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Corporate Political Donations: Investment or Agency?

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Abstract

Abstract: We examine corporate donations to political candidates for federal offices in the United States from 1991 to 2004. Firms that donate have operating characteristics consistent with the existence of a free cash flow problem, and donations are negatively correlated with returns. A \$10,000 increase in donations is associated with a reduction in annual excess returns of 7.4 basis points. Worse corporate governance is associated with larger donations. Even after controlling for corporate governance, donations are associated with lower returns. Donating firms engage in more acquisitions and their acquisitions have significantly lower cumulative abnormal announcement returns than non-donating firms. We find virtually no support for the hypothesis that donations represent an investment in political capital. Instead, political donations are symptomatic of agency problems within firms. Our results are particularly useful in light of the Citizens United ruling, which is likely to greatly increase the use of corporate funds for political donations.

KEYWORDS: political contributions, agency problems, stock returns

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Introduction

Why do companies make donations to political parties and to candidates for political office? Companies do not have political preferences per se. They may, however, have an economic interest in various legislative actions, regulatory decisions, or other political outcomes. Thus, one reason why companies may donate is to influence the political process in ways that improve firm performance. An alternative reason is that, while companies do not have political preferences, their managers do. In this view, political donations need not be associated with firm performance and in fact, may damage firm returns as they represent a form of perquisites consumption for the firm's managers. This form of perquisites consumption is often not transparent or visible to shareholders, and can indicate wider agency problems at the firm.

While these two possibilities for why firms donate are not mutually exclusive, they do have very different implications for the firm and its shareholders. Under the first view, donations are an investment in political capital that should, in expectation, generate positive returns for the firm. Under the second view, donations are symptomatic of an agency problem that should lower returns for the firm. We examine which of these views more accurately characterizes political donations in the United States.

We use comprehensive data on corporate political donations from the Center for Responsive Politics. Our data span from 1991 to 2004 and include the four main types of political donations: political action committee (PAC) donations, donations by individuals affiliated with a company, soft money donations, and donations to 527 Committees. We focus specifically on donations made directly from corporate funds—soft money donations and donations to 527 Committees. Of all the publicly-traded firms, only 11.27% or 1,381 firms donated directly from corporate funds during our sample period. Our focus on donations made from corporate funds is particularly salient in the wake of the Supreme Court decision in *Citizens United v. Federal Election Commission*, which essentially eliminates restrictions on the use of corporate funds in elections. We discuss this in greater detail in Section 2.

We find that firms that donate directly from corporate funds have operating characteristics consistent with the firms facing a free cash flow problem—they are large, slowly-growing firms that have more free cash flow, yet engage in less R&D and investment spending. We also find that donations are negatively correlated with future excess returns. An increase in soft money and 527 Committee donations of \$10,000 is associated with a reduction in excess returns of 7.4 basis points in the following year. Similar to Yermack's (2006) results for the personal use of corporate aircraft by CEOs, this reduction in shareholder value far outstrips the dollar value of the donations. This suggests that

political donations may be a useful window into the presence of wider agency problems within firms. To address endogeneity concerns, we instrument for donations and find similar negative associations between donations and returns.

Third, we find that better corporate governance (smaller boards, CEOs who are not also chairman of their board, less abnormal CEO compensation, larger block ownership, and larger institutional ownership) is associated with smaller donations. However, even after we control for corporate governance, we continue to find a negative association between donations and excess returns. Thus, while better governance may attenuate donations, the negative association between donations and excess returns is not wholly attributable to an omitted governance effect. Fourth, we find that firms that make political donations engage in more acquisitions than do non-donating firms. Further, donating firms' acquisitions have significantly lower cumulative abnormal announcement returns than do non-donating firms' acquisitions.

We also examine whether donations to the winning party in an election lead to higher event-study returns. We find positive one-day abnormal returns to donating to the winning party in presidential and congressional election years. This is consistent with the prior literature and has been viewed as supporting the investment hypothesis. For longer-horizon returns, we find no evidence of a positive effect of donating to winners in either presidential or congressional elections. Importantly, we generally find that donating to either winners or losers is associated with worse returns than not donating at all. This provides us with a direct test of the two hypotheses, and our findings are consistent with the agency hypothesis but hard to reconcile with the investment hypothesis.

We also consider the possibility that politicians may do favors for firms and then firms may donate to politicians. If so, a positive effect of political favors on firm returns may occur prior to the donations. To address this, we examine returns for firms that start donating when there is a shift in political control, since these firms are unlikely to be donating in response to past favors. In this case, we still find a strong negative association between firm returns and initiating donations to a party that wins political control. Thus, our results cannot simply be driven by firms choosing to donate after political favors are bestowed. In addition, we examine a subsample of companies in industries that receive government contracts since, for these companies, donations are more likely to be an investment in political capital. We do not find evidence of the hypothesized positive association between donations and returns.

Overall, we find only limited support for the hypothesis that political donations directly from corporate funds represent an investment in political capital. Taken together, our results suggest that political donations are reflective of an agency problem. Given the magnitude of the destruction of shareholder

value that we document, it is more plausible that corporate political donations are symptomatic of wider agency problems in the firm.

The existing literature—which we review in the next section—has largely focused on short-term event studies that examine whether corporate political connections or donations are valuable. While event studies can detect changes in firm value attributable to certain events (e.g., elections), they do not measure potential offsetting costs due to potential agency problems from the donations themselves. In contrast, we test two competing hypotheses—donations as reflective of an agency problem between managers and shareholders versus donations as an investment in political capital. In order to do so, our approach differs along three dimensions.

First, we use the direct monetary amount of donations, which allows us to test the two competing hypotheses, since donations can either be an investment or a measure of perquisites consumption. Second, our focus on soft money donations and 527 Committee donations, which come directly from corporate resources, eliminates concerns that PAC donations are only an indirect form of corporate donations that cannot be attributed to agency concerns. Third, we study long-horizon returns, which help us to formally distinguish between the agency and investment hypotheses. Our focus on stock returns is appropriate given that political donations over our sample period are not disclosed in a transparent or timely fashion to shareholders, and are therefore likely to be capitalized into stock prices only slowly over time.

1. Literature Review and Experimental Design

This paper contributes to a growing literature that looks at the intersection of politics and finance. Several recent papers present event studies examining the effects of the 2000 U.S. presidential elections on companies aligned with Republicans or Democrats, including Knight (2006), Goldman, Rocholl and So (2009), Shon (2010), and Jayachandran (2006). In general, these papers find that good (bad) news for Republicans is associated with a positive (negative) stock price reaction for Republican-leaning firms and a negative (positive) stock price reaction for Democratic-leaning firms. In contrast to our study, these papers necessarily focus on short-run returns, small samples, and isolated events. Cooper, Gulen, and Ovtchinnikov (2010) find evidence of a positive effect of donations on firm value and we discuss their results in greater detail in Section 4.

By contrast, other studies document the ineffectiveness of campaign donations as a form of gaining influence or buying favorable policies. Ansolabehere, de Figueiredo and Snyder (2003) show that when one controls for unobserved constituent and legislator effects, there is little relationship between money and legislator votes. Ansolabehere, Snyder and Ueda (2004) examine the

excess returns of firms that give large amounts of soft money and firms that give no soft money, and changes in those excess returns around five key events in the approval of the Bipartisan Campaign Reform Act of 2002. They find no noticeable effect on the valuation of Fortune 500 firms that give large amounts of soft money relative to the firms that give no soft money.

We note that much of the prior literature uses short-term event studies to examine the effect of political donations on firm returns. We examine long-term (one-year) stock returns instead of short-horizon stock returns for three reasons. First, a short-run event study around an election does not allow us to detect an agency motive for donations. If political donations are a private benefit for managers, then the election outcome is not informative one way or another for shareholders. In this case, an agency motive would be entirely consistent with the results in Ansolabehere, de Figueiredo and Snyder (2003), and Ansolabehere, Snyder and Ueda (2004) that show no immediate benefits from donations.

Second, firms that do not donate are generally left out in the election event studies of donations to winners and losers.¹ However, an examination of non-donors provides valuable information about the motives for donation. As we noted before, many companies choose not to donate, presumably because the costs of donating exceed the benefits. Understanding the determinants of corporate donations helps us distinguish whether donations are related to shareholder value creation or to the management's private benefits.

Third, the short event window of election outcome announcements does not allow us to fully examine the investment value of corporate political donations. If corporate political donations are made as an investment on behalf of shareholders, then the investment value should be incorporated into stock prices as the investment outcomes are realized (or expected to be realized). The probability of these favorable outcomes may increase at the time of the election, but are likely to increase much more over time as the legislative process unfolds—as favorable legislation moves through committees, the House, and the Senate. Since those outcomes take a substantial amount of time to be realized, and there is still a high degree of uncertainty about those outcomes at the time of the election, long-term stock performance appears to be a better measure of the investment value of corporate political donations than the short-term stock returns following an election. Of course, there is also a cost to using long-term stock performance in that long-term stock returns are noisier than event-horizon returns. Later in the paper, we also examine the one-day announcement return associated with the election outcome for completeness.

A second strand of the literature argues that political connections positively influence firm performance.² Other research, however, documents that corporate

¹ An exception is Ansolabehere, Snyder and Ueda (2004)

² See for example Fisman (2001) and Faccio (2006).

political connections are costly to the firm due to rent-seeking by politicians.³ Politically connected firms show low industry-adjusted financial performance, labor capital ratios, and R&D spending relative to other firms of the same age and size. Our results for US firms that donate to politicians are consistent with the results of the studies that find negative effects of political connections on firm performance, but we emphasize a different mechanism. We show that political donations are associated with and indicative of conflicts between shareholders and managers. Our focus on agency problems within firms is distinct from but also complementary to rent-seeking by politicians. We also note that political connections (personal ties between politicians and corporate managers or corporations) are separate from political donations (payments from corporations to politicians). While political connections represent long-term relationships, political donations tend to be transactional and short-term, and vary over time and are spread across parties and candidates.

2. Data

Corporations may be affiliated with giving money to political parties and candidates through four different channels: donations to Political Action Committees (PACs), donations from individuals who list the corporation as their employer, soft money donations, and donations to 527 groups. PACs solicit donations from employees, aggregate the funds, and then make donations to candidates and parties. Although the PAC is set up by the company, its funds come from employee donations, not company resources. Individual donations come directly from individuals, who are asked to disclose their employer when they make donations in excess of \$200 (donations smaller than \$200 are not tracked). PAC and individual donations need not reflect the preferences of either the firm's shareholders or its managers—they may simply reflect the preferences of the individual making the donations.

Soft money donations are unlimited campaign donations to the national parties for party-building activities such as get-out-the-vote drives and non-party specific advertising. Soft money donations are made directly by the company and its officers using company funds. Soft money donations were banned as a result of the Bipartisan Campaign Reform Act as of November 6, 2002, but were an important means of political giving throughout all but the last election cycle of our sample period. After soft money was banned, direct donations from corporate funds switched to 527 groups. These are tax-exempt organizations under section 527 of the Internal Revenue Code and they exist to raise money for political activities like voter mobilization efforts and issue advocacy. These groups became

³ See Morck, Stangeland, and Yeung (2000) for Canada; Fan, Wong, and Zhang (2007) for China; and Bertrand et al. (2005) for France.

more important after the abandonment of soft money donations, which is apparent from Table 1.

On January 21, 2010, the United States Supreme Court effectively struck down the ban on soft money donations from the Bipartisan Campaign Reform Act in its decision in *Citizens United v. Federal Election Commission*. The Supreme Court held that corporate funding of independent political broadcasts in elections cannot be limited under the First Amendment. While the decision does not address the ban on direct donations from corporations to candidates, the decision allows corporate funding of broadcasts that independently support or oppose candidates and positions. As a result, corporations are essentially unlimited in the amount that they can spend on elections going forward.

In this study we primarily report results for soft money and 527 Committee donations. However, our results are quite similar if we also include individual and PAC donations. We focus on soft money and 527 Committee donations because these represent a direct use of corporate funds, whereas PAC and individual donations come from individuals and not the corporation. Moreover, in the wake of the *Citizens United* decision, going forward, direct donations of corporate funds will become much more important. Soft money and 527 Committee donations represent historical examples of direct donations of corporate funds. Focusing on these funding sources makes our tests more relevant for future outcomes.⁴

The Center for Responsive Politics (CRP) has created a comprehensive database based on the Federal Election Commission (FEC) filings that links all four types of donations (PAC, individual, soft money, and 527 groups) to the donor's affiliated organization. Our donation data from 1991 to 2004 comes from this CRP database. These data cover donations to candidates for federal offices (congressional and executive) and national parties; they do not include donations to candidates for state level offices. Further, we do not examine lobbying expenditures in this paper. The CRP reports that there is little correlation between the firms' lobbying expenditures and firms' political donations, suggesting that these are distinct categories for attempting to garner influence.⁵

We aggregate donations of subsidiaries at the level of the parent company and attribute donations of acquired companies made after the acquisition was completed to the acquiring company. We exclude private companies and US subsidiaries of foreign companies, which results in a final sample of 1,381 publicly traded companies that make donations. Over our sample period, only 11.27% of all publicly traded firms donated to candidates for federal offices using corporate funds.

⁴ See also Coates (2010).

⁵ See also Yu and Yu (2010).

Table 1: Summary Statistics of Corporate Political Donations

Panel A: Corporate Political Donations: 1991 – 2004

This panel shows the dollar value of corporate political donations (in millions) at the federal level for the entire sample period and for each sample year. The donation data is obtained from the Center for Responsive Politics (CRP). “PAC Donations” are corporate donations to political action committees, and are also called hard money donations. “Soft Money Donations” are corporate contributions made outside the federal contribution limits to the national parties or outside interest groups. “Individual Money Donations” are limited, regulated contributions made by an individual affiliated with a corporation to a candidate’s campaign committee, a PAC, or a political party. “Donations to 527 Committees” are corporate donations to tax-exempt groups organized under section 527 of the Internal Revenue Code to raise money for political activities including voter mobilization efforts, issue advocacy, etc. Median donations are conditional on positive donations of that type. All the donations are expressed in 2004 dollars.

	# of Obs.	Total Donations	PAC Donations	Soft Money Donations	Individual Money Donations	Donations to 527 Committees
Total	12105	1421.234	604.935	504.953	290.721	20.630
Mean	12105	0.117	0.050	0.042	0.024	0.002
Median	12105	0.028	0.023	0.029	0.008	0.003
1991	708	44.126	26.952	8.588	8.587	0.000
1992	818	82.470	45.542	20.641	16.286	0.000
1993	758	43.054	25.565	10.300	7.182	0.000
1994	888	75.961	44.388	18.286	13.287	0.000
1995	880	71.489	29.928	27.772	13.739	0.000
1996	1205	133.100	49.496	64.363	19.241	0.000
1997	875	72.027	31.591	29.101	11.330	0.000
1998	934	114.400	48.300	49.813	16.285	0.000
1999	880	105.484	36.367	42.700	26.415	0.000
2000	1011	192.141	53.470	104.470	34.199	0.000
2001	867	106.214	38.801	53.483	13.894	0.000
2002	863	152.574	57.818	75.434	19.275	.0525
2003	780	88.148	49.196	0.000	34.855	4.096
2004	818	140.103	67.519	0.000	56.103	16.481

Table 1, Panel A displays the total donations as well as the four categories of political donations by year and shows that for our sample, PAC, soft money, 527 donations, and individual accounted for 42.6%, 35.5%, 1.5%, and 20.5% of total donations, respectively. Throughout this study, all donations are expressed in

2004 dollars. Panel B shows donations aggregated at the industry level for financial trading, telecommunication, utilities, banking, and transportation, the five industries that donated the most money during our sample period based on the Fama-French (1997) 49 industry classification. Both panels show an election year effect: donation levels are higher in even years that correspond to congressional and presidential elections.

Table 1: Summary Statistics of Corporate Political Donations

Panel B: Top Five Donating Industries

The top five industries ranked according to the total dollar value of industry national level political donations (in millions) from 1991 through 2004. The industries are defined according to the Fama-French 49 industry classification.

Year	Fin. Trad.	Telecomm	Utilities	Banking	Transportation
1991-2004	226.361	110.288	99.905	80.637	76.365
1991	8.178	2.229	2.765	1.830	2.217
1992	15.754	3.899	4.596	3.160	3.154
1993	7.734	2.869	2.977	1.336	2.301
1994	12.892	5.176	4.709	2.228	3.321
1995	11.551	6.468	4.532	2.467	3.668
1996	22.379	9.418	8.265	4.707	7.604
1997	13.959	4.953	5.504	3.125	3.368
1998	20.492	8.450	7.986	5.686	6.101
1999	18.841	9.294	8.341	4.969	7.390
2000	28.277	17.357	14.081	10.312	10.248
2001	12.834	9.643	8.991	9.302	7.287
2002	18.824	16.276	12.766	11.455	8.388
2003	15.863	5.830	7.019	5.359	4.992
2004	18.783	8.426	7.372	14.701	6.325

We investigate the effect of political donations in year t on future stock returns in year $t + 1$. If year t is an election year, we expect a portion of the future annual stock return associated with political donations in this year to be driven by the announcement effect of the election outcome. To capture this announcement return, we calculate the annual return variable as the buy-and-hold return from the first Wednesday of November until the first Monday of November the following year. For example, we associate the 2001 (year $t+1$) return (calculated from Wednesday, Nov. 8, 2000 until Monday, Nov. 5, 2001) with all political donations made from January 1, 2000 until December 31, 2000 (year t). In election years, the vast majority of donations are made prior to the election, so the slight overlap in periods (between November 8 and December 31, 2000 in this example) is not, in practice, a problem.

Table 2: Summary Statistics

“Excess Return” is relative to the four-factor model, equal weight (EW) or value weight (VW). “Book/Market” is book value of equity over market value of equity. “ROA” is operating income after depreciation over total assets. “Sales Growth” is the two year average sales growth. “Free CF” is free cash flow as defined in Lehn and Poulsen (1989) over total assets. “Leverage” is long-term debt over total assets. “R&D” is R&D expenditures over total assets. “Investment” is net investing cash flow over total assets. “Sales Impact” is firm sales over total industry sales. “Assets” is book value of assets. “Target” (“Acquirer”) indicates whether a firm is a target (an acquirer) during the year. “Insider Own” (“Block Own”, “Institutional Own”) is the percentage ownership of officers and directors (blockholders, institutional shareholders). “Abnormal Compensation” is excess CEO compensation from predicted value. “Industry Frequency” is the fraction of firms in an industry that donate in a year. Wilcoxon-Z statistics are reported for subsample comparisons. *** indicates significance at the 1% level.

Variables	Donating Sample	# of Obs.	Non-donating Sample	# of Obs.	Wilcoxon Z
Excess Return (EW)	0.028	5250	0.036	71442	-5.58***
Excess Return (VW)	0.003	5250	0.007	71442	-1.61
Book/Market	0.519	5403	0.698	72200	-21.04***
ROA	0.083	5423	0.003	72144	33.61***
Sales Growth	0.187	5309	0.226	66362	-0.98
Free CF	0.085	4749	-0.001	57563	19.95***
Leverage	0.224	5418	0.156	73098	34.23**
R&D	0.018	5389	0.042	72920	-11.35***
Investment	0.102	5179	0.095	64571	9.43***
Sales Impact	0.050	5464	0.004	72857	92.66***
Assets	16132	5499	862	74117	97.20***
Target	0.068	5499	0.053	84154	2.55**
Acquirer	0.213	5499	0.122	84154	28.40***
Insider Own	0.113	4088	0.207	52880	-34.16***
Block Own	0.285	4095	0.357	52957	-15.17***
Institutional Own	0.510	4094	0.284	52791	50.28***
Abnormal Compensation	0.028	3957	-0.008	12900	27.02***
Industry Frequency	0.189	5499	0.116	84154	46.67***

The daily stock returns for our calculations are from the Center for Research in Security Prices (CRSP). We use both the delisting information from the daily CRSP file and the Securities Data Company (SDC) Platinum database to identify companies that have been involved in mergers or acquisitions as either an acquirer or as a target. Ownership data (the fraction of shares owned by insiders, block holders, and institutions) comes from Compact Disclosure. The number of directors (board size) is calculated for all companies in our sample that are either covered by Compact Disclosure or by RiskMetrics. We construct an indicator variable that equals one if the Chief Executive Officer (CEO) is also the Chairman of the Board (CEO Chair) for all companies for which this information is available through either Compact Disclosure, RiskMetrics, or Execucomp. Based on its four-digit Standard Industrial Classification SIC code, we assign each company to one of the Fama-French 49 industries. This classification is used to control for industry effects and calculate each firm's sales impact, defined as the company's sales scaled by the sales of all companies in the same industry, and industry frequency, defined as the fraction of firms in an industry that donate.

Finally, each CEO's abnormal compensation is calculated as the deviation from predicted compensation based on firm size and industry median-adjusted prior stock and accounting performance. All other firm characteristics are obtained from the CRSP/Compustat merged database. Definitions and summary statistics are in Table 2. As is clear from the summary statistics, there are important differences between donating and non-donating firms. The key difference for our purposes is that the mean excess future return for soft money and 527 Committee donating firms is 2.8% while for non-donating firms, it is 3.6%.⁶ This difference is large, and we explore it throughout the rest of the paper.

3. Determinants of Corporate Political Donations

A. Why do Firms Chose to Donate?

Firms may donate for a variety of reasons. We focus on two important ones. First, donations may represent a form of investment in political capital. In this view, firms donate because they expect the recipients of the donations (national level politicians and/or committees associated with the national political parties) to reward the donations with favorable legislation. An example of this is Altria Group, the parent company of Phillip Morris—the largest corporate contributor in our sample—which presumably has an economic interest in discouraging

⁶ Excess returns are measured relative to the four-factor model, which we describe in Section 4. Excess returns for the whole sample are positive because of equal-weighting. Value-weighting yields mean excess returns of 30 and 70 basis points for donating and non-donating firms respectively. For both equal weight and value weight excess returns, medians are essentially 0.

increased tobacco and cigarette taxes as well as in limiting government regulation of tobacco products.

Second, donations may represent an agency problem. Corporate donations are largely unobservable to shareholders. While donations are disclosed to the government, they are not disclosed in firm financial statements, usually not discussed in board meetings, and generally small enough to evade shareholder scrutiny. If donations represent an agency problem, then they do not generate returns for shareholders. Instead, donations are a form of perquisites consumption for top managers. Managers may have personal preferences over candidates and parties they wish to support that are simply unrelated to the firm's activities.

To test this, we collected the individual political contributions of CEOs of the top 20 donating companies in our sample. Our data source for CEO contributions is www.campaignmoney.com. For each CEO we calculate the total contribution to the Democratic party ("ceodem_cycle") and to the Republican party ("ceorep_cycle") during each election cycle (2 years) in our sample. We compute the relative Republican index for each CEO in each election cycle as follows:

$$RelRep_CEO = (ceorep_cycle - ceodem_cycle) / (ceorep_cycle + ceodem_cycle)$$

We have 138 non-missing RelRep_CEO observations for the top 20 donating companies. We then compute the same measure for each company in each election cycle using the company's political contribution data. We find that the correlation between RelRep_CEO and RelRep_Firm is 0.75. We further define an indicator variable "Republican CEO" that equals one if RelRep_CEO > 0, and another indicator variable "Republican Firm" that equals one if RelRep_Firm > 0. We find that the correlation between "Republican CEO" and "Republican Firm" is 0.81. In summary, we find that a CEO's political orientation is highly correlated with the firm's political orientation. Of course, this evidence is only suggestive, as the CEO may donate personally in conjunction with the firm's interest.

In addition, donations may grant access to politicians. While such access could be valuable for the firm, it may also simply be a way for executives to demonstrate their own power and prestige. Such donations may pave the way for executives to be appointed to cabinet positions or ambassadorships. As an example, the CRP's "The Bush Administration Embassy Row" project lists 40 major ambassadorial picks who donated large amounts to the Bush campaigns and the Republican Party during the 2000, 2002, and 2004 election cycles. Among the 40 large-donor ambassadors, 33 were corporate CEOs, presidents or founders, or their immediate family members (e.g., wife). In some cases, such political appointments might be beneficial for the firm. In other cases, such appointments

may be simply neutral or even negative for the firm, as we expect for ambassadorial appointments for CEOs.

Even if donations represent an agency problem, it is difficult to identify the exact nature of the agency problem. Do donations represent perquisites consumption? Or, do they signify that top executives are busy attending to political issues that are peripheral to shareholders and therefore neglecting the firm? Perhaps donations simply reflect a propensity to squander excess cash. All of these are possibilities, but are hard to disentangle. Because we cannot directly identify the source of agency problems, we look for evidence that is consistent with the presence of agency problems in broader terms. We then examine whether agency problems or efficient investment better describe why firms make political donations.

B. Characteristics Associated with Donations

Our previous discussion makes clear that firms choose whether and how much to donate. What factors influence these decisions? In Table 3, we estimate donations as a function of a vector of firm characteristics as well as industry and year dummies. Year dummies are critical as Table 1 shows that donations are larger in even-numbered years, which correspond to national level elections, while industry dummies are also critical because of industry variation in donations.

As noted before, 93.9% of our firm-year observations are donations of 0. In Table 3, the first column displays the results from a probit specification where the dependent variable, donation dummy, takes a value of 1 if the firm donates in that year and 0 otherwise. The second column displays the results from a Tobit specification where the dependent variable is the logarithm of donations. All of the independent variables for these specifications are measured as of the year prior to the donating year. Throughout, we use robust standard errors clustered by firm. In general, the results are quite consistent.

Firms that donate and firms that donate more tend to have lower book-to-market ratios, more assets, lower sales growth, more free cash flow, less leverage, less R&D spending, and less investment (capital expenditure) spending (in the probit specification). This set of characteristics implies that firms that donate are larger, have more cash, and are growing more slowly. Interestingly, firms that donate more do not seem to spend this cash on R&D or physical capital as they invest less in R&D and physical assets than firms that donate less.

Table 3: Characteristics of Donating Firms

The table presents Probit and Tobit regression coefficients (not marginal effects) of corporate soft money and 527 Committee donations on firm characteristics. “Donation Dummy” equals one if a firm makes soft money or 527 Committee donations in that year and 0 otherwise. “Log(Donation Value)” is the logarithm of the dollar value of soft money and 527 Committee donations (in millions). All the independent variables are measured as of the year prior to the donating year. Robust standard errors clustered by firm are reported in brackets. ***, **, and * indicate significance at the 1%, 5%, and 10% levels, respectively.

	(1) Probit Donation Dummy	(2) Tobit Log(Donation Value)
Book/Market	-0.170*** (0.043)	-0.026*** (0.006)
ROA	-0.118 (0.351)	0.061 (0.052)
Sales Growth	-0.053 (0.038)	-0.006 (0.006)
Free CF	0.242** (0.125)	0.052* (0.028)
Leverage	-0.132 (0.124)	-0.026 (0.017)
R&D	-0.672 (0.471)	-0.103 (0.067)
Investment	-0.062 (0.105)	0.006 (0.015)
Sales Impact	2.221*** (0.808)	0.113** (0.051)
Log(Assets)	0.521*** (0.018)	0.073*** (0.004)
Target	-0.088** (0.036)	-0.018*** (0.005)
Acquirer	0.193*** (0.034)	0.020*** (0.005)
Ind. Donation Frequency	4.273*** (0.477)	0.384*** (0.076)
Constant	-5.735*** (0.257)	-0.797*** (0.051)
Industry & Year	Included	Included
Observations	50426	50426
Log pseudo-likelihood	-6582	-4885

This last finding is surprising in light of the fact that the firms that donate more have lower book-to-market ratios. If we think of the book-to-market ratio as the inverse of Tobin's Q or a proxy for growth opportunities, the firms that donate more should be investing more and yet they do not. While these results are suggestive, they are certainly not conclusive. These results could be consistent with the view that firms that donate have a free cash flow-based agency problem. On the other hand, these results could also be consistent with the view that these firms are investing in political capital rather than R&D or physical capital. Investments in political capital may lead to protection against competitors, the awarding of contracts or subsidies from the government.

Several other characteristics stand out as well. Firms that are large relative to their industries as measured by their fraction of industry sales (sales impact) donate more. Thus, size, both in absolute and relative terms to the industry, matters for donations. Firms in industries that have a high fraction of donors tend to donate more. Because many firms are participants in the market for corporate control during our sample period, we include both a target firm and an acquirer dummy in our specifications. Target firms are less likely to donate and donate less. Acquirers are more likely to donate and donate more.

In general, we conclude that larger firms with more free cash flow and less conventional investment spending tend to donate more. At this stage, we do not claim any causal relation between these characteristics and donations. However, these associations are sufficiently suggestive to question whether donations are investments that generate better returns or symptomatic of agency problems. We turn to this question in the next section.

4. Donations and Returns

The relation between donations and firm returns could be either positive or negative. If donations are investments, then we expect there to be a positive reduced-form relation between donations and returns. If donations are symptomatic of an agency problem, then we expect a negative reduced-form relation between donations and returns. The null hypothesis is that donations and stock returns are unrelated, either because there is no economic relation or because markets correctly and fully anticipate both donations and their impact on stock returns. We focus on one-year stock returns because corporate political donations are not disclosed in a transparent or timely fashion to shareholders, and are likely to be capitalized into stock prices only slowly over time.

To examine this question, we define our dependent variable, firm-level excess returns (XR), as one-year buy-and-hold returns minus the expected return. We use the four-factor model as our benchmark asset pricing model. We define the expected return for firm i as:

$$E(R_{it}) = r_{ft} + \beta_{1i}Market_t + \beta_{2i}SMB_t + \beta_{3i}HML_t + \beta_{4i}MOM_t$$

where r_{ft} is the risk-free rate. The coefficients on the factors are estimated separately for each firm based on the prior sixty months of returns and factors. The excess return is then:

$$XR_{it+1} = R_{it+1} - E(R_{it+1}).$$

We winsorize the excess returns at the top and bottom one percent. Next we regress excess returns on donations. The general form of our specification is:

$$XR_{it+1} = \alpha + \beta_1 Donation_{it} + \beta_2 (YearDummies) + \varepsilon_{it+1}.$$

The first column of Table 4, Panel A contains results from an Ordinary Least Squares (OLS) specification of returns on soft money and 527 Committee donations. Following Petersen (2009), we include year dummies and cluster the standard errors at the firm level. We find a negative and significant coefficient of -0.074 on donations.⁷ This coefficient implies that an incremental donation of \$10,000 would be associated with a negative 7.4 basis point excess return. This is not trivial. The median donating firm has a market value of equity of \$1.8 billion. The 7.4 basis point loss translates into a dollar loss of \$1.33 million associated with the \$10,000 soft money or 527 Committee donations.

The above result clearly suggests that more is lost than the simple dollar value of the donation. Instead, we view donations as providing us with a window into firm value destruction, similar to the result in Yermack (2006) that finds large negative returns associated with the CEOs' use of corporate aircrafts. We will more formally link value destruction to agency problems later in the paper. While the dollar loss is certainly surprising, it may also explain why 89% of publicly-traded firms do not donate directly from corporate funds—donations are associated with bad outcomes for shareholders.

⁷ One concern is that this result may be driven by specific years or only a small number of years. To address this, we perform cross-sectional regressions year-by-year and then use the Fama-Macbeth procedure to find time-series average coefficients and standard errors and find consistent results (not reported). In further robustness tests (unreported), we examine donations cumulated over two years and cumulative excess returns over the subsequent two years (e.g. a congressional election cycle), as well as donations cumulated over four years and cumulative excess returns over the subsequent four years (e.g. a presidential election cycle). The results are virtually identical. In other unreported tests, we replicate all of our results including both PAC donations and individual donations. The results are quite similar. Thus, whether we include or exclude PAC donations does not affect our results. This result is also robust to estimation using weighted least squares, where the weights are the market values of the firms, and also without winsorizing excess returns.

Because donations are substantially skewed, in all subsequent specifications based on the dollar value of donations, we use the logarithm of donations. To handle observations with no donations, we add one to each observation so that all observations with zero raw donations are represented by $\log(1) = 0$ in the transformed observations. The second column of Table 4, Panel A contains the results when we replace the dollar value of donations with $\log(\text{donations})$. The coefficient on $\log(\text{donations})$, -0.111 , gives us a similar interpretation to our previous result—a firm choosing to start donating \$10,000 would experience an 11.1 basis point reduction in excess returns.

Table 4: Relation between Donations and Future Excess Returns

Panel A: Four Factor Excess Returns

The dependent variable is a firm’s 12-month buy-and-hold excess return using the four-factor model from November 1 to the following October 31. Monthly excess returns are cumulated over the 12-month period. “Donation” (in millions) is a company’s annual soft money and 527 Committee donations, and “Log(Donation)” is equal to the logarithm of Donation + 1 to handle zero donation amounts. Robust standard errors clustered by firm are reported in brackets. ***, **, and * indicate significance at the 1%, 5%, and 10% levels, respectively.

	Four Factor Excess Return			
	(1)	(2)	(3)	(4)
	OLS	OLS	Selection Probit	Selection Tobit
Donation	-0.074*** (0.028)			
Log(Donation)		-0.111*** (0.040)		-0.120*** (0.046)
Donation Dummy			-0.051*** (0.013)	
λ			0.028*** (0.022)	0.010 (0.006)
Constant	0.032*** (0.009)	0.032*** (0.009)	0.007 (0.011)	0.004 (0.011)
Year Dummies	Included	Included	Included	Included
Observations	76692	76692	46497	46497
Adjusted R-squared	0.01	0.01	0.01	0.01

As noted in the previous section, the decision of whether and how much to donate is clearly endogenous. Our prior specifications do not take account of this potential endogeneity. Because most firms choose not to donate, our first concern is to address a firm's propensity to donate. Using the method of Li and Prabhala (2008), we estimate the following two-stage Heckman selection model:

$$D_{it}^* = \gamma Z_{it-1} + u_{it} ; D_{it} = 1 \text{ if } D_{it}^* > 0, \text{ and } D_{it} = 0 \text{ if } D_{it}^* \leq 0.$$

$$XR_{it+1} = \alpha + \beta_1 D_{it} + \beta_2 \lambda_i + \beta_3 (\text{YearDummies}) + \varepsilon_{it+1}.$$

The first equation is the probit selection equation. Z is a set of variables that are correlated with a firm's propensity to donate—in this case, all of the variables used in Table 3, Column 1. As we noted in Table 1B, there is a clear industry component to donations. Our selection equation thereby includes industry fixed effects. λ is the inverse Mills ratio computed from the selection equation. The second equation is the return regression including the donation dummy. The results of this specification are in the third column of Table 4. Correcting for a firm's propensity to donate (or the private information that leads the firm to donate), we estimate a negative and significant coefficient on the donation dummy of -0.051.⁸

While the probit-selection specification addresses a firm's propensity to donate, it does not take into account the information contained in how much a firm chooses to donate (and thus may overstate the effect of donations on returns). Following Li and Prabhala (2008), we estimate the following two-stage Heckman-style Tobit selection model:

$$D_{it}^* = \gamma Z_{it-1} + u_{it} ; D_{it} = \log(D_{it}^*) \text{ if } D_{it}^* > 0, \text{ and } D_{it} = 0 \text{ if } D_{it}^* \leq 0.$$

$$XR_{it+1} = \alpha + \beta_1 D_{it} + \beta_2 \lambda_i + \beta_3 (\text{YearDummies}) + \varepsilon_{it+1}.$$

The first equation is the Tobit selection equation in which Z is a set of variables that are correlated with the amount a firm donates (D_{it}^*). In this case, Z is all of the variables used in Table 3, Column 2. λ is the inverse Mills ratio computed from the selection equation. The second equation is the return regression including the amount of donations. The results from the second equation are in the fourth column of Panel A of Table 4. Correcting for the information in how much the firm chooses to donate, we estimate a negative and significant coefficient on donations of -0.120.

⁸ Note that this model and the following Tobit selection model are primarily identified through the “industry donation frequency” variable from the first stage regression.

As a further robustness check, we consider an alternative asset pricing model for our definition of excess returns. Daniel, Grinblatt, Titman, and Wermers (1997) [DGTW] form 125 benchmark portfolios based on market capitalization, book-to-market, and prior year stock return characteristics. Excess returns for each firm i are the difference between raw returns and the DGTW benchmark portfolio return:

$$XR_{it+1} = R_{it+1} - R_{pt+1}.$$

Table 4: Relation between Donations and Future Excess Returns

Panel B: DGTW Excess Returns

The dependent variable, excess return, is a firm’s one-year buy-and-hold return minus the corresponding DGTW benchmark portfolio return. Monthly excess returns are cumulated over the 12-month period. The three models are those from Panel A. Robust standard errors clustered by firm are reported in brackets. ***, **, and * indicate significance at the 1%, 5%, and 10% levels, respectively.

	DGTW Excess Return		
	(1)	(2)	(3)
	OLS	Selection Probit	Selection Tobit
Log(Donation)	-0.060** (0.026)		-0.068* (0.041)
Donation Dummy		-0.039*** (0.013)	
λ		0.021** (0.008)	0.004 (0.005)
Constant	0.053*** (0.013)	0.032** (0.014)	0.030** (0.014)
Year Dummies	Included	Included	Included
Observations	54445	39579	39579
Adjusted R-squared	0.002	0.01	0.01

The results for the OLS and selection models using DGTW excess returns are in Panel B of Table 4. The results are similar, although the coefficients are somewhat smaller in magnitude and less significant. Thus, we do not take a stand on whether factors or characteristics are relevant for asset pricing and simply note that our results are robust to the choice of asset pricing model.

In Panel C of Table 4, we consider other specifications to further demonstrate the robustness of our results. One possible objection is that donations matter for returns only for specific industries, such as regulated industries. To address this, we first add industry fixed effects to the OLS specification using the four-factor model for excess returns in the first column of Panel C of Table 4. Our results are unaffected. Second, if donations matter only for industries with a high level of aggregate donations, then industry fixed effects may be insufficient to isolate an effect of donations on returns. The second column restricts our sample to the five largest donating industries and the results are again similar.⁹

Table 4: Relation between Donations and Future Excess Returns

Panel C: Additional Regression Specifications

The dependent variable, excess return, is computed based on the four-factor model. “Donation” (in millions) is a company’s annual soft money and 527 Committee donations. We add one to all donation observations before taking the logarithm. Robust standard errors clustered by firm are reported in brackets. ***, **, and * indicate significance at the 1%, 5%, and 10% levels, respectively.

	(1) OLS (w/ industry dummies)	(2) OLS (top 5 donating industries only)	(3) OLS	(4) OLS (donating sample only)	(5) IV
Log(Donation)	-0.100** (0.040)	-0.098** (0.048)			
Donation			-0.087** (0.038)		
(Donation) ²			0.009 (0.017)		
Log(Donation) (0 < Donation < Median)				1.243 (2.083)	
Log(Donation) (Donation ≥ Median)				-0.096** (0.049)	
ExpDonation					-0.046** (0.023)
Constant	0.017 (0.050)	-0.007 (0.014)	0.032*** (0.009)	0.051 (0.032)	0.024** (0.010)
Year Dummies	Included	Included	Included	Included	Included
Industry Dummies	Included				
Observations	76692	20072	76692	5250	22588
Adjusted R-squared	0.01	0.02	0.01	0.01	0.01

⁹ In unreported results, we examine the relationship between donations and returns industry-by-industry. Out of the 49 Fama-French industries, 37 show a negative relation between donations and returns, including all five of the largest industries by dollar value of donations. Of the 37 industries with negative coefficients, 20 are statistically significant. In none of the industries with positive coefficients are the coefficients statistically significant.

Another possibility is that the returns to donations show nonlinear or non-monotonic effects. In particular, large donations may yield positive returns while small donations do not. Such an effect would be consistent with the fact that Altria (formerly Phillip Morris) is the largest donor in our sample, presumably seeking to forestall adverse tobacco legislation (although Altria also generates large free cash flows). To examine this possibility, we consider two nonlinear specifications in columns 3 and 4.

The third column reports results from an OLS specification of excess returns based on the four-factor model that includes both donations and donations squared. The coefficient on donations, -0.087, is negative and significant, while the coefficient on donations squared, 0.009, is positive and insignificant. This is weak evidence in support of a U-shaped relation between donations and returns. The inflection point occurs at donations of \$4.7 million, so that only companies donating more than \$4.7 million in a single year begin to see an increase in returns for their marginal dollar donated. In our sample, there is only one such firm-year observation, suggesting that donations are unlikely to be a positive investment through virtually the entire distribution of our sample.

The fourth column reports results from a spline specification, in which we estimate coefficients on two segments—donations below and above the median value of donations in the sample. We find a positive and insignificant coefficient on the segment below the median value of donations, while a negative and significant coefficient above the median value. These results are consistent with our previous findings.

Our results thus far suggest a negative relation between donations and excess returns. However, this relation need not be causal and donations may be endogenous. To ascertain causality, we instrument for the firm's level of donations. The specification in the fifth column of Panel C of Table 4 is:

$$\begin{aligned} \text{Log}(\text{Donation}_{it}) &= \delta_1 X_{it-1} + v_{it}; \\ XR_{it+1} &= \alpha + \beta_1 \hat{D}on_{it} + \beta_2 (\text{YearDummies}) + \varepsilon_{it+1}, \end{aligned}$$

in which $\hat{D}on_{it} = \hat{\delta}_1 X_{it-1}$. The first stage regression is used to predict the logarithm of donations. The instrument X in the first stage regression is the logarithm of a firm's soft money political donations for the year 1992. The dependent variable is the logarithm of the firm's soft money and 527 Committee donations where the dependent variable is measured from 1996 to 2004. In effect, we are using lagged donations as our instrument, but the lag length increases from four years for 1996 donations to twelve years for 2004 donations. The second stage regression is the excess return regression, where expected donations are measured in the year prior to the excess returns. The donation instrument is measured at least four years prior to the donation year and so, it is measured at

least five years prior to the excess returns. Donations from at least five years prior are unlikely to be correlated with current excess returns except through what they tell us about a firm's propensity to donate. Statistically, instrument X is uncorrelated with the error term in the excess return regressions, but is positively correlated with current donations.¹⁰ Thus, we have plausible exogenous variation related to donations but unrelated to future excess returns. The fifth column restricts the excess return regression to those firms that have non-missing excess returns from 1996 to 2004. The coefficient estimate for expected (instrumented) donations is -0.046 and is statistically significant. These results imply that exogenous variation in donations is associated with negative excess returns.

In a recent paper, Cooper, Gulen and Ovtchinnikov (2010) examine firm-level PAC donations to US political campaigns from 1979 to 2004 and report that the number of politicians to whom a firm donates is positively correlated with future stock returns. Aside from differences in data, there are three important differences between our paper and their findings. Their primary variable is how many different candidates a firm has supported over the previous five years, not the dollar value of donations. We focus on the dollar value a firm has given in the aggregate. If donations are an investment, then the dollar value of donations seems to be the more appropriate measure of investing in political capital.

Second, we focus on soft money and 527 Committee donations while they focus on PAC donations. As mentioned previously, PAC donations come from individuals associated with the firm, not directly from the firm's funds. Because individuals can direct how they would like the PAC to give the money that they have donated, PAC donations cannot be attributed directly to the firm's or its managers' preferences. This makes inference from PAC donations challenging.

The third difference is how they specify their asset pricing tests. In their primary return specifications, they use three lagged firm-specific characteristics— $\ln(\text{book-to-market})$, $\ln(\text{market value of equity})$, and 12-month buy-and-hold returns—that correspond to the DGTW benchmark portfolios we use in Panel B of Table 4. While our focus is not on the best way to perform asset pricing tests, we note that this difference in specification partially explains the differences in results, as our results using the DGTW benchmark portfolios are somewhat weaker than our results using the four-factor model. Nevertheless, our results are robust to the characteristic-based asset pricing approach used in Cooper, Gulen and Ovtchinnikov (2010).

Our specifications in Table 4, coupled with the results from the previous section, suggest that donations are symptomatic of an agency problem. Larger firms with more free cash flow, and less R&D and investment spending donate more. Firms that donate have lower excess returns. Further, the more a firm

¹⁰ Tests of the validity of the instrument and the exclusion restriction are available upon request.

donates, the lower the excess returns. These results seem less consistent with the political capital hypothesis and more supportive of the agency problem hypothesis. However, the evidence thus far is indirect. In the next section, we turn to more direct tests of the agency hypothesis.

5. Donations and Agency Problems

A. Corporate Governance

In order to examine whether donations could be reflective of agency problems, we ask whether mechanisms thought to constrain or exacerbate agency problems influence donations and subsequently, excess returns. Our perspective thus far is that firms with agency problems could see them manifested as having excess free cash flow leading to high levels of donations. The agency problems then lead to poor future excess returns. The donations do not cause the agency problems but are symptomatic of them.

Various corporate governance variables have been shown to exacerbate or mitigate agency problems. For example, Yermack (1996) argues that firms with large board of directors seem to be ineffective in constraining agency problems. Thus, we include board size as a measure of board effectiveness. Morck, Shleifer and Vishny (1989) argue that CEOs who are also chairman of the board are entrenched and therefore better able to engage or indulge in agency behavior. We include a dummy variable if the CEO is also chairman of the board. Abnormally high CEO compensation (defined as compensation minus predicted compensation based on firm size and industry median adjusted prior stock and accounting performance) is thought to be a contemporaneous indicator of agency problems.¹¹ In addition, three ownership variables are thought to potentially constrain agency behavior. Greater insider ownership provides direct incentives for managers not to engage in agency behavior, as well as being reflective of better managers.¹² Greater block and institutional ownerships are thought to limit agency behavior as block and institutional owners are more likely to be effective monitors.¹³

To see whether these mechanisms influence donations, we augment our donation specification from Table 3 with each of the agency-controlling or agency-associated mechanisms. The results are in Panel A of Table 5. The dependent variable is the logarithm of the dollar value of soft money and 527 Committee donations. Each column adds one of the agency-controlling mechanisms to the original set of covariates *Z*. The last column includes all mechanisms simultaneously. Because each mechanism comes from a different

¹¹ See for example, Hartzell, Ofek and Yermack (2004), and Bebchuk and Fried (2004).

¹² Hadlock (1998); Milbourn (2003); and Aggarwal and Samwick (2006).

¹³ Holderness (2003).

data source, we have differing numbers of observations across the columns and also relative to Table 3.

Table 5: Corporate Governance and Corporate Political Donations

Panel A: Governance Characteristics and Donations

This table reports OLS regressions of the logarithm of soft money and 527 Committee donations (in millions) on governance characteristics and control variables. We add one to zero donation observations before taking the logarithm. Robust standard errors clustered by firm are reported in brackets. ***, **, and * indicate significance at the 1%, 5%, and 10% levels, respectively. All regressions include industry and year dummies.

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Board Size	0.001*** (0.000)						0.002** (0.001)
CEO Chair		0.003*** (0.001)					0.004** (0.002)
Abnormal Compensation			0.057** (0.024)				0.045 (0.028)
Insider Own				-0.0002 (0.001)			-0.004 (0.007)
Block Own					-0.007*** (0.001)		0.008 (0.006)
Institutional Own						-0.023*** (0.003)	-0.039*** (0.008)
Book/Market	-0.002*** (0.000)	-0.002*** (0.001)	-0.005** (0.003)	-0.002*** (0.000)	-0.002*** (0.000)	-0.003*** (0.000)	-0.005* (0.003)
ROA	0.007 (0.008)	0.008 (0.009)	0.031 (0.026)	0.003 (0.007)	0.003 (0.007)	0.006 (0.007)	0.038 (0.030)
Sales Growth	-0.002** (0.001)	-0.001 (0.001)	0.003 (0.003)	-0.001*** (0.000)	-0.001*** (0.000)	-0.002*** (0.000)	-0.001 (0.003)
Free CF	0.018*** (0.006)	0.022*** (0.008)	0.039* (0.022)	0.014*** (0.005)	0.014*** (0.005)	0.014*** (0.005)	0.039 (0.025)
Leverage	-0.015*** (0.003)	-0.019*** (0.003)	-0.027*** (0.008)	-0.012*** (0.002)	-0.012*** (0.002)	-0.015*** (0.003)	-0.030*** (0.011)
R&D	-0.005 (0.005)	-0.005 (0.005)	0.027 (0.020)	-0.007* (0.004)	-0.008** (0.004)	-0.001 (0.004)	0.044 (0.027)
Investment	-0.001 (0.002)	-0.001 (0.003)	0.010 (0.006)	-0.002 (0.002)	-0.002 (0.002)	0.001 (0.002)	0.013 (0.009)
Sales Impact	0.292*** (0.045)	0.323*** (0.054)	0.200*** (0.063)	0.258*** (0.043)	0.254*** (0.043)	0.237*** (0.043)	0.119** (0.056)
Log(Assets)	0.006*** (0.001)	0.008*** (0.001)	0.016*** (0.002)	0.006*** (0.001)	0.006*** (0.001)	0.008*** (0.001)	0.018*** (0.002)
Target	-0.003*** (0.001)	-0.004*** (0.001)	-0.004* (0.002)	-0.002*** (0.001)	-0.002*** (0.001)	-0.002*** (0.001)	-0.006** (0.003)
Acquirer	0.002** (0.001)	0.000 (0.001)	0.001 (0.002)	0.001 (0.001)	0.001 (0.001)	0.001* (0.001)	0.001 (0.003)
Ind. Donation Frequency	0.052*** (0.020)	0.060** (0.028)	0.073 (0.048)	0.026 (0.020)	0.025 (0.020)	0.024 (0.019)	0.044 (0.044)
Constant	-0.052*** (0.006)	-0.056*** (0.007)	-0.126*** (0.014)	-0.034*** (0.004)	-0.031*** (0.004)	-0.036*** (0.004)	-0.133*** (0.016)
Observations	24515	28433	13565	37094	37183	37051	7658
R-squared	0.177	0.216	0.262	0.169	0.171	0.179	0.252

Table 5: Corporate Governance and Corporate Political Donations

Panel B: Excess Return Regressions

The dependent variable in all regressions is the excess return based on the four-factor model. “Donation” (in millions) is a company’s annual soft money and 527 Committee donations. We add one to all donation observations before taking the logarithm. Robust standard errors clustered by firm are reported in brackets. ***, **, and * indicate significance at the 1%, 5%, and 10% levels, respectively.

	(1) OLS	(2) Selection Probit	(3) Selection Tobit
Log (Donation)	-0.136*** (0.049)		-0.178*** (0.056)
Donation Dummy		-0.082 *** (0.028)	
λ		0.050*** (0.020)	0.012 (0.010)
Board Size	-0.012*** (0.002)	-0.010*** (0.003)	-0.013*** (0.003)
CEO Chair	0.014 (0.012)	0.008 (0.014)	0.006 (0.014)
Abnormal Compensation	-0.044 (0.059)	0.013 (0.059)	-0.001 (0.059)
Insider Own	0.036 (0.048)	0.048 (0.053)	0.049 (0.054)
Block Own	-0.001 (0.027)	-0.018 (0.032)	-0.007 (0.031)
Institutional Own	-0.152*** (0.031)	-0.146*** (0.035)	-0.153*** (0.035)
Constant	0.204*** (0.036)	0.212*** (0.043)	0.224*** (0.043)
Year Dummies	Included	Included	Included
Observations	9448	7268	7268
R-squared	0.03	0.03	0.03

The results are consistent with the agency hypothesis. Larger boards are associated with larger donations. Firms in which the CEO is also the chairman of the board have larger donations. Higher abnormal CEO compensation is associated with larger donations. Firms in which there is greater insider ownership have smaller donations in Column 4, although this relation is insignificant. Firms in which there is large block ownership have smaller donations. Firms in which there is large institutional ownership have smaller donations. In Column 7, which

includes all agency variables at once, the results are largely consistent, although only three variables - board size, whether the CEO is a chairman, and institutional ownership - continue to be statistically significant. Thus, to the extent that these corporate governance variables either exacerbate or control agency problems, they also seem to have the same effect on donations.

It is also worth examining what impact these variables have on the relation between donations and returns. One possibility is that while donations may be reflective of an agency problem, this effect is entirely subsumed by corporate governance so that corporate governance variables are omitted factors in the return-donation regressions. In Panel B of Table 5, we modify the OLS and selection specifications from Panel A of Table 4. We add the six corporate governance variables (board size, CEO Chair, abnormal compensation, insider ownership, block ownership, and institutional ownership) to the excess return regression (for the selection specification, this is the second stage regression).

In all three specifications, the coefficient on the logarithm of soft money and 527 Committee donations is negative and significant (-0.136, -0.082, -0.178 respectively) and larger in absolute value than the analogous specifications in Panel A of Table 4. Due to the inclusion of the governance variables, the number of observations is greatly reduced relative to the return specifications in Panel A of Table 4. Once we control for governance, the negative relation between donations and returns is exacerbated. This suggests that corporate governance variables constrain agency problems and attenuate the negative donation-return relation. There are two potential interpretations of this. First, there are aspects of agency that are not captured by our governance variables and so, agency problems that result in donations go beyond governance control. Second, once we control for aspects of governance (which ameliorate or exacerbate agency problems) in our specifications, the negative donation-return relation is driven by something other than agency. We return to this possibility in Section 6.

For now, we note that the two findings in this section—the positive correlation between governance variables that exacerbate agency problems and donations, and the negative correlation between governance variables that control agency problems and donations, coupled with the increase in the magnitude of the coefficient on donations in return-donation regressions that include governance variables—are supportive of the agency hypothesis.¹⁴

¹⁴ In unreported results, we have also examined the effect of greater disclosure (transparency) of political donations. We find that firms with greater disclosure of political donations have less negative donation-return relations, suggesting that greater transparency attenuates the negative effects of donations.

B. Mergers and Acquisitions

Next, we examine the effect of corporate political donations on mergers and acquisitions. Mergers and acquisitions are thought to be especially fraught with agency problems.¹⁵ Table 2 shows that donating firms are unconditionally more likely to be both acquirers and targets than are non-donating firms. Table 3 shows a strong positive association between donations and whether a firm is an acquirer after controlling for many other firm characteristics. Such an association is consistent with both donations and acquisitions being manifestations of agency problems.

To explore this, we ask whether acquisitions following political donations are more likely to be bad for shareholders by examining cumulative abnormal returns (CAR) around acquisition announcements for donating acquirers versus non-donating acquirers. As a univariate comparison, the CAR from one day before to one day after announcement is on average -2.6 basis points (median = -0.2 basis points) for donating acquirers, while it is on average 158 basis points (median = 56 basis points) for non-donating acquirers. The difference between donating acquirers and non-donating acquirers is statistically significant.

In Table 6, we present two regression specifications to control for other factors that influence acquisition announcement returns. The first specification controls for deal characteristics, while the second specification also controls for acquirer characteristics. In both specifications, the CAR is significantly lower for acquirers that made a donation in the year of or the year prior to the acquisition announcement. In Column 2, a donating acquirer's CAR is 66.1 basis points lower than a non-donating acquirer's, controlling for firm and deal characteristics. Hence, it appears that donating firms make worse acquisitions than do non-donating firms. This finding is once again, consistent with the agency explanation.

¹⁵ See for example, Gompers, Ishii and Metrick (2003).

Table 6: Donations and Acquirer Returns

This table reports OLS regressions of acquisition announcement returns (in percent), CAR [-1,+1], on a donation dummy that equals one if the firm made soft money or 527 Committee donations to politicians in the year of, or the year before, the acquisition announcement. “Tobin’s Q” is market value of assets divided by book value of assets. “Deal Size” is the ratio of deal value over the acquirer’s market capitalization averaged across the transactions by the same acquirer in a year. Observations with Deal Size less than 1% are excluded. “Public Target” is the fraction of transactions in a year in which the target is a publicly traded company. “% of Stock” is the fraction of transaction value paid with stock averaged across transactions by the same acquirer in a year. “Cash Ratio” is the firm’s ratio of cash to total assets. Robust standard errors are reported in brackets. ***, **, and * indicate significance at the 1%, 5%, and 10% levels, respectively.

	(1)	(2)
Donation Dummy	-0.946*** (0.256)	-0.661*** (0.251)
Deal Size	0.520 (0.352)	0.655* (0.384)
Public Target	-3.470*** (0.288)	-3.532*** (0.283)
% of Stock	-0.624* (0.325)	-0.355 (0.326)
Tobin’s Q		-0.437*** (0.102)
Cash Ratio		1.179 (0.921)
Log(Assets)		-0.001** (0.0005)
Constant	2.398*** (0.167)	2.954*** (0.235)
Observations	6949	6653
Adjusted R-squared	0.03	0.04

6. Donations as an Investment

A. Is donating to the election’s winner an investment?

Using event studies around election outcomes, previous research finds that donating to the winning party is associated with positive stock price reactions while donating to the losing party is associated with negative stock price

reactions. An alternative explanation is that the negative returns we document may simply be an outgrowth of losing political bets made over the period we study. Had firms bet on political winners, then they would have enjoyed positive returns on their investments in political capital.

To explore this possibility, we separate years into three categories — years with a presidential election (e.g., years evenly divisible by four), years with a congressional election only (e.g., years evenly divisible by two but not by four), and non-election years (e.g., odd-numbered years). For the two categories of election years, we define a dummy variable “Win” as follows. In a presidential election year, if donations by a firm to the party that wins the presidency exceed 50% of total donations, then Win = 1 for that firm, and 0 otherwise. In a congressional election year, if donations by a firm to the party that wins net seats (e.g., the party’s total seats in Congress increase) exceed 50% of total donations, then Win = 1 for that firm, and 0 otherwise. Win is not defined for non-election years.

To explore this, we ask whether acquisitions following political donations are more likely to be bad for shareholders by examining cumulative abnormal returns (CAR) around acquisition announcements for donating acquirers versus non-donating acquirers. As a univariate comparison, the CAR from one day before to one day after announcement is on average -2.6 basis points (median = -0.2 basis points) for donating acquirers, while it is on average 158 basis points (median = 56 basis points) for non-donating acquirers. The difference between donating acquirers and non-donating acquirers is statistically significant.

In Panel A of Table 7 we report several specifications to examine the possibility that what matters for donations as investments is donating to the winning party. In Columns 1, 3, and 5, we regress excess returns on the logarithm of soft money and 527 Committee donations for presidential election years, congressional election years, and non-election years, respectively. The relation between donations and excess returns is negative in all three cases, although insignificant for presidential election years. These results are consistent with our results from Table 4.

In Columns 2 and 4, we add an interaction between donations and Win for presidential and congressional election years. The investment hypothesis predicts that the effect of donations should be insignificant, while the interaction of donations and Win should be positive and significant. For presidential elections, the coefficient on donations is negative and insignificant, and the coefficient on the interaction is positive and insignificant and smaller in absolute value than the coefficient on donations. For congressional elections, the coefficient on the interaction is positive but insignificant, while the coefficient on donations is negative, large in magnitude, and significant. Donating leads to large negative returns, while donating to the winning party does not offset the negative returns to

donating. For one-year excess returns there is no support for the hypothesis that donating to the winning party leads to better returns. Importantly, the agency hypothesis predicts that the coefficient on donations should be negative in these specifications and that the coefficient on the interaction terms should be insignificant, as mirrored in the finds.

Table 7: Returns to Donation: Variation across Elections

Panel A: Future Excess Returns

This Panel shows future one-year excess returns computed based on the four-factor model: the three Fama-French factors and the momentum factor. Panel B has cumulative abnormal returns where “CAR [-1, +1]” is the market-adjusted election announcement return from day 1 to day 2 after election day. “Donation” is the dollar amount of soft money and 527 Committee donations (in millions). “Log(Donation) to Winner” is the logarithm of the firm’s donation if and only if more than 50% of the firm’s soft money donation goes to the winning party, and zero otherwise. For a congressional election, the winning party is defined as the party that gains seats in the congress (the Senate and the House). Robust standard errors clustered by firm are reported in brackets. ***, **, and * indicate significance at 1%, 5%, and 10% levels, respectively.

	Future Excess Return				
	Presidential		Congressional		No Election
	(1)	(2)	(3)	(4)	(5)
Log(Donation)	-0.049 (0.070)	-0.103 (0.098)	-0.294*** (0.052)	-0.326*** (0.093)	-0.167** (0.054)
Log(Donation) to Winner		0.096 (0.114)		0.051 (0.108)	
Constant	0.026*** (0.007)	0.026 (0.007)	0.116*** (0.009)	0.116*** (0.009)	0.048*** (0.011)
Year Dummies	Included	Included	Included	Included	Included
Observations	21220	21220	17058	17058	38414
R-squared	0.01	0.01	0.01	0.01	0.01

As an additional robustness test, we replicate the results from the event study literature mentioned before. In Panel B of Table 7, we examine cumulative abnormal returns from one day before to one day after presidential and congressional elections. Consistent with the event study literature that focuses on presidential elections, we find in Columns 1 and 2 that donations are positively associated with one-day returns in presidential elections and that this effect comes entirely from donating to winners. Conversely, for congressional elections, donations are negatively associated with one-day returns. This negative

association is primarily driven by donations to the losing party, where donations to the winning party offset the negative coefficient on donations. We can therefore reconcile our results with those in the event study literature—examining only presidential elections provides an incomplete picture of the relation between donations and returns. For one-day returns, there are positive returns from donations to the winning party in presidential and congressional elections, but there are negative returns from donations to the losing party in congressional elections.

Table 7: Returns to Donation: Variation across Elections

Panel B: Election Announcement Returns

This Panel shows cumulative abnormal returns where “CAR [-1, +1]” is the market-adjusted election announcement return from day 1 to day 2 after election day. “Donation” is the dollar amount of soft money and 527 Committee donations (in millions). “Log(Donation) to Winner” is the logarithm of the firm’s donation if and only if more than 50% of the firm’s soft money donation goes to the winning party, and zero otherwise. For a congressional election, the winning party is defined as the party that gains seats in the congress. Robust standard errors clustered by firm are reported in brackets. ***, **, and * indicate significance at 1%, 5%, and 10% levels.

	Election Announcement CAR[-1, +1]			
	Presidential		Congressional	
	(1)	(2)	(3)	(4)
Log(Donation)	0.019*** (0.006)	0.007 (0.007)	-0.004 (0.006)	-0.019*** (0.008)
Log(Donation) to Winner		0.021*** (0.010)		0.022** (0.011)
Constant	-0.004*** (0.001)	-0.004*** (0.001)	0.006*** (0.001)	0.006*** (0.001)
Observations	22390	22390	18061	18061
R-squared	0.01	0.01	0.01	0.01

In sum, these results for one-year and one-day returns suggest that donating to the winning party in presidential election years has transient positive effects. This transient positive effect does not persist to the one-year horizon. Furthermore, to the extent that donating to the winning party in congressional elections offsets the negative effect of donations, this effect is also transient. At the one-year horizon, the positive effects of donations to winners entirely disappear. Other than for one-day returns when donating in presidential elections, the primary effect of donations on returns is negative. In most cases, not donating dominates donating, even if donating to the winning party.

B. Are donations a reward to politicians for past political favors?

Our tests assume that firms first donate and then politicians respond with either favors for firms or managers. The operating assumption is that favors for firms should be reflected in stock returns. Another possibility is that politicians do favors for firms and then the firms donate to the politicians. To the extent that firm returns increase as a result of favors, we would miss the returns that occur prior to the donations. A backward-looking approach to donations, in which favors and returns occur prior to donations, would not be captured in our previous specifications. While Table 2 shows that excess returns in the year prior to the donation are lower for donors versus non-donors, this does not fully resolve the issue. While we cannot identify past political favors to firms, we can examine this issue indirectly by focusing on a set of firms for which it is unlikely that donations are a reward for past political favors.

We examine firms that initiate donations concurrent with or immediately subsequent to a change in political control. To see the rationale for this test, consider the 1994 House and Senate elections. In that election, the Republican Party gained control of both the House and Senate. Now consider donors who started donating in 1994 or 1995 and gave the majority of their donations to Republican candidates. Prior to 1994, the Republican party was not in power. So, these donations were unlikely a reward for past political favors. Conversely, after 1994, the Republicans were well-positioned to provide favors on a going-forward basis. So, when political control changes, are the returns for the firms that initiate donations to the winning party positive (returns to investment) or negative (no returns to investment)?

We examine five specific events that correspond to all federal level changes of control during our sample. First, as described above, we examine firms that initiate donations in 1994 or 1995 and give the majority of their donations to the Republican candidates for House and Senate elections. This corresponds to the Republican party winning majority seats in Congress in 1994. Second, we examine firms that initiate donations in 2001 and give the majority of their donations to the Democratic candidates in Senate elections. This corresponds to the disassociation of Senator James Jeffords from the Republican Party to becoming independent and subsequently voting for Democratic control of the Senate. Third, we examine firms that initiate donations in 2002 or 2003 and give the majority of their donations to the Republican candidates for Senate elections. This corresponds to the Republicans winning majority Senate control in 2002. Fourth, we examine firms that initiate donations in 1992 or 1993 and give the majority of their donations to the Democratic presidential candidates (Bill Clinton and all of his Democratic primary opponents). This corresponds to President Clinton winning the presidency in 1992. Fifth, we examine firms that initiate

donations in 2000 or 2001 and give the majority of their donations to the Republican candidates for president (George W. Bush and all of his Republican primary opponents). This corresponds to President Bush winning the presidency in 2000. We assign a treatment dummy equal to one for all firm-year observations that meet the above criteria.

Table 8: Are Donations a Response to Past Political Favors?

Panel A: Summary Statistics

The “Treatment Dummy” is an indicator that equals one if a firm initiates soft money or 527 Committee donations, and gives more than 50% of its soft money and 527 Committee donations to the political party that enters power in that year.

	Mean Excess Return	# of Observations
Treatment group	-0.024	176
Donation initiators not in the treatment group	-0.010	270
Non-initiating Donors	0.031	4804
Non-donors	0.036	71442

Panel B: Regression Results

The dependent variable in each regression is the future excess return. “Donation” is the dollar amount of soft money and 527 Committee donations (in millions). Robust standard errors clustered by firm are reported in brackets. ***, **, and * indicate significance at the 1%, 5%, and 10% levels, respectively.

	(1)	(2)
Treatment Dummy	-0.102** (0.041)	-0.099** (0.041)
Log(Donation)		-0.107*** (0.040)
Constant	0.031** (0.009)	0.032*** (0.009)
Year Dummies	Included	Included
Observations	76692	76692
R-squared	0.01	0.01

Table 8, Panel A provides summary statistics for the treatment and several other groups. Mean excess annual returns relative to the four-factor model for the treatment group are -24 basis points and there are 176 firm-year observations that meet the criteria above. We also report mean excess returns for firms that initiated donations in the treatment years, but gave the majority of their donations to the other political party. In addition, we have mean excess returns for firms that had

previously donated and mean excess returns to non-donors. In all cases, the excess returns are for the year following the donations. Excess returns for first-time donors to a party that wins control are *lower* than excess returns for first-time donors to the losing party, which in turn are lower than excess returns to existing donors. Excess returns to all categories of donors are lower than excess returns for non-donors. These results are exactly the opposite of what we would expect if donations were an investment in political capital.

Table 8, Panel B, demonstrates these results in a regression. The negative and significant coefficient on the treatment dummy in Column 1 shows that excess returns are lower for firms that initiate donations to the party that wins control. For these firms, it is implausible that their donations are in response to past political favors, since the party to which they donate was not in power. When we add the logarithm of donations in Column 2, we find—consistent with our previous results—that donations are negatively associated with future excess returns. In addition, excess returns are still lower for firms that initiate donations to the party that wins control, suggesting that these donations are unlikely to be an investment in political capital. In light of our agency results before, it is more plausible that political donations are seeking favors for managers rather than firms.

C. Would returns be worse without donations?

While the evidence is consistent with the agency hypothesis, it is possible donations do represent a positive net present value investment for some firms. Because we do not observe the state of the world in which donating firms do not donate, we cannot tell if the relation between donations and returns is causal. If the firms had not donated, it is possible that their returns would have been even worse.

To address this possibility, we utilize the propensity matching method. In the first stage, we run the Probit regression as in Table 3, Column 1, to obtain the predicted probability of a firm being a soft money and 527 Committee donor. This Probit model includes firm-specific characteristics (firm size, return on assets, the book-to-market ratio, sales growth, free cash flow, leverage, etc.) as well as industry and time effects that are related to corporate political donations. We generate the predicted propensity to donate, *PSCORE*, for each firm-year in the sample. *PSCORE* summarizes the cost-benefit tradeoff of donating for a firm in a specific year based on the firm's characteristics.

Table 9: Matching on Propensity to Donate

We run the Probit regression in Table 3, Column 1, to obtain the predicted probability of a firm being a soft money and/or 527 Committee donor. We generate the predicted propensity to donate, *PSCORE*, for each firm in the sample. For each donating firm in each year, we find the non-donating firm with the closest *PSCORE* in the same year. Panel A shows the summary statistics of *PSCORE* across the donating firms and the matched non-donating firms. Panel B shows the summary statistics of four factor excess returns across the two groups of firms.

	<i>Panel A: Summary Statistics of Propensity to Donate</i>		<i>Panel B: Summary Statistics of Excess Returns</i>	
	<i>PSCORE</i>		Four Factor Excess Return	
	Donating Firms	Matched Non-donating Firms	Donating Firms	Matched Non-donating Firms
Mean	0.471	0.472	0.036	0.064
Median	0.468	0.469	-0.026	0.0003
Std. Dev.	0.293	0.293	0.531	0.467
Observations	3870	3870	3870	3870
	T-test for equality of <i>PSCORE</i> : p-value=0.91 Wilcoxon Z-test for equality of <i>PSCORE</i> : p-value=0.89		T-test for equality of excess returns: p-value=0.003 Wilcoxon Z-test for equality of excess returns: p-value=0.0006	

Each year, for all individual donating firms, we find the non-donating firms with the closest *PSCORE* in the same year, excluding firm-year observations with *PSCOREs* falling outside the common range across the two samples. This means that we find a matching firm that was subject to a very similar cost-benefit tradeoff of donating, but chose not to donate. Thus, the matching firm serves as the counterfactual. The matching process generates 3,870 firm-year observations of donating firms and 3,870 firm-year observations of propensity-matched, non-donating firms. Table 9, Panel A shows the summary statistics of *PSCORE* across the donating firms and the matched non-donating firms. The distributions are similar.

In the final stage, we compare the excess returns of the two samples. Table 9, Panel B shows that donating firms on average experience an excess return that is 2.8% lower than the propensity-matched non-donating firms' excess return. The median excess return for the donating sample is -2.63% lower than the propensity-matched, non-donating firms. Both the T-test and Wilcoxon Z-test show that the difference between the two samples is statistically significant. This result suggests that firms that make soft money and 527 Committee donations

tend to substantially underperform relative to similar firms that do not engage in such activity. To the extent that firm characteristics accurately summarize the cost-benefit tradeoff of donating, these results mitigate the concern that donating firms would have performed even worse had they not donated.

D. Donations and government contracts

As another test, we examine the relationship between donations and industries that rely heavily on government contracts. We hypothesize that, for firms in industries in which government purchases are a large fraction of firm revenues, political donations are more likely to be an investment in political capital¹⁶ and that returns are positively associated with donations.

In order to test this hypothesis, we gather data on the percentage of sales to federal, state, and local governments for 1,172 industry groups from the 2002 Economic Census (details available upon request). We assign to each company in our sample the company's industry level of sales to the government. In effect, we are assigning an industry fixed effect to the firms in our sample, albeit at a very high level of disaggregation with 1,172 industry classifications. We regress one-year excess returns on donations excluding individual donations, industry sales to the government, and the interaction of donations and industry sales to the government. The hypothesis is that the coefficient on the interaction of donations and industry sales should be positive. In other words, in industries in which government contracts matter to firm revenues, the returns to donating are positive. For donations, we report results for both a dummy variable, if the firm donates, as well as the dollar amount a firm donates.

The results are in Table 10. Columns 1 and 3 report results from a baseline regression of excess returns on donations and sales to the government. Consistent with our prior results, the relation between donations and returns is negative. Firms in industries that derive a higher fraction of total revenues from sales to government have higher excess returns. In Columns 2 and 4, we add the interaction of donations with industry sales to the government. In neither case is the coefficient on the interaction term positive. These results suggest that firms in industries with a large fraction of sales to the government do not earn higher returns from donating.

¹⁶ Agrawal and Knoeber (2001).

Table 10: Government Contracts and Returns to Donations

The dependent variable is one-year excess returns based on the four-factor model. Data on the fraction of industry sales to the government (“Sales to Government”) are taken from the 2002 Economic Census. “Donation” is either the dollar amount of soft money and 527 Committee donations or a dummy variable for whether the firm makes such donations at all. Robust standard errors clustered by firm are reported in brackets. ***, **, and * indicate significance at the 1%, 5%, and 10% levels, respectively.

	(1)	(2)	(3)	(4)
Donation (dummy)	-0.037*** (0.016)	-0.036** (0.018)		
Log (Donation)			-0.267** (0.148)	-0.274** (0.180)
Sales to Government	0.036 (0.052)	0.037 (0.053)	0.038 (0.051)	0.043 (0.052)
Donation × Sales to Government		-0.013 (0.204)		-2.007 (2.350)
Constant	0.029 (0.022)	0.029 (0.022)	0.027 (0.022)	0.026 (0.022)
Year Dummies	Included	Included	Included	Included
Observations	10982	10982	10982	10982
R-squared	0.01	0.01	0.01	0.01

7. Conclusion

Our results suggest that corporate political donations in the US are reflective of agency problems. We find that firms that donate directly out of corporate funds are larger, have more free cash flow, and have lower R&D and investment spending. We also find that donations are negatively correlated with future excess returns. An increase in donations of \$10,000 is associated with a reduction in excess returns of 7.4 basis points. Worse corporate governance is associated with larger donations. Worse governance characteristics explain part but not all of the negative return-donation relation. Furthermore, firms that make political donations are more likely to engage in acquisitions than firms that do not make donations. In addition, donating firms engage in worse acquisitions than firms that do not donate, as measured by cumulative abnormal announcement returns.

Our findings are consistent with the fact that shareholders are taking an increased interest in political donations. According to the Center for Political Accountability (see www.politicalaccountability.net), “73% [of surveyed shareholders] agreed that corporate political spending is often undertaken to advance the private political interests of corporate executives rather than the

company's interest.” According to Guerrera (2007), “investors argue that public disclosure and board oversight [are] essential to ensure that executives do not use corporate money to help political allies or channel funds to politicians whose agendas contravene company policies.” Our results support the view that lack of transparency allows donations to function as a form of private benefits for managers. Our findings may shed light on why 89% of the publicly traded firms in the US make no political donations out of corporate funds at all during our entire sample period — shareholders are unlikely to benefit from such donations. This perspective may be particularly useful in light of the Citizens United ruling that may potentially increase the use of corporate funds greatly for political donations.

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