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Citation	Heese, Jonas, Mozaffar Khan, and Karthik Ramanna. "Is the SEC Captured? Evidence from Comment-Letter Reviews." Harvard Business School Working Paper, No. 17-087, April 2017. (Revised June 2017; forthcoming at the Journal of Accounting & Economics.)
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June 9, 2017

SEC oversight of publicly listed firms ranges from comment letter (CL) reviews of firms' reporting compliance to pursuing enforcement actions against violators. Prior literature finds that firm political connections (PC) *negatively* predict enforcement actions, inferring SEC capture. We present new evidence that firm PC *positively* predict CL reviews and substantive characteristics of such reviews, including the number of issues evaluated and the seniority of SEC staff involved. These results, robust to identification concerns, are inconsistent with SEC capture and indicate a more nuanced relation between firm PC and SEC oversight than previously suggested.

Keywords: comment letters, political connections, regulatory capture, SEC enforcement

JEL classification: D72, G18, M41, M48

1. Introduction

The Securities and Exchange Commission (SEC) oversight process involves a range of activities, from advice and monitoring to enforcement actions. Enforcement actions have been studied in the prior literature to understand both their determinants and consequences. A firm's political connections (PC) in particular are hypothesized from capture theory (e.g., Stigler 1971) to bias downward the likelihood of enforcement actions and the magnitude of penalties, as politicians can interfere with SEC investigations, use budget allocations to control the SEC, or affect SEC officials' careers (Weingast 1984).[1] Empirical evidence suggestive of SEC capture by politically connected firms is reported in Correia (2014) and Yu and Yu (2011), who find a negative relation between firm PC and enforcement actions (which are pursued by the SEC's Division of Enforcement or DOE).

Interpreting the results in the prior literature as evidence of lax SEC oversight of PC firms is complicated by the fact that SEC oversight involves more than enforcement actions. In particular, the agency also routinely reviews firms' SEC filings to *monitor* and *enhance* firms' compliance with disclosure and accounting regulation (SEC 2015b). SEC questions and concerns in the course of these reviews are communicated to firms through comment letters (CLs) that require response and remediation. In this paper, we examine the relation between firm PC and the likelihood of receiving CLs to shed fuller light on the relation between corporate political connectedness and SEC oversight.

The CL review process is conducted by the SEC's Division of Corporation Finance (DCF). The volume of CLs is large, as between 20% and 40% of U.S. listed firms have received a CL in each year between 2005 and 2012. In contrast, enforcement actions are relatively infrequent. CLs are issued on a variety of topics (e.g., revenue recognition, goodwill

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[1] Throughout the paper we refer to "political connections" and "politically connected" as PC.

impairment) depending on the nature of the SEC concern generated by its review. The initial CL might request clarification and disclosure of further information that leads to a sequence of "rounds" of communication between the SEC and the firm. The CL process concludes when the DCF is satisfied with compliance and issues a "no further comment" letter, or when the DCF refers the matter to the SEC's DOE. CLs therefore are an important part of SEC oversight. In this light, a number of recent studies have investigated the determinants and consequences of CLs (e.g., Cassell et al. 2013; Bozanic et al. 2015; Johnston and Petacchi 2014; Dechow et al. 2016). These studies have not, however, examined the relation between firm PC and the likelihood of receiving CLs.

SOX Section 408, paragraph (b), identifies some firm characteristics ("factors") for the SEC to consider in its CL reviews. This guidance concludes by stating that "any other factors that the Commission may consider relevant" can also be used in determining which firms are reviewed, suggesting that the SEC is given some discretion. If firms' political connections are one such discretionary factor, then we expect a significant relation between firm PC and CL review likelihood. Moreover, if the SEC is captured as suggested in the prior literature, and such capture is manifested through lax oversight, we expect this relation to be negative.

On the other hand, there are reasons to expect a positive relation between these variables. For example, the SEC's CL review process may not be captured (and, in fact, prior claims of SEC capture, which are based on small samples of firms facing enforcement actions, may be overstated). If so, and if firm PC is a distinct risk factor for financial-reporting issues, we would expect a positive relation between firm PC and CL reviews.

To investigate the relation between firm PC and CL reviews we obtain all comment letters from the Audit Analytics database for 2005-2012 and retain those related to firms' 10-K filings. PC firms are identified through contemporaneous contributions to Political Action Committees (PAC) or alternatively through their lobbying expenditures. Results indicate that

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PC firms are more likely to receive a CL after controlling for a host of CL determinants identified in the prior literature. The controls include accounting quality and complexity proxies, such as accounting restatements, internal control weaknesses, the length and linguistic complexity of financial statements, and the number of SEC filings made by each firm during the year. Our results on PC contrast with prior findings of a negative association between PC and SEC enforcement actions and suggest SEC capture by PC firms is not indicated in the CL review process. We return to a discussion of this primary finding shortly.

We conduct a range of tests that collectively are intended to mitigate endogeneity concerns and examine the robustness of the primary result. First, we estimate the tests in a propensity-score-matched sample wherein PC and non-PC firms are matched by year, the specific SEC office conducting the review, and all covariates in the regression model (Ho et al. 2007). Results indicate PC firms are more likely to receive a CL: for instance, we find that while firms making political contributions have a 38.5% probability of receiving a CL, matched non-contributing firms have a probability of 33.7%, a statistically significant difference that also appears to be economically substantive.

Second, we conduct cross-sectional tests exploiting variation in the targets of firms' political activities. Specifically, we examine the relation between CL and firms that have either lobbied the SEC directly or are top contributors to legislators serving on SEC oversight committees. We find that such firms are significantly more likely to receive CL reviews, providing further support to the primary result.

Third, to further mitigate more general endogeneity concerns we use an instrumental-variables (IV) approach. As in prior research (e.g., Blackburne 2014; Correia 2014), our instruments for a firm's PAC and lobbying expenditures are, respectively, the sum of PAC and lobbying expenditures made by other firms in the same 4-digit SIC industry and the same size decile. These industry-size peer contributions are likely to be associated with the political

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contributions of a given firm due to peer effects driving political activity (e.g., Grier et al. 1994; Kim 2008), but they are less likely to directly drive the likelihood of that firm receiving a comment letter. IV results are consistent with our main findings. We additionally use a new IV – state-level voter turnout. State turnout rates capture the state population's political engagement and are therefore likely to be associated with the political contributions of a given firm (the firm is more likely to be politically engaged), but turnout rates are less likely to drive the likelihood of that firm receiving a comment letter. The results using this IV are consistent with the main findings.

The final set of tests examines the substantive characteristics of CL reviews of PC versus non-PC firms. We examine four characteristics, the first three of which are from prior literature (Cassell et al. 2013): (i) the number of core and non-core earnings topics in the CL; (ii) the number of days between the initial receipt of a CL and the receipt of a "no further comment" letter; (iii) the number of communication rounds between the SEC and firms; and (iv) the involvement of an SEC supervisor in a firm's comment-letter review. We find that PC firms receive more substantive reviews along all these dimensions, indicating that the SEC's CL reviews of PC firms are not perfunctory.

We offer some potential explanations for our primary finding of a positive association between firm PC and SEC CL reviews in comparison to the prior finding of a negative relation between firm PC and enforcement. First, it is possible that both the DOE and DCF are captured and coordinate such that the DCF proactively "works with" PC firms in the CL stage to actively remediate issues and preempt escalation to the enforcement stage. However, this explanation faces two major hurdles: (i) it requires a more elaborate coordination between different divisions of the SEC than is reported (anecdotally) by current and former SEC

officials;[2] and (ii) it does not explain why PC firms that have ostensibly captured the SEC could not simply hire former SEC officials to vet their financial statements prior to submission, thereby lowering the likelihood of being subject to a publicly visible CL review process. We therefore do not view this as a likely explanation.

Another potential explanation is that only the DOE, which pursues enforcement actions, but not the DCF, which conducts the CL reviews, is politically captured. For instance, the politically appointed Commissioners vote in a closed meeting on the DOE staff's enforcement recommendation, but Commissioners do not directly influence the issuance of a comment letter by the DCF. However, this argument of targeted capture of the DOE does not in itself explain a positive relation (as opposed to no relation) between PC and the likelihood and substantive characteristics of CL as we document. Thus, this explanation alone cannot account for our results.

A related explanation is that the SEC DCF actively targets PC firms in the CL review stage. This account does not require an anti-political vendetta on part of the SEC's DCF; it may simply be that political connectedness is a useful heuristic for issues the DCF seeks to address at the CL stage. Our identification tests allay concerns that firm PC proxies for known and latent financial-reporting risk characteristics; the tests suggest that the DCF may view firm PC as a distinct risk indicator. If true, then the remediation of issues at the CL stage can explain in part the lower likelihood of subsequent enforcement action against PC firms documented in the prior literature. This explanation, which is inconsistent with the SEC capture hypothesis, appears most likely to us.

A fourth possibility is that the PC measures used in the literature to establish a negative association between firm political connectedness and SEC enforcement are noisy or biased

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[2] We thank the reviewer for supplying this information.

representations of firms' true political connections. In particular, the fraud-prone firms that are more likely to receive SEC scrutiny at the enforcement stage may underreport their political contributions (e.g., to diffuse media scrutiny), yielding the negative result in the prior literature. Since all firms, not just fraud-prone firms, are subject to SEC scrutiny at the CL stage, the concern about underreporting of political contributions is less likely to apply in our sample. Put differently, if fraud-prone firms underreport PC, our sample is less biased than those used in prior tests, and the true relation between firm PC and SEC oversight (even at the enforcement stage) is positive, inconsistent with SEC capture. While we do not necessarily view this data issue as the most likely explanation for results in the prior literature, exploring this concern about the prior literature's measures of PC is an opportunity for future research. Our findings give new impetus for such research.

The simple conclusion we draw from our results is that it is difficult to infer that SEC oversight of PC firms is captured or lax as is suggested in prior literature. Rather, our results suggest a more nuanced relation between PC and SEC oversight in that SEC capture, if it exists, may be less blatant or pronounced than previously thought. The maintained assumption here, as in the prior literature, is that some SEC officials are at least nominally aware of firms' political connectedness. Anecdotal descriptions of the DCF's review process are supportive of this idea – senior SEC officials, who are more likely to be politically astute, allocate and oversee staff reviews of firms. Moreover, our finding that more senior SEC officials are involved in CL reviews of PC firms is consistent with this notion.

This paper contributes to the accounting literature on regulation and the political process by presenting a fuller picture of the role of firm political connections in SEC oversight. We also contribute to the growing literature on CL determinants and consequences (e.g., Cassell et al. 2013; Bozanic et al. 2015; Johnston and Petacchi 2014; Dechow et al. 2016). By focusing on how firm PC affects the likelihood of receiving CLs, we extend the economic

analysis of CL activity into the political domain. The political behavior of regulators is an important but understudied area in accounting (e.g., Kothari et al. 2010). Finally, our paper is one of the few studies in regulation that provides evidence inconsistent with regulatory capture – although empirical work on capture is limited, the evidence is largely supportive of capture (see, e.g., Dal Bo's, 2006, review).

The rest of the paper proceeds as follows. Section 2 describes the institutional background to the SEC's CL process and develops our hypotheses. Section 3 describes the sample and primary research design and presents descriptive statistics. Section 4 presents the main empirical results. Section 5 presents results of tests on the substantive characteristics of SEC CL reviews. Section 6 concludes.

2. Background

2.1. The SEC's Comment-Letter Review Process

The SEC is composed of several divisions, including the Division of Enforcement (DOE) and the Division of Corporation Finance (DCF). The former handles investigations of possible violations of federal securities laws, including violations of requirements for U.S. listed companies to provide financial reports in accordance with U.S. GAAP. The latter provides interpretive assistance to listed companies with regards to SEC rules, which includes reviewing firm financial reporting in real time to monitor and enhance compliance (SEC 2015b). The goal of the review is the protection of investors and is described by the DCF as a "dialogue with a company about its disclosures" (SEC 2015b).

Section 408 of the Sarbanes-Oxley Act of 2002 (SOX) requires the DCF to review U.S. listed-firm filings at least once every three years. This review is done by one of twelve offices

at the DCF, each led by an assistant director, where the offices are organized by industry.[3] The assistant directors are overseen by associate directors, and the deputy director and director of the DCF oversee the entire filing review process. Similar to the Internal Revenue Service's audit formula, the DCF does not discuss the specifics of when and why certain firms are reviewed. Section 408 of SOX specifies criteria that the DCF should consider in selecting firms to review (which we describe in a later section).[4] The DCF reviews vary in scope by the number of topics covered and the seniority of SEC staff involved (GAO 2013). Some reviews focus on just one topic, e.g., financial-statement presentation. Other reviews can cover dozens of topics, including substantive accounting issues like revenue recognition and asset impairment policies. Similarly, some reviews appear to be largely conducted by junior-level staff of the rank of staff accountant, while other reviews appear to also involve senior staff of the rank of branch chief or assistant director.

If questions arise during a financial-reporting review, the DCF issues a comment letter to the reporting firm. The comment letter is an expression of concern by the SEC and an opportunity for the firm to respond to SEC questions about the firm's reporting practices. This comment letter process, once initiated, varies considerably by duration to resolution and the number of intermediate rounds of formal questions and answers between the DCF and the firm.

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[3] All offices are located at the SEC headquarters in Washington, D.C. Each of these twelve offices is staffed with 25 to 35 professionals, primarily accountants and lawyers, and reviews filings of companies in a particular industry as each office has specialized industry, accounting, and disclosure expertise (SEC 2015b). These industries are healthcare and insurance; consumer products; information technologies and services; natural resources; transportation and leisure; manufacturing and construction; financial services I; real estate and commodities; beverages, apparel and mining; electronics and machinery; telecommunications; and financial services II.

[4] DCF aims to review the most highly capitalized companies every year. In addition, division management suggests criteria for selecting other companies for review and allows discretion for assistant directors to make selections within these parameters. According to division officials, together these companies account for a substantial percentage of total market capitalization (GAO 2013).

The outcomes of the comment letter process also vary considerably. The process can result in no action by the firm if all of the SEC's questions are satisfactorily resolved. It may also result in the firm filing an amendment to clarify its prior financial reports or agreeing to adjust future filings in response to a resolution with the SEC over financial reporting concerns (SEC 2015b). In cases where the SEC's concerns are significant and substantively unresolved by the firm's responses, the comment letter process can end with the firm making a restatement of past financial reports. In a few cases, the comment letter process may conclude with the DCF recommending the case to the DOE for enforcement action. These referred cases usually involve suspected willful violation of securities laws by the firms concerned. To effect coordination between the DCF and the DOE, the SEC has in place a special department known as the Office of Enforcement Liaison (OIG 2008). Finally, DCF makes its comment letters and company responses to those comment letters publicly available on the SEC's EDGAR system.

Figure 1 shows the timeline of a 10-K comment-letter review for a firm with a fiscal-year ending on December 31, using the review of American International Group, Inc.'s (AIG) Form 10-K for the fiscal year ended December 31, 2013 as an example. In particular, AIG filed its 10-K on February 20, 2014 and received the first comment letter from DCF on April 29, 2014. AIG sent a response to the SEC on May 13, 2014, i.e., within ten business days, and received the "no further comment" letter from DCF on June 4, 2014. The correspondence between the SEC and AIG was published on EDGAR on July 2, 2014, i.e., no earlier than 20 business days after the completion of its review.

– Please insert Figure 1 about here –

2.2. Regulatory Capture

The regulatory capture hypothesis (e.g., Stigler 1971) predicts that political connections help firms extract rents from public agents like politicians and regulators. In the context of the

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SEC specifically, the capture hypothesis suggests that politically connected firms have allies in Congress and the executive administration who can intercede with the SEC on their behalf if needed. Congress determines the SEC's budget and oversees its operations, while the president of the United States, with the advice and consent of the Senate, appoints SEC commissioners and names the SEC chairman (SEC 2015a). As such, pursuing enforcement actions against politically connected firms could be costly to SEC commissioners and staff if such actions antagonize the SEC's overseers. Correia (2014) reports that firms' political connections mitigate the likelihood and degree of SEC enforcement actions in that PC firms are less likely to receive Accounting and Auditing Enforcement Releases and receive lower penalties if prosecuted. Yu and Yu (2011) also report that firms' political connections influence the likelihood and degree of SEC enforcement decisions.

The possibility of regulatory capture is moderated by the idea that Congress and the president likely balance special-interest favors with voter support (also see Heese 2015). If politicians and regulators go too far in terms of providing special-interest favors (e.g., sparing politically connected firms from enforcement actions even after egregious accounting violations or, at least, doing so too often), then these public agents are likely to face voter backlash (the "political cost hypothesis" of Watts and Zimmerman 1978). For instance, after the failure of Enron, senior politicians in both parties faced criticisms over their close connections to that firm, particularly over concerns that these relationships might have enabled more lax regulatory oversight.

Overall, given myriad forces that regulators and politicians have to balance, it is unclear how blatant or pronounced SEC capture is likely to be. SEC oversight involves activities that are not limited to enforcement actions; it extends to comment-letter reviews. As such, it is difficult to draw strong conclusions about the laxness of SEC oversight of PC firms based on enforcement actions alone. Our objective in this paper is to provide evidence on the relation

between PC and the likelihood and substantive characteristics of CL reviews. If SEC capture by PC firms is empirically descriptive, we expect a negative relation between PC and the likelihood and substantive characteristics of CL reviews.

As in the prior literature, a maintained assumption in the discussion above is that SEC officials are at least nominally aware of firms' political connectedness. Anecdotal interview evidence from a former DCF staffer is supportive of this idea. The former staffer spoke of a "top-down" management style, where senior SEC officials, who are more likely to be politically astute, allocate and oversee staff reviews of firms. In line with this anecdotal evidence, a GAO (2013) report notes that "using selective review criteria, assistant director offices evaluate company and transaction disclosures to determine the appropriate level of review of each transactional filing" and that assistant directors allocate as well as oversee lower level staff. Assistant Directors are monitored by Associate Directors who have to report to the head of the division. Finally, as maintained by Blackburne (2014), DCF staff does not necessarily need to observe the political contributions directly if these contributions are correlated with other indicators of political connectedness that staff does observe, such as inquiries from congressional staff or lobbyists.

3. Sample, Research Design, and Descriptive Statistics

3.1. Sample

We obtain data on comment letters from Audit Analytics for 2005 through 2012. The sample begins in 2005 because this is the first year for which all necessary comment-letter data necessary are publicly available.[5] The sample ends in 2012, the last year for which we could ensure that we had all relevant comment letters for the study. We exclude foreign firms

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[5] On June 24, 2004, the SEC announced it would make comment and response letters related to filings filed after August 1, 2004 publicly available. On May 12, 2005, the SEC actually began to release the comment letters (SEC 2004).

cross-listed in the U.S., for two reasons. First, foreign firms are less likely to receive comment letters. Second, and more importantly for our study, foreign firms are legally not allowed to influence electoral outcomes in the United States – for instance, foreign firms cannot create a Political Action Committee (PAC).

The final sample consists of 33,084 firm-year observations, representing 5,848 distinct firms as shown in Table 1, Panel A. Table 1, Panel B, shows that on average about one-third of the firms receive a comment letter, suggesting that the SEC has achieved its goal of reviewing at least 33 percent of firms each year. The average (median) comment letter addresses nine (seven) topics, and its resolution takes, on average, 67 (57) days and four (four) rounds of responses with the SEC.

– Please insert Table 1 about here –

3.2. Research Design

The primary regression model to examine the relation between PC firms and the incidence of receiving a comment letter is the following, where the subscript *i* represents the firm and *t* the year:

$$\Pr(\text{Comment\_Letter}_{it}) = \beta_0 + \beta_1 \text{PC}_{it} + \sum_n \beta_n \text{Controls}_{it} + e_{it} \qquad (1)$$

Comment_Letter$_{it}$ is an indicator equal to one if the firm *i* received a comment letter related to its 10-K filings for the fiscal year ended *t*, and 0 otherwise. We estimate Model 1 using logistic regression estimation.

Following prior literature (Correia 2014; Blau et al. 2013; Yu and Yu 2011) and guidance from the Center for Responsive Politics (CRP 2013), we use two primary measures to identify PC firms: contemporaneous lobbying expenditures by the firm and contemporaneous PAC

donations.[6] We obtain data on firms' lobbying expenditures from the CRP and measure political connections as the natural logarithm of (one plus) firms' lobbying expenditures, denoted *Log_Lobby_Amount*. We obtain data on firms' PAC contributions from the Federal Elections Commission database and measure political connections as the natural logarithm of (one plus) firms' PAC contributions, denoted *Log_PAC_Amount*. In robustness tests described later in the manuscript we also use alternative measures of political connections.

The control variables in the regression are mainly motivated by SOX Section 408, paragraph (b), as well as Cassell et al. (2013) who study the likelihood of firms receiving comment letters. In particular, SOX Section 408, paragraph (b), identifies firms for the SEC to consider in its reviews of filings: "(1) issuers that have issued material restatements of financial results; (2) issuers that experience significant volatility in their stock price as compared to other issuers; (3) issuers with the largest market capitalization; (4) emerging companies with disparities in price-to-earnings ratios; (5) issuers whose operations significantly affect any material sector of the economy; and (6) any other factors that the Commission may consider relevant."

With respect to factor (1), we include proxies for internal control quality (*IC_Weak*) and previous failures in financial reporting (*Restate*). We set *IC_Weak* (*Restate*) equal to 1 if the company reported a material weakness (issued a restatement) in year *t*, and 0 otherwise. As the SEC may increase scrutiny in year *t* based on prior internal control weaknesses or restatements, we also include lagged values of *IC_Weak* and *Restate*, i.e., *IC_Weak_Lag* and *Restate_Lag*, respectively. With respect to factor (2), to identify issuers with high volatility in their stock price, we create an indicator equal to 1 if a firm is in the highest quartile of the

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distribution of volatility of abnormal stock returns, denoted *High_Volatility*. With respect to factors (3) and (5), we include firm size (*Log_Mark_Cap*) in the models. With respect to factor (4), we use the *Market_to_Book* ratio to capture firms' growth expectations. Factor (6) allows discretion to the SEC in deciding firm characteristics that might indicate whether more or less firm scrutiny is warranted, and therefore we include a number of additional proxies that we expect to affect SEC scrutiny. The focus of our tests is to examine whether one of these discretionary firm characteristics is PC.

Prior research generally finds that financial reporting quality is higher for larger, more mature, and more profitable companies. Thus, we include a firm's age, denoted as *Firm_Age*, a *Loss* indicator that is one if a firm's net income is negative, and zero otherwise, and a *Low_Market_to_Book* indicator equal to one if the market-to-book ratio is below one. We include the Altman *Z-Score* (Altman 1968) as a proxy for financial distress because financially distressed firms are more likely to be noncompliant with GAAP (Brazel et al. 2009; Dechow et al. 1996). Cassell et al. (2013) find that company complexity increases the extent and likelihood of review. We therefore include sales growth, *Chg_Sales*, an indicator for merger and acquisition activity, *M&A*, and an indicator for restructuring charges, *Restructuring*. As prior literature suggests that disclosure quality and reporting compliance are higher when companies intend to issue securities (e.g., Ettredge et al. 2011), we follow Ettredge et al. (2011) and use subsequent debt and equity issuances, *Ext_Financing*, to proxy for management's plans to issue new equity or debt securities. Following Francis et al. (1994), we include an indicator variable for companies in highly litigious industries, *Litigation_Ind*, because such companies are likely to be subject to heightened scrutiny from regulators, investors, and auditors.

We construct an indicator variable, denoted *Big_4*, equal to one for all firms audited by a Big 4 firm, and zero otherwise. As Big 4 auditors are generally considered higher quality than

non-Big 4 auditors (DeFond 1992; DeFond et al. 2016; Palmrose 1988), clients of the Big 4 may be less likely to violate GAAP. As an additional auditor characteristic, we include auditor tenure, *Auditor_Tenure*, which could be associated with higher reporting quality due to auditor learning or lower reporting quality if auditor independence is compromised (Geiger and Raghunandan 2002; Johnson et al. 2002; Myers et al. 2003). We differentiate between auditor changes initiated by the client, *Auditor_Dismissed*, and those initiated by the auditor, *Auditor_Resigned*, to control for their potentially varying effects on our dependent variables.

We also include proxies for firms' governance characteristics. Following Cassell et al. (2013), we include an indicator if the CEO is the chairman of the board of directors (*CEO_Chair*), the number of independent board members (*Outside_Directors*), the number of board meetings (*Board_Mtgs*) as well as CEO and CFO tenure (*CEO_Tenure* and *CFO_Tenure*, respectively). Since data required to construct these internal governance variables are available for only a subset of our sample, missing values are set to 0 but we include separate indicator variables (*Gov_Missing*) set equal to 1 when the governance data are unavailable, and 0 otherwise (Cassell et al. 2013).

Finally, we include SEC office-year fixed effects to control for idiosyncratic office and time factors that can influence the likelihood of receiving a CL. For instance, Blackburne (2014) suggests that annual SEC office budgets affect the likelihood of receiving a comment letter for all firms reviewed by that office in a particular year. Appendix A presents our variable definitions.

3.3. Descriptive Statistics

Table 2 reports descriptive statistics for the variables described above. Panel A presents statistics for the complete pooled sample. Panel B compares means between PC and non-PC firms (defined in Panel B as firms with either PAC or lobbying activity), while Panel C compares means between comment-letter and no-comment-letter firms. Note that while all

firms are subject to a review once every three years, not all reviewed firms receive a comment letter. Panel A of Table 2 shows that in the full sample 13 percent (18 percent) of firms contribute to PACs (have lobbying expenditures), spending on average about $164,000 ($1,107,000). Panel B shows that PC firms are significantly larger, older, less likely to report a loss, and more likely to have a Big 4 auditor. They also have a longer relationship with their auditors, fewer instances of auditor resignation or dismissal, more board meetings and outside directors, shorter CEO tenure, fewer incidences of internal control weaknesses or restatements, more M&As, and lower Z-Scores. Panel C shows that firms with comment letters are significantly larger, older, more likely to have restated financials, less likely to have an internal control weakness, more likely to have a Big 4 auditor, and less likely to have a low market-to-book ratio. They also have a higher volatility, a longer tenure with their auditors, more board meetings, more outside directors, and smaller changes in sales.

– Please insert Table 2 about here –

Both measures of firms' political connections are correlated with each other (0.50) and with firm size (0.40 to 0.46), emphasizing the importance of controlling for firm size in our empirical tests.

4. Political Connections and the Likelihood of Receiving a Comment Letter

4.1. Main Results

Full Sample Tests. Table 3 shows the results of estimating equation 1 in the pooled sample. We find a positive and significant coefficient on both *Log_Lobby_Amount* and *Log_PAC_Amount*, indicating that PC firms are more likely to receive a comment letter. These results contrast with prior studies that document a negative association between political connectedness and SEC oversight in the form of enforcement. Instead, the results suggest that in the context of DCF reviews, political connections attract greater SEC oversight.

The coefficients on the control variables are consistent with prior research (e.g., Cassell et al. 2013). In particular, we find that firms with lagged internal control weaknesses as well as contemporaneous restatements are more likely to receive a comment letter. Larger, older, loss-making, low market-to-book, and restructuring firms, as well as firms with more board meetings, fewer outside directors, and with high volatility are also more likely to receive a comment letter. Firms with external financing are less likely to receive a comment letter.

– Please insert Table 3 about here –

4.2. Enhancing Identification

In this section we describe a battery of tests that address endogeneity concerns stemming from non-random treatment effects and potential correlated omitted variables, measurement error, and simultaneity.

4.2.1. Propensity-Score Matched Test

A potential concern with the results in Table 3 is that PC and non-PC firms are systematically different and non-randomly assigned to their respective groups. To mitigate this concern, we create a propensity-score matched sample of PC and non-PC firms. For these tests, PC is alternatively defined as a firm with non-zero PAC contributions and non-zero lobbying expenditures. We then match to each PC firm a non-PC firm from the same year, reviewed by the same SEC office, and of similar characteristics along all of the covariates used in Table 3, using a propensity score matching method. We match PC and non-PC firms within a predefined propensity score radius (or "caliper") of 0.0005, and allow for replacement in the selection of matches to ensure that we find a meaningful match for each of the PC firms (Shipman et al. 2017).[7] For the 4,301 PC firm-years defined as having non-zero

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[7] Shipman et al. (2017) argue that matching without replacement may result in lower quality matches and smaller sample size than matching with replacement, as each control observation may be matched only once, even if it is

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PAC contributions, we find matches for 768 PC firm-years yielding a total sample size of 1,536. For the 5,955 PC firm-years defined as having non-zero lobbying expenditures, we find matches for 1,943 PC firm observations yielding a total sample size of 3,886. As reported in Table 4, Panel A and B, the mean comparisons of matched pairs indicate that the matching procedure successfully balances covariates.[8] As shown in Table 4, Panel C, while PAC (lobbying) firms have a 38.5% (35.7%) probability of receiving a comment letter, matched non-PAC (non-lobbying) firms have a probability of 33.7% (32.5%). These differences in comment letter likelihood between PC and non-PC firms are statistically significant at the five percent level, consistent with the results in Table 3.[9]

The PSM balances on observable covariates, so in order to quantify the potential impact of unobserved covariates we relax the assumption that matched observations have the same probability of being a PC firm (Rosenbaum 2002). We find that the results would still be significant at the 90% confidence level if non-PC firms were up to 1.5 (for PAC contributions) or up to 1.3 (for lobbying expenditures) times more likely to be a non-PC firm. As no benchmark exists to determine whether a given hidden bias is large (Armstrong et al. 2010), this finding only provides an insight into robustness with respect to potential hidden bias.

– Please insert Table 4 about here –

the best match for several treatment observations. Thus, replacing observations reduces bias because each treated observation matches with the most similar control observation.

[8] To assess the models' ability to correctly predict firm PC, we report the percentage under the ROC curve for these models (denoted AUC). A value of 0.5 indicates no ability to discriminate, while a value of 1 indicates perfect ability to discriminate. As reported in Table 4, the AUC in Column 1, Panel A (i.e., using *Lobby* as measure of PC) is 0.831, and the AUC in Column 1, Panel B (i.e., using *PAC* as measure of PC) is 0.883, suggesting the models have reasonable ability to correctly predict firm PC.

[9] Stuart and Rubin (2007) note that "… a drawback of matching with replacement is that it may be that only a few unique control units will be selected as matches." We therefore also conduct PSM without replacement. The results are similar to those with replacement (untabulated).

4.2.2. Cross-Sectional Test

To further alleviate potential concerns about omitted variables correlated with PC that might be driving the results, we alternatively identify PC firms as those with lobbying and PAC contributions *targeted specifically at the SEC*. In particular, we create an indicator variable, *Lobby_SEC*, equal to one if the firm explicitly lobbied the SEC and equal to zero otherwise. We identify these firms from lobbying reports filed with the Senate Office of Public Records.[10] For PAC contributions, we identify firms that are the top contributors, denoted *Top_SEC_Contributor*, to congressmen or senators serving on SEC oversight committees (i.e., the House or Senate Banking, Commerce, or Appropriations committees) as reported in the Federal Elections Commission database. Prior research has argued and shown that politicians serving on these oversight committees can affect SEC policies more effectively than other politicians (e.g., Weingast 1984; Correia 2014; Heese 2015). About 1.1 percent of firms in our sample are top contributors and about 0.6 percent of firms lobby the SEC directly. These cross-sectional measures of political connectedness are less correlated with firm size (i.e., 0.18 for top contributing firms and 0.12 for firms lobbying the SEC).

As shown in Table 5, we find that—after controlling for firms' overall lobbying expenditures and PAC contributions—firms that lobby the SEC directly and are the top contributor to politicians serving on SEC oversight committees are significantly more likely to receive a comment letter. These cross-sectional tests provide support to the main results that firm PC attracts SEC scrutiny in the CL review process.

– Please insert Table 5 about here –

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[10] The Lobbying Disclosure Act of 1995 requires lobbying firms and organizations to register and file reports of their lobbying activities with the Secretary of the Senate and the Clerk of the House of Representatives. These reports are made publicly available and disclose the specific lobbying issues and all federal agencies "contacted by the registrant in connection with the general issue area during the reporting period."

4.2.3. Instrumental Variables Test

As another approach to mitigate endogeneity concerns we use an instrument for firm PC. As in prior literature (e.g., Correia 2014), our instruments for a firm's PAC and lobbying expenditures are, respectively, the sum of PAC and lobbying expenditures made by other firms in the same 4-digit SIC industry and the same employee-size decile. These industry-size peer contributions are likely to be associated with the political contributions of a given firm due to peer effects driving political activity (e.g., Grier et al. 1994; Kim 2008). However, they are less likely to directly drive the likelihood of that firm receiving a comment letter.

Following the approach described by Larcker and Rusticus (2010) to test the validity of instruments, we find that both instruments are strongly associated with firms' political spending (see Table 8, Panel A, Columns 1 and 3) with partial F-Tests of 88.31 and 80.63, respectively, which are above the thresholds recommended by Stock et al. (2012). The tests for over-identification restrictions, which are appropriate under the assumption that at least one of the instruments is valid, fail to reject the hypothesis that the instruments are exogenous (p-values are 0.32 and 0.38 for lobbying and PAC contributions, respectively), suggesting the instruments have some validity. The results of the second stage IV regressions (see Table 6, Panel A, Columns 2 and 4) are consistent with the main results reported earlier. Specifically, the results suggest that in the DCF context PC firms are more likely to experience SEC oversight via a comment letter.

A concern with the use of the instruments above arises if industry-wide political costs (Watts and Zimmerman 1986) drive both firm-level accounting choices and industry- & firm-level political contributions. In this case, the instrument (industry-level political contributions) is not exogenous to the response variable (CL review likelihood) because the response variable is known to be driven by firm-level accounting choices. If true, the instrument here is invalid. We therefore also use another IV that is less vulnerable to this concern – state-level

voter turnout. (We continue to use the original instruments to be comparable with prior literature, e.g., Blackburne, 2014, and Correia, 2014.)

State turnout rates, calculated as ballots counted divided by the voting-eligible population for the general elections, can proxy for the state population's political engagement and are therefore likely to be associated with the political contributions of a given firm (e.g., the firm might be more politically engaged). But turnout rates are less likely to directly drive the likelihood of that firm receiving a comment letter, making turnout rates a reasonable instrument in our setting. Accordingly, we replace our industry instrument with the state turnout rates and follow the same approach as described above.[11] We find that the instruments in this new approach are associated with firms' political spending (see Table 6, Panel B, Columns 1 and 3) with partial F-Tests of 32.80 and 56.10, respectively, which are above the thresholds recommended by Stock et al. (2012). The tests for over-identification restrictions, which are appropriate under the assumption that at least one of the instruments is valid, also fail to reject the hypothesis that the instruments are exogenous (p-values are 0.15 and 0.78 for lobbying and PAC contributions, respectively), suggesting the instruments have some validity. The results of the second stage IV regressions (see Table 6, Panel B, Columns 2 and 4) are consistent with the main results reported earlier.

<div align="center">– Please insert Table 6 about here –</div>

4.2.4. Other Robustness Tests

Long-Term PC Measures. A potential simultaneity concern is that firms initiate lobbying and political contributions when they make more opaque accounting choices and that the latter are associated with CL receipt likelihood. Supplementing the tests above we further address

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[11] Our IV tests require at least two instruments with the condition that at least one is valid (Hausman, 1978; Larcker and Rusticus, 2010). Thus, we retain the size-matched instrument in the second set of IV tests using state voter turnout.

this endeogeneity concern by replacing the contemporaneous measures of political spending with long-term measures (e.g., Correia 2014). In particular, *Long_Term_Lobby* and *Long_Term_PAC* are defined, respectively, as the sum of PAC and lobbying spending over the prior five years, requiring further that the firm in question contributed in the current year. Such a long-term, consistent history of political spending—that has been established before the start of the SEC's three year review cycle—is less likely to be associated with any contemporaneous latent accounting quality concern that might drive SEC scrutiny; rather it more likely reflects a firm's predetermined long-term policy on political spending.

For the sample of PC firms the average long-term PAC amount is about $372,068 and the average long-term lobbying amount is $4,751,018. Table 7 presents the multivariate results using *Long_Term_Lobby* and *Long_Term_PAC*. The model in Table 7 is similar to that in Table 3. The results are also similar as the coefficients on the proxies for political connectedness are positive and statistically significant when predicting the likelihood of receiving comment letters.

Differences in Accounting Quality. Another potential concern is that firms' political connections proxy for accounting compliance and reporting issues that drive their higher likelihood of receiving comment letters. We control for this possibility in the regressions described above through multiple proxies: accounting restatements, internal control weaknesses, the 10-K length (word count) and linguistic complexity (FOG index), and the number of SEC filings. Further, in untabulated tests, we find that PC firms do not have lower accounting quality than non-PC firms using these proxies, after controlling for other known determinants of accounting quality from the prior literature. This is consistent with recent research (Duo, 2016) that also finds that PC firms' accounting quality is not lower than that of non-PC firms.

– Please insert Table 7 about here –

5. Political Connections and Comment-Letter Review Characteristics

To shed more light on the nature of comment-letter reviews for politically connected firms, in this section we examine whether the substantive characteristics of SEC CL reviews differ across PC and non-PC firms.

We use the following regression model where the subscript i represents the firm and t the year:

$$\text{Comment\_Letter\_Characteristics}_{it} = \beta_0 + \beta_1 \text{PC}_{it} + \sum_n \beta_n \text{Controls}_{it} + e_{it} \qquad (2)$$

We examine several comment-letter characteristics using data obtained from Audit Analytics. First, we follow Palmrose and Scholz (2004) and Cassell et al. (2013) and classify topics in a firm's first SEC comment letter in a given year that affect revenues, cost of goods sold, selling, general and administrative expenses, and other primary operating activities as "core" earnings topics, denoted *Core_Topics*; topics that affect special one-time items or non-operating activities, such as impairments, restructurings, M&A, discontinued operations, extraordinary items, taxes and goodwill, are classified as "non-core" earnings topics, denoted *Non_Core_Topics*.[12] Second, we use the elapsed time in days from a firm's first SEC comment letter (in a given year) to the SEC's "no further comment" letter as a measure of the review period, denoted *Time*. Third, we use the total number of letters from the SEC to a given firm in a given year, representing the number of rounds in the review, denoted *Rounds*. Finally, we identify whether a supervisor of the SEC review staff was involved in a given firm's review, denoted *Supervisor*. In particular, we define a supervisor as an SEC staff member of the rank of "Accounting Branch Chief" or higher based on the Division of Corporation Finance's hierarchy of review staff as shown on its website (SEC 2015b). Branch chiefs have managerial

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[12] As a robustness test, we also use the number of core earnings topics in all letters from the SEC. The results are unaffected using this alternative measure.

responsibilities and allocate line staff to specific firm reviews. This test helps to better understand whether the SEC allocates more resources (in terms of more senior staff) to reviews of PC firms.

We use OLS regressions for the first four dimensions of comment-letter characteristics and a Logit regression for the last dimension (*Supervisor*). For Model 2 we report results using three different measures of PC, i.e., the contemporaneous measures, the IV measures, and the long-term measures, *Long_Term_Lobby* and *Long_Term_PAC*. Following Cassell et al. (2013), we run Model 2 on the subset of firm-years that received a comment letter and include the total number of comment topics in the first comment letter from the SEC, denoted *Topics*, as an additional control. Further, we control for the dynamic nature of interactions between firms and the SEC by including the first lag of the dependent variable as an additional control. We also control for firms' abnormal engagement, denoted *Abn_Length*, in interactions with the SEC by including the absolute deviation from the average firm response length to the first SEC letter per year, SEC industry office, and number of topics decile. The intuition is that firms that either respond briefly or too extensively compared to other firms reviewed by the same SEC industry office, in the same year, and with a similar number of topics addressed might be trying to evade with too little detail or obfuscate with too much detail. We suppress all the control variables in Table 8 for brevity.

Panels A to E of Table 8 show the results of estimating equation 2 for the different dimensions of review characteristics. The coefficients on the different measures of firms' political connectedness are positive and statistically significant in all models, with two exceptions: the contemporaneous and long-term measures of firm lobbying when examining the duration of the comment-letter review (*Time*). The results generally indicate that comment letters to PC firms address more core and non-core earnings topics, take more time and more rounds to resolve, and are more likely to involve an SEC supervisor. These results suggest PC

firms are subjected to more substantive reviews than non-PC firms, indicating the review of PC firms does not appear to be superficial.

– Please insert Table 8 about here –

A potential alternative explanation for these results is that PC firms "push back" more in the CL review process and this push back is not captured by the *Abn_Length* measure in the regressions. Put differently, rather than the SEC being more substantive in its review of PC firms, it is the PC firms that are more confrontational. One challenge with this explanation is that it is unclear that being evasive, dilatory, or obfuscating with the SEC is a judicious tactic for PC firms *on average*. "Best practices" guidance for firms from auditors[13] on responding to CLs is consistent with this challenge. Further, given the public visibility of the CL review process, it is unclear that firms can gain in terms of public perception from engaging in an unnecessarily protracted review. The interpretation that the SEC conducts a more substantive CL review of PC firms appears to be more plausible.[14]

6. Conclusion

Prior research suggests that PC firms are less likely to be subject to SEC enforcement actions. However, enforcement is only one part of SEC oversight. The SEC also periodically reviews the filings of public companies and issues CLs to *monitor* and *enhance* compliance with disclosure and accounting regulation. In this paper, we examine the relation between PC firms and CL reviews to shed fuller light on the relation between PC firms and SEC oversight.

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[13] See, for example, PwC (2014).

[14] As an alternative, we follow Cassell et al. (2016) and control for firm push back using their variable *Length_Ratio*: the length (in characters) of the company's response by the length (in characters) of the SEC's initial comment letter. Our results hold using this alternative measure. In additional unreported tests we identify firms' 10-K amendments and restatements that occurred during the review process and examine whether our proxies for a more extensive review process are positively associated with such amendments and restatements. For four of the five proxies we find a positive and significant association with the probability to amend and restate, suggesting that more extensive reviews have consequences for firms. Though we are reluctant to over-infer from this result, to some extent it suggests that "pushing back" against the SEC is not a prudent tactic.

Across a range of tests that are intended to collectively mitigate identification concerns, results indicate that PC firms are more likely to receive a CL. Results further indicate that CLs issued to PC firms have more core and non-core earnings topics, take longer to conclude in terms of number of days and rounds, and are more likely to involve a supervisor. This suggests CL reviews are not conducted perfunctorily by the SEC.

Our results suggest that it is difficult to necessarily conclude that SEC oversight of PC firms is captured or lax as indicated in prior literature. Rather, our findings point to a more nuanced relation between PC and SEC oversight in that SEC capture, if it exists, may be less blatant or pronounced than previously thought. Firms' political connections appear to be a flag for added scrutiny in the CL review stage. Understanding the causes of this is one opportunity for future research.

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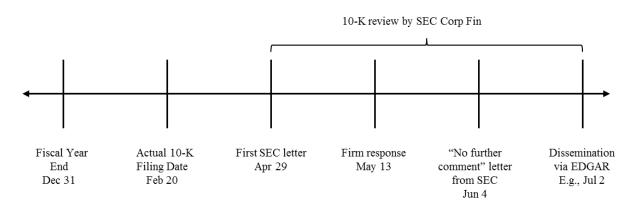
Appendix A: Variable Definitions

Variable	Description
Primary Dependent Variable	
Comment_Letter	1 if a firm has received a comment letter related to its 10-K filings from the SEC in year *t* as reported in Audit Analytics, and zero otherwise.
Review Characteristics Variables	
Topics	The total number of issue codes, assigned by Audit Analytics, in the first comment letter from the SEC.
Core_Topics	The total number of core-earnings topics issue-codes (i.e., revenues, cost of goods sold, SG&A expenses, and other primary operating activities), assigned by Audit Analytics, in the first comment letter from the SEC. For a detailed list of the assignment of issue codes, see Appendix B of Cassell et al. (2013).
Non-Core_Topics	The total number of non-core earnings topics issue-codes (i.e., acquisitions, asset sales, capitalization of expenditures, comprehensive income, consolidation issues such as off-balance sheet items, debt, stock options and compensation, foreign and subsidiary issues, intercompany accounting issues, tax issues, and dividends), assigned by Audit Analytics, in the first comment letter from the SEC. For a detailed list of the assignment of issue codes, see Appendix B of Cassell et al. (2013).
Supervisor	1 if a comment-letter review involved a supervisor, i.e., an SEC staff member of the rank of "Accounting Branch Chief" or above, and zero otherwise. This variable is based on the organizational chart of the Division of Corporation Finance available at https://www.sec.gov/corpfin/Article/filing-review-process---corp-fin.html.
Rounds	The number of letters from the SEC, as reported by Audit Analytics, representing the number of rounds from the first letter to the "no further comment" letter.
Time	The response time (in days) from the first comment letter to the "no further comment" letter, as reported by Audit Analytics.
Political Connections Variables	
Lobby	1 if a firm's lobbying expenditures as reported in the Center for Responsive Politics (CRP) dataset are greater than 0, zero otherwise.
Log_Lobby_Amount	The natural log of a firm's lobbying expenditures as reported in the CRP dataset.
Long_Term_Lobby	The natural log of the sum of a firm's lobbying expenditures in years *t* to *t-4* as reported in the CRP dataset, requiring that the firm contributed in year *t*.
Lobby_SEC	1 if a firm lobbies the SEC directly as reported in the CRP dataset, zero otherwise.
Industry_Lobby_Amount	The natural log of the sum of firms' lobbying expenditures per industry-year (4-digit SIC code).
Size_Lobby_Amount	The natural log of the sum of firms' lobbying expenditures per size decile-year using the number of employees as a measure for firm size.
PAC	1 if a firm's PAC contributions as reported in the Federal Elections Commission database are greater than 0, zero otherwise.
Log_PAC_Amount	The natural log of a firm's PAC contributions as reported in the Federal Elections Commission database.
Long_Term_PAC	The natural log of the sum of a firm's PAC contributions in years *t* to *t-4* as reported in the Federal Elections Commission database, requiring that the firm contributed in year *t*.
Top_SEC_Contributor	1 if a firm is the top contributor to politicians that serve on an SEC oversight committee (i.e., the House or Senate Banking, Commerce or Appropriations committees) as reported in the Federal Elections Commission database, zero otherwise.
Industry_PAC_Amount	The natural log of the sum of firms' PAC contributions per industry-year (4-digit SIC code).

Size_PAC_Amount	The natural log of the sum of firms' PAC contributions per size decile-year using the number of employees as a measure for firm size.
Voter_Turnout	State turnout rates calculated as ballots counted divided by the voting-eligible population for the 2004 to 2012 general elections, as reported on www.electproject.org.

Control Variables

Section 408 Criteria

High_Volatility	An indicator variable set equal to 1 if the volatility of abnormal monthly stock returns (equal to the monthly return [RET] minus the value weighted return [VWRTD]) is in the highest quartile in a given fiscal year, and 0 otherwise. We obtain this data from CRSP.
IC_Weak	An indicator variable set equal to 1 if the internal control audit opinion (under SOX Section 404) or the management certification (under SOX Section 302) as reported in Audit Analytics is qualified for a material weakness in year *t*.
IC_Weak_Lag	An indicator variable set equal to 1 if *IC_Weak* is equal to 1 in year *t*-1, and 0 otherwise. We obtain this data from Audit Analytics.
Log_Mark_Cap	The natural log of market capitalization, calculated as shares outstanding at fiscal year-end (CSHO) times the share price at fiscal year-end (PRCC_F), as reported in Compustat.
Restate	An indicator variable set equal to 1 if the company filed a 10-K restatement in year *t*, as reported in Audit Analytics.
Restate_Lag	An indicator variable set equal to 1 if *Restate* is equal to 1 in year *t*-1, and 0 otherwise, as reported in Audit Analytics.
Irregular_Restate	1 if the restatement is related to an accounting irregularity, and zero otherwise. We follow Srinivasan et al. (2014) and define restatements related to severe accounting irregularities using (i) ex post measures using external or board investigation (Hennes et al. 2008), and (ii) ex ante measures using the core/non-core account classification (Palmrose et al. 2004). Core accounts are those related to revenue recognition, cost of goods sold, operating expenses, or depreciation. The classification uses restatement descriptions provided in Audit Analytics.

Other Company Characteristics

Log_Words	The natural log of the number of words of firms' 10-K, as reported in the WRDS SEC Analytics Suite.
Fog	The Fog index, developed by Robert Gunning, calculated as follows: Fog = (words per sentence + percent of complex words) * 0.4. The index indicates the number of years of formal education a reader of average intelligence would need to read the text once and understand it, as reported in the WRDS SEC Analytics Suite.
Filings	The number of registration filings with the SEC made by a firm per year, as reported in the WRDS SEC Analytics Suite.
Chg_Sales	The percentage change in annual sales (REVT) as reported in Compustat from year *t*-1 to year *t*.
F-Score	Predicted value = -7.893 + 0.79 * RSST accruals + 2.518 * Change in receivables + 1.191 * Change in inventory + 1.979 * % Soft assets + 0.171 * Change in cash sales + -0.932 * Change in ROA + 1.029 * Actual issuance. Based on this predicted value the probability is calculated as $e^{(\text{predicted value})}/(1+e^{(\text{predicted value})})$. To arrive at the F-score the probability is divided by the unconditional probability, i.e., misstating firm-years/(non-misstating firm-years + misstating firm-years). For more details see Dechow et al. (2011).
Ext_Financing	The sum of equity financing and debt financing scaled by total assets, measured in *t*+1, following Ettredge et al. (2011). Equity financing equals the sales of common and preferred stock (SSTK) minus the purchases of common and preferred stock (PRSTKC) minus dividends (DV). Debt financing equals long-term debt issued (DLTIS) minus long-term debt reduction (DLTR) minus the change in current debt (DLCCH). We obtain this data from Compustat.

Litigation_Ind	An indicator variable set equal to 1 if the company is in a highly litigious industry (four-digit SIC industry codes 2833–2836, 3570–3577, 3600–3674, 5200–5961, or 7370–7374, following Francis et al. (1994), and 0 otherwise.
Firm_Age	A firm's age; based on first time appearance in Compustat.
Loss	An indicator variable set equal to 1 if earnings before extraordinary items (IB) as reported in Compustat are negative in year t and 0 otherwise.
M&A	An indicator variable set equal to 1 for non-zero acquisitions or mergers as reported on a pre-tax basis (AQP) in Compustat in year t and 0 otherwise.
Market_to_Book	Firm's market value scaled by firm's book value, i.e., (Compustat item: CSHO * Compustat item: PRCC) / Compustat item: CEQ.
Low_Market_to_Book	1 if a firm's market-to-book ratio is below 1, zero otherwise.
Restructuring	An indicator variable set equal to 1 for non-zero restructuring costs as reported in Compustat on a pre-tax basis (RCP) in year t and 0 otherwise.
Z-Score	Altman's Z-score is measured following Altman (1968) and is equal to 1.2 * [net working capital (ACT-LCT)/total assets (AT)] + 1.4 * [retained earnings (RE)/total assets] + 3.3 * [earnings before interest and taxes (PI + XINT)/total assets] + 0.6 * [market value of equity (CSHO * PRCC_F)/book value of liabilities (LT)] + 1.0 * [sales (SALE)/total assets]. We obtain this data from Compustat.
Abn_Length	Absolute deviation from the average firm response length to the first SEC letter per year, SEC industry office, and number of topics decile.

Auditor Characteristics

Auditor_Dismissed	An indicator variable set equal to 1 if the auditor was dismissed as reported in Audit Analytics in year t, and 0 otherwise.
Auditor_Resigned	An indicator variable set equal to 1 if the auditor resigned as reported in Audit Analytics in year t, and 0 otherwise.
Auditor_Tenure	The number of consecutive years (through year t) as reported in Audit Analytics during which the auditor has audited the company.
Big_4	1 if a firm's auditor is a Big 4 auditor as reported in Audit Analytics, zero otherwise.

Governance Characteristics

Board_Mtgs	The number of board meetings as reported in the Corporate Library. This variable is set equal to 0 if the data are missing and an indicator variable for $Gov\_Missing_{BoardMtgs}$ is set equal to 1.
CEO_Chair	An indicator variable set equal to 1 if the CEO is also the chairman of the board of directors, and 0 otherwise, as reported in ExecuComp. This variable is set equal to 0 if the data are missing and an indicator variable for $Gov\_Missing_{CEO\_Chair}$ is set equal to 1.
CEO_Tenure	The number of years the CEO has served in his/her current role as reported in ExecuComp. This variable is set equal to 0 if the data are missing and an indicator variable for $Gov\_Missing_{CEO\_Tenure}$ is set equal to 1.
CFO_Tenure	The number of years the CFO has served in his/her current role as reported in the Corporate Library. This variable is set equal to 0 if the data are missing and an indicator variable for $Gov\_Missing_{CFO\_Tenure}$ is set equal to 1.
Outside_Directors	The number of independent board members, defined as the number of outside directors, as reported in the Corporate Library. This variable is set equal to 0 if the data are missing and an indicator variable for $Gov\_Missing_{Outside\_Directors}$ is set equal to 1.

Figure 1: Example Timeline of a Comment-Letter Review

10-K review by SEC Corp Fin

| Fiscal Year End Dec 31 | Actual 10-K Filing Date Feb 20 | First SEC letter Apr 29 | Firm response May 13 | "No further comment" letter from SEC Jun 4 | Dissemination via EDGAR E.g., Jul 2 |

This figure shows the timeline of a comment-letter review for a firm with fiscal year end on December 31. As an example, the review of American International Group, Inc.'s (AIG) Form 10-K for the Fiscal Year ended December 31, 2013 has been used.

Table 1: Sample Selection

Panel A: Sample Selection

	Firm-years	Firms
Firm(-years) with Compustat and Audit Analytics identifiers 2005-2012	40,761	7,440
Less: Firm(-years) of cross-listed firms	6,420	1,262
Less: Firm(-years) with missing data	1,257	330
Final sample for Model 1	33,084	5,848
Less: Firm(-years) without a comment letter	22,096	1,322
Final sample for Model 2	10,988	4,526

Panel B: Comment Letter Statistics

Year	Firms with complete data	Proportion of firms receiving a comment letter in %	Firms receiving a comment letter	Mean number of topics	Median number of topics	Mean number of core earnings topics	Median number of core earnings topics	Mean number of non-core earnings topics	Median number of non-core earnings topics	Mean time spent in days	Median time spent in days	Mean number of rounds	Median number of rounds
2005	4,696	22.00	1,033	11.46	9	1.22	1	1.88	1	71.68	64	4.19	4
2006	4,575	28.85	1,320	9.77	7	0.98	1	1.93	1	73.14	63	4.49	4
2007	4,433	29.59	1,311	9.40	7	0.89	1	1.88	1	69.20	61	4.38	4
2008	4,312	34.23	1,476	8.32	6	0.65	0	1.42	1	66.26	55	4.48	4
2009	4,081	43.06	1,757	9.15	6	0.65	0	1.49	1	72.11	64	4.79	5
2010	3,845	43.72	1,681	8.83	6	0.56	0	1.11	1	68.74	58	4.69	5
2011	3,773	33.97	1,282	10.15	7	0.54	0	1.58	1	61.08	47	4.43	4
2012	3,369	39.62	1,335	7.38	5	0.47	0	1.29	1	55.68	43	4.24	4
Mean	4,136	34.38	1,422	9.31	6.63	0.75	0.38	1.57	1	67.24	56.88	4.46	4.25

The table displays comment letter statistics over the period 2004-2012 for U.S. listed firms. All variables are winsorized at 1% and 99% levels. See Appendix A for variable definitions.

Table 2: Descriptive Statistics

Panel A: Pooled sample

Variable	N	Mean	Std.	Median
Both PAC and Lobby	33,084	0.02	0.13	0
PAC	33,084	0.13	0.34	0
PAC_Amount	4,301	163,903	300,216	54,236
Lobby	33,084	0.18	0.38	0
Lobby_Amount	5,955	1,107,081	2,678,878	240,000
IC_Weak	33,084	0.06	0.23	0
Restate	33,084	0.08	0.27	0
High_Volatility	33,084	0.25	0.43	0
Mark_Cap	33,084	2,650	6,860	404
Market_to_Book	33,084	2.60	4.18	1.72
Firm_Age	33,084	18.37	14.65	14
Loss	33,084	0.32	0.46	0
Low_Market_to_Book	33,084	0.23	0.42	0
Z-Score	33,084	3.16	7.64	1.82
Chg_Sales	33,084	0.07	0.26	0.02
M&A	33,084	0.02	0.14	0
Words	33,084	41,312	19,411	37,468
Fog	33,084	20.07	0.89	20.03
Filings	33,084	118.05	91.88	90
Restructuring	33,084	0.01	0.11	0
Ext_Financing	33,084	0.05	0.23	0.00
Litigation_Ind	33,084	0.27	0.44	0
Big_4	33,084	0.69	0.46	1
Auditor_Resigned	33,084	0.01	0.12	0
Auditor_Tenure	33,084	11.93	14.13	7.24
Auditor_Dismissed	33,084	0.05	0.21	0
Board_Mtgs	15,609	7.88	2.93	7
Outside_Director	15,609	6.39	2.28	6
CEO_Tenure	11,904	8.95	6.78	7
CEO_Chair	14,181	0.46	0.50	0
CFO_Tenure	2,463	4.07	3.02	3

Panel B: Sample partitioned on political connections

Variable	N	Politically connected firms Mean (1)	N	Politically non-connected firms Mean (2)	Difference (1) – (2)
Comment_Letter	7,428	0.448	25,656	0.305	0.143***
IC_Weak	7,428	0.039	25,656	0.062	-0.023***
Restate	7,428	0.070	25,656	0.081	-0.011***
High_Volatility	7,428	0.152	25,656	0.277	-0.125***
Mark_Cap	7,428	7,708	25,656	1,159	6,549***
Market_to_Book	7,428	2.87	25,656	2.53	0.34***
Firm_Age	7,428	25.61	25,656	16.24	9.37***
Loss	7,428	0.21	25,656	0.34	-0.13***
Low_Market_to_Book	7,428	0.168	25,656	0.248	-0.80***
Z-Score	7,428	2.66	25,656	3.31	-0.65***
Chg_Sales	7,428	0.070	25,656	0.069	0.001
M&A	7,428	0.023	25,656	0.019	0.004**
Words	7,428	51,583	25,656	38,222	13,361***
Fog	7,428	20.23	25,656	20.03	0.20***
Filings	7,428	165.28	25,656	104.57	60.71***
Restructuring	7,428	0.016	25,656	0.011	0.005***
Ext_Financing	7,428	0.017	25,656	0.059	-0.042***
Litigation_Ind	7,428	0.22	25,656	0.28	-0.06***
Big_4	7,428	0.91	25,656	0.62	0.29***
Auditor_Resigned	7,428	0.005	25,656	0.017	-0.012***
Auditor_Tenure	7,428	17.60	25,656	10.09	7.51***
Auditor_Dismissed	7,428	0.033	25,656	0.051	-0.018***
Board_Mtgs	4,933	8.14	10,676	7.86	0.28***
Outside_Director	4,910	7.49	10,699	5.87	1.62***
CEO_Tenure	4,139	8.19	7,765	9.65	-1.46***
CEO_Chair	5,527	0.51	8,654	0.49	0.02***
CFO_Tenure	740	4.60	1,723	4.66	-0.06

Panel C: Sample partitioned on receipt of comment letter

Variable	N	Comment letter firms Mean (1)	N	No-letter firms Mean (2)	Difference (1) – (2)
PAC	10,988	0.187	22,096	0.103	0.084***
PAC_Amount	10,988	20,359	22,096	8,760	11,599***
Lobby	10,988	0.235	22,096	0.146	0.089***
Lobby_Amount	10,988	134,974	22,096	62,418	72,556***
IC_Weak	10,988	0.051	22,096	0.060	-0.009***
Restate	10,988	0.083	22,096	0.077	0.006*
High_Volatility	10,988	0.221	22,096	0.263	-0.042***
Mark_Cap	10,988	4,116	22,096	1,903	2,213***
Market_to_Book	10,988	2.66	22,096	2.58	0.08
Firm_Age	10,988	20.40	22,096	17.34	3.06***
Loss	10,988	0.28	22,096	0.33	-0.05***
Low_Market_to_Book	10,988	0.212	22,096	0.239	-0.027***
Z-Score	10,988	3.06	22,096	3.21	-0.15
Chg_Sales	10,988	0.065	22,096	0.071	-0.006**
M&A	10,988	0.025	22,096	0.018	0.007***
Words	10,988	44,378	22,096	39,662	4,716***
Fog	10,988	20.13	22,096	20.04	0.09***
Filings	10,988	135.81	22,096	109.34	26.47***
Restructuring	10,988	0.015	22,096	0.011	0.004***
Ext_Financing	10,988	0.032	22,096	0.059	-0.027***
Litigation_Ind	10,988	0.26	22,096	0.27	-0.01*
Big_4	10,988	0.774	22,096	0.645	0.129***
Auditor_Resigned	10,988	0.011	22,096	0.016	-0.005***
Auditor_Tenure	10,988	13.40	22,096	10.97	2.43***
Auditor_Dismissed	10,988	0.043	22,096	0.049	-0.006**
Board_Mtgs	6,249	8.02	9,360	7.90	0.12***
Outside_Director	6,210	6.44	9,399	6.18	0.26***
CEO_Tenure	4,377	9.10	7,527	9.03	0.07
CEO_Chair	6,136	0.468	8,045	0.441	0.027***
CFO_Tenure	846	4.12	1,617	4.06	0.06

Table 2 shows the summary statistics for all variables used in Model 1 over the period 2005-2012. Panel A shows statistics for the pooled sample. Panel B shows means separately for politically connected and politically non-connected firms. Politically connected firms have lobbying expenditures or PAC contributions larger than zero and non-connected firms do not. Panel C shows means separately for firms that receive a comment letter and firms that do not receive comment letters. The table also displays the differences between the means of these variables. ***, **, and * indicate the significance at the 1%, 5% and 10% level, respectively. Appendix A presents variable definitions.

Table 3: PC and CL Likelihood

Variables	(1) Comment_Letter	(2) Comment_Letter
Log_Lobby_Amount	0.006**	
	(0.02)	
Log_PAC_Amount		0.015***
		(0.00)
Section 408 Criteria		
IC_Weak	0.032	0.033
	(0.59)	(0.57)
IC_Weak_Lag	0.156***	0.158***
	(0.01)	(0.00)
Restate	0.171***	0.173***
	(0.00)	(0.00)
Restate_Lag	-0.006	-0.005
	(0.90)	(0.92)
High_Volatility	0.202***	0.196***
	(0.00)	(0.00)
Log_Mark_Cap	0.201***	0.197***
	(0.00)	(0.00)
Market_to_Book	-0.003	-0.003
	(0.31)	(0.34)
Other Company Characteristics		
Firm_Age	0.004***	0.004***
	(0.00)	(0.00)
Loss	0.087***	0.085***
	(0.00)	(0.01)
Low_Market_to_Book	0.091***	0.086**
	(0.01)	(0.01)
Z-Score	-0.000	-0.000
	(0.30)	(0.30)
Chg_Sales	0.019	0.023
	(0.73)	(0.67)
M&A	0.010	0.016
	(0.90)	(0.85)
Restructuring	0.144	0.145
	(0.17)	(0.17)
Ext_Financing	-0.095***	-0.094***
	(0.01)	(0.01)
Litigation_Ind	-0.016	-0.010
	(0.62)	(0.75)
Log_Words	0.119***	0.118***
	(0.00)	(0.00)
Fog	0.007	0.008
	(0.59)	(0.54)

Filings	0.001***	0.001***
	(0.00)	(0.00)
Auditor Characteristics		
Big_4	-0.045	-0.045
	(0.14)	(0.15)
Auditor_Resigned	0.072	0.071
	(0.53)	(0.54)
Auditor_Tenure	0.000	0.000
	(0.65)	(0.67)
Auditor_Dismissed	0.078	0.080
	(0.19)	(0.18)
Governance Characteristics		
Board_Mtgs	0.010**	0.009**
	(0.03)	(0.03)
Outside_Director	-0.020***	-0.022***
	(0.01)	(0.00)
CEO_Tenure	0.002	0.002
	(0.28)	(0.27)
CEO_Chair	0.041	0.038
	(0.28)	(0.32)
CFO_Tenure	0.000	0.000
	(0.72)	(0.74)
Constant	-4.133***	-4.090***
	(0.00)	(0.00)
Gov_Missing	Yes	Yes
SEC office-year FE	Yes	Yes
SE clustered by	Firm	Firm
Observations	33,084	33,084
Pseudo R-square	0.085	0.085

The table presents results on the relation between firm PC and CL likelihood. The dependent variable in all models is an indicator variable equal to one if a firm received a comment letter referring to its 10-K filings, and zero otherwise. All models span the period 2005–2012. The results reported are from a logistic regression estimation and use the full sample as defined in Table 1, Panel A. *p*-values are displayed in parentheses below the coefficient estimate. *, **, *** represent significance at the 10, 5, and 1 percent level (two-tailed), respectively. Appendix A presents variable definitions.

Table 4: Propensity Score Matching

Panel A: First stage regression and covariate balance using LOBBY as measure of PC

Variables	(1) Lobby	(2) Mean lobby firm	(3) Mean matched non-lobby firm	(4) Mean Difference (2) – (3)
Section 408 Criteria				
IC_Weak	0.030	0.064	0.061	0.003
	(0.73)			(0.64)
IC_Weak_Lag	0.061	0.063	0.057	0.006
	(0.47)			(0.38)
Restate	0.028	0.088	0.091	-0.003
	(0.68)			(0.78)
Restate_Lag	0.029	0.084	0.081	0.003
	(0.66)			(0.73)
High_Volatility	-2.327***	0.111	0.115	-0.004
	(0.00)			(0.67)
Log_Mark_Cap	0.547***	6.181	6.209	-0.028
	(0.00)			(0.60)
Market_to_Book	0.006	0.933	0.929	0.004
	(0.26)			(0.97)
Other Company Characteristics				
Firm_Age	0.005**	16.323	16.934	-0.611
	(0.08)			(0.12)
Loss	0.221***	0.356	0.348	0.008
	(0.00)			(0.64)
Low_Market_to_Book	0.300***	0.196	0.203	-0.007
	(0.00)			(0.57)
Z-Score	-0.019***	3.482	3.557	-0.075
	(0.00)			(0.76)
Chg_Sales	-0.038	0.085	0.074	0.011
	(0.68)			(0.18)
M&A	-0.043	0.021	0.022	-0.001
	(0.73)			(0.82)
Restructuring	-0.073	0.014	0.015	-0.001
	(0.60)			(0.79)
Ext_Financing	0.050	0.083	0.095	-0.012
	(0.18)			(0.55)
Litigation_Ind	-0.551***	0.306	0.306	0.000
	(0.00)			(0.97)
Log_Words	0.273***	9.979	9.907	0.072
	(0.00)			(0.38)
Fog	-0.137***	18.931	18.806	0.125
	(0.00)			(0.42)
Filings	0.001**	118.34	117.38	0.96
	(0.04)			(0.73)
Auditor Characteristics				
Big_4	0.012	0.781	0.766	0.015
	(0.91)			(0.25)
Auditor_Resigned	0.035	0.011	0.012	-0.001
	(0.85)			(0.76)
Auditor_Tenure	0.003	11.762	12.164	-0.402
	(0.22)			(0.37)
Auditor_Dismissed	-0.030	0.042	0.046	-0.004

	(1)	(2)	(3)	(4)
	(0.72)			(0.48)
Governance Characteristics				
Board_Mtgs	0.030**	4.139	3.999	0.140
	(0.01)			(0.32)
Outside_Director	0.129***	3.281	3.081	0.200
	(0.00)			(0.18)
CEO_Tenure	-0.029***	3.263	2.940	0.323
	(0.00)			(0.17)
CEO_Chair	0.167*	0.220	0.202	0.018
	(0.06)			(0.18)
CFO_Tenure	-0.010	1.990	1.949	0.041
	(0.29)			(0.72)
Constant	-5.011***			
	(0.00)			
Gov_Missing	Yes			
SEC office-year FE	Yes			
SE clustered by	Firm			
Observations	33,084	1,943	1,943	
Area under ROC curve (AUC)	0.831			
Pseudo R-square	0.252			

The table presents the propensity score estimation (column 1) and covariate balance between the matched pairs of lobbying and non-lobbying firms (columns 2-4). The dependent variable in Column 1 is *LOBBY* and we predict the likelihood of having lobbying expenditures based on all covariates used in our main model presented in Table 3, SEC office, and year to calculate the propensity scores using Probit regression estimation with replacement. The model spans the period 2005–2012. Second, we match each lobbying firm to a non-lobbying firm within the same year, SEC Office, and all other covariates, using the propensity scores obtained from the Probit regression. To ensure the smallest propensity-score distance between the treatment and control firms, we apply a caliper matching estimator of 0.0005. Columns 2-4 report the average values of the variables used in the matching procedure after matching and the average difference in these variables of lobbying and the matched non-lobbying firms. *P*-values are displayed in parentheses below the coefficient estimate. *, **, *** represent significance at the 10, 5, and 1 percent level (two-tailed), respectively; variables are winsorized at 1% and 99% levels. See Appendix A for variable definitions.

Panel B: First stage regression and covariate balance using PAC contribution as measure of PC

Variables	(1) PAC	(2) Mean PAC firm	(3) Mean matched non-PAC firm	(4) Mean Difference (2) – (3)
Section 408 Criteria				
IC_Weak	-0.157	0.051	0.040	0.011
	(0.22)			(0.33)
IC_Weak_Lag	-0.199	0.057	0.046	0.011
	(0.11)			(0.30)
Restate	-0.048	0.076	0.074	0.002
	(0.60)			(0.92)
Restate_Lag	-0.013	0.083	0.078	0.005
	(0.88)			(0.71)
High_Volatility	-1.016***	0.221	0.224	-0.003
	(0.00)			(0.90)
Log_Mark_Cap	0.586***	6.466	6.511	-0.045
	(0.00)			(0.59)
Market_to_Book	0.001	0.671	0.947	-0.276
	(0.89)			(0.19)
Other Company Characteristics				
Firm_Age	0.008**	18.672	18.747	-0.075
	(0.02)			(0.92)
Loss	-0.005	0.237	0.255	-0.018
	(0.96)			(0.41)
Low_Market_to_Book	0.505***	0.225	0.203	0.022
	(0.00)			(0.29)
Z-Score	-0.076***	2.616	2.485	0.131
	(0.00)			(0.57)
Chg_Sales	-0.145	0.064	0.076	-0.012
	(0.16)			(0.33)
M&A	-0.393**	0.025	0.017	0.008
	(0.02)			(0.28)
Restructuring	-0.012	0.014	0.013	0.001
	(0.95)			(0.83)
Ext_Financing	-0.152	0.051	0.034	0.017
	(0.44)			(0.54)
Litigation_Ind	-0.838***	0.180	0.207	-0.027
	(0.00)			(0.18)
Log_Words	0.179*	10.144	10.203	-0.059
	(0.06)			(0.59)
Fog	-0.085*	19.279	19.433	-0.154
	(0.09)			(0.46)
Filings	0.001**	119.920	121.390	-1.470
	(0.05)			(0.74)
Auditor Characteristics				
Big_4	0.433**	0.811	0.797	0.014
	(0.02)			(0.48)
Auditor_Resigned	-0.139	0.009	0.013	-0.004
	(0.71)			(0.47)
Auditor_Tenure	-0.000	13.630	13.356	0.274
	(0.94)			(0.73)
Auditor_Dismissed	-0.182	0.043	0.052	-0.009
	(0.12)			(0.40)
Governance Characteristics				

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Board_Mtgs	0.020	4.507	4.664	-0.157
	(0.17)			(0.49)
Outside_Director	0.109***	3.800	3.802	-0.002
	(0.00)			(0.99)
CEO_Tenure	-0.015	3.787	3.616	0.171
	(0.12)			(0.59)
CEO_Chair	0.010	0.271	0.242	0.029
	(0.93)			(0.20)
CFO_Tenure	0.001	2.313	2.276	0.037
	(0.10)			(0.86)
Constant	-6.089***			
	(0.00)			
Gov_Missing	Yes			
SEC office-year FE	Yes			
SE clustered by	Firm			
Observations	33,084	768	768	
Area under ROC curve (AUC)	0.883			
Pseudo R-square	0.335			

The table presents the propensity score estimation (column 1) and covariate balance between the matched pairs of PAC and non-PAC firms (columns 2-4). The dependent variable in Column 1 is *PAC* and we predict the likelihood of contributing to PACs based on all covariates used in our main model presented in Table 3, SEC office, and year to calculate the propensity scores using Probit regression estimation with replacement. The model spans the period 2005–2012. Second, we match each PAC firm to a non-PAC firm within the same year, SEC Office, and all other covariates, using the propensity scores obtained from the Probit regression. To ensure the smallest propensity-score distance between the treatment and control firms, we apply a caliper matching estimator of 0.0005. Columns 2-4 report the average values of the variables used in the matching procedure after matching and the average difference in these variables of PAC and the matched non-PAC firms. *P*-values are displayed in parentheses below the coefficient estimate. *, **, *** represent significance at the 10, 5, and 1 percent level (two-tailed), respectively; variables are winsorized at 1% and 99% levels. See Appendix A for variable definitions.

Panel C: Average Treatment Effects

Variables	**N**	**Comment_Letter**
Mean Lobby Firm	1,943	0.357
Mean Matched Non-Lobby Firm	1,943	0.325
Mean Difference		**0.033****
Mean PAC Firm	768	0.385
Mean Matched Non-PAC Firm	768	0.337
Mean Difference		**0.048****

This table reports the average treatment effect of firm PC on CL likelihood using the propensity score matched samples from Panel A and B. *P*-values are displayed in parentheses below the coefficient estimate. *, **, *** represent significance at the 10, 5, and 1 percent level (two-tailed), respectively. Appendix A presents variable definitions.

Table 5: Cross-Sectional Tests

Variables	(1) Comment_Letter	(2) Comment_Letter
Log_Lobby_Amount	0.005*	
	(0.06)	
Lobby_SEC	0.352**	
	(0.03)	
Log_PAC_Amount		0.013***
		(0.00)
Top_SEC_Contributor		0.256**
		(0.04)
Controls	Yes	Yes
SEC office-year FE	Yes	Yes
SE clustered by	Firm	Firm
Observations	33,084	33,084
Pseudo R-square	0.085	0.085

The table presents the relation between firm PC *targeted at the SEC* and CL likelihood. The dependent variable in all models is an indicator variable equal to one if a firm received a comment letter referring to its 10-K filings, and zero otherwise. All models span the period 2005–2012. The results reported are from a logistic regression estimation. *P*-values are displayed in parentheses below the coefficient estimate. *, **, *** represent significance at the 10, 5, and 1 percent level (two-tailed), respectively; variables are winsorized at 1% and 99% levels. See Appendix A for variable definitions.

Table 6: Instrumental Variables Approach

Panel A: Instrumental Variables Approach – Industry PC

Variables	(1) 1st stage Log_Lobby_Amount	(2) 2nd stage Comment_Letter	(3) 1st stage Log_PAC_Amount	(4) 2nd stage Comment_Letter
Log_Lobby_Amount		0.016***		
		(0.00)		
Industry_Lobby_Amount	0.007***			
	(0.00)			
Size_Lobby_Amount	0.567***			
	(0.00)			
Log_PAC_Amount				0.015***
				(0.00)
Industry_PAC_Amount			0.003***	
			(0.00)	
Size_PAC_Amount			0.659***	
			(0.00)	
Controls	Yes	Yes	Yes	Yes
Gov_Missing	Yes	Yes	Yes	Yes
SEC office-year FE	Yes	Yes	Yes	Yes
SE clustered by	Firm	Firm	Firm	Firm
Exogeneity test (p-value)	0.00		0.01	
Partial F-test (instruments, stage 1)	88.31		80.63	
Test overidentifying restrictions (p-value)	0.32		0.38	
Observations	33,084	33,084	33,084	33,084
(Pseudo) R-square	0.275	0.085	0.309	0.085

This table presents the relation between firm PC and CL likelihood using IV. The models presented here differ in their dependent variables, variables included, and estimation technique. The dependent variable in Columns 2 and 4 is an indicator variable equal to one if a firm received a comment letter referring to its 10-K filings, and zero otherwise. The dependent variable in Columns 1 and 3 is the contemporaneous PC measure. Columns 1 and 3 are the first stage regression for our IV. Columns 2 and 4 are the second stage regression. The results from Columns 2 and 4 are from a logistic regression estimation. Columns 1 and 3 use OLS. All models span the period 2005–2012. *p*-values are displayed in parentheses below the coefficient estimate. *, **, *** represent significance at the 10, 5, and 1 percent level (two-tailed), respectively; variables are winsorized at 1% and 99% levels. See Appendix A for variable definitions.

Panel B: Instrumental Variables Approach – Voter Turnout

Variables	(1) 1st stage Log_Lobby_ Amount	(2) 2nd stage Comment_Let ter	(3) 1st stage Log_PAC_A mount	(4) 2nd stage Comment_Let ter
Log_Lobby_Amount		0.016***		
		(0.00)		
Voter_Turnout	2.142***		1.190*	
	(0.00)		(0.09)	
Size_Lobby_Amount	0.449***			
	(0.00)			
Log_PAC_Amount				0.017***
				(0.00)
Size_PAC_Amount			0.621***	
			(0.00)	
Controls	Yes	Yes	Yes	Yes
Gov_Missing	Yes	Yes	Yes	Yes
SEC office-year FE	Yes	Yes	Yes	Yes
SE clustered by	Firm	Firm	Firm	Firm
Exogeneity test (p-value)	0.00		0.00	
Partial F-test (instruments, stage 1)	32.80		56.10	
Test overidentifying restrictions (p-value)	0.15		0.78	
Observations	33,084	33,084	33,084	33,084
(Pseudo) R-square	0.264	0.085	0.318	0.085

This table presents the relation between firm PC and CL likelihood using IV. The models presented here differ in their dependent variables, variables included, and estimation technique. The dependent variable in Columns 2 and 4 is an indicator variable equal to one if a firm received a comment letter referring to its 10-K filings, and zero otherwise. The dependent variable in Columns 1 and 3 is the contemporaneous PC measure. Columns 1 and 3 are the first stage regression for our IV. Columns 2 and 4 are the second stage regression. The results from Columns 2 and 4 are from a logistic regression estimation. Columns 1 and 3 use OLS. All models span the period 2005–2012. p-values are displayed in parentheses below the coefficient estimate. *, **, *** represent significance at the 10, 5, and 1 percent level (two-tailed), respectively; variables are winsorized at 1% and 99% levels. See Appendix A for variable definitions.

Table 7: Long-term Measures of PC

	(1)	(2)
Variables	Comment_Letter	Comment_Letter
Long_Term_Lobby	0.008***	
	(0.00)	
Long_Term_PAC		0.012***
		(0.00)
Controls	Yes	Yes
Gov_Missing	Yes	Yes
SEC office-year FE	Yes	Yes
SE clustered by	Firm	Firm
Observations	33,084	33,084
(Pseudo) R-square	0.085	0.085

This table presents the relation between firm long-term PC and CL likelihood. The dependent variable in Columns 1 and 2 is an indicator variable equal to one if a firm received a comment letter referring to its 10-K filings, and zero otherwise. Column 1 includes the long-term lobby measure. Column 2 includes the long-term PAC measure. The results are from a logistic regression estimation. All models span the period 2005–2012. *P*-values are displayed in parentheses below the coefficient estimate. *, **, *** represent significance at the 10, 5, and 1 percent level (two-tailed), respectively; variables are winsorized at 1% and 99% levels. See Appendix A for variable definitions.

Table 8: Characteristics of Comment-Letter Reviews

Panel A: Number of Core Earnings Topics

Variables	(1) Core_Topics	(2) Core_Topics IV 2nd stage	(3) Core_Topics	(4) Core_Topics	(5) Core_Topics IV 2nd stage	(6) Core_Topics
Log_Lobby_Amount	0.005** (0.02)	0.041*** (0.00)				
Long_Term_Lobby			0.004* (0.06)			
Log_PAC_Amount				0.006** (0.04)	0.049*** (0.00)	
Long_Term_PAC						0.005** (0.04)
Controls	Yes	Yes	Yes	Yes	Yes	Yes
Gov_Missing	Yes	Yes	Yes	Yes	Yes	Yes
SEC office-year FE	Yes	Yes	Yes	Yes	Yes	Yes
SE clustered by	Firm	Firm	Firm	Firm	Firm	Firm
Observations	10,988	10,988	10,988	10,988	10,988	10,988
R-square	0.261	0.191	0.265	0.265	0.193	0.258

Panel B: Number of Non-Core Earnings Topics

Variables	(1) Non_Core_Topics	(2) Non_Core_Topics IV 2nd stage	(3) Non_Core_Topics	(4) Non_Core_Topics	(5) Non_Core_Topics IV 2nd stage	(6) Non_Core_Topics
Log_Lobby_Amount	0.012*** (0.01)	0.112*** (0.00)				
Long_Term_Lobby			0.007** (0.03)			
Log_PAC_Amount				0.011** (0.02)	0.111*** (0.00)	
Long_Term_PAC						0.010** (0.02)
Controls	Yes	Yes	Yes	Yes	Yes	Yes
Gov_Missing	Yes	Yes	Yes	Yes	Yes	Yes
SEC office-year FE	Yes	Yes	Yes	Yes	Yes	Yes
SE clustered by	Firm	Firm	Firm	Firm	Firm	Firm
Observations	10,988	10,988	10,988	10,988	10,988	10,988
R-square	0.292	0.217	0.338	0.289	0.219	0.338

Panel C: Number of Rounds

Variables	(1) Rounds	(2) Rounds IV 2nd stage	(3) Rounds	(4) Rounds	(5) Rounds IV 2nd stage	(6) Rounds
Log_Lobby_Amount	0.011* (0.06)	0.161*** (0.00)				
Long_Term_Lobby			0.010* (0.06)			
Log_PAC_Amount				0.018** (0.01)	0.129*** (0.00)	
Long_Term_PAC						0.019*** (0.00)
Controls	Yes	Yes	Yes	Yes	Yes	Yes
Gov_Missing	Yes	Yes	Yes	Yes	Yes	Yes
SEC office-year FE	Yes	Yes	Yes	Yes	Yes	Yes
SE clustered by	Firm	Firm	Firm	Firm	Firm	Firm
Observations	10,988	10,988	10,988	10,988	10,988	10,988
R-square	0.091	0.065	0.090	0.092	0.063	0.092

Panel D: Total Time

Variables	(1) Time	(2) Time IV 2nd stage	(3) Time	(4) Time	(5) Time IV 2nd stage	(6) Time
Log_Lobby_Amount	0.229 (0.21)	0.838* (0.06)				
Long_Term_Lobby			0.187 (0.27)			
Log_PAC_Amount				0.667*** (0.00)	0.922** (0.03)	
Long_Term_PAC						0.750*** (0.00)
Gov_Missing	Yes	Yes	Yes	Yes	Yes	Yes
SEC office-year FE	Yes	Yes	Yes	Yes	Yes	Yes
SE clustered by	Firm	Firm	Firm	Firm	Firm	Firm
Observations	10,988	10,988	10,988	10,988	10,988	10,988
R-square	0.093	0.079	0.095	0.095	0.084	0.096

Panel E: Supervisor involved in Review

Variables	(1) Supervisor	(2) Supervisor IV 2nd stage	(3) Supervisor	(4) Supervisor	(5) Supervisor IV 2nd stage	(6) Supervisor
Log_Lobby_Amount	0.011*	0.124**				
	(0.09)	(0.02)				
Long_Term_Lobby			0.009*			
			(0.09)			
Log_PAC_Amount				0.022**	0.060**	
				(0.03)	(0.03)	
Long_Term_PAC						0.016*
						(0.06)
Controls	Yes	Yes	Yes	Yes	Yes	Yes
Gov_Missing	Yes	Yes	Yes	Yes	Yes	Yes
SEC office-year FE	Yes	Yes	Yes	Yes	Yes	Yes
SE clustered by	Firm	Firm	Firm	Firm	Firm	Firm
Observations	10,988	10,988	10,988	10,988	10,988	10,988
Pseudo R-square	0.231	0.188	0.219	0.229	0.187	0.221

This table shows the relation between PC and CL characteristics for firms that receive a CL in year t. In Panel A, the dependent variable is the number of core earnings topics a firm received in a comment letter referring to its 10-K filings. In Panel B, the dependent variable is the number of non-core earnings topics a firm received in a comment letter referring to its 10-K filings. In Panel C, the dependent variable is the number of rounds between the firm and SEC. In Panel D, the dependent variable is the number of days taken between the firm and SEC to resolve the topics mentioned in the comment letter. In Panel E, the dependent variable equals one if a supervisor is involved in the comment-letter review, and zero otherwise. Columns 1 and 4 in all panels use the contemporaneous PC measures. Columns 2 and 5 report the second stage IV results. Columns 3 and 6 use the long-term PC measures. All models span the period 2005–2012 and are estimated within the subset of firm-years that received a comment letter (see Table 1, Panel A for the sample selection). The results reported are from an OLS regression estimation in Panel A-D and from a Logit estimation in Panel E. P-values are displayed in parentheses below the coefficient estimate. *, **, *** represent significance at the 10, 5, and 1 percent level (two-tailed), respectively; variables are winsorized at 1% and 99% levels. See Appendix A for variable definitions.