Independence of Financial Oversight

Evidence on Stakeholder Influence on Different Dimensions of SEC Independence

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liebevolle und großzügige Unterstützung haben meinen Werdegang geprägt und mein Studium und somit diese Dissertation überhaupt erst ermöglicht.

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List of Abbreviations

AAER   Accounting and Auditing Enforcement Release

BaFin   Federal Financial Supervisory Authority

CFO   Chief Financial Officer

CL   comment letter

CRP   Center for Responsive Politics

DCF   Division of Corporation Finance

DID   Difference-in-Differences

DoE   Division of Enforcement

DoJ   Department of Justice

EDGAR   Electronic Data Gathering, Analysis, and Retrieval

ESMA   European Securities and Markets Authority

FEC   Federal Election Commission

FISG   Financial Market Integrity Strengthening Act

FREP   Financial Reporting Enforcement Panel

FTC   Federal Trade Commission

GSEM   generalized structural equation modeling

IPO   Initial Public Offering

IRS   Internal Revenue Service

ITSFEA   Insider Trading and Securities Fraud Enforcement Act of 1988

NAFTA   North American Free Trade Agreement

PAC   Political Action Committee

PC   political connections

PCAOB   Public Company Accounting Oversight Board

SEA   Securities Exchange Act of 1934

SEC	United States Securities and Exchange Commission
SEM	structural equation modeling
SOPR	Senate's Office of Public Records
SOX	Sarbanes-Oxley Act of 2002
TPP	Trans-Pacific Partnership
US	United States
USMCA	Agreement between the United States of America, the United Mexican States, and Canada

Introductory
Summary

Independence is a state or condition of a plethora of matters, whose concrete meaning is highly context-dependent. On an individual level, it describes a person's ability to make its own choices out of its free will, and to take responsibility for them. Independence, in that context, is often used in conjunction with the term *autonomy* as a state of self-determination of a human's free will. In philosophy, this concept was coined by Immanuel Kant, who claimed a human to act morally accountable out of his own reason instead of following a foreign authority (Kant, 1786; Prechtl, 2008). Independence, thereby, does not only refer to natural, but also to legal persons and has to be considered even at an institutional level. In relation to a country or a nation, respectively its governance, the term mainly refers to the ability to govern itself without external interference or domination (self-governance) and, thus, the government's capability to act autonomously (Prechtl, 2008). Further, the term denotes a country's *sovereignty* over its territory.

All of these considerations have in common the notion of self-reliance, freedom from external control or influence, and the ability to make decisions without coercion or reliance on others. Independence has various, even context-dependent, dimensions. For instance, a student strives to be *financially* independent from his parents. The Basic Law for the Federal Republic of Germany ensures the judges to be independent in *personal* and *substantive matters* (Art. 97), thus to be only subject to the law without any other external instruction options. Or, specific organizations demand to have an own legal personality to be able to make own agreements, for that to be *legally* independent. Independence, by that, is either deemed as the ultimate state of autonomy with absence of any dependencies from externals, or any condition in between with a specific degree of dependencies.[1] The benefits of a natural or legal person's independence mainly depend on its environmental circumstances, personal targets and preferences, or overriding goals and principles. Independence, by that, cannot be considered as ex-ante desirable.

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[1] For instance, Weißgärber (2016) and Oertel (2000) discuss a dynamic process of separation regarding administrative units where full autonomy had already not been achieved.

Independence is frequently discussed in the context of financial oversight[2] authorities. Regarding the United States Securities and Exchange Commission (SEC), the term already appears in the designation of the agency's type, *independent agency*. A growing strand of literature applies the capture theory (Stigler, 1971; Peltzman, 1976) to the SEC and investigates whether the agency acts independently from special interest groups and the Congress (e.g., Correia, 2014; Heese et al., 2017; Khokhar & Shahriari, 2022; Mehta & Zhao, 2020; Thompson, 2022). However, this literature suffers from several issues. Firstly, the term *independent agency* is often misunderstood (Morrison, 1988). Instead of a complete independence from any external stakeholder, the term refers only to the (intended) lack of opportunity for the United States (US) President to remove agency heads at will (Manners & Menand, 2021; Sunstein & Vermeule, 2021; H.L.R., 2013). Secondly, research on regulatory capture frequently points out associations and correlations that are representing other patterns beside regulatory capture (Carpenter, 2014). Thirdly, literature on SEC capture usually measures observable SEC issues like Accounting and Auditing Enforcement Releases (AAERs) or comment letter (CL) which limits the researches informative value to the specific SEC division disclosing the issues instead of the entire Commission.

Independence was even a commonly used discussion item in the context of the Wirecard accounting scandal in 2020 and the potential omissions of the German financial supervision and enforcement institutions, Financial Reporting Enforcement Panel (FREP) and Federal Financial Supervisory Authority (BaFin) (e.g., ESMA, 2020; Kaufhold et al., 2021). For instance, the FREP's head, Edgar Ernst, was criticized for being personally dependent when holding supervisory board mandates (ESMA, 2020). Additionally, the BaFin was considered as not

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[2]The terms "financial oversight" and "financial supervision" are not legally-defined and used inconsistently in prior literature. I use the term "financial supervision" to describe a regularly or selective disclosure review, as it is conducted by the SEC's Division of Corporation Finance (DCF) (a German equivalent would be "Bilanzkontrolle"). In distinction to this, "enforcement" denotes law enforcement and penalization, as it is conducted by the Division of Enforcement (DoE). The term "financial oversight" is used for the entire process, including filing review as well as enforcement.

being independent in substantive matters from the German Ministry of Finance (Kaufhold et al., 2021). Nevertheless, also this discussion suffers from substantial weaknesses. The demand for independence from political influence has often been maintained, but not sufficiently substantiated (e.g., AKBR, 2020; Böcking et al., 2020; Langenbucher et al., 2020). Furthermore, the discussion is often limited to a specific dimension of independence, ignoring that a financial oversight agency's independence encompasses a wide range of aspects.

This thesis contributes to the ongoing debate on financial supervision and enforcement agencies' independence. It addresses the weaknesses and issues of the public debate as well as prior literature, that are pointed out above. The thesis provides a holistic view on agency independence with special consideration of the SEC.

Part A[3], as an extensive introductory part, provides a literature-based discussion on the necessity of financial oversight and its conducting agency to be independent. It points out all financial supervision's stakeholders that potentially influence an agency and classifies dimensions of agency independence. As a result of these considerations, I derive a matrix that juxtaposes stakeholders and independence dimensions (see Figure I.1 for this matrix). This array allows to effectively discuss weaknesses in agency governance and to precisely categorize research on agency independence. Concerning financial supervision and enforcement agencies, I elaborate and evaluate the most critical dependencies, based on prior literature.

The subsequent parts B–D provide empirical evidence on the consequences of specific stakeholders' influence considering the different dimensions of independence, as derived in part A. These parts focus on the SEC, as they contribute to a literature strand on SEC independence that found indistinct results whether undue influence of specific stakeholders exists (e.g., Yu & Yu, 2011; Correia, 2014; Heese et al., 2017; Khokhar & Shahriari, 2022; Heese, 2019). The

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[3]There is a working paper version available of part A. I refer to it in the other parts of this thesis as Piering (2024a).

Figure I.1:
Classification of Parts B–D within the Agency Independence Matrix
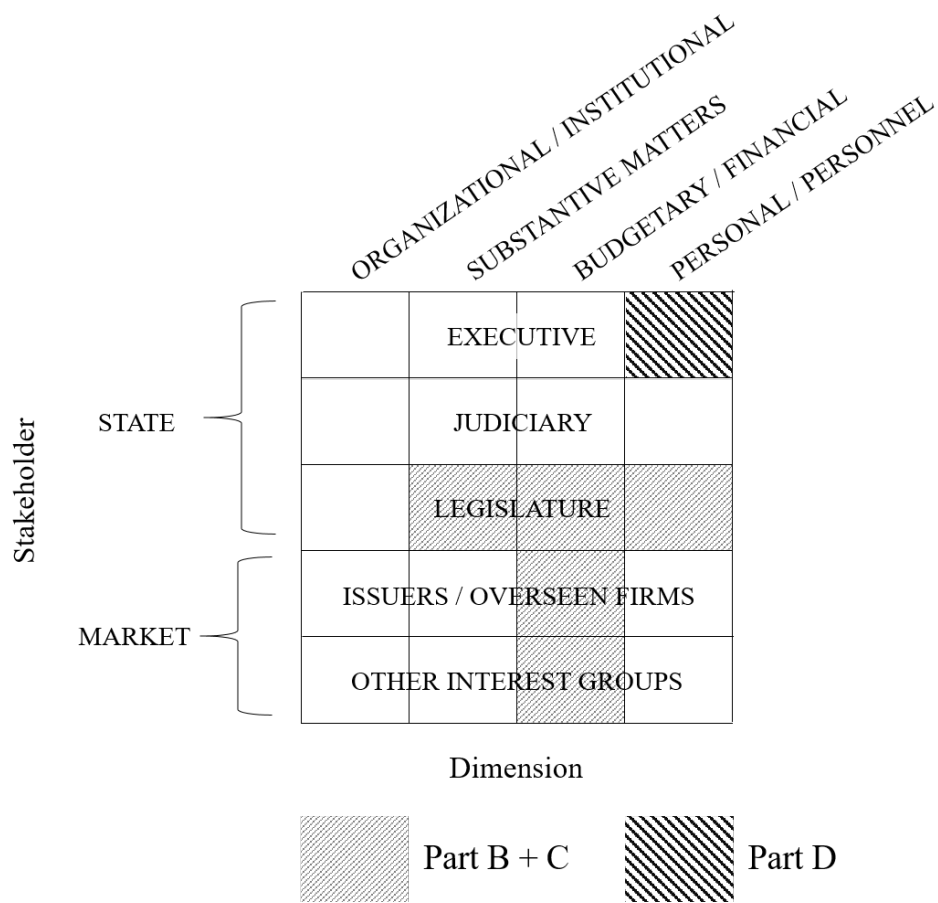
underlying mechanisms, that induce dependencies and that are investigated in the following parts, are categorized within the independence matrix (Figure I.1).

Part B[4] investigates whether the SEC is subject to regulatory capture and how capture depends on the Commissioners' composition. Capture theory (Stigler, 1971; Peltzman, 1976) is based on the iron triangle relation (Freeman, 1965; Adams, 1982) between bureaucratic agencies (such as the SEC), the Congress, and special interest groups. The SEC is overseen by the Congress and dependent on congressional budget setting. In turn, Congressmen can be supported by special interest groups through campaign contributions or lobbying expenditures. Capture theory suggests that these groups contribute to politicians in order to achieve favorable treatment by the

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[4]There is a working paper version available of part B. I refer to it in the other parts of this thesis as Piering (2024c).

SEC. Considering the agency independence matrix (Figure I.1), dependencies reflected in capture theory are both on the legislature (Congress) and market participants (issuers and other interest groups). Dependencies on the Congress are regarding personnel (consent to Commissioner nomination), budget (budget appropriation), and substantive matters (congressional oversight). With respect to market stakeholders, dependencies can be categorized as "financial" (lobbying expenditures and contributions). I apply a 3-step-model, developed by Carpenter (2014), to investigate for the DCF being captured. As prior literature assumed agency behavior strongly align with the agency head's composition (Keyser, 2023), I further test if financial supervision on politically connected firms significantly altered after a major change in the Commission. I find no indication of DCF capture. Instead, SEC financial supervision is more pronounced for politically connected firms. Even the major change in the Commission's heads, dominated by the new chairman Jay Clayton, did not make the DCF more susceptible to capture. Instead, the findings support to the concept of an effective oversight.

Part C[5] is a joint project with Jan Seitz. It addresses dependencies of the SEC on Congress and special interest groups in the sense of capture theory like part B, but expands the investigation to the entire SEC instead of only one division by using a relatively novel approach to measure SEC behavior. Prior literature that investigated SEC capture (e.g., Correia, 2014; Heese et al., 2017), as well as part B, suffer from a limitation due to the used measure for SEC behavior as the dependent variable. When using observable SEC issues, such as AAERs or CL, the informative value of a study is always limited to the corresponding SEC division that is issuing, e.g., the DCF for CL. We use a relatively new measure for SEC monitoring by observing downloads of firm filings from the SEC database Electronic Data Gathering, Analysis, and Retrieval (EDGAR), that had been conducted by SEC staff itself. This measure allows us an observation of the entire,

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[5]There is a working paper version available of part C. I refer to it in the other parts of this thesis as Seitz & Piering (2024).

cross-divisional, SEC oversight activity, including initial filing review that does not lead to a comment letter, as well as enforcement investigations. We find that firms' political connections have an attention-grabbing effect. An additional mediation analysis shows that the increased comment letter receipt likelihood for politically connected firms, as discussed in part B, can be explained to a large extent by this attention-grabbing effect and the increased monitoring level.

Part D[6] addresses independence from a further stakeholder in financial supervision and enforcement: the executive. In contrast to parts B and C, which take the "traditional" regulatory capture model with interacting interest groups and the Congress as one basis, part D discusses mechanisms of presidential influence on the SEC. It investigates, whether the SEC was dependent from former President Donald Trump regarding their financial supervision. This part takes back the discussion on agency independence to the original idea when establishing the SEC as an independent agency (instead of an executive branch agency): to detach the President from undue influence on the agency. The subject of discussion is the President's ability to appoint SEC commissioners, to nominate the chairman, and – most important – to remove agency heads. Thus, the dependencies can be categorized as *personnel independence* within the matrix (Figure I.1). As especially removal conditions are highly debatable (Sunstein & Vermeule (2021) denote them as "one of the great unanswered questions in American public law"), the agency's heads cannot rely on being secured from removal at will. For that, there is some motivation to follow presidential preferences. With the inauguration of former President Donald Trump, an obvious and clearly observable break in politicians' ideology came along. Considering Trump's political agenda (e.g., the "America first" phrase from his "Make America Great Again" campaign), I find a significant change in SEC financial supervision behavior. The SEC is likely to prefer American firms over foreign and those belonging to specific industries when issuing comment letters since Trump's presidency.

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[6]There is a working paper version available of part D. I refer to it in the other parts of this thesis as Piering (2024b).

In summary, this thesis contributes to the ongoing debate on the independence of financial supervision and enforcement agencies. It provides a holistic view on agency independence considering all potential stakeholders and dimensions. Regarding the SEC, dependencies on the Congress (and indirectly on market stakeholders) do not seem to be as problematic as prior literature suggested. My findings indicate that financial supervision works effectively without any indices of capture, as politically connected firms attract SEC attention (part C) and, as a result, are more likely to receive a comment letter (part B). However, the findings of part D show that the discussion on SEC independence should focus more on its originally intention: insulation from presidential control. Only a factual independence from undue influence, regardless of whether it is exerted by politics or market participants, can ensure financial supervision and enforcement to work effectively.

Part A:

*Financial Supervision, Enforcement,
and their Authorities – a Classification*

Abstract

Recent corporate scandals have risen debates on financial supervision and enforcement agencies' independence. Prior literature also revealed lacks in independence. Nevertheless, the discussion is mainly about single aspects of agencies' dependencies. This paper provides a systematic view on financial oversight and enforcement independence. It points out all potential stakeholders and interest groups from which an agency might be dependent on. The dimensions of independence are systematically derived from literature and linked to stakeholders. The paper closes with an evaluation of the most critical dependencies and advice on avoiding potential inefficiencies resulting from these dependencies.

1 Introduction

"Independence" is a prevalently and in a variety of ways used concept in the context of financial supervision[7] and enforcement agencies[8]. Debates about agency independence frequently arise in close link with corporate (accounting) scandals. For instance, after the detection of the large Wirecard accounting scandal, the independence of the Financial Reporting Enforcement Panel (FREP), a private body that was entitled to conduct filing review on a first-stage, and the federal competent authority BaFin, was under public discussion and led to a tightening of capital markets law (e.g., Kaufhold et al., 2021; ESMA, 2020; Langenbucher et al., 2020; Osman, 2021). In that context, the BaFin President, Mark Branson, stated that there is a necessity of a total independence regarding operative supervision (Osman, 2021). The independence of the US financial supervision and enforcement authority SEC is also frequently subject of research (e.g., H.L.R., 2013; Karmel, 2016b; Bressman & Thompson, 2010; Heese et al., 2017; Heese, 2019; Correia, 2014; Piering, 2024c).

The main purpose of independent agencies is the ensuring of democratic governance integrity and the improvement of its quality and resilience (Bulmer, 2019). Thus, they are often intended to be additional to (and independent of) the three traditional branches of government (Bulmer, 2019), which are the executive, the legislature and the judiciary. The discussion on agency

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[7]In this paper, I use the terms "financial supervision" and "financial oversight" interchangeable. In the current context, the term mainly denotes a supervision on the punctual and complete filing of mandatory firm disclosures and a review of its content. In practice, financial supervision is commonly broader. The German Federal Financial Supervisory Authority (BaFin) activity covers, besides filing review, banking and insurance supervision. In the context of filing review, prior research uses various terms instead of financial supervision (e.g., Blackburne (2014) uses the term "regulatory oversight") or extends its meaning to other activities (e.g., Heese et al. (2017) used the term "SEC oversight" for filing review and enforcement.). The SEC itself denotes filing review and enforcement as "active regulatory oversight" (SEC, 2000). Financial supervision is to be distinguished from external audit.

[8]The terms "authority" and "agency" are both used in practice with only little differences in meaning depending on the context. While the term "agency" generally refers to a government organization with responsibility for specific functions or tasks, such as the United States Securities and Exchange Commission (SEC) as an independent agency, the term "authority" is a more general one referring to any organization with decision making or enforcement power. Such an organization with regulatory authority is the German BaFin. Nevertheless, both organizations are comparable regarding their legal suspension and enforcement power. The terms "authority" and "agency" are therefor interchangeably used in this research paper.

independence in general originally comes from the central bank sector (e.g., Cukierman et al., 1992; Goodman, 1991; Vaubel, 1997; Laurens et al., 2009). Specifically for financial supervision and enforcement agencies, the debate on independence suffers from five main issues.

The first major issue is the uncertainty of what "independence" actually means. The term "independent agency" can be found either in US, but also in European and German public law (*unabhängige Institutionen*). In the US, the term emphasizes a detachment from the executive, mainly the President – in contrast to "executive branch agencies" –, but is frequently misunderstood, especially in non-US literature (Morrison, 1988)[9]. A common approach limits the "independence" of independent agencies to the lack of opportunity for the President to remove agency heads at will (Manners & Menand, 2021; Sunstein & Vermeule, 2021; H.L.R., 2013). In Germany, the main characteristic of independent authorities is is that their decision-making is detached from directly democratically legitimized bodies (e.g., the Parliament), and independent from electoral considerations as their staff is not elected directly by the people (Bredt, 2006). Nevertheless, these descriptions are vague. For instance, the former German Federal Minister for Economic Affairs, Günter Rexrodt, assured to respect the Federal Network Agency's independence, but gave no clue about the consequences (Oertel, 2000). In fact, there are no objective criteria existent to qualify an organization as independent (Groenleer, 2009), taking into account that agency independence can never be absolute (Quintyn, 2008). However, financial supervision and enforcement agency's independence is much more multi-layered and comprises more criteria than the narrow concepts cited above.

The second issue is the consideration of agency independence being ex-ante beneficial. In fact, the benefit is content-dependent. Although there are many reasons to enhance financial supervision and enforcement agencies' independence, several problems arise in that context. The question about the democratic legitimization and a democracy deficit is central (e.g., Quintyn,

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[9]This literature often extends the interpretation of "independent" to other stakeholders, e.g., the legislature.

2008). Besides that, a too high degree of agencies' independence could lead to a protection of unnecessary agencies from shutdown, a limitation of cooperation between agencies or to an unauthorized extension of authority and powers (Heine & Mause, 2013). Ergo, there is a point in between dependency and independence for an agency to fulfill its delegated tasks optimally (Moe, 1995).

The third issue is that the discussion on independence is mostly held from a legal perspective (e.g., Fischer-Appelt, 1999). The justification for the requirement of financial supervision and enforcement, though, must also be made from an economic point of view. The necessity of financial supervision and enforcement can be argued both from an economic and a market framework perspective. At capital markets, issuers and investors get into contractual relationships. Their relation is characterized by information asymmetries that lead to a principal-agent problem (Jensen & Meckling, 1976). To solve this problem, the disclosure of financial accounting information and the assurance of their reliability is of great importance (Jensen & Meckling, 1976; Ng, 1978; Healy & Palepu, 2001) to make the market work efficiently (Fama, 1970). The introduction of external auditors can solve this problem only partially, as they are self-interested parties in a further arising agency relation (Watts & Zimmerman, 1983; Kraakman, 1986; Levitt, 1998; Coffee, 2004). Thus, an independent authority that works in addition to external auditors is necessary from an economic point of view. The market framework perspective ties in with the relevance of functioning capital markets for modern economies (Casey, 1971; Cooley & Walter, 2010; Pilbeam, 2010).

The fourth issue is prior literature's restriction to selected dimensions and formal aspects of independence ignoring that a huge variety of aspects must fit together to achieve a truly independent financial supervision and enforcement. Furthermore, there is a gap between a formal independence – that what is defined in statutes – and the actual independence of agencies which is

indicated by policy decisions and policy outcomes (Hanretty & Koop, 2012). As a consequence, a proper classification of all relevant aspects and dimensions of agency independence is needed.

The last issue is that the discussion on independence usually only considers independence from one stakeholder or a specific group of stakeholders ignoring that various kinds of stakeholders have motivation to intervene in agency activity in general and specifically in financial supervision and enforcement. Research and public discussion mostly refer to independence from government and politics (e.g., Fischer-Appelt, 1999). Independence from other stakeholders is rarely discussed.[10] This paper categorizes state and market stakeholders of oversight agencies. Governments have short-term interests that might lead to an adoption of a less stringent approach of supervision in order to receive voters' support (Quintyn & Taylor, 2002). For that reason, a higher degree of independence from government would isolate the agency from electoral cycles (Fraccaroli et al., 2020). A core problem coming along with this insulation is the question of an agency's democratic legitimization (Fischer-Appelt, 1999; Bredt, 2006; Kruse, 2013). Market participants such as issuers or interest groups (e.g., external auditors) have further, contrary interests as disclosure of misbehavior or poor performance can have negative consequences for them, such as reputational loss. The nature of the authorities' dependency from external stakeholders can be graded in several steps, whereby a lower degree of formal dependency does not necessarily mean that there is actually less opportunity to exert influence.

The general necessity of a functional independent financial supervision and enforcement, like it is derived from economic and market framework perspective, is independent from the actual governmental structure. The specific design of an independent authority, however, strongly depends on governmental specifics (e.g., whether there is a parliamentary or presidential govern-

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[10]Kruse (2013) mentions other stakeholders like interest groups, but explicitly only refers to independence from government. Heine & Mause (2013) argue that interest groups as addressees of regulation could have possibilities to intervene in hybrid regulation that combines public and private aspects, such as private accounting standards boards.

ment). Thus, in this paper a differentiation between the necessity of a functional independence of financial supervision and enforcement, on the one hand, and the independence of the conducting institution, on the other hand, is made.

The issues described above are addressed in this research. For that, the remainder of this paper proceeds as follows: Section 2 derives theoretical demand for independent financial supervision and enforcement from an economic perspective and a perspective of regulatory policy and market framework. It further points out stakeholders and interest groups of supervision and enforcement. Section 3 classifies the meaning of independence in an agency governance framework and shows interdependencies with other governance aspects. Section 4 derives dimensions of independence on an operational level regarding enforcement agencies. This section points out possible dependencies from external stakeholders for each dimension and discusses whether specific aspects of agency independence are needed to ensure an independent enforcement. Section 5 concludes and shows future research options.

2 Demand for an Independent Financial Supervision and Enforcement

2.1 Financial Supervision and Enforcement from a Micro-Economic Perspective

A capital market is a place where capital providers – investors – and capital users – issuers – enter into mutual contractual relationships. The capital market acts as an intermediary between these two parties (Kaufhold et al., 2021). From the separation of ownership and control, which is a core characteristic of a public company, an agency problem arises (Jensen & Meckling, 1976). Generally, a principal-agent-problem occurs when a principal delegates competencies to an agent in a contractual relationship in order to act in his interest (Fama, 1980; Jensen

& Meckling, 1976). The agent is compensated for his effort, but acts opportunistically by maximizing his own benefit. Thus, there are divergences of interests between principal and agent (Jensen & Meckling, 1976). Additionally, the agent has an information advantage over the principal regarding his characteristics, intentions and actions (Breton, 1995; Breid, 1995). As a consequence, the principal is not able to observe the agent's behavior immediately (Arrow, 1985). The situation is costly for both parties: the principal establishes monitoring mechanisms over the agent (monitoring costs), whereas the agent attempts to build trust with the principal (bonding costs) (Jensen & Meckling, 1976). To solve this dilemma and minimize occurring agency costs, mechanisms must be implemented that make it rational for the agent to act in the principal's interest, balancing drawbacks and advantages of his performance contribution (Jensen & Meckling, 1976; Bockmann, 2012). The provision of information – commonly financial accounting information – from the better informed agent, e.g., a firm's manager, to the principal (owner) can reduce information asymmetries and lower agency costs (Ng, 1978). The agency problem is particularly pronounced in the context of an anonymous capital market. The efficient-market hypothesis of Fama (1970) states that the efficiency of a market depends on its ability to process information (historical, publicly available or private) and which information is therefore reflected in the stock price. A semi-strong efficient capital market incorporates all publicly available information in the price (Fama, 1970). Thus, the assurance of a capital market to be efficient is highly dependent on the availability and disclosure of corporate information (Healy & Palepu, 2001).

Coming back to the agency problem, especially the information asymmetry and divergent interests between owner and manager, there is a necessity to control for the availability, relevance, quality and reliability of the disclosed information (Jensen & Meckling, 1976; Healy & Palepu, 2001). A typical mechanism is the implementation of an independent third-party auditor.

Historical development shows that professional auditors have been appointed even in the absence of specific obligation and regulation to do so due to its major economic importance (Watts & Zimmerman, 1983; Hörner, 2020).[11]

Although high quality audit indubitably contributes to reducing information asymmetries, the introduction of an auditor into the contractual relationships of a company can arise another agency problem.[12] The external auditor is appointed by the manager to review the firm's financial accounting and receives a compensation for his work. In this situation, a new agency relation between manager (principal) and auditor (agent) occurs. The auditor, so far, cannot be considered as a neutral monitor, but acts with his own incentive structure as an economic agent (Velte & Weber, 2011). Between investor and auditor, a further agency relation occurs, as the investors delegated the audit of financial accounting information to the external auditor instead of conducting it by themselves, which would lead to a free-rider problem and increased agency costs (Watts & Zimmerman, 1983). This relation is often denoted as a "Gatekeeper-function" of the external auditor for the investor (e.g., Levitt, 1998; Kraakman, 1986) which bases on a systematization of Gilson & Kraakman (1984). A gatekeeper is a reputational intermediary that has only a limited payoff from an involvement in misconduct (Coffee, 2004). Thus, a gatekeeper should receive only a limited loan besides its reputation capital (Coffee, 2004). As the auditor is compensated for his work by the manager, a dilemma arises as he is "dealing with two masters" (Shapiro, 2005).

Figure A.1 shows the contractual structures between investors, managers and auditors to visualize the occurring agency problem.

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[11]A huge research field is about audit quality (e.g., DeAngelo, 1981; DeFond & Zhang, 2014). This will not be further discussed at this point.

[12]A similar problem arises in the context of introducing a supervisory board as an internal control body. The role of the supervisory board will not be further discussed at this point as it is a specific feature of the internal governance system in Germany.

Figure A.1:
Agency Problem of the Auditor
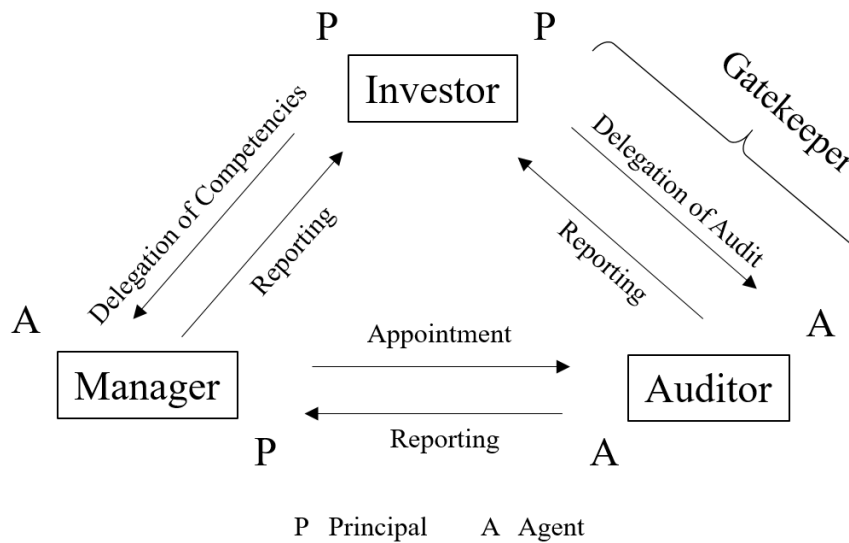
Due to these agency problems between auditors, managers, and investors, a further – independent – supervisory and enforcement authority is appropriate (Bockmann, 2012) which is not in any contractual relationship with the other three parties. It is not necessarily the case that the authority has to actively review again all disclosed information, but already the threat of significant sanctions in the event of detected irregularities or misconduct has a preventive function (Tielmann, 2001).

Practical experience demonstrates that the enforcement of accounting standards is essential to achieve high quality accounting (Böcking et al., 2015). Research provided evidence that stricter enforcement is beneficial for market liquidity (Christensen et al., 2013, 2016) and lower cost of capital as investors lower their required return in the case of stricter enforcement (Hail & Leutz, 2006). Additionally, analysts' forecasts are more accurate when enforcement is more developed (Preiato et al., 2013) and stronger (Hope, 2003).

The relations shown above are all market-based. From an economic perspective, the actual grade of a supervisory and enforcement agency's independence from the government is marginal as long as the major stakeholders are able to evaluate supervisory and enforcement efficacy and have the power to punish the agency for misbehavior (Heine & Mause, 2013).

2.2 Financial Supervision and Enforcement from a Perspective of Regulatory Policy and Market Framework

Besides the above presented economic reason – the demand from the market to establish mechanisms to control for information availability and validity – there must be a rationale for government intervention in capital markets when establishing financial supervision and enforcement in the context of market framework in a free market economy. Capital markets are of tremendous importance for modern political economies. Heilmann (2003) denoted them as their "Central Nervous System". On the one hand, a functioning capital market ensures peoples' living standards, jobs and opportunities, the financing of government spending, as well as a general liquidity through pension funds, life insurances and stock ownerships (Casey, 1971; Frach, 2007; Cooley & Walter, 2010, e.g.,). On the other hand, a lack in the capital market's function can lead to significantly negative real effects. Due to systematic connections and trust dependencies, the failure of one single public firm can destabilize the entire market (Pilbeam, 2010). Recent corporate scandals and failures, such as Enron, WorldCom, Lehman Brothers or Wirecard, have impressively demonstrated this impact. Thus, a functioning capital market is important for a state for two reasons: to support the positive effects of economic welfare and to prohibit or limit a loss in economic welfare (Thiele, 2014). The governmental intervention in the form of bringing regulation, supervision, and enforcement to the market is executed in order to avoid the negative effects of an unregulated market.

Although any regulation can be considered as a modification of the free market economy (Fischer, 2008), one can state that markets are artificial constructions that are not able to exist without a political and legal framework (Frach, 2007), due to their complexity and high importance for the economy. Accordingly, governmental intervention and regulation should ensure a functioning, competitive market (market making) and straighten out negative social and political effects (market correction) (Eberlein, 2000). In fact, governmental intervention seems to be necessary in every field where market failure is likely to appear (Akerlof, 1970).[13] The creation of a supervisory and enforcement agency from the perspective of regulatory policy and market framework – in contrast to the pure micro-economic perspective – is accordingly not resulting from contracts between market participants, but from circumstances that are relevant for the entire society (Heine & Mause, 2013). One aim of market framework in the context of financial markets is that investors can be confident in the market (ESMA, 2014). For that, market participants need to trust in a fair, unbiased and continuous law application that is independent from short-term political goals (Kaufhold et al., 2021). A supervisory and enforcement authority can be considered as a guard to apply the legal framework for the market in a fair and indiscriminate way (Krahnen & Moretti, 2015; Dell'Ariccia & Marquez, 2006; Kaufhold et al., 2021). In the context of market framework, the theoretical functionality of supervisory and enforcement is extended. As described above, the announcement of mistakes itself can have a preventive function. Nevertheless, the external auditor is missing a legal option to penalize a misreporting firm (Bockmann, 2012). In the absence of governmental authority – in a free market economy – even an introduced independent supervisory authority would not have any power to sanction wrongdoing. So, a governmental authorized and legitimized authority is necessary to act as an independent supervisor and enforcer having a corrective function (Bockmann, 2012). A core question that comes along is about whether supervision and enforcement should be conducted by

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[13]For a deeper insight into this so-called "Krisentheorie", please note Fülbier (1998).

the government itself, hence a part of the executive or the legislature, or another professional institution or competent authority that is not part of the government (Kruse, 2013). In its most extreme form, it would be a completely autonomous and legally independent institution (Von Bonin, 1979). A core problem that comes along with authorities' independence is the loss of democratic legitimization of the supervisory and enforcement agency (e.g., Bredt, 2006; Ludwigs, 2011; Quintyn, 2008). This issue will be discussed in the following section. To decide which type of institution is appropriate for supervision and enforcement, I relate to the four-field matrix that is provided by Kruse (2013). It differentiates between the normative content of a subject and the necessary expertise. On the one hand, financial supervision and enforcement of accounting rules have a low normative content as their aim and their normative elements are in the public interest[14], commonly known and manifested in law. On the other hand, a high expertise is required as these tasks are far away from standardized routines, but individual and challenging in each case.[15] Following Kruse (2013), a professional institution is appropriate to conduct financial supervision and enforcement.

2.3 Stakeholders and Interest Groups

A serious weakness most of prior research about independence of agencies and independent enforcement has in common is a focus on specific stakeholders ignoring the circumstance that various agencies' stakeholders have potential influential power and diverse motivation to intervene in enforcement agencies' matters[16]. This subsection provides a proposal of a systematization of enforcement agencies' stakeholders. Figure A.2 presents this systematization.

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[14]For a detailed discussion on the public interest in financial supervision, see also Piering (2024a).

[15]In that context, the high demands on the profession of external auditors or Certified Public Accountants with strictly regulated and challenging professional examinations is mentioned.

[16]These matters include not only substantive matters, but also agenda, budget or personnel matters. For a discussion about dimensions of independence, see section 3.

Figure A.2:
Agencies' Stakeholders

State			Market	
Executive	Legislature	Judiciary	Issuers	Other Interest Groups
• President • Ministries • Governmental Agencies	• Parliament • Congress • Upper/Lower House	• Supreme Court • Other National Courts • International Courts	• Public Firms • Managers • Investors	• Auditors • Trade and Professional Associations • Lobbyists / Campaign Committees
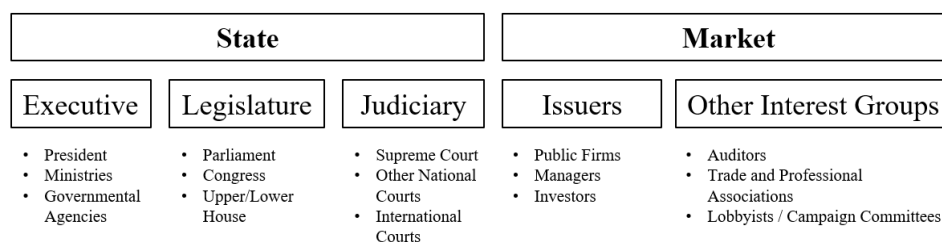
On a first stage level, a general distinction between state and market stakeholders can be drawn. On state level, in the case of separation of powers – the so-called *trias politica* – one can differentiate between judiciary, legislature and executive.[17] A common term in prior literature is *Government* (e.g., Kaufhold et al., 2021). Nevertheless, this term is inconsistently used with regard to the encompassing parts of the state authorities. A narrow interpretation only encloses the executive (*Regierung*). In some literature, it encloses legislating bodies as well as executive bodies like ministries, or the President (e.g., Laffont & Tirole, 1991). Some literature additionally mentions the judiciary (e.g., Lewis, 2003; Maskin & Tirole, 2004), and some also explicitly other public authorities like independent or federal agencies (e.g., Heine & Mause, 2013; Wilson, 1989), which are also sometimes denoted as "bureaucracy" (e.g., Lewis, 2003; Alesina & Tabellini, 2007; Wilson, 1989). An extensive discussion about the consideration of bureaucratic agencies as a governmental part is provided by Strauss (1984). In the following, the term *government* encloses all three branches (executive, legislature, judiciary). Other public authorities like German Federal Agencies will mostly be assigned to the executive as these authorities assist the executive branch and enforce federal laws (Art. 86 Basic Law for the

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[17]The governmental system of dividing power into three branches has to be distinguished from other types of state governments, like the parliamentary system. The main difference between these two is the overlapping functions between legislature and executive. Additionally, in parliamentary systems, the democratic legitimization of the executive is derived from the legislature, whereas in separated branch government the executive is directly elected and therefore legitimized by the people. In the following, I refer to these differences when necessary.

Federal Republic of Germany). Nevertheless, there is no ex-ante conviction of a financial supervision and enforcement agency to be part of the executive.

Kruse (2013) notes that the demand and extent of an agency's independence from state level institutions depends on its intended function and, thus, on its appropriate and selected institutionalization. For financial supervision and enforcement of accounting rules, a professional institution seems to be appropriate. Following Kruse (2013), a participation of political institutions in supervision and enforcement is not required. Nevertheless, conducting sovereign tasks, such as enforcing law, needs at least formal democratic legitimization.

Democratic legitimization requires an involvement of the **legislature** (Bredt, 2006; Weißgärber, 2016). In contrast to the executive, whose election mode depends on the current governmental system, the legislature in democratic states is elected by the people. Ergo, an establishment of agencies by federal law – such as the creation of the SEC by the Securities Exchange Act of 1934 (SEA) in 1934 – requires legislative participation. In the further process, the legislature might also be responsible for general agency oversight, agenda/policy or budget setting, or nomination of agency heads and staff.

Besides legislature, the **executive** can be an influential stakeholder in financial supervision and enforcement. In some cases, like for the German BaFin or US executive branch agencies, the conducting authority is a governmental agency that is part of the executive. In these cases, there might be more or less strict ties regarding oversight or rights to issue instructions.

At this point, it is necessary to discuss why politicians – both from the legislature and the executive – are motivated to intervene in financial supervision and enforcement. Prior literature often simply refers to short-term government incentives (e.g., Kaufhold et al., 2021) insinuating seek for vote-maximization about the politician (e.g., Quintyn & Taylor, 2002). Politicians' short-term interests are often against the independence of agencies as this limits their current

power (Kruse, 2013). Three main theories about why politicians intervene in regulation have been provided by political science literature (Bischof et al., 2020). Regulatory capture theory (Stigler, 1971; Peltzman, 1976) is an economic description of politicians' special (self-)interests, that are either addressed by special interest groups (e.g., by political contributions, Grossman & Helpman (1994)) in exchange of favor special treatments by agencies that are dependent on congressional funding, or reflected in the politicians' seek of maximizing political support in the form of votes (Heese, 2019). Public interest theory considers politicians as persons of character acting in the best interest of the public (e.g., Pigou, 1938; Wittman, 1977; Alesina & Tabellini, 1988; Callander, 2008; Hail et al., 2018). Ideology theory (e.g., Kau & Rubin, 1979; Kalt & Zupan, 1984; Mian et al., 2010) states that politicians' decision-making is based on the politicians' personal beliefs (e.g., Smith et al., 2012) or from more rationale motives like signaling to voters (Kalt & Zupan, 1984; Poole & Rosenthal, 1996). Prior research provided evidence that nearly all of these theories might explain politicians' intervention in financial supervision and enforcement (capture theory: Correia (2014); Heese et al. (2017)), voters' interest theory: Heese (2019), ideology theory: Piering (2024b)).

Additional to the typical executive institutions – President and ministries –, also other governmental agencies might be stakeholders in financial supervision and enforcement. These connections are most relevant when two agencies are entitled to regulate or supervise the same or similar issues (Heine & Mause, 2013). In case of a greater degree of independence, a coordination problem between these agencies arises (Moe, 1995; Heine & Mause, 2013).

Finally, the **judiciary** is the third force of the three governmental branches. It has the power to review actions by administration, legislature and executive, the so-called judicial review (Jowell, 2000; Elliott, 2001; Oliver, 2000), which is in line with the idea of checks and balances and determines the limits of governmental power (Griffith, 1977). As being part of the executive, the

supervision and enforcement agency's actions are subject to judicial review.[18] In common law countries, the judiciary also makes specific laws by itself which might affect financial supervision or enforcement (Griffith, 1977).

On market level, a differentiation between issuers and other interest groups is made. **Issuers** are those legal entities that sell their shares on a primary market or whose stocks are traded on a secondary market. Their stake in the supervisory and enforcement process has been demonstrated in section 2.1. Nevertheless, the consideration of the issuer as one stakeholder is contrary to the argumentation of divergent interests between investors and managers in financial supervision and enforcement, as prior discussed. This consideration has to be delimited from the following classification. The most important reason for that is the consideration of issuers as legal entities instead of a collection of contractual relationships between managers, owners, and employees. Possible dependencies of agencies with issuers will primarily appear at a legal entity level. This might be, for instance, penalties from enforcement actions or other legal consequences regarding financial accounting disclosure, but also financial contributions, the right of appeal or possible voting rights regarding nominations. It is noteworthy that legal consequences might also target parts of issuers, such as managers personally liable. Thus, the different parties have stakes and personal interests in oversight, but their sole power might be marginal.

Other interest groups have a specific stake in the market belonging on their function. These are especially auditors, trade and professional associations, lobbyists, or other interest groups that depend on the public law framework, e.g., Political Action Committees (PACs) in the United States.[19]

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[18]For the extensive discussion whether the judiciary and which of its institutions are effectively able to rein in executive power, see exemplary Ahdout (2022).

[19]Like for financial accounting, scientists could also be considered as an interest group (e.g., Tielmann, 2001). However, this group usually has no specific self-interest in financial supervision and enforcement, but is professionally balanced.

As for issuers, the auditor's stake in financial supervision and enforcement has also been drawn in section 2.1. The object of financial supervision and enforcement, a firm's financial accounting disclosure, in many cases has already been audited by an external auditor when it comes to supervision or enforcement investigation (Ewert & Wagenhofer, 2019). As this auditor is also an economic participant in the market, he is striving to increase his earnings (Mattheus, 2009). Any release resulting from supervision or enforcement is a flag for low audit quality (Florou et al., 2019). In many cases, audit deficiencies are cited directly in an enforcement release, including the auditor firm's name (Feroz et al., 1991). Literature on auditor independence argues with mainly two appearing consequences for the auditor. Firstly, an auditor builds reputational capital in the form of expected profits from audit fees of other clients (DeFond & Zhang, 2014; DeAngelo, 1981). In case of losing reputation, this impairs his ability to attract and retain clients and lowers his probability of re-engagement (DeFond & Zhang, 2014). Secondly, an auditor tries to avoid being exposed to litigation (Dye, 1993). The expected penalties for an auditor increase with stronger enforcement regimes (Ewert & Wagenhofer, 2019). From these reasons, an auditor is interested in avoiding any negative releases regarding his clients. For that, auditors have obvious stakes in supervision and enforcement. A further, minor, stake is that auditor's penalty can also result from the auditor oversight board, such as the Public Company Accounting Oversight Board (PCAOB) in the US. In this specific case, the SEC, as the supervision and enforcement authority, also has control over the PCAOB, e.g., by the appointment of the PCAOB members (Keyser, 2023).

Trade and professional associations can represent the interests of certain groups, such as labor unions or representatives of specific industries. For instance, Piering (2024b) provided evidence that the SEC adjusted its oversight intensity regarding specific industries dependent on

the incumbent President. Thus, there would be an interest for representatives of certain industries to intervene in financial supervision.

Finally, depending on the actual public law framework, interest groups, like lobbyists, and special campaign contribution committees, like PACs, could have stake in financial supervision and enforcement. As presented in the iron triangle relation for the US (Freeman, 1965; Adams, 1982), the interaction between interest groups, the Congress and agencies could lead to regulatory capture (Stigler, 1971; Peltzman, 1976). These groups act in the interest of their contributers, e.g., issuers, in order to achieve beneficial treatment from the agency in their favor.[20]

3   Independence in the Context of Agency Governance

When establishing an agency that is conducting financial supervision and enforcement, a proper agency governance has to be set up that avoids an agency behavior as an "uncontrolled fourth branch of government" (Majone, 1993). Prior literature discussed shortcomings arising from too-independent agency (e.g., Heine & Mause, 2013; Quintyn, 2008). Additionally, the question of the democratic legitimization of the agency is present, as a too-independent agencies could lead to a democratic deficit (Quintyn, 2008). A discussion on agency independence must necessarily also address points like accountability of the agency against the public or transparency of its decision making. Considerations about the interdependencies between these different aspects of agency governance mostly come from literature on central bank independence (e.g., Laurens et al., 2009; Capie et al., 1994; Quintyn & Taylor, 2002). Quintyn (2008) provides a four-pillar framework on regulatory governance in the context of independent regulatory agencies. Although

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[20]In the end, nearly every stakeholder that has special interests in accounting and standard-setting could be considered as a potential stakeholder of financial supervision and enforcement. A discussion on further private groups can be obtained from Haller (1994).

a financial supervision and enforcement agency does not necessarily conduct regulatory activities, the arguments regarding governance are also valid for the primer.

The four pillars that are strongly interdependent are presented in Figure A.3.

Figure A.3:
Four Pillars of Agency Governance
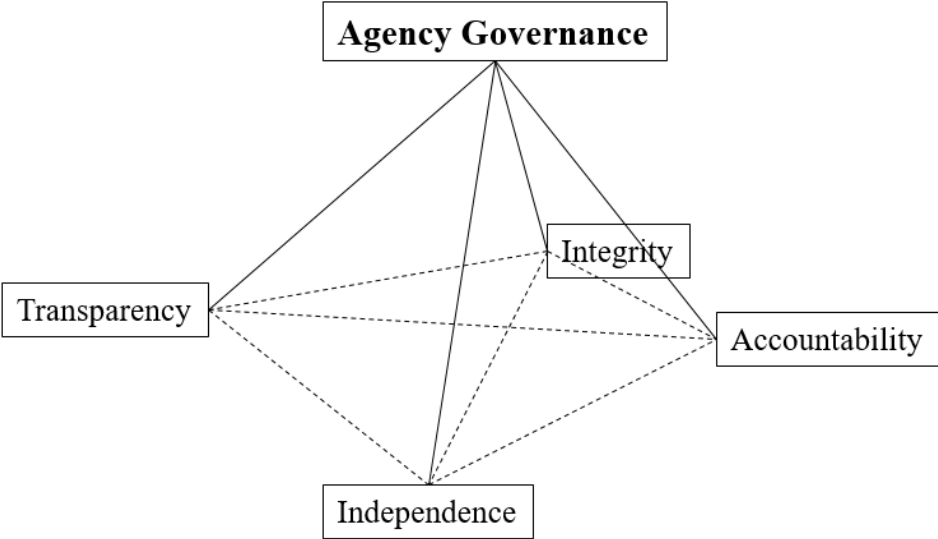
Figure A.3 based on Quintyn (2008).

Following this framework, *independence* is defined as the insulation from improper influence from politics and industry (or further economic stakeholders). Unlike often mentioned, it is one part of the interdepending pillars of governance and not an end in itself (Quintyn, 2008). The dimensions of independence will be discussed in the following section.

An inseparable link exists between independence and *accountability*. Jenny (2012) states that independence and accountability act complementary and accountability is necessary to ensure independence in a long-term perspective. An often made narrowing and equalization of accountability with reporting is not reaching far enough, as it encloses more aspects (Quintyn,

2008). Four functions, that are derived by Hüpkes et al. (2005) and Quintyn et al. (2007), are (1) the classical filing of accounts about the agency's activity, (2) the maintenance and enhancement of legitimacy[21] as an understanding of the politics, the overseen firms and the general public that the agency's activities are well understood and, thus, supported, (3) the enhancement of integrity of the agency's governance to avoid an agency's staff intended self-interest capture, and (4) to enhance the agency's performance by preventing the agency to become uninformed, lazy, corrupt or to disguise its superfluousness (Heine & Mause, 2013).

Transparency describes a setting of the agency being transparent about its decisions, rules and frameworks, available and processed data, and its terms of accountability towards its stakeholders. At last, *integrity* encloses all mechanisms that ensure agency staff behaves in line with the institutional goals rather than self-interested.

There is empirical evidence provided by Laurens et al. (2009) of highly significant positive interdependencies between central banks independence, accountability, and transparency. The discussion about the dimensions of agency independence will refer at some points to these interdependencies.

4 Dimensions of Financial Supervision and Enforcement Authority Independence

To achieve a functional independent financial supervision and enforcement, whose necessity has been derived in section 2, the organization conducting filing review and enforcement – also referred as agency or authority –, needs to be independent in various dimensions. Prior literature used different approaches for categorizing agency independence with heterogeneous labels for each dimension. In this study, I use four different labels for dimensions of independence.

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[21]This understanding of legitimacy is not equal to the legal legitimacy that is discussed in the foregoing section.

Figure A.4 shows these dimensions relative to stakeholders from which the agency could (or frequently should) be independent from.

Figure A.4:
Dimensions of Independence
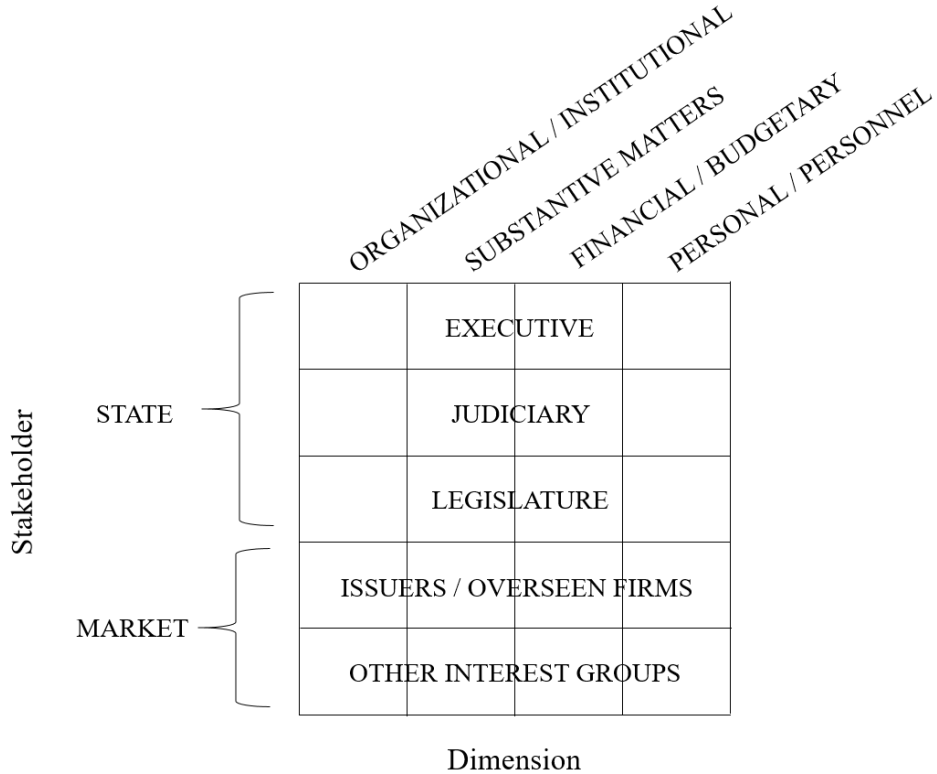
The following subsections will present these dimensions in detail, discuss dependencies from specific stakeholders and derive an optimal degree of independence. Please note that not every matrix field has to be discussed in detail, as some dependencies from specific stakeholders appear to be less problematic or nearly not existent.[22]

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[22]I.e., dependencies from judiciary typically arise from judicial review which is a core principle in democratic government states. For sure, courts could intervene in nearly every matter regarding agency's decisions, organization or funding if it is inconsistent with the constitution. This does not seem to be problematic and, thus, will not be extensively discussed further.

4.1 Organizational and Institutional Independence

Organizational and institutional independence describe independence in matters regarding the enforcement authority's establishment and abolishment, modification possibilities concerning constitution and statute, legal basis, and organizational structure. In prior literature, this dimension or at least parts of it have been denoted as institutional independence *(institutionelle Unabhängigkeit)* (Kruse, 2013; Weißgärber, 2016; Oertel, 2000; Andrae, 2012), organizational independence *(organisationsrechtliche Unabhängigkeit)* (Han, 2015; Weißgärber, 2016), structural (Verhoest et al., 2004; Jenny, 2012), policy (Groenleer, 2009) and legal (Groenleer, 2009) independence.

This dimension could be interpreted as a kind of meta-level above the further three dimensions, as it is related to nearly everything that determines budgetary/financial, personal/personnel, and independence in substantive matters (Kruse, 2013). The organizational and institutional setting of an agency, thus, is basically for the agency's ability to act independently in substantive matters (Weißgärber, 2016).

Basically, in a democracy, the setting and changing of the legal framework conditions of an agency that has governmental authority – such as enforcing capital market law – must be democratically legitimized (Kruse, 2013). The legitimization can be carried out either by the legislature, i.e., a parliament or Congress, or the executive. The establishment of a financial supervision and enforcement agency must therefore be exerted by a democratically legitimized governmental body. Nevertheless, the bodies also have the power to change the agency's legal framework conditions. Typically, majorities in the legislature and the executive change in fixed terms. For that, the legal framework has to be designed in a way that limits short-term changes in the agency's constitution that are likely to appear after a change in majorities and that could affect current investigations, supervisions or enforcement decision processes (Kruse, 2013). Several

mechanisms to protect the agency from this intervention might be imaginable. First, a waiting period for legal framework changes to become effective could be implemented in the agency's constitution (Kruse, 2013). This would hinder current majorities in the legislature or, more important, the executive to benefit from legal framework changes, as they cannot be sure about whether they are still in term when the changes become effective. Second, the requirement for an approval of a further instance regarding the changes could be implemented in the constitution (Kruse, 2013). Who might be an appropriate institution depends on the state's government. The most important condition is that also this instance is democratically legitimized, such as a directly elected President. In case of the federal governmental system in Germany, typically an approval by the Federal Council (*Bundesrat*) to acts initiated by the parliament (*Bundestag*) is demanded. In any case, the requirement for approval by a court, and thus an institution from judiciary, is unproblematic. Last, the agency's independence as a matter of fact could be integrated in the state's constitution (Kruse, 2013). This would result in higher thresholds for agency's legal framework changes, as constitutional amendments usually require a special majority. Although independence of several agencies is commonly anchored in constitutional law, this brings us full circle to the question of what independence actually means as discussed in this paper. The same considerations and arguments apply for the agency's abolishment.

To ensure independent activity, at first the authority conducting financial supervision and enforcement needs a legal personality (Groenleer, 2009). Without a legal personality, the agency might easily be abolished when political majorities change (Lewis, 2003). Contrary, it is difficult to change an agency's legal status once the agency has been founded with an own legal personality (Verhoest et al., 2004).

The foundation of a financial supervision and enforcement agency can be exerted by individual national law or constitutional law (Bredt, 2006). Like already discussed above, the

independence of the agency is enhanced if it is based on constitutional law. Not only the degree of legitimization, but also the thresholds for a current government to significantly change the agency's organizational structures due to short-term political interests, is enhanced.

To limit executive influence, it is necessary to create an entity separate from ministries (Jenny, 2012). In the US, an agency type called "independent agency" has evolved since the 1920s (Verkuil, 1988; Miller, 1986; Corrigan & Revesz, 2017). In contrast to executive branch agencies, the aim of this type is an insulation from executive control. These agency types are typically not created by executive action, but by federal law, as the executive is not likely to establish an independent agency (Lewis, 2003). Unlinke in Germany, an agency type that is gladly chosen to give some kind of autonomy to an authority is the German federal public law institution with legal capacity (*rechtsfähige Anstalt des öffentlichen Rechts*) (Han, 2015). As controversially discussed after the Wirecard scandal, this kind of agency is not necessarily independent from the executive, as major decisions of the BaFin's supervisory process need prior approval by the German Ministry of Finance or can be altered afterwards (*Rechts- und Fachaufsicht*) (Kaufhold et al., 2021).

Regarding the agency's organization, the hierarchical and governance structure is important for several reasons. The degree of independence is lower in case the agency is managed by a single person, e.g., a President, instead of a board that decides cooperatively (Kruse, 2013; Bredt, 2006). Multi-member commissions ensure continuity and consistency in the decision-making process, as one individual being influenced by external stakeholders is not able to make decisions alone (Quintyn et al., 2007). In enhancing independence of a multi-member commission, agency heads should be nominated in staggered terms and by different institutions (Bredt, 2006; Kruse, 2013). For instance, at the SEC, commissioners serve a five-years term that is staggered so every

year there is one commissioner's change. Presidents, thus, are usually not able to nominate an absolute majority of agency heads during their tenure (Bredt, 2006).[23]

A further aspect, that is sometimes considered as an individual dimension, is an agency's policy autonomy (Verhoest et al., 2004; Groenleer, 2009). This aspect encloses the agency's possibility to make decisions about its policy goals by itself, decisions about policy instruments as well as its target audience (McNamara, 2002; Verhoest et al., 2004; Groenleer, 2009). The ability to make policy related decisions without direct intervention of external stakeholders has to be delimited from the independence in substantive matters (see the following subsection). The main difference is that policy independence only requires a fixed definition of the agency's overall objective, but the way it is reached lies in the agency's responsibility. Independence in substantive matters does not necessarily require policy autonomy. A hazard of an agency being autonomous regarding its policy is a self-extension of competencies beyond its originally intended function (Heine & Mause, 2013).

As already discussed in section 3, an agency's statutes should require a specific degree of transparency (Jenny, 2012; Quintyn, 2008) and accountability (Quintyn et al., 2007; Quintyn, 2008) in the decision-making process (Jenny, 2012). Being transparent about decisions, they could be scrutinized both by state and market stakeholders which lowers the risk of political influence (Quintyn et al., 2007; Quintyn, 2008).

Regarding market stakeholders like issuers and other interest groups, further possible dependencies in organizational and institutional matters are rare. A problem arises when oversight authorities are not purely public, but at least partly private, as it had happened with the German FREP. Those agencies are likely to consist of mainly private interest groups that staff committees or boards which tend to represent private group's interests (besides general legitimization

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[23]Note that this staggered-term nomination is not effective in case of commissioners' retirements. Piering (2024c) exploits consequences of one exception for the Trump's presidency when the President was able to nominate a majority of commissioners within one year, supported by a Republican dominated Senate.

problems) (Heine, 2008). In these cases, two main mechanisms need to be established. First, the statutes – with respect to the considerations of policy independence – should limit membership conditions. For instance, individual companies as well as external auditors were not allowed to become regular members of the association. Only representations by significant interest groups were possible (DPR, 2009). Second, decisions of those agencies – especially in enforcement context – should not get a generally valid legitimization, but need to require individual consent by a public authority, such as it had been implemented for the German FREP.

4.2   Independence in Substantive Matters

Independence in substantive matters denotes a condition that no other entity, regardless of whether public or private, can exert influence on the agency's decisions (Bredt, 2006; Groß, 2014). In prior literature, this dimension or at least parts of it have also been denoted as policy independence (Groenleer, 2009; Verhoest et al., 2004)[24], substantive independence *(inhaltliche Unabhängigkeit)* (Kruse, 2013), functional independence *(sachliche Unabhängigkeit)* (Bredt, 2006; Siekmann, 2005; Weißgärber, 2016), functional independence *(funktionelle Unabhängigkeit)* (Siekmann, 2005; Weißgärber, 2016) and material independence *(materielle Unabhängigkeit)* (Weißgärber, 2016). Following Kaufhold et al. (2021), I denote this dimension of independence as those in substantive matters *(sachlich-funktional)*.

The dimension in substantive matters refers to the right to directly influence the decision making (*Primärentscheidungsrechte*) in supervision, e.g., filing review, and enforcement actions, and has to be differed from decisions regarding personnel and the delegation of tasks to the agency (*Delegationsentscheidungen*) (Kruse, 2013; Andrae, 2012).

The most important point in this context is the agency's instruction autonomy meaning that the government – particularly the executive – is forbidden to give any instructions (Jestaedt,

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[24]Please note the remarks regarding policy autonomy in the foregoing subsection.

1993). This does not preclude the submission of arguments and non-binding advice (Kruse, 2013). In case the political institutions had a right to authorize reservations or to verify agency's decisions, the independence in substantive matters would also be massively cut (Kruse, 2013).

A problem that is arising with independence in substantive matters is how agency's decision making process is reviewed to avoid negative consequences from too-independent agencies, such as a protection of redundant agencies or an extension of competences by themselves (Heine & Mause, 2013). The question is whether, how and from whom the agency's execution of the predefined tasks should or could be monitored.

One negative example for too far-reaching supervisory powers is the oversight on the legality and appropriateness of the German BaFin's decisions (*Rechts- und Fachaufsicht*) by German Federal Ministry of Finance (Kaufhold et al., 2021). Following the supervisory principles of the German Federal Ministry of Finance over the BaFin, the Ministry intends to effectively control the activity of the BaFin (Hermes, 2010). The close link between BaFin and the Ministry became obvious in the time of the failure of Wirecard. The procedure of the BaFin investigation seemed to be in close consultation with the German Federal Ministry of Finance as the ministry requested several reports from the BaFin and the BaFin reported at least 20 times to the Ministry (German Federal Ministry of Finance, 2020). Nevertheless, the European Securities and Markets Authority (ESMA)'s Peer Review Committee did not identify any evidence on the Ministry to influence BaFin on any actions to take in that case (ESMA, 2020).

In contrast to that, in the US, the SEC is insulated from executive control in substantive matters. The oversight belongs to specific congressional committees and, hence, to the legislature. An executive intervention would be a clear case of violating the separation of power principle (Strauss, 1984). A general conviction, thus, is that agency's activities are controlled only by the courts (Kaufhold et al., 2021).

In contrast to state and political institutions, possibilities for market participants to directly influence agency's decisions seem to be rare. Any attempt would be classified as corruption.

4.3 Budgetary and Financial Independence

Budgetary and financial independence describe independence in funding and spending of monetary matters. Prior literature denoted this dimension as financial *(finanzielle)* (e.g., Groenleer, 2009; Weißgärber, 2016; Kaufhold et al., 2021; Groß, 2014) or budgetary independence *(budgetäre Unabhängigkeit)* (e.g., Kruse, 2013; Han, 2015; Quintyn et al., 2007) interchangeable. Nevertheless, mixing up these terms is inaccurate as they are closely linked either to funding (financial) or spending (budgetary). Enforcement agencies' activities are bounded by their financial resources and the possibility to decide about their use (Groenleer, 2009). The behavior of an organization, namely an enforcement agency, can be influenced by the budgeting system (Covaleski & Dirsmith, 1986).

The two important points in that context creating dependencies are about who is able to decide about the agency's budget and spendings and how the agency is generating its financial resources. It is worth mentioning that both points interact on a high level.

Independence in budgetary matters refers to the agency's ability to decide about the size and spending of the own budget (Quintyn et al., 2007; Groenleer, 2009) and specific allocation and priorities within the budget (Quintyn et al., 2007). This independence could be granted either absolutely, meaning the agency's principal has no option to decide about any issues in budget, or relatively, meaning the principal once decides about a basic amount of budget when creating the agency, but later on it could only be altered on the basis of previously defined criteria (Andrae, 2012). Even the relative independence would hinder a principal from putting politically motivated pressure on the agency. If these external budgetary decisions are made on a yearly base the grade of independence is higher compared to task or project related funding

appropriations (Bredt, 2006). The dependency in budgetary matters from a (political) principal limits the agency's independence for several reasons, especially when the principal puts pressure on the budget (Quintyn et al., 2007). Executives could threaten to withhold or reduce funding if the enforcement agency is too strict against politically linked issuers (Quintyn et al., 2007). For instance, SEC funding is highly dependent on political considerations (Bealing, 1994). Congressional budget setting in the past had been used to ensure that the SEC staff behaved in line with political preferences, although their work was not monitored on a daily base (Weingast, 1984). In cases when the output performance of agencies is the key indicator for their successful work, like for financial supervision and enforcement, budget constraints can have negative implications to the agency's performance. For instance, the SEC's enforcement often targets companies that are closely related to an SEC office and is specially conducted in cases where there is already high expertise within the agency to save resources (Kedia & Rajgopal, 2011; Gadinis, 2012), whereas enforcement actions against complex, multinational companies appear to be avoided (Langevoort, 2006).

Budget might also be cut during cost-saving measures (Quintyn et al., 2007), although these times especially require strong balance sheet control and enforcement. The SEC was underfinanced at some time not being able to adequately fulfill the filing review, as the Congress did not get the SEC's budgetary necessities (Seligman, 2004).

Additionally, limited budget could restrict attractive salaries for competent staff (Quintyn et al., 2007).

A possible way to reduce dependencies from one specific stakeholder in budgetary matters is a share of right to say regarding the agency's budget (Bredt, 2006). In that case, budget could be proposed and justified by the enforcement agencies based on objective criteria (Quintyn et al., 2007).

A last point that has to be addressed in the context of budgetary independence is the allocation of profits. In some kinds of institutionalization, the agency is able to generate profits and might be obliged to transfer it to its principals. This seems to be problematic in case the maximization and transfer of profits is one target of the agency given by its principals (Andrae, 2012). Thus, profit transfer is not problematic in case profit is not an agency performance measure.

An agency's financial independence addresses some further points regarding funding. In general, agencies that generate own funds – in distinction to a reliance on public or state resources – are basically less dependent on governmental and political principals (Pfeffer & Salancik, 1978; Bredt, 2006). From governmental view, these institutions have associated costs that include salaries, allowances and office expenses. These costs can place a heavy burden on the national budget, particularly in countries with notably limited financial resources (Bulmer, 2019). A possible way to create own funds is a levy on issuers (Quintyn et al., 2007). Those fees could be designed like general charges for the agency when participating in a financial market and could be measured, for instance, by company size. However, fee-based funding is under pressure when the industry is in trouble. A possible solution for this issue is to allow the agency to build up reserve funds (Quintyn et al., 2007). A further conceivable funding could be based on penalties for rule violations. However, this type of financing could arise further dependencies as funding-related considerations might affect review and enforcement decisions.

4.4 Personal and Personnel Independence

Personal and personnel independence describe independence of agencies' staff and heads from other stakeholders (personal) as well as regarding recruitment and qualification of agencies' staff and heads (personnel).

Prior literature denoted this dimension as personnel *(personelle)* (Groenleer, 2009; Han, 2015; Oertel, 2000; Bredt, 2006) or personal independence *(persönliche Unabhängigkeit)* (Kruse, 2013; Kaufhold et al., 2021; Andrae, 2012).

The most important point in the context of personnel is the appointment and removal of agency heads. In contrast to direct intervention in an agency's decisions, the possibility to influence the agency in substantive matters indirectly by the appointment and removal of agency heads at will is of limited transparency towards the public (Kruse, 2013). In case politicians could nominate agency heads directly without further requirements, this would substitute an absence of politicians' possibility to influence in substantive matters (Kruse, 2013). Thus, it would be appropriate to split the right of appointment between two parties (Kruse, 2013; Andrae, 2012). For instance, in the US, the nomination of the SEC's commissioners is split between the executive (President) and the legislature (Senate), which is sometimes considered as the best mode of appointment (e.g., Quintyn et al., 2007). Whereas the President appoints the Commissioners, the Senate is entitled to advise and consent to this nomination (SEC, 2023b). There is anecdotal evidence that this system actively prohibits the President to nominate Commissioners just by his preferences, especially when the legislature is dominated by the opposite party (Karmel, 2016b).

The split between two political institutions is only effective in the case of checks and balances, but not in a parliamentary system, where the legitimization of the executive is based on the election of the legislature, e.g., the parliament (Andrae, 2012). Especially in these cases, other nominating mechanisms need to be established. Various options are conceivable: Firstly, a random selection by lot (Andrae, 2012). This would ensure the greatest independence of the selected ones, but it might lead to a lack in functionality if the potential candidates were not chosen wisely. Secondly, a nomination committee where either agency members have a say in appointments (Bredt, 2006) or an external institution that is independent from the politics has.

This idea clashes with the fact that the agency, especially when enforcing accounting standards, executes state power. So far, this mechanism misses a sufficient democratic legitimization. Thirdly, a split between two different institutions, from which at least one is democratically legitimized (Andrae, 2012). The other institution should be independent from political influence and might introduce a kind of rotation within its members, so there is a systematic change between influential institution (Kruse, 2013). This idea balances the necessity of legitimization with the impossibility of one institution to appoint the agency's heads by its will. Nevertheless, the nomination committee might be the connecting point for the regulated firms, thus the issuers or other interest groups, to take influence on the agency's staffing.

The removal conditions are of particular importance (Bredt, 2006; Quintyn et al., 2007). In case agency heads were removed at will by politicians, the agency would be likely to be captured by short-term political interests. Fixed terms of agency heads guarantee that they are not easily dismissed by politicians (Lewis, 2003). Nevertheless, there might be circumstances of a too large degree of independence that has negative consequences, e.g., that agency heads expand their competencies by themselves (Heine & Mause, 2013). To protect the public from any agency wrongdoing, specific terms of agency heads removal might be defined by law. It becomes problematic if these terms are not precisely defined. For instance, the US President is entitled to remove the SEC's chairman in case of inefficiency, neglect of duty, or malfeasance in office (Manners & Menand, 2021; Sunstein & Vermeule, 2021; U.S. Supreme Court, 2010). Nevertheless, these terms have never been specified by law and, hence, a commonly accepted definition is non-existent (Lessig & Sunstein, 1994). Thus, the conditions under which the President is actually entitled to remove agency's heads are unclear. H.L.R. (2013) concludes that SEC commissioners are removable at the President's will. Piering (2024b) assumes that these uncertainties regarding removal conditions let the SEC's heads behave in line with the

President's will. Another possible way to secure the public from misbehavior that is granting the greatest independence is to properly set out in law removal conditions and let the courts decide about (Kruse, 2013).

Further aspects that enhance agency independence in personnel matters are the ability to recruit and dismiss staff by their own (Keohane, 1969; McNamara, 2002), the freedom to train and pay own staff (Groenleer, 2009) and that staff and agency heads do not need to be accountable against the government (Keohane, 1969).

In contrast to personnel independence, Bredt (2006) states that personal independence means agency staff can make decisions without the fear of personal disadvantages. Additionally, this term seems to entail that agency staff makes no decisions in the prospect of personal benefits. That said, personal qualifications like professional expertise or personal experiences of agency heads are important (Kruse, 2013). This point interacts with the appointment mechanisms and is from greater importance when agency heads are appointed by politicians directly.

Personal dependencies of agency staff with issuers or other interest groups can arise in the context of career concerns. Agency staff is likely to work for companies that they had overseen before as well as for other interest groups after their agency term. This so-called "revolving door" phenomenon can be observed in several countries (Frach, 2007). This could be problematic for several reasons. Firstly, the staff can behave favorable against specific firms considering their personal career opportunities. Secondly, overseen firms can benefit from the employment of prior staff. For instance, Correia (2014) provided evidence that firms that employ lobbyists who have prior worked for the SEC have a lower likelihood to be targeted by enforcement actions and face lower penalties in case it was targeted. One possibility to enhance independence in that case is to introduce a "cool-down" period (Andrae, 2012). This means that staff is forbidden to be employed by firms they had previously overseen for a specific number of years. Another

possibility is to prolong the staffs regular terms, i.e. until their regular retirement age or, in the most extreme variant, for lifetime (Kruse, 2013). This has to be considered directly related to removal conditions to ensure the agency works effectively.

In case agency heads terms are limited, the question whether they could be re-appointed gets meaningful against the backdrop of personal independence. The consequences are two-fold and closely related to what has already been discussed above. On the one hand, the prohibition of a re-appointment would release agency heads from a dependency on the appointing institution to behave in line with their interest. On the other hand, this could support a closer bond to the overseen firms due to career concerns (Andrae, 2012).

Finally, the personal independence of agency heads and staff is dependent on their direct or indirect connections to the overseen firms. These would likely lead the staff to maximize their personal benefit. Possible connections are, beside others, supervisory board mandates or stock ownerships. Regarding the prior German FREP President Edgar Ernst, the ESMA stated that board members should not be allowed to exercise any supervisory board mandates (ESMA, 2020). Moreover, as discussed in the context of the Wirecard failure, BaFin staff were forbidden to privately trade any equities or bonds (Art. 4 Financial Market Integrity Strengthening Act (FISG)). As there is no reason for these ties, they should be prohibited.

4.5 Visualized Results

This section provided an overview of the four dimensions of financial supervision and enforcement agency's independence and critical dependencies from external stakeholders under each dimension. Figure A.5 visualizes the discussion's results on the prior derived matrix. The colors label whether these dependencies are unproblematic (green), should be avoided (red), or need a more differentiated discussion (yellow), as derived in prior subsections.

Figure A.5:
Heatmap: Visualized Results
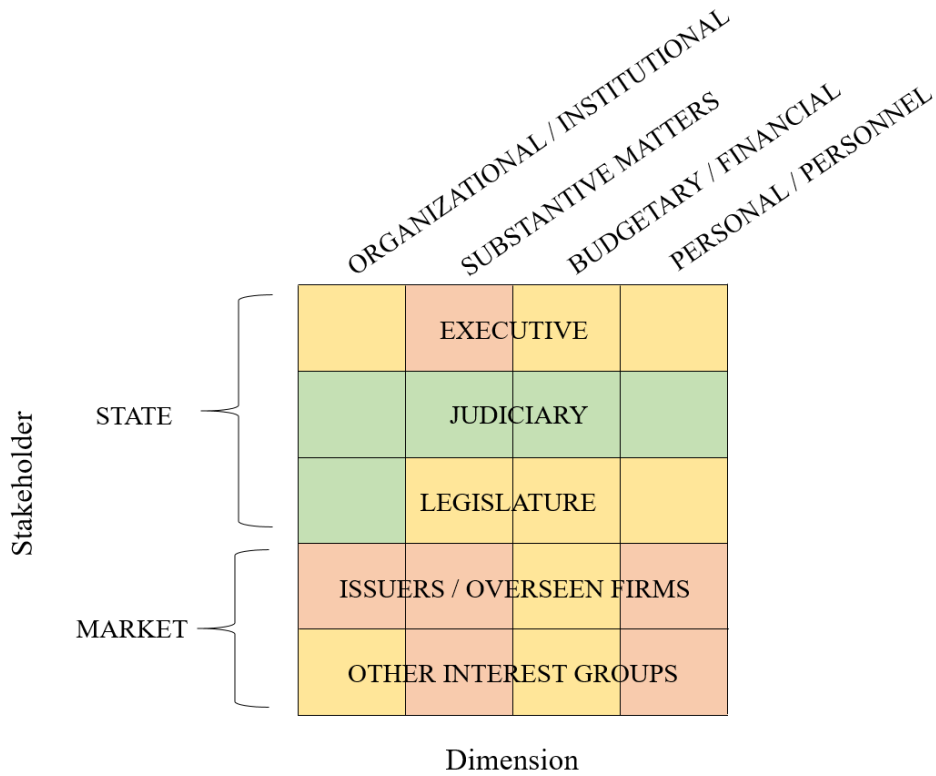
Figure A.5 shows summarized results of section 4 in the manner of a heatmap. Green boxes show stakeholder-independence-dimension combinations that are unproblematic. Red boxes stand for combinations that should be avoided. Yellow boxes label stakeholder-dimension combinations that need deeper insights, more differentiated discussion and which threats are context-dependent.

In relation to state stakeholders, a main issue on dependencies from the executive is their politicians' very short-term interest. Politicians tend to influence agency behavior in a way that secures their re-election. As a consequence, an oversight authority needs to be mostly insulated from executive influence – especially in systems where the executive derives its democratic legitimization indirectly. Dependencies from legislature in general appear to be less problematic conditional to an effective control mechanism, at the best, by judicial review. As a core concern about independent agencies is their democratic legitimization, an authority being

fully independent from state stakeholders is, beside further reasons, because of this consideration impossible.

Furthermore, special attention needs to be paid on dependencies from market stakeholders. In general, there is little need to establish an agency dependent from this group. Defensible links might result from agency funding in case of a levy or interest groups' memberships.

5   Summary and Conclusion

The independence of financial supervision and enforcement agencies has long been discussed in various situations and times. Political discussion as well as research on agency independence often suffer from a limited point of view that does not cover all aspects and dimensions of agency independence. This paper presents a novel categorization of financial supervision and enforcement agencies' independence developing a matrix that shows the four dimensions of independence relative to all possible agency stakeholders. The discussion shows that a narrowed view only on dependencies from the government or politics, as often made in literature, does not contribute to the special agency relation of financial supervision and enforcement authorities. A view-extension on the contractual relationship with market stakeholders like overseen firms or auditors is necessary to ensure an financial supervision and enforcement agency can work without undue influence in its intended way. The developed matrix opens 4x5 possible dependency-stakeholder-combinations, whereas not every of these have been discussed in detail. The elaboration of an extensive literature overview and the provision of empirical evidence where missing are future research opportunities.

Part B:

Was the Clayton SEC captured?
– Evidence from Political Connections and SEC Comment Letters

Abstract

There is a public interest in the SEC's mission to ensure fair markets and to protect investors. Special interest groups take actions to influence the SEC seeking gain from beneficial treatment, thus to capture the SEC. There is anecdotal evidence that the SEC's behavior is strongly dependent from the commissioners' composition and the chairman's personality. This paper applies the model provided by Carpenter (2014) to evaluate whether the SEC was captured during the Jay Clayton chairmanship (2017-2020) respectively whether capture was more effective during this time. I find firms maintaining political connections in general are more likely to receive a comment letter which is contrary to suggested SEC capture. This effect is more pronounced during Clayton's chairmanship. The findings contribute to the literature on SEC capture providing first evidence on the effect of significant changes in the Commission on SEC policy.

1 Introduction

The United States Securities and Exchange Commission (SEC) has been established as an independent agency by the Congress through the Securities Exchange Act of 1934 (SEA) after the stock market crash of 1929. As regulators see a public interest in fair and orderly securities markets (SEA SEC. 2; ITSFEA SEC. 7 (a) (4)), Congress delegated competencies to the SEC. It equipped the Commission with enormous power to ensure that investors are provided with material information (e.g., by reviewing initial and regular corporate filings by the Division of Corporation Finance (DCF)) and sanctioning securities laws violations (e.g., by issuing Accounting and Auditing Enforcement Releases (AAERs) by the Division of Enforcement (DoE)). This financial supervision and enforcement must be carried out independently from external stakeholders to work effectively (e.g., Piering, 2024a). Regulatory capture theory (e.g., Stigler, 1971; Peltzman, 1976) suggests that special interest groups take specific actions to achieve favorable treatment by bureaucratic agencies. The efficacy of these actions depend on the agency heads' composition and might change after commissions' adjustments (Keyser, 2023). Regarding the SEC, firms contribute to Congressmen that can intercede with the SEC in order to benefit from special treatment (e.g., Correia, 2014). Prior research found indistinct results supportive (Gadinis, 2012; Yu & Yu, 2011; Correia, 2014; Mehta & Zhao, 2020; Fulmer et al., 2022) or inconsistent (Blackburne, 2014; Khokhar & Shahriari, 2022; Heese et al., 2017; Seitz & Piering, 2024; Thompson, 2022) with SEC capture. Nevertheless, making fundamental conclusions about the entire SEC being or not being captured based on this literature is not recommendable for two main reasons. First, the SEC's duties are very extensive and distributed over six divisions (SEC, 2022). Their tasks, underlying internal structures and processes, and their real effects on stakeholders such as special interest groups differ widely. Even SEC oversight

consists of enforcement as well as selective filing review (Heese et al., 2017; Khokhar & Shahriari, 2022). SEC capture research, thus, is always limited in its statement to the SEC's division whose outcome (e.g., AAERs or comment letters) is being examined as the dependent variable. Second, research on regulatory capture frequently suffers from associations and correlations pointed out representing other patterns beside regulatory capture (Carpenter, 2014).

In the first part of this two-fold paper, I use a framework designed by Carpenter (2014) to provide evidence on SEC capture with respect to the DCF on a proper basis. The 3-step-model which is central in this framework requires (1) a clear derivation of the public interest in an agency's regulation, (2) actions taken by special interest groups to induce the agency to prefer special over public interest, and (3) a policy shift from public to special interests. In the second part, I investigate whether significant changes in the SEC's commission lead to more or less pronounced DCF capture.

Firstly, I derive a public interest in the SEC's supervision from the goals the Congress set when creating the SEC (SEA) and expanding its scope (Insider Trading and Securities Fraud Enforcement Act of 1988 (ITSFEA), Sarbanes-Oxley Act of 2002 (SOX)), from the SEC's mission it has given itself, as well as relevant literature. Although prior research mainly examines enforcement actions to investigate SEC capture (Yu & Yu, 2011; Gadinis, 2012; Correia, 2014; Khokhar & Shahriari, 2022), I use firms' likelihood to receive a comment letter on their 10-K as a proxy in line with Heese et al. (2017) to observe SEC supervision activity as many of prior research using enforcement data may suffer from small sample bias (Heese et al., 2017; Khokhar & Shahriari, 2022).

Secondly, I observe firms' lobbying expenditures and Political Action Committee (PAC) contributions as indicators of special interest groups' actions. Firms typically establish political connections in order to exert influence on SEC policy. These connections are frequently measured

by firms' lobbying expenditures (Yu & Yu, 2011; Correia, 2014; Heese et al., 2017) as well as their contributions to PACs (Snyder, 1990; Milyo et al., 2000; Cooper et al., 2010; Khokhar & Shahriari, 2022).

Thirdly, a policy shift would be indicated by a significant change in SEC supervisory behavior against politically connected firms. I find a significantly positive relation between firms' lobbying expenditures and their likelihood to receive a comment letter on their 10-K in general. A slightly positive, but less significant relation is also observable for PAC contributions. These findings are supportive to those of Heese et al. (2017). In contrast to prior research contributing to the idea of SEC capture (especially Correia (2014)), Heese et al. (2017) conclude that the role of firms' political connections in SEC oversight is more nuanced. Some research interprets these findings in the light of the political cost hypothesis where politicians intervene in SEC policy balancing special interest groups and voter's support in order to avoid voter backlash (e.g., Khokhar & Shahriari, 2022). An alternative interpretation might be that the SEC is robust to political influence and, thus, campaign contributions and lobbying expenditures with the aim of influencing SEC supervision are ineffective. On the other hand, firms' political connections might, for instance, indicate specific risks that regulators might pay attention to. Heese et al. (2017) assume that political connections attract SEC attention which is contrary to SEC capture. Recent studies providing further insight into the role of firms' political connections on the SEC decision making process support this conclusion. They show increasing SEC monitoring activity (Seitz & Piering, 2024) as well as a decreasing likelihood of a confidential treatment order being approved after internal scrutiny (Thompson, 2022) for politically connected firms. Following the assumption that legislators likely prefer stricter scrutiny of PC[25] firms (Thompson, 2022; McCubbins & Schwartz, 1984), my findings corroborate the view that the SEC is acting in the public interest rather than special interests regarding its supervision.

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[25]"PC" in the following abbreviates "political connections" respectively "politically connected".

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Along this general finding of the SEC's filing review not being captured over a long term, serious doubts may arise whether the ability of interest groups to influence the SEC's supervision depends on the composition of the SEC's commissioners and its chairman. Although the independence of financial regulation agencies like the SEC has long been regarded as a core aspect, a policy makers' paradigm shift towards more politically controlled officials has been observed since the financial crisis of 2007/2008 (Gadinis, 2013). The question of the commissioners' identities is highly relevant as these officers are responsible for agenda setting, establishment of budget priorities and substantive decisions regarding policy and regulative procedures (Breger & Edles, 2015; Fischer, 2008). Prior research, for instance, provides evidence that professional and political characteristics of SEC commissioners are reflected in the extent of reliability vs. relevance of accounting standards exposure drafts (Allen & Ramanna, 2013). The former SEC commissioner Roberta S. Karmel reports on a "poisonous partisanship" that threatens the SEC's independence since Obama's presidency (Karmel, 2016b). She depicts the commissioner candidates' qualifications are based on ideological correctness rather than expertise and, thus, the SEC has become an agency riven by partisanship instead of a collegial agency of non-partisan experts (Karmel, 2016b). This kind of partisanship might distract the SEC from its core mission (Schoeff, 2015). Nevertheless, the question whether the presumed loss of independence regarding politicians results in a significant adjustment of SEC policy in temporal proximity to President changes is ambiguous. On the one hand, Presidents are typically not able to quickly appoint a majority of commissioners, as opposition-party commissioners are not loyal to the President, but committed to the opposition party's agenda (Devins & Lewis, 2008). Thus, holdovers from prior administrations improve the agency's independence (Morrison, 1988). The commissioners' staggered terms expiry secures that the SEC's policy is hedged (Fischer, 2008; Datla & Revesz, 2013; Phillips, 2023). Additionally, this structure ensures that the majority of commissioners

must be captured rather than just one individual (Bressman & Thompson, 2010). On the other hand, there is anecdotal evidence on the placement of commissioners that believe in a special – likely the United States (US) President's – way of government, regardless of whether they are Democrats or Republicans (Morrison, 1988). Moreover, it is unlikely to conclude that the power between the commissioners and the chairman is balanced. The Reorganization Plan No. 10 of 1950[26] transferred power over personnel appointment and supervision, the distribution of business as well as the use of funds from the commissioners to the chairman. Thus, there is almost unrestricted power of the chairman over the Commission, whereas the other commissioners only have little influence (Burton, 2019). Phillips (2023) characterizes this kind of agency governance as Strong-Chair model. There is anecdotal evidence that the SEC's policy and actual activity is strongly dependent on the chairman's personality (Phillips & Zecher, 1981). In 2017, when Donald Trump's presidency begun, there were significant changes within the SEC's commission. First, the Chair had to be reappointed after Mary Jo White, serving as the chairman under Obama's second presidency, announced her resignation (Das & Wolff, 2016). The subsequent chairman, Jay Clayton, had been described as "a 180 from Chairman Mary Jo White" (Michaels & Hoffman, 2017) and was, ex-ante, expected to support large firms to raise capital in public markets instead of tightening regulation (Picker, 2017), which was granted by these firms (Antilla & Rivlin, 2018). Second, two further seats had been vacant since the end of 2015. As the Senate was dominated by the Republicans during that time, also these assignments could have been made by Donald Trump's favor. For that, contrary to the idea of staggered terms, three posts were to be nominated from January 2017 on (Das & Wolff, 2016).[27]

Prior research shows that significant changes in a board's senior staff or agency's heads could increase the susceptibility to regulatory capture (e.g., Keyser, 2023). Thus, it is questionable

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[26]5 U.S. Code, Appendix, "Reorganization Plan No. 10 of 1950".
[27]For a visualization of the SEC's commission composition, see Appendix B.B.

whether the changes in the SEC's commission even let the agency to be captured. In the second part of this paper, I investigate whether a shift in financial supervision towards special interests of politically connected firms is observable during the Clayton chairmanship.

I find a generally lower comment letter receipt likelihood for the Clayton chairmanship, as the overall number of initiated comment letter cases became lower. Additionally, the complexity of each case decreased. Whereas political connections increase comment letter receipt likelihood in general, I find that this effect is more pronounced during the Clayton chairmanship for firms' lobbying expenditures, while there is no statistical significant difference for PAC contributions. This evidence indicates, contrary to prior conjectures, that there is no hint of the SEC conducting financial supervision less independent during Clayton's chairmanship and, thus, the Clayton SEC does not seem to be captured. On the other hand, there is a significant change in financial supervision observable as firms' lobbying activities increase comment letter receipt likelihood more strongly. Taking into consideration that the SEC's divisions act semi-autonomous and the DCF is clearly structured with extensively reviewed and monitored processes (Katz, 2010), this observation might result from the DCF's heads' awareness of potential capture by PC firms and thus an enhancement of financial supervision against these firms.

This paper contributes to the literature on regulatory capture in three ways. First, it validates the findings of Heese et al. (2017) for another time frame and other political and economical circumstances. Second, it sets research on SEC capture into a proper theoretical framework by applying the model of Carpenter (2014) on SEC filing review. Third, it sheds light on the SEC oversight policy dependency on the commission's composition and changes that come along with disruptions in its composition by providing empirical evidence.

The remainder of this paper proceeds as follows: Section 2 provides background information on the SEC's mission, regulatory capture theory and evidence on SEC capture. Section 3 deploys

the Carpenter (2014) framework on SEC filing review and outlines the research design. Section 4 explains about the data and shows descriptive statistics. In section 5, I discuss the empirical results regarding the general investigation of SEC capture, whereas section 6 discusses the impacts of the commission's composition changes on SEC policy and financial supervision behavior. Section 7 concludes and presents future research options.

2   Background

2.1   Mission of the SEC

The SEC was established in 1934 as a final consequence of the stock market crash of 1929 after long-time market abuses reached their peak in the 1920s (Skousen, 1991). Prior state laws had proven to be ineffective, thus a conviction of federal regulation necessity was growing (Lasser & Garardi, 1934). The Congress created the SEC with the SEA and stated its mission in Sec. 2 as follows: *"(...) regulation and control [of security transactions] and matters related thereto (...), to require appropriate reports, to remove impediments to and perfect the mechanisms of a national market system for securities and a national system for the clearance and settlement of securities transactions and the safeguarding of securities and funds related thereto, and to impose requirements necessary to make such regulation and control reasonably complete and effective, in order to protect interstate commerce, the national credit, the Federal taxing power, to protect and make more effective the national banking system and Federal Reserve System, and to insure the maintenance of fair and honest markets in such transactions(.)"*

In 1988, the Congress made some additional provisions on the SEC's mission with the ITSFEA (Sec. 7 (a) (4)): *"(...) maintaining fair and orderly securities trading, assuring the fairness of securities transactions and markets and protecting investors."*

The SEC itself derives its mission from these Acts and refers to it as *"protecting investors, maintaining fair, orderly, and efficient markets, and facilitating capital formation"* (SEC, 2023a). Like those federal securities laws it oversees, the three-part mission addresses both companies offering securities for sale as well as securities traders (SEC, 2023e). A core principle of the SEC's mission is to ensure that issuers tell the truth about their business and traders treat investors fairly and orderly (SEC, 2023d). In order to fulfill these tasks, the SEC is – beside others – empowered to enforce securities laws and to selectively review public companies' disclosures to ensure that investors are provided with material information.

2.2 Regulatory Capture Theory

There is no generally accepted definition of regulatory capture existent, as many theories lack in specific points (Posner, 1974; Carpenter & Moss, 2014). In a common understanding of regulatory capture, regulatory agencies are (successfully) targeted by firms they regulate to act in line with their preferences (Stigler, 1971; Posner, 1974; Carpenter, 2014). The agency-enacted regulation has to be distinguished from those conducted by legislature (Posner, 2014). Regulatory agencies are typically established by the Congress when public interests in specific economic fields are potentially harmed by special (private) interests (Keyser, 2023). As the Congress delegates responsibilities to regulatory agencies, a principal-agent-problem arises. To solve this dilemma, monitoring systems are typically implemented, such as congressional oversight, nomination competencies or budget appropriation mechanisms, which are intended to make the agency act in line with its mission (*Congressional Dominance Theory*, Weingast, 1984; Weingast & Moran, 1983; McCubbins, 1999). Special interest groups can support politicians' re-elections, e.g., by contributing to a Political Action Committee or by lobbying. In exchange of favor, politicians are likely to put pressure on a regulatory agency in line with their supporters' interests (*Regulatory Capture Hypothesis*, Stigler, 1971; Peltzman, 1976). Political connections

are typically long-termed (Grossman & Helpman, 1994). Nevertheless – as voters are aware of potential political favors – politicians have to take care on voter backlash if their provision of special favors is too extensive (*Political Cost Hypothesis*, Watts & Zimmerman, 1978). Thus, Congressmen probably have to find a balance between favoring special interests and voter support (Heese et al., 2017; Heese, 2019).

The interactions and exchanges of favor between regulatory agencies, regulated firms respective special interest groups and the Congress are shown in the *Iron Triangle* relation (Freeman, 1965; Adams, 1982).

2.3 Evidence on SEC Capture

The idea of regulatory capture was applied on the SEC by prior research. Most literature suggests that firms use political connections to Congressmen and Executives to gain beneficial treatment. The underlying mechanism assumed by this research is that Congressmen – especially those serving on an SEC oversight committee – have budgetary control, oversight authority and nomination competencies regarding commissioners.[28] Prior literature – providing anecdotal and empirical evidence – finds non-uniform results supportive (Gadinis, 2013; Yu & Yu, 2011; Correia, 2014; Mehta & Zhao, 2020) or inconsistent (GAO, 2013; Blackburne, 2014; Khokhar & Shahriari, 2022; Heese et al., 2017; Seitz & Piering, 2024; Thompson, 2022) with SEC capture.

Yu & Yu (2011) found that lobbying firms have a significantly lower hazard rate for fraud detection. However, their investigation bases on a sample of companies that have been subject to lawsuits, and therefore covers SEC activity only marginally. A direct link between PC firms and the SEC was investigated by Correia (2014). She found that PC firms are less likely to be targeted

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[28]The banking committees (United States Senate Committee on Banking, Housing, and Urban Affairs; United States House Committee on Financial Services) oversee the SEC. The United States Senate Committee on Commerce, Science, and Transportation oversees securities issues. The United States House Committee on Energy and Commerce oversees accounting issues. The appropriations committees (United States Senate Committee on Appropriations; United States House Committee on Appropriations) decide on appropriations.

by an SEC enforcement action. Additionally, firms contributing to PACs and lobbying directly to the SEC face lower penalties if prosecuted. Correia (2014) concludes that firms use long-term political contributions in exchange for favors in regulation, here lower level of enforcement actions, which is in line with Snyder (1990). Contrary, Khokhar & Shahriari (2022) find that firms with stronger political connections are more likely to be criminally charged and imposed fines are relatively higher for these firms. They control for party-depending contributions which are relatively higher for the Republican party. Khokhar & Shahriari (2022) conclude that SEC enforcement is not captured by PC, but consider their results as supportive to the political cost hypothesis (Watts & Zimmerman, 1978).

Instead of enforcement outcomes, Heese et al. (2017) investigated the effect of a firm's PC on comment letter reviews. They found a positive relation between PC and comment letter reviews. Firms with PAC contributions and lobbying expenditures are more likely to receive a comment letter on their 10-K. They infer that SEC oversight – different from previous assumptions – is not captured by a firm's political connections, but rather the relation between the SEC and PC firms is more nuanced. Heese et al. (2017) argue that a firm's political connections might proxy for risk indicators regarding financial reporting and, thus, SEC oversight seems to be effective instead of lax due to capture. Heese et al. (2017) provide another potential explanation for their results namely that only the DoE is captured, but the DCF is not. Further research uses measures different from AAERs or comment letters to investigate the role of a firm's political connections on SEC activity. Seitz & Piering (2024) observe SEC EDGAR downloads proxy for cross-divisional monitoring activity. They find that PC in general increase SEC oversight. This finding is supportive for Heese et al.'s (2017) suggestion that PC proxy for financial reporting risk and SEC oversight is effective. Thompson (2022) investigates whether the SEC is more likely to approve confidential treatment orders of politically connected firms. They find that the

SEC is more likely to reject PC firms' confidential treatment orders after internal scrutiny into the confidential treatment process.

3   Capture Detection Framework

3.1   Public Interest in SEC Financial Supervision

To provide a proper diagnosis of regulatory capture, Carpenter's (2014) model of measuring agency capture requires demonstrations of three main conditions that are discussed in this and the following subsections of section 3. First, there must be a defensible model of general or public interest. This interest lies in the authority of administrating regulation that is delegated to a specific regulator and embodied in people's welfare (Carpenter, 2014). The deviation of actions actually taken by an authority from those that would be taken without regulatory capture rules its extent (Keyser, 2023). Thus, capture is an agency's failure to serve the pubic interest[29], as intended by the Congress (Shapiro, 2012).

Although commonly used in policy development context, "the" public interest is hardly to be defined, highly dependent on the regulatory context and subject to extensive interpretations (Dellaportas & Davenport, 2008). A typology of public interest theories has been provided by Cochran (1974) which differs regarding the constituents that define the public and the ethical standard the theory relies on, from idealism/altruism to self-interests.

The Congress' intention regarding SEC financial supervision and its assumption of public interest is expressed in SEA, ITSFEA and SOX. When creating the SEC, the Congress stated in SEA that *"transactions in securities as commonly conducted upon securities exchanges [...]*

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[29]Besides the theoretically founded public interest underlying the capture identification, there is also a strand of literature explaining politicians behavior with a public interest (e.g., Pigou, 1938; Wittman, 1977; Alesina & Tabellini, 1988; Callander, 2008; Hail et al., 2018). Nevertheless, this kind of public interest has to be considered separately as it is based on a subjective impression of politicians who see themselves acting in the best public interest.

are effected with a national public interest which makes it necessary to [...] control of such transactions [...] to insure the maintenance of fair and honest markets" (SEA SEC. 2). Unlike commonly believed in scholar, there was neither an intention to *protect the public interest* when creating the SEC (Huber, 2015), nor to protect the public interest by federal securities laws in general (Huber, 2016)[30]. Later, this was confirmed by SOX SEC. 3 (a) which states that the SEC's rules should be *"necessary or appropriate in the public interest or for the protection of investors"*.

Concluding from SEA, the Congress states that the assurance of fair and honest markets is necessary in the public interest – not, that the assurance is the public interest. Functioning and efficient markets are considered as national assets that ensure peoples' living standards and opportunities, as well as a general liquidity through pension funds, life insurances and stock ownerships (Casey, 1971), and, thus, are a precondition for a successful economy (Hörner, 2020).

Investors' interests – as mentioned in SOX – are especially a protection against fraud. As this mainly takes place on the institutional rather than the individual level, it is more about protecting the investing public than investing individuals. Thus, investors' interests are considered as supplementary and subordinated to the public's (Fischer, 2008).

A *fair* market implies that every individual is provided with material and correct information for investment decisions, and fraudulent behavior is sanctioned (Fischer, 2008). The necessity of information is a result from the principal-agent-problem where asymmetries arise between owners and managers (Jensen & Meckling, 1976). Considering the theory of Fama (1970), a semi-strong efficient capital market reflects all publicly available information in the stock price. Thus, the assurance of a capital market to be *efficient* is highly dependent on the availability and

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[30]Nevertheless, the instruction given to the SEC by the Congress resulting from ITSFEA SEC. 7 (a) (4) to make an investigation *"of the adequacy of the Federal securities laws and rules and regulations thereunder for the protection of the public interest and the interests of investors"* differ from this concept by explicitly mention the protection of the public interest.

disclosure of corporate information (Healy & Palepu, 2001). To ensure the market efficiency and the provision of material information to the investor, public firms are required to disclose corporate information, such as SEC filings under SEA. Nevertheless, critics question whether the SEC's corporate disclosure effectively improves security pricing mechanisms and point out that the high level of disclosures price intensity is contrary to the public interest (Phillips & Zecher, 1981).

As there are conflicts of interest between managers and owners, resulting from the principal-agent-problem, a control for the availability, relevance, quality and reliability of the disclosed information is necessary (Jensen & Meckling, 1976; Healy & Palepu, 2001). In absence of strong monitoring and sanctioning systems, shareholders and investors will otherwise loose trust in the market (Walla, 2012). Thus, there is a general conviction to protect markets from failure through strong government interventions (Black, 2001). As a result of several corporate and accounting scandals, the Congress tightened oversight mandating the SEC to *"review disclosures made by issuers reporting under section 13(a) of the Securities Exchange Act of 1934 (including reports filed on Form 10–K), and which have a class of securities listed on a national securities exchange or traded on an automated quotation facility of a national securities association, on a regular and systematic basis for the protection of investors."* (SOX Sec. 408 (a)).[31]

As follows from all above, the SEC's financial supervision is necessary to satisfy the public interest. Conversely, it also follows that the public interest lies in an effective SEC oversight. An effective oversight, that ensures a *fair* market in line with the public interest, requires independence from every stakeholder that is able to influence the SEC's financial supervision in each way that is contrary to the mandate given by the Congress. The moment a stakeholder is able

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[31] In addition to SEC oversight, several further monitoring systems have been introduced in corporate governance, such as external auditors. Nevertheless, auditors' independence is widely discussed in literature (e.g., DeFond & Zhang, 2014; Dye, 1993) and auditors have no authority to sanction misreporting (Bockmann, 2012). For a deeper insight into the necessity of financial monitoring and enforcement in the context of external auditors, see (Piering, 2024a). Finally, auditors act under the supervision of the PCAOB which, in turn, is mandated by the SEC.

to influence or actually influences the SEC in an unintended way, an effective oversight ensuring a fair market is hampered. A detailed insight into the necessity of a supervision authority to act independently is provided by Piering (2024a).

As an interim result of this subsection, there is a public interest in an independent SEC financial supervision.

3.2 Political Connections of Interest Groups

The second condition in Carpenter's (2014) model is a demonstration of action and intent by the regulated industry or special interest groups. This activity aims to induce the regulator to favor special interests over public interests. Thus, the regulator's view on a specific topic has to be influenced. Regarding the SEC, two categories of influencing-intended actions can be distinguished: direct and indirect. Direct influence especially appears regarding the SEC's rulemaking activity. Firms and interest groups are invited to send comments on various rules, releases, and filings during different stages of rulemaking. These comments are made publicly available afterwards. Additionally, the public is often also invited to submit written statements on specific topics that are discussed during SEC open meetings. As statements on rulemaking provide the SEC with access to firms' expectations regarding the impact of proposed rules, this kind of direct influence may be considered to be in the public interest (Keyser, 2023). Indirect influence can be exerted through involvement in federal political activity. The underlying mechanism is well described in the iron triangle literature (Freeman, 1965; Adams, 1982) and discussed in section 2. Two ways of influencing federal political activity are contributions to Political Action Committees and lobbying. These two forms are regularly investigated in SEC capture literature (e.g., Correia, 2014; Heese et al., 2017; Khokhar & Shahriari, 2022).[32]

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[32]Beside these measures, many other definitions of a firm maintaining political connections exist (Habib et al., 2018), e.g., if one of its large shareholders or top officers is a member of parliament or a minister (Faccio, 2006).

Firms, as well as individuals, can contribute to PACs that raise and pool money for campaigns pro or against congressional or presidential candidates (Khokhar & Shahriari, 2022). PAC contributions are strictly regulated and limited (Milyo et al., 2000). Compared to the number of individuals, significantly fewer firms contribute to PACs, but the amount-per-firm is much higher (Cooper et al., 2010; Khokhar & Shahriari, 2022). Thus, PAC contributions have a significant impact on politics and policy (Cooper et al., 2010).

Slightly more than 3 % of all firms in the US dataset contributed to PACs. The average amount of total contributions per firm is between 127,000 US-$ (2012) to 150,000 US-$ (2017), while some firms spent over 1,500,000 US-$ per year for campaign contributions. PAC contributions are highly dependent on firm size and industry. Especially large firms maintain political connections through campaign contributions. Around 17 % of all utilities firms have PAC contributions, whereas less than 1 % of the financial industries firms contribute to PACs.

Unlike PAC contributions, lobbying expenditures are not capped. Thus, the average amount of total expenditures per firm is much higher compared to PAC contributions with 1.7M US-$ (2019) to 3.7M US-$ (2018). Between 2012 and 2020, 6.5 % to 7.5 % of all firms contained in the US dataset had lobbying expenditures with a slightly upward trend. Although publicly available data on lobbying are an aggregated amount and, thus, there is no possibility to allocate spending by target, all expenditures are aimed to influence political activity and policy (Milyo et al., 2000). In several cases, firms' lobbying expenditures address one or more specific issues. Especially the general-issue areas "Accounting" and "Finance" target SEC-relevant topics. Between 2012 and 2020, 28 cases targeted accounting issues, whereas in 482 cases, firms lobbied for finance issues. In several cases, firms employ lobbyists that previously worked for the SEC. Additionally, some lobbyists work as an SEC commissioner or staff member after being employed by a company. These lobbyists have special inner knowledge of SEC working procedures and maintain social

connections to SEC staff (Correia, 2014; Shen & Tan, 2023). As special, firms can also lobby directly to government agencies. Nearly 1 % of all lobbying cases at least partly target the SEC directly. This kind of lobbying does not need an involvement in federal politics via congressional intervention, but can be viewed as direct influence. Thus, the Carpenter model's requirement of attempted influence by issuers can be considered fulfilled, as firms' large amounts of campaign contributions and huge lobbying expenditures are actions aimed at influencing SEC activities.

3.3 Policy Shift

Following Carpenter's (2014) model of measuring agency capture, the third condition must be a shift in regulatory policy from public interest to industries' or special interests. Special interests are those outside of industry interests, like interests of labor unions (Carpenter, 2014). In the SEC's case, occurred capture could be presumed if its actual execution of its functions deviates negatively from the Congress' intention, when it delegated functions to the SEC. These duties are mainly a selective review of public companies' disclosures to ensure that investors are provided with material information by the DCF and enforcement of securities laws by the DoE (Khokhar & Shahriari, 2022). As there are material consequences of a comment letter receipt for a public firm (e.g., Baldwin et al., 2013; Gietzmann & Pettinicchio, 2014; Ettredge et al., 2011; Hribar et al., 2014; Cassell et al., 2013; Johnston & Petacchi, 2017)[33] – as well as of enforcement activities (e.g., Dechow et al., 1996; Karpoff et al., 2008a,b) –, any reduction of supervision or enforcement intensity serves special interests instead of the public, as SEC financial supervision in general has beneficial informational effects (Johnston & Petacchi, 2017).

To detect a shift in SEC policy, there is a need to observe SEC activity. Prior research on SEC behavior, their target choice and regulatory capture uses different measures for SEC activity.

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[33]Please note that some research also finds only little economic significance of comment letters and thus question whether they are an appropriate measure for SEC capture (e.g., Johnston, 2023).

Correia (2014) and Heese (2019) observe AAERs issued by the Division of Enforcement. This measure encloses SEC enforcement of federal securities law actions that are related to accounting or auditing issues. Gadinis (2012) observes enforcement issues other than AAERs like Litigation Releases or Administrative Proceedings. Kedia & Rajgopal (2011), Mehta & Zhao (2020) and Khokhar & Shahriari (2022) observe all releases by the DoE including AAERs. A further approach to measure DoE's behavior is the study of undisclosed SEC investigations (Blackburne et al., 2021; Blackburne & Quinn, 2023), as this measure covers also all of the investigations that did not lead to an observable outcome.

Heese et al. (2017) focus on comment letters issued by the Division of Corporation Finance. Unlike DoE outcomes, which often suffer from small sample bias (Heese et al., 2017; Khokhar & Shahriari, 2022), the number of observable comment letters per year enables a representative examination. A comment letter is issued to an EDGAR filer in case there are any questions, uncertainties or detected mistakes resulting from the conducted filing review. Blackburne (2014) uses the allocation of budget and staffing to each office within the DCF that is assigned with filing review as a proxy for SEC oversight intensity.

A major drawback of the metrics mentioned above in context of observing SEC behavior and policy, is their limitation to just one division, in this case the DoE or the DCF. Rare exceptions with a wider coverage are Thompson (2022) and Seitz & Piering (2024). Thompson (2022) uses Confidential Treatment Orders to observe SEC behavior and investigates whether firms' requests for confidential treatment are approved or rejected by the SEC. This measure covers the activity of at least two divisions, as Confidential Treatment Orders are issued by either the DCF or the Division of Investment Management depending on delegated authority (SEC, 2023f). Seitz & Piering (2024) use EDGAR downloads conducted by the SEC itself as a measure of SEC monitoring, without the need of an observable outcome. This measure is not retraceable to a

specific office or division. Nevertheless, Seitz & Piering (2024) assume that most of the traffic is generated by the DCF's staff during filing review.

When investigating SEC behavior during the Clayton chairmanship, there is a requirement for a sufficiently large number of observations at a limited time frame, thus, observing DoE's enforcement releases might result in a small sample bias. For that, I use comment letters issued by the DCF. As described above, this measure and a potential shift in financial supervision is limited in statement to the activity of the DCF.

4 Research Design, Data, and Descriptive Statistics

4.1 Research Design

To investigate the relation between firm's political connections and the comment letter receipt likelihood, I run the following regression model:

$$PR(COMMENT\_LETTER_{i,t}) = \beta_0 + \beta_1 PC_{i,t} + \beta_2 CLAY + \beta_3 INTERACT + \beta_n Controls_{i,t-1} + e_{i,t}$$

$COMMENT\_LETTER_{i,t}$ is a variable becoming 1 if a firm i received a 10-K related comment letter in year t and 0 otherwise. As the dependent variable is binary, I run a logit regression for the estimation of models 1–11. The models differ in their political connections measure as the main independent variable. Firm's political connections are measured both by lobbying expenditures and PAC contributions, following prior literature (e.g., Correia, 2014; Yu & Yu, 2011; Heese et al., 2017; Seitz & Piering, 2024). For lobbying, Log_Lobby indicates a firm's lobbying expenditures in year t. Furthermore, I measure PC in the long-term view by calculating the sum of lobbying expenses over the last three years (t_{-1} to t_{-3}) as Log_PI_Lobby. In addition, $Log\_PI\_Lobby\_linked\_to\_SEC$, $PI\_Lobbyist\_linked\_to\_SEC$ and PI_Lobby_SEC are more

specified lobbying measures with a closer relation to the SEC. See Appendix B.A for detailed information and Correia (2014) and Seitz & Piering (2024) for a discussion on these variables. Log_PAC indicates a firm's PAC contributions in year t. For the long-term view, I calculate the total amount of PAC contributions over the last five years (t_{-1} to t_{-5}) as Log_PI_PAC. $Log\_PI\_Related$ is a more specified measure for long-term PAC contributions to politicians serving in an SEC oversight committee. All continuous PC variables are calculated in logarithmic form due to high skewness.

As this paper investigates whether PC have a greater impact on the comment letter receipt likelihood during Clayton's chairmanship, $CLAY$ is a binary variable becoming 1 for a firm-year observation between 2017-2020, 0 otherwise.

$INTERACT$ is an interaction term between $CLAY$ and the PC variable, depending on the underlying model, to estimate the difference-in-differences.

I use a set of control variables in line with prior literature (e.g., Cassell et al., 2013; Correia, 2014; Heese et al., 2017; Piering, 2024b; Seitz & Piering, 2024), that partly refer to factors mentioned in SOX Sec. 408 (b) for filing review selection. $CHANGE\_SALES$ is an indicator for complexity and LEV for risk, which might be review criteria. MTB is a firm's market-to-book ratio that controls for companies having high growth expectations. To control for financial reporting quality, I use LOW_MTB and $LOSS$, following Heese et al. (2017). I use $LMVE$ (natural logarithm of a firm's market value of equity) to control for firm size, which is a SEC filing review criterion. ROA indicates a firm's efficiency and general situation within its competition market. I winsorize all continuous variables at the 1st and 99th percentile. Additionally, I include industry and year fixed effects to control for invariant factors. Year fixed effects are excluded for all investigations using $CLAY$ as an independent variable, due to the reason that time effects are explicitly relevant for these regressions.

4.2 Data

Data on SEC comment letters can be obtained either from a commercial financial database or directly from the SEC database EDGAR. A discussion about advantages and disadvantages of EDGAR usage to reconstruct comment letter cases can be found in Piering (2024b). I obtain comment letter data from EDGAR.

Firm's political connections are measured by PAC contributions and lobbying expenditures. Following a detailed description provided by Correia (2014), I obtain data on PAC contributions from the Federal Election Commission's (FEC) website.[34] Additionally, I obtain data on Congressional Committee assignments from Charles Stewart III's congressional data page.[35]

I obtain data on firms' lobbying expenditures from the Center for Responsive Politics (CRP)[36], that compiled lobbying data from lobbying disclosure reports filed with the Senate's Office of Public Records (SOPR). I additionally measure lobbying expenditures made directly to the SEC or those made by a lobbying firm that has a link to the SEC, following Correia (2014). I obtain data on SEC employees from the CRP.

I further obtain data for firm financials from Thomson Reuters EIKON. The complete dataset consists of 209,665 firm-year observations, including a significant number of delisted or merged firms. I pick static and time series data for 2012-2020 and delete all observations if their last available data is dated before 2012. I further drop all observations with missing values for firm's home country respectively non-US firms, missing industry classification and missing controls. I retain 53,148 firm-year observations.

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[34] http://www.fec.gov.
[35] https://web.mit.edu/17.251/www/data_page.html.
[36] http://wwww.opensecrets.org.

Table B.1:
Sample Selection

	Firm-years	Firms
Complete EIKON sample (2011-2020)	209,665	23,630
less: last available financials before 2012	(107,361)	(12,297)
less: missing values for industry classification	(3,364)	(360)
less: missing values for controls	(34,709)	(2,316)
less: values for non-US-firms	(11,083)	(1,542)
Final sample	53,148	7,115

Table 1 describes the sample selection process.

4.3 Descriptive Statistics

The frequency of initiated comment letter cases per year is reported in Table B.2. The number of comment letter cases per year is decreasing over the time. This observation is in line with prior literature (e.g., Piering, 2024b; Johnston, 2023). Possible interpretations might either be a general enhancement of firms' disclosure quality or a weakening of SEC financial supervision level.

Table B.2:
Frequency of Comment Letter Cases by year

Comment Letter case issue year	Number of Firm Observations	Number of Comment Letter cases	Percentage
2012	4,874	1,228	25.19
2013	5,143	1,213	23.59
2014	5,462	865	15.84
2015	5,821	896	15.39
2016	6,117	816	13.34
2017	6,322	745	11.78
2018	6,518	497	7.63
2019	6,594	346	5.25
2020	6,297	356	5.65

Table B.2 reports about the frequency of initiated comment letter cases per year.

Descriptive statistics on the dataset can be obtained from Tables B.3 and B.4. Table B.3 reports descriptives for political connections in absolute values (U.S.-$) for firm-years with PC available. As these measures for PC are very skewed, I use them in logarithmic form.

Table B.3:
Summary Statistics – Absolute Values

	n	mean	p50	sd	min	max
COMMENT_L~R	53,148	0.131	0	0.337	0	1
ROUNDS	6,962	3.712	3	1.303	3	15
Lobby	4,013	2.20e+6	3.60e+5	16,347,725.593	5,000	1.001e+9
PI_Lobby	3,964	6.33e+6	8.96e+5	26,224,542.501	5,000	1.002e+9
PI_Lobby_l~d_to_SEC	130	5.84e+5	2.95e+5	1,111,326.279	7,000	9,140,000
PAC	2,212	1.41e+5	51,500	238,287.427	-2.21e+4	1,745,436
PI_PAC	2,041	3.77e+5	95,980	745,908.936	-4,000	5,171,879
PI_Related	1,863	1.68e+5	48,100	313,625.494	250	2,223,891

Table B.3 reports descriptive statistics for COMMENT_LETTER and PC variables in absolute terms. See Appendix B.A for variable definitions.

Table B.4:
Summary Statistics

Panel A: Pooled Sample

	n	mean	p50	sd	min	max
COMMENT_LETTER	53,148	0.131	0	0.337	0	1
ROUNDS	6,962	3.712	3	1.303	3	15
Log_Lobby	53,148	0.979	0.000	3.463	0.000	20.724
Log_PI_Lobby	53,148	1.034	0.000	3.682	0.000	20.726
Log_PI_Lobby_linked_to_SEC	53,148	0.031	0.000	0.620	0.000	16.028
PI_Lobbyist_linked_to_SEC	53,148	0.002	0.000	0.049	0.000	1.000
PI_Lobby_SEC	53,148	0.004	0.000	0.066	0.000	1.000
Log_PAC	53,137	0.445	0.000	2.167	0.000	14.373
Log_PI_PAC	53,147	0.439	0.000	2.226	0.000	15.459
Log_PI_Related	53,148	0.377	0.000	2.004	0.000	14.615
issue_acc	53,148	0.002	0.000	0.091	0.000	10.000
issue_fin	53,148	0.057	0.000	0.767	0.000	27.000
doj	53,148	0.009	0.000	0.200	0.000	11.000
CHANGE_SALES	53,148	0.181	0.000	0.985	–1.000	8.023
LEV	53,148	2.056	0.944	5.747	–20.989	29.980
MTB	53,148	1.317	1.431	24.734	–285.167	131.165
LOW_MTB	53,148	0.360	0.000	0.480	0.000	1.000
LMVE	53,148	12.142	12.436	2.927	4.078	18.212
LOSS	53,148	0.419	0.000	0.493	0.000	1.000
ROA	53,148	–1.274	0.008	8.508	–107.053	0.698

Panel B: Sample partitioned on PC

	PC-firms		Non-PC-firms		Difference
	n	mean (1)	n	mean (2)	(1) – (2)
COMMENT_LETTER	4,533	0.286	48,615	0.117	1.329***
ROUNDS	1,295	3.706	5,667	3.714	−0.008
CHANGE_SALES	4,533	0.136	48,615	0.185	−0.048***
LEV	4,533	1.954	48,615	2.065	−0.111
MTB	4,533	2.987	48,615	1.161	1.825***
LOW_MTB	4,533	0.146	48,615	0.380	−0.234**
LMVE	4,533	15.188	48,615	11.858	3.330***
LOSS	4,533	0.231	48,615	0.436	−0.205***
ROA	4,533	−0.006	48,615	−1.393	1.387***

Table B.4 reports descriptives for the pooled sample and, additionally, partitioned on different binary variables. Panel A reports about the pooled sample. The comment letter receipt likelihood over the entire period is around 13 %. A comment letter case takes around 3.7 rounds on average. The control variables are mostly in line with prior literature (e.g., Heese et al., 2017). Nevertheless, it is noteworthy that there are more extreme values for some controls observable, compared to prior literature (especially for MTB and ROA). This issue is mainly based on the circumstance that my sample consists of even smaller firms registered to the SEC, with sometimes a considerably amount of negative equity.

Panel B reports descriptive statistics for the entire sample partitioned on PC. A high significance in mean differences for $COMMENT\_LETTER$ indicates that PC firms in general are more likely to receive a comment letter. PC firms are also larger, have a greater market-to-book ratio and a better firm performance.

Descriptive statistics partitioned on $COMMENT\_LETTER$ can be obtained from panel C. Firms receiving a comment letter have more short- and long-term lobbying expenditures as well as greater amounts of PAC contributions. They are lobbying more often for financial issues and to the Department of Justice. Comment letter firms are on average larger, have a greater debt-to-equity ratio and report losses less often.

Panel C: Sample partitioned on COMMENT_LETTER

	CL-firms		Non-CL-firms		Difference
	n	mean (1)	n	mean (2)	(1) − (2)
Log_Lobby	6,962	2.134	46,186	0.805	1.329***
Log_PI_Lobby	6,962	2.243	46,186	0.852	1.391***
Log_PI_Lobby_linked_to_SEC	6,962	0.087	46,186	0.022	0.065***
PI_Lobbyist_linked_to_SEC	6,962	0.007	46,186	0.002	0.005***
PI_Lobby_SEC	6,962	0.012	46,186	0.003	0.009***
Log_PAC	6,959	1.100	46,178	0.346	0.754***
Log_PI_PAC	6,961	1.097	46,186	0.340	0.757***
Log_PI_Related	6,962	0.955	46,186	0.290	0.665***
issue_acc	6,962	0.003	46,186	0.002	0.001
issue_fin	6,962	0.178	46,186	0.040	0.140***
doj	6,962	0.015	46,186	0.008	0.007***
CHANGE_SALES	6,962	0.187	46,186	0.180	0.008
LEV	6,962	2.168	46,186	2.039	0.129*
MTB	6,962	2.421	46,186	1.151	1.270***
LOW_MTB	6,962	0.198	46,186	0.385	−0.187***
LMVE	6,962	14.079	46,186	11.850	2.229***
LOSS	6,962	0.268	46,186	0.441	−0.173***
ROA	6,962	−0.161	46,186	−1.442	1.281***

Panel D reports descriptives partitioned on $CLAY$. Firms in general are less likely to receive a comment letter during Clayton's chairmanship. This observation is consistent with prior research findings (e.g., Johnston, 2023) and might be a first indication of a policy shift since Clayton's chairmanship. Additionally, the complexity of each comment letter case became weaker. While lobbying expenditures seem to decrease over time, PAC contributions are not changing significantly. While most of the control variables do not strongly differ, firms' debt-to-equity ratio decreased significantly as well as their return on assets.

Table B.5 reports the correlation for the most important variables excluding controls. There is a positive correlation between $COMMENT\_LETTER$ and all PC measures. Additionally, lobbying and PAC measures have a positive correlation indicating that politically connected firms use both channels, lobbying expenditures and PAC contributions, not alternatively, but complementary and simultaneously. The correlation between $COMMENT\_LETTER$ and all

Panel D: Sample partitioned on CLAY

	Pre-CLAY		Post-CLAY		Difference
	n	mean (1)	n	mean (2)	(1) – (2)
COMMENT_LETTER	27,417	0.183	25,731	0.076	0.108***
ROUNDS	5,018	3.801	1,944	3.485	0.316***
Log_Lobby	27,417	0.948	25,731	1.013	−0.065**
Log_PI_Lobby	27,417	0.999	25,731	1.071	−0.072**
Log_PI_Lobby_linked_to_SEC	27,417	0.029	25,731	0.032	−0.004
PI_Lobbyist_linked_to_SEC	27,417	0.002	25,731	0.003	0.000
PI_Lobby_SEC	27,417	0.006	25,731	0.003	0.002***
Log_PAC	27,411	0.455	25,726	0.435	0.020
Log_PI_PAC	27,416	0.446	25,731	0.431	0.015
Log_PI_Related	27,417	0.385	25,731	0.368	0.017
issue_acc	27,417	0.002	25,731	0.001	0.001
issue_fin	27,417	0.063	25,731	0.051	0.013*
doj	27,417	0.008	25,731	0.010	−0.003
CHANGE_SALES	27,417	0.226	25,731	0.133	0.093***
LEV	27,417	2.156	25,731	1.949	0.207***
MTB	27,417	1.333	25,731	1.300	0.034
LOW_MTB	27,417	0.359	25,731	0.362	−0.003
LMVE	27,417	12.097	25,731	12.190	−0.093***
LOSS	27,417	0.403	25,731	0.436	−0.033***
ROA	27,417	−1.025	25,731	−1.540	0.515***

Table B.4 shows descriptive statistics for the pooled sample (Panel A) and partitioned on specific variables. In panel B, the entire sample is partitioned on PC. In Panel C, the sample is partitioned on $COMMENT\_LETTER$. Panel D partitions the entire sample on time by the variable $CLAY$ becoming 1 for 2017 to 2020. The differences are tested by a t-test. See Appendix B.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

control variables can be obtained from Table B.6. Most of the control variables correlate with each other in line with the expectations. Table B.7 reports the correlation between the political connections variables and the control variables. There are no conspicuous patterns observable.

Table B.5:

Correlation Table – Political Connections

	CL	Log_Lobby	Log_PI_Lobby	Log_PI_y	Log_PI EC	PI_Lobb C	PI_LLobb C	Log_PAC	Log_PI AC	Log_PI_d
CL	1.000									
Log_Lobby	0.130***	1.000								
Log_PI_Lobby	0.127***	0.944***	1.000							
Log_PI_Lobby_1 C	0.035***	0.201***	0.203***	1.000						
PI_Lobbyist_li C	0.036***	0.201***	0.203***	0.995***	1.000					
PI_Lobby_SEC	0.047***	0.263***	0.267***	0.226***	0.215***	1.000				
Log_PAC	0.117***	0.599***	0.596***	0.190***	0.191***	0.255***	1.000			
Log_PI_PAC	0.115***	0.589***	0.590***	0.195***	0.195***	0.263***	0.972***	1.000		
Log_PI_Related	0.112***	0.579***	0.576***	0.197***	0.198***	0.272***	0.943***	0.973***	1.000	

Table B.5 reports correlations between the most important variables. See Appendix B.A for variable definitions.

$* \ p < 0.10$, $** \ p < 0.05$, $*** \ p < 0.01$

Table B.6:

Correlation Table – Control Variables

	CL	CHANGE_S	LEV	MTB	LOW_MTB	LMVE	LOSS	ROA
COMMENT LETTER	1.000							
CHANGE_SALES	0.003	1.000						
LEV	0.008*	-0.035***	1.000					
MTB	0.017***	0.006	0.359***	1.000				
LOW_MTB	-0.131***	-0.003	-0.236***	-0.258***	1.000			
LMVE	0.257***	-0.026***	0.110***	0.075***	-0.520***	1.000		
LOSS	-0.118***	0.063***	-0.172***	-0.064***	0.298***	-0.479***	1.000	
ROA	0.051***	-0.009**	0.080***	0.082***	-0.184***	0.241***	-0.187***	1.000

Table B.6 reports correlations between the most important dependent variable and all control variables. See Appendix B.A for variable definitions.

$* \ p < 0.10$, $** \ p < 0.05$, $*** \ p < 0.01$

Table B.7:

Correlation Table – PC and Control Variables

	Log_Lobby	Log_PILob	Log_PI_Lob	Log_PIEC	PI_Lob_C	PI_Lobb_C	Log_PAC	Log_PI_PAC	Log_PI_d
CHANGE_SALES	-0.014***	-0.021***	-0.007	-0.007	-0.011***	-0.011***	-0.023***	-0.024***	-0.023***
LEV	-0.003	-0.002	0.010**	0.009**	0.015***	0.015***	0.018***	0.018***	0.020***
MTB	0.019***	0.018***	0.012***	0.012***	0.009**	0.009**	0.020***	0.019***	0.020***
LOW_MTB	-0.134***	-0.132***	-0.019***	-0.019***	-0.041***	-0.041***	-0.100***	-0.098***	-0.095***
LMVE	0.311***	0.308***	0.077***	0.076***	0.106***	0.106***	0.268***	0.263***	0.257***
LOSS	-0.113***	-0.114***	-0.031***	-0.031***	-0.041***	-0.041***	-0.117***	-0.115***	-0.112***
ROA	0.042***	0.042***	0.008*	0.008	0.010**	0.010**	0.032***	0.030***	0.029***

Table B.7 reports correlations between the political connections variables and all control variables. See Appendix B.A for variable definitions.

$* \ p < 0.10$, $** \ p < 0.05$, $*** \ p < 0.01$

5 Political Connections and SEC Comment Letters

The main results for the relation between a firm's lobbying expenditures and their comment letter receipt likelihood are presented in Table B.8. There is a highly significant positive relation between lobbying variables and $COMMENT\_LETTER$ for the entire time period, both for Log_Lobby in model 1 and Log_PI_Lobby in model 2, which reflects long-term lobbying expenditures. These results indicate that lobbying firms in general have a greater likelihood of a comment letter receipt depending on the extent of their lobbying expenditures. The findings are in line with Heese et al. (2017) who also shows a significant positive association between lobbying expenditures and comment letter receipt likelihood. For more specified measures of lobbying expenditures, shown in models 3–5, no significant effect on $COMMENT\_LETTER$ is observable. Controls are mostly in line with prior research (Cassell et al., 2013; Heese et al., 2017; Seitz & Piering, 2024). An additional analysis on firm's lobbying expenditures on specific issues can be obtained from Table B.9. There is no significant effect of firms lobbying to specific relevant issues (accounting or finance) respectively to the Department of Justice observable, as these firms do not have a systematically greater or lower comment letter receipt likelihood.

The second measure that proxies for a firm's political connections is PAC contributions, either short- or long-term, as well as those supporting candidates that serve for an SEC oversight committee. Table B.10 presents the multivariate regression results for the relation between firm's PAC contributions and their comment letter receipt likelihood. There is a significant positive association (5 %-level) between short-term and long-term PAC contributions and the firm's comment letter receipt likelihood. Regarding a firm's PAC contribution related to congressional candidates serving for an SEC oversight committee, there is a slightly significant positive (10 %-level) effect on $COMMENT\_LETTER$ over the entire sample period. These observations

<div align="center">

Table B.8:

COMMENT_LETTER and Lobbying

</div>

	Model 1	Model 2	Model 3	Model 4	Model 5
Log_Lobby	0.013***				
	(3.25)				
Log_PI_Lobby		0.012***			
		(3.03)			
Log_PI_Lobby_linked_to_SEC			0.017		
			(0.89)		
PI_Lobbyist_linked_to_SEC				0.238	
				(1.03)	
PI_Lobby_SEC					-0.095
					(-0.56)
CHANGE_SALES	0.029**	0.030**	0.029*	0.029*	0.029*
	(1.99)	(2.02)	(1.96)	(1.96)	(1.95)
LEV	-0.008**	-0.008**	-0.007**	-0.007**	-0.007**
	(-2.21)	(-2.21)	(-2.07)	(-2.07)	(-2.04)
MTB	-0.000	-0.000	-0.000	-0.000	-0.000
	(-0.30)	(-0.29)	(-0.35)	(-0.36)	(-0.34)
LOW_MTB	-0.081*	-0.080*	-0.072	-0.072	-0.070
	(-1.84)	(-1.82)	(-1.63)	(-1.64)	(-1.58)
LMVE	0.351***	0.351***	0.359***	0.359***	0.360***
	(41.49)	(41.69)	(44.44)	(44.43)	(44.20)
LOSS	0.185***	0.186***	0.186***	0.186***	0.186***
	(4.67)	(4.68)	(4.67)	(4.67)	(4.68)
ROA	0.011*	0.011*	0.011*	0.011*	0.011*
	(1.76)	(1.76)	(1.74)	(1.74)	(1.73)
Constant	-5.526***	-5.535***	-5.617***	-5.616***	-5.631***
	(-40.98)	(-41.13)	(-42.43)	(-42.42)	(-42.38)
Industry FE	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes
Observations	53,148	53,148	53,148	53,148	53,148
Pseudo R^2	0.162	0.162	0.161	0.161	0.161

t statistics in parentheses

Table B.8 presents the results for the estimation of the main model. The dependent variable is COMMENT_LETTER, which is an indicator variable becoming 1 if a firm received a 10-K related comment letter in year t, 0 otherwise. The variables of interest for model 1–model 5 are the lobbying proxies for political connections (PC). All specifications include industry and year fixed effects. See Appendix B.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

	Model 6	Model 7	Model 8
Log_Lobby	0.014***	0.015***	0.016***
	(3.29)	(3.57)	(3.80)
ACC_Dummy	-2.637		
	(-0.53)		
Log_Lobby_x_ACC_Dummy	0.151		
	(0.45)		
FIN_Dummy		-1.583	
		(-1.24)	
Log_Lobby_x_FIN_Dummy		0.095	
		(1.12)	
DoJ_Dummy			-3.853
			(-1.39)
Log_Lobby_x_DoJ_Dummy			0.194
			(1.08)
Industry FE	Yes	Yes	Yes
Year FE	Yes	Yes	Yes
Controls	Yes	Yes	Yes
Observations	53,148	53,148	53,148
Pseudo R^2	0.162	0.162	0.162

t statistics in parentheses

Table B.9 presents the results for the estimation of the main model. The dependent variable is COMMENT_LETTER, which is an indicator variable becoming 1 if a firm received a 10-K related comment letter in year t, 0 otherwise. The variables of interest for model 6–model 8 are the interaction terms of the main lobbying variable (Log_Lobby) and the issue indicators (ACC_Dummy, FIN_Dummy, and DoJ_Dummy). All specifications include industry and year fixed effects. See Appendix B.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

are in line with prior literature that also provided evidence of increasing comment letter receipt likelihood for PAC firms (e.g., Heese et al., 2017; Seitz & Piering, 2024).

The interpretation of these results is not intuitive. Contrary to the first assumption, there is no negative relation between firm's lobbying expenditures or PAC contributions, indicating a firm's political connectedness, and their comment letter receipt likelihood. Yet, that would have been expected as the observable policy shift following Carpenter's (2014) model of measuring agency capture in the event that lobbying firms successfully targeted the SEC. In that case, there would

Table B.10:

COMMENT_LETTER and PAC

	Model 9	Model 10	Model 11
Log_PAC	0.013** (2.17)		
Log_PI_PAC		0.011** (1.99)	
Log_PI_Related			0.011* (1.79)
CHANGE_SALES	0.030** (2.00)	0.029** (2.00)	0.029** (1.99)
LEV	-0.008** (-2.19)	-0.007** (-2.17)	-0.007** (-2.16)
MTB	-0.000 (-0.23)	-0.000 (-0.34)	-0.000 (-0.34)
LOW_MTB	-0.077* (-1.75)	-0.077* (-1.74)	-0.076* (-1.73)
LMVE	0.354*** (42.39)	0.355*** (42.49)	0.355*** (42.62)
LOSS	0.185*** (4.65)	0.187*** (4.69)	0.186*** (4.67)
ROA	0.011* (1.75)	0.011* (1.76)	0.011* (1.75)
Constant	-5.564*** (-41.20)	-5.571*** (-41.25)	-5.576*** (-41.32)
Industry FE	Yes	Yes	Yes
Year FE	Yes	Yes	Yes
Observations	53,137	53,147	53,148
Pseudo R^2	0.161	0.161	0.161

t statistics in parentheses

Table B.10 presents the results for the estimation of the main model. The dependent variable is COMMENT_LETTER, which is an indicator variable becoming 1 if a firm received a 10-K related comment letter in year t, 0 otherwise. The variables of interest for model 9–model 11 are the PAC proxies for political connections (PC). All specifications include industry and year fixed effects. See Appendix B.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

likely have been procedures and instructions within the Commission to lower oversight intensity

for these firms. This does not seem to be the case here. However, there is research providing

evidence on lower enforcement intensity for politically connected firms (e.g., Correia, 2014; Yu

& Yu, 2011; Mehta & Zhao, 2020) interpreting their findings as the SEC being captured. These findings are not inevitably contrary to mine, as they relate to enforcement actions by the DoE. As the SEC operates through quasi-independent divisions (Katz, 2010), these findings are (a) exclusively valid for the DoE, not the entire SEC, and (b) without reference to the DCF.

Rather, I find results contrary to the assumption of regulatory capture, as comment letter receipt likelihood is higher for lobbying firms and those contributing to PACs, which are similar to those of Heese et al. (2017).

Some research interpret these findings from the perspective of the political cost hypothesis (e.g., Khokhar & Shahriari, 2022). This hypothesis, first introduced by Watts & Zimmerman (1978), states that politicians might face voter backlash in case they go too far in the support of special-interest groups, as voters are aware of these connections. Thus, the politicians' intervention in SEC policy must balance special-interest groups' and voters' support. Like regulatory capture theory, this hypothesis presupposes that there is indeed an intervention of politicians, probably Congressmen, that successfully influences SEC behavior. Another potential explanation might be that politicians are not easily able to influence the policy of the SEC's filing review. Seligman (2004) states that capture theory and its kindred variants tempt to underestimate the idealism of agency staff. Additionally, systematical influence on SEC policy requires a tight agency structure. Katz (2010), a former Secretary of the SEC, argues that this is entirely not the case with the Commission, which he says has never been well-managed. The structure, culture and pattern of decision-making is individually dependent on the division (Katz, 2010). Regarding the filing review conducting DCF, he states that it is highly diversified over the different offices (Katz, 2010). Besides that, capturing the filing review process is complex, as an extensive review of the internal processes is implemented (Katz, 2010). Rather, the outcome of an individual filing review is highly dependent on the ideosyncratic reviewer style (Baugh et al., 2021), as

decision making is usually influenced by the cognitive attributes and the decision style of the decision maker (Hough & Ogilvie, 2005). Thus, systematical political intervention in the filing review process seems to be unlikely.

Rather, the increasing likelihood of a comment letter receipt for politically connected firms might be an indicator of effective oversight. Firms' political connections might, for instance, indicate specific risks that regulators pay attention to. Heese et al. (2017) suggest that firms' political connections attract SEC scrutiny, although they find no evidence of lower accounting quality of PC firms compared to non-PC firms. This conclusion is supported by recent studies that provided further insight into the role of firms' political connections on the SEC decision making process. Seitz & Piering (2024) show increasing SEC monitoring activity for politically connected firms. Their finding is not limited to the DCF, although they argue that most of the EDGAR download traffic might result from DCF filing review. This assumption is also supported by Thompson (2022), who notes a decreasing likelihood of a confidential treatment order being approved after internal SEC scrutiny for politically connected firms. Following the assumption that legislators likely prefer stricter scrutiny of PC firms (Thompson, 2022; McCubbins & Schwartz, 1984), my findings indicate the SEC is acting in the public rather than special interest regarding financial supervision.

There is no distinct result for the specific measures $Log\_PI\_Lobby\_linked\_to\_SEC$, $PI\_Lobbyist\_linked\_to\_SEC$ and Log_Lobby_SEC. Prior research provided evidence that the involvement of former SEC lawyers helps firms to secure more favorable outcomes from a comment letter, as former SEC lawyers have greater familiarity with former SEC colleagues. Nevertheless, my findings cannot validate the assumption that the political connection channel, even if the involved politicians are closer connected to the SEC, seems to help firms to gain from the comment letter review process.

For further tests with another measure of SEC financial supervision conducted by the DCF, I use $ROUNDS$ as a proxy for the complexity of each comment letter case. The results can be obtained from Table B.11.

In general, the findings are not conclusive regarding the sensitivity of the comment letter process' complexity against firms' political connections with one exemption. A slightly significant negative association can be observed between PI_Lobby_SEC and $ROUNDS$. This result indicates that firms lobbying directly to the SEC have less complex comment letter cases. One has to be careful not to overstate this finding as other explanations beside capture might be applicable, such as these firms are closer connected to the SEC and some communication regarding filing review proceed informally via private channels.

Table B.11:
ROUNDS and Lobbying / PAC

	Model 12	Model 13	Model 14	Model 15	Model 16	Model 17	Model 18	Model 19
Log_Lobby	-0.000 (-0.26)							
Log_PI_Lobby		-0.002 (-0.54)						
Log_PI_Lobby~SEC			0.016 (0.77)					
PI_Lobbyist~SEC				0.234 (0.86)				
PI_Lobby_SEC					-0.216* (-1.89)			
Log_PAC						-0.004 (-0.76)		
Log_PI_PAC							-0.003 (-0.66)	
Log_PI_Related								-0.005 (-0.85)
Constant	3.639*** (24.21)	3.629*** (24.16)	3.659*** (24.81)	3.661*** (24.82)	3.626*** (24.46)	3.624*** (24.25)	3.625*** (24.31)	3.619*** (24.23)
Industry + Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Observations	6,962	6,962	6,962	6,962	6,962	6,959	6,961	6,962
R^2	0.028	0.028	0.028	0.028	0.028	0.028	0.028	0.028

t statistics in parentheses

Table B.11 presents the results for the estimation of the additional model. The dependent variable is ROUNDS, which indicates the number of comment letters exchanged between the SEC and a targeted firm in case a firm received an initial comment letter. The variables of interest for model 12–model 19 are the lobbying and PAC proxies for political connections (PC). All specifications include industry and year fixed effects. See Appendix B.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

6 Political Capture of the Clayton SEC

In this section, I investigate the impact of the significant change in commissioner staffing, especially the introduction of Jay Clayton as the chairman, on SEC financial supervision. More specifically, the section examines whether DCF's comment letter review against politically connected firms is more or less pronounced during Clayton's chairmanship. For that, I conduct a Difference-in-Differences (DID)-estimation with $CLAY$ treatment for all observations for the years 2017-2020. The main results for the DID estimation relating to firm's lobbying expenditures and their comment letter receipt likelihood are presented in Table B.12 and B.13.

A general decrease in comment letter receipt likelihood over time is observable for the entire sample as $CLAY$ is negative with a high significance. As my sample only consists of US firms, this finding is in line with Piering (2024b) who documents a significantly lower likelihood to receive a comment letter for US firms compared to foreign for this time. He interprets this findings as the SEC is influenced by Donald Trump to act in line with his policy and thus is preferring US firms over foreign firms for his presidency (Piering, 2024b).

The interaction terms between the lobbying measures and $CLAY$ have a significantly positive coefficient both for short- and long-term lobbying expenditures as well as those where the SEC is lobbied directly. The greater likelihood of a comment letter receipt for lobbying firms is more pronounced for the timeframe of Clayton's chairmanship compared to the years before. Regarding lobbying expenditures, these results are contrary to the assumption of a captured SEC. For more specified lobbying measures, I mainly do not find any distinct results. The observable significantly positive coefficients are in line with the general findings for lobbying expenditures.

Table B.12:
COMMENT_LETTER and Lobbying (II)

	Model 1		Model 2		Model 3		Model 4		Model 5	
Log_Lobby	0.013*** (3.29)	0.007 (1.53)								
Log_PI_Lobby			0.012*** (3.17)	0.006 (1.25)						
Log_PI_Lob_SEC					0.017 (0.98)	0.026 (1.08)				
PI_Lobbyist_SEC							0.251 (1.13)	0.360 (1.17)		
PI_Lobby_SEC									-0.075 (-0.45)	-0.219 (-1.11)
CLAY	-1.133*** (-38.50)	-1.162*** (-36.56)	-1.134*** (-38.51)	-1.166*** (-36.71)	-1.132*** (-38.52)	-1.130*** (-38.27)	-1.132*** (-38.52)	-1.130*** (-38.26)	-1.132*** (-38.53)	-1.136*** (-38.42)
INTERACT		0.014** (2.32)		0.016*** (2.69)		-0.019 (-0.73)		-0.241 (-0.69)		0.468* (1.72)
Industry FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Observations	53,148	53,148	53,148	53,148	53,148	53,148	53,148	53,148	53,148	53,148
Pseudo R^2	0.142	0.142	0.142	0.142	0.142	0.142	0.142	0.142	0.142	0.142

t statistics in parentheses

Table B.12 presents the results for the estimation of the main model. The dependent variable is COMMENT_LETTER, which is an indicator variable becoming 1 if a firm received a 10-K related comment letter in year t, 0 otherwise. The variables of interest for model 1–model 5 are the lobbying proxies for political connections (PC). CLAY is an indicator variable becoming 1 for the years 2017-2020, 0 otherwise. INTERACT is the interaction term as a product of CLAY and the model depending PC variable. All specifications include industry fixed effects, as well as control variables. See Appendix B.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

Table B.13:

COMMENT_LETTER and Lobbying (II, cont.)

	Model 6		Model 7		Model 8	
Log_Lobby	0.013***	0.013***	0.014***	0.014***	0.016***	0.016***
	(3.33)	(3.33)	(3.39)	(3.40)	(3.86)	(3.86)
ACC_Dummy	-3.768	-5.920				
	(-0.76)	(-1.24)				
Log_Lobby_x_ACC_Dum	0.230	0.351				
	(0.69)	(1.11)				
FIN_Dummy			-1.512	-1.458		
			(-1.22)	(-1.20)		
Log_Lobby_x_FIN_Dummy			0.096	0.085		
			(1.16)	(1.03)		
DoJ_Dummy					-3.859	-3.691
					(-1.43)	(-1.37)
Log_Lobby_x_DoJ_Dummy					0.197	0.203
					(1.12)	(1.15)
CLAY	-1.133***	-1.134***	-1.134***	-1.140***	-1.132***	-1.130***
	(-38.50)	(-38.48)	(-38.51)	(-38.30)	(-38.44)	(-38.24)
INTERACT		0.0905		0.0215		-0.0437
		(1.46)		(1.46)		(-1.58)
Industry FE	Yes	Yes	Yes	Yes	Yes	Yes
Controls	Yes	Yes	Yes	Yes	Yes	Yes
Observations	53,148	53,148	53,148	53,148	53,148	53,148
Pseudo R^2	0.142	0.142	0.142	0.142	0.143	0.143

t statistics in parentheses

Table B.13 presents the results for the estimation of the main model. The dependent variable is COMMENT_LETTER, which is an indicator variable becoming 1 if a firm received a 10-K related comment letter in year t, 0 otherwise. The variables of interest for model 6–model 8 are the interaction terms of the main lobbying variable (Log_Lobby) and the issue indicators (ACC_Dummy, FIN_Dummy, and DoJ_Dummy). CLAY is an indicator variable becoming 1 for the years 2017-2020, 0 otherwise. INTERACT is the interaction term as a product of CLAY and the model depending PC variable. All specifications include industry fixed effects, as well as control variables. See Appendix B.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

The findings are somewhat complex to be interpreted. First, there is a significant change in SEC policy observable, as the comment letter likelihood in general decreases. A potential explanation is provided by Johnston (2023), who assumes that the decline reflects an SEC's acknowledgment to a limited value of comment letters in general and, thus, is not correlated to

any change in the Commission's heads. This explanation seems to be appropriate if one assumes that the DCF conducts its review – also due to structural reasons – relatively independent from short-term policy changes.

On the other hand, this change might also result from a policy change coming along with the exchange of the Chair and the strong break in the Commission's composition. The reference period largely coincides with the term of Mary Jo White serving as the SEC's chairman. White has been attested to do a great job as she has been criticized both by the right and the left (Karmel, 2016b). Under the assumption that the SEC's chairman has significant influence on SEC policy (Phillips & Zecher, 1981), I would expect the SEC to behave strongly in line with its mandate and the public interest for this time. In contrast, Jay Clayton was expected to emphasize companies raise capital in the public markets over tightening regulation (Picker, 2017). He was criticizing the Obama-era SEC for a "zealous" law enforcement that would have caused lasting harm to the competitiveness of American regulated firms and the American capital market (Michaels & Hoffman, 2017). Additionally, the resignation of the democratic commissioner Robert Jackson Jr. left the Republicans with a stronger control over the SEC at a time where they were easing financial regulation (Kiernan, 2020). That said, the lowering level of oversight intensity might result from a chairman's directive.

Second, the change in oversight policy regarding politically connected firms is contrary to what might be assumed to happen with the inauguration of Trump and the chairmanship of Jay Clayton. Clayton was denoted as a "*dealmaker with experience in advising banks on dealings with the government*" (Picker, 2017). He had represented several Wall Street clients before (Antilla & Rivlin, 2018) and was criticized by Senator Catherine Cortez Masto, who voted against Clayton's nomination, questioning his independence and competencies as he had a long career representing firms that are regulated by the SEC, but a lack in law enforcement experience

(Masto, 2017). Thus, a slightly more beneficial treatment of large, politically connected firms would have been imaginable. Nevertheless, financial supervision is more pronounced against these firms under Clayton's chairmanship. There are two potential interpretation for this finding. One considers the DCF's filing review independent from potential short-term policy changes. More, there might be an awareness within the DCF's staff of possible attempts to exert influence from the President or the new chairman to beneficially treat political supporters. The DCF reacts with increased supervision for these firms which could mean the oversight works effectively. The other potential explanation considers the policy influence of Jay Clayton contrary to the first assumption. Prior his nomination, he said that there would be no space for bad actors (Henning, 2017). The former SEC chairman Harvey Pitt denoted the nomination of Jay Clayton as a "high-quality appointment" (Picker, 2017). Thus, he might also direct a policy that is contrary beneficial treatment of politically connected firms.

The results regarding PAC contributions can be obtained from Table B.14. The interaction terms between the PAC contribution measures and $CLAY$ have no observable significant coefficients at all. The results cannot indicate a significant change in impact of firms' PAC contributions on the SEC financial supervision for the timeframe of Clayton's chairmanship compared to the years before.

Unlike lobbying expenditures, the DCF seems to be robust in filing review regarding PAC contributions. As there is no significant effect observable, interpretations would be too speculative to do.

For further tests with another measure of SEC financial supervision conducted by the DCF, I use $ROUNDS$ as a proxy for the complexity of each comment letter case. The results can be obtained from Tables B.15 and B.16. Again, there is a highly significant negative coefficient for $CLAY$, indicating that the complexity of comment letter cases is significantly lower for the

Table B.14:

COMMENT_LETTER and PAC (II)

	Model 9		Model 10		Model 11	
Log_PAC	0.014**	0.008				
	(2.42)	(1.16)				
Log_PI_PAC			0.013**	0.008		
			(2.30)	(1.18)		
Log_PI_Related					0.012**	0.008
					(2.02)	(0.99)
CLAY	-1.132***	-1.145***	-1.132***	-1.143***	-1.132***	-1.142***
	(-38.49)	(-37.31)	(-38.49)	(-37.39)	(-38.50)	(-37.50)
INTERACT		0.014		0.011		0.012
		(1.48)		(1.21)		(1.14)
Industry FE	Yes	Yes	Yes	Yes	Yes	Yes
Controls	Yes	Yes	Yes	Yes	Yes	Yes
Observations	53,137	53,137	53,147	53,147	53,148	53,148
Pseudo R^2	0.142	0.142	0.142	0.142	0.142	0.142

t statistics in parentheses

Table B.14 presents the results for the estimation of the main model. The dependent variable is COMMENT_LETTER, which is an indicator variable becoming 1 if a firm received a 10-K related comment letter in year t, 0 otherwise. The variables of interest for model 9–model 11 are the PAC proxies for political connections (PC). CLAY is an indicator variable becoming 1 for the years 2017-2020, 0 otherwise. INTERACT is the interaction term as a product of CLAY and the model depending PC variable. All specifications include industry fixed effects, as well as control variables. See Appendix B.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

timeframe of Clayton's chairmanship compared to the time before. Nevertheless, the change in

impact of firms' political connections on their comment letter case complexity is not significant.

Table B.15:

ROUNDS and Lobbying (II)

	Model 12	Model 13	Model 14	Model 15	Model 16
Log_Lobby	-0.001				
	(-0.23)				
Log_PI_Lobby	0.001	-0.002			
	(0.29)	(-0.44)			
Log_PI_Lobby_SEC		0.000	0.018		
		(0.08)	(0.86)		
PI_Lobbyist_SEC			0.031	0.255	
			(1.12)	(0.95)	
PI_Lobby_SEC				0.429	-0.213*
				(1.22)	(-1.86)
CLAY	-0.319***	-0.305***	-0.315***	-0.315***	-0.320***
	(-10.27)	(-8.87)	(-10.14)	(-10.12)	(-10.32)
	-0.303***	-0.319***	-0.319***	-0.319***	-0.319***
	(-8.84)	(-10.26)	(-10.29)	(-10.29)	(-10.19)
INTERACT	-0.006	-0.005	-0.040	-0.531	-0.087
	(-1.10)	(-0.99)	(-1.39)	(-1.44)	(-0.44)
Industry FE	Yes	Yes	Yes	Yes	Yes
Controls	Yes	Yes	Yes	Yes	Yes
Observations	6,962	6,962	6,962	6,962	6,962
Adjusted R^2	0.019	0.019	0.019	0.019	0.019

t statistics in parentheses

Table B.15 presents the results for the estimation of the additional model. The dependent variable is ROUNDS, which indicates the number of comment letters exchanged between the SEC and a targeted firm in case a firm received an initial comment letter. The variables of interest for model 12–model 16 are the lobbying proxies for political connections (PC). CLAY is an indicator variable becoming 1 for the years 2017-2020, 0 otherwise. INTERACT is the interaction term as a product of CLAY and the model depending PC variable. All specifications include industry fixed effects, as well as control variables. See Appendix B.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

ROUNDS and PAC (II)

	Model 17		Model 18		Model 19	
Log_PAC	-0.003	-0.002				
	(-0.53)	(-0.32)				
Log_PI_PAC			-0.002	-0.002		
			(-0.40)	(-0.28)		
Log_PI_Related					-0.003	-0.004
					(-0.61)	(-0.51)
CLAY	-0.319***	-0.316***	-0.319***	-0.318***	-0.319***	-0.320***
	(-10.28)	(-9.57)	(-10.30)	(-9.70)	(-10.30)	(-9.79)
INTERACT		-0.002		-0.001		0.000
		(-0.27)		(-0.11)		(0.04)
Industry FE	Yes	Yes	Yes	Yes	Yes	Yes
Controls	Yes	Yes	Yes	Yes	Yes	Yes
Observations	6,959	6,959	6,961	6,961	6,962	6,962
Adjusted R^2	0.020	0.020	0.020	0.020	0.020	0.020

t statistics in parentheses

Table B.16 presents the results for the estimation of the additional model. The dependent variable is ROUNDS, which indicates the number of comment letters exchanged between the SEC and a targeted firm in case a firm received an initial comment letter. The variables of interest for model 17–model 19 are the PAC proxies for political connections (PC). CLAY is an indicator variable becoming 1 for the years 2017-2020, 0 otherwise. INTERACT is the interaction term as a product of CLAY and the model depending PC variable. All specifications include industry fixed effects, as well as control variables. See Appendix B.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

In late 2016, prior to the actual break in the Commission and the inauguration of Donald Trump, the former SEC commissioner Roberta S. Karmel had expressed the fear that *"the Trump Administration and the Republican Congress will try to destroy the [...] SEC's independence"* (Karmel, 2016b). With regard to the DCF's filing review against politically connected firms, this research finds no hint of less independence for the Clayton SEC. Instead, the SEC still seems to conduct financial supervision in line with the public interest.

7 Conclusion

The question whether special interest groups are able to capture the SEC intending a preferred treatment has long been discussed in regulatory literature. Nevertheless, research on regulatory capture often suffers from associations and correlations that represent other patterns beside capture (Carpenter & Moss, 2014). Furthermore, due to complex structures within the commission, prior research on SEC capture can mostly be limited in its findings to the division of its observed outcome. I provide new evidence on SEC's Division of Corporation Finance capture using a framework provided by Carpenter & Moss (2014). I find an increasing comment letter receipt likelihood for politically connected firms which is contrary to the assumption of SEC capture. Instead, I interpret these findings as an indicator of the DCF's filing review works effectively considering firms' political connections as a red flag.

When investigating SEC behavior, particular attention needs to be paid to the role of the SEC's commissioners, especially its chairman, due to his enormous power over the agenda and policy. A significant cut came along with the nomination of Jay Clayton by President Trump, which was intensified by appointments of three further commissioners within one year instead of the typical staggered terms. Examining whether this break leads to an agenda adjustment regarding supervision of politically connected firms, I find that the increased likelihood of a comment letter receipt for these firms is significantly stronger for Clayton's term. I interpret this finding contrary to fears that the Clayton SEC might become less independent.

As already addressed and made clear several times above, the measurement of SEC capture via comment letter receipt likelihood and, thus, my investigation is not without limitations, some of which are institutional and some of which are technical related. The most important is – as stated above – the validity of an investigation of SEC capture is only given for the division the

observed outcome was issued from. The findings of Correia (2014) and Heese et al. (2017), thus, are not necessarily contrary, as they cover different SEC divisions. My study also uses comment letters issued by the DCF as the dependent variable for the multivariate regression. For that, also the outcome of my investigation is limited in its informative value to the DCF. When asking about SEC capture in the title of this paper, this investigation can give only partial evidence. While I find that firms' political connections do not result in capture with regard to the DCF, it might be different for other divisions. As for related studies, a caveat of my investigation might be an endogeneity problem with regard to the measures for PC. The measures could, for instance, be correlated with the error term or suffer from a self-selection bias in case firms that are in fact likely to be reviewed by the SEC contribute for that reason.[37]

Regarding the question on the "Clayton effect" – due to the significant change in the Commission which is against the idea of staggered terms –, no statement can be made on whether the findings result from the change in the entire Commission or would have also appeared if only the chairman had changed. Furthermore, my investigation only considers the effects of one specific chairman and commissioner staff change on the DCF's policy. Extending the timeframe to cover multiple changes as well as observing other outcomes like AAERs to get a more broaden view on SEC activity is a possibility for future research.

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[37]A common approach to control for this problem is the conduction of an instrumental variable investigation (e.g., Correia, 2014; Heese et al., 2017). At this point, I refer to the instrumental variable approach that is conducted by Seitz & Piering (2024) for a similar dataset. Their findings support the view that lobbying and likewise PAC contributions are risk-factors that have an attention-grabbing effect on the SEC.

Variable	Definition
Dependent variables	
COMMENT_LETTER	Binary variable becoming 1 in case a firm received an initial comment letter relating to its 10-K or 20-F filing in the respective year and the comment letter case took an odd number of rounds; obtained from EDGAR.
ROUNDS	Number of rounds a comment letter case took; obtained from EDGAR.
Political Connections Variables	
Lobby	The total amount of lobbying expenditures made by the firm during the fiscal year.
Log_Lobby	The natural logarithm of 1 + the total amount of lobbying expenditures made by the firm during the fiscal year.
PI_Lobby	The total amount of lobbying expenditures made by the firm over the previous three years.
Log_PI_Lobby	The natural logarithm of 1 + the total amount of lobbying expenditures made by the firm over the previous three years.
PI_Lobbyist_linked_to_SEC	Indicator variable equal to 1 if the firm employed at least one lobbyist within the previous three years that either previously worked for the SEC or is currently employed by the SEC, 0 otherwise.
PI_Lobby_linked_to_SEC	The total amount of lobbying expenditures made by the firm through a lobbyist linked to the SEC over the previous three years.
Log_PI_Lobby_linked_to_SEC	The natural logarithm of 1 + the total amount of lobbying expenditures made by the firm through a lobbyist linked to the SEC over the previous three years.
PI_Lobby_SEC	Indicator variable equal to 1 if the firm lobbied the SEC directly over the previous three years, 0 otherwise.
ACC_Dummy	1 if the firm lobbied for accounting issues, 0 otherwise.
FIN_Dummy	1 if the firm lobbied for finance issues, 0 otherwise.
DoJ_Dummy	1 if the firm lobbied the Department of Justice directly, 0 otherwise.
PAC	Total amount of PAC contributions made by the firm during the fiscal year.
Log_PAC	The natural logarithm of 1 + the total amount of PAC contributions made by the firm during the fiscal year.
PI_PAC	The total amount of PAC contributions made by the firm over the previous five years.

Log_PI_PAC	The natural logarithm of 1 + the total amount of PAC contributions made by the firm over the previous five years.
PI_Related	The total amount of PAC contributions made to politicians that serve in an SEC oversight committee (Banking, Commerce or Appropriations committee) in the current election cycle.
Log_PI_Related	The natural logarithm of 1 + the total amount of PAC contributions made to politicians that serve in an SEC oversight committee (Banking, Commerce or Appropriations committee) in the current election cycle.

Independent Variables

CLAY	Binary variable becoming 1 for a firm-year observation from 2017 – 2020, 0 otherwise.
INTERACT	Interaction term, binary variable Product of CLAY**Political Connections Variables*.
CHANGE_SALES	The percentage of change in annual sales (Worldscope Items (WC01001 - l.WC01001) / l.WC01001); winsorized on 1 % level.
LEV	Debt-to-equity ratio (Worldscope Items WC03351 / WC03995); winsorized on 1 % level.
MTB	Market-to-book ratio (Worldscope Items WC08001 / WC03995); winsorized on 1 % level.
LOW_MTB	Binary variable becoming 1 in case a firm's market-to-book ratio is smaller than 1; 0 otherwise.
LMVE	Natural logarithm of market value of equity (Worldscope Item WC08001); winsorized on 1 % level.
LOSS	Binary variable becoming 1 in case a firm reports a loss (Worldscope Item WC01551 $<$ 0); 0 otherwise.
ROA	Return on assets calculated as a firm's return in year t / a firm's average total assets in 1 (Worldscope Items WC01551 / ((WC02999 + l.WC02999) / 2); winsorized on 1 % level.

Appendix B.B:

Members of the SEC Commission

Source: SEC (2023b)

Part C:
Political Connections and SEC Monitoring

Abstract

We examine the effects of firms' political connections (PC) on SEC oversight. Capture theory suggests that firms seek lower SEC regulation by contributing to politicians that control SEC activity. Prior literature measures of SEC oversight only cover outcomes of SEC filing reviews or enforcement investigations of only one division at a time, disregarding that initial review or investigation decisions are not reflected in this consideration. We provide evidence on the effects of PC on SEC oversight using a novel approach that covers the entire monitoring activity by investigating SEC-initiated EDGAR downloads. We find PC increase SEC monitoring activity in general, supporting the idea that PC proxies financial reporting risk. Additional mediation analyses show that the increased SEC monitoring explains an increasing comment letter receipt likelihood for PC firms; supporting the attention-grabbing effect of PC. These findings contribute to the literature by shedding light on the SEC's behavior during the entire oversight process in the presence of PC.

1 Introduction

The United States Securities and Exchange Commission (SEC) oversight[38] has come under public scrutiny for several recent corporate scandals, such as Enron, WorldCom, Theranos, and further. Research has widely investigated the determinants and consequences of SEC oversight. For instance, a comment letter (CL) receipt could result in upward pressure on audit fees (Gietzmann & Pettinicchio, 2014), and enforcement actions are costly both for firms and managers (Karpoff et al., 2008a).

Following implications from capture theory (e.g., Stigler, 1971; Peltzman, 1976), firms might try to benefit from political connectedness resulting in lax SEC oversight. Prior literature finds indistinct results regarding the effect of firms' political connections (PC) on SEC oversight. Yu & Yu (2011) and Correia (2014) outline a negative relation between firms' political connectedness and enforcement actions. Contrary, Khokhar & Shahriari (2022) find that politically connected firms are more likely to be targeted by enforcement actions and imposed fines are relatively higher for those firms. At executive level, Fulmer et al. (2022) find that political connections reduce civil and criminal sanctions for fraudulent managers. Heese et al. (2017) provide a wider view on SEC oversight considering comment letter issues. Contrary to prior research, they find a positive relation between PC and the likelihood of a CL receipt which refutes the assumption of SEC capture. All these studies have two main disadvantages in common: First, they solely focus either on filing review or enforcement, ignoring that SEC oversight is a complex process that involves various SEC divisions[39] and is highly dependent on how the SEC's rank and file employees choose firms at their discretion. Second, these studies measure SEC activity by observable

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[38]Following Heese et al. (2017), our definition of SEC oversight covers selective filing review, conducted by the Division of Corporation Finance (DCF), as well as enforcement actions by the Division of Enforcement (DoE).

[39]Although Heese et al. (2017) mentions this issue explicitly, their research covers only observable outcomes of the DCF.

SEC issues like comment letters or Accounting and Auditing Enforcement Releases (AAERs); ignoring those investigations do not always lead to an observable issue.[40]

A remarkable exception is Blackburne (2014), who provides a dataset consisting of budget and staffing allocations which seems to be a better approximation of SEC oversight activity, but only focuses on the Division of Corporation Finance. Holzman et al. (2023) also use a dataset of formal SEC investigations to analyze SEC target selection. They find, among others, that SEC target selection is driven by a a firm's likelihood of regulatory non-compliance and public trigger events like media coverage. Lee (2021) divides the enforcement process into investigation and enforcement decisions. He finds no evidence for lobbying influencing investigation decisions, whereas enforcement decisions are affected. Gunny & Hermis (2020) are aware that the SEC's decision to issue a comment letter is a joint function of the filing review probability and the comment letter issue probability. They deal with this issue by estimating both the review selection probability and the comment letter issue probability in a bivariate probit model. Stice-Lawrence (2023) examines the behavioral biases of SEC staff attention in the case of the alphabetical order of firm names, and thus, like us, focuses on the operation behavior of SEC employees and does not refer to a specific division.

We provide a relatively novel approach using a dataset of Electronic Data Gathering, Analysis, and Retrieval (EDGAR) downloads by the SEC itself to better understand the impact of PC on SEC oversight behavior in general; and in particular to that of rank and file employees. As SEC oversight, to our conception, describes the entire universe of filing reviews and enforcement actions of the DCF and the DoE (Heese et al., 2017; Ege et al., 2019), we denote the observable activities as SEC monitoring following Stice-Lawrence (2023). In advantage, our approach captures the operational working of the SEC also in cases that do not lead to issues like CL or

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[40]Blackburne et al. (2021) and Blackburne et al. (2021) show the notable economic effects even undisclosed and, thus, publicly unobservable SEC investigations can have. Nevertheless, Blackburne & Quinn (2023) point out that firms' managers have incentives to disclose SEC investigations.

AAERs. Thus, we are the first to provide evidence of how PC influence SEC monitoring in general instead of final issue decisions. Therefore, our first research question is: How is SEC monitoring affected by firms' political connections?

We consider two different effects of PC on SEC monitoring to be possible. SEC monitoring might decrease for PC firms, resulting from SEC capture as SEC employees are aware of firms' PC and thus omit these firms from monitoring. SEC monitoring might also increase for PC firms as PC could be interpreted as risk factors and thus attract SEC attention.

We use common measures for PC following prior literature (e.g., Correia, 2014; Yu & Yu, 2011; Heese et al., 2017). We either measure lobbying expenditures by firms as well as contributions to Political Action Committees (PACs). We measure both short-term and long-term relationships. To shed light on PC that could have a direct influence on SEC activity, we measure PAC contributions to congressional candidates that serve in an SEC oversight committee, lobbying expenses by lobbyists having a link to the SEC, as well as lobbying expenditures directly to the SEC.

We find that PC, as measured by lobbying expenditures and contributions to PACs, have an attention-grabbing effect and lead to a higher SEC monitoring level. In particular, we find these effects for such cases where the lobbyist involved in the lobbying activity was or is linked to the SEC through an employment relationship, or the SEC is lobbied directly.

We confirm the robustness of our findings by an additional instrumental variables approach and entropy balancing.

The attention-grabbing effect, that we provide evidence on, was assumed by Heese et al. (2017) to explain the increased CL receipt likelihood for PC firms. Nevertheless, this was only a suggestion of an underlying mechanism. In contrast to prior research, our design allows us to observe attention directly via SEC monitoring. Although our measure covers the entire SEC

activity, we assume that a significant part is generated by the DCF's rank and file employees (Stice-Lawrence, 2023). From here, our second research question arises: To which extent can the increased CL receipt likelihood of PC firms be explained by SEC monitoring? To answer this, we conduct a set of mediation analyses to investigate the role of SEC monitoring on the CL receipt likelihood for PC firms. In general, we find that SEC monitoring is the causal link between PC and CL likelihood. According to these results, we can support the assumption of Heese et al. (2017), that attention-grabbing is the reason of the increased CL likelihood for PC firms.

We contribute to the literature in three ways. First and most important, we provide novel evidence on the impact of political connections on the SEC's decision-making process. In contrast to prior studies, we do not focus on one SEC division and observable outcomes, but on the entire SEC oversight process by observing monitoring activity of the entire authority. We find evidence that PC basically trigger SEC attention and monitoring increases. Second, we provide insights into the SEC's inner workings of the financial oversight, showing that attention from PC contributes substantially to the likelihood of receiving a CL. Third, we contribute to political connections literature as we provide evidence on the effects of different characteristics of PC.

Our paper proceeds as follows: Section 2 provides background information on SEC oversight activity as well as regulatory capture and depicts our research question and research design. Section 3 describes our data and shows descriptives. Section 4 presents our empirical findings regarding SEC monitoring and controls for robustness. Section 5 expands our study by an mediation analysis to provide evidence on the attention-grabbing effect of PC within financial oversight. Section 6 discusses our findings and concludes.

2 Background

2.1 SEC Monitoring

This study aims to better understand the influence of PC on SEC oversight activity. Prior literature partially mixes up terms like monitoring and oversight, and thereby their definitions in the SEC context; thus, we first outline the underlying purpose of these activities and clarify the terminology. The SEC's mission to "maintain fair, orderly, and efficient markets", among others, forms the basis of the various oversight activities (SEC, 2021b). For this reason, a complex procedure of reviewing firms' filings made under the Securities Act of 1933 and the Securities Exchange Act of 1934, which is publicly available on SEC's EDGAR, is conducted. The DCF selectively reviews firms' filings "to monitor and enhance compliance with the applicable disclosure and accounting requirements" (SEC, 2021c). In case there is a need for further information, clarification from the registrant, or mistakes detected, the DCF issues an initial comment letter which often leads to dialogue over several rounds. In addition, the SEC implemented a suspicion-based investigation and a penalty process (enforcement). The DoE conducts investigations into possible violations of the federal securities laws (SEC, 2021a). A substantial violation results in an AAER issue to clarify the circumstances and civil law consequences.

Blackburne (2014) and Nam & Thompson (2023) equal *regulatory oversight* to the DCF's filing review process. Lee (2021) denotes *oversight enforcement* an entire process, from preliminary inquiry over an internal investigation to an enforcement action. Heese et al. (2017), Iselin et al. (2022) and Kolev et al. (2023) define *SEC oversight* as a range of activities, from advice and *monitoring* in the SEC's filing review process to enforcement actions. They limit *monitoring* to filing review by the DCF. Although the term *monitoring* is used in the SEC's own definition of the filing review process, one should not confound monitoring of firms' compliance with

disclosure and accounting requirements with monitoring activities during the entire oversight process, as accessing and checking firms' filings is necessary also during the enforcement process. Khokhar & Shahriari (2022) and Stice-Lawrence (2023) define *SEC monitoring* as the entire financial oversight process, including filing review and selection process as well as enforcement investigations. The main difference in this definition is that SEC oversight describes the entire process, including filing review and enforcement. In contrast, SEC monitoring denotes the actual SEC activity of checking firms' filings within the entire oversight process. We follow this definition of SEC monitoring.

Similar to variations in definitions, measures of SEC monitoring vary in prior research. Heese et al. (2017) and Nam & Thompson (2023) measure *SEC oversight* by 10-K related comment letter issued by the DCF. Brown et al. (2023) also use 10-K related comment letters as an observable outcome of *SEC attention* to measure *SEC scrutiny*. Iselin et al. (2022) measure *DCF monitoring* in three ways with comment letters as an ex-ante monitoring measure, a comprehensive listing of all conducted DCF filing reviews, and SEC-initiated EDGAR downloads. As they are aware that EDGAR downloads are not only conducted by the DCF, they designate it as a measure of *SEC attention*. The EDGAR downloads measure is also used by Kolev et al. (2023), who apply it as an alternative proxy for SEC filing review, and Stice-Lawrence (2023), who doesn't limit it to DCF filing review, but uses it as a measure of *SEC monitoring* including further divisions operations.

SEC oversight has been subject to various streams of research. Prior literature mainly deals with determinants and consequences of comment letter issues by the DCF or enforcement actions by the DoE.

The DCF is required to review firms' filings at least once every three years by Section 408 of the Sarbanes-Oxley Act of 2002 (SOX). The criteria mentioned in Section 408 (b) – e.g., material

restatements in firms' financial results, issuers with high stock-price volatility, and large market capitalization – are positively associated with the receipt of a comment letter (e.g., Cassell et al., 2013; Johnston & Petacchi, 2017). Also, other factors such as low profitability, high complexity, weak governance increase a firm's comment letter receipt likelihood, whereas Big 4 audited firms have a lower likelihood for a comment letter receipt (Cassell et al., 2013). In case of Initial Public Offerings (IPOs), firms' Chief Financial Officer (CFO) expertise is negatively associated to comment letter complexity (Ertimur & Nondorf, 2006). Blackburne (2014) assumes that the filing review activity is affected by the allocated budget of the SEC office that is conducting the review. In relation to enforcement, the distance of a firm's headquarter to the nearest SEC office seems to influence investigation decisions (Kedia & Rajgopal, 2011). Ege et al. (2019) provide evidence that unexpected resource constraints affect the quality of SEC oversight of periodic reports as comment letters for periodic filings are of lower quality during periods of abnormally high transactional filings. Similarly, Gunny & Hermis (2020) find that the SEC is less likely to issue a 10-K comment letter when busy. An extensive literature review regarding the SEC filing review process is provided by Cunningham & Leidner (2022). With respect to SEC monitoring, Stice-Lawrence (2021) finds a decrease in times of internal reorganization and a lower likelihood for firms scattered over different regions and industries. Stice-Lawrence (2023) outlines that firms with names further down the alphabet are less likely to be monitored by the SEC.

2.2   Regulatory Capture and Political Connections

Dependencies between interest groups, congressional committees, and bureaucratic agencies were systematically shown by Freeman (1965) and Adams (1982). Interactions take place in the flows of information and influence in a triangle relationship denoted as "iron triangle". Bureaucratic agencies like the SEC are dependent on congressional committees resulting from

funding, political support, and oversight (Congressional Dominance Theory, Weingast (1984); Weingast & Moran (1983); McCubbins (1999)).

The congress receives electoral support from interest groups, e.g., in the form of contributions to the re-elections of politicians who favor special legislation, in order to reduce the probability and the size of the wealth transfers generated by regulatory enforcement (Political Cost Hypothesis, Watts & Zimmerman (1978)). A correlation between political spending and reduced regulatory enforcement is observable as firms use political contributions as a signal to fight against agencies' decisions (Gordon & Hafer, 2005).

Following the triangle relationship – as politicians seek interest groups' support with votes or money – these groups have extraordinary power on agencies creating a demand for special regulation (Regulatory Capture Theory, Stigler (1971); Peltzman (1976)). Interest groups support politicians with political contributions (Grossman & Helpman, 1994). The exchange of political support by interest groups and wealth transfer by regulation agencies often take place in case of long-term relationships between firms and politicians (Snyder, 1990). As a result, interest groups could trigger special treatment from agencies, like low regulation, if they support the congress. Firms can be counted to interest groups in these relationships.

Literature on firms' political connections is widely spread. Nonetheless, definitions of politically connected firms differ. A common approach was provided by Faccio (2006) who defines that a firm is connected with a politician if one of the firm's large shareholders or top officers is a member of parliament, a minister, or the head of state or is closely related to a top official. This is an example of a directly nameable relationship measure. Another common way is measuring firms' political expenditures respectively contributions like PAC contributions or lobbying expenditures.

Firms can establish political connections with the intention to gain benefits in accounting topics, although prior literature findings are not conclusive about the real benefits. Among others, PC firms can profit from preferential access to lenders and lower taxes (Faccio, 2006), low debt and equity costs (Boubakri et al., 2012) and favorable regulations (Goldman et al., 2009). Extensive surveys on the literature on accounting-related political connections are provided by Habib et al. (2018) and Preuss & Königsgruber (2021).

2.3   Research Questions

Following the Congressional Dominance Theory, the SEC can be subject to political influence by the congress. We can point out three critical mechanisms of political control over SEC activity. First, budget setting (Weingast, 1984) has a direct impact on SEC activity as monitoring decisions are always made under limited resources. Politicians can use the budget to control the SEC acts in line with their interests. Second, congressional oversight (e.g., Weingast, 1984; Weingast & Moran, 1983) can be costly for the SEC in case the congress starts an investigation. Last, the Senate consents to the U.S. President's appointment of the SEC commissioners. On the one hand, these commissioners have an outstanding role in the SEC oversight process as they – beside others – can vote on DoE's enforcement decisions. On the other hand, commissioners often have political career history or future, so they intend to maximize their career opportunities by acting in line with congressional interests.

The firms – represented by interest groups in the "iron triangle" relation – might seek rents in SEC oversight. A lower level of filing review as well as lower investigation likelihood and, if prosecuted, lower penalties are beneficial to firms by intuition. Thus, firms intend to use political connections such as lobbying or contributions to congressional candidates to make them put pressure on the SEC. Prior literature indicates that political connections are often long-termed (e.g., Snyder, 1992).

First evidence suggestive of SEC capture has been provided by Yu & Yu (2011) who found that lobbying firms that are subject to security class action lawsuits have longer class action periods concluding that lobbying delays fraud detection. Similarly, Heese (2019) finds that firms that have political influence – operationalized as large employers – experience fewer enforcement actions by the SEC. Correia (2014) applies this idea to the SEC's choice of enforcement targets. These studies report a negative relation between PC and enforcement outcomes by the DoE. Firms spending in PACs or lobbying activities are less likely to be involved in enforcement actions and face lower penalties if being prosecuted. Correia (2014) considers this finding supportive to the idea that firms use long-term political contributions in exchange for regulatory favors. Furthermore, in a German setting, Heese (2022) finds a negative association between industry employment of senior regulators of the Financial Reporting Enforcement Panel and enforcement actions, which is also indicative of regulatory capture.

Heese et al. (2017) argue that interpreting this result as generalized SEC capture is complicated, as SEC oversight includes more than enforcement actions. They extend the oversight measure to comment letter outcomes and find a positive relation between PC and the comment letters issued by the DCF. Their main conclusion is that SEC capture is not indicated in the filing review process, and prior findings concluding SEC capture from enforcement investigations seem to be overstated. A potential explanation for their findings contrary to SEC capture provided by Heese et al. (2017) is that political connectedness is a risk indicator that leads the DCF to target PC firms in the review process actively. In line with prior literature, Heese et al. (2017) assume that some SEC officials are at least nominally aware of firms' political connections. Khokhar & Shahriari (2022) find that politically connected firms are more likely to be criminally charged by the DoE and imposed fines are higher if prosecuted. They conclude that SEC enforcement is not captured by firms' political connections.

These studies have in common a measure of SEC activity by observing outcomes like AAERs or CL. Investigating political connectedness' influence on SEC oversight by measuring outcomes seems to be difficult for different reasons.

First, we have no indication that criteria determining initial decisions like reviewing filings or investigating potential fraud are similar to those leading to final decisions like CL issues or AAERs. For instance, Johnston & Petacchi (2017) conjecture that SOX Section 408 (b) criteria increase the likelihood of a firm to be reviewed as comment letter likelihood increases. From our perspective, in this context the link between review likelihood and comment letter receipt likelihood must be viewed in a more nuanced way. Nevertheless, the comment letter receipt likelihood is dependent on the review likelihood. An interesting approach is provided by Gunny & Hermis (2020), who estimate both the review and the comment letter issue likelihood in a bivariate probit model. Lee (2021) also addresses this problem in context to PC by dividing the enforcement process into investigation and enforcement decisions. While the investigation decisions are made by staff, enforcement decisions are authorized by commissioners. Thus, political connections could function in various ways.

Second, congressional control like budget setting or oversight might affect SEC activity differently in various stages of oversight. For instance, constrained resources could have a potentially more decisive effect on review decisions, but not on comment letter issue decisions. Third, SEC officials aware of firms' political connections might influence AAER or CL issue decisions, but not the usual review business. Fourth, the effect of PC might be unequally distributed over the SEC as politically appointed SEC commissioners vote on DoE's enforcement issue decisions, but not on CL issues (which appear much more often). Last, observing outcomes like AAERs or CL typically means observing the behavior of one single division. Nevertheless, research often draws contestable conclusions about the entire SEC ignoring that the different

divisions are organized semi-autonomous (Katz, 2010). In fact, the indistinct results of prior research regarding SEC capture (e.g., Correia, 2014; Heese et al., 2017; Khokhar & Shahriari, 2022) might result from various underlying observed outcomes from different divisions.

To better understand actual SEC activity cross-divisional and independent of observable outcomes as proxies for final decisions, a measure of SEC employees' behavior is used in this research. Stice-Lawrence (2023) suggests that the SEC is opaque regarding its own operations to prevent firms from systematically capturing the SEC's regulatory process. Taking advantage of the circumstance that the SEC and their employees were unaware that their EDGAR downloads were observable and identifiable as reported by Stice-Lawrence (2023), we follow her suggestion in measuring SEC monitoring. With this approach, all downloads of firm-specific filings from EDGAR by an IP address linked to the SEC are tracked. Compared to previous research, the concept of SEC monitoring makes it possible to capture the internal working practices of the SEC rank and file staff (Stice-Lawrence, 2023).

This measure has some substantial advantages compared to CL or AAER. First, we use a method to observe not just issues, but the entire review process, especially including initial decisions that do not lead to an outcome. Second, we tap SEC activity at every stage of the oversight process, no matter if it belongs to the DCF or the DoE, as firm disclosures need to be accessed even during enforcement investigations and decisions (Defond et al., 2018). Prior research provides evidence that SEC downloads spike around CL issues and the beginning of enforcement investigations (Stice-Lawrence, 2023) which confirms that the SEC uses its own database EDGAR for filing review and enforcement investigations. Thus, this measure seems to be appropriate to cover the overall monitoring activity in the SEC oversight process. We develop the following research question from the considerations above:

RQ1: How is SEC monitoring affected by firms' political connections?

We consider two possible contrary impacts following prior literature. First, SEC monitoring could be negatively affected by firms' political connections. This consideration is in line with the idea of SEC capture (Correia, 2014). In the case of systematically lower SEC monitoring for PC firms, SEC employees must be aware of PC and thus actively omit PC firms in their oversight process. Second, SEC monitoring could be positively affected by firms' political connections. Heese et al. (2017) support the second conjecture, who assume the DCF actively targets PC firms in their filing review and conducts more substantive reviews than for non-PC firms, as PC proxies for financial reporting risk characteristics. The suspected underlying mechanism is as follows: PCs represent a risk factor for firms' financial reporting. These risks attract the attention of SEC staff and thus lead to a increased probability of receiving a comment letter. Nevertheless, this remained an assumption, as Heese et al. (2017) were not able to observe actual SEC rank and file employees review activity, but only base their assumption on the observed CL outcome. Our measure for SEC monitoring is able to fill in the gap by providing insights in the underlying mechanism. Thus, we can gain deeper understanding into a central component of SEC oversight in a novel way by directly observing the behavior of employees between the triggering element (PC) and the outcome (CL). A more in-depth insight into these processes is, therefore, part of the current scientific discourse on the internal behavior of the SEC (Bonsall et al., 2024; Stice-Lawrence, 2023). This leads to our second research question:

RQ2: To which extent can the increased comment letter receipt likelihood of PC firms be explained by SEC monitoring?

2.4 Research Design

To investigate the relation between PC firms and SEC monitoring, we use the following fixed effects regression model:

$$SEC\_Monitoring_{i,t+1} = PC_{i,t} + Firm\_Level\_Controls_{i,t} + Year\_FE + Industry\_FE + e_{i,t}$$

The subscript i represents the individual firm, whereas t stands for the year. $SEC\_Monitoring_{i,t+1}$ is the natural logarithm of 1 + the total number of SEC-initiated firm-specific EDGAR downloads per calendar year. In line with prior literature (Correia, 2014; Yu & Yu, 2011; Heese et al., 2017), we measure PC either by firms' lobbying expenditures (Log_Lobby) or by PAC contributions (Log_PAC). Since all PC variables have high skewness, we use all continuous PC variables in logarithmic form.

We also measure PC in the long-term view by calculating the sum of lobbying expenses over the last three years (t_{-1} to t_{-3}) as Log_PI_Lobby. For the PAC contributions, we calculate the total amount of PAC contributions over the last five years (t_{-1} to t_{-5}) as Log_PI_PAC. These measures are in line with the long-term view of political expenditure, according to Snyder (1992).

In addition, we expand both long-term measures to the extent to which the PC target the SEC itself. We consider in the variable $Log\_PI\_Lobby\_linked\_to\_SEC$ just long-term lobbying expenditures that went through a registered lobbyist who is linked to the SEC. To supplement, we use the two indicator variables $PI\_Lobbyist\_linked\_to\_SEC$, a dummy for $Log\_PI\_Lobby\_linked\_to\_SEC$, and PI_Lobby_SEC, a dummy for direct lobbying the SEC in long-term.

We measure $Log\_PI\_Related$, our long-term PAC variable directly related to the SEC, only including PAC contributions made to politicians serving in an SEC oversight committee. We follow Correia (2014) in all presented variable definitions for PC.

Additionally, we include a set of control variables in our regression model. Thereby, we follow Heese et al. (2017) and Cassell et al. (2013), who refer to the various factors used by the SEC under SOX Section 408 (b), to identify companies for filing reviews, and Correia (2014) for supplementary control variables. We use the market-related measure Log_Market_Cap to control for the firm size, which is also a review criterion under SOX Section 408 (b). To control for emerging companies with high growth expectations, but more immature accounting and governance processes (higher risks), we use $Market\_to\_Book$. In line with Heese et al. (2017), we control for financial reporting quality using $Low\_Market\_to\_Book$, $Loss$, $Zscore$, and Age. As additional control variables, we use $Change\_Sales$ and $Leverage$, for complexity and risk, respectively, which may attract the SEC's attention. Furthermore, we use the distance to the next SEC office ($Log\_SEC\_Office\_Dist$) as a control variable to account for potential geographical constraints (Kedia & Rajgopal, 2011). We winsorize all continuous variables at the 1th and 99th percentile.

Additionally, we added aggregated SEC downloads to all specifications to reduce possible noise from automated downloads (Stice-Lawrence, 2023). We include year and industry fixed effects (4-digit SIC) in all specifications to control for time and industry invariant factors. By using year fixed effects, we address the increase in EDGAR downloads over time in an attempt to reduce noise in the measurement of SEC monitoring. We include industry fixed effects to control for correlated omitted variables which we assume to be inherent to our study, in particular due to data availability reasons. It follows that our study focuses on the effects of political connections on the within-industry variation of SEC monitoring. A drawback associated with the use of high-dimensional fixed effects, such as firm fixed effects, however, is that they may induce measurement error (Jennings et al., 2023). We address this by reviewing all of our main specifications using deHaan's (2021) approach (see Appendix C.B).

In our robustness checks, we try to address endogeneitiy concerns, e.g., through omitted variables and measurement error. In particular, it can be argued that there are other influencing factors that we either cannot measure or for which we have no data, which could bias our inference.

In the first set of additional tests, we apply an instrumental variable approach. Our instruments for the respective lobbying and PAC expenditures (only for the non-indicator variables) are the respective sum of the lobbying and PAC expenditures of the other firms in the same 4-digit SIC industry, and the state-level voter turnout rates (Heese et al., 2017; Correia, 2014; McDonald & Popkin, 2001).[41] The rationale for using industry PC as an instrument is based on the assumption that they are likely to affect the PC of firms through peer effects, whereas there is no direct link to SEC monitoring (Grier et al., 1994; Kim, 2008; Heese et al., 2017). A similar argument can be made for voter turnout rates. While these should not be directly related to SEC monitoring, they could have an influence on firms' political connections. In the second set, we use entropy balancing to mitigate concerns that there are systematic differences between PC and non-PC firms, i.e., the treatment PC is not randomly assigned (Hainmueller, 2012; McMullin & Schonberger, 2022).

To answer the second research question, we use path analysis or, since our path is rather simple, a mediation model. Mediation analysis is an approach to find out why a variable X influences a variable Y, i.e., to investigate the mechanism of the underlying relationship (Jollineau & Bowen, 2023; Hayes, 2022). Applied to our study, this approach allows us to find out whether political connections influence financial oversight directly ($PC \rightarrow Pr(CL)$), indirectly through the mediator SEC monitoring ($PC \rightarrow$ SEC monitoring $\rightarrow Pr(CL)$), or through both directly and

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[41]The voter turnout rate is calculated based on the voting-eligible population, as suggested by McDonald & Popkin (2001). The data is publicly available on the University of Florida Election Lab website (https://election.lab.ufl.edu/voter-turnout/).For years without an election, the voter turnout of the previous year was assumed.

indirectly. Technically, we implement this with structural equation modeling (Bhattacharya et al., 2012; Mayew et al., 2020; Bonsall et al., 2024) and, for validation reasons, with the – outdated – casual step approach according to Baron & Kenny (1986).

3 Data

3.1 SEC Monitoring

3.1.1 Measure

We measure SEC monitoring by the natural logarithm of 1 plus the SEC initiated firm-specific EDGAR downloads per calendar year. Thereby we get the EDGAR downloads from the EDGAR Log File Data Set (log files), which logs all user activity in the EDGAR database. This database, provided by the SEC itself, contains all forms and filings of registrants required by law. Since the log files record the IP address for each individual access, along with other meta-information, we can analyze the user activity of the various stakeholders of financial reporting (e.g., Bernard et al., 2020; Bozanic et al., 2017; Drake et al., 2015, 2016, 2017). However, to provide privacy for individual users, the last of the four octets was encoded with a combination of three unique letters (e.g., 123.456.789.abc). This is of no consequence for our analysis, as the SEC itself occupies one large block of IP addresses, so the encoded IP address octet is not needed to assign an IP address to the SEC (Stice-Lawrence, 2023). Thus, the EDGAR accesses of the SEC, or more precisely the EDGAR downloads of the individual SEC employees, represent a straightforward measure for disclosure monitoring.

Similar measures based on EDGAR accesses have been applied in the literature for other stakeholders. For example, Drake et al. (2017) and Loughran & McDonald (2017) examined the access behavior of investors, Bernard et al. (2020) studied the accesses among rivals, Drake et al. (2019) that of auditors, and Bozanic et al. (2017) looked at that of the Internal Revenue

Figure C.1:

Total SEC Monitoring per year
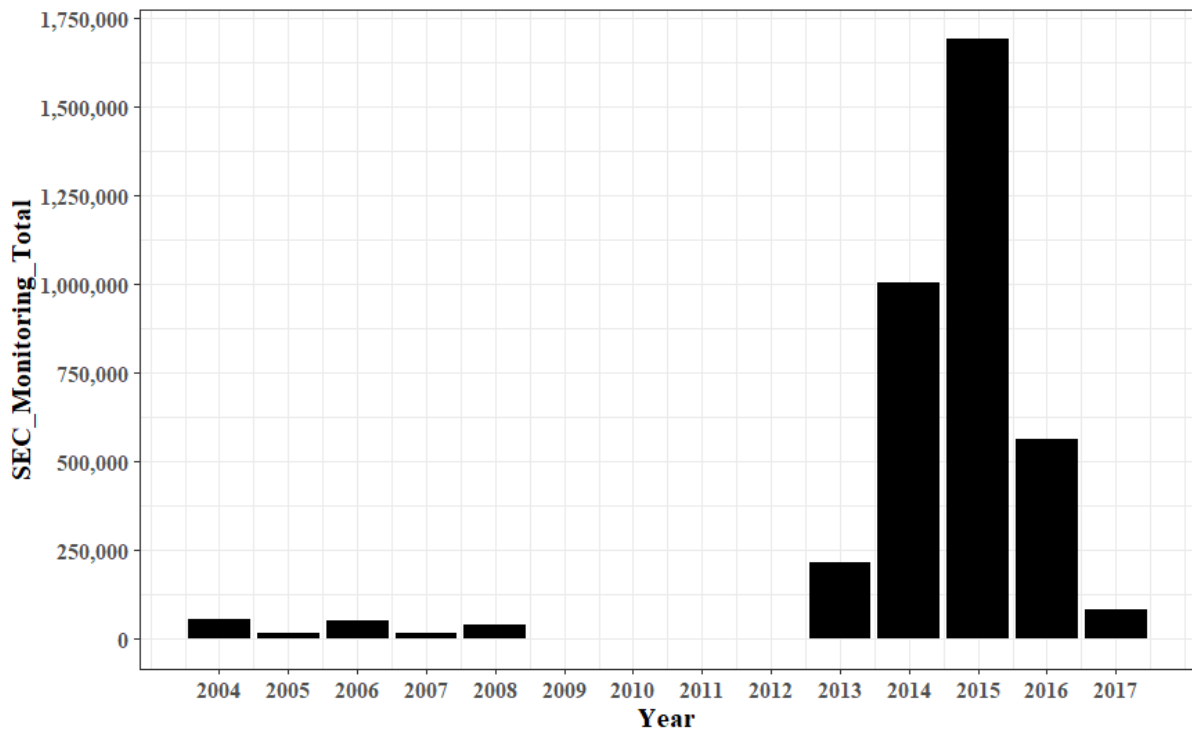
Service (IRS). Our measure is based on the measures of Stice-Lawrence (2021, 2023), Iselin et al. (2022), and Kolev et al. (2023), who investigated the determinants of SEC monitoring.

In total, we observe an unadjusted number of 32,172,990 accesses by the SEC to firm filings in the raw data. As can already be seen in Figure C.1, there are no SEC downloads observable in EDGAR for the years 2009–2012. We remove these years from the analysis as described in the sample selection. Figure C.1 also shows the high volatility of EDGAR accesses.

3.1.2 Potential Noise and Bias

In its nature, our measurement for SEC monitoring is subject to several potential noises and biases.

First, it is important to note that there are other channels for monitoring (e.g., site visits or firms' websites), and – most importantly – there is an internal EDGAR for the SEC itself.

However, the reliance on monitoring data based on external EDGAR should not lead to any problematic bias. In particular, internal EDGAR also includes operations performed by SEC staff (e.g., comment letter conversations and applications for confidential treatment) that are not of interest in our study or would tend to bias our measure of SEC monitoring. Inherently, these types of activities are mandatory and, thus, not in the interest of our study. In addition, SEC staff seemed to be generally unaware that their external EDGAR accesses were being logged (Stice-Lawrence, 2023).

Second, as already mentioned above and as Figure C.1 shows, SEC downloads are subject to a high degree of volatility and, in particular, an increasing trend over time. Presumably, parts of this increase could be due to automated downloads by the SEC (Stice-Lawrence, 2021). In addition, it is well known that the SEC has adopted a data-driven approach under its Accounting Quality Model, often referred to as "RoboCop" (Brown et al., 2023; Stice-Lawrence, 2021; Lewis, 2012). It is possible, therefore, that our measurement for SEC monitoring captures downloads that have resulted from this type of data-driven approach. According to Stice-Lawrence (2021), two possible consequences follow from this. First, mass downloads could introduce noise into the SEC monitoring measurement. We address this with the inclusion of time fixed effects and control for total SEC downloads (Stice-Lawrence, 2023). Second, mass downloads may also reveal SEC preferences for certain firms and therefore have genuine interest for our study.

Third, there may be reasons for downloads that are not related to official SEC operations (e.g., for private investment activities of SEC staff). While this could be a reason for noise in the measurement, it should not systematically bias our results since these downloads are not correlated with actual SEC activities (Stice-Lawrence, 2023). Moreover, any reviewing of SEC staff on EDGAR may lead to the discovery of conspicuous firms. According to anecdotal

evidence, this might be the case. Therefore, it seems reasonable to include such downloads in the measurement of SEC monitoring (Stice-Lawrence, 2021, 2023).

The three listed aspects of noise and bias have the property that they are essentially additive in nature, thus they tend to be less problematic econometrically (Stice-Lawrence, 2023; Wooldridge, 2020, pp. 308–309).

3.2 Political Connections

Following Correia (2014) and Heese et al. (2017), we use either firms' PAC contributions as well as lobbying expenditures for PC measures. This approach allows us a kind of comparability to prior research. A PAC is a special organization that raises and pools contributions to donate campaigns pro or contra congressional or presidential candidates. Although a firm can be connected to a PAC and can cover its operating costs, contributions come from executives and shareholders. Nevertheless, firms' top executives typically decide about PAC contributions (Correia, 2014) and this measure is a common proxy for PC (e.g., Milyo et al., 2000; Farber et al., 2007). Following Correia (2014), we obtain data on PAC contributions from the Federal Election Commission's (FEC) website.[42] We further obtain data on Congressional Committee assignments from Charles Stewart III's congressional data page.[43]

Firms lobby congressmen and federal agencies like the SEC with large amounts of money to benefit from regulatory actions. We obtain data on firms' lobbying expenditures from the Center for Responsive Politics (CRP)[44] that compiled lobbying data from lobbying disclosure reports filed with the Senate's Office of Public Records (SOPR). In contrast to PAC contributions, we cannot track lobbying expenses to specific congressmen or congressional candidates. Since we have a particular interest in firms' connections to the SEC, we either measure lobbying

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[42]http://www.fec.gov.
[43]https://web.mit.edu/17.251/www/data_page.html.
[44]http://wwww.opensecrets.org.

expenditures made directly to the SEC or those made by a lobbying firm that has a link to the SEC. Following Correia (2014), we define a lobbying firm having a link to the SEC if they employ a lobbyist that has worked for the SEC previously or employed a lobbyist that is working for the SEC afterward. We obtain these Revolving Door data on SEC employees also from the CRP.

We report descriptive statistics for the PC in U.S.-$ and $SEC\_Monitoring\ (Downloads)$ in Table C.1, excluding firm-years where no PC were available. The amounts are comparable in magnitude to the literature (Correia, 2014). Notable here are the in some cases substantial amounts for lobbying, e.g., for long-term lobbying PI_Lobby up to U.S.-$ 156,787,100. PAC contributions, on the other hand, are, as expected, substantially smaller in value. This is not surprising given that lobbying expenditures are uncapped, unlike PAC contributions. Moreover, the measures for PC are very skewed; thus, we use the variables in logarithmic form in our analysis.

Table C.1:

Summary Statistics – SEC_Monitoring (Downloads) and Political Connections

	count	mean	median	sd	min	max
SEC_Monitoring (Downloads)	14,107	257	72	449	1	4,172
Lobby	3,295	2,079,385	400,000	4,703,155	5,000	59,941,000
PI_Lobby	3,235	5,755,347	1,000,000	13,135,453	6,500	156,787,100
PI_Lobby_linked_to_SEC	126	3,327,663	261,750	14,415,969	7,000	103,840,000
PAC	2,243	125,697	44,500	216,501	-5,000	1,568,664
PI_PAC	2,079	313,456	76,624	651,558	-1,000	5,176,300
PI_Related	1,912	145,699	38,704	284,414	-1,000	2,233,775

Total Firm-Year Observations: 15,114

Table C.1 contains descriptive statistics for SEC_Monitoring and political connections (PC) variables in absolute terms. See Appendix C.A for variable definitions.

3.3 Sample

Table C.2 provides a summary of our sample selection procedure. We obtain firm financials from EIKON. Our sample spans from 2004–2017, since we cannot obtain EDGAR log files earlier than 2004 and later than 2017. Following Heese et al. (2017), we exclude foreign firms as they are not allowed to create a PAC and, thus, are unable to influence electoral outcomes in the United States.

We also exclude firms whose fiscal years do not end on December, 31. These exclusions are necessary because we compute $SEC\_Monitoring$ on a calendar year basis, and we are concerned that this could lead to distortions in our final sample with regard to the temporal structure of the SEC attention. In line with Stice-Lawrence (2023), we gap the sample period for the intervals in which there were no EDGAR accesses from the SEC. These gaps occurred at certain periods when SEC internal EDGAR traffic was routed through internal servers, causing them to be missed out of the EDGAR Log File Data Set. Therefore, we exclude the years 2009–2012 from our investigation.

For the PAC and lobbying data, due to the lack of a dedicated firm identifier, we use a semi-automated approach based on the Jaro-Winkler similarity to link the PAC and lobbying information to the EIKON data (Sariyar & Borg, 2010). Similarly, we add the data on Congressional Committee assignments to the politicians supported by the PACs.

The final sample consists of a panel of 15,114 firm-year observations, corresponding to 2,514 distinct firms. These summate to 3,726,518 EDGAR accesses by the SEC.

Table C.2:

Sample Selection

	Firm-years	Firms
Full EIKON sample (2004–2017)	116,074	8,291
(Cross-listed firms)	(4,088)	(292)
(Fiscal year end not 31.12)	(61,435)	(2,687)
(Missing data)	(29,751)	(2,782)
(2009–2012)	(5,686)	(16)
Final Sample	15,114	2,514

Table C.2 describes the sample selection process.

3.4 Descriptive Statistics

Table C.3 reports the descriptive statistics for the variables included in our study. $SEC\_Monitoring$ is consistent in magnitude with the reported figures from Stice-Lawrence (2021). We can observe $SEC\_Monitoring$ for 93 percent of the firm-years (see Table C.1). This is in line with our expectations, as the SEC itself is one of the primary EDGAR users and accesses files on EDGAR in high volumes. The variables for lobbying and PAC contributions are economically reasonable and correspond to the logarithmic variables presented in the data section. In only 0.5 percent of firm-years, there is a connection to the SEC through a lobbyist who works or has worked for the SEC in the past three years ($PI\_Lobbyisit\_linked\_to\_SEC$).

In contrast, for 1.3 percent of the firm-years, there was direct lobbying to the SEC in the past three years (PI_Lobby_SEC). In 1.1 percent of firm-years, the Department of Justice (DoJ) was lobbied. Accounting issues were lobbied in 0.2 percent of the firm-years and finance issues in 2.4 percent. The magnitude and distribution of the control variables are in line with expectations from the literature.

As reported in Table C.4, Panel A, all the variables for PC correlate with each other with positive significance. Moreover, all variables in our study for PC, except $Log\_PI\_Lobby\_linked\_to\_SEC$ and $PI\_Lobbyist\_linked\_to\_SEC$, also correlate significantly positive with $SEC\_Monitoring$.

Table C.3:
Summary Statistics

	mean	median	sd	min	max
SEC_Monitoring	3.932	4.007	2.058	0.000	8.336
Log_Lobby	2.838	0.000	5.437	0.000	16.500
Log_PI_Lobby	2.970	0.000	5.759	0.000	17.609
Log_PI_Lobby_linked_to_SEC	0.053	0.000	0.765	0.000	11.695
PI_Lobbyist_linked_to_SEC	0.005	0.000	0.073	0.000	1.000
PI_Lobby_SEC	0.012	0.000	0.108	0.000	1.000
Log_PAC	1.561	0.000	3.801	0.000	13.190
Log_PI_PAC	1.532	0.000	3.897	0.000	14.030
Log_PI_Related	1.328	0.000	3.543	0.000	13.262
ACC_Dummy	0.002	0.000	0.049	0.000	1.000
FIN_Dummy	0.024	0.000	0.152	0.000	1.000
DoJ_Dummy	0.011	0.000	0.105	0.000	1.000
CL	0.193	0.000	0.395	0.000	1.000
Log_Market_Cap	13.443	13.568	2.444	6.735	18.810
Market_to_Book	3.076	2.289	10.784	-96.117	62.195
Low_Market_to_Book	0.185	0.000	0.388	0.000	1.000
Loss	0.367	0.000	0.482	0.000	1.000
Zscore	1.534	2.559	24.055	-224.233	118.797
Leverage	1.083	0.758	4.145	-35.285	33.317
Change_Sales	0.163	0.032	0.704	-0.966	6.891
Log_SEC_Office_Dist	4.801	5.317	2.213	0.000	8.535
Age	21.356	20.000	9.537	2.000	37.000
Observations	15,114				

Table C.3 describes the descriptive statistics of all variables. See Appendix C.A for variable definitions.

This might already be a preliminary indicator for explaining that PC might be positively related to SEC monitoring since the SEC is aware of PC as a risk factor and therefore targets such firms.

Figure C.2 shows a validation of our SEC monitoring measure. The line graphs show the weekly SEC monitoring (aggregated and logarithmized) for the 24 weeks before and after a comment letter receipt. In contrast to the line graphs in Stice-Lawrence (2023), we have split our observations of SEC monitoring by whether the observed firms had lobby expenditures (Figure C.2.1) or PAC contributions (Figure C.2.2) in the previous year. The four graphs Figure C.2.1 and C.2.2 reveal that SEC monitoring peaks shortly before the receipt of a comment letter. The increase in SEC monitoring starts around 9-12 weeks before the comment letter

receipt and ends with a sharp drop after the letter is received. These descriptive results are in line with Stice-Lawrence (2023), who additionally reports a similar pattern for enforcement investigations and restatements. The first insight that can be derived from this, at least graphically, is that the use of the public EDGAR plays a certain role for SEC staff in the financial oversight process. Another noticeable observation is that the firms with PC (i.e., that lobbied or made PAC contributions in the previous year) receive consistently more SEC attention than those that are not politically connected.

The correlations of the control variables with $SEC\_Monitoring$ are in line with expectations, as are the correlations between the control variables (Table C.4, Panel B). Table C.4, Panel C shows the correlations between the variables for PC and the control variables. Again, no conspicuous patterns emerge, as all variables show the correlations as expected.

Figure C.2:
Weekly SEC Monitoring around Comment Letter Receipt

Figure C.2.1: Weekly SEC Monitoring around Comment Letter Receipt (Lobby)
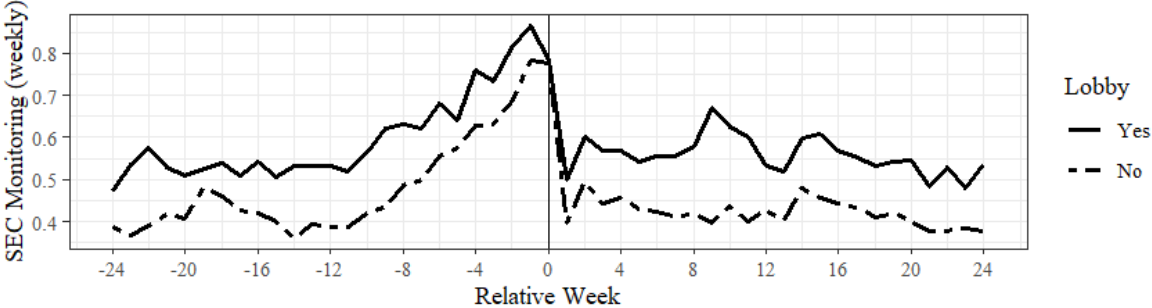
Figure C.2.2: Weekly SEC Monitoring around Comment Letter Receipt (PAC)
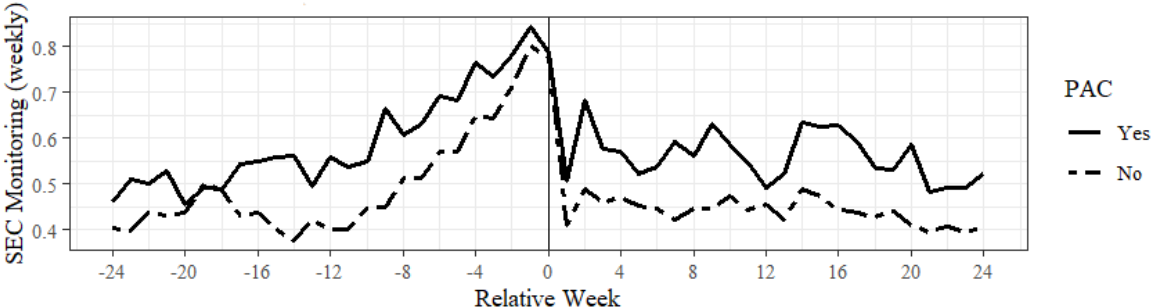
Table C.4:
Correlation Tables

Panel A: Political Connections

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
(1) SEC_Monitoring	1.000								
(2) Log_Lobby	0.113***	1.000							
(3) Log_PI_Lobby	0.114***	0.931***	1.000						
(4) Log_PI_Lobby_linked_to_SEC	-0.002	0.148***	0.151***	1.000					
(5) PI_Lobbyist_linked_to_SEC	-0.002	0.157***	0.161***	0.948***	1.000				
(6) PI_Lobby_SEC	0.081***	0.238***	0.243***	0.072***	0.076***	1.000			
(7) Log_PAC	0.055***	0.569***	0.563***	0.151***	0.164***	0.231***	1.000		
(8) Log_PI_PAC	0.055***	0.561***	0.560***	0.152***	0.165***	0.240***	0.969***	1.000	
(9) Log_PI_Related	0.057***	0.550***	0.549***	0.156***	0.171***	0.245***	0.941***	0.973***	1.000

Panel B: Control Variables

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
(1) SEC_Monitoring	1.000									
(2) Log_Market_Cap	0.084***	1.000								
(3) Market_to_Book	-0.002	0.094***	1.000							
(4) Low_Market_to_Book	0.005	-0.351***	-0.386***	1.000						
(5) Loss	0.085***	-0.482***	-0.025***	0.247***	1.000					
(6) Zscore	-0.021***	0.273***	0.179***	-0.331***	-0.181***	1.000				
(7) Leverage	0.004	0.122***	0.650***	-0.325***	-0.074***	0.049***	1.000			
(8) Change_Sales	0.014*	-0.052***	0.018**	-0.029***	0.059***	0.009	-0.026***	1.000		
(9) Log_SEC_Office_Dist	-0.120***	0.099***	-0.024***	0.078***	-0.099***	-0.012	0.018**	-0.028***	1.000	
(10) Age	-0.119***	0.365***	-0.007	-0.135***	-0.349***	0.034***	0.062***	-0.109***	0.014*	1.000

Panel C: PC and Control Variables

	Log_Lobby	Log_PI_Lobby	Log_PI_Lobby_1_t_SEC	Log_PAC	Log_PI_PAC	Log_PI_Related
Log_Market_Cap	0.445***	0.440***	0.099***	0.410***	0.406***	0.403***
Market_to_Book	0.017**	0.014*	0.000	0.022***	0.019**	0.019**
Low_Market_to_Book	-0.096***	-0.096***	-0.031***	-0.096***	-0.095***	-0.091***
Loss	-0.193***	-0.194***	-0.049***	-0.208***	-0.202***	-0.194***
Zscore	0.042***	0.037***	0.005	0.025***	0.022***	0.021**
Leverage	0.063***	0.065***	0.007	0.080***	0.077***	0.074***
Change_Sales	-0.052***	-0.057***	-0.008	-0.054***	-0.055***	-0.053***
Log_SEC_Office_Dist	-0.040***	-0.034***	-0.030***	-0.018**	-0.013	-0.014*
Age	0.329***	0.344***	0.095***	0.393***	0.401***	0.388***

Table C.4 presents correlations. Panel A presents the Pearson correlations between the political connections (PC) variables and SEC_Monitoring and between the PC variables themselves. Panel B presents the Pearson correlations between the control variables and SEC_Monitoring and between the control variables themselves. Panel C presents the Pearson correlations between the political connections (PC) variables and the control variables. See Appendix C.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

4 Political Connections and SEC Monitoring

4.1 Main Findings

We present our main results for the relationship between lobbying and SEC monitoring in Table C.5, estimating the equation we introduced in our research design. We examine different lobbying variables for the effect of PC on SEC monitoring in each of the five different specifications (Model 1 to 5). All five specifications show a positive and significant coefficient for our lobbying proxies. Model 1, our baseline model, examines the effect of Log_Lobby – reflecting lobbying expenditures in the year prior to the monitoring activity – on $SEC\_Monitoring$. This finding can also illustrated as follows: A one percent change in lobbying expenditures (corresponding to a change of U.S.-\$10,794 related to the mean lobbying expenditures) increases the number of SEC's EDGAR downloads per year by approx. 7.2.

For Model 2, which measures PC as long-term lobbying expenditures (Log_PI_Lobby), and for Model 3, which considers long-term lobbying expenditures in which the lobbyist has ties to the SEC ($PI\_Lobby\_linked\_to\_SEC$), we also obtain positive and significant results. The rationale for using long-term measures is that PCs usually have an effect over a longer period of time; thus, according to the literature, they correspond more to a measure for a more effective long-term strategy regarding political spending (Correia, 2014; Heese et al., 2017; Snyder, 1992). We find the same effect for the corresponding indicator variable $PI\_Lobbyist\_linked\_to\_SEC$ in Model 4. Similarly, in Model 5 we find that lobbying the SEC directly (PI_Lobby_SEC) has a significant and positive effect on $SEC\_Monitoring$.

All these results suggest that the SEC in particular monitors those firms that have PCs and thus follow the hypothesis of Heese et al. (2017), who interpret PC as a risk factor. This also applies, in particular, to cases in which the PC to the SEC is through former or current SEC

employees. Even direct SEC lobbying suggests that PC is a risk factor. Consequently, in our analyses we cannot find any evidence of SEC capture as pointed out by the study of Correia (2014). The control variables are as expected for all specifications and consistent with the literature (e.g., Heese et al., 2017).

In a further analysis, we consider in Table C.6 lobbying on issues particularly relevant to the firms. These issues include those that relate to accounting (ACC_Dummy) or finance (FIN_Dummy) topics. Thus, we assume such PC are in particular related to the SEC's mandate. Moreover, in Model 8 we consider cases where firms lobbied the DoJ (DoJ_Dummy). We interact each of the dummy variables for accounting and finance issues with $Log\_Lobbying$ since both indicator variables are related to year t as well. In addition, each of our models contains the $Log\_Lobbying$ and the corresponding dummy variable. In line with our baseline model, the $Log\_Lobbying$ variable remains positive and significant for these three specifications (Model 6 – 8).

For the respective interactions of the three dummy variables with the lobbying expenditure measure, the coefficients for all the dummy variables are positive and for cases related to financial issues and the DoJ also significant. These results imply that for situations where lobbying involves SEC-relevant issues, an increase in lobbying expenditures leads to an increase in SEC monitoring. Likewise, we find this incremental effect for cases relating to the DoJ.

Thus, we can conclude that lobbying, in addition to the general attention-seeking effect, is particularly strong for cases that are explicitly relevant to the daily work of the SEC. Hence, this would also be contrary to the hypothesis of SEC capture.

In Table C.7, we find a stable positive and significant effect on $SEC\_Monitoring$ for all specifications measuring PC using PAC contributions. So this holds for PAC contributions in year t (Log_PAC), for long-term PAC contributions (Log_PI_PAC), as well as for PAC contributions

Table C.5:
SEC Monitoring and Lobbying

	Model 1	Model 2	Model 3	Model 4	Model 5
Log_Lobby	0.028***				
	(6.88)				
Log_PI_Lobby		0.026***			
		(6.75)			
Log_PI_Lobby_linked_to_SEC			0.115***		
			(5.96)		
PI_Lobbyist_linked_to_SEC				1.234***	
				(6.26)	
PI_Lobby_SEC					0.376***
					(2.89)
Log_Market_Cap	0.080***	0.0810***	0.104***	0.104***	0.104***
	(7.54)	(7.72)	(11.02)	(10.98)	(10.93)
Market_to_Book	0.001	0.0014	0.001	0.001	0.001
	(1.05)	(1.08)	(1.01)	(1.05)	(1.00)
Low_Market_to_Book	-0.085*	-0.082*	-0.057	-0.057	-0.057
	(-1.83)	(-1.76)	(-1.20)	(-1.22)	(-1.22)
Loss	0.179***	0.179***	0.187***	0.187***	0.187***
	(5.20)	(5.19)	(5.40)	(5.39)	(5.38)
Zscore	-0.002***	-0.002***	-0.002***	-0.002***	-0.002***
	(-4.05)	(-4.02)	(-4.40)	(-4.39)	(-4.44)
Leverage	-0.006*	-0.006*	-0.005	-0.005	-0.005
	(-1.68)	(-1.69)	(-1.32)	(-1.38)	(-1.41)
Change_Sales	0.059***	0.059***	0.057***	0.057***	0.058***
	(4.98)	(5.01)	(4.78)	(4.78)	(4.83)
Log_SEC_Office_Dist	-0.098***	-0.098***	-0.103***	-0.103***	-0.104***
	(-10.75)	(-10.78)	(-11.16)	(-11.16)	(-11.18)
Age	0.007***	0.006***	0.010***	0.010***	0.009***
	(3.20)	(3.03)	(4.69)	(4.68)	(4.58)
Agg_SEC_Downloads	Yes	Yes	Yes	Yes	Yes
Fixed Effects	Year/Ind.	Year/Ind.	Year/Ind.	Year/Ind.	Year/Ind.
Observations	15,114	15,114	15,114	15,114	15,114
R^2	0.687	0.687	0.686	0.686	0.684
Adjusted R^2	0.680	0.680	0.678	0.678	0.677

t statistics in parentheses

Table C.5 presents the results for the estimation of the main model. The dependent variable is SEC_Monitoring, which corresponds to the natural logarithm of 1 + the total number of SEC-initiated firm-specific EDGAR downloads in year *t+1*. The variables of interest for Model 1 – Model 5 are the lobbying proxies for political connections (PC). All specifications include year and industry fixed effects, as well as control variables. See Appendix C.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

	Model 6	Model 7	Model 8
Log_Lobby	0.028***	0.027***	0.026***
	(6.82)	(6.62)	(6.28)
ACC_Dummy	-1.814		
	(-1.15)		
Log_Lobby×ACC_Dummy	0.145		
	(1.26)		
FIN_Dummy		-1.879**	
		(-2.31)	
Log_Lobby×FIN_Dummy		0.142**	
		(2.54)	
DoJ_Dummy			-3.891***
			(-2.80)
Log_Lobby×DoJ_Dummy			0.309***
			(3.21)
Controls	Yes	Yes	Yes
Agg_SEC_Downloads	Yes	Yes	Yes
Fixed Effects	Year/Ind.	Year/Ind.	Year/Ind.
Observations	15,114	15,114	15,114
R^2	0.687	0.688	0.689
Adjusted R^2	0.680	0.680	0.681

t statistics in parentheses

Table C.6 presents the results for the estimation of our main model. The dependent variable is SEC_Monitoring, which corresponds to the natural logarithm of 1 + the total number of SEC-initiated firm-specific EDGAR downloads in year *t+1*. The variables of interest for Model 6 – Model 8 are the interaction terms of the main lobbying variable (Log_Lobby) and the issue indicators (ACC_Dummy, FIN_Dummy, and DoJ_Dummy). All specifications include year and industry fixed effects, as well as control variables. See Appendix C.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

that relate to lawmakers serving on an SEC oversight committee ($Log\_PI\_Related$). Again, as with lobbying expenditures, these results for PAC contributions can be illustrated as follows. Here, a one percent change in PAC contributions (corresponding to a change of U.S.-$1,257 related to the mean PAC contributions) increases the number of SEC's EDGAR downloads per year by approx. 13.1. The result remains virtually unchanged if we include lobby expenditures as a control.

Table C.7:

SEC Monitoring and PAC Contributions

	Model 9	Model 10	Model 11	Model 12
Log_PAC	0.051***			0.041***
	(8.75)			(7.23)
Log_PI_PAC		0.049***		
		(8.28)		
Log_PI_Related			0.054***	
			(8.49)	
Log_Lobby				0.018***
				(4.46)
Controls	Yes	Yes	Yes	Yes
Agg_SEC_Downloads	Yes	Yes	Yes	Yes
Fixed Effects	Year/Ind.	Year/Ind.	Year/Ind.	Year/Ind.
Observations	15,114	15,114	15,114	15,114
R^2	0.689	0.689	0.689	0.690
Adjusted R^2	0.682	0.681	0.682	0.683

t statistics in parentheses

Table C.7 shows the results for the estimation of our main model. The dependent variable is SEC_Monitoring, which corresponds to the natural logarithm of 1 + the total number of SEC-initiated firm-specific EDGAR downloads in year *t+1*. The variables of interest for Model 9 – Model 12 are the PAC proxies for PC. All specifications include year and industry fixed effects, as well as control variables. See Appendix C.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

In summary, we can interpret PAC contributions according to Heese et al. (2017) as a risk factor that attracts the attention of the SEC in its oversight process. Overall, our main results show a consistent picture of a positive and significant correlation between PC and SEC monitoring.

4.2 Robustness Checks

A caveat of our investigation is that PC are subject to a possible endogeneity problem, i.e., our measures of PC are correlated with the error term. These endogeneity problems arise from the fact that we could not randomize how our firms were treated (i.e., determine which firms became PC). Additionally, it cannot be ruled out that our estimation is biased by omitted variables or that our variables are subject to measurement error. In particular, the bias due to omitted variables

seems to be an important source of concern. Thus, the assumption that there are missing variables in our model that are correlated with both PC and SEC monitoring seems reasonable.

To mitigate these concerns, we run regressions with instrument variables for our main and long-term specification of PC. More specifically, we estimate the instrumental variable models for $Log\_Lobbying$ (Model 13), $Log\_PI\_Lobbying$ (Model 14), Log_PAC (Model 15), Log_PI_PAC (Model 16), and $Log\_PI\_Related$ (Model 17) in Tables C.9 and C.10.[45] The instrumental variable approach is common in the literature (Correia, 2014; Heese et al., 2017). As instruments for the continuous lobbying and PAC contributions measures, we use the corresponding industry aggregated sums of lobbying expenditures and PAC contributions, respectively. The rationale behind this approach is that while peer effects in the industry and for firms of similar size are likely to increase the intensity of PC, there is no direct logical link between these effects and the SEC's monitoring activity (Heese et al., 2017). The magnitudes of the instruments are within an economically reasonable range (see descriptives in Table C.8). As a further instrument, we use the $Voter\_Turnout$ of the respective state. The rationale for this instrument is similar. In states with a high voter turnout, it could be particularly beneficial for firms to be politically connected, i.e., to lobby or contribute to PACs. In contrast, a relationship between voter turnout and SEC monitoring seems implausible. Voter turnover is, therefore, suitable as an instrument on a theoretical basis.

In the first stage, we test the validity of each of the instruments using partial F-test (Stock et al., 2002; Larcker & Rusticus, 2010). We find in all our models that the instruments have a significant relationship with the PC and are above the critical value of 11.59 proposed by Stock et al. (2002) (see Tables C.9 and C.10). Furthermore, we test our potentially endogenous regressors for exogeneity for the respective first-stage regression. However, for all five specifications, we

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[45]We do not estimate an instrumental variable model for $Log\_PI\_Lobby\_linked\_to\_SEC$, as this variable has only 126 non-zero observations; therefore, inferences here would have to be viewed with extreme caution.

Table C.8:
Summary Statistics Instruments

	mean	median	sd	min	max
Log_Sum_Industry_Lobby	10.857	13.704	6.947	0.000	18.257
Log_Sum_Industry_PI_Lobby	11.459	14.595	7.351	0.000	19.591
Log_Sum_Industry_PAC	7.386	10.358	6.037	0.000	14.839
Log_Sum_Industry_PI_PAC	7.550	10.633	6.408	0.000	16.041
Log_Sum_Industry_PI_Related	6.840	9.680	6.087	0.000	15.281
Voter_Turnout	0.518	0.541	0.116	0.281	0.790
Observations	15,114				

Table C.8 presents the summary statistics for the instrumental variables. See Appendix C.A for variable definitions.

cannot reject the null hypothesis that the regressors are exogenous. In addition, our test for the overidentification restriction fails to reject the hypothesis that our instruments are exogenous. This indicates at least some validity for our instruments and is in line with the tests of Heese et al. (2017).

In Table C.9, we find that lobbying has a positive and significant effect on both current lobbying spending and long-term lobbying expenditures (see Models 13 and 14). These results confirm our main findings from Table C.5. Thus, the results from the instrumental variable approach support the view that lobbying is a risk factor according to Heese et al. (2017) that attracts the SEC attention. The findings for PC, measured by PAC contributions in the instrumental variable approach (see Table C.10), remain virtually unchanged – in fact, they are even more pronounced – from the findings in the main analysis. Thus, we also identify an attention-increasing effect on the SEC by PC measured by PAC contributions. These results indicate that there is a direct link between PC and SEC monitoring that is not distorted by problems such as omitted variables.

Table C.9:

SEC Monitoring and Lobbying: Instrumental Variables Approach

	Model 13		Model 14	
	Log_Lobby	SEC_Monitoring	Log_PI_Lobby	SEC_Monitoring
Log_Lobby		0.043**		
		(2.52)		
Log_PI_Lobby				0.035**
				(2.14)
Industry_Sum	-0.222***		-0.228***	
	(-11.14)		(-11.02)	
Voter_Turnout	-0.912		-0.539	
	(-1.25)		(-0.71)	
Controls	Yes	Yes	Yes	Yes
Fixed Effects	Year/Ind.	Year/Ind.	Year/Ind.	Year/Ind.
Exogeneity p-value	0.343		0.569	
F-Statistics	62.74		60.85	
Overidentifying p-value	0.271		0.325	
Observations	15101	15101	15101	15101
(Pseudo) R^2	0.0267	0.670	0.0279	0.670

t statistics in parentheses

Table C.9 presents the results of the instrumental variable approach. The dependent variable is SEC_Monitoring, which corresponds to the natural logarithm of $1 +$ the total number of SEC-initiated firm-specific EDGAR downloads in year $t+1$. The variables of interest for Model 13 and Model 14 are, in each case, one of the lobbying measures as a proxy for political connections (PC). In columns (1) and (3) – showing the first-stage of our results – the industry sum and the size sum of the respective lobbying measures are used as instruments. All specifications include year and industry fixed effects, as well as control variables. See Appendix C.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

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Table C.10:

SEC Monitoring and PAC: Instrumental Variables Approach

	Model 15		Model 16		Model 17	
	Log_PAC	SEC_Monitoring	Log_PI_PAC	SEC_Monitoring	Log_PI_Related	SEC_Monitoring
Log_PAC		0.078***				
		(4.96)				
Log_PI_PAC				0.062***		
				(4.38)		
Log_PI_Related						0.0726***
						(4.44)
Industry_Sum	-0.319***		-0.360***		-0.322***	
	(-13.66)		(-14.56)		(-14.02)	
Voter_Turnout	-0.223		-0.017		-0.028	
	(-0.42)		(-0.03)		(-0.06)	
Year FE	Yes	Yes	Yes	Yes	Yes	Yes
Controls	Yes	Yes	Yes	Yes	Yes	Yes
Fixed Effects	Year/Ind.	Year/Ind.	Year/Ind.	Year/Ind.	Year/Ind.	Year/Ind.
Exogeneity p-value	0.070		0.331		0.220	
F-Statistics	93.35		106.1		98.28	
Overidentifying p-value	0.316		0.384		0.371	
Observations	15101	15101	15101	15101	15101	15101
(Pseudo) R^2	0.0671	0.671	0.0841	0.672	0.0767	0.672

t statistics in parentheses

Table C.10 presents the results of the instrumental variable approach. The dependent variable is SEC_Monitoring, which corresponds to the natural logarithm of 1 + the total number of SEC-initiated firm-specific EDGAR downloads in year $t+1$. The variables of interest for Model 15 – Model 17 are, in each case, one of the PAC measures as a proxy for political connections (PC). In columns (1), (3), and (5) – showing the first-stage of our results – the industry sum and the size sum of the respective lobbying measures are used as instruments. All specifications include year and industry fixed effects, as well as control variables. See Appendix C.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

To address further concerns stemming from endogeneity, we use an entropy balancing approach (Hainmueller, 2012). This aims to balance systematic differences between PC and non-PC firms resulting from a non-random assignment of this treatment. Entropy balancing is a more modern approach than the propensity score matching used by Heese et al. (2017), for example, with the advantage that no observations are lost. Since our data is in a panel setting, we follow the McMullin & Schonberger (2022) approach and perform entropy balancing separately for each observation year. The aim of entropy balancing is to weight the control sample so that the covariate moments – in our case, the mean, the variance, and the skewness – are almost identical to the treatment sample (PC).

As covariates, we use all the control variables from our main tests. We perform entropy balancing for the two main specifications. Thus, an assignment as treatment is done for the firm years that had either lobbying expenditures or PAC contributions in year t. We then estimate on the newly weighted sample with our usual research design (i.e., same variable definitions and fixed effects) in Table C.11. The results for Log_Lobby and Log_PAC remain the same in direction and significance level, but are marginally weaker than in the main analysis. This indicates that our results are robust to the concern that they originate from the non-random assignment of the treatment.

Entropy Balancing

	Model 18	Model 19
Log_Lobby	0.023***	
	(4.02)	
Log_PAC		0.043***
		(5.72)
Log_Market_Cap	0.083***	0.100***
	(4.31)	(4.08)
Market_to_Book	-0.001	0.001
	(-0.24)	(0.30)
Low_Market_to_Book	-0.122	-0.113
	(-1.36)	(-1.09)
Loss	0.115**	0.162**
	(2.01)	(2.38)
Zscore	-0.003	-0.004**
	(-1.60)	(-2.46)
Leverage	0.002	0.000
	(0.30)	(0.04)
Change_Sales	0.110***	0.156***
	(4.69)	(4.11)
Log_SEC_Office_Dist	-0.122***	-0.116***
	(-8.05)	(-7.02)
Age	0.016***	0.014***
	(4.63)	(3.47)
Agg_SEC_Downloads	Yes	Yes
Fixed Effects	Year/Ind.	Year/Ind.
Observations	12,631	12,652
R^2	0.637	0.681
Adjusted R^2	0.626	0.672

t statistics in parentheses

Table C.11 presents the results of the entropy balanced estimation. The dependent variable is SEC_Monitoring, which corresponds to the natural logarithm of 1 + the total number of SEC-initiated firm-specific EDGAR downloads in year *t+1*. The variables of interest for Model 18 – Model 19 are the main lobbying (*Log_Lobby*) and PAC (*Log_PAC*) proxies for PC. All specifications include year and industry fixed effects, as well as control variables. See Appendix C.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

5   The Role of Political Connections and SEC Monitoring in Financial Oversight

Our findings regarding SEC monitoring of PC firms are in line with those Heese et al. (2017) found for CL likelihood. These results raise the question whether increased CL likelihood is really due to the attracted attention of PC firms, as assumed by Heese et al. (2017). In other words, is there really a attention-based mechanism which explains the higher CL likelihood for PC firms?

To investigate this phenomenon and in line with our target to better understand SEC activity, we perform a mediation analysis in form of a structural equation modeling (SEM) (Bhattacharya et al., 2012; Bonsall et al., 2024; Jollineau & Bowen, 2023; Mayew et al., 2020).[46] We perform this mediation analysis, a subtype of path analysis, to understand the underlying process or mechanism by which PC influences financial oversight. For robustness reasons, we perform the somewhat outdated Baron & Kenny (1986) causual step approach (see Appendix C.C).

In our analyses, PC is the independent variable, the likelihood of receiving a comment letter is the dependent variable[47], and the mediator corresponds to SEC monitoring.

Our approach follows the basic structure of Bonsall et al.'s 2024 analysis, which examines a similar question in relation to the SEC's internal operations. They use a mediation analysis framework to understand the relationship between public and private enforcement in the context of SEC's business. In this respect, our question also relates to the procedures within the SEC.

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[46]For accounting research using large archival data, the SEM approach is advantageous over the often-used PROCESS tool (Hayes, 2022), as it allows more flexibility with respect to common econometric methods (e.g., fixed effects).

[47]Therefore, we use a logit-based generalized structural equation modeling (GSEM) for the paths that have CL receipt as the dependent variable. $Comment\_Letter$ is an indicator for firm-years with a 10-K related comment letter in year t+1. In contrast to prior research, we do not obtain 10-K related CL from a financial database. Instead, we collect data directly from EDGAR index files and check each comment letter for its 10-K relation. This approach has some advantages in comparison to the use of financial database CL data. First, we avoid potential bias resulting from financial database use. Second, and – from our perspective – more important is the fact that both $Comment\_Letter$ and $SEC\_Monitoring$ variables result from the same source.

More specifically, we are interested in the extent to which the increased CL likelihood for PC firms is explained through the attention effect that (Heese et al., 2017) assumes. For this purpose, the method of path analysis is applicable, since it is possible to determine the relative share of the individual paths within a complex model. We have a comparatively simple mediation model, which we estimate with a GSEM. This approach allows us to estimate the direct, indirect, and total effects (e.g., Hayes, 2022; Jollineau & Bowen, 2023). In addition, our models include all fixed effects and control variables from the analyses of the relationship between PC and SEC monitoring (see section 4). In total, we estimate four different models that differ only in the PC proxy. The first two models are on lobbying measures for PC, and the other two are on PAC measures. For each type of PC, we consider the main variables (Log_Lobby and Log_PAC), as well as the long-term variables (Log_PI_Lobby and Log_PI_PAC). We obtain estimates for the three paths (A-C) and the resulting indirect and direct effects for each of our four models. The results can be found in Table C.12 and are illustrated in Figure C.3.

Path A is the relationship between PC and SEC monitoring. This path, thus, corresponds to that of our study from section 4. The results of our estimates correspond, as expected, approximately to our previous results. Therefore, they each show a positive and significant relationship.

Path B shows the relationship between SEC monitoring and CL likelihood. This is a central component of our models, as we are trying to illustrate what proportion of the link between PC and CL likelihood can really be explained by SEC attention. As we can already expect from our graphical illustration shown in Figure C.2, this relationship is likewise positive. Indeed, we can observe a positive and significant relationship for all four of our specifications. This again triangulates our assumption that SEC monitoring is indeed an appropriate measure to capture the

internal operation of the SEC (especially in the Division of Corporation Finance). Thus, this shows that the use of EDGAR is indeed a component of SEC oversight.

Path C refers to the link between PC and CL likelihood. This corresponds to the relationship investigated by Heese et al. (2017). The results also show a positive and significant association, which is initially in line with expectations from the literature. However, the results also reveal that our four cases are in fact (complementary) partial mediations. This suggests that parts of the link between PC and comment letter receipt remain unexplained due to the assumed attention effect, which in itself prompts future research. The proportion of the relationship between PC and CL likelihood, that can be explained by this direct path, lies between 42 % (Log_PAC model) and 69 % (Log_Lobby model). These percentage shares represent the proportions of path C relative to the total effect. The total effect is the effect that results from the sum of the direct effect (Path C) and indirect effect (Path A × Path B).

Figure C.3:
Mediation Analyses

Figure C.3.1

SEC_Monitoring

(A) 0.0281***   (B) 0.3787***

Log_Lobby   ⟶   Comment Letter

(C) 0.0241***

Figure C.3.2

SEC_Monitoring

(A) 0.0264***   (B) 0.3801***

Log_PI_Lobby   ⟶   Comment Letter

(C) 0.0193***

Figure C.3.3

SEC_Monitoring

(A) 0.0511***   (B) 0.3830***

Log_PAC   ⟶   Comment Letter

(C) 0.0140**

Figure C.3.4

SEC_Monitoring

(A) 0.0489***   (B) 0.3830***

Log_PI_PAC   ⟶   Comment Letter

(C) 0.0142**
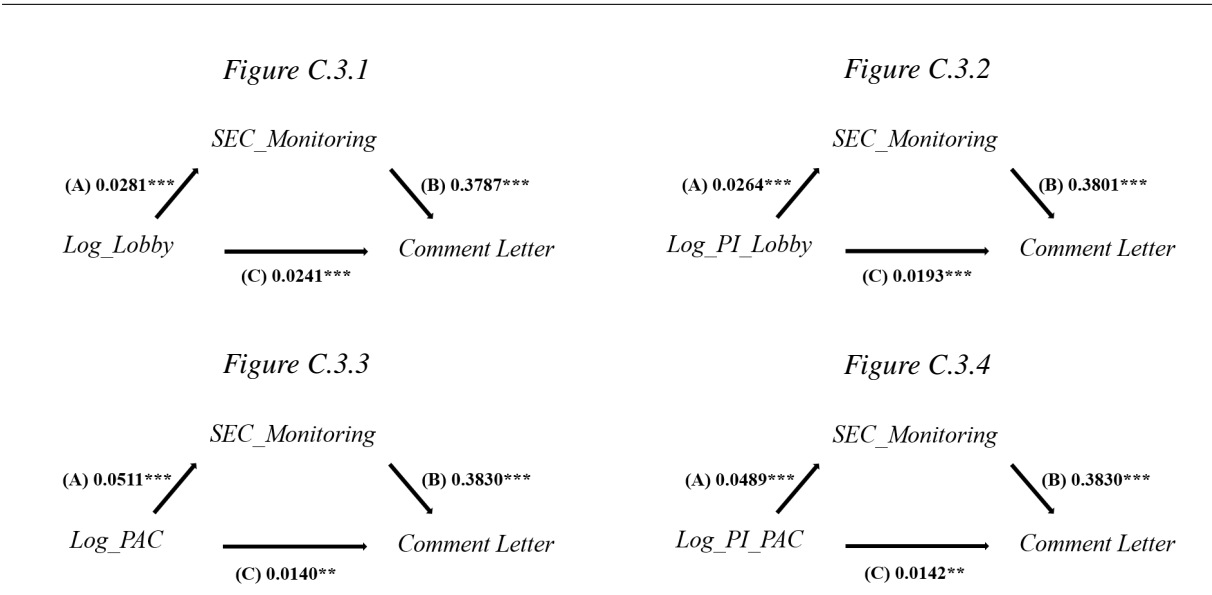
Table C.12:
Mediation Analyses: PC, SEC Monitoring, and Oversight

Panel A:		Lobbying Proxies for Political Connections			
		PC=Log_Lobby		PC=Log_PI_Lobby	
		Coeff.	z-stat	Coeff.	z-stat
Total Effect		0.035***	7.04	0.029***	6.25
Direct Paths					
A		0.028***	12.85	0.026***	12.70
B		0.379***	15.56	0.380***	15.63
C		0.024***	4.95	0.019***	4.17
	percentage	*69 %*		*66 %*	
Indirect Path					
A × B		0.011***	9.91	0.010***	9.86
	percentage	*31 %*		*34 %*	
Control Variables		Yes		Yes	
Fixed Effects		Year/Ind.		Year/Ind.	
Observations		15,114		15,114	

Panel B:		PAC Proxies for Political Connections			
		PC=Log_PAC		PC=Log_PI_PAC	
		Coeff.	z-stat	Coeff.	z-stat
Total Effect		0.034***	4.69	0.033***	4.69
Direct Paths					
A		0.051***	15.86	0.049***	15.44
B		0.383***	15.73	0.383***	15.74
C		0.014**	1.98	0.014**	2.05
	percentage	*42 %*		*43 %*	
Indirect Path					
A × B		0.020***	11.17	0.019***	11.02
	percentage	*58 %*		*57 %*	
Control Variables		Yes		Yes	
Fixed Effects		Year/Ind.		Year/Ind.	
Observations		15,114		15,114	

Table C.12 presents the results for the mediation analyses. CL receipt is the dependent and SEC monitoring is the mediation variable in all specifications. PC represents the independent variable. Panel A shows the mediation analyses for standard and long-term lobbying as a proxies for PC. Panel B exhibits the analyses for standard and long-term PAC as a proxies for PC. For all models we present the total effect, the three direct paths as well as the indirect path. We indicate the coefficient and the z-statistic in each case. For the indirect path and for path C (direct link from PC to CL receipt) we present the relative share of this path. All specifications include year and industry fixed effects, as well as control variables. See Appendix C.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

Conversely, this means that the indirect effect lies between 31 % and 58 %. In our mediation analyses, these indirect effects can be equated to the attention-grabbing effect. This means that the increased CL likelihood is explained by the path or the proportion of PC via SEC monitoring. Accordingly, this corresponds to a very substantial proportion of the overall effect, and illustrates that the theory of an attention-grabbing effect is based on sound empirical foundations. This answers the question to what extent the increased CL receipt likelihood of PC firms can be explained by SEC monitoring. In particular, this approach makes it possible to examine the actual behavior of rank-and-file employees of the SEC in order to explain a regulatory outcome.

For robustness reasons, we apply the mediation analysis approach according to Baron & Kenny (1986). Again, as in our GSEM analyses, we consider the following proxies for PC: Log_Lobby and Log_PI_Lobby as well as Log_PAC and Log_PI_PAC. In this regression-based approach, we estimate a series of different regressions (Baron & Kenny, 1986; Burt & Hampton, 2017). In particular, we estimate the following regressions:

First, we estimate the regression from the dependent variable ($Comment\_Letter$) on the independent variable (PC) with a logit regression.[48] These estimates can be found in Appendix C.C, Panel A, showing a positive and significant effect for each PC variable.

Second, the regression of the mediator ($SEC\_Monitoring$) on the independent variable (PC). We already estimated this in section 4 and found a positive and significant effect for all PC coefficients on $SEC\_Monitoring$.

In the third step, we investigate the combined effect of SEC monitoring and PC on CL issues. Although $SEC\_Monitoring$ – especially measured in the way we provided – captures the entire SEC oversight activity, DCF filing review activity is predominantly represented (Iselin et al., 2022). As filing review is conditional for a comment letter receipt (Gunny & Hermis, 2020), we

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[48]Whether checking this total effect is a necessary condition is controversial in the literature (e.g., Hayes, 2022, pp.119–128).

expect a significantly positive relation between $Comment\_Letter$ and $SEC\_Monitoring$. We control all our analyses for time trends and industry characteristics using year and industry fixed effects. In addition, we include our standard control variables. Our findings are presented in Appendix C.C, Panel B.

As expected, we find a significantly positive relation between $Comment\_Letter$ and $SEC\_Monitoring$ for all our specifications, indicating that SEC monitoring increases a firm's likelihood of receiving a comment letter. The results suggest that a significant part of SEC monitoring activity belongs to DCF filing review. In connection with the steps carried out before, we can infer mediation effects. Also for our four proxies for PC, we find positive significant effects on the CL likelihood. Thus, like our GSEM approach, this also supports the existence of a partial and complementary mediation for each variable of PC. However, we find the coefficients for the PC variables Log_PAC and Log_PI_PAC are only significant at the 10 % level (B 3 and B 4 in Appendix C.C – Panel B). This again underlines our findings that a large part of the increased CL likelihood can be explained by the attention-grabbing effect of PC. However, the Baron & Kenny (1986) approach does not allow us to calculate percentage values.

6 Conclusion

Prior research finds ambiguous results whether SEC oversight is captured by PC firms, but frequently suffers from a missing ability to observe actual SEC activity when observing outcomes like CL or AAERs and a focus on only one division in each case. We provide a novel approach to shed fuller light on the influence of PC on SEC monitoring and its role withing the entire SEC oversight activity, by measuring SEC monitoring with SEC initiated EDGAR downloads. We find PC is increasing SEC monitoring in general. As a result, we are able to gain a deeper insight into the behavior of the SEC's rank and file employees.

Bringing our results together, we can find a robust positive relationship between PC and SEC monitoring. This correlation speaks for an attention-grabbing effect of PC, like Heese et al. (2017) assumed. This is underlined as we consider our measure of SEC monitoring as a direct measure of SEC behavior. As we demonstrate in our mediation analyses, the attention-grabbing effect represents a substantial share of the increased CL likelihood of PC firms. There are various factors that could explain the SEC's increased awareness towards PC firms.

The first and most immediate reason is that firms' lobbying expenditures are of high transparency in the US and, thus, attract increased general attention. The second reason is the expected rumor caused by lobbying and PAC contributions, especially if it is directed to the SEC. The third is the potential attention resulting from personal relationships between current SEC staff and former staff now acting as lobbyists. The fourth explanation is a indirect and unintentional channel in the political process, that these PC firms exert pressure within the iron triangle relationship and thereby bring these firms into the focus of the SEC, possibly unintentionally and not related with the SEC oversight. For example, political involvement during the SEC's rulemaking process could be such a case.

However, our study is also subject to limitations. The first relates to our measure of SEC monitoring. Our SEC monitoring measure covers the entire SEC download activity and does not differentiate EDGAR downloads to distinct SEC divisions or offices. Thus, we cannot explain the impact of PC in different stages and divisions of the SEC oversight process. In addition, there are, of course, other channels through which SEC staff can obtain information about firms. Another limitation is that there could be other factors related to PC, such as certain financial reporting characteristics which are also correlated with PC and drive our results. For example, Chaney et al. (2011) found that earnings quality is lower for PC firms than for non-PC firms, and Braam et al. (2015) found that PC firms substitute real earnings management for accrual-based

earnings management. Through our additional analyses, however, we have tried to address this endogeneity problem.

These factors could, therefore, also explain why we only find partial mediation in our mediation analysis. Thus, future research could look at which other factors of PC are relevant besides the attention-grabbing effect. In addition, the role of the attention-grabbing effect in other divisions of the SEC (especially the DoE) may also be worth investigating.

Variable	Definition
Primary Dependent Variable	
SEC_Monitoring	The natural logarithm of 1 + the total number of SEC-initiated firm-specific EDGAR downloads per year.
Political Connections Variables	
Lobby	The total amount of lobbying expenditures made by the firm during the fiscal year.
Log_Lobby	The natural logarithm of 1 + the total amount of lobbying expenditures made by the firm during the fiscal year.
PI_Lobby	The total amount of lobbying expenditures made by the firm over the previous three years.
Log_PI_Lobby	The natural logarithm of 1 + the total amount of lobbying expenditures made by the firm over the previous three years.
PI_Lobbyist_linked_to_SEC	Indicator variable equal to 1 if the firm employed at least one lobbyist within the previous three years that either previously worked for the SEC or is currently employed by the SEC, 0 otherwise.
PI_Lobby_linked_to_SEC	The total amount of lobbying expenditures made by the firm through a lobbyist linked to the SEC over the previous three years.
Log_PI_Lobby_linked_to_SEC	The natural logarithm of 1 + the total amount of lobbying expenditures made by the firm through a lobbyist linked to the SEC over the previous three years.
PI_Lobby_SEC	Indicator variable equal to 1 if the firm lobbied the SEC directly over the previous three years, 0 otherwise.
ACC_Dummy	1 if the firm lobbied for accounting issues, 0 otherwise.
FIN_Dummy	1 if the firm lobbied for finance issues, 0 otherwise.
DoJ_Dummy	1 if the firm lobbied the Department of Justice directly, 0 otherwise.
PAC	Total amount of PAC contributions made by the firm during the fiscal year.
Log_PAC	The natural logarithm of 1 + the total amount of PAC contributions made by the firm during the fiscal year.
PI_PAC	The total amount of PAC contributions made by the firm over the previous five years.
Log_PI_PAC	The natural logarithm of 1 + the total amount of PAC contributions made by the firm over the previous five years.
PI_Related	The total amount of PAC contributions made to politicians that serve in an SEC oversight committee (Banking, Commerce or Appropriations committee) in the current election cycle.

Log_PI_Related	The natural logarithm of 1 + the total amount of PAC contributions made to politicians that serve in an SEC oversight committee (Banking, Commerce or Appropriations committee) in the current election cycle.

SEC Oversight Variable

CL	CL is a indicator variable equal to 1, if a firm receive a 10-K related comment letter for year *t+1* (Source: EDGAR).

Firm Characteristics Variables

Log_Market_Cap	The natural logarithm of 1 + the firm's market capitalization.
Market_to_Book	Firm's market-to-book-ratio.
Low_Market_to_Book	1 if Market_to_Book is lower than 1.
Loss	1 if a firm reported a loss in year t, 0 otherwise.
Zscore	Altman's Z-score based on Altman (1968) is equal to $1.2\times$((total current assets - total current liabilities)/total assets) + $1.4\times$(retained earnings/total assets) + $3.3\times$(earnings before interest and taxes/total assets) + $0.6\times$(market capitalization/total liabilities) + $1.0\times$(total sales/total assets).
Leverage	Is equal to the sum of long-term debt and total current liabilities divided by total shareholder equity.
Change_Sales	Is the percentage of change in annual sales.
Log_SEC_Office_Dist	The natural logarithm of 1 + the distance in miles to the closest SEC office (regional offices or the headquarter).
Age	A firm's age in years; Based on the first occurrence of accounts in Datastream.

Additional Variables

Agg_SEC_Downloads	The natural logarithm of 1 + the total number of all SEC-initiated EDGAR downloads per year.

Instruments

Log_Sum_Industry_Lobby	The natural logarithm of 1 + the total amount of lobbying by other firms within the same 4-digit SIC industry.
Log_Sum_Industry_PI_Lobby	The natural logarithm of 1 + the total amount of long-term lobbying (three years) by other firms within the same 4-digit SIC industry.
Log_Sum_Industry_PAC	The natural logarithm of 1 + the total amount of PAC contributions by other firms within the same 4-digit SIC industry.

Log_Sum_Industry_PI_PAC	The natural logarithm of 1 + the total amount of long-term PAC contributions (five years) by other firms within the same 4-digit SIC industry.
Log_Sum_Industry_PI_Related	The natural logarithm of 1 + the total amount of long-term PAC contributions made to politicians that serve in an SEC oversight committee (Banking, Commerce or Appropriations committee) in the current election cycle by other firms within the same 4-digit SIC industry.
Voter_Turnout	The state-level voter turnout rate is calculated based on the voting-eligible population, as suggested by McDonald & Popkin (2001). For years without an election, the voter turnout of the previous year is assumed. The raw data is publicly available on the University of Florida Election Lab website.

Appendix C.B:
Fixed Effects Evaluation

Table Appendix C.B – Panel A:
Summary Statistics of Fixed Effects

| | Number of ... | | | Observations per group | | |
	Observations	Groups	Singletons	Min.	Avg.	Max.
SIC	15,114	333	13	1	45.39	1,049
Year	15,114	10	0	923	1,511.40	2,149
Joint singletons	.	.	0	.	.	.
Total singletons	.	.	13	.	.	.

Appendix C.B – Panel A shows that there are in total 13 singletons (0.086 % of all observations. Additionally, it shows the minimum, average, and maximum of observations per fixed effect group)

Table Appendix C.B – Panel B:

Variables that are Constant within a Fixed Effects Group

	Number of ...		SIC*		Year*	
	Obs	Singl	#Groups	#Obs	#Groups	#Obs
SEC_Monitoring	15,114	13	1	9	0	0
Log_Lobby	15,114	13	112	1,648	0	0
Log_Market_Cap	15,114	13	0	0	0	0
Market_to_Book	15,114	13	0	0	0	0
Low_Market_to_Book	15,114	13	88	1,141	0	0
Loss	15,114	13	53	521	0	0
Zscore	15,114	13	0	0	0	0
Leverage	15,114	13	0	0	0	0
Change_Sales	15,114	13	0	0	0	0
Log_SEC_Office_Dist	15,114	13	70	543	0	0
Age	15,114	13	72	596	0	0

Appendix C.B – Panel B shows the number of groups and observations that are constant within the fixed effects groups for the main dependent (*SEC_Monitoring*) and independent variables (*Log_Lobby* and controls). Columns with * were computed excluding singleton observations.

Table Appendix C.B – Panel C:
Residual Variation after Partialling-Out

| | N* | Std. Dev. | | | R2 by fixed effect | | R2 |
		Pooled	Within*	Ratio (%)	SIC	Year	Overall
SEC_Monitoring	15,101	2.0581	1.1982	58.22	0.050	0.631	0.661
Log_Lobby	15,101	5.4374	4.8277	88.79	0.211	0.000	0.212
Log_Market_Cap	15,101	2.4435	2.0705	84.73	0.277	0.006	0.283
Market_to_Book	15,101	10.7838	10.6163	98.45	0.030	0.002	0.032
Low_Market_to_Book	15,101	0.3880	0.3647	93.99	0.104	0.014	0.117
Loss	15,101	0.4820	0.4146	86.03	0.247	0.025	0.261
Zscore	15,101	24.0547	23.1338	96.17	0.070	0.006	0.076
Leverage	15,101	4.1448	3.9902	96.27	0.073	0.001	0.074
Change_Sales	15,101	0.7043	0.6905	98.03	0.035	0.005	0.040
Log_SEC_Office_Dist	15,101	2.2131	1.9825	89.58	0.197	0.002	0.198
Age	15,101	9.5367	7.4794	78.43	0.331	0.097	0.385

Appendix C.B – Panel C shows the variation lost or absorbed due to fixed effects. The table shows standard deviations and R2 measures for variation. It presents the standard deviation a pooled sample, for the within fixed effect standard deviation, and its ratio. The R2 measures show the proportion of fixed effect explained variation. Columns with * were computed excluding singleton observations.

Appendix C.C: Mediation Analysis in the style of Baron & Kenny (1986)

Table Appendix C.C – Panel A:

Political Connections and Comment Letter

	A 1	A 2	A 3	A 4
Log_Lobby	0.0315***			
	(5.96)			
Log_PI_Lobby		0.0263***		
		(5.27)		
Log_PAC			0.0278***	
			(3.69)	
Log_PI_PAC				0.0273***
				(3.65)
Log_Market_Cap	0.143***	0.148***	0.162***	0.162***
	(8.88)	(9.28)	(10.32)	(10.40)
Market_to_Book	-0.005	-0.005	-0.005	-0.005
	(-1.47)	(-1.46)	(-1.55)	(-1.54)
Low_Market_to_Book	-0.149*	-0.141*	-0.131*	-0.130
	(-1.89)	(-1.79)	(-1.65)	(-1.63)
Loss	0.137**	0.138**	0.143**	0.141**
	(2.17)	(2.18)	(2.26)	(2.23)
Zscore	0.001	0.001	0.001	0.001
	(0.62)	(0.60)	(0.53)	(0.54)
Leverage	0.001	0.001	0.002	0.002
	(0.17)	(0.19)	(0.24)	(0.24)
Change_Sales	0.060**	0.060**	0.058*	0.058*
	(2.02)	(2.02)	(1.95)	(1.94)
Log_SEC_Office_Dist	-0.148***	-0.149***	-0.152***	-0.152***
	(-10.95)	(-11.04)	(-11.27)	(-11.29)
Age	0.005	0.005	0.006*	0.006*
	(1.54)	(1.54)	(1.76)	(1.67)
Agg_SEC_Downloads	Yes	Yes	Yes	Yes
Fixed Effects	Year/Ind.	Year/Ind.	Year/Ind.	Year/Ind.
Observations	14,889	14,889	14,889	14,889
Pseudo R^2	0.132	0.131	0.130	0.130

t statistics in parentheses

Appendix C.C – Panel A shows the results for the estimation of a logit regression of Comment Letter (CL) on our main political connections proxies. CL is a indicator variable equal to 1, if a firm receive a 10-K related comment letter for year *t+1*. The variables of interest the political connections proxies Log_Lobby, Log_P_Lobby, Log_PAC, and Log_PI_PAC. All specifications include industry and year fixed effects, as well as control variables.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

Table Appendix C.C – Panel B:
CL Likelihood, SEC Monitoring, and PC

	B 1	B 2	B 3	B 4
SEC_Monitoring	0.379***	0.380***	0.383***	0.383***
	(16.36)	(16.39)	(16.51)	(16.51)
Log_Lobby	0.024***			
	(4.59)			
Log_PI_Lobby		0.019***		
		(3.87)		
Log_PAC			0.014*	
			(1.89)	
Log_PI_PAC				0.014*
				(1.94)
Log_Market_Cap	0.116***	0.121***	0.134***	0.134***
	(7.33)	(7.71)	(8.78)	(8.82)
Market_to_Book	-0.005	-0.005	-0.005	-0.005
	(-1.45)	(-1.44)	(-1.51)	(-1.50)
Low_Market_to_Book	-0.135*	-0.127	-0.116	-0.116
	(-1.70)	(-1.61)	(-1.46)	(-1.46)
Loss	0.081	0.082	0.088	0.086
	(1.27)	(1.29)	(1.37)	(1.36)
Zscore	0.002	0.002	0.001	0.001
	(1.29)	(1.27)	(1.18)	(1.19)
Leverage	0.002	0.002	0.002	0.002
	(0.24)	(0.26)	(0.33)	(0.32)
Change_Sales	0.043	0.042	0.040	0.040
	(1.42)	(1.41)	(1.34)	(1.34)
Log_SEC_Office_Dist	-0.121***	-0.122***	-0.125***	-0.125***
	(-9.04)	(-9.11)	(-9.29)	(-9.30)
Age	0.002	0.003	0.004	0.004
	(0.73)	(0.78)	(1.14)	(1.08)
Agg_SEC_Downloads	Yes	Yes	Yes	Yes
Fixed Effects	Year/Ind.	Year/Ind.	Year/Ind.	Year/Ind.
Observations	14,889	14,889	14,889	14,889
Pseudo R^2	0.151	0.150	0.149	0.149

t statistics in parentheses

Appendix C.C – Panel B shows the results for the estimation of a logit regression of CL on SEC_Monitoring and four different proxies for PC. CL is a indicator variable equal to 1, if a firm receive a 10-K related comment letter for year *t+1*. SEC_Monitoring corresponds to the natural logarithm of 1 + the total number of SEC-initiated firm-specific EDGAR downloads in year *t+1*. All specifications include year and industry fixed effects, as well as control variables.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

Part D:

Is the SEC "trumped"?
– Independence of US Financial Supervision from Presidential Influence

Abstract

The extent of presidential influence on independent agencies is one of the greatest questions in American public law. This paper discusses mechanisms of presidential influence on the SEC. I provide first evidence of an SEC's financial supervision change in line with former President Trump's policy. I find the SEC is lowering the level of financial supervision over American firms compared to foreign firms during Trump's presidency. Additionally, firms belonging to industries that are preferred by Trump's policy face a lower level and a lower complexity of financial supervision. These findings contribute to the literature of SEC capture by shedding light on the President's ability to influence SEC behavior.

1 Introduction

Independence of the United States Securities and Exchange Commission (SEC) is widely discussed in literature (e.g., Karmel, 2016b; Bressman & Thompson, 2010; Heese et al., 2017; Heese, 2019; Correia, 2014). However, relatively little is known about presidential influence on the SEC and its consequences. The SEC was founded in 1934 in response to the Wall Street Crash of 1929 as an independent agency to ensure investor protection and maintain efficient and fair markets (SEC, 2023a). Especially in non-US literature, the term "independent" is frequently misunderstood (Morrison, 1988). Unlike executive branch agencies which are under direct control of the US President, the term "independent" refers to the separation from executive, legislature, and judiciary and not to an actual grade of independence (Miller, 1988). These agencies are often described as "fourth branch" of the US federal government (e.g., Koslow, 1990). Nonetheless, also independent agencies are not fully independent from governmental influence. The Congress oversees SEC's operations, whereas the House has budget control. The President appoints SEC commissioners – with advice and consent of the Senate – and nominates the SEC chairman. Besides appointment, the President also has the power to remove agency heads for three causes: inefficiency, neglect of duty, and malfeasance in office (Manners & Menand, 2021; Sunstein & Vermeule, 2021). While these causes have never been defined by the Congress or the Courts, the question of whether they permit the President to remove agency heads at pleasure (e.g., for failing to follow directives), or only in case of unfaithfulness and incompetence is not to be answered unambiguously (Manners & Menand, 2021). The extent of presidential influence on independent agencies is designated as "one of the great unanswered questions in American public law" (Sunstein & Vermeule, 2021).

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Political science literature developed three main theories about why politicians intervene in regulation (Bischof et al., 2020). Regulatory capture theory (Stigler, 1971; Peltzman, 1976) is an economic description of politicians' special (self-)interests. Interest groups supporting politicians (e.g., by political contributions, Grossman & Helpman (1994)) to favor special treatments by agencies as they are dependent on congressional funding. Heese (2019) argues that regulatory capture not only results from firm's political connections, but also from politicians seek to maximize political support in the form of votes. Public interest theory sees politicians as persons of character acting in the best interest of the public (e.g., Pigou, 1938; Wittman, 1977; Alesina & Tabellini, 1988; Callander, 2008; Hail et al., 2018). Besides special interests, politicians' ideology – a set of principles and core beliefs about politics – plays an important role in decision-making (e.g., Kau & Rubin, 1979; Kalt & Zupan, 1984; Mian et al., 2010). Ideology could result from a politician's personal beliefs (e.g., Smith et al., 2012) or from more rationale motives like signaling to voters (Kalt & Zupan, 1984; Poole & Rosenthal, 1996).

Prior empirical research found the SEC is affected by political influence in different ways. In line with capture theory, Yu & Yu (2011) find that firms with lobbying expenditures have a significantly lower hazard rate for fraud detection. Correia (2014) tests for Political Action Committee (PAC) contributions and lobbying and finds that politically connected firms on average are less likely to be involved in SEC enforcement actions and face lower penalties if prosecuted by the SEC. Contrary, Heese et al. (2017) and Khokhar & Shahriari (2022) find that political connections are positively connected with SEC supervision as politically connected firms are more likely to receive a 10-K related comment letter (Heese et al., 2017) respectively to be targeted by enforcement actions (Khokhar & Shahriari, 2022). In addition, Heese (2019) finds the SEC's behavior also reflects voter's interests. Relatively little attention has been paid so far on the effect of politicians' ideology on SEC behavior.

An obvious break in politicians' ideology came along with Donald Trump's presidency. His political ideology – strikingly represented by the phrase "Make America Great Again" – is characterized by preference of specific industries (e.g., fossil energy or steel and aluminum) as well as an "America first" agenda resulting in a strong preference of US firms over foreign firms.

In this paper I investigate whether SEC's financial supervision[49] changed during Donald Trump's presidency, thus if the SEC is "trumped". In that case I would expect a lack of independence leading to oversight actions in line with Trump's politics. In that case and in line with Donald Trump's political ideology, I would expect the SEC to prefer either US firms in general over foreign firms or US firms belonging to specific industries over others in this time.

To measure agency preferences, a common approach relies on observed agency behavior (Clinton et al., 2012). Prior research mainly used AAERs (e.g., Kedia & Rajgopal, 2011; Correia, 2014; Heese, 2019) or comment letters (e.g., Heese et al., 2017; Gunny & Hermis, 2020; Gietzmann & Pettinicchio, 2014; Baugh et al., 2021) as a measure for SEC activity. As this paper focuses on SEC financial supervision activity, comment letters are used as an observable SEC behavior. Within their financial oversight process, the SEC's Division of Corporation Finance (DCF) reviews firms filings. In case of accounting or reporting mistakes, obscurities or potential deficiencies, a comment letter is issued to the filer. Afterwards, this firm has a limited number of days to respond to the SEC, either by correcting the mistake or by explaining obscurities. To ensure integrity and effectiveness of the review process, selection criteria are not publicly disclosed (SEC, 2023c). As comment letter receipts could lead to increasing costs for firms like tax or audit fees (Baldwin et al., 2013; Gietzmann & Pettinicchio, 2014; Kubick et al., 2016), firms are interested in preventing comment letter receipts. I use comment letter data

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[49]Please note that the term "financial supervision" refers to the SEC's filing review, conducted by the Division of Corporation Finance, in contrast to "financial oversight" that denotes the entire oversight process, including enforcement.

relating to 10-K and 20-F filings available on EDGAR for the years 2012 to 2020 to test for the hypothesis of the SEC as being "trumped".

I find United States (US) firms in general are more likely to receive a comment letter over the entire period. For both, US and foreign firms, the likelihood is lower in this period. The difference in likelihoods is significantly greater for US firms than for foreign indicating a change in financial supervision by the SEC which might result from a preference of US firms over foreign firms in Trump's presidency. I further find firms belonging to industries being preferred by Trump's politics have a significantly lower likelihood for a comment letter receipt and face significantly shorter comment letter processes, measured by the number of rounds, indicating a less complex process for these firms. A robustness check for firms explicitly not being preferred by Trump's politics indicates that SEC's financial supervision is still strong for these firms, although the comment letter likelihood decreased in general in Trump's presidency. I provide first evidence for a change in SEC's financial supervision in Trump's presidency. The findings indicate that the SEC acts in line with Trump's political ideology. I contribute to prior literature by providing evidence about the absence of SEC's political independence not based on capture theory, public interest theory, or voter's interests theory, but based on political ideology. Further, I strongly pronounce presidential influence on the SEC more than congressional.

The remainder of this paper proceeds as follows: Section 2 provides background information on political influence on independent agencies and SEC comment letters. Section 3 develops the hypotheses. Section 4 explains about the data, research design, and descriptive statistics. In section 5, I discuss the empirical results, robustness checks, and limitations, whereas section 6 concludes and shows future research options.

2 Background

2.1 Political Influence on Independent Agencies

Independent agencies differ from executive branch agencies in the way that they are insulated especially from presidential control and directive in at least some ways (Corrigan & Revesz, 2017; Bressman & Thompson, 2010; Verkuil, 1988).[50] A common approach to define independent agencies is that their heads are protected against presidential removal at will (e.g., H.L.R., 2013; Sunstein & Vermeule, 2021).[51] Nevertheless, prior literature describes about political control by Congress and President on bureaucratic agencies and provides empirical evidence. These theories include both the underlying mechanisms as well as politicians' incentives and motivation to intervene in bureaucratic agencies' activity.

The extent of presidential influence on independent agencies is designated as "one of the great unanswered questions in American public law" (Sunstein & Vermeule, 2021). There are three major mechanisms of presidential influence on independent agencies imaginable: the removal of commissioners, their appointment, and the nomination of the chairman. The discussion about it started with President Roosevelt's removal of William E. Humphrey serving as a commissioner for the Federal Trade Commission (FTC) because of political reasons (Selin, 2015). As a consequence, the U.S. Supreme Court ruled that the President is allowed to remove a commissioner in agencies like the FTC only for specified reasons (U.S. Supreme Court, 1935). These "for cause" reasons are inefficiency, neglect of duty, and malfeasance in office[52] and thus not politically motivated will (Manners & Menand, 2021; Sunstein & Vermeule,

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[50]There is no legal definition on "independent agency" (also designated as "independent regulatory agency" or "federal independent regulatory agency" (e.g., Karmel, 2016a)) existent.

[51]Although independence from presidential removal is the common defining element, other aspects like control of litigation or funding also contribute to agencies' independence (Breger & Edles, 2015). A systematization of agency independence has been provided by Piering (2024a). However, please mind the differentiation between "independent agency" as an agency type in the US and the actual grade of agency independence.

[52]These terms are sometimes abbreviated to "INM" (Sunstein & Vermeule, 2021; Manners & Menand, 2021).

2021). With the *Free Enterprise Fund* decision, the U.S. Supreme Court assumed in 2010 that the for-course removal restrictions from the *Humphrey's Executor* decision are also valid for the removal of SEC commissioners (U.S. Supreme Court, 2010). Nevertheless, the terms "inefficiency", "neglect of duty" and "malfeasance in office" have never been legally specified by the Supreme Court and a commonly accepted definition is not existent (Lessig & Sunstein, 1994). Frequently, the terms "malfeasance in office" and "neglect of duty", which are grounded in English common law, are understood as failures to faithfully execute legal duties like erroneous decisions of policy and law, and corruption, whereas "inefficiency" deals with wasteful, clumsy, and lazy behavior (Manners & Menand, 2021; Sunstein & Vermeule, 2021). Academics widely discuss the limits of these terms. Lessig & Sunstein (1994) see frequent or important failures of commissioners to follow the President's wishes as a good cause for presidential removal. Strauss (1989) suggests that a refusal to follow certain presidential directives might justify a commissioner's removal. Shane (1989) only considers failure to comply with a legal mandate as a good cause for removal. Manners & Menand (2021) see these terms as authorizations for Presidents to remove unfaithful or incompetent agency heads, but not for failing to follow presidential directives. In contrast, Miller (1986) sees presidential directives as instructions that officials have to follow, thus non-compliance with these directives can be considered as "neglect of duty" or "malfeasance". Sunstein & Vermeule (2021) point out two opposing views on presidential authority over independent agencies: a minimalist approach with a very narrow interpretation of the INM terms leading to *policy independence*, and a maximalist approach which provides the President *broad policymaking control*. They evolve another approach of *presidential review* that allows the President to remove a commissioner for violating statutory responsibilities and thus includes policy arguments. They see the existing statutes granting Presidents a significant degree of authority over independent agencies. The protection against

removal at will is sometimes seen as the core characteristic of independent agencies (Miller, 1988). But, as shown above, the terms for removal have never been defined by the Congress or the Courts, and thus the question of whether they permit the President to remove agency heads at pleasure (e.g., for failing to follow directives), or only in case of unfaithfulness and incompetence is not to be answered unambiguously (Manners & Menand, 2021). While others don't do, H.L.R. (2013) concludes that SEC commissioners are removable at will. As a consequence of the uncertainty in this issue, commissioners can't be sure not to be removed by the President for political and policy reasons.

Besides removal, also the appointment of commissioners is a potential gateway for presidential influence (e.g., Chu & Garvey, 2015). In the past, Presidents used appointees in agencies' leaderships for gaining control over policymaking (Heclo, 1977; Lewis, 2008; Selin, 2015). There is anecdotal evidence that, in prior administrations, Presidents used to place agency heads that firmly believe in their view of government (e.g., Morrison, 1988). The former SEC Commissioner Roberta S. Karmel stated that, in recent times, the agency heads qualifications were based on "ideological correctness rather than expertise" (Karmel, 2016b). Nevertheless, the possibilities for appointments are not without limitations. The President appoints SEC commissioners – with advice and consent of the Senate – and nominates the SEC chairman.

To limit a clear political alignment, only three commissioners shall be members of the same political party (15 U.S.C. § 78d). This would mean at maximum a relation of 3:2 between the largest political parties, Republicans and Democrats. In practice, the nomination of SEC commissioners is highly partisanship- and ideology-depending rather than expertise-based (Karmel, 2016a). Although this constellation allows one political party to own the majority on the commission, the US Senate has to consent to the nomination of the commissioners (15 U.S.C. § 78d). Because of that, there is no freedom for the President to appoint any candidate

just by will, but with respect to balance of political powers (Karmel, 2016a). Furthermore, Presidents typically are not able to appoint a majority of commissioners very fast (Devins & Lewis, 2008). But, once the President appointed a majority, independent agencies are likely to agree to presidential preferences (Devins & Lewis, 2008).

A particular focus is on the role of the SEC's chairman (who is part of the Commission) and who is nominated by the President. A trend of the chairman belonging to the President's party is observable (see Appendix D.B).

The dependencies – more precise characterized as an exchange of interests and favors relationship – between Congress, interest groups, and bureaucratic agencies have first been described in the "iron triangle" literature (Freeman, 1965; Adams, 1982). The relation between Congress and bureaucratic agencies is modeled by the Congressional Dominance Theory (Weingast, 1984; Weingast & Moran, 1983; McCubbins, 1999; Miller, 2005; Oritani, 2010). According to the principal agent problem, the Congress delegates responsibilities to bureaucratic agencies. Additionally, it implements monitoring systems and sets incentives for the agencies to act in line with the Congresses goals. The Congress can either use budget setting (Weingast, 1984), congressional oversight (Weingast, 1984; Weingast & Moran, 1983; McCubbins, 1999) or the appointment and removal of commissioners (Shotts & Wiseman, 2010) to push agencies for decisions that are in line with their interests. Additionally, considerations regarding agencies' commissioners' career concerns are important to understand further motivation for acting in line with politicians' interests. Commissioners often have political careers prior or after their SEC tenure, which provides an incentive to act in line with politicians' interests (Alesina & Tabellini, 2007).[53]

The politicians' interests are reflected by three main explanations: capture theory, ideology theory, and public interest theory (Kothari et al., 2010; Bischof et al., 2020; Hail et al., 2018;

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[53]For an overview of current and previous SEC commissioners, see SEC (2023b).

Allen & Ramanna, 2013). Capture theory describes politicians seek for support of interest groups by votes or money in exchange for favorable regulation (Stigler, 1971; Peltzman, 1976). Interest groups support politicians by political contributions (Grossman & Helpman, 1994). The exchange of political support and wealth transfer often takes place in case of long-term relationships between firms and politicians (Snyder, 1990). These politicians' interests are designated as *special interests*. Following the triangle relationship, interest groups could trigger special treatment from agencies like low regulation if they support the Congress because the agencies are dependent on congressional funding and political support. A link between political expenditures and reduced discretionary regulatory enforcement can be observed in the absence of political interference if firms use political contributions to signalize their willingness to pursue one's policy goals and to fight agency decisions (Gordon & Hafer, 2005).

Voters anticipate agencies' special-interest favors for firms lobbying to politicians (political cost hypothesis, Watts & Zimmerman, 1978). Thus, beside special interests, politicians' influence on regulatory agencies is also motivated by *voters' interests* as politicians seek to maximize the number of votes. (Heese, 2019; Stigler, 1971; Peltzman, 1976).

Another strand of literature considers regulators as persons of character acting in the best *public interest* (Pigou, 1938; Wittman, 1977; Alesina & Tabellini, 1988; Callander, 2008; Hail et al., 2018). This theory argues that markets are imperfect and politicians see their mission to correct these imperfections with socially optimal legislation (Posner, 1974). Nevertheless, the literature provides evidence tending stronger to principal-agent based capture theory (Bischof et al., 2020).

A third main view on politicians' motivation to intervene in agencies decisions is *politicians' ideology* (e.g., Kau & Rubin, 1979; Kalt & Zupan, 1984; Poole & Rosenthal, 1996; Hail et al., 2018). Ideology is a consistent set of normative statements and principles (Kalt & Zupan, 1984)

which is independent of self-interest motivation (Kau & Rubin, 1979). Common approaches of ideology-differentiation are liberal–conservative, left–right (Poole & Rosenthal, 1996), or socialistic–capitalistic (Hail et al., 2018). The origin of a politician's ideology might lie in personal characteristics and history like genetics (Smith et al., 2012), or in more rational calculation regarding communication to voters (Kalt & Zupan, 1984). Separating the effects of economic interests from ideology has been challenging in prior literature (Mian et al., 2010). Regarding the appointment of commissioners, presidential preferences and choices are driven by ideology (Devins & Lewis, 2008).

A last possible reason for political influence might be an uninformed politician (Hail et al., 2018) which might lead to aimless influence.

2.2   Evidence on SEC Independence

Prior literature provides evidence on SEC's independence. It considers mainly firm's political connections, lobbying expenditures, and political contributions, resulting in political influence that put pressure on SEC supervision and enforcement. Thus, prior literature mainly argues with economic interests like special-interests and voter's interests. Kedia & Rajgopal (2011) analyze the efficacy of the SEC's enforcement program and investigate whether a firm's propensity to adopt aggressive accounting practices is influenced by the firm's awareness of SEC enforcement. They find that firms located closer to SEC offices and located in areas with greater past SEC enforcement activity are less likely to restate their financial statement. They further find that the SEC is more likely to investigate firms located close to SEC offices and with higher visibility. Kedia & Rajgopal (2011) conclude that the SEC enforcement is not as effective as it could be due to various ex-ante information sets of managers that influence their willingness of misreporting and thus accounting quality. Following capture theory, Yu & Yu (2011) investigate whether firms' lobbying expenditures influence fraud detection. They find that lobbying firms have a

significantly lower hazard rate for fraud detection, evade fraud detection over 100 days longer, and are less likely to be detected by regulators by around 40 %. Correia (2014) investigates whether firms with political connections have lower SEC enforcement costs. Two different stages of the SEC enforcement process should indicate this: the enforcement action decision against a firm and the regulatory penalties a firm must pay. She finds that politically connected firms on average are less likely to be involved in SEC enforcement actions. Additionally, these firms face lower penalties if they are prosecuted by the SEC. Long-term political action committee contributions and lobbying expenditures are used as indicators for political connections. Correia (2014) suggests that the SEC's enforcement actions are not only influenced by considerations about the specific case, but also by other impacts and wonders whether the enforcement process is effective. Heese et al. (2017) state that SEC oversight not only consists of enforcement actions, but also of the comment letter review process by the DCF. It would not be possible to make a point about how blatant SEC capture is likely to be by focusing only on enforcement actions like prior studies do. Thus, they investigate whether firm's political connections predict comment letter reviews to control for SEC capture. Based on a sample of 10-K comment letters to US domestic firms issued between 2005 and 2012 they examine the relation between the incidence of comment letter receipt and political connection. Contemporaneous lobbying expenditures and contemporaneous political action committee donations are used as measures for political connections. Heese et al. (2017) find – contrary to prior research – a positive association between political connectedness of firms and the likelihood of comment letter issuance. These findings indicate that political connection attracts greater SEC oversight. They further find that comment letters that are issued to politically connected firms contain more core and non-core earnings topics, take more days and rounds to conclude, and are more likely to involve a supervisor. Heese et al. (2017) conclude that SEC oversight is – in contrast to prior investigations – not captured

or lax regarding political connections of firms. Instead, political connections seem to be a hint for extra scrutiny in the comment letter review process. In addition, Heese (2019) points out that not only firm's political connections could be a reason for political influence on the SEC, but also voters' interests. He investigates whether voters' interests are reflected in the choice of SEC's enforcement targets. This examination does not cover SEC oversight in general, but especially SEC enforcement actions. He finds that large firms are less likely to be targeted by SEC enforcement actions. These large firms are also less likely to experience enforcement actions during presidential elections if they are based in a politically important state, and if they are based in high-unemployment states during elections of senators who serve on SEC oversight committees. Further, large firms that are located in high-unemployment districts face lower enforcement actions in case that their congressmen serve on SEC oversight committees. Heese (2019) concludes that voters' interests are reflected in SEC enforcement actions. Mehta & Zhao (2020) document that SEC enforcement decisions have significantly negative consequences for politicians' election outcomes in case a financial misconducting firm is located close to the politician. To limit potential negative career effects, SEC-relevant politicians (having oversight responsibilities) influence the SEC.

2.3   Evidence on SEC Comment Letters

Comment letters are observable outcomes of the SEC and thus an appropriate measure of SEC financial supervision behavior conducted by the DCF. Prior literature examined the determinants and the effects and consequences of comment letter receipts on companies. Comment letter receipts depend both on firm and SEC characteristics. The probability of a firm's comment letter receipt is mainly driven by the Sarbanes-Oxley Act of 2002 (SOX) Sec. 408 criteria as well as low profitability, high complexity, small audit firm engagement, and governance weakness (Cassell et al., 2013). The number of comment letter receipts is directly influenced by the CFO's

management experiences (Ertimur & Nondorf, 2006). Furthermore, comment letters might be an indicator of Corporate Governance quality and compliance with disclosure requirements (Ettredge et al., 2011). SEC business affects the likelihood of comment letter receipts (Gunny & Hermis, 2020) as well as comment letter quality (Ege et al., 2019), whereas SEC reviewer idiosyncrasies could influence cross-sectional variation in comment letter issues (Baugh et al., 2021).

Comment letter receipts increase the probability of an auditor's change and, thus, audit fees might increase (Baldwin et al., 2013). This initial rise persists in the following periods (Gietzmann & Pettinicchio, 2014). As audit fees are an appropriate measure of accounting quality, a comment letter receipt seems to be an evidence of poor accounting quality (Hribar et al., 2014). Comment letters also affect corporate taxes as firms receiving a tax-related comment letter decrease their tax avoidance behavior and face an increase in expected tax costs (Kubick et al., 2016). As comment letters seem to affect future financial reporting outcomes, one can predict future restatements and next-year write-downs (Ryans, 2020). Some further evidences could be found not having monetary consequences. An effect often observed is a decrease in information costs as comment letters are associated with a decrease in information asymmetry (e.g., Bozanic et al., 2017; Johnston & Petacchi, 2017). The more comment letters are issued to a firm over time and the more severe they are, the likelihood of a CFO replacement increases (Gietzmann et al., 2016). In case of qualitative disclosures, firms not receiving any comment letter modify their next year's filings if a peer, rival or industry leader receives a comment letter on its filing ("spillover effect") (Brown et al., 2018).

On the capital market's side, one can observe a decrease in shares of institutional investors after a comment letter receipt (Gietzmann & Isidro, 2013). A comment letter issue also leads to increasing information asymmetry between institutional and private investors (Johnson et al.,

2021). The effects of a comment letter receipt are stronger for firms with a higher proportion of institutional investors (Duro et al., 2019). For foreign firms, negative-tone language comment letters – in contrast to positive –, lead to significant investor reactions (Chantziaras et al., 2021).

3 Hypothesis Development

As resources of the SEC are constrained, a necessity for filing review and enforcement targets choice is given. While details about filing review selection criteria as well as about the selection and decision process itself regarding comment letters or AAERs are not publicly communicated, influence from external stakeholders, like reviewed firms, lobbying agencies, and politicians, might be effective. Prior literature provided empirical evidence on SEC independence, mainly focusing on economic interests and capture theory (Correia, 2014; Yu & Yu, 2011; Heese et al., 2017; Heese, 2019). The underlying mechanism assumed by this literature is mainly the Congressional Dominance Theory, where Congressmen – especially those being members of SEC oversight committees – use congressional oversight and budget setting to put pressure on the SEC's decisions. However, empirical evidence on the President's influence on the SEC has not been provided so far.

Anecdotal evidence reports on at least attempted influence of Presidents on the SEC. During the 2008 presidential election campaign, Senator John McCain claimed, he would fire the SEC's chairman if he were President (Mason, 2008; Karmel, 2016b; H.L.R., 2013). Although this statement was soon rectified by his campaign in the way that the President has no power to fire the chair by will, the McCain campaign pronounced that he could pressure the chairman for resignation (Moran, 2008).

The discussion about presidential influence on independent agencies – especially on the SEC – became topical once again with the presidential campaign of Donald Trump for mainly two reasons:

First, Trump explicitly targeted the SEC with his political agenda. He asked the SEC to end quarterly earnings reports and grounded the necessity with cost benefits and greater business flexibility a twice-yearly disclosure system would have (Trump, 2018). As of December, 2018, the SEC seemed to fulfill Trump's demand as it started to review the quarterly earnings reports process by seeking comments on this process. During his campaign, Trump engaged Paul Atkins, a former SEC commissioner, advising him on vacancies and policy decisions regarding the SEC. As the former chair Mary Jo White left the SEC in January, 2017, Trump had the opportunity to nominate three commissioners including a new chairman. Immediately before Trump's presidency began, Das & Wolff (2016) saw the appointment of a new chairman as the "starting point for realignment" at the SEC. In response to Paul Atkins' statements regarding future SEC policy, Das & Wolff (2016) expected at least a general slowing down in enforcement areas, while they thought it premature to suggest about a weaker enforcement against large financial institutions.

Second, Trump's understanding of political action suggested at least attempted influence on independent agencies. Shane (2016) assumed Trump to treat the federal bureaucracy like the cast of *The Celebrity Apprentice*[54]. He stated that this understanding of politics, including a kind of "fire-mentality", is reflected in the so-called *unitary executive theory*. This theory bases on Article II of the Constitution of the United States which vests the President with the executive power. Unitarians argue, that the wording of Article II – *the* executive power – does

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[54]*The Apprentice* and its spin-off *The Celebrity Apprentice* were TV-shows hosted by Donald Trump, in which he looked for a future employee for one of his companies. In each episode, one candidate had to leave the show because of poor performance. His phrase "You're fired!" became characteristic for Trump and his TV-show.

not let executive power be subdivided and thus the President needs to control about independent agencies (Shane, 2016).

Rarely, political actions and decisions were more difficult to foresee as under the presidency of Donald Trump. Traditional political conventions did not seem to be in force as he broke the mold of bilateral partnerships and changed fundamental political strategies. These breaks could be observed in nearly every political section. A key slogan used during his campaign was "America first". On November 21, 2016, he described his „America first"-vision as he wanted "the next generation of production and innovation to happen right here on our great homeland, America", regardless of whether it would be "producing steel, building cars, or curing disease". He wanted to "create wealth and jobs for American workers." (Trump, 2016b). The political actions that were supposed to reach this goal consist of various parts. First, Trump announced to withdraw from trade deals or renegotiate them (Trump, 2016a). He called the Trans-Pacific Partnership (TPP) a „potential disaster" for his country and pronounced to withdraw from it within his first days of presidency (Woolf et al., 2016). In the first presidential debate in 2016, Trump termed the North American Free Trade Agreement (NAFTA) with Canada and Mexico "the single worst trade deal ever approved" in the United States which he would either renegotiate or break (POLITICO staff, 2016). Finally, the trade pact was replaced by the Agreement between the United States of America, the United Mexican States, and Canada (USMCA) which was signed on 30th September, 2018. In both cases, Trump saw a major discrimination against American firms. In a speech at a metals recycling factory in Pennsylvania during his campaign, he suggested the TPP to "put the interests of foreign countries above our own" and declared it as the "death blow for American manufacturing" (TIME staff, 2016). As he declared his vision to revitalize the domestic economy, on average every 59th word in his speech was America, American, or Americanism. Second, Trump pledged to introduce an "End of Offshoring Act" to

discourage firms from producing in other countries and shipping goods back to the US tax-free (Trump, 2016a). Therefor he wanted to impose tariffs. Although such an act has not been introduced by the US Congress until now, various tariffs have been established since Trump's inauguration. Import tariffs on aluminum (10 %) and steel (25 %) have been ordered against most countries like Canada, Mexico, and the European Union excluding Argentina and Australia (SBS, 2018). Furthermore, Trump set import tariffs on solar panels (30 %) and washing machines (20-50 %) (Gonzales, 2018). In addition, Donald Trump imposed a tariff of 25 % on more than 800 strategically important goods imported from China starting on July 6, 2018 (Lawder & Blanchard, 2018).

As he was setting import tariffs or toughened trade agreements, Donald Trump obviously preferred American firms over foreign. Beside trade agreements and tariffs, other ways of privileging would be imaginable. All methods seem to have in common a creation of a "comfortable setting" for American firms. This setting could lead to a competitive advantage by increasing sales or improving a firm's financial situation. A weaker regulatory environment could also support a "comfortable setting" as it could lead to a better cost-benefit relation. One field of regulation can be seen in the SEC's financial supervision. It becomes visible – and for firms also perceptible – by the issuance of comment letters. As stated above, firms might have great interest in avoiding a comment letter receipt through a number of negative consequences like increasing costs or negative capital market responses. Weakening the financial supervision only for American firms therefrom could improve their competitiveness and create a so-called "comfortable setting".

I assume this policy to result from different motives: Donald Trump's ideology is reflected as well as his special (personal) and voters interests. From the mechanisms of presidential influence on independent agencies, several reasons for the SEC following Trump's policy of

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preferring American over foreign firms in weakening financial supervision over American firms might be derived: First, the gaining of control over SEC policy can result from appointing commissioners and nominating a chairman that act in line with Trump's agenda. When Trump's presidency began, two commissioners' seats were vacant, while Mary J. White's term as SEC chair terminated. Thus, the new chairman, Jay Clayton, was of Donald Trump's preference. Lately in January, 2018, with the appointment of the Republican commissioner Pierce and the democratic commissioner Jackson, the SEC's commission was dominated by members selected by Trump. An overview of the composition of the SEC's commission is presented in Appendix D.C. Second, the uncertainties about removal at will could put pressure on the SEC commissioners. If a commissioner cannot be aware of protection against removal for political reasons, he will more likely act in line with Trump's agenda. In both cases, a direct and an indirect affection are imaginable. The direct affection needs a personal address to the commissioners by Donald Trump or his staff. The indirect affection results from a commissioner's personal awareness, either regarding his appointment circumstances or the uncertainty about removal at will. Whereas Naughton et al. (2018) were not able to detect a significant difference in monitoring between US firms and foreign firms, but a little weaker monitoring for cross-listed firms, one could imagine a change in Trump's presidency:

H1: SEC supervision prefers American firms over foreign firms in Donald Trump's presidency.

Coming back to Trump's initiated tariffs, these measures only target special goods respectively industries. A further look into his program and speeches reveals a list of specific industries he was going to support explicitly or implicitly. In Trump's "Contract with the American Voter", published during his campaign, he promised to lift restrictions on American energy reserves

targeting and supporting the oil, gas, and coal industry(Trump, 2016a). In the same document, he also promised to boost energy, water, and environmental infrastructure. This should be supported by an Energy and Infrastructure Act. With expanding infrastructure, also the construction industry would benefit. The tariffs mentioned above target special goods in order to support specific industries by increasing local sourcing and production and decreasing trades and imports. Mineral resources steel and aluminum should positively be affected explicitly. More implicitly, the renewable energies industry is supported by tariffs on solar panels. In the early days of his presidency, Donald Trump pledged to a group of bankers a fast deregulation and lower oversight level (Javers, 2017). Although not within the promised six months, the deregulation laws passed the Congress in 2018. In 2017, under Trump's presidency, the tax code was overhauled by the Tax Cuts and Job Act. Real estate businesses were allowed to take advantage of a tax break. The act was designated as a "windfall to real estate investors" (Browning & Bain, 2017).

Referring to H1, it could be helpful for reaching the target of "America first" to weaken regulatory oversight. It would be meaningful to have a closer look at only American firms. As described above, some of Donald Trump's promises or political actions target specific industries. For several reasons, these industries could be preferred implicitly or explicitly. This raises the question of whether a potential weakening of regulatory oversight does not occur constantly over all industries by the same level, but – in line with Trump's implicit or explicit industry preference – for some industries stronger than for others. If Donald Trump puts pressure on the SEC by influencing their financial supervision decisions, an industry preference could also become visible in its financial supervision actions.

H2: SEC supervision prefers American firms belonging to specific industries over American firms belonging to other industries in Donald Trump's presidency.

4 Research Design, Sample, and Descriptive Statistics

4.1 Research Design

In case the SEC prefers American firms over foreign firms in Donald Trump's presidency, I expect American firms to have a lower comment letter receipt likelihood after Trump's inauguration. On the other hand, I expect foreign firms to have a constant or increasing likelihood of a comment letter receipt after Trump's inauguration. To examine the relation between US firms and the incidence of receiving a comment letter before and in Trump's presidency, I run the following regression model:

$$PR(COMMENT\_LETTER_{i,t}) = \beta_0 + \beta_1 US_i + \beta_2 TRUMP + \beta_3 INTERACT + \beta_n Controls_{i,t-1} + e_{i,t} \tag{1}$$

The dependent variable $COMMENT\_LETTER$ is an indicator equal to one if a firm i received a comment letter that is related to its 10-K respectively 20-F filing for year t. $INTERACT$ is the product of US_i and $TRUMP$ to estimate the interaction of US_i and $TRUMP$ in a Difference-in-Differences (DID) design. I include a set of control variables to the regression model. The choice of control variables follows Heese et al. (2017) and Cassell et al. (2013), who refer to the various factors used by the SEC under SOX Section 408 (b), to identify companies for filing reviews, and Correia (2014) for supplementary control variables. I use the total-asset-related measure $SIZE$ and the market-based measure $LMVE$ to control for the firm size, which is also a review criterion under SOX Section 408 (b). To control for emerging companies with high growth expectations, I use MTB which reports a firm's market-to-book ratio. In line with Heese et al. (2017), I control for financial reporting quality using $LOSS$. As additional control variables, I use LEV for complexity and risk, and ROA respectively, which may attract the SEC's attention. I winsorize all continuous variables at the 1st and 99th percentile.

A summary of all variables can be obtained from Appendix D.A. The model is estimated by a logistic regression excluding (Model 1) and including (Model 2) the interaction term.

A further indication for preference for American firms could be fewer rounds of each comment letter case. This would result in less complexity and less costs for affected firms. It would also be an indication for easier satisfaction of the SEC with American firms' responses or less different topics in every comment letter case. If the SEC prefers American firms over foreign firms in Donald Trump's presidency, I expect American firms to face fewer comment letter rounds after Trump's inauguration. On the other hand, in case of implicit or explicit discrimination against foreign firms, I would expect these firms to face at minimum the same number of rounds per case in Trump's presidency. To examine whether the complexity of a comment letter case changed for US firms compared to foreign firms in Trump's presidency, I run the following regression model:

$$ROUNDS_{i,t} = \beta_0 + \beta_1 US_i + \beta_2 TRUMP + \beta_3 INTERACT + \beta_n Controls_{i,t-1} + e_{i,t} \qquad (2)$$

The dependent variable $ROUNDS$ is a measure that counts the number of UPLOAD and CORRESP letters in each comment letter case. The model is estimated by a linear regression excluding (Model 1) and including (Model 2) the interaction term.

In case the SEC prefers American firms belonging to specific industries over others in Donald Trump's presidency, I would expect these firms to have a lower comment letter receipt likelihood after Trump's inauguration in relation to firms not belonging to those industries. If specific industries were preferred by receiving fewer comment letters, this would mean all other industries' firms would have at least the same likelihood of a comment letter receipt as before. Similar to H1, another indication for preference could be the number of rounds a comment letter process takes. As firms get benefits from fewer rounds, the SEC could weaken requirements for preferred firms which could result in fewer rounds in every comment letter case. To investigate

whether industries I assume to be preferred in Trump's presidency are less likely to receive a comment letter and face fewer comment letter rounds, I exclude all foreign firms for these models. I run the regressions (3) and (4) for the DID with the independent variables $PREF_i$ and $TRUMP$:

$$PR(COMMENT\_LETTER_{i,t}) = \beta_0 + \beta_1 PREF_i + \beta_2 TRUMP + \beta_3 INTERACT + \beta_n Controls_{i,t-1} + e_{i,t} \tag{3}$$

$$ROUNDS_{i,t} = \beta_0 + \beta_1 PREF_i + \beta_2 TRUMP + \beta_3 INTERACT + \beta_n Controls_{i,t-1} + e_{i,t} \tag{4}$$

A main issue on DID estimations is the assumption of parallel trends. To control for this issue, I plot the means of $COMMENT\_LETTER$ per year partitioned on the treatment (US) for the pre-event window. As observable in Figure D.1, the trends of comment letter receipt likelihood for US as well as non-US firms are almost parallel. For that, no doubt about a limited appropriateness of a DID estimation arises.

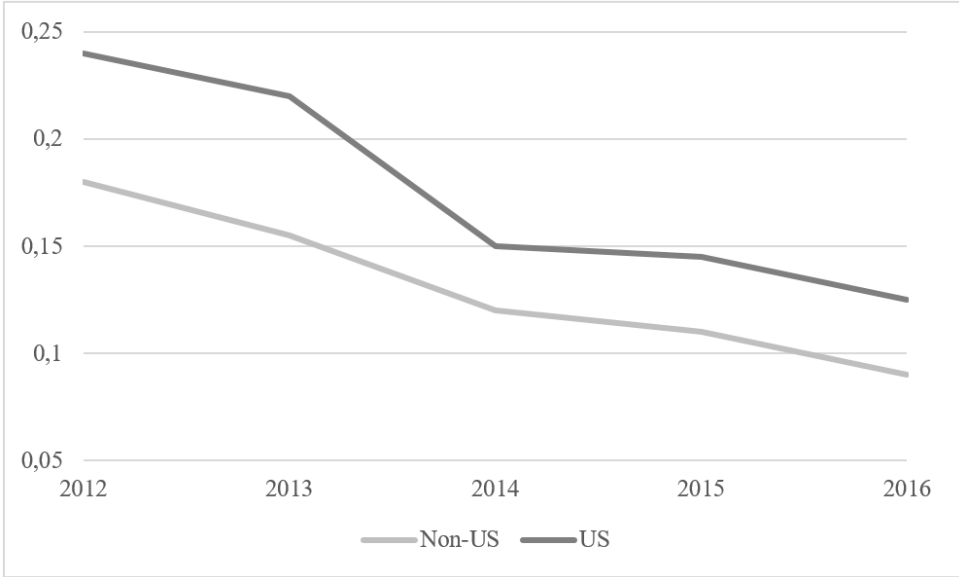**Figure D.1:**

Parallel Trends Assumption

Figure D.1 plots the means of COMMENT_LETTER per year partitioned on Non-US and US for the pre-event window.

4.2 Sample

I obtain data on SEC comment letters from the SEC database EDGAR. This database contains information on all public firms registered at the SEC including all required firm filings like 10-Ks, 20-Fs or 8-Ks, voluntary filings as well as comment letters released by the SEC and the corresponding firm response letters. While prior research usually uses commercial database' comment letter data, I systematically construct each comment letter case from UPLOAD and CORRESP files under the following conditions: First, a case must start with an initial UPLOAD letter sent by the SEC. Second, a case must end with a "no further comment" letter sent by the SEC (UPLOAD). Third, each case must consist of an odd number of letters. Fourth, the filing types "UPLOAD" and "CORRESP" must appear in turn. Last, the time span between two following letters must not exceed 40 days to avoid overlapping events.[55] To control for regularly and recurring effects, I set the time frame from 2012 to 2020. I identify 13,048 distinct comment letter cases, from which I can uniquely assign 10,026 to Datastream firms. In contrast to Heese et al. (2017), I explicitly do not exclude foreign firms. They contend – without providing evidence – that foreign firms are less likely to receive comment letters. Prior studies (e.g., Naughton et al. (2018)) concluded that the SEC allocates its oversight duties with foreign regulators which could lead to a less number of comment letters for foreign firms. These circumstances have no influence on my investigation for the following reasons: first, my investigation of H2 only targets US firms. Foreign firms are not affected by the hypothesis. Second – and more important – I primarily do not compare US firms to foreign firms, but the development of each group before

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[55]There is a small number of cases where this method leads to erroneous results, especially for conversations taking a lot of rounds. To illustrate this issue, Appendix D.D shows the case of the "New Oriental Education & Technology Group Inc.". The initial comment letter regarding the 2011's 20-F was issued by April 2, 2012 followed by 14 further CORRESP and UPLOAD letters. Three of the CORRESP letters only ask for an extension of the deadline to respond. These letters do not count in the ROUNDS measure as they are followed by a further CORRESP (the firm's actual answer). The SEC's UPLOAD, dated November 20, 2012, opens another case regarding 2012's 20-F. Both cases are closed by a consolidated "no further comment" letter by March 8, 2013. Instead of a 13 rounds tanking case for 2011's 20-F and a 7 rounds taking case for 2012's 20-F, my measure creates a 19 rounds taking case for 2011's 20-F. As stated before, this error only occurs in a few cases with a high number of rounds.

and after Trump's inauguration to investigate H1. Thus I retain all comment letters relating to 10-K and 20-F filings. I further obtain data on the whole US sample from Thomson Reuters EIKON. I pick static and time series data for 2012-2020 and delete all observations having their last available data before 2012. I further drop all observations with missing values for firm's home country, industry classification, and controls. I retain 71,619 firm-year observations.

For the reasons presented above, I allocate firms belonging to the following Thomson Reuters Business Classification Industry Group industries to be preferred by Donald Trump's policy: Coal, Oil & Gas, Oil & Gas Related Equipment and Services, Renewable Energy, Metals & Mining, Construction Materials, Banking Services, Investment Banking & Investment Services, and Real Estate Operations.

Table D.1:

Sample Selection

	Firm-years	Firms
Complete EIKON sample	209,961	23,637
less: last available financials before 2012	(107,590)	(12,304)
less: missing values for industry classification	(3,364)	(360)
less: missing values for country classification	(1,576)	(1,108)
less: missing values for controls	(33,291)	(1,256)
Final sample for H1 investigation	64,140	8,609
less: Non-US firms	(10,971)	(1,494)
Final sample for H2 investigation	53,169	7,115

Table D.1 describes the sample selection process.

4.3 Descriptive Statistics

Table D.2 reports the frequency of comment letter cases. One can observe a decreasing number of comment letter cases per year while the number of firms increases.[56] Two main reasons are imaginable for this first indication: either firms enhanced disclosure quality which means fewer comments are necessary on their filings or SEC's financial supervision became weaker. This observation is in line with Johnston (2023) who interprets the strong decline with an SEC's acknowledgment of limited comment letter value and consequently adjusted supervisory activity. Figure D.2 also plots the decreasing number of comment letters issued by the SEC on each day.

Table D.2:
Frequency of Comment Letter cases by year

Comment Letter case issue year	Number of Firm Observations	Number of Comment Letter cases	Percentage
2012	5,861	1,422	24.26
2013	6,184	1,387	22.43
2014	6,573	1,000	15.21
2015	7,023	1,039	14.79
2016	7,378	948	12.85
2017	7,624	878	11.52
2018	7,874	565	7.18
2019	7,995	398	4.98
2020	7,628	404	5.30

Table D.2 reports about the frequency of initiated comment letter cases per year.

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[56]Compared to prior research (e.g., Heese et al. (2017)), my sample consists of a larger number of firms with complete data per year, mainly because I do not exclude foreign or cross-listed firms as well as database-related differences. Further, my number of comment letter cases per year seems to be somewhat smaller compared to prior research. Heese et al. (2017) report a number of 1,335 comment letter cases for 2012 only for US firms, whereas I identify 1,264. This difference is mainly due to the fact that prior research uses databases like AuditAnalytics for comment letter data.

Figure D.2:
Number of total Comment Letter uploads per day
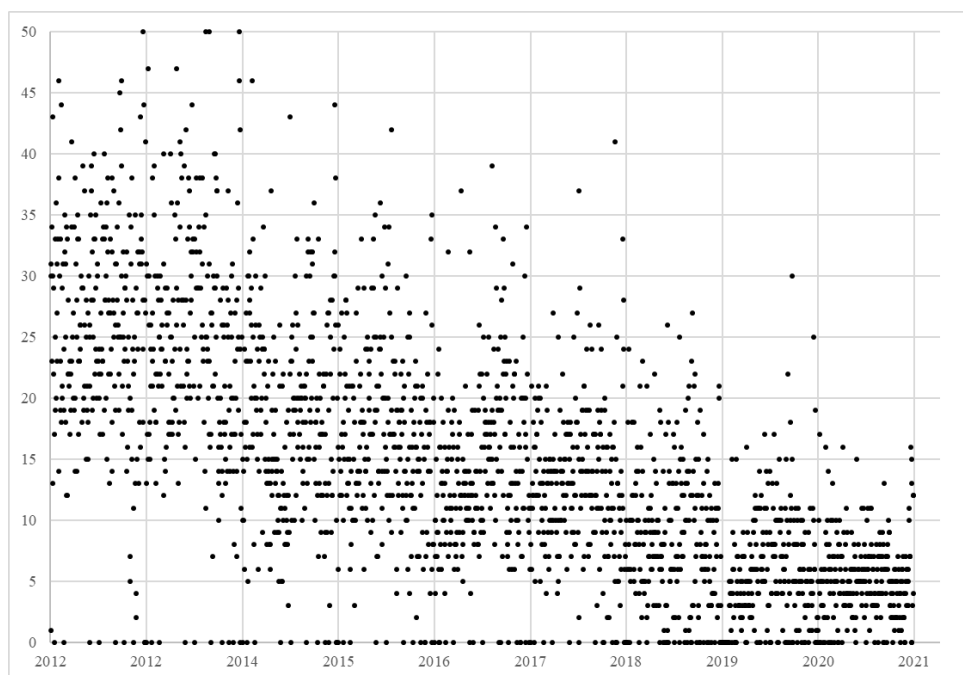
Figure D.2 plots the number of total comment letter uploads made by the SEC per day for the years 2012–2020.

Table D.3 reports the percentages of comment letter firms by year and industry group. One can either compare the development among the years or the average percentage of comment letters by industry with the percentage of the Datastream population. In most cases there are no conspicuous differences or industries only slightly under- or overrepresented. Stronger aberrations can be observed for the following industries: Banking Services' firms are strongly overrepresented in the average population, whereas their proportion in the comment letter population is considerably lower. Collective Investments' and Holding Companies' firms seem to be underrepresented in the comment letter population, whereas Residential & Commercial REIT's seem to be strongly overrepresented.

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Table D.3:

Percentage of Comment Letter firms and Datastream firms by Industry

	2012	2013	2014	2015	2016	2017	2018	2019	2020	Total	Population
Aerospace & Defense	1.62	1.59	1.50	1.73	1.05	1.25	2.48	1.26	1.49	1.54	1.22
Automobiles & Auto Parts	1.41	1.30	1.10	1.64	1.27	2.28	1.95	3.02	1.24	1.57	1.18
Banking Services	7.59	8.00	6.70	5.58	5.59	6.04	4.42	6.03	2.48	6.33	11.56
Beverages	0.84	0.50	0.80	0.96	0.84	0.91	1.59	0.75	0.74	0.85	0.95
Biotechnology & Medical Research	2.53	2.31	2.10	1.92	3.16	3.64	3.89	5.78	5.45	2.96	4.44
Chemicals	2.25	1.87	2.40	2.50	3.06	1.94	3.36	2.26	2.72	2.40	1.68
Coal	0.49	0.65	0.70	0.77	0.42	0.46	0.71	1.76	0.25	0.63	0.43
Collective Investments	0.14	0.22	0.40	0.10	0.11	0.11	0.00	0.25	0.00	0.16	1.95
Communications & Networking	1.83	1.44	2.00	1.73	0.95	1.71	1.95	0.75	1.73	1.60	1.53
Computers, Phones & Household Electro..	1.20	1.08	1.20	0.96	1.16	1.25	0.88	0.25	0.99	1.07	1.38
Construction & Engineering	1.05	0.87	1.00	0.96	0.74	1.48	0.71	0.75	0.74	0.96	0.66
Construction Materials	0.56	0.50	0.40	0.48	0.32	0.46	0.35	1.26	0.50	0.50	0.43
Consumer Goods Conglomerates	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.25	0.01	0.03
Containers & Packaging	0.70	0.65	0.60	0.77	0.84	0.68	0.53	0.50	0.99	0.70	0.45
Diversified Industrial Goods Wholesal..	0.00	0.07	0.10	0.10	0.11	0.23	0.18	0.25	0.25	0.11	0.11
Diversified Retail	0.84	1.01	0.90	0.58	1.27	0.68	1.24	1.51	0.74	0.93	0.59
Electrical Utilities & IPPs	1.97	1.80	2.50	2.02	1.48	2.16	2.65	0.75	1.24	1.93	1.61
Electronic Equipment & Parts	0.77	0.65	1.10	0.96	0.53	1.14	0.00	0.75	0.50	0.76	0.64
Financial Technology (Fintech) & Infr..	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.25	0.01	0.03
Food & Drug Retailing	1.20	1.37	1.30	1.25	0.63	1.37	1.77	1.26	0.74	1.22	0.94
Food & Tobacco	1.41	1.95	1.90	2.02	1.69	1.25	2.30	1.26	2.72	1.78	2.56
Freight & Logistics Services	1.41	1.44	0.90	0.77	1.16	1.14	1.77	3.02	2.72	1.38	1.08
Healthcare Equipment & Supplies	3.45	3.46	2.90	3.37	4.54	3.30	3.54	2.76	3.96	3.48	4.01
Healthcare Providers & Services	2.11	1.87	2.00	1.44	1.48	2.51	1.77	2.51	1.73	1.92	1.83
Holding Companies	0.14	0.14	0.30	0.19	0.00	0.11	0.00	0.25	0.00	0.14	0.39
Homebuilding & Construction Supplies	1.05	1.23	0.80	1.25	1.37	1.14	1.06	2.01	1.49	1.19	0.95
Hotels & Entertainment Services	2.53	3.60	3.50	3.56	3.27	4.21	3.72	5.03	4.21	3.53	2.69
Household Goods	0.63	0.79	0.40	0.77	0.53	0.46	1.24	0.00	0.74	0.63	0.49
Industrial Conglomerates	0.56	0.29	0.30	0.48	0.32	0.68	0.71	0.50	0.00	0.44	0.24
Insurance	3.38	3.68	1.70	2.12	1.69	3.42	2.48	2.51	2.97	2.74	2.07

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	2012	2013	2014	2015	2016	2017	2018	2019	2020	Total	Population
Investment Banking & Investment Servi..	2.81	2.45	1.60	2.31	1.58	1.37	0.71	1.26	1.24	1.93	2.06
Leisure Products	0.42	0.58	0.50	0.29	0.74	0.91	0.88	1.26	1.49	0.66	0.64
Machinery, Equipment & Components	5.06	4.90	5.20	4.14	5.38	4.78	4.60	2.76	5.20	4.80	4.61
Media & Publishing	2.32	1.66	2.20	2.79	3.48	2.73	3.36	2.51	3.71	2.59	2.61
Metals & Mining	3.02	3.39	4.10	2.89	2.32	2.62	3.01	2.51	2.72	3.03	2.46
Miscellaneous Educational Service Pro..	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1.24	0.06	0.04
Multiline Utilities	0.35	0.22	0.30	0.38	0.63	0.34	0.53	0.00	0.50	0.36	0.27
Natural Gas Utilities	0.49	0.50	0.50	0.48	0.84	0.46	1.06	0.25	0.50	0.56	0.32
Office Equipment	0.21	0.22	0.00	0.19	0.11	0.00	0.18	0.25	0.00	0.14	0.17
Oil & Gas	3.94	4.33	5.70	4.43	3.90	2.62	3.54	3.27	4.95	4.13	4.43
Oil & Gas Related Equipment and Servi..	2.39	2.67	3.90	2.41	4.54	3.64	1.95	2.51	1.98	2.97	2.40
Paper & Forest Products	0.21	0.43	0.20	0.38	0.42	0.46	0.18	0.00	0.25	0.31	0.41
Passenger Transportation Services	1.05	0.58	0.40	0.58	0.53	1.37	1.42	1.01	1.24	0.83	0.65
Personal &Household Products & Services	1.41	1.08	1.60	1.73	1.48	1.48	1.06	1.26	1.73	1.42	1.26
Pharmaceuticals	2.53	2.09	2.30	1.92	2.95	1.71	1.95	1.76	2.48	2.23	2.65
Professional & Commercial Services	4.22	4.25	3.50	4.91	5.17	4.78	3.54	3.02	5.94	4.38	4.44
Real Estate Operations	0.84	1.08	0.80	1.83	1.05	1.03	0.71	0.75	0.74	1.03	1.53
Renewable Energy	0.77	0.94	1.70	1.25	1.37	0.68	0.71	0.25	0.50	0.99	1.07
Residential & Commercial REIT	7.74	7.07	7.30	10.01	7.49	7.18	8.50	6.78	0.00	7.39	2.96
Residential & Commercial REITs	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	2.23	0.11	0.44
Semiconductors & Semiconductor Equipm..	3.02	2.67	2.30	2.60	3.16	3.53	1.95	4.52	3.47	2.91	2.24
Software & IT Services	6.68	6.85	7.20	6.93	6.96	6.61	6.37	10.80	8.17	7.09	8.28
Specialty Retailers	3.38	3.82	3.50	3.66	3.27	2.85	2.83	2.76	3.22	3.36	2.32
Telecommunications Services	2.18	2.16	1.90	1.83	2.11	1.59	2.48	0.75	1.24	1.93	2.08
Textiles & Apparel	0.91	1.23	1.70	0.77	0.63	1.03	1.24	0.75	0.99	1.04	1.01
Transport Infrastructure	0.00	0.22	0.00	0.00	0.21	0.11	0.00	0.00	0.00	0.07	0.21
Uranium	0.00	0.00	0.00	0.10	0.00	0.00	0.00	0.00	0.00	0.01	0.03
Water & Related Utilities	0.35	0.29	0.10	0.19	0.11	0.11	0.00	0.00	0.50	0.20	0.28

Table D.3 shows the percentage of firms that received a comment letter per year distributed by Thomson Reuters Business Classification Industry Groups. The last column shows the entire Datastream population by Thomson Reuters Business Classification Industry Groups.

Descriptive statistics on the dataset can be obtained from Table D.4.

The probability of a comment letter receipt over the entire period is around 12 %. This number seems to be reasonable as the SEC states a company's regular financial filings are reviewed every three years and not every review leads to a comment letter. On average, a comment letter case takes around 3.8 rounds. 83 % of the entire firm-years were observed for companies from the United States, whereas 26 % of the firm-year observations belong to companies I assign to industries favored by Trump. Panel B reports descriptive statistics for the entire sample partitioned on US. One can observe a high significance in mean differences for $COMMENT\_LETTER$. Around 12 % of all US-firm-year observations are linked with a 10-K comment letter, whereas only 9 % of the Non-US firms received a comment letter on their yearly filing. If a firm received a comment letter, the case took slightly more rounds for Non-US firms. Panel E reports descriptive statistics for the entire sample partitioned on $TRUMP$. One can observe a strongly significant lower probability of a comment letter receipt for Trump's presidency in general. A slightly, but strongly significant decrease in the number of rounds is also observable.

Table 5 reports the correlation for the most important variables excluding controls. In line with prior descriptive statistics, one can observe a slightly positive correlation between US and $COMMENT\_LETTER$ indicating that US firms could be more likely to receive a comment letter over the entire period. The slightly negative correlation between $COMMENT\_LETTER$ and $PREF$ could also indicate that firms I expect to be preferred seem to be less likely to receive a comment letter over the entire period. On the other hand, US firms seem to face fewer comment letter rounds per case as the negative correlation indicates, whereby firms I expect to be preferred seem to face more comment letter rounds over the entire period. One can further observe the correlation between these variables and the $TRUMP$ variable. The negative correlation be-

Table D.4:
Summary Statistics

Panel A: Pooled Sample

	n	mean	p50	sd sd	min	max
COMMENT_LETTER	64,140	0.125	0.000	0.331	0.000	1.000
ROUNDS	8,041	3.744	3.000	1.362	3.000	19.000
US	64,140	0.829	1.000	0.377	0.000	1.000
PREF	53,169	0.263	0.000	0.440	0.000	1.000
ANTI	53,169	0.090	0.000	0.286	0.000	1.000
LEV	64,140	2.105	0.967	5.623	–20.580	29.980
MTB	64,140	1.332	1.401	24.742	–275.986	131.165
LOW_MTB	64,140	0.369	0.000	0.483	0.000	1.000
LMVE	64,140	12.426	12.729	3.015	4.127	18.224
LOSS	64,140	0.401	0.000	0.490	0.000	1.000
ROA	64,140	–1.139	0.010	8.026	–106.447	0.698
CHANGE_SALES	64,140	0.174	0.000	0.970	-1.000	8.029

Panel B: Sample partitioned on US

	US-firms		Non-US firms		Difference
	n	mean (1)	n	mean (2)	(1) – (2)
COMMENT_LETTER	53,169	0.131	10,971	0.097	0.035***
ROUNDS	6,979	3.712	1,062	3.953	−0.241***
CHANGE_SALES	53,169	0.181	10,971	0.144	0.037***
LEV	53,169	2.062	10,971	2.313	−0.251***
MTB	53,169	1.347	10,971	1.256	0.092
LOW_MTB	53,169	0.360	10,971	0.414	−0.054***
LMVE	53,169	12.149	10,971	13.769	−1.620***
LOSS	53,169	0.418	10,971	0.316	0.102***
ROA	53,169	–1.263	10,971	–0.534	0.730***

Panel C: Sample partitioned on PREF

	PREF-firms		Non-PREF-firms		Difference
	n	mean (1)	n	mean (2)	(1) – (2)
COMMENT_LETTER	13,970	0.101	39,199	0.142	−0.041***
ROUNDS	1,411	3.787	5,568	3.694	0.093**
CHANGE_SALES	13,970	0.148	39,199	0.192	−0.044***
LEV	13,970	4.684	39,199	1.128	3.556***
MTB	13,970	1.248	39,199	0.383	−0.134
LOW_MTB	13,970	0.439	39,199	0.332	0.108***
LMVE	13,970	11.922	39,199	12.230	−0.308***
LOSS	13,970	0.323	39,199	0.452	−0.129***
ROA	13,970	–0.641	39,199	–1.485	0.845***

Panel D: Sample partitioned on COMMENT_LETTER

	CL-firms		Non-CL-firms		Difference
	n	mean (1)	n	mean (2)	(1) − (2)
US	8,041	0.868	56,099	0.823	0.045***
PREF	6,979	0.202	46,190	0.272	−0.070***
ANTI	6,979	0.113	46,190	0.086	0.027***
CHANGE_SALES	8,041	0.183	56,099	0.173	0.010
LEV	8,041	2.247	56,099	2.085	−0.367***
MTB	8,041	2.332	56,099	1.188	1.143***
LOW_MTB	8,041	0.221	56,099	0.391	−0.170***
LMVE	8,041	14.198	56,099	12.172	2.025***
LOSS	8,041	0.266	56,099	0.420	−0.155***
ROA	8,041	−0.150	56,099	−1.280	1.131***

Panel E: Sample partitioned on TRUMP

	Pre-TRUMP		Post-TRUMP		Difference
	n	mean (1)	n	mean (2)	(1) − (2)
COMMENT_LETTER	33,019	0.176	31,121	0.072	0.103***
ROUNDS	5,976	3.836	2,245	3.507	0.329***
US	33,019	0.831	31,121	0.827	0.004
PREF	27,439	0.269	25,730	0.257	0.012***
ANTI	27,439	0.091	25,730	0.089	0.002
CHANGE_SALES	33,019	0.215	31,121	0.131	0.083***
LEV	33,019	2.213	31,121	1.991	0.223***
MTB	33,019	1.362	31,121	1.300	0.062
LOW_MTB	33,019	0.368	31,121	0.370	−0.002
LMVE	33,019	12.409	31,121	12.444	−0.004
LOSS	33,019	0.382	31,121	0.420	−0.038***
ROA	33,019	−0.921	31,121	−1.369	0.449***

Table D.4 shows descriptive statistics for the pooled sample (Panel A) and partitioned on specific variables. In panel B, the entire sample is partitioned on US which means US firms and foreign firms. Panel C reports about all US firms that are partitioned on $PREF$ depending on their industry classification. Pref-firms are those belonging to industries I assume to be preferred. Panel D partitions the entire sample on $COMMENT\_LETTER$ which means a firm-year observation is linked with a comment letter receipt. Panel E partitions the entire sample on time by the variable $TRUMP$ becoming 1 for 2017 to 2020. The differences are tested by a t-test. See Appendix D.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

tween $TRUMP$ and $COMMENT\_LETTER$ respectively $TRUMP$ and $ROUNDS$ could indicate that firms in general are less likely to receive a comment letter and face fewer comment letter rounds in Trump's presidency. The following section will test for these circumstances.

Table D.5:
Correlation Table – H1

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
(1) CL	1										
(2) ROUNDS	-0.156***	1									
(3) TRUMP	0.039***	-0.108***	1								
(4) US	0.003	-0.060***	-0.006	1							
(5) CHN_S	0.010**	0.039***	-0.043***	0.014***	1						
(6) LEV	0.015***	-0.012	-0.020***	-0.017***	-0.035***	1					
(7) MTB	-0.117***	-0.008	-0.001	0.001	0.006	0.337***	1				
(8) LOW_MTB	0.222***	0.036***	0.002	-0.042***	-0.011***	-0.216***	-0.253***	1			
(9) LMVE	-0.104***	-0.021**	0.006	-0.202***	-0.033***	0.128***	0.069***	-0.475***	1		
(10) LOSS	0.047***	0.037***	0.038***	0.078***	0.063***	-0.165***	-0.062***	0.275***	-0.488***	1	
(11) ROA		-0.029***	-0.028***	-0.034***	-0.010**	0.077***	0.082***	-0.170***	0.234***	-0.185***	1

Table D.5 displays the correlation analysis on the most important variables for H1 (entire dataset). See Appendix D.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

Table D.6:
Correlation Table – H2

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
(1) CL	1										
(2) ROUNDS		1									
(3) TRUMP	-0.160***	-0.109***	1								
(4) PREF	-0.053***	0.029**	-0.013***	1							
(5) CHN_S	0.003	0.032***	-0.047***	-0.020***	1						
(6) LEV	0.008*	-0.014	-0.018***	0.273***	-0.035***	1					
(7) MTB	0.017***	-0.017	-0.001	-0.002	0.006	0.361***	1				
(8) LOW_MTB	-0.131***	0.022*	0.002	0.099***	-0.003	-0.236***	-0.260***	1			
(9) LMVE	0.257***	-0.009	0.016***	-0.046***	-0.026***	0.109***	0.075***	-0.519***	1		
(10) LOSS	-0.119***	0.040***	0.033***	-0.115***	0.063***	-0.172***	-0.064***	0.298***	-0.478***	1	
(11) ROA	0.051***	-0.031***	-0.030***	0.044***	-0.010**	0.080***	0.083***	-0.184***	0.240***	-0.187***	1

Table D.6 displays the correlation analysis on the most important variables for H2 (only US firms). See Appendix D.A for variable definitions.
* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

5 Independence of SEC Financial Supervision

5.1 Main Findings

To visualize the underlying idea of the DID investigation and report directly interpretable likelihoods, table D.7 shows DID results based on mean comparison.[57] Both US and non-US firms have a significantly lower likelihood of a comment letter receipt in Trump's presidency (C resp. D). Non-US firms have a lower likelihood of a comment letter receipt over the entire period than US firms (A resp. B). This finding is in line with the idea of a SEC's share of oversight authority with foreign agencies (Duro et al., 2019; Chantziaras et al., 2021; Naughton et al., 2018; Giamouridis et al., 2018). The difference in differences is significantly negative (E). This indicates that – although US firms are still more likely to receive a comment letter in Trump's presidency –, the gap in comment letter receipt likelihood became significantly smaller.

Table D.7:

Difference-in-Differences Analysis Results for H1

	TRUMP = 0 (Pre)	TRUMP = 1 (Post)	Difference
US (Treatment)	0.183 n = 27,439	0.076 n = 25,730	-0.108*** (C)
Non-US (Control)	0.137 n = 5,580	0.056 n = 5,391	-0.081*** (D)
Difference	-0.047*** (A)	-0.020*** (B)	-0.027*** (E)
$R^2 = 0.030$			

Table D.7 shows univariate DID results for $COMMENT\_LETTER$. $COMMENT\_LETTER$ is equal to 1 if a firm received a 10-K or 20-F related comment letter in year t. The table displays the interaction of US and $TRUMP$. See Appendix D.A for variable definitions.
* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

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[57]Please note that these results are only for a first visualization to better understand the underlying DID design. To display directly interpretable likelihoods, some simplifications had to be carried out: Instead of a logistic regressions, the DID design is based on mean comparison and t-tests. For that, any control variables as well as fixed effects had been omitted.

Multivariate regression results for H1 can be obtained from table D.8. The interaction coefficient which can be interpreted as the difference in differences is negative at a 5 % level. The control variables' coefficients are mainly consistent with prior literature (e.g., Cassell et al., 2013; Heese et al., 2017).

Referring to the number of rounds a comment letter case takes, one can observe a general decrease over time. Both US and non-US firms have less complex comment letter cases in Trump's presidency. The coefficient for the interaction term is slightly positive, but not significant. Thus, I get no clear indication of whether the shortening of the comment letter cases is more distinct for foreign firms than for US firms.

Interpreting comment letter receipts likelihood and comment letter case rounds as indicators for SEC's financial supervision behavior, I get some indications of the SEC acting in line with Trump's policy. The significantly greater negative difference of comment letter receipt likelihood for US firms before (table D.7, A resp. E) and in Trump's presidency (B resp. E) compared to foreign firms indicates a weaker general supervision, especially for US firms and thus a kind of privilege. The complexity of the entire process – indicated by comment letter rounds – is not affected.

Table D.9 shows multivariate regression results for H2.

Firms that belong to industries I expect to be preferred in Trump's presidency are less likely to receive a comment letter over the entire period. The interaction coefficient which can be interpreted as the difference in differences is negative with a significance at a 1 % level. This indicates that – although the likelihood of a comment letter receipt is lower for all firms in Trump's presidency –, the gap in comment letter receipt likelihood became greater for firms I expect to be preferred. These firms face significantly more rounds in a comment letter case before and in Trump's presidency. The difference to the other firms' likelihood becomes smaller

Table D.8:
Multivariate Regression Results for H1

	COMMENT_LETTER		ROUNDS	
	Model 1	Model 2	Model 3	Model 4
US	0.927***	0.978***	-0.220***	-0.249***
	(15.79)	(15.13)	(-3.72)	(-3.37)
TRUMP	-1.097***	-0.954***	-0.327***	-0.415***
	(-41.03)	(-13.99)	(-10.92)	(-4.21)
INTERACT		-0.167**		0.101
		(-2.25)		(0.98)
LEV	-0.005	-0.005	-0.002	-0.002
	(-1.48)	(-1.47)	(-0.47)	(-0.48)
MTB	-0.000	-0.000	0.000	0.000
	(-0.49)	(-0.49)	(0.48)	(0.47)
LOW_MTB	-0.014	-0.013	0.063	0.061
	(-0.35)	(-0.33)	(1.45)	(1.41)
LMVE	0.322***	0.323***	0.002	0.001
	(43.62)	(43.64)	(0.18)	(0.14)
LOSS	0.128***	0.128***	0.086**	0.085**
	(3.42)	(3.44)	(2.05)	(2.04)
ROA	0.015**	0.015**	-0.013	-0.013
	(2.16)	(2.16)	(-1.42)	(-1.41)
CHANGE_SALES	0.039***	0.039***	0.060***	0.060***
	(3.01)	(2.98)	(2.87)	(2.88)
Constant	-6.548***	-6.599***	4.021***	4.052***
	(-45.48)	(-45.03)	(25.14)	(24.46)
Industry FE	Yes	Yes	Yes	Yes
Observations	64,140	64,140	8,041	8,041
R^2			0.021	0.021
Adjusted R^2			0.019	0.019
Pseudo R^2	0.128	0.128		

t statistics in parentheses

Table D.8 shows multivariate regression results for H1. Models 1 and 2 are estimated by a logit regression. Models 3 and 4 are estimated by an OLS regression. The dependent variables are $COMMENT\_LETTER$ for Models 1 and 2 and $ROUNDS$ for Models 3 and 4. $COMMENT\_LETTER$ is equal to 1 if a firm received a 10-K or 20-F related comment letter in year t. $ROUNDS$ is the number of rounds a comment letter case takes. The variables of interest for Model 2 and Model 4 are $INTERACT$ as the product of US and $TRUMP$. All specifications include firm fixed effects, as well as control variables. See Appendix D.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

Table D.9:

Multivariate Regression Results for H2

	COMMENT_LETTER		ROUNDS	
	Model 1	Model 2	Model 3	Model 4
PREF	-0.255***	-0.162***	0.075*	0.107**
	(-6.09)	(-3.57)	(1.89)	(2.38)
TRUMP	-1.148***	-1.084***	-0.321***	-0.297***
	(-39.16)	(-33.25)	(-9.22)	(-7.77)
INTERACT		-0.325***		-0.138
		(-4.33)		(-1.51)
LEV	-0.005	-0.005	-0.003	-0.003
	(-1.39)	(-1.43)	(-0.85)	(-0.86)
MTB	-0.000	-0.000	-0.000	-0.000
	(-0.64)	(-0.68)	(-0.27)	(-0.28)
LOW_MTB	-0.033	-0.040	0.041	0.039
	(-0.79)	(-0.94)	(0.93)	(0.90)
LMVE	0.337***	0.336***	0.020**	0.021**
	(43.35)	(43.19)	(2.43)	(2.47)
LOSS	0.077**	0.077**	0.131***	0.132***
	(2.04)	(2.03)	(3.38)	(3.40)
ROA	0.014*	0.014*	-0.013**	-0.013**
	(1.90)	(1.89)	(-2.33)	(-2.34)
CHANGE_SALES	0.027*	0.027*	0.041**	0.042**
	(1.87)	(1.90)	(2.17)	(2.21)
Constant	-5.782***	-5.795***	3.454***	3.443***
	(-50.77)	(-50.80)	(27.53)	(27.39)
Observations	53,169	53,169	6,979	6,979
R^2			0.016	0.017
Adjusted R^2			0.015	0.015
Pseudo R^2	0.138	0.138		

t statistics in parentheses

Table D.9 shows multivariate regression results for H2. Models 1 and 2 are estimated by a logit regression. Models 3 and 4 are estimated by an OLS regression. The dependent variables are $COMMENT\_LETTER$ for Models 1 and 2 and $ROUNDS$ for Models 3 and 4. $COMMENT\_LETTER$ is equal to 1 if a firm received a 10-K or 20-F related comment letter in year t. $ROUNDS$ is the number of rounds a comment letter case takes. The variables of interest for Model 2 and Model 4 are $INTERACT$ as the product of $PREF$ and $TRUMP$. All specifications include firm fixed effects, as well as control variables. See Appendix D.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

at a 10 % level in Trump's presidency. These results indicate that SEC financial supervision became weaker for firms belonging to industries I expect to be preferred compared to others in Trump's presidency.

5.2 Robustness Checks

To test whether the findings above regarding preferred industries hold for other industry compositions, I introduce a robustness check for industries potentially being in conflict with Trump's political (or at least personal) agenda. While I provide evidence of a weaker supervision against preferred industries firms, the effect of a "trumped" SEC might also result in a stronger supervision against industries which are hereinafter referred to as "Anti industries". To test for this effect, I introduce another binary variable $ANTI$ becoming 1 for firms belonging to industries I assume to be in conflict with Trump's agenda. I link the following industries (derived from Thomson Reuters industry classification) to these Anti industries: Freight & Logistics Services, Passenger Transportation Services, Hotels & Entertainment Services and Media & Publishing.

A result of Donald Trump's "America first" vision with local sourcing and lowered foreign trade as a consequence of imposed tariffs is a smaller demand for freight and logistics services. Although Donald Trump established a $ 1.5 trillion infrastructure plan, the focus is on roads and bridges and thus on individual transportation (Short, 2019), mainly in those states that supported him (Bloom, 2018). Funding for public mass transportation was cut down. The Trump Organization LLC, owned by Donald Trump, operates a small two-digit number of luxury hotels. Due to a personal commercial interest, a stronger supervision against competitors might be helpful for Trump. Characteristic of Donald Trump's communication is the extensive Twitter usage, whereas traditional news and media are often flagged as "fake news" providers. In January 2017, shortly after his inauguration, Trump accused the press of being an "enemy of the American people" (Kalb, 2018).

Table D.10 shows multivariate regression results for this robustness check.

Firms that belong to industries I expect to be explicitly not preferred in Trump's presidency and thus face a stronger SEC supervision are more likely to receive a comment letter over the entire period. The interaction coefficient is positive with a significance at a 1 % level. This indicates that – although the likelihood of a comment letter receipt is lower for all firms in Trump's presidency –, the gap in comment letter receipt likelihood became greater for firms I expect to be explicitly not preferred. While the interaction term regarding $ROUNDS$ for Pref-industry firms is significantly negative, I find no distinct hint that the complexity also became weaker for Anti industry firms. The results of this robustness check indicate that SEC financial supervision did not only became weaker for firms belonging to industries I expect to be preferred compared to others in Trump's presidency, but – contradictory – also became stronger for firms belonging to industries I expect to be explicitly not preferred.

I further run a placebo test with nine randomly selected industries. Table D.11 shows multivariate regression results for this robustness check.

As expected, I find no significant coefficients for $PREF\_RAND$ and $INTERACT$. These findings strengthen my assumption of presidential influence on the SEC.

5.3 Limitations

The results provided above are by dint of various reasons not without limitations. Some result from the mode of data collection, some from statistical issues, some are content-related. I drop all observations not resulting in an odd number of rounds. This procedure might exclude all comment letter cases that are still under investigation meaning all firms that did not receive a "No further comment"-letter until the date of this research. Close to the foregoing issue, cases might also not be closed even if they result in an odd number of rounds. The explanatory power of my models is limited as I had to drop around one third of all comment letter observations

Table D.10:

Robustness Checks for H2

	COMMENT_LETTER		ROUNDS	
	Model 1	Model 2	Model 3	Model 4
ANTI	0.184***	0.004	-0.103**	-0.109*
	(3.62)	(0.07)	(-2.11)	(-1.80)
TRUMP	-1.146***	-1.205***	-0.320***	-0.322***
	(-39.11)	(-38.55)	(-9.20)	(-8.65)
INTERACT		0.515***		0.017
		(6.00)		(0.16)
LEV	-0.010***	-0.010***	-0.002	-0.002
	(-3.19)	(-3.19)	(-0.57)	(-0.57)
MTB	-0.000	-0.000	-0.000	-0.000
	(-0.08)	(-0.11)	(-0.36)	(-0.36)
LOW_MTB	-0.072*	-0.074*	0.054	0.054
	(-1.72)	(-1.77)	(1.25)	(1.24)
LMVE	0.340***	0.340***	0.020**	0.020**
	(43.95)	(43.92)	(2.43)	(2.43)
LOSS	0.104***	0.106***	0.129***	0.129***
	(2.79)	(2.85)	(3.33)	(3.33)
ROA	0.012*	0.012*	-0.013**	-0.013**
	(1.79)	(1.81)	(-2.23)	(-2.23)
CHANGE_SALES	0.028*	0.027*	0.041**	0.041**
	(1.93)	(1.89)	(2.16)	(2.16)
Constant	-5.892***	-5.875***	3.478***	3.478***
	(-52.19)	(-51.98)	(27.77)	(27.76)
Observations	53,169	53,169	6,979	6,979
R^2			0.016	0.016
Adjusted R^2			0.015	0.015
Pseudo R^2	0.137	0.138		

t statistics in parentheses

Table D.10 shows multivariate regression results for the robustness check on H2. Models 1 and 2 are estimated by a logit regression. Models 3 and 4 are estimated by an OLS regression. The dependent variables are $COMMENT\_LETTER$ for Models 1 and 2 and $ROUNDS$ for Models 3 and 4. $COMMENT\_LETTER$ is equal to 1 if a firm received a 10-K or 20-F related comment letter in year t. $ROUNDS$ is the number of rounds a comment letter case takes. The variables of interest for Model 2 and Model 4 are $INTERACT$ as the product of $ANTI$ and $TRUMP$. All specifications include firm fixed effects, as well as control variables. See Appendix D.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

Table D.11:

Robustness Checks for H2 – Placebo Test

	COMMENT_LETTER		ROUNDS	
	Model 1	Model 2	Model 3	Model 4
PREF_RAND	0.070	0.049	0.045	0.071
	(1.48)	(0.92)	(1.02)	(1.38)
TRUMP	-1.145***	-1.155***	-0.324***	-0.310***
	(-39.13)	(-36.58)	(-9.34)	(-8.25)
INTERACT		0.066		-0.096
		(0.79)		(-0.98)
LEV	-0.010***	-0.010***	-0.001	-0.001
	(-3.23)	(-3.23)	(-0.43)	(-0.43)
MTB	-0.000	-0.000	-0.000	-0.000
	(-0.04)	(-0.04)	(-0.41)	(-0.43)
LOW_MTB	-0.071*	-0.071*	0.053	0.053
	(-1.69)	(-1.69)	(1.23)	(1.22)
LMVE	0.340***	0.340***	0.020**	0.020**
	(43.90)	(43.90)	(2.39)	(2.38)
LOSS	0.094**	0.094**	0.127***	0.128***
	(2.51)	(2.50)	(3.26)	(3.28)
ROA	0.012*	0.012*	-0.013**	-0.013**
	(1.78)	(1.78)	(-2.24)	(-2.25)
CHANGE_SALES	0.025*	0.025*	0.041**	0.042**
	(1.77)	(1.77)	(2.18)	(2.20)
Constant	-5.883***	-5.881***	3.465***	3.461***
	(-52.07)	(-52.04)	(27.64)	(27.60)
Observations	53,169	53,169	6,979	6,979
R^2			0.016	0.016
Adjusted R^2			0.015	0.015
Pseudo R^2	0.137	0.137		

t statistics in parentheses

Table D.11 shows multivariate regression results for the placebo robustness check on H2. Models 1 and 2 are estimated by a logit regression. Models 3 and 4 are estimated by an OLS regression. The dependent variables are $COMMENT\_LETTER$ for Models 1 and 2 and $ROUNDS$ for Models 3 and 4. $COMMENT\_LETTER$ is equal to 1 if a firm received a 10-K or 20-F related comment letter in year t. $ROUNDS$ is the number of rounds a comment letter case takes. The variables of interest for Model 2 and Model 4 are $INTERACT$ as the product of $PREF\_RAND$ and $TRUMP$. All specifications include firm fixed effects, as well as control variables. See Appendix D.A for variable definitions.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

which I could not merge with firm data due to database reasons. This issue has no effects on the number of rounds observed, but on the probability of a comment letter receipt which is slightly too low. A further, additional fact could also have influence on the results: since there have been unusually long Government Shutdowns in Donald Trump's presidency, the SEC had many days without usual business. For instance, the shutdown starting on December 22, 2018 ended after 35 days and was the longest in the United States' history. During these shutdowns, the SEC operates in accordance with a special shutdown plan being available, e.g., to respond to emergency situations. Standard work like financial filings review is not done during this time.

Figure D.3 shows the number of comment letter cases initiated on each day. One can observe noticeably many days without any initial comment letter in late 2018 and early 2019. This finding seems to be directly linked to Government Shutdowns and result in a lower number of initial comment letters. As there are no significantly high numbers of comment letter issues after a shutdown, one can assume the SEC's supervision is not caught up afterwards. This might be a further reason for a decrease in comment letter receipts probability.

The last – and likely most important – limitation affects the significance of my results concerning the initial question of whether the SEC is trumped. Although some clear results regarding a significant change in SEC supervision of American vs. foreign firms since 2017 are observable, there is no hint for causality. My investigation cannot give an answer if the change in SEC supervision is a result of a change in economics or politics fundamentally, if it results from Donald Trump's direct order or if there are other reasons like legislative changes or internal changes in selection criteria that modified supervision activity. Additionally, it is worth mentioning that the results are only valid for the DCF's financial supervision and not for the entire SEC, as the different divisions act quasi-autonomous (Katz, 2010) and, thus, findings for one division are not readily transferable to another.[58].

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[58]This issue is discussed in greater detail in Piering (2024c).

Figure D.3:
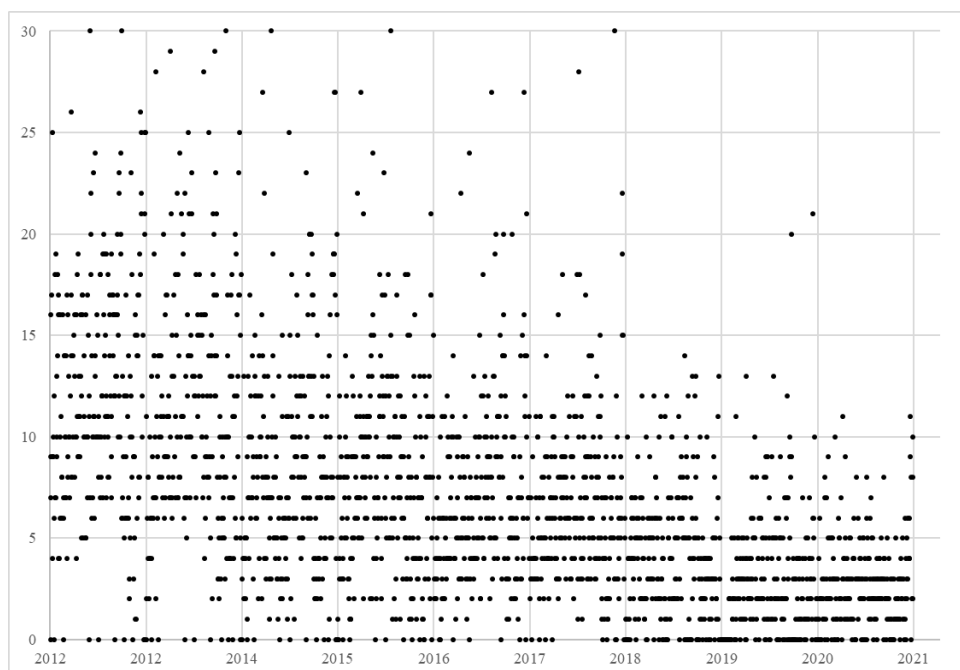*Number of initial Comment Letter uploads per day*

Figure D.3 plots the number of SEC-initiated comment letter cases per day for the years 2012–2020.

6 Conclusion

The extent of presidential influence on independent agencies has been long discussed. As the core characteristic of agencies like the SEC is often be seen in the absence of presidential removal of commissioners by will, Constitution, SEC statutes as well as the Supreme Court are silent on the conditions of a "good cause" for presidential removal. Prior literature focuses on congressional influence on the SEC and finds indistinct results regarding SEC capture by lobbying expenditures or political contributions. I provide first evidence for presidential influence on SEC financial supervision. While a major change in public policy came along with Donald Trump's presidency, a change in financial supervision that is in line with his policy would be expected in case of effective influence. I find a significant change in SEC financial supervision in

Donald Trump's presidency. Compared to foreign firms, US firms have a significantly stronger decrease in comment letter receipts likelihood. Furthermore, special industries have a lower comment letter receipt likelihood and face a less complex supervision process, indicated by the number of rounds a comment letter case takes. These findings are in line with Donald Trump's "America first" vision and preference for specific industries. Future research might address a causality issue on a qualitative level and control for other possible influential factors like changes in law or SEC's statutes.

Variable	Definition
Dependent variables	
COMMENT_LETTER	Binary variable becoming 1 in case a firm received an initial comment letter relating to its 10-K or 20-F filing in the respective year and the comment letter case took an odd number of rounds; obtained from EDGAR.
ROUNDS	Number of rounds a comment letter case took; obtained from EDGAR.
Independent Variables	
TRUMP	Binary variable becoming 1 for a firm-year observation from 2017 – 2020, 0 otherwise
US	Binary variable becoming 1 in case a firm belongs to the United States, dependent on Worldscope Item WC06026; obtained from Datastream.
PREF	Binary variable for all US firms becoming 1 in case a firm refers to the Thomson Reuters Business Classification Industry Group 501010 "Coal", 501020 "Oil & Gas", 501030 "Oil & Gas Related Equipment and Services", 502010 "Renewable Energy", 512010 "Metals & Mining", 512020 "Construction Materials", 551010 "Banking Services", 551020 "Investment Banking & Investment Services" or 554020 "Real Estate Operations", 0 otherwise.
ANTI	Binary variable for all US firms becoming 1 in case a firm refers to the Thomson Reuters Business Classification Industry Group 524050 "Freight & Logistics Services", 524060 "Passenger Transportation Services", 533010 "Hotels & Entertainment Services" or 533020 "Media & Publishing", 0 otherwise.
PREF_RAND	Binary variable for all US firms becoming 1 in case a firm refers to the Thomson Reuters Business Classification Industry Group 512010 "Metals & Mining", 532020 "Textiles & Apparel", 534030 "Speciality Retailers", 542010 "Personal & Household Products & Services", 562020 "Biotechnology & Medical Research", 571070 "Integrated Hardware & Software", 581010 "Telecommunications Services", 591010 "Electrical Utilities & IPPs", or 631010 "Miscellaneous Educational Service Providers", 0 otherwise.
INTERACT	Interaction term, binary variable Product of TRUMP*US for H1 Product of TRUMP*PREF for H2.

CHANGE_SALES	The percentage of change in annual sales (Worldscope Items (WC01001 - l.WC01001) / l.WC01001); winsorized on 1 % level.
LEV	Debt-to-equity ratio (Worldscope Items WC03351 / WC03995); winsorized on 1 % level.
MTB	Market-to-book ratio (Worldscope Items WC08001 / WC03995); winsorized on 1 % level.
LOW_MTB	Binary variable becoming 1 in case a firm's market-to-book ratio is smaller than 1; 0 otherwise.
LMVE	Natural logarithm of market value of equity (Worldscope Item WC08001); winsorized on 1 % level.
LOSS	Binary variable becoming 1 in case a firm reports a loss (Worldscope Item WC01551 $<$ 0); 0 otherwise.
ROA	Return on assets calculated as a firm's return in year t / a firm's average total assets in 1 (Worldscope Items WC01551 / ((WC02999 + l.WC02999) / 2); winsorized on 1 % level.

Appendix D.B:

List of SEC Chairmen

Name	Tenure	Incumbent President
Joseph P. Kennedy (D)	02.07.34 – 23.09.35	Roosevelt (D)
James M. Landis (D)	23.09.35 – 15.09.37	Roosevelt
William O. Douglas (D)	21.09.37 – 16.04.39	Roosevelt
Jerome N. Frank (D)	18.05.39 – 09.04.41	Roosevelt
Edward C. Eicher (D)	09.04.41 – 20.01.42	Roosevelt
Gadson Purcell (D)	20.01.42 – 30.06.46	Roosevelt
James J. Caffrey (D)	23.07.46 – 31.12.47	Roosevelt
Edmond M. Hanrahan (D)	18.05.48 – 03.11.49	Truman (D)
Harry A. McDonald (R)	04.11.49 – 25.02.52	Truman
Donald C. Cook (D)	26.02.52 – 17.06.53	Truman
Ralph H. Demmler (R)	17.06.53 – 25.05.55	Eisenhower (R)
J. Sinclair Armstrong (R)	25.05.55 – 27.06.57	Eisenhower
Edward N. Gadsby (R)	20.08.57 – 26.03.61	Eisenhower
William L. Cary (D)	27.03.61 – 20.08.64	Kennedy (D)
Manuel F. Cohen (D)	20.08.64 – 22.02.69	Kennedy
Hamer H. Budge (R)	22.02.69 – 02.01.71	Johnson (D)
William J. Casey (R)	14.04.71 – 02.02.73	Nixon (R)
G. Bradford Cook (R)	03.03.73 – 16.05.73	Nixon
Ray Garrett, Jr. (R)	06.08.73 – 28.10.75	Nixon
Roderick M. Hills (R)	28.10.75 – 10.04.77	Ford (R)
Harold M. Williams (D)	18.04.77 – 01.03.81	Carter (D)
John Shad (R)	06.05.81 – 18.06.87	Reagan (R)
David S. Ruder (R)	07.08.87 – 30.09.89	Reagan
Richard C. Breeden (R)	11.10.89 – 07.05.93	George Bush (R)
Arthur Levitt (D)	27.07.93 – 09.02.01	Clinton (D)
Harvey L. Pitt (R)	03.08.01 – 17.02.03	George W. Bush (R)
William H. Donaldson (R)	18.02.03 – 30.06.05	George W. Bush
Christopher Cox (R)	03.08.05 – 20.01.09	George W. Bush
Elisse B. Walter (D)	15.12.12 – 09.04.13	George W. Bush
Mary L. Schapiro (I)	27.01.09 – 14.12.12	Obama (D)
Mary Jo White (I)	10.04.13 – 20.01.17	Obama
Jay Clayton (I)	04.05.17 – 23.12.20	Trump (R)
Gary Gensler (D)	since 17.04.21	Biden (D)

Appendix D.C:

Members of the SEC Commission

Source: SEC (2023b)

Appendix D.D:

UPLOAD Letters Regarding "New Oriental Education & Technology Group Inc."

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

DIVISION OF
CORPORATION FINANCE

April 2, 2012

Via Email
Louis T. Hsieh
President and Chief Financial Officer
New Oriental Education & Technology Group Inc.
No. 6 Hai Dian Zhong Street, Haidian District
Beijing 100080
People's Republic of China

> **Re:** **New Oriental Education & Technology Group Inc.**
> **Form 20-F for Fiscal Year Ended May 31, 2011**
> **Filed October 14, 2011**
> **File No. 001-32993**

Dear Mr. Hsieh:

We have reviewed your filing and have the following comments. In some of our comments, we may ask you to provide us with information so we may better understand your disclosure.

Please respond to this letter within ten business days by amending your filing, by providing the requested information, revised disclosures or by advising us when you will provide the requested response. If you do not believe our comments apply to your facts and circumstances or do not believe an amendment is appropriate, please tell us why in your response.

After reviewing any amendment to your filing and the information you provide in response to these comments, we may have additional comments.

Risk Factors, page 5

1. As a public company, your auditor is required by law to undergo regular Public Company Accounting Oversight Board (PCAOB) inspections to assess its compliance with U.S. law and professional standards in connection with its audits of financial statements filed with the SEC. The PCAOB, however, is currently unable to inspect the audit work and practices of your auditor (see http://pcaobus.org/International/Inspections/Pages/IssuerClientsWithoutAccessList.aspx). As a result of this obstacle, investors in U.S. markets who rely on your auditor's audit reports are deprived of the benefits of PCAOB inspections of auditors. Therefore, please state this fact under a separate risk factor heading. Explain that this lack of inspection prevents the PCAOB from regularly evaluating your auditor's audits and its quality control procedures.

UPLOAD: Comment letter issued on April 2, 2012 regarding Form 20-F for Fiscal Year Ended May 31, 2011. Initial comment letter for this case.

November 20, 2012

<u>Via E-mail</u>
Louis T. Hsieh
President and Chief Financial Officer
New Oriental Education & Technology Group Inc.
No. 6 Hai Dian Zhong Street
Haidian District, Beijing 100080
People's Republic of China

> Re: **New Oriental Education & Technology Group**
> **Form 20-F for the Fiscal Year Ended May 31, 2012**
> **Filed October 12, 2012**
> **File No. 001-32993**

Dear Mr. Hsieh:

We have reviewed your filing and have the following comments. In some of our comments, we may ask you to provide us with information so we may better understand your disclosure.

Please respond to this letter within ten business days by amending your filing, by providing the requested information, or by advising us when you will provide the requested response. If you do not believe our comments apply to your facts and circumstances or do not believe an amendment is appropriate, please tell us why in your response.

After reviewing any amendment to your filing and the information you provide in response to these comments, we may have additional comments.

"We rely on contractual arrangements for our operations in China…," page 14

1. Please expand paragraph two of this risk factor to address the risk that one of the consequences of the inability to enforce your contractual arrangements, namely the inability to exert control, could be the inability to consolidate your financial statements. In addition, state the portion of your historic revenues and operations attributable to New Oriental China and its schools and subsidiaries.

2. Please expand this risk factor to address the risk that certain of your service agreements permit the schools and subsidiaries of New Oriental China to terminate the agreement without the consent of your wholly owned subsidiaries in China and certain of these agreements require both parties to consent to the agreements' renewal, as discussed on page 48.

UPLOAD: Comment letter issued on November 20, 2012 regarding Form 20-F for Fiscal Year Ended May 31, 2012. Initial comment letter for this case. Due to the proximity to the last CORRESP letter regarding prior years 20-F related comment letter case (October 5, 2012), this letter is irregularly count as number 13 of the prior case.

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March 8, 2013

<u>**Via E-Mail**</u>
Louis T. Hsieh
President and Chief Financial Officer
New Oriental Education & Technology Group Inc.
No. 6 Hai Dian Zhong Street
Haidan District, Beijing 100080
People's Republic of China

Re:	**New Oriental Education & Technology Group Inc.**
	Form 20-F for the Fiscal Year Ended May 31, 2011
	Filed October 14, 2011
	Form 20-F for the Fiscal Year Ended May 31, 2012
	Filed October 12, 2012
	No. 001-32993

Dear Mr. Hsieh:

We have completed our review of your filings. We remind you that our comments or changes to disclosure in response to our comments do not foreclose the Commission from taking any action with respect to the company or the filings and the company may not assert staff comments as a defense in any proceeding initiated by the Commission or any person under the federal securities laws of the United States. We urge all persons who are responsible for the accuracy and adequacy of the disclosure in the filings to be certain that the filings include the information the Securities Exchange Act of 1934 and all applicable rules require.

Sincerely,

/s/ Carlos Pacho for

Larry Spirgel
Assistant Director

UPLOAD: Comment letter issued on March 8, 2013 regarding Form 20-F for Fiscal Years Ended May 31, 2011 and May 31, 2012. Closing comment letter for these cases. Due to the irregular assignment of the 2012-related comment letters to the prior year, this letter is irregularly count as number 19 of the 2011 case. Correctly, it had to be number 13.

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Declaration of Own Contribution

Parts A, B and D of this thesis are single-authored. Part C is a co-authored project with Jan Seitz.

Each of the authors contributed to this project as follows: I provided data on SEC comment letters from Electronic Data Gathering, Analysis, and Retrieval (EDGAR), PAC contributions from the Federal Election Commission (FEC)'s website, lobbying expenditures from the Center for Responsive Politics (CRP), congressional committee data from Charles Stewart III's data page, as well as firm financials from EIKON. Jan Seitz provided data on EDGAR activity from EDGAR log files. Data processing and empirical analyses were jointly conducted with Jan Seitz in the lead.

Both authors jointly wrote the paper. While I mainly took responsibility for the introduction, the literature review on SEC monitoring and regulatory capture, and the exploitation of the research questions, Jan Seitz was in the lead in describing about the research design, data and descriptives, the empirics, and the discussion on the main findings.

Both authors presented the research project at at least one research conference.