	71,488	0.03	0.18	0.00	0.00	0.00	0.00	1.00
Lobby_3yr	71,488	0.16	0.37	0.00	0.00	0.00	0.00	1.00
Lobby_1yr	71,488	0.15	0.36	0.00	0.00	0.00	0.00	1.00
Lobby_Senate	8,455	0.98	0.15	0.00	1.00	1.00	1.00	1.00
Lobby_House	8,455	0.98	0.15	0.00	1.00	1.00	1.00	1.00
Lobby_SEC	8,455	0.05	0.22	0.00	0.00	0.00	0.00	1.00
Lobby_DOJ	8,455	0.12	0.32	0.00	0.00	0.00	0.00	1.00
Lobby_Budget	8,455	0.02	0.15	0.00	0.00	0.00	0.00	1.00
Lobby_Revolving	8,455	0.14	0.35	0.00	0.00	0.00	0.00	1.00
Lobby_Fin	8,455	0.18	0.38	0.00	0.00	0.00	0.00	1.00
Lobby_Tax	8,455	0.51	0.50	0.00	0.00	1.00	1.00	1.00
Lobby_Acc	8,455	0.03	0.17	0.00	0.00	0.00	0.00	1.00
Lobby_Bud	8,455	0.43	0.50	0.00	0.00	0.00	1.00	1.00
Lobby_Tor	8,455	0.07	0.25	0.00	0.00	0.00	0.00	1.00
Size	71,488	4.95	2.62	-1.13	3.06	4.99	6.86	10.78
BM	71,488	0.26	1.85	-11.75	0.13	0.38	0.73	4.45
Leverage	71,488	0.43	1.01	0.00	0.02	0.20	0.41	7.16
Age	71,488	15.86	12.44	0.00	6.00	13.00	22.00	55.00
SP500	71,488	0.08	0.28	0.00	0.00	0.00	0.00	1.00
Analysts	71,488	4.60	7.57	0.00	0.00	0.00	7.00	64.00
DACC	71,488	0.00	0.06	-0.87	0.00	0.00	0.00	1.07
Distance	71,488	4.36	2.07	-0.78	3.39	4.31	5.94	9.16
Fraud_score	71,488	4.10	1.26	1.11	3.09	4.08	5.04	8.93
AAER	982	0.15	0.36	0.00	0.00	0.00	0.00	1.00
Ch_Lobby	982	0.19	0.91	-1.00	-0.14	0.00	0.23	6.00
Ch_Lobby_Senate	982	0.20	0.93	-1.00	-0.19	0.00	0.25	6.16
Ch_Lobby_House	982	0.20	0.92	-1.00	-0.18	0.00	0.29	6.00
Ch_Lobby_SEC	982	-0.04	0.19	-0.97	0.00	0.00	0.00	0.14
Ch_Lobby_DOJ	982	-0.04	0.21	-1.00	0.00	0.00	0.00	0.29
Ch_Lobby_Budget	982	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Ch_Lobby_Revolving	982	-0.06	0.27	-1.00	0.00	0.00	0.00	0.50
Ch_Lobby_Fin	982	0.01	0.37	-1.00	0.00	0.00	0.00	1.37

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Variable								
Ch_Lobby_Tax	982	0.08	0.63	-1.00	0.00	0.00	0.03	3.72
Ch_Lobby_Acc	982	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Ch_Lobby_Bud	982	-0.01	0.53	-1.00	0.00	0.00	0.00	3.00
Ch_Lobby_Tor	982	-0.02	0.13	-1.00	0.00	0.00	0.00	0.20
Ch_Lobby_2yr	982	0.29	1.03	-0.90	-0.11	0.00	0.31	7.25
Ch_Lobby_Senate_2yr	982	0.31	1.07	-0.90	-0.13	0.00	0.39	7.72
Ch_Lobby_House_2yr	982	0.29	1.02	-0.90	-0.13	0.00	0.34	7.25
Ch_Lobby_SEC_2yr	982	-0.03	0.14	-0.77	0.00	0.00	0.00	0.07
Ch_Lobby_DOJ_2yr	982	-0.04	0.20	-1.00	0.00	0.00	0.00	0.17
Ch_Lobby_Budget_2yr	982	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Ch_Lobby_Revolving_2yr	906	-0.03	0.22	-1.00	0.00	0.00	0.00	0.50
Ch_Lobby_Fin_2yr	982	0.03	0.39	-1.00	0.00	0.00	0.00	1.46
Ch_Lobby_Tax_2yr	982	0.11	0.67	-1.00	0.00	0.00	0.03	4.44
Ch_Lobby_Acc_2yr	982	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Ch_Lobby_Bud_2yr	982	0.04	0.63	-1.00	0.00	0.00	0.00	3.64
Ch_Lobby_Tor_2yr	982	-0.02	0.12	-0.83	0.00	0.00	0.00	0.13

Panel B. Sample partitioned on Lobby_3yr

	(1) Lobby_3yr=0		(2) Lobby_3yr=1		Test of Differences (1)-(2)	
Variable	N	Mean	N	Mean	Difference	t-stat
Size	60,109	4.435	11,379	7.644	-3.209***	-130.00
BM	60,109	0.242	11,379	0.338	-0.095***	-5.04
Leverage	60,109	0.455	11,379	0.295	0.160***	15.40
Age	60,109	14.054	11,379	25.374	-11.320***	-94.37
SP500	60,109	0.029	11,379	0.368	-0.339***	-130.00
Analysts	60,109	3.376	11,379	11.052	-7.676***	-110.00
DACC	60,109	0.000	11,379	-0.002	0.002***	3.00
Distance	60,109	4.368	11,379	4.346	0.022	1.03
Fraud_score	60,109	3.991	11,379	4.687	-0.697***	-55.08

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Panel C. Pearson correlation matrix (Investigation Analysis)

		(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)	(18)	(19)	(20)	(21)	(22)
(1)	SEC_Investigation	1.00																					
(2)	Lobby_3yr	0.06	1.00																				
(3)	Lobby_Senate	0.01	0.96	1.00																			
(4)	Lobby_House	0.01	0.96	0.92	1.00																		
(5)	Lobby_SEC	0.04	0.03	0.03	0.03	1.00																	
(6)	Lobby_DOJ	0.06	0.05	0.05	0.05	0.11	1.00																
(7)	Lobby_Budget	0.01	0.02	0.02	0.02	0.00	0.07	1.00															
(8)	Lobby_Revolving	0.04	0.06	0.05	0.06	0.10	0.17	0.06	1.00														
(9)	Lobby_Fin	0.07	0.07	0.07	0.07	0.36	0.16	0.03	0.14	1.00													
(10)	Lobby_Tax	0.03	0.15	0.15	0.15	0.16	0.17	0.04	0.15	0.31	1.00												
(11)	Lobby_Acc	0.04	0.03	0.03	0.03	0.18	0.11	0.02	0.05	0.13	0.13	1.00											
(12)	Lobby_Bud	0.05	0.13	0.13	0.13	0.10	0.16	0.06	0.17	0.20	0.28	0.08	1.00										
(13)	Lobby_Tor	0.02	0.04	0.04	0.04	0.05	0.11	0.09	0.08	0.12	0.18	0.14	0.13	1.00									
(14)	Size	0.11	0.45	0.14	0.14	0.18	0.20	0.06	0.19	0.30	0.50	0.11	0.23	0.18	1.00								
(15)	BM	0.01	0.02	0.00	0.00	-0.01	-0.02	0.02	0.01	0.02	-0.02	-0.01	0.00	0.00	0.20	1.00							
(16)	Leverage	-0.03	-0.06	-0.12	-0.11	-0.03	-0.04	-0.01	-0.03	-0.02	-0.02	-0.03	-0.05	-0.04	-0.27	-0.39	1.00						
(17)	Age	0.01	0.33	0.05	0.04	0.11	0.05	-0.03	0.07	0.22	0.38	0.05	0.22	0.14	0.35	0.05	-0.09	1.00					
(18)	SP500	0.08	0.45	0.09	0.08	0.19	0.19	0.06	0.18	0.31	0.49	0.13	0.26	0.19	0.50	0.02	-0.05	0.38	1.00				
(19)	Analysts	0.09	0.37	0.09	0.08	0.18	0.12	0.05	0.13	0.20	0.33	0.09	0.13	0.07	0.65	0.06	-0.11	0.25	0.54	1.00			
(20)	DACC	0.00	-0.01	0.02	0.01	-0.02	-0.02	0.02	-0.02	-0.01	0.02	-0.02	0.00	0.00	-0.02	0.01	0.00	0.00	-0.01	-0.03	1.00		
(21)	Distance	0.11	0.00	0.00	0.00	-0.03	-0.09	-0.02	-0.08	-0.04	0.02	0.00	-0.03	0.03	-0.02	0.04	0.00	0.01	-0.02	-0.02	0.00	1.00	
(22)	Fraud_score	0.04	0.20	0.08	0.08	0.05	0.02	0.07	0.06	0.08	0.07	-0.03	0.04	-0.01	0.42	0.03	-0.05	0.18	0.19	0.33	0.33	0.00	1.00

This table presents Pearson correlations for SEC investigation analysis sample. Correlations statistically significant at 1% level are highlighted in bold. I define all variables in Table 1.

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Panel D. Pearson correlation matrix (Enforcement Analysis)

		(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)	(18)	(19)	(20)	(21)
(1)	AAER	1.00																				
(2)	Ch_Lobby	-0.04	1.00																			
(3)	Ch_Lobby_Senate	-0.04	**0.90**	1.00																		
(4)	Ch_Lobby_House	-0.06	**0.88**	**0.94**	1.00																	
(5)	Ch_Lobby_SEC	-0.01	**0.09**	0.05	0.04	1.00																
(6)	Ch_Lobby_DOJ	-0.02	0.06	0.02	0.01	0.00	1.00															
(7)	Ch_Lobby_Budget	.	.	.	.	.	.	.														
(8)	Ch_Lobby_Revolving	-0.04	0.06	0.06	0.07	-0.03	**0.15**	.	1.00													
(9)	Ch_Lobby_Fin	0.05	**0.16**	**0.15**	**0.13**	**0.15**	0.05	.	0.02	1.00												
(10)	Ch_Lobby_Tax	-0.04	**0.29**	**0.29**	**0.30**	0.09	-0.04	.	0.03	**0.11**	1.00											
(11)	Ch_Lobby_Acc	.	.	.	.	.	.	.	.	.	.											
(12)	Ch_Lobby_Bud	-0.02	0.07	**0.09**	**0.10**	0.05	0.03	.	0.02	**-0.09**	0.07	.	1.00									
(13)	Ch_Lobby_Tor	-0.08	0.06	0.06	0.06	0.00	0.05	.	0.08	0.00	0.07	.	0.03	1.00								
(14)	Size	0.07	-0.04	-0.01	-0.02	**-0.14**	**-0.14**	.	**-0.13**	0.03	**0.09**	.	0.00	-0.07	1.00							
(15)	BM	0.06	-0.04	-0.02	-0.03	0.00	-0.04	.	-0.04	0.02	0.03	.	0.01	-0.01	**0.23**	1.00						
(16)	Leverage	**0.09**	0.05	0.02	0.01	-0.04	0.00	.	-0.06	0.05	-0.03	.	-0.06	-0.02	-0.02	**-0.09**	1.00					
(17)	Age	**0.11**	**-0.11**	**-0.10**	**-0.09**	**-0.14**	-0.06	.	-0.04	0.01	0.04	.	0.01	-0.08	**0.43**	0.04	0.05	1.00				
(18)	SP500	**0.10**	**-0.09**	-0.07	-0.05	**-0.10**	**-0.13**	.	**-0.15**	-0.01	0.08	.	0.00	-0.05	**0.66**	**0.15**	0.00	**0.41**	1.00			
(19)	Analysts	-0.02	-0.03	-0.02	-0.01	-0.03	-0.04	.	-0.07	0.01	0.04	.	0.03	-0.02	**0.60**	**0.15**	**-0.13**	**0.17**	**0.46**	1.00		
(20)	DACC	0.00	0.03	0.04	0.04	0.04	0.02	.	-0.02	0.08	0.02	.	-0.07	-0.02	0.01	0.02	0.07	0.06	0.03	-0.03	1.00	
(21)	Distance	0.00	-0.04	-0.06	-0.07	0.03	-0.06	.	0.02	-0.08	0.03	.	-0.07	-0.03	-0.04	-0.05	-0.05	0.01	-0.05	0.02	-0.02	1.00

This table presents Pearson correlations for SEC enforcement analysis sample. Correlations statistically significant at 1% level are highlighted in bold. I define all variables in Table 1.

Table 4. Effect of proactive lobbying on an SEC investigation

Variables	Dependent variable: SEC_Investigation				
	(1)	**(2)**	**(3)**	**(4)**	**(5)**
Lobby_3yr	0.797***	0.112*	0.100		
	(15.215)	(1.739)	(1.542)		
Lobby_1yr				0.099	0.086
				(1.502)	(1.310)
Size		0.288***	0.259***	0.289***	0.260***
		(19.217)	(16.389)	(19.311)	(16.467)
BM		-0.064***	-0.062***	-0.064***	-0.062***
		(-3.505)	(-3.467)	(-3.511)	(-3.472)
Leverage		-0.030	-0.034	-0.030	-0.034
		(-0.907)	(-1.015)	(-0.899)	(-1.007)
Age		-0.007***	-0.006**	-0.007***	-0.006**
		(-2.738)	(-2.332)	(-2.697)	(-2.291)
SP500		-0.064	-0.061	-0.061	-0.057
		(-0.746)	(-0.713)	(-0.709)	(-0.676)
Analysts		0.008**	0.009**	0.009**	0.009**
		(2.453)	(2.535)	(2.457)	(2.539)
DACC		0.764**	0.724**	0.763**	0.722**
		(2.073)	(1.979)	(2.071)	(1.977)
Distance		0.393***	0.394***	0.393***	0.394***
		(20.002)	(20.129)	(19.997)	(20.125)
Fraud_score			0.178***		0.178***
			(5.612)		(5.623)
Year FE	Yes	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes	Yes
SE clustered by Firm	Yes	Yes	Yes	Yes	Yes
Observations	71,488	71,488	71,488	71,488	71,488
Pseudo R^2	0.048	0.137	0.138	0.137	0.138
Regression type	Logit	Logit	Logit	Logit	Logit

The dependent variable is an indicator set to 1 if the SEC opens an investigation on a firm in year t+1, and 0 otherwise. I use a logit estimator for the models, clustering the standard errors by firm. *, **, and *** indicate significance at the 10%, 5%, and 1% levels, respectively. T-statistics are presented in parentheses below the coefficients. Continuous variables are winsorized at 1% and 99% levels. I define all variables in Table 1.

Table 5. Effect of proactive lobbying by lobbying contacts on an SEC investigation

	Dependent variable: SEC_Investigation					
Variables	(1)	(2)	(3)	(4)	(5)	(6)
Lobby_Senate	0.288					
	(0.689)					
Lobby_House		0.141				
		(0.318)				
Lobby_SEC			0.303			
			(1.428)			
Lobby_DOJ				0.229		
				(1.527)		
Lobby_Budget					0.137	
					(0.524)	
Lobby_Revolving						0.216*
						(1.657)
Size	0.205***	0.206***	0.205***	0.198***	0.206***	0.201***
	(3.743)	(3.778)	(3.770)	(3.649)	(3.770)	(3.708)
BM	-0.061	-0.062	-0.059	-0.061	-0.062	-0.063
	(-1.371)	(-1.385)	(-1.367)	(-1.406)	(-1.403)	(-1.429)
Leverage	0.169	0.160	0.152	0.149	0.151	0.152
	(1.247)	(1.148)	(1.140)	(1.117)	(1.125)	(1.142)
Age	-0.004	-0.004	-0.004	-0.004	-0.004	-0.005
	(-0.825)	(-0.827)	(-0.878)	(-0.877)	(-0.815)	(-0.885)
SP500	0.172	0.172	0.162	0.156	0.169	0.161
	(1.118)	(1.117)	(1.053)	(1.005)	(1.100)	(1.050)
Analysts	0.008	0.008	0.007	0.008	0.008	0.008
	(1.382)	(1.382)	(1.253)	(1.342)	(1.403)	(1.320)
DACC	0.576	0.588	0.621	0.617	0.593	0.654
	(0.526)	(0.538)	(0.572)	(0.567)	(0.543)	(0.594)
Distance	0.573***	0.573***	0.573***	0.573***	0.573***	0.573***
	(9.640)	(9.643)	(9.664)	(9.650)	(9.644)	(9.684)
Fraud_score	0.242***	0.243***	0.248***	0.241***	0.243***	0.239***
	(3.653)	(3.663)	(3.751)	(3.611)	(3.664)	(3.593)
Year FE	Yes	Yes	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes	Yes	Yes
SE clustered by Firm	Yes	Yes	Yes	Yes	Yes	Yes
Observations	8,455	8,455	8,455	8,455	8,455	8,455
Pseudo R^2	0.174	0.174	0.174	0.174	0.174	0.174

I estimate the models within the subsample of firm-years with corporate lobbying activities, using a logit estimator with standard errors clustered by firm. *, **, and *** indicate significance at the 10%, 5%, and 1% levels, respectively. T-statistics are presented in parentheses below the coefficients. Continuous variables are winsorized at 1% and 99% levels. I define all variables in Table 1.

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Table 6. Effect of proactive lobbying by lobbying issues on an SEC investigation

Variables	Dependent variable: SEC_Investigation				
	(1)	**(2)**	**(3)**	**(4)**	**(5)**
Lobby_Fin	0.514***				
	(3.911)				
Lobby_Tax		-0.109			
		(-0.819)			
Lobby_Acc			-0.116		
			(-0.562)		
Lobby_Bud				0.227**	
				(1.979)	
Lobby_Tor					-0.153
					(-0.922)
Size	0.184***	0.216***	0.208***	0.197***	0.210***
	(3.366)	(3.881)	(3.785)	(3.606)	(3.836)
BM	-0.051	-0.066	-0.063	-0.059	-0.063
	(-1.141)	(-1.450)	(-1.407)	(-1.309)	(-1.406)
Leverage	0.128	0.152	0.150	0.159	0.148
	(0.951)	(1.131)	(1.117)	(1.196)	(1.101)
Age	-0.006	-0.004	-0.004	-0.005	-0.004
	(-1.233)	(-0.740)	(-0.824)	(-1.006)	(-0.740)
SP500	0.134	0.194	0.176	0.146	0.179
	(0.868)	(1.225)	(1.144)	(0.949)	(1.157)
Analysts	0.008	0.009	0.008	0.009	0.008
	(1.318)	(1.420)	(1.403)	(1.431)	(1.345)
DACC	0.582	0.623	0.587	0.583	0.592
	(0.534)	(0.568)	(0.538)	(0.531)	(0.542)
Distance	0.574***	0.572***	0.573***	0.572***	0.573***
	(9.671)	(9.642)	(9.659)	(9.667)	(9.656)
Fraud_score	0.251***	0.242***	0.244***	0.249***	0.243***
	(3.781)	(3.647)	(3.675)	(3.727)	(3.660)
Year FE	Yes	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes	Yes
SE clustered by Firm	Yes	Yes	Yes	Yes	Yes
Observations	8,455	8,455	8,455	8,455	8,455
Pseudo R^2	0.178	0.174	0.174	0.175	0.174

I estimate the models within the subsample of firm-years with corporate lobbying activities, using a logit estimator with standard errors clustered by firm. *, **, and *** indicate significance at the 10%, 5%, and 1% levels, respectively. T-statistics are presented in parentheses below the coefficients. Continuous variables are winsorized at 1% and 99% levels. I define all variables in Table 1.

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Table 7. Effect of reactive lobbying on an SEC enforcement action

Panel A. One-year change in lobbying expenditures (and by lobbying contact) around SEC investigations

Variables	(1)	(2)	(3)	(4)	(5)	(6)	(7)
			Dependent variable: AAER				
Ch_Lobby	-0.299**						
	(-2.284)						
Ch_Lobby_Senate		-0.255**					
		(-2.247)					
Ch_Lobby_House			-0.341***				
			(-2.873)				
Ch_Lobby_SEC				0.348			
				(0.482)			
Ch_Lobby_DOJ					0.259		
					(0.879)		
Ch_Lobby_Budget						-	
Ch_Lobby_Revolving							-0.265
							(-0.722)
Size	-0.053	-0.053	-0.053	-0.059	-0.060	-0.065	-0.068
	(-0.546)	(-0.547)	(-0.546)	(-0.607)	(-0.617)	(-0.678)	(-0.698)
BM	0.125	0.132	0.133	0.130	0.133	0.130	0.130
	(0.752)	(0.776)	(0.758)	-0.818	(0.824)	(0.818)	(0.810)
Leverage	1.322**	1.297**	1.302**	1.242**	1.230**	1.219**	1.200**
	(2.280)	(2.240)	(2.246)	(2.046)	(2.064)	(2.055)	(2.044)
Age	0.025**	0.025**	0.025**	0.027**	0.026**	0.026**	0.026**
	(2.048)	(2.040)	(2.020)	(2.192)	(2.148)	(2.161)	(2.150)
SP500	0.584*	0.600*	0.622*	0.623*	0.636**	0.628*	0.615*
	(1.793)	(1.853)	(1.907)	(1.955)	(1.976)	(1.956)	(1.897)
Analysts	-0.005	-0.005	-0.006	-0.006	-0.005	-0.005	-0.005
	(-0.371)	(-0.390)	(-0.407)	(-0.433)	(-0.404)	(-0.381)	(-0.404)
DACC	-1.628	-1.527	-1.356	-2.064	-1.893	-1.892	-1.974
	(-0.659)	(-0.609)	(-0.538)	(-0.786)	(-0.754)	(-0.755)	(-0.781)
Distance	0.009	0.007	0.006	0.014	0.018	0.016	0.015
	(0.195)	(0.159)	(0.141)	(0.315)	(0.387)	(0.340)	(0.343)
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes
SE clustered by Firm	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Observations	982	982	982	982	982	982	982
Pseudo R^2	0.175	0.174	0.177	0.168	0.168	0.168	0.168

Panel B. One-year change in lobbying expenditures by lobbying issues

Variables	(1)	(2)	(3)	(4)	(5)
			Dependent variable: AAER		
Ch_Lobby_Fin	0.031				
	(0.120)				
Ch_Lobby_Tax		-0.366**			
		(-2.167)			
Ch_Lobby_Acc			-		
Ch_Lobby_Bud				-0.038	
				(-0.182)	
Ch_Lobby_Tor					-0.827
					(-1.426)
Size	-0.066	-0.050	-0.065	-0.066	-0.069
	(-0.679)	(-0.499)	(-0.678)	(-0.682)	(-0.718)
BM	0.129	0.148	0.130	0.130	0.128
	(0.816)	(0.799)	(0.818)	(0.817)	(0.807)
Leverage	1.215**	1.208**	1.219**	1.215**	1.186**
	(2.052)	(2.075)	(2.055)	(2.041)	(2.002)
Age	0.026**	0.027**	0.026**	0.026**	0.025**
	(2.160)	(2.245)	(2.161)	(2.161)	(2.092)
SP500	0.629*	0.604*	0.628*	0.628*	0.635**
	(1.950)	(1.908)	(1.956)	(1.955)	(2.000)
Analysts	-0.005	-0.006	-0.005	-0.005	-0.006
	(-0.383)	(-0.462)	(-0.381)	(-0.379)	(-0.418)
DACC	-1.933	-1.631	-1.892	-1.923	-1.908
	(-0.755)	(-0.642)	(-0.755)	(-0.769)	(-0.759)
Distance	0.016	0.016	0.016	0.015	0.014
	(0.355)	(0.357)	(0.340)	(0.317)	(0.317)
Year FE	Yes	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes	Yes
SE clustered by Firm	Yes	Yes	Yes	Yes	Yes
Observations	982	982	982	982	982
Pseudo R^2	0.167	0.173	0.168	0.168	0.170

The dependent variable is an indicator set to 1 if a firm receives an AAER during or within two years after a formal SEC investigation closes, and 0 otherwise. I estimate the models within the subsample of firm-years with corporate lobbying activities, using a logit estimator with standard errors clustered by firm. *, **, and *** indicate significance at the 10%, 5%, and 1% levels, respectively. T-statistics are presented in parentheses below the coefficients. Continuous variables are winsorized at 1% and 99% levels. I define all variables in Table 1.

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Table 8. Effect of longer-term reactive lobbying on an SEC enforcement action

Panel A. two-year change in lobbying expenditures (and by lobbying contact) around SEC investigations

Variables	Dependent variable: AAER						
	(1)	**(2)**	**(3)**	**(4)**	**(5)**	**(6)**	**(7)**
Ch_Lobby_2yr	-0.312**						
	(-2.420)						
Ch_Lobby_Senate_2yr		-0.237**					
		(-2.461)					
Ch_Lobby_House_2yr			-0.359***				
			(-3.028)				
Ch_Lobby_SEC_2yr				-0.805			
				(-1.190)			
Ch_Lobby_DOJ_2yr					0.149***		
					(2.716)		
Ch_Lobby_Budget_2yr						-	
Ch_Lobby_Revolving_2yr							-0.059
							(-0.133)
Control variables	Included	Included	Included	Included	Included	Included	Included
SE clustered by Firm	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Observations	982	982	982	982	982	982	902
Pseudo R^2	0.177	0.174	0.180	0.169	0.170	0.168	0.180

Panel B. two-year change in lobbying expenditures by lobbying issues

Variables	Dependent variable: AAER				
	(1)	**(2)**	**(3)**	**(4)**	**(5)**
Ch_Lobby_Fin_2yr	-0.170				
	(-0.703)				
Ch_Lobby_Tax_2yr		-0.316*			
		(-1.934)			
Ch_Lobby_Acc_2yr			-		
Ch_Lobby_Bud_2yr				0.141	
				(0.930)	
Ch_Lobby_Tor_2yr					-1.217*
					(-1.653)
Control variables	Included	Included	Included	Included	Included
Year FE	Yes	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes	Yes
SE clustered by Firm	Yes	Yes	Yes	Yes	Yes
Observations	982	982	982	982	982
Pseudo R^2	0.168	0.172	0.168	0.169	0.172

The dependent variable is an indicator set to 1 if a firm receives an AAER during or within two years after a formal SEC investigation closes, and 0 otherwise. I estimate the models within the subsample of firm-years with corporate lobbying activities, using a Logit estimator with standard errors clustered by firm. *, **, and *** indicate significance at the 10%, 5%, and 1% levels, respectively. T-statistics are presented in parentheses below the coefficients. Continuous variables are winsorized at 1% and 99% levels. I define all variables in Table 1.

Table 9. IV probit analysis on an SEC investigation

Variables	(1) Stage 1 Lobby_3yr	(2) Two-step probit SEC_Investigation
Lobby_3yr		0.693
		(1.60)
PRisk	0.046***	
	(15.15)	
Control Variables	Included	Included
Year FE	Yes	Yes
Industry FE	Yes	Yes
Observations	33,691	33,691
Exogeneity test (p-value)		0.155
Partial F-stat (instrument, stage 1)	209.99	
Regression type	ivprobit	

The dependent variable is an indicator set to 1 if the SEC opens an investigation on a firm in year t+1, and 0 otherwise. I use two stage probit model with an instrumental variable (a firm level political risk). *, **, and *** indicate significance at the 10%, 5%, and 1% levels, respectively. T-statistics are presented in parentheses below the coefficients. Continuous variables are winsorized at 1% and 99% levels. I define all variables in Table 1.

Table 10. Effect of corporate lobbying on an SEC investigation using entropy balancing

Panel A. Covariate balance for entropy balanced sample partitioned on Lobby_3yr

Variable	Mean		Standardized differences	Variance		Variance Ratios
	Lobby_3yr=0	Lobby_3yr=1		Lobby_3yr=0	Lobby_3yr=1	
Size	7.643	7.644	-0.0005	3.854	4.346	1.128
BM	0.337	0.338	-0.0002	0.659	1.791	2.719
Leverage	0.295	0.295	0.0003	0.305	0.151	0.495
Age	25.370	25.370	0.0000	220.100	235.000	1.068
SP500	0.368	0.368	-0.0002	0.233	0.233	1.000
Analysts	11.050	11.050	0.0000	106.300	118.600	1.116
DACC	-0.002	-0.002	0.0000	0.003	0.002	0.850
Distance	4.346	4.346	0.0000	4.532	4.309	0.951
Fraud_score	4.687	4.687	0.0000	1.609	1.511	0.939

In this panel, I present the entropy-balanced-sample comparisons for lobbying and non-lobbying firms. I calculate the standard differences as the difference in means between the treatment and controlled samples, scaled by the standard deviation of the respective variable for the treatment sample for each covariate. The variance ratios use the treatment (control)sample standard deviation of the respective covariate as the numerator (denominator). Continuous variables are winsorized at 1% and 99% levels. I define all variables in Table 1.

Panel B. Effect of corporate lobbying on SEC investigation using entropy balanced sample

Variables	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
					Dependent variable: SEC_Investigation							
Lobby_3yr	0.051											
	(0.545)											
Lobby_Senate		1.063*										
		(1.698)										
Lobby_House			0.824									
			(1.257)									
Lobby_SEC				0.326								
				(1.543)								
Lobby_DOJ					0.245							
					(1.629)							
Lobby_Budget						0.138						
						(0.529)						
Lobby_Revolving							0.229*					
							(1.768)					
Lobby_Fin								0.520***				
								(3.948)				
Lobby_Tax									-0.077			
									(-0.577)			
Lobby_Acc										-0.093		
										(-0.453)		
Lobby_Bud											0.245**	
											(2.132)	

Lobby_Tor												-0.136
												(-0.814)
Control variables	Included	Included	Included	Included	Included	Included	Included	Included	Included	Included	Included	Included
SE clustered by Firm	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Observations	71,488	8,455	8,455	8,455	8,455	8,455	8,455	8,455	8,455	8,455	8,455	8,455
Pseudo R^2	0.143	0.175	0.175	0.175	0.175	0.175	0.174	0.178	0.174	0.174	0.175	0.174

The vector of controls in panel B mirrors those in Table 4 (untabulated). I use a Logit estimator, clustering the standard errors by firm. *, **, and *** indicate significance at the 10%, 5%, and 1% levels, respectively. T-statistics are presented in parentheses below the coefficients. Continuous variables are winsorized at 1% and 99% levels. I define all variables in Table 1.

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Table 11. Strategic corporate lobbying and fraud risk

Variables	Dependent variable: Lobby_up		
	(1)	**(2)**	**(3)**
Fraud_score	0.069**	0.016***	0.020**
	(2.260)	(2.589)	(2.329)
Size	0.219***	0.044***	0.023***
	(14.949)	(16.042)	(2.985)
BM	-0.067***	-0.014***	-0.012***
	(-4.286)	(-4.242)	(-2.998)
Leverage	0.177	0.030	0.051
	(1.550)	(1.534)	(1.449)
CF	0.226***	0.032***	0.022
	(2.773)	(3.025)	(0.988)
R&D	0.010	0.002	0.006
	(0.508)	(0.663)	(0.960)
HHI	-1.922	-0.306	0.696
	(-0.941)	(-1.085)	(0.872)
Year FE	Yes	Yes	Yes
Industry FE	Yes	Yes	No
Firm FE	No	No	Yes
SE clustered by Firm	Yes	Yes	Yes
Observations	10,415	10,855	10,855
Pseudo R^2/Adj R^2	0.078	0.101	0.126
Regression type	Logit	OLS	OLS

The dependent variable is an indicator set to 1 if a firm increases lobbying expenditures from year t to year t+1, and 0 otherwise. I estimate the models within the subsample of firm-years with corporate lobbying activities, using a Logit estimator with standard errors clustered by firm. *, **, and *** indicate significance at the 10%, 5%, and 1% levels, respectively. T-statistics are presented in parentheses below the coefficients. Continuous variables are winsorized at 1% and 99% levels. I define all variables in Table 1.

Table 12. the SEC's prosecutorial discretion and corporate lobbying

Variables	(1)	(2)	(3)	(4)	(5)	(6)	(7)
			Dependent variable: AP_Civil				
Ch_Lobby	-0.038						
	(-0.104)						
Ch_Lobby_Senate		-0.142					
		(-0.240)					
Ch_Lobby_House			-0.226				
			(-0.336)				
Ch_Lobby_SEC				-2.136*			
				(-1.843)			
Ch_Lobby_DOJ					-4.031		
					(-1.222)		
Ch_Lobby_Budget						-	
Ch_Lobby_Revolving							1.358
							(1.437)
Control variables	Included	Included	Included	Included	Included	Included	Included
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes
SE clustered by Firm	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Observations	137	137	137	137	137	137	137
Pseudo R^2	0.354	0.354	0.354	0.373	0.368	0.354	0.369

The dependent variable is an indicator set to 1 if the SEC litigates a firm in both administrative proceedings and a federal court, and 0 if the SEC brings administrative proceedings only. I estimate the models within the subsample of firm-years with corporate lobbying activities, using a Logit estimator with standard errors clustered by firm. The vector of controls mirrors those in Table 4. *, **, and *** indicate significance at the 10%, 5%, and 1% levels, respectively. T-statistics are presented in parentheses below the coefficients. Continuous variables are winsorized at 1% and 99% levels. I define all variables in Table 1.

Table 13. Commissioners' political affiliation and an SEC enforcement action

| Variables | Dependent variable: AAER | | | | | |
	(1)	(2)	(3)	(4)	(5)	(6)
Ch_Lobby	-0.299**					
	(-2.284)					
Ch_Lobby_Senate		-0.255**				
		(-2.247)				
Ch_Lobby_House			-0.341***			
			(-2.873)			
Ch_Lobby_2yr				-0.312**		
				(-2.420)		
Ch_Lobby_Senate_2yr					-0.237**	
					(-2.461)	
Ch_Lobby_House_2yr						-0.359***
						(-3.028)
SEC_PA	5.059***	5.013***	5.115***	5.157***	5.083***	5.255***
	(4.420)	(4.426)	(4.458)	(4.467)	(4.460)	(4.540)
Control variables	Included	Included	Included	Included	Included	Included
Year FE	Yes	Yes	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes	Yes	Yes
SE clustered by Firm	Yes	Yes	Yes	Yes	Yes	Yes
Observations	982	982	982	982	982	982
Pseudo R^2	0.175	0.174	0.177	0.177	0.174	0.180

The dependent variable is an indicator set to 1 if a firm receives an AAER during or within two years after a formal SEC investigation closes, and 0 otherwise. I estimate the models within the subsample of firm-years with corporate lobbying activities, using a Logit estimator with standard errors clustered by firm. *, **, and *** indicate significance at the 10%, 5%, and 1% levels, respectively. T-statistics are presented in parentheses below the coefficients. Continuous variables are winsorized at 1% and 99% levels. I define all variables in Table 1.

Table 14. Meetings with SEC Chair and an SEC enforcement action

Variables	Dependent variable: AAER			
	(1)	**(2)**	**(3)**	**(4)**
Ch_Lobby	-0.285**	-0.299**		
	(-2.134)	(-2.236)		
Ch_Lobby_3yr			-0.293**	-0.315**
			(-2.223)	(-2.364)
Chair_Firm_Meet	1.390***		1.374***	
	(2.793)		(2.772)	
Chair_Congress_Meet		0.539*		0.546*
		(1.683)		(1.692)
Control Variables	Included	Included	Included	Included
Year FE	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes
SE clustered by Firm	Yes	Yes	Yes	Yes
Observations	982	982	982	982
Pseudo R^2	0.193	0.180	0.194	0.182

The dependent variable is an indicator set to 1 if a firm receives an AAER during or within two years after a formal SEC investigation closes, and 0 otherwise. I estimate the models within the subsample of firm-years with corporate lobbying activities, using a Logit estimator with standard errors clustered by firm. *, **, and *** indicate significance at the 10%, 5%, and 1% levels, respectively. T-statistics are presented in parentheses below the coefficients. Continuous variables are winsorized at 1% and 99% levels. I define all variables in Table 1.

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Figure 1. Flowchart of an SEC Investigation and Enforcement Process
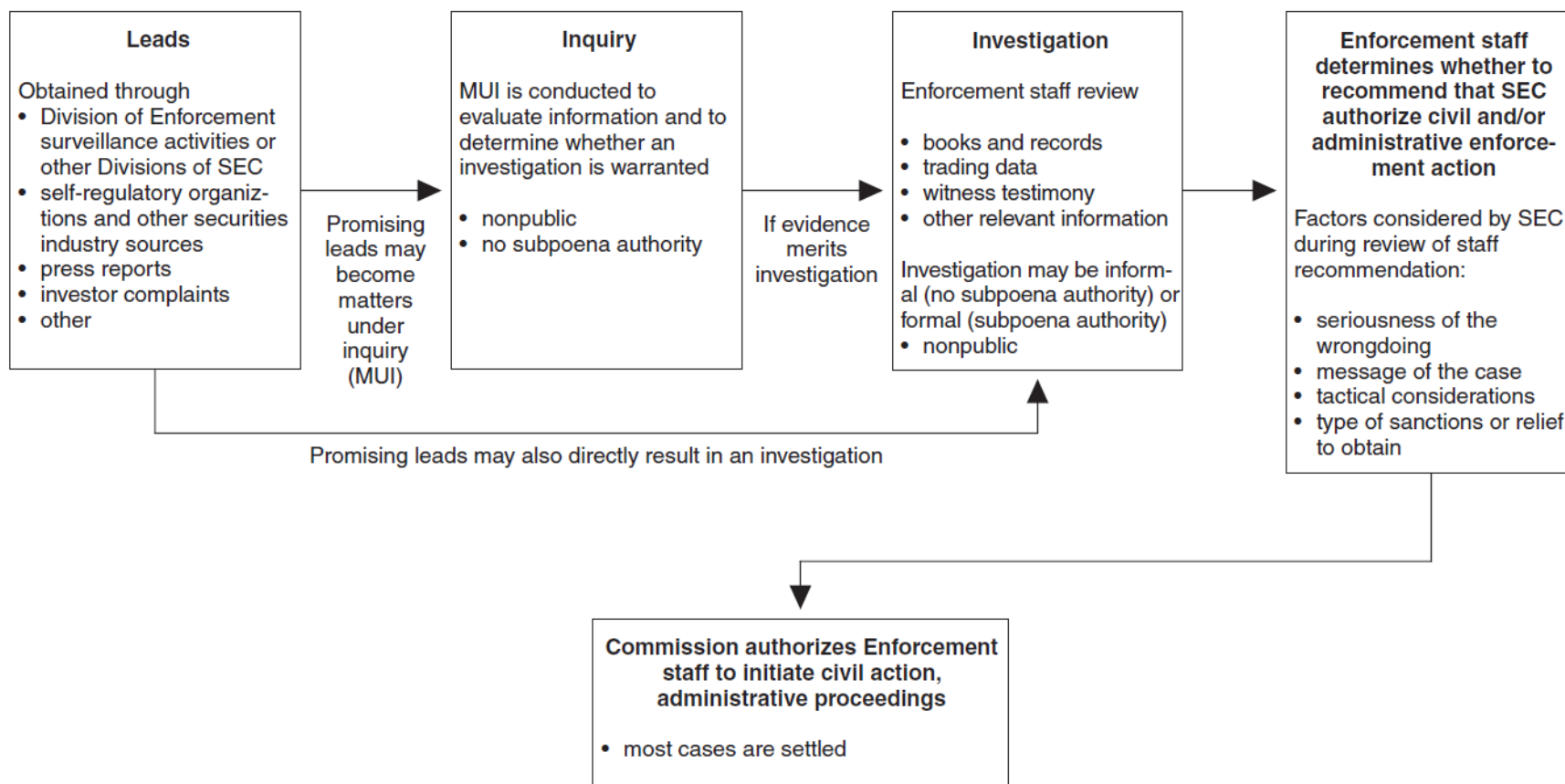
The figure is from GAO report "Securities and Exchange Commission Additional Actions Needed to Ensure Planned Improvements Address limitations in Enforcement Division Operations" (2007).

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