

# CORPORATE POLITICAL ACTIVITY AND FIRM OUTCOMES: A META-ANALYSIS

MICHAEL HADANI

DEPARTMENT OF MANAGEMENT - LONG ISLAND UNIVERSITY

720 Northern Boulevard – Brookville, NY 11548 - 1300

Phone: (516) 299 3307 - Fax: (516) 2993917

Email: [michael.hadani@liu.edu](mailto:michael.hadani@liu.edu)

NICOLAS M. DAHAN

SCHOOL OF ECONOMICS AND BUSINESS - ST MARY'S COLLEGE OF CA

JEAN-PHILIPPE BONARDI

FACULTY OF BUSINESS AND ECONOMICS (HEC) - UNIVERSITY OF  
LAUSANNE

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## ABSTRACT

Using meta-analytic methods on a sample of 74 studies, we explore the links between CPA and public policy outcomes, and between CPA and firm outcomes. We find that CPA has at best a weak effect and that it appears to be better at maintaining public policy than changing them.

## INTRODUCTION

Corporate Political Activity (CPA), defined as "corporate attempts to shape government policy" (Hillman, Keim & Schuler, 2004: 837), represents a non-market strategic approach that is on the rise in US politics (Hersch, Netter & Pope, 2008) due to the sharp rise in economic intervention of the federal and state governments since 2008 (Kaiser, 2009; Reich, 2009). Nevertheless, a close look at the evidence up to date may leave firms' shareholders and their boards at a loss as to the actual impact of CPA. Indeed, empirical studies offer a confusing picture, as there is mounting evidence challenging the common view that CPA is beneficial to firms which pursue it (for example, Hart, 2004; Hadani, 2011; Lowery, 2007). On the one hand, there is a long-standing view that CPA is a "strategic" non-market activity, which can generate firm-specific gains (Hillman, 2005; Hillman & Keim, 2005; Rehbein & Schuler, 1999; Schuler). This view has enjoyed some empirical (yet contextual) support over the past decades (such as Bonardi, Holburn, & Vanden Bergh, 2006; Hillman, Zardhooki & Bierman, 1999).

On the other hand, an increasing number of scholars express skepticism over the business case for CPA (Ansolabehere, De Figueiredo, and Snyder, 2003; Milyo, Primo and Groseclose, 2000 among others). For example, Hersch, Netter and Pope (2008) fail to find any association between firms' PAC and lobbying activities and firm performance

measured as Tobin's Q. Aggarwal, Mesche and Wang (2011) find a negative association between different measures of CPA and firm performance (see also Coates, 2011).

In this paper, we wish here to offer a meta-analysis of CPA studies in order to further explore these two arguments. More precisely, we look at the following question: does CPA generate any concrete benefit to the firm that engages in it? Our meta-analytic study is thus focused on CPA's impact on firm performance (as opposed to CPA antecedents), in the USA only (to control for the legal and institutional context). Unlike Lux et al., (2011) we attempt to open the black box of CPA by examining both the intermediary linkages among types of CPA and policy making outcomes, the impact of policy making outcomes on firm outcomes (performance) as well as the direct impact of CPA on firm outcomes (similar to the Lux et al., 2011, study).

## **EXPLORING CPA'S OUTCOMES**

In order to be effective, CPA needs first to be able to secure political access to public policy makers, followed by influence over them, which can be converted into a favorable public policy decisions (Hillman, Keim, & Schuler, 2004; Shaffer, 1995) or the ability to stall adverse legislation (Kersh, 1986). The dominant strategic management view of the public policy environment is that of a marketplace where several public policy demanders vie for the supply of a favorable public policy decisions (Bonardi, Hillman, & Keim, 2005; Keim, 2011). In such a marketplace, the 'price' being negotiated between sellers and buyers is an exchange of resources deemed of equivalent value: a public policy decision which would improve corporate performance (a form of rent extraction: Stigler, 1971; Tollison, 1982) in return for resources valuable to public policy makers, such as wining and dining, free trips, relevant technical information, campaign donations, favorable grassroots mobilization or media exposure (Bonardi, 2011; Dahan, 2005; Hillman & Hitt, 1999).

*Proposition 1: Ceteris paribus CPA will not be positively associated with public policy outcomes.*

### **CPA and Types of Public Policy Outcomes**

However not all CPA targets respond similarly. In an attempt to refine our understanding of the relationship among CPA and policy outcomes such as voting behavior, we want to review meta-analytically empirical studies in terms of the type of public policy outcomes that firms seek out. As several scholars point out, the public policy environment is very conservative (Kindleberger, 1970), due to the difficulty of challenging prior hard-to-reach compromises, as well as the fact that past policy choices tend to lock-in and restrict future choices down a certain policy path (Pierson, 2000). Thus taking a new direction is a much harder proposition than maintaining the public policy status quo (Baumgartner et al., 2009; Wilson, 1989).

Accordingly, we distinguish between two types of desired public policy outcome: a new (presumably favorable) public policy decision which would represent a departure from existing policy (which we call "promoting public policy change"), as opposed to a policy continuity decision (that is, killing an attempt at public policy change, which we call "maintaining stable public policy outcomes"). Public policy continuity may be a very

desirable outcome to some firms. It represents a goal of political risk minimization, buffering the firm from a potentially hostile environment in order to maintain a beneficial status quo situation (Baumgartner et al., 2009; Baysinger, 1984; Meznar & Nigh, 1995). For example, an oil company could be politically active simply to challenge any regulatory attempt at switching to alternative sources of energy (such as removing oil subsidies, mandatory car fuel efficiency increases, creating carbon taxes, etc). These political activities would enable the oil company to continue to use a very profitable market strategy for a longer duration, which would be an extremely valuable public policy outcome to the company and its shareholders. However when a firm tries to challenge existing legislation – create a policy change – such as supporting the passage of new legislation, they will likely face stronger opposition from existing or entrenched political interests and their supporters (Baumgartner et al., 2009 see also Smith, 2000).

We therefore distinguish our meta-analytic analyses depending on the type of public policy outcome a firm seeks out, and we expect to find a stronger link between CPA and public policy outcome when a firm attempts to maintain policy status quo, in comparison to firms trying to promote new legislation.

*Proposition 2: Ceteris paribus CPA is more positively associated with maintaining stability in public policy making than with promoting changes in public policy making.*

### **CPA and Public Policy Outcomes: The Case of Regulation**

Many scholars point out that the type of public policy environment in which a firm is engaged has a significant bearing on its chances of success. A case in point is the nature of the interaction between regulatory agencies (and their personnel) and the corporate targets of their regulatory action. While in theory regulatory agencies are not supposed to regularly consult or seek advice from the targets of their regulation the reality is very different. The concept of regulatory capture, describing a situation in which a state agency advances the interest of its regulated entities, such as the economic or the commercial interests of corporations, has been long noted by Stigler's (1971) Nobel Prize winning work. In economics the theory of regulatory capture argues that regulated interests not only have the incentives but often have the economic resources to try to interact with and access policy makers (regulators and their staff) by providing them with information and feedback both in formally but also and behind the scenes (Laffont & Tirole, 1991; Levine & Forrence, 1990). Regulators in fact will interact with their targets to assess their state and to collect technical information they need to conduct their business (Bouwen, 2002; Wilson, 1980); there is an organic dependency between the parties based on the nature of the typical regulatory process in the USA. We expect that it will be easier for firms to obtain a favorable public policy decision from a regulatory agency, where most issues bureaucrats deal with are very technical, and have a low level of external salience, allowing less visible compromises with industry interests, than with political institutions composed of elected officials (such as Congress).

*Proposition 3: Ceteris paribus CPA will be positively associated with regulatory agencies decisions.*

### **Public Policy Outcomes and Corporate Performance**

As noted by resource dependence theory (Pfeffer & Salancik, 1978) the main impetus of CPA is firms' dependence on government decision making and regulation, which can strongly constrain firms' strategic autonomy. When a governmental decision is made with regard to industry or firm conduct one can assume it will have an impact of firm outcomes. Studies on changes in regulation support this notion.

*Proposition 4: Ceteris paribus variance in public policy outcomes is associated with variance in firm-level performance.*

## **CPA and Corporate Performance**

Given the ambiguous impact of CPA on outcomes we draw two alternative propositions:

*Proposition 5a: Ceteris paribus CPA is not associated with corporate performance.*

*Proposition 5b: Ceteris paribus CPA is positively associated with corporate performance.*

## **METHODS**

### **Literature search**

In conducting a meta-analysis we thought to identify the universe of relevant studies that pertain specifically to our theoretical proposals. Therefore, we searched for studies that explored how different forms of CPA impact policy outcomes, how policy outcomes impact firm outcomes and how firm CPA impacts firm outcomes. We define 'CPA' as broadly as possible as to include the maximum number of relevant studies, books, dissertations and unpublished work such as working papers. Thus CPA includes any mention of the following strings: corporate political activity, corporate political strategy, PAC or PAC contributions, soft money or soft money contributions, business political, government relations, lobbying, grassroots lobbying, political service, political networks, political ties.

### **Criteria for scholarship inclusion**

In order for a study to be included in the analysis it had to empirically (and not purely theoretically) analyze the relationship among our focal variables such as between types of CPA and policy outcomes. Here we further refined our inclusion criteria as to include studies that measure different aspects of CPA, or measured policy outcomes as either voting outcomes, or decision making outcomes associated with governmental agencies such as regulatory agencies and those studies that include firm outcomes such as performance (market or accounting based measures). We excluded case studies for obvious reasons (no means to derive an effect size). Our initial search yielded over 120 articles, books and unpublished work while our final sample included 74 articles, books and unpublished work from the early 1980s to 2011, covering 177, 617 observations.

Statistically for studies to be included in the meta-analysis they needed to clearly report sample size, sample years, and have a direct or indirect (amenable for statistical transformation) measure of effect size. The best effect size measure for use in a meta-

analysis is the correlation between the independent and dependent variables –  $r$  – or the multiple  $r$  (controlling for other variables) (Borenstein, Hedges, Higgins, & Rothstein, 2009; Hunter & Schmidt, 2004; Lux et al., 2011). However other measures of effect size that can be transformed to  $r$  also exist. Here we used  $t$  statistics, converted to  $r$  based on Hunter and Schmidt's (1990) formula, standardized beta coefficients converted to  $r$  based on Peterson and Brown's (2005) formula, and the odds ratio based on the natural log of the odds ratio (see Borenstein et al., 2009).

## **Procedure**

For each study we calculated an average effect size if more than one statistical test was reported (Hunter & Schmidt, 2004). However when examining the relative impact of CPA's ability to promote legislative change versus stability (proposition 3) we separated between the relevant effect size estimates when available within and across studies.

We used the Hunter and Schmidt (2004) random effects meta-analysis approach which assumes the average effect size varies randomly among studies as they are sampled from populations that may have different population effect sizes (Borenstein et al., 2009). Fixed effects models assume that all of the variability between effect sizes is due to sampling error (Hunter & Schmidt, 2004). Random effects models however assume that the variability between effect sizes is due to sampling error plus variability in the population of effects (unique differences in the set of true population effect sizes). As such variability in effect size is due to “subject” level noise and true unmeasured differences across studies.

Thus, random effects models involve estimating two error terms, compared to a single error term for a fixed effect approach. When using random effects models we would likely expect effect sizes to be heterogeneous since they are taken from different populations (Hunter & Schmidt, 2000; Field, 2005a). We then derived the effect size – the  $r$  metric – from studies' reported statistical data, and then calculated the mean effect size for each category of interest we also calculated the unbiased effect size ( $\rho$ ), the variance of sample effect sizes, the sampling error variance, the variance of population effect size, and tested the homogeneity of effect sizes across the population of studies we collected and the 95% confidence interval. We also calculated the significance of the mean effect size (Johnson et al., 1995); this test posits that the mean effect size  $r$  is equal to a population mean effect of zero. It is important to note that using Fisher's  $Z$  transformation of effect sizes (Hedges & Olkin, 1985; Hedges & Vevea, 1998) does not change the estimation of our effect sizes.

## **Key measures**

*Corporate political activity.* We measured CPA as any firm non market behavior that included at least one of the following: PAC contributions, lobbying activity (outside or in-house), any expenses related to lobbying, the existence of political ties between the firm and policy makers (contacts or politically ties directors) and petitions to or interactions with regulatory agencies.

*Policy outcomes.* We measured policy outcomes as reflecting voting outcomes in Congress and/or in the Senate or the decisions made by government agencies such as regulatory agencies or other government agencies (for example, PUCs which regulate utilities or decisions made by the international trade commission).

*Firm outcomes.* We measured firm outcomes as any measure that pertains to firm performance such as accounting based measures (return on assets, return in sales, market share, etc.) and financial based measures (such as market value).

## **RESULTS**

Proposition 1, which proposed that CPA will not impact policy outcomes, was supported ( $r=.02$ ,  $\rho=.06$ ,  $p>.05$ ). Proposition 2 argued that CPA is more positively associated with maintaining stability in policy making than with promoting changes in policy making. We found weak mean effect sizes for both promoting change ( $r=.02$ ,  $\rho=.08$ ,  $p>.05$ ) and for maintaining stability in policy outcomes ( $r=.05$ ,  $\rho=.14$ ,  $p>.05$ ) but comparatively the mean effect size for maintaining stability in policy outcomes was larger than the one for promoting changes, in particular the estimate for mean effect size correction for the population ( $\rho$ ) which was larger for maintaining policy outcomes than for changing them ( $\rho=.14$  versus  $\rho=.08$ ). Because the mean effect sizes were not significant it is unclear if these differences are meaningful, yet given the differences of the populations estimated mean effect sizes ( $\rho$ ) it appears (tentatively) that the proposition was supported. Proposition 3 argued that CPA will be positively associated with regulatory agencies decisions. Though the mean effect size was moderate in strength it was not significant ( $r=.23$ ,  $\rho=.25$ ,  $p>.05$ ), though the population estimate was moderately large as well. Proposition 4 argued that variance public policy outcomes is associated with variance in firm-level performance, and it was not supported ( $r=.04$ ,  $\rho=.02$ ,  $p>.05$ ). Proposition 5a argued for no direct associations between CPA and firm performance. Proposition 5b argued for a positive association between CPA and firm performance. We found support for proposition 5a ( $r=.001$ ,  $\rho=.10$ ,  $p>.05$ ).

## **DISCUSSION – CONCLUSION**

In many ways much of the research on CPA, at least in the field of management, assumes that it is an effective non-market strategy to access legislators and influences the public policy making process. Our exploratory analysis is not as sanguine. We find no systematic evidence to support the view that CPA, either indirectly or directly, impacts firms' bottom line. This by no means indicates that CPA is an ineffective. Since we found significant and systematic variance for many of the relationships we explored (in terms of non-homogeneity of the mean effect size) it is clear that contexts exist under which CPA is more and is less effective. However one should view CPA and its supposed benefits more cautiously than extant scholarship assumes.

## **REFERENCES AVAILABLE FROM THE AUTHORS**