

# Partisan Regulatory Actions: Evidence from the SEC \*

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May 23, 2024

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\*We thank Pat Akey, Hami Amiraslani, Jennifer Arlen (NYU Law), Jim Brickley, Jungcho Choi, Rich Frankel, Ray Gao, Eric Gelsomin, Sudarshan Jayaraman, Jennifer Jia, Xiumin Martin, Clive Lennox, Hao Qu, Shiva Rajgopal, Charles Wasley, Xixi Xiao, Yuanzhe Zhang, Katie Zheng, Jerry Zimmerman, participants at FIU Research Day Conference, and seminar participants at CUHK-Shenzhen, INSEAD, Peking University, UIUC, University of Rochester, and Washington University in St. Louis, for helpful feedback. We are indebted to Dan Taylor, Terrence Blackburne, and Sara Toynbee for sharing SEC investigations data, authors of Babenko et al. (2020) for CEO political contributions data, and Charles Stewart III for congressional committee membership data. We are grateful to the Simon Business School for financial support.

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# Partisan Regulatory Actions: Evidence from the SEC

## Abstract

We study the influence of political partisanship in SEC investigations and AAER enforcement actions against financial misconduct. We find that the SEC is more likely to launch an investigation against a firm that is misaligned with the agency's political ideology than for other firms. The likelihood of an AAER appears unaffected by political misalignment, but once named in an AAER, a misaligned firm faces harsher penalties than other firms. We find higher Type I error rates (more false positives) in SEC investigations among misaligned firms and higher Type II error rates (more false negatives) among non-misaligned firms, suggesting misallocation of scarce enforcement resources due to partisanship.

*JEL codes:* G18, K22, K42, M41

*Keywords:* SEC, Partisanship, Political ideology, Enforcement, Legal penalties, Accounting fraud, Misreporting, Career concerns

*“To ensure that the Commission remains non-partisan, no more than three Commissioners may belong to the same political party.”*

– The Securities and Exchange Commission Website

*“The agency seeks to direct its limited resources toward cases that are likely to have the greatest impact in furthering the SEC’s mission.”*

– SEC Annual Performance Report, FY 2022

## **1. Introduction**

The Securities and Exchange Commission (SEC) plays a central role in maintaining the integrity of the U.S. securities markets through its enforcement of federal securities laws. The manner with which these enforcement activities are carried out by the SEC has significant implications for the health of the financial markets. The stated missions of the SEC, i.e., protecting investors, maintaining fair, orderly, and efficient markets, and facilitating capital formation, allow no room for partisan politics. However, with the sharp rise of political partisanship in the U.S., few economic and social activities are completely immune from its influence (Iyengar and Westwood, 2015; Iyengar, Lelkes, Levendusky, Malhotra, and Westwood, 2019; Boxell, Gentzkow, and Shapiro, 2022).

The top leadership of the SEC is borne out of the political process because the five Commissioners are political appointees of the U.S. President, with advice and approval of the Senate. Against this inherently political backdrop is the built-in mechanism to protect the SEC’s independence from undue political influence through the requirement that no more than three out of the five Commissioners may belong to the same political party.<sup>1</sup> However, question remains as to whether partisan politics hold sway in some of the SEC’s most consequential functions, such as those related to its regulatory actions against financial misconduct by security issuers. This is the focus of our study. Specifically, we examine whether political partisanship plays a role in SEC regulatory actions,

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<sup>1</sup><https://www.sec.gov/about/commissioners>

as reflected in 1) its investigations of financial misconduct and 2) AAER enforcement actions stemming from the investigations. Understanding these questions will shed light on how the SEC deploys its scarce resources and whether the landscape of the federal securities laws enforcement is skewed by partisan politics.

Whether political partisanship affects the SEC's investigative and enforcement activities is ex ante unclear. On the one hand, the issuance of an AAER requires a vote by the five SEC Commissioners. Recent work by [Engelberg, Henriksson, Manela, and Williams \(2023\)](#) documents increasing partisanship at the SEC as reflected in the SEC Commissioners' speeches and their voting behavior on the Commission's decisions, orders, and rules. On the other hand, AAERs are among the most high-profile enforcement actions issued by the SEC, with large consequences for the targeted firms, their investors, auditors, executives, and employees (e.g., [Feroz, Park, and Pastena, 1991](#); [Karpoff, Lee, and Martin, 2008a,b](#); [Choi and Gipper, 2024](#)). The weight of the decision and the care that goes into it means that extraneous considerations, such as partisan politics, may be mitigated or even eliminated. In other words, the SEC may be able to serve its core missions without the interference of partisan politics when it comes to issuing AAERs.

It is important to recognize that the vast majority of the enforcement personnel at the SEC are not political appointees.<sup>2</sup> These civil servants are responsible for initiating and carrying out SEC investigations, which are necessary precursors to the AAERs. Unlike political appointees in federal agencies in the U.S., who experience pronounced turnover when the political party that controls the White House changes, the career outcomes of civil servants in these agencies are largely shielded from these political cycles ([Spenkuch, Teso, and Xu, 2023](#)). It is therefore expected that their actions are to some degree protected from political considerations. On the other hand, the hierarchical structure of a bureaucracy, such as the SEC, suggests that the "political tone at the top" may

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<sup>2</sup>Only the highest level of the SEC leadership (the five Commissioners) are political appointees, i.e., directly appointed by elected politicians (the U.S. President in this case). The Director of the Enforcement Division is appointed by the Chair of the SEC.

percolate to lower levels of the organization and potentially affect regulatory actions conducted by career bureaucrats even though they are not themselves political appointees. If career bureaucrats expect partisan preferences at the top leadership, they may skew their investigations and enforcement actions accordingly.

If partisan politics play a role in SEC regulatory actions against financial misconduct, we expect different intensities of these actions for firms that are misaligned versus non-misaligned with the SEC's political ideology. We call this as the *partisan regulatory actions hypothesis*. We measure the SEC's political leaning through its leadership team composition, i.e., the party (Democratic versus Republican) affiliation of the majority of the Commissioners at any given point in time.<sup>3</sup> We proxy for a firm's political leaning through the party to which the CEO contributes the most to.<sup>4</sup> We define a firm as politically misaligned with the SEC if its political ideology does not match the SEC's political ideology.<sup>5,6</sup> The partisan regulatory actions hypothesis predicts more intensive regula-

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<sup>3</sup>We assign the Commissioner(s) not officially affiliated with a political party the party of the appointing President.

<sup>4</sup>Following prior literature, we use CEO personal contributions instead of firm PAC (political action committee) contributions to classify firm ideology (e.g., [Hong and Kostovetsky, 2012](#); [Lee, Lee, and Nagarajan, 2014](#); [Hutton, Jiang, and Kumar, 2014](#); [Jiang, Kumar, and Law, 2016](#)). Because the CEO is essentially the face of a firm, their personal contributions are likely symbolic of the firm's value system. While a CEO may contribute to both political parties, this does not necessarily indicate strategic behavior, as the CEO could be contributing to candidates based on issues. Our goal is to capture the political *leaning* of the CEO while recognizing the nuances in political beliefs and that an individual may lean one way but may not fit neatly into a single-party political box. We do not use firm's PAC contributions to infer firm's ideological leaning because firms, typically with access to more resources than individuals, use PAC contributions as an important strategic tool for buying political influence either to create value (e.g., [Duchin and Sosyura, 2012](#); [Akey, 2015](#)), or because of agency problems (e.g., [Aggarwal, Meschke, and Wang, 2012](#)). Consistent with this idea, [Correia \(2014\)](#) notes that firms use PAC contributions to buy political access or favor, rather than for ideological reasons. We note that all our empirical analysis controls for firm PAC contributions. We also do not use voter registration records to infer ideological leaning (e.g., [Kempf and Tsoutsoura, 2021](#); [Fos, Kempf, and Tsoutsoura, 2023](#)) because it requires making requests to individual states and many states do not share voter registration records.

<sup>5</sup>CEO contribution is only a marker of the firm's values and beliefs – our predictions do not require the SEC to directly observe CEO personal contributions. We conjecture that the firm's/CEO's ideology is likely known in the top business and regulatory circles (for example, through participation at Davos World Economic Forum Annual Meetings). However, for researchers this information is less easily observable. While it may be the case that firm/CEO ideology is also reflected in activities such as CEO tweets, however, business leaders may self-censor their public statements and such data is unlikely to be systematic.

<sup>6</sup>A given firm's political misalignment with the SEC can change due to (i) a change in the SEC's ideology, (ii) a change in the current CEO's ideology, or (iii) a CEO turnover that brings in a new CEO with a different ideology.

tory actions against firms that are politically misaligned with the SEC.<sup>7</sup>

A substantial literature in political science documents that political ideology is becoming a highly significant dimension of people's social identity, and that there is strong affective polarization along party lines in America today (e.g., [Iyengar et al., 2019](#)). There is evidence of strong out-group animus and distrust along party lines (e.g., [Balliet, Tybur, Wu, Antonellis, and Van Lange, 2018](#)), and the effects extend beyond political topics to various social and economic decisions (e.g., [Iyengar and Westwood, 2015](#)). This general lack of trust against opposing partisans can manifest as more intensive SEC regulatory actions against misaligned firms in the form of greater suspicion of financial misconduct at these firms and more skepticism in the face of potentially exonerating evidence. We refer to this as the *psychological effect channel* of partisan regulatory actions.

In addition to the psychological effect of low trust against out-group members, pursuing regulatory actions against firms with close ties to the opposing party could also be a calculated move on the part of the SEC Commissioners and their subordinates to please own party politicians if the regulatory actions potentially cause reputational and financial damage to the opposing political party and its corporate supporters. We refer to this as the *career concerns channel* of partisan regulatory actions.

We test the partisan regulatory actions hypothesis through two types of SEC regulatory actions: 1) investigations of financial misconduct, and 2) AAER enforcement actions.<sup>8</sup> Using a sample of 1,568 SEC investigations opened between 2001 and 2015 (based on [Blackburne, Kepler, Quinn, and Taylor \(2021\)](#)'s data obtained through FOIA requests), we find that the likelihood of an SEC investigation is significantly higher for firms with

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<sup>7</sup>We use the Democratic versus Republican dichotomy as a proxy for the differences in political belief systems. The hypothesized partisan behavior of the regulator could be driven by differences in the "D versus R" party "label" or the differences in the underlying belief systems these labels represent. The distinction is not important for our inferences of partisan behavior.

<sup>8</sup>The SEC Enforcement Division staff may launch an investigation of financial misconduct after obtaining promising leads and evidence through informal inquiries. When the Enforcement staff determines from the investigation that the case has merits, they can recommend the case to the Commissioners for enforcement actions, which require a vote from the five Commissioners. Enforcement actions may take the form of Civil Action or Administrative proceedings, which are publicly released by the SEC as an AAER (Accounting and Auditing Enforcement Release).

political ideology misaligned with that of the SEC's than for other firms. This effect is stronger for firms with stronger ideology. These findings offer support for the partisan regulatory actions hypothesis in SEC investigations of financial misconduct.

We next turn to AAER enforcement actions, with a sample of 699 AAERs issued from 2001 to 2015. Several features of AAERs set them apart from investigations. First, issuing an AAER is a much weightier decision than launching an investigation, considering the heavy consequences of an AAER for a targeted firm and its stakeholders and contracting parties. The necessary caution and care going into the decision to issue an AAER can conceivably mitigate, or even eliminate, extraneous considerations such as partisan politics. Second, an AAER is, by definition, public whereas an investigation can remain undisclosed (e.g., [Blackburne and Quinn, 2023](#)), meaning the former is subject to more public scrutiny for possible political influence than the latter. The potential reputational loss from being perceived as partisan could act as a discipline against such behavior. Our empirical analysis suggests that the likelihood of receiving an AAER is no different for politically misaligned firms versus other firms. However, for firms that do receive an AAER, enforcement penalties are harsher for misaligned firms.

Collectively, the above evidence suggests that partisan politics exerts influence in SEC regulatory actions against financial misconduct, especially pertaining to the initiation of an investigation. However, the SEC enforcement system appears to have some ability to self-correct and protect against the influence of partisanship when it comes to the crucial decision of issuing an AAER, such that the extensive margin (likelihood) of an AAER appears unaffected by partisanship although the intensive margin (penalties) of an AAER is not immune from such influence.

We next conduct tests to distinguish between the *psychological effect channel* and the *career concerns channel* of partisan regulatory actions by studying the SEC Commissioners' age. The psychology and political science literatures show that partisanship is generally acquired in a person's formative years and remains stable through life

(e.g., [Sears, 1975](#); [Iyengar et al., 2019](#)). On the other hand, career concerns tend to be more pronounced for those who are younger and with a longer work horizon (e.g., [Gibbons and Murphy, 1992](#)). Our evidence of partisan regulatory actions (regarding both the likelihood of an investigation and the harshness of AAER penalties) is stronger when SEC Commissioners from the majority party are younger, suggesting the career concerns channel at work, i.e., SEC Commissioners' partisan regulatory actions seem, at least in part, to be an effort to appease own political party for career gains. To more directly link Commissioners' partisan regulatory actions to future career gains as we hypothesize in *career concerns channel*, we explore the association between the SEC Commissioners' partisan enforcement and their career outcomes and find evidence that suggests better career outcomes for Commissioners with more partisan enforcement.

We next turn our analysis to firm behavior. According to [Becker \(1968\)](#)'s theory on the economics of crime, the decision to commit a crime involves cost and benefit tradeoffs by the would-be criminal. [Kedia and Rajgopal \(2011\)](#) find evidence consistent with firms taking into account the SEC's enforcement preferences when committing financial misconduct. If political misalignment with the SEC is one factor that increases the detection likelihood and the penalties of misconduct (i.e., the expected costs of the crime), it can discourage a misaligned firm from engaging in misconduct in the first place. Meanwhile, a non-misaligned firm may feel emboldened by lower expected SEC oversight and thus commit more misdeeds. This would predict a negative relation between misconduct and political misalignment with the SEC. On the other hand, a firm's political (mis)alignment may change with shifts in the larger political climate or the firm's own political affinity. The statute of limitation of most federal crimes (including financial misdeeds) is a non-trivial five-year period, during which time the political leaning of the SEC could have changed even if the firm's own political affinity remains the same. In light of the uncertainty in future political alignment with, and enforcement by, the SEC, a firm may not factor its current political (mis)alignment with the SEC into its decision to



commit financial misconduct. We find that misaligned firms are no less, or more, likely to initiate misreporting, as measured by subsequent financial statement restatements, suggesting that firms do not find it on net beneficial to internalize the SEC's partisan regulatory actions when committing misconduct.

The above findings together, i.e., misaligned firms are no more likely to transgress while the SEC more heavily targets its regulatory actions towards these firms due to partisanship, imply potential misallocation of the agency's scarce resources. If excessive resources are allocated to investigating misaligned firms, we expect investigations of misaligned firms to lead to more false positives (Type I errors) that do not result in AAERs. This is exactly what we find – conditional on investigation, the SEC is less likely to bring AAERs against misaligned firms than for other firms. Given the SEC's budget constraints (e.g., [Kedia and Rajgopal, 2011](#)), greater Type I errors for misaligned firms suggests potentially greater Type II errors (false negatives) for non-misaligned firms as less than optimal level of resources are allocated to monitoring these firms. Again, we find supporting evidence for this prediction. Conditional on firm misreporting as captured by financial statement restatements, the SEC is less likely to investigate non-misaligned firms, especially for more severe cases of misreporting. Interestingly, conditional on firm misreporting, the SEC is not less likely to bring an AAER against non-misaligned firms. In other words, the evidence of greater false negatives among non-misaligned firms applies to SEC investigations but not to AAERs. The above results on Type I and II errors together suggest that resources allocated towards investigating misaligned firms take resources away from investigating non-misaligned firms who misreport.

All our tests control for a host of firm characteristics, and industry and year fixed effects. Importantly, we control for firm political connections as measured by political contributions through corporate PACs (political action committees) to politicians serving on congressional committees with SEC oversight (e.g., [Correia, 2014](#)). Alternatively, our results are also robust to controlling for total PAC contributions and SEC-related firm

lobbying. While our sample period ends in 2014 due to availability of investigation data, we continue to find harsher monetary enforcement penalties for misaligned firms when we extend the sample period through 2020.

We contribute to the literature that studies political influence in SEC's enforcement actions (e.g., [Correia, 2014](#); [Mehta and Zhao, 2020](#)). However, we are different from these prior studies in several aspects. First, unlike prior literature that focuses on firms' political connections (for example, through political contributions and lobbying as in [Correia \(2014\)](#)), our interests are centered on the SEC's political leaning and the implications for its regulatory actions. As a result, the conceptual foundations are different between our and prior studies on political connections. Our predictions are based on political partisanship, which is a distinct economic force from the idea of regulatory capture ([Stigler, 1971](#); [Peltzman, 1976](#); [Watts and Zimmerman, 1986](#)) that underpins the literature on political connections (e.g., [Correia \(2014\)](#)). Furthermore, the concept of political (mis)alignment is necessarily conditional on the regulator's ideology, while political connections can be established regardless of the regulator's political affinity. Finally, we examine how political influence may manifest in both SEC investigations and AAER enforcement actions, while prior studies focus on AAER enforcements (e.g., [Correia, 2014](#); [Mehta and Zhao, 2020](#)).<sup>9</sup>

Our study also contributes to the literature on partisanship and the effect of political misalignment. While a large body of evidence suggests that political (mis)alignment affects the decisions of economic actors, including households (e.g., [Gillitzer and Prasad, 2018](#); [Meeuwis, Parker, Schoar, and Simester, 2022](#); [McCartney, Orellana-Li, and Zhang, 2023](#)), firms (e.g., [Rice, 2020](#); [Engelberg, Guzman, Lu, and Mullins, 2022](#); [Duchin, Farroukh, Harford, and Patel, 2021](#)), sophisticated economic agents, such as bankers, credit

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<sup>9</sup>[Heese, Khan, and Ramanna \(2017\)](#) document a positive association between political connections and SEC oversight through comment letters, contradicting the inference of regulatory capture in [Correia \(2014\)](#) based on enforcement actions. [Hutton, Shu, and Zheng \(2022\)](#) attribute the findings in [Heese et al. \(2017\)](#) to regulatory transparency (i.e., public disclosure of comment letters since 2004) disciplining the SEC's actions. Like [Correia \(2014\)](#), [Heese et al. \(2017\)](#) focus on political connections, which is conceptually different from the construct of political misalignment that we study.

analysts, and mutual fund managers (e.g., [Dagostino, Gao, and Ma, 2023](#); [Kempf and Tsoutsoura, 2021](#); [Fos, Kempf, and Tsoutsoura, 2022](#)), the inferences in the literature are not unequivocal. For example, [Mian, Sufi, and Khoshkhrou \(2023\)](#) conclude that household spending is insensitive to partisan bias in household economic expectations. Our findings also paint a nuanced picture – partisan bias appears to afflict SEC investigations and AAER penalties (intensive margin) but the likelihood of AAERs (extensive margin) seem unscathed. In other words, not all is lost.

The recent study by [Engelberg et al. \(2023\)](#) finds evidence of partisanship in the SEC Commissioners’ speeches and voting behavior by showing that SEC commissioners “talk” like their party’s politicians and vote along party lines. However, [Engelberg et al. \(2023\)](#) do not examine how the SEC acts against firms that do not share its ideology. We study the effects of partisanship on some of the most consequential regulatory actions of the SEC, i.e., its investigations of financial misconduct and AAER enforcement actions. This, to our knowledge, is new to the literature, and answers the call in [Amiram, Bozanic, Cox, Dupont, Karpoff, and Sloan \(2018\)](#)’s survey on financial fraud and misconduct to better understand the SEC’s objective function related to its enforcement and detection of misconduct.

## **2. Data and key variable measurements**

### **2.1. Data sources and sample construction**

We obtain data on S&P 1500 firm CEOs’ individual political campaign contributions between 2000 and 2014 from [Babenko, Fedaseyeu, and Zhang \(2020\)](#). The Federal Election Campaign Act (FECA) allows individuals to contribute directly to political candidates running in federal elections (house, senate, or president) but imposes limits on individual contributions to candidates. The limit on individual contribution per election

per candidate was \$3,300 in 2023-24.<sup>10</sup> Political candidates, in turn, are required to itemize and disclose to the FEC the identity of the individual contributor (name, employer, occupation, and address) for all individual contributions above \$200.<sup>11</sup> FEC makes this data publicly available on its website. Babenko et al. (2020) merge S&P 1500 firm CEOs with the FEC individual contributions data using individual name and employer. This data set forms our basis for measuring firm political ideology.

We obtain raw data on all closed SEC investigations between January 1, 2000, and August 2, 2017, from Blackburne et al. (2021). While the SEC can investigate entities other than public firms (for example, investment advisors, broker-dealers, accounting firms), Blackburne et al. (2021) match entities under investigation with public companies listed on the three major U.S. exchanges. We obtain data on SEC Accounting and Auditing Enforcement Releases (AAERs) issued between May 17, 1982, and December 31, 2021, from Dechow, Ge, Larson, and Sloan (2011). We hand-collect data on monetary penalties in AAERs from the SEC website. We create three separate categories of the penalty amounts – civil penalty, disgorgement, and prejudgment interest. The total penalty amount contains penalties that fall into the three categories, plus any other penalty amount outside these categories.

We obtain data on restatements from Audit Analytics, firm fundamentals from Compustat, stock returns from CRSP, and analyst following from I/B/E/S. We obtain data on SEC Commissioners' historical start and end dates, political party affiliation,<sup>12</sup> and location of SEC regional offices from the SEC website. We hand-collect SEC Commissioners' date of births by searching various online sources. We obtain corporate PAC contributions from the FEC website and corporate lobbying data from the OpenSecrets.

We construct a firm-year panel of S&P 1500 firms in the Babenko et al. (2020) sam-

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<sup>10</sup><https://www.fec.gov/help-candidates-and-committees/candidate-taking-receipts/contribution-limits/>

<sup>11</sup>Babenko et al. (2020) report that unitemized individual contributions (less than \$200) constituted only 21% of the total individual contributions in 2010.

<sup>12</sup><https://www.sec.gov/about/sechistoricalsummary>

ple. We calculate CEOs' individual political contributions to the candidates of the Republican Party and to the Democratic Party.<sup>13</sup> We then merge firm fundamentals from Compustat and stock returns data from CRSP. We also merge incidence of future SEC investigations and AAERs, and monetary penalty imposed in AAERs. Our primary sample comprises 27,227 firm-years, for 2,143 distinct firms, between 2000 and 2014. The start and end year of our sample period is based on availability of Babenko et al. (2020) data needed to construct firm ideology. For these firms, SEC opens 1,568 investigations (946 unique firms, 1,466 firm-years), and releases 699 AAERs (206 unique firms, 321 firm-years), between 2001-2015. We winsorize continuous variables at top and bottom 1%.

## 2.2. Measuring firm ideology

Motivated by the notion that the CEO is the face of the firm, our empirical strategy to identify firm political ideology is based on the CEO's individual political contributions. We employ two versions of firm ideology – *time-varying* and *time-invariant*. First, at the beginning of the sample for each firm, we analyze the CEO's political contributions and classify the firm as a Republican (Democratic) firm if the CEO contributes more to the Republican (Democratic) party than to the Democratic (Republican) party. Once assigned, the political ideology of the firm stays the same in subsequent years unless the pattern of CEO contribution changes, i.e., unless the CEO contributes more to the other party, in which case the firm's ideology changes to the other party.<sup>14</sup> We call this measure of firm-ideology, *time-varying*.<sup>15</sup>

For the *time-invariant* firm ideology measure, we first aggregate the firm's CEO contributions to each party for the entire sample period. Using this cumulative contribution, we classify a firm as a Republican (Democratic) firm for the entire sample pe-

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<sup>13</sup>We do not consider contributions to other parties because they are not economically meaningful – CEOs in our sample contribute to other parties in less than 1% of the cases.

<sup>14</sup>We replace missing time-varying firm ideology before we observe the first instance of CEO contribution in our sample with the ideology based on the first instance of CEO contribution.

<sup>15</sup>The *time-varying* measure of firm ideology allows a firm's ideology to change due to a change in the current CEO's ideology, or a CEO turnover that brings in a new CEO with a different ideology.

riod if the cumulative contribution to the Republican (Democratic) party is more than the cumulative contribution to the Democratic (Republican) party. For a given firm, this measure of firm ideology does not change anytime during the sample period. For both measures, we also retain firms with no ideology, i.e., no CEO political contributions.<sup>16</sup>

### **2.3. Measuring SEC ideology**

The SEC has five Commissioners that are all appointed for a term of five years by the President with the advice and consent of the Senate. Terms are staggered such that each year, one Commissioner's term ends. At the end of their term, Commissioners may serve up to 18 months until a replacement is found. At any point in time, no more than three out of five Commissioners may be affiliated to the same party.<sup>17</sup>

Similar to that for firm ideology, our empirical strategy to identify SEC ideology relies on party affiliation of the SEC leadership, i.e., party affiliation of the SEC Commissioners. Every day, we assign the SEC the party that the majority of the SEC Commissioners are affiliated to.<sup>18</sup> We assign the Commissioners with no party affiliation (i.e., independent) the party of the President that appointed the Commissioner. The party of the SEC for a given year is the party that the majority of the Commissioners are affiliated to for the most number of days in the year. For example, if 300 out of 365 days in a year, three out of five SEC commissioners are Republican (Democratic), then the SEC is Republican (Democratic) that year.

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<sup>16</sup>The two measures of firm ideology are correlated. Among time-varying Republican (Democratic) firm-years, around 92% (78%) of the firm-years are also time-invariant Republican (Democratic). Among firm-years with no ideology as per our time-varying measure, more than 95% of the firm-years have no ideology as per our time-invariant measure.

<sup>17</sup><https://www.sec.gov/about/commissioners>

<sup>18</sup>In doing this, we do not use days with less than five Commissioners.

## 2.4. Measuring ideological misalignment

We define ideological misalignment for a given firm-year as an indicator that equals one if the firm ideology is different from the SEC ideology. Firms with no ideology are not misaligned with the SEC. For example, if the SEC is Republican in the year 2004, then all the Democratic firms in 2004 are ideologically misaligned with the SEC, while Republican firms and firms with no political ideology are not misaligned with the SEC. When using the *time-varying* measure of firm ideology, misalignment for a firm can change if the firm ideology changes or if the SEC ideology changes. However, when using the *time-invariant* measure of firm ideology, misalignment for a firm can only change with a change in SEC ideology.

## 3. Research design and descriptive statistics

### 3.1. Research design

To examine SEC's partisan regulatory actions, our basic regression specification is the following:

$$SEC\ Action_{it+1} = \beta\ Misalignment_{it} + \gamma' X_{it} + \alpha_j + \alpha_t + \varepsilon_{it+1} \quad (1)$$

where  $i, j, t$  index firm, SIC-2 digit industry, and year, respectively. Depending on the test, *SEC Action* is (i) an indicator that equals one if the SEC opens an investigation against the firm  $i$  (*SEC Investigation*), (ii) an indicator that equals one if the SEC releases an AAER against the firm  $i$  (*AAER*), or (iii) the natural logarithm of one plus the monetary penalty imposed on the firm  $i$  in an AAER (*CivPen, Disg, PreInt, TotalPen*). *Misalignment* is an indicator that equals one if the firm ideology is different from the SEC ideology (see Sections 2.2, 2.3, and 2.4 for construction). To allow *SEC Action* to be a reaction to the firm's misalignment status, we measure *SEC Action (Misalignment)* in the year  $t+1$  ( $t$ ).

Our *partisan regulatory actions* hypothesis predicts that the SEC’s regulatory actions are more intensive against firms that are politically misaligned with the SEC, i.e.,  $\beta > 0$ .

$X$  is a vector of control variables guided by prior literature (e.g., [Kedia and Rajgopal, 2011](#); [Correia, 2014](#); [Blackburne, Bozanic, Johnson, and Roulstone, 2020](#); [Blackburne et al., 2021](#); [Holzman, Marshall, and Schmidt, 2024](#)). To control for the firm fundamentals that might affect the likelihood of misreporting and in turn SEC actions against the firm,  $X$  includes various firm characteristics – size (*Size*), book-to-market (*BM*), leverage (*Leverage*), profitability (*ROA*), annual stock returns (*Stock Return*), annual stock return volatility (*Idiosyncratic Volatility*). We also control for discretionary accruals (*DACC*) ([Kothari, Leone, and Wasley, 2005](#)). To additionally control for firm visibility and monitoring by the SEC, we control for analyst following (*Analyst Following*), distance to the nearest SEC regional office (*Distance to SEC*) ([Kedia and Rajgopal \(2011\)](#)), and whether the firm is in the S&P500 index (*SP500*). Finally, to control for the effect of firm’s political connections on SEC actions ([Correia, 2014](#)), we control for firm political contributions through corporate PACs in the last five years to politicians serving on congressional committees with SEC oversight (*PAC Contri SEC-Relevant*). Alternatively, instead of firm PAC contributions to SEC-relevant politicians, we individually also control for total firm PAC contributions over the last five years, or firm lobbying to the SEC over the last three years (untabulated). All variables are defined in Appendix A. We include SIC-2 industry fixed effects to absorb time-invariant industry level factors that affect SEC actions, and year fixed effects to absorb time varying factors, such as macroeconomic conditions and SEC’s total budget, that might affect SEC actions. We cluster standard errors by firm to account for any within-firm correlation in residuals.

### 3.2. Descriptive statistics

Figure 1 shows the distribution of firm ideology (time-varying) over time and across Fama-French 12 sectors. Across all years and most sectors, more firms are Repub-



lican than Democratic. The gap between the proportion of Republican and Democratic firms is more pronounced in some sectors than others. For example, the energy and the manufacturing sectors have much more Republican firms than Democratic firms, whereas, this gap is much smaller in the business equipment and software and the telecom sectors.

Figure 2 shows the political party composition of the SEC Commissioners over time. With one Commissioner's term ending each year, the staggered appointment of SEC Commissioners follows the rule that no more than three out of five commissioners may belong to the same political party. This means that sometimes the President may need to appoint a Commissioner from the opposite party or an independent Commissioner with no official party affiliation. As evident in the figure, the political affiliation of the majority of SEC commissioners at any point in our sample period largely aligns with the party of the President in power (we assume that an independent Commissioner is more likely to align with the party of the appointing President). This suggests that the President carefully, and strategically, manages the party composition of the Commissioners so as to maintain own-party majority on the Commission.<sup>19,20</sup> Figure 3 shows ideological misalignment over time and across sectors. Figure 4 shows incidence of SEC investigation opening over the years and across sectors.

Table 1 reports descriptive statistics for our firm-year sample. SEC opens an investigation against firms in our sample in 5.4% of the firm-years, and releases an AAER in 1.2% of the firm-years.<sup>21</sup> Around 30% of the firm-years are ideologically misaligned (time-varying firm ideology) with the SEC. The average firm has total assets of \$1.9 bil-

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<sup>19</sup>Anecdotal evidence also suggests the majority party pays close attention to the party composition of the SEC to carefully manage the majority. For example, see the Wall Street Journal article on December 20, 2021, "Republican SEC Commissioner Roisman to Leave Agency" (Michaels, 2021)

<sup>20</sup>To alleviate concerns that our main results (see Section 4) might be driven by firms misaligned with the party of the President (and not the SEC), which might make firms reliant on federal support (e.g., subsidies, government contracts, etc.) perform poorly, in turn engage in more misreporting to hide deteriorating performance, and thus face greater SEC investigation rate, all our tests control for a host of time-varying firm characteristics, especially firm performance (return on assets, stock returns) and discretionary accruals.

<sup>21</sup>Without requiring non-missing controls.

lion, ROA of 3.3%, and annual stock returns of 14.1%. The average firm is followed by 4.47 analysts, and 25.8% of the firm-years are in the S&P 500. The average five-year PAC contribution to SEC-relevant politicians for firms who make PAC contributions is \$124,000. Panel B reports the descriptive stats for monetary penalty amounts in AAERs. The median penalty for those who receive monetary penalty in AAER is \$1.48 million. Table 2 reports the correlation matrix.

## 4. Results

To test our *partisan regulatory actions* hypothesis, we focus on two important SEC actions – SEC investigations and AAER enforcements.

### 4.1. Ideological misalignment and SEC investigations

To examine whether the SEC is more likely to investigate politically misaligned firms as compared to other firms, we start by plotting the average incidence of SEC investigations for misaligned and non-misaligned firms in Figure 5. Panel (a) and (b) use time-varying and time-invariant measure of firm ideology, respectively. Across both measures, we find that the incidence of SEC investigations is higher for misaligned firms as compared to other firms, on average. When we plot these averages for each year in Figure 6, we continue to find higher SEC investigation rate for misaligned firms than other firms in most years. Next, we estimate Eq. (1) for SEC investigations in Table 3. Column (1) uses misalignment calculated with our time-varying measure of firm ideology, and includes industry and year fixed effects. The coefficient on *Misalignment* suggests that the SEC is more likely to open investigations against firms politically misaligned with the SEC. We find similar result in column (2) when we additionally include control variables, and in column (3) when we estimate logit model instead of OLS model. The estimates in column (2) suggest that the SEC's investigation rate is 1 percentage point higher for the politically

misaligned firms than for the other firms. When compared to the mean SEC investigation rate of 5.8% in that sample, the estimate equates to a 17.24% higher investigation rate for the politically misaligned firms as compared to the other firms.

We find similar results in columns (4)-(6) using our time-invariant measure of firm ideology to calculate misalignment (i.e., firm ideology stays constant and misalignment only changes due to change in SEC ideology). Estimates in column (5) suggest that SEC's investigation rate is 1.3 percentage point (22.41% of the mean) higher for the politically misaligned firms as compared to the other firms.<sup>22</sup> Overall, these results provide the first evidence consistent with our *partisan regulatory actions* hypothesis – the SEC is more likely to investigate firms that are politically misaligned with the SEC.

[Correia \(2014\)](#) documents that firms with long term political contributions through PAC and lobbying are less likely to receive an AAER from the SEC. Following [Correia \(2014\)](#), all our tests control for firm's political connections as measured by corporate PAC contributions in the last five years to politicians that serve on congressional committees with SEC-oversight. The coefficient on *PAC Contri SEC-Relevant* loads negatively in columns (2) and (4), suggesting that the SEC is less likely to investigate firms that make more PAC contributions to SEC-relevant politicians. While not the focus of our paper, note that this is a new result consistent with [Correia \(2014\)](#), who examined AAERs but not SEC investigations. Following [Correia \(2014\)](#), our results are also robust to controlling for firm's total PAC contributions in the last five years, or firm's total SEC-related lobbying in the last three years (untabulated).

To provide further support to our reasoning that the CEO's individual contribution better reflects firm ideology whereas firm's PAC contributions better reflect firm's strategic goal of gaining political influence, we re-estimate column (2) and (5) after defining

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<sup>22</sup>We do not include firm fixed effects in our tests because occurrence of investigations and enforcement actions are not very common in our sample. In untabulated analysis, when we replace industry fixed effects with firm fixed effects in column (2) (column (5)), our inference is unchanged, and the estimates suggest that the investigation rate is 0.9 (1.1) percentage point higher for misaligned firms compared to other firms (t-stats = 2.070 and = 2.681, respectively).

firm ideology using the party that receives the majority of the firm's PAC contributions. We do not find any association between firm PAC contribution based misalignment with the SEC and the SEC investigation rate (untabulated), further reinforcing our choice of using CEO's individual contributions as opposed to firm's PAC contributions to measure firm ideology.

Next, we exploit the fact that our measure of firm ideology allows us not only to identify firm ideology, but also identify how strong the firm ideology is. If our results are on account of SEC's partisan regulatory actions, we expect misaligned firms with stronger political ideology to elicit more partisan actions from the SEC. We identify firms with stronger ideology in two ways. First, we identify stronger ideology firms as those whose CEO only contributes to one political party. This method identifies 26.1% of the observations as having a stronger ideology (*Stronger-Ideology Firm<sub>1</sub>*), and the rest as having a weaker ideology (*Weaker-Ideology Firm<sub>1</sub>*). Second, we identify stronger ideology firms as those whose ideology based on CEO contributions for at least six out of eight election cycles is the same during our sample period. This more stringent method identifies 5.5% of the observations as having a stronger (weaker) ideology (*Stronger-Ideology Firm<sub>2</sub>*), and the rest as having a weaker ideology (*Weaker-Ideology Firm<sub>2</sub>*).

We modify Eq. (1) by interacting *Misalignment* with *Stronger-Ideology Firm* and *Weaker-Ideology Firm*, and including the main term *Stronger-Ideology Firm*. This allows us to estimate the effect of misalignment on SEC investigations separately for stronger ideology firms and weaker ideology firms. Consistent with the SEC's partisan behavior, across all columns in Table 4, we find that the SEC is significantly more likely to investigate misaligned stronger-ideology firms than misaligned weaker-ideology firms, as compared to non-misaligned firms.<sup>23</sup> In fact, while we detect the partisan investigation effect even for the relatively weaker ideology misaligned firms, the size of the effect for stronger

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<sup>23</sup>Our inference is unchanged if we define *Stronger Ideology* firms as those whose CEOs direct more than 90% of their individual contributions to one party.

ideology firms is at least two times that of the effect for weaker ideology firms.<sup>24</sup>

## 4.2. Ideological misalignment and AAER enforcement actions

We next turn our attention to the second key SEC action we examine – AAER enforcement actions. Investigations are a necessary precursor to any enforcement, are initiated by the SEC staff privately, and can remain undisclosed by the firm absent any enforcement action (Blackburne et al., 2021). However, AAERs differ on at least two key dimensions. First, they are much more consequential for all parties involved, including the firm, investors, and employees (e.g., Feroz et al., 1991; Karpoff et al., 2008a,b; Choi and Gipper, 2024). Second, they are public, subjecting the SEC to more public scrutiny for any (perceived) partisan behavior. These two key differences suggest that our SEC investigations result may not necessarily extend to AAERs.

We examine both the extensive margin (likelihood of receiving an AAER) and the intensive margin (monetary penalty imposed in an AAER) of the enforcement outcomes. In Table 5, Panel A, we estimate Eq. (1) for the likelihood that a firm receives an AAER from the SEC. Using both time-varying and time-invariant measures of firm ideology to calculate misalignment with the SEC and both OLS and logit models, we fail to detect any difference in the probability of receiving an AAER for the politically misaligned firms as compared to other firms.

While the probability of receiving an AAER is no different between misaligned and other firms, next, in Panel B, we examine monetary enforcement penalties for firms that do receive an AAER. We separately examine four monetary penalty variables – civil penalty (*CivPen*), disgorgement (*Disg*), prejudgment interest (*PreInt*), and the total of all penalty amounts including those not included in the first three variables (*TotalPen*).<sup>25</sup>

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<sup>24</sup>It is difficult to identify a similar variation in the extent of partisanship of SEC Commissioners. One might argue that Commissioners appointed by Presidents whose party also controls the Senate might be more partisan than Commissioners appointed during other times. When defined this way, we do find some evidence (untabulated) that suggests that the higher investigation rate against misaligned firms is stronger when the SEC has a greater fraction of high partisan Commissioners among the majority party.

<sup>25</sup>Civil penalty is the fine for the misconduct; disgorgement is the remedy for gains obtained through

Using the time-varying measure of firm ideology, we do not find that penalty amounts are significantly different for firms ideologically misaligned with the SEC. However, when we use the time-invariant measure of firm ideology, we detect significantly higher disgorgement penalty and prejudgment interest penalty for misaligned firms vs. other firms. Estimates using the time-invariant firm ideology suggest that disgorgement penalty and prejudgment interest penalty for misaligned firms are, on average, 4.2% and 2.5% higher, respectively. We revisit this result in Section 4.3 when we separately estimate these effects for SEC Commissioner's with higher vs. lower career concerns.

While our sample period ends in 2014 because of availability of the investigation data, in Panel C we extend the sample period through 2020 by supplementing our AAER data available through 2021 with hand collected penalties data through 2021. Because our firm ideology data also ends in 2014, for this test we assume that the firm ideology stays constant between 2014 and 2020. Specifically, for time-varying (time-invariant) firm ideology measure, we assign the last observable firm ideology (the time-invariant firm ideology) in our sample to every year for the firm beyond 2014. We continue to find in the extended sample that for misaligned firms as compared to other firms, the likelihood of receiving an AAER is no different (Panel C1), but enforcement penalties are harsher (specifically, disgorgement penalty when using time-varying firm ideology, and disgorgement and prejudgment interest penalty when using time-invariant firm ideology, reported in Panel C2).

Overall, these results suggest that while SEC investigations appear to have a partisan bias, evidence on partisan bias in enforcement actions is more nuanced and depends on which margin one looks at – the extensive margin or the intensive margin. It appears as if the care and scrutiny that goes into bringing an AAER against a firm eliminates any partisan bias that exists in investigations against ideologically misaligned firms (i.e., the

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the misconduct; and prejudgment interest is the interest on any disgorgement amounts (17 C.F.R. §201.600(a)), typically calculated from the time of the misconduct to the month prior to when disgorgement payment is due (17 C.F.R. §201.600(b)).

extensive margin). However, if firms do receive an AAER, the partisan bias seems to survive and results in harsher penalties against firms ideologically misaligned with the SEC (i.e., the intensive margin).

### 4.3. Career concerns of SEC Commissioners

To distinguish between *psychological effect channel* and *career concerns channel* in a non-mutually exclusive way, next, we exploit the idea that while partisan ideology is likely formed in early years and remains relatively stable through lifetime (e.g., [Sears, 1975](#); [Iyengar et al., 2019](#)), career concerns are much more pronounced earlier as compared to later in life (e.g., [Gibbons and Murphy, 1992](#); [Chevalier and Ellison, 1999](#)). This suggests that while both younger and older SEC Commissioners are likely set in their ways in terms of political ideology, younger SEC Commissioners face greater career concerns than older SEC Commissioners. To the extent that regulatory actions against opposite party firms cause political damage to the opposite party, *career concerns channel* suggests that younger commissioners may have greater incentive to achieve better career outcomes by being harsher against opposite party firms to please own party politicians. Such a channel is distinct from the *psychological effect channel* that is based on a general mistrust against groups with a different ideology. As with our main hypothesis, if the SEC career bureaucrats anticipate such Commissioners' career concerns, they may skew their investigations and enforcement actions to align with the Commissioners' preferences.

Table 6, Panel A, reports the results for SEC investigations. To capture career concerns, we focus on the age of the majority party Commissioners because our focus is on partisan behavior motivated, at least in part, by career concerns (e.g., [Chevalier and Ellison, 1999](#)). We calculate the average age of the majority party Commissioners, and define *Young SEC* (*Old SEC*) as an indicator that equals one if this measure is below (above) the

sample median.<sup>26</sup> We modify Eq. (1) by interacting *Misalignment* with *Young SEC* and *Old SEC*, and including the term *Young SEC*, to estimate the effect of misalignment on SEC investigations when majority party SEC Commissioners are younger vs. older, on average. Across both measure of firm ideology and using OLS and logit models, we find that the partisan SEC investigations are driven by younger majority party Commissioners. Estimates in column (1) suggest that when majority party SEC Commissioners are younger, SEC is 1.7 percentage points more likely to investigate misaligned firms (i.e., 29.3% higher investigation rate than the sample mean investigation rate of 5.8%). However, when majority party SEC Commissioners are older, SEC does not investigate misaligned firms at a differential rate.

We find a similar pattern when we examine monetary enforcement penalties in Panel B (specifications are analogous to those in Table 5, Panel B). When using the time-varying measure of firm ideology, we find that disgorgement penalty amounts are significantly higher for misaligned firms when majority party SEC Commissioners are younger, but fail to find a similar effect when majority party SEC Commissioners are older. When we use the time-invariant measure of firm ideology, we detect, for younger majority party SEC Commissioners, significantly higher penalty amounts for misaligned firms vs. other firms across all the four penalty measures. Estimates from columns (5) to (8) suggest that when the majority party SEC Commissioners are younger, the penalty amounts for misaligned firms are, on average, 8.9%, 6.4%, 3.6%, and 9.8% higher for civil penalty, disgorgement, prejudgment interest, and total penalties, respectively. In contrast, when the majority party Commissioners are older, we do not find any evidence that penalties are harsher against misaligned firms as compared to other firms.

Overall, these results suggest that the SEC Commissioners' career incentive to gain political mileage within the own party by acting harsher against the opposite party firms explains at least part of our evidence on partisan regulatory actions hypothesis. In Sec-

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<sup>26</sup>The median age is 57 years.



tion 4.6, we explore the association between the SEC Commissioners' partisan enforcement actions and career outcomes after their tenure ends, and find evidence that indeed suggests better career outcomes for more partisan Commissioners.

#### **4.4. Firm behavior: Financial misreporting**

Having shown that firms ideologically misaligned with the SEC are more likely to get investigated by the SEC and face harsher penalties in case of enforcement, next, we explore whether misaligned firms internalize in their misreporting decisions the SEC's partisan enforcement preferences. [Becker \(1968\)](#)'s economic theory of crime suggests that a prospective criminal trades off the costs against the benefits of committing the crime. In the context of financial misreporting, evidence in [Kedia and Rajgopal \(2011\)](#) seems consistent with [Becker \(1968\)](#)'s theory, and suggests that firms take into account the SEC's enforcement preferences (e.g., geographic proximity) in their misreporting decisions. If ideological misalignment increases firms' expected likelihood of being investigated and penalties in case of enforcement, it may discourage misaligned firms from misreporting, or encourage non-misaligned firms to misreport, at least at the margin. However, multiple factors also suggest otherwise. First, after initiating misreporting, the firm's (CEO's) ideology might change with CEO turnover or changes in the larger political climate. Second, the SEC Commissioners' party composition might change, potentially changing the firm's misalignment with the SEC. Third, the five-year statute of limitation on most federal offenses (including financial misconduct) further raises the uncertainty about how long the political (mis)alignment might go on after the misconduct. This suggests that firms may not necessarily take political misalignment into account in their misreporting decision.

To examine the association between ideological misalignment with the SEC and the firm's misreporting behavior, our regression specification is the following:

$$Misreporting_{it+1} = \beta Misalignment_{it} + \gamma' X_{it} + \alpha_j + \alpha_t + \varepsilon_{it+1} \quad (2)$$

All terms in Eq. (2) are identical to those in Eq. (1), except the outcome variable,  $Misreporting_{t+1}$ , which is an indicator that equals 1 if the firm initiates financial misreporting in the year  $t+1$ . We follow prior literature and identify deliberate financial misreporting using income decreasing restatements, i.e., we retain restatements with a negative cumulative effect on net income and drop restatements with a positive effect, zero effect, or no available magnitude of the effect on net income (e.g., [Kedia and Rajgopal, 2011](#); [Leone, Li, and Liu, 2021](#)).

Table 7 shows the results using both measures of firm ideology, and OLS and logit models. We fail to detect any difference between misaligned and other firms in the probability of initiating financial misreporting ( $t$ -stats range between 0.304 to 0.460). In untabulated analysis, we find similar results if we only focus on high severity cases of misreporting, as measured by (i) the cumulative impact of restatement on earnings more than 3% of the total assets one year before the beginning of misreporting, or (ii) Big R restatements. This suggests that when firms trade off the costs and benefits of misreporting, SEC's partisan preferences do not play a big enough role to sway the firm's misreporting decision, on average, and that other factors likely play a more dominant role in the firm's misreporting decision (e.g., capital market expectations, CEO's compensation incentives, etc.).

## 4.5. Ideological misalignment and SEC's resource allocation

### 4.5.1. False positives in SEC investigations

Our evidence thus far suggests that while ideologically misaligned firms are no different from other firms in the likelihood of financial misreporting, the SEC is more likely to target ideologically misaligned firms. Given the SEC's limited resources (e.g., [Kedia](#)

and Rajgopal, 2011), this raises concerns about the SEC’s resource allocation decisions. If the SEC investigates misaligned firms at a higher rate, but such firms are no more likely to misreport, it suggests that SEC investigations of misaligned firms may have greater false positives (i.e., Type-I errors). Specifically, we examine whether conditional on an investigation, misaligned firms are less likely to receive an AAER. Note that we are *not* suggesting that absent SEC’s partisan behavior, there will be no false positives in SEC investigations. All we are saying is that the false positive rate is *relatively higher* for SEC investigations of misaligned firms as compared to that of other firms.

To examine this issue, we estimate the following specification:

$$No\ AAER_k = \beta\ Misalignment_k + \gamma'X_k + \alpha_j + \alpha_t + \varepsilon_k \quad (3)$$

where  $k$  indexes SEC investigations. We estimate this equation on a sample of 1,385 SEC investigations.<sup>27</sup> *No AAER* is an indicator that equals one if no AAER is released against the firm under investigation during the investigation period (i.e., anytime between the opening and the closing of the investigation).  $X$  is the vector of control variables as in Eq. (1), measured in the year of opening of the SEC investigation.

Table 8 reports the results. Estimates in column (3) suggest that SEC investigations of misaligned firms as compared to other firms are 4.4 percentage points more likely to not result in any AAER enforcement. When compared to the sample mean of 0.879, this equates to a 5% higher rate for misaligned firm investigations where the SEC does not bring an AAER against the firm. We find largely similar results in all other columns (except the coefficient in column (1), which is positive but does not load at conventional levels).

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<sup>27</sup>We lose some investigation observations due to missing values for controls.

#### 4.5.2. *False negatives in SEC investigations*

Working with a limited budget, if the SEC directs excessive resources towards monitoring misaligned firms, it is possible that it diverts scarce resources away from monitoring other firms (i.e., non-misaligned firms), some of whom may be engaging in financial misreporting. This could result in lower monitoring and, in turn, lower detection of non-misaligned firms' misreporting (i.e., Type II errors, or false negatives). Furthermore, such a lack of monitoring might be especially relevant for more severe cases of misreporting, which may require greater regulatory resources to uncover. We follow [Kedia and Rajgopal \(2011\)](#) to identify misreporting firms using income decreasing restatements. To examine whether the SEC is more likely to miss detecting (severe) cases of misreporting by non-misaligned firms, we estimate the following specification on a sample of 851 income decreasing restatements that end at some point during our sample period:

$$Not\ Detected_m = \beta Non - Misalignment_m + \gamma' X_m + \alpha_j + \alpha_t + \varepsilon_m \quad (4)$$

where  $m$  indexes restatement events. To capture SEC's inaction against misreporting, we define *Not Detected* as an indicator that equals one if the SEC does not open an investigation against the misreporting firm within three years after the end of misreporting. For example, if misreporting ends in the year 2005, *Not Detected* indicator equals one if the SEC does not open an investigation against the firm by the end of 2008. *Non-Misalignment* is an indicator that equals one if the firm is not ideologically misaligned with the SEC (i.e., when *Misalignment* equals zero).  $X$  is the vector of control variables as in Eq. (1), measured in the last year of misreporting.

Table 9 reports the results. Columns (1)-(4) use time-varying measure of firm ideology, and columns (5)-(8) use time-invariant measure of firm ideology. The coefficient on *Non-Misalignment* is statistically insignificant at conventional levels in columns (1)

and (2) using OLS and logit model. To further examine whether SEC fails to investigate severe cases of misreporting by non-misaligned firms, we follow prior literature and identify more severe cases of misreporting using the cumulative impact of the restatement on income (e.g., Leone et al., 2021). We define *High Misreport* (*Low Misreport*) as an indicator that equals one if the cumulative impact of the restatement on income is more (less) than 3% of the total assets one year before the start of misreporting.<sup>28</sup> We interact *Non-Misalignment* with *High Misreport* and *Low Misreport*, and include the term *High Misreport*.

In column (3), we find a positive and significant coefficient on *Non-Misalignment*  $\times$  *High Misreport* and insignificant coefficient on *Non-Misalignment*  $\times$  *Low Misreport*. This suggests that, indeed, the SEC is less likely to open investigations against non-misaligned firms for severe cases of misreporting. We find similar result using logit model in column (4). When we use time-invariant firm ideology in columns (5)–(8), we continue to find evidence of SEC’s inaction against misreporting. In column (5), the coefficient estimate of 0.090 on *Non-Misalignment* suggests that, conditional on misreporting, non-misaligned firms are 14.7% more likely to not be investigated by the SEC as compared to the mean non-investigation rate in our misreporting sample. We find similar result for severe cases of misreporting in columns (7) and (8). In untabulated analysis, our inferences are unchanged if we restrict our sample of restatements for this analysis to only Big-R restatements.

Collectively, analysis in this section points to potential resource misallocation at the SEC. While firms ideologically misaligned and non-misaligned with the SEC are no different in their propensity to initiate financial misconduct, it seems as if the SEC directs excessive resources towards investigating misaligned firms (as evidenced by lower rate of AAER conditional on investigation for misaligned firms). In turn, working with a constrained budget, it seems that the SEC directs inadequate resources towards investi-

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<sup>28</sup>The high-severity cut-off identifies the top quartile of restatements based on their cumulative impact on income.

gating misreporting by non-misaligned firms (as evidenced by lower rate of investigation conditional on misreporting for non-misaligned firms).

#### **4.6. Career outcomes of SEC Commissioners with partisan enforcement actions**

Recall that our *career concerns hypothesis* is based on the idea that SEC Commissioners may act harsher against the opposite party firms to please own party politicians who can help the Commissioners advance in their careers. Consistent with that idea, we show in Section 4.3 that our main results are driven by younger Commissioners, who likely face stronger career concerns than older Commissioners. To provide further evidence in support of that channel, we now explore a more direct link between Commissioners' partisan enforcement actions during their tenure and future career outcomes once their tenure ends. If career concerns is indeed one of the channels that explains Commissioners' partisan enforcement, we expect Commissioners with more partisan enforcement to achieve better future career outcomes.

We collect data on the career trajectory of SEC Commissioners from LinkedIn and other online sources. We focus on Commissioners who are affiliated to the majority party during their tenure, because we cannot attribute SEC's partisan actions to Commissioners from the minority party. We estimate the following equation on a sample of 13 SEC Commissioners during our sample period:<sup>29</sup>

$$New\ Roles_c = \beta\ PartisanEnforcement_c + Age_c + \varepsilon_c \quad (5)$$

where  $c$  indexes SEC Commissioners. *New Roles* is the natural logarithm of one plus the number of new roles in the public or private sector the Commissioner takes on within two years of the end of their tenure as SEC Commissioner. We also construct an al-

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<sup>29</sup>We drop one Commissioner because we cannot accurately find the employment history after the end of the tenure of that Commissioner.

ternative version of *New Roles* that counts only new leadership roles in public or private sector, where we identify leadership roles as those that involve being a chairman, president, board of director, board of trustee, founder, or CEO.<sup>30</sup> *Partisan Enforcement* for a Commissioner measures the cumulative SEC actions against misaligned firms minus the cumulative SEC actions against non-misaligned firms, scaled by the sum of the two numbers, during the Commissioner’s tenure. We construct three versions of *Partisan Enforcement* corresponding to three SEC actions: (i) *Partisan Investigations* (based on number of SEC investigations), (ii) *Partisan AAERs* (based on number of AAERs released), and (iii) *Partisan Penalty* (based on total monetary enforcement penalties).<sup>31</sup> We also employ three additional versions of *Partisan Penalty* corresponding to civil penalty (*Partisan Civil Penalty*), disgorgement (*Partisan Disgorgement*), and prejudgment interest (*Partisan Prejudgment Interest*). All our *Partisan Enforcement* measures are increasing in enforcement actions against politically misaligned firms relative to non-misaligned firms during the majority party Commissioner’s tenure. To control for the fact that some Commissioners may choose not to take on new roles after a certain age, we control for the natural logarithm of their age when their tenure ends (*Age*).

Table 10 reports the results. Estimates in Panel A, column (1), based on time-varying measure of firm ideology, suggests that Commissioners with a track record of more partisan investigations during their tenure take on more roles in the public or private sector after their tenure as a Commissioner ends. We do not detect a similar effect for *Partisan AAERs* in column (2) or *Partisan Penalty* in column (3). However, when using the time-invariant measure of firm ideology (columns (4) to (6)), we find that all three measures of partisan enforcement are positively associated with Commissioners taking on more new roles after their tenure ends. We find a similar pattern when we limit our at-

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<sup>30</sup>We classify around 74% of the new roles as leadership roles. The median Commissioner takes on four new roles (three new leadership roles) within two years of the end of their tenure.

<sup>31</sup>For example, “*Partisan Investigation*” is defined as the number of investigations during the SEC Commissioner’s tenure against misaligned firms minus that against non-misaligned firms, scaled by the sum of the two numbers. Other *Partisan Enforcement* variables are defined analogously.

tention to only leadership roles in columns (7) to (12). In terms of economic magnitude, the estimates in column (1) suggest that a one standard deviation increase in partisan investigations during a Commissioner's tenure is associated with 27% more new roles within two years of the end of their tenure.<sup>32</sup> In Panel B, we separately estimate Eq. (5) for the three categories of *Partisan Penalty*. We find that partisan civil penalty is positively associated with more new roles, and some evidence that partisan disgorgement penalty is associated with more new roles.

Overall, the exploratory analysis in this section suggests a positive association between SEC Commissioners' partisan actions and better career outcomes.<sup>33</sup> This seems consistent with the notion that SEC Commissioners' partisan behavior is motivated, at least in part, by a desire to please own party politicians to achieve better career outcomes once their tenure ends.

## 5. Conclusion

We investigate whether partisan politics play a role in SEC enforcement actions against financial misconduct. Our evidence is nuanced. We find that the SEC is more likely to launch an investigation against a firm that is politically misaligned with the agency's ideology. However, when it comes to the highly consequential decision of issuing an AAER, its likelihood is not sensitive to political misalignment, although once a firm is named in an AAER, penalties are harsher for misaligned firms.

Our findings indicate the presence of partisan politics in SEC investigative and enforcement proceedings, however, the system appears to have the ability to guard against the influence of partisanship when the stakes are sufficiently high (as in the case of issu-

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<sup>32</sup>We interpret economic magnitude by multiplying the coefficient on *Partisan Investigations* (2.283) with the standard deviation of *Partisan Investigations* (0.118).

<sup>33</sup>We recognize that more (leadership) roles may not perfectly capture better career outcomes for Commissioners. For example, we do not observe the pecuniary or non-pecuniary utility they derive from the new roles. We also do not observe other benefits they can derive without taking on new roles, such as signing lucrative book deals.



ing an AAER). Despite the apparent checks and balances in these high-stakes situations, partisanship in SEC investigations means that the agency's scarce resources are likely misallocated. Consistent with this, we find higher Type I (II) error rates in SEC investigations, i.e., more false positives (negatives), in identifying financial misconduct among misaligned (non-misaligned) firms.

We contribute to the understanding of the SEC's objective function by identifying a factor not studied in prior literature, i.e., partisan politics, in SEC enforcement actions. Our evidence bears relevance for investors that the SEC is charged to protect, companies under SEC monitoring, and taxpayers who provide funding for the agency.

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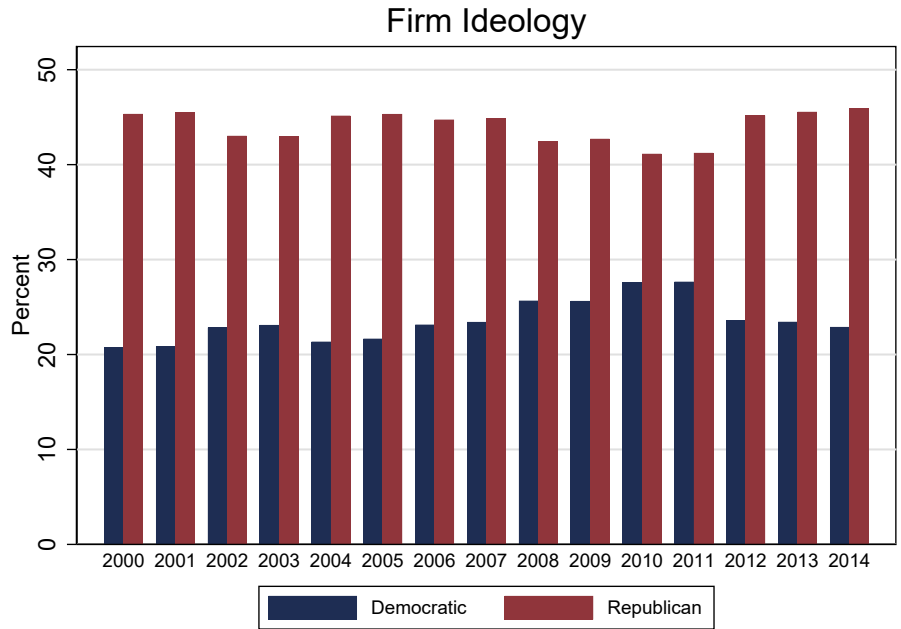
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## A. Appendix: Variable Definitions

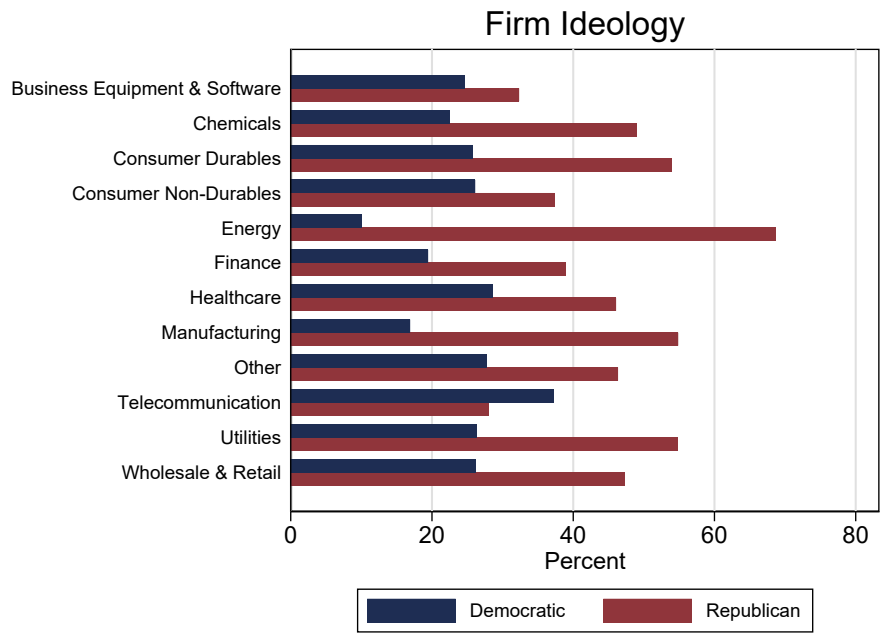
| <b>Variable</b>          | <b>Description</b>   |
|--------------------------|--|
| Misalignment             | An indicator variable that equals to one if the firm's political ideology is different from the SEC's ideology, and zero otherwise.  |
| SEC Investigation        | An indicator variable that equals to one if the SEC opens an investigation against the firm, and zero otherwise.   |
| AAER                     | An indicator variable that equals to one if the SEC issues an AAER against the firm, and zero otherwise.   |
| CivPen                   | Natural logarithm of one plus the dollar amount of civil penalty imposed in an AAER.   |
| Disg                     | Natural logarithm of one plus the dollar amount of disgorgement imposed in an AAER.  |
| PreInt                   | Natural logarithm of one plus the dollar amount of prejudgement interest imposed in an AAER.   |
| TotalPen                 | Natural logarithm of one plus the dollar amount of total penalty imposed in an AAER.   |
| Misreporting             | An indicator variable that equals to one if the firm initiates financial misreporting as identified through subsequent income decreasing restatement, and zero otherwise.  |
| Size                     | The natural logarithm of total assets.   |
| BM                       | Book value of equity scaled by market value of equity.   |
| Leverage                 | Total liabilities scaled by total assets.  |
| ROA                      | Net income scaled by total assets.   |
| Analyst Following        | Natural logarithm of one plus the number of analysts following the firm (I/B/E/S).   |
| DACC                     | Performance matched discretionary accruals (Kothari et al., 2005).   |
| Distance to SEC          | Natural logarithm of one plus the distance (km) between the firm headquarter zipcode and the nearest SEC regional office zipcode.  |
| SP500                    | An indicator variable that equals one if the firm is part of the S&P500 index, and zero otherwise.   |
| PAC Contri SEC-Relevant  | Total firm political contributions (PAC) in the last five years to politicians currently serving on congressional committees with SEC oversight (the U.S. Senate Committee on Banking, Housing, and Urban Affairs and the U.S. House of Representatives Committee on Financial Services), scaled by total assets. Multiplied by 100 when used in regressions, to ease interpretation of coefficient estimates. |
| Stock Return             | Firm's buy-and-hold stock returns during the year.   |
| Idiosyncratic Volatility | Standard deviation of the residual from a market model of the firm's daily returns estimated over the year.  |

## Appendix: Variable Definitions (Continued)

| <b>Variable</b>                     | <b>Description</b>  |
|-------------------------------------|---|
| Stronger-Ideology Firm <sub>1</sub> | An indicator variable that equals to one if the firm's CEO only contributes to one political party, and zero otherwise. Weaker-Ideology Firm <sub>1</sub> equals one when Stronger-Ideology Firm <sub>1</sub> equals zero.  |
| Stronger-Ideology Firm <sub>2</sub> | An indicator variable that equals to one for firms whose ideology based on CEO contributions for at least six out of eight election cycles is the same during our sample period, and zero otherwise. Weaker-Ideology Firm <sub>2</sub> equals one when Stronger-Ideology Firm <sub>2</sub> equals zero. |
| Young SEC                           | An indicator variable that equals to one if the average age of the majority party SEC Commissioners is below the sample median, and zero otherwise. Old SEC is an indicator that equals one if Young SEC is zero.   |



(a)



(b)

Fig. 1. Firm ideology

Notes. This figure plots distribution of firm ideology over time in Panel (a) and across sectors in Panel (b).



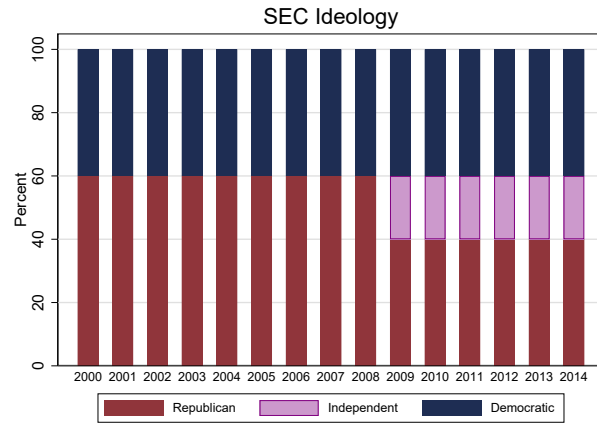


Fig. 2. SEC ideology

Notes. This figure plots the party affiliation of the SEC Commissioners over time.

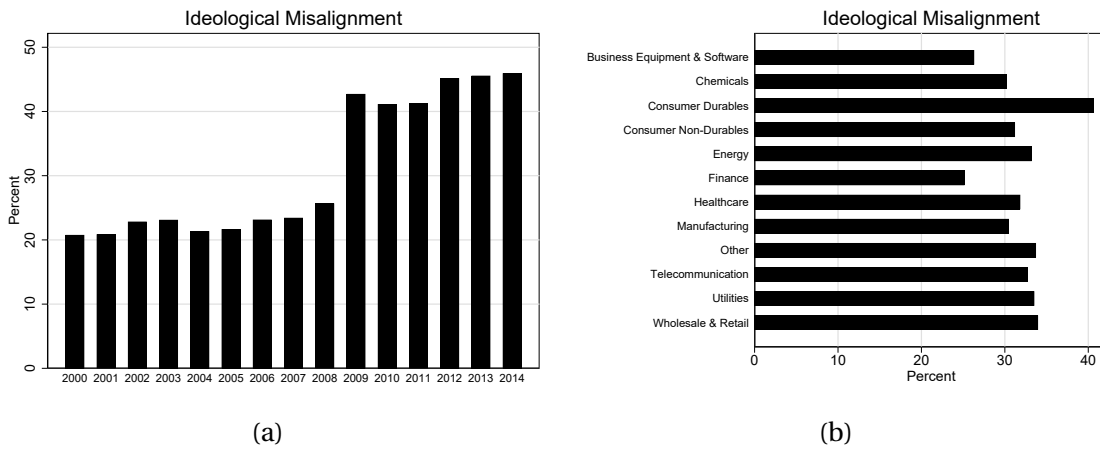
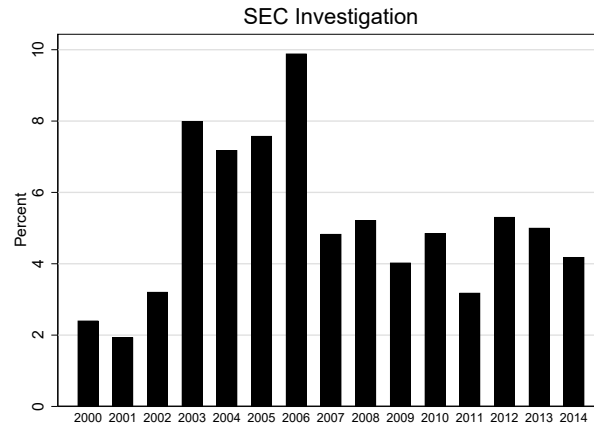
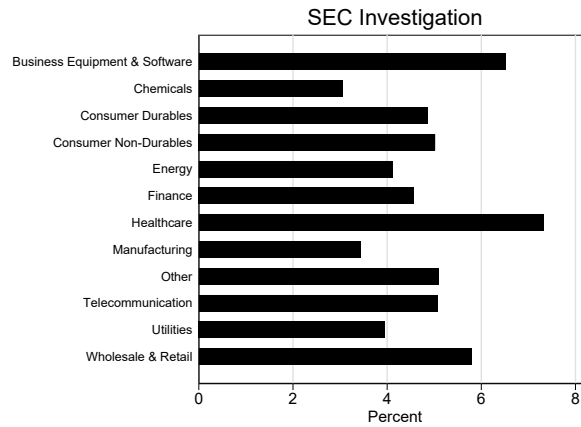


Fig. 3. Ideological misalignment

Notes. This figure plots distribution of ideological misalignment between firms and the SEC over time in Panel (a) and across sectors in Panel (b).



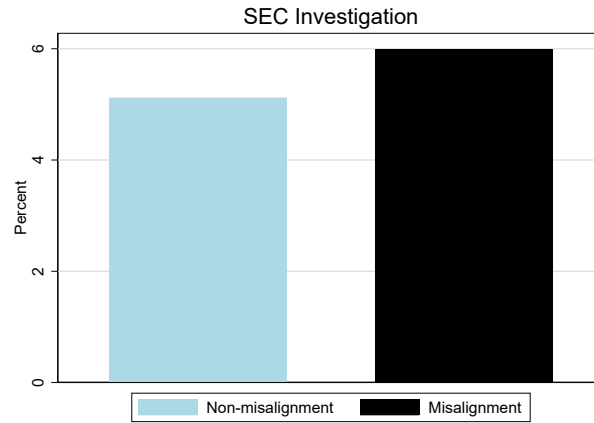
(a)



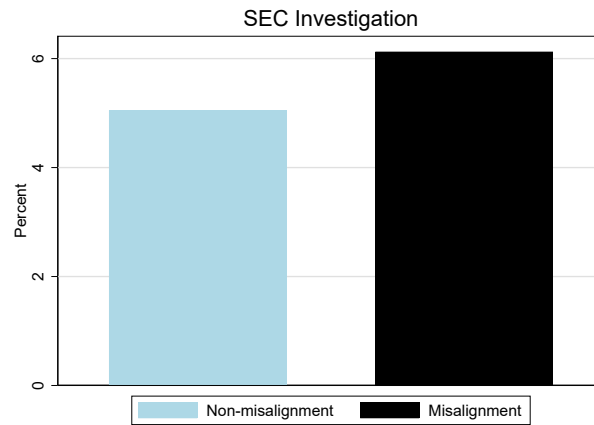
(b)

Fig. 4. SEC investigation

*Notes.* This figure plots distribution of SEC investigations over time in Panel (a) and across industries in Panel (b).



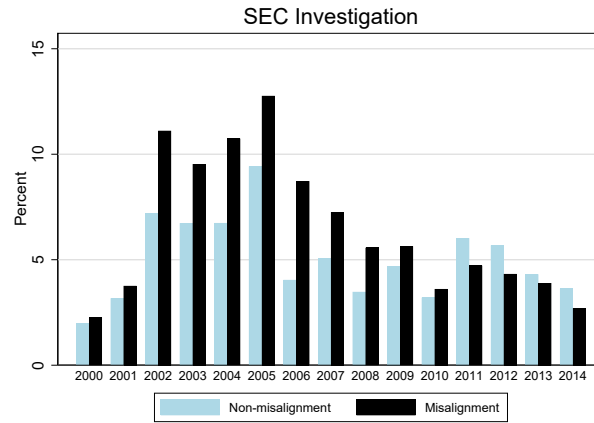
(a)



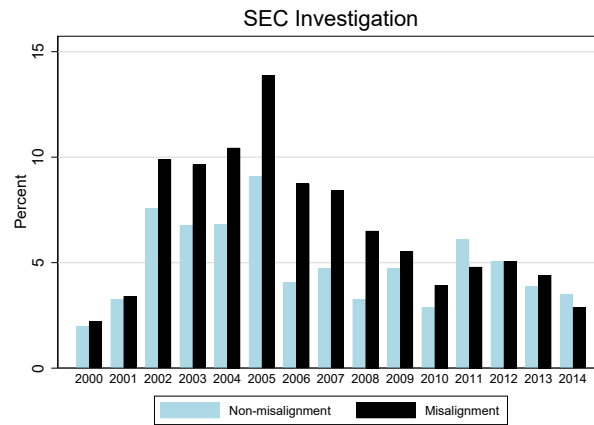
(b)

Fig. 5. Ideological misalignment and SEC investigation

*Notes.* This figure plots the average incidence of SEC investigation in our firm-year sample, for ideologically misaligned and non-misaligned firms. Panel (a) uses the time-varying measure of firm ideology and Panel (b) uses the time-invariant measure of firm ideology.



(a)



(b)

Fig. 6. Ideological misalignment and SEC investigation by year

*Notes.* This figure plots the yearly average incidence of SEC investigation in our firm-year sample, for ideologically misaligned and non-misaligned firms. Panel (a) uses the time-varying measure of firm ideology and Panel (b) uses the time-invariant measure of firm ideology.

Table 1: Descriptive statistics

## Panel A: Firm-year sample

|  | Mean   | SD    | Q1     | Median | Q3    | N      |
|--|--------|-------|--------|--------|-------|--------|
| <i>Dependent variables</i>                 |        |       |        |        |       |        |
| SEC Investigation <sub>t+1</sub>           | 0.054  | 0.226 | 0.000  | 0.000  | 0.000 | 27,227 |
| AAER <sub>t+1</sub>                        | 0.012  | 0.108 | 0.000  | 0.000  | 0.000 | 27,227 |
| CivPen <sub>t+1</sub>                      | 0.088  | 1.101 | 0.000  | 0.000  | 0.000 | 27,227 |
| Disg <sub>t+1</sub>                        | 0.055  | 0.875 | 0.000  | 0.000  | 0.000 | 27,227 |
| PreInt <sub>t+1</sub>                      | 0.032  | 0.622 | 0.000  | 0.000  | 0.000 | 27,227 |
| TotalPen <sub>t+1</sub>                    | 0.106  | 1.249 | 0.000  | 0.000  | 0.000 | 27,227 |
| Misreporting <sub>t+1</sub>                | 0.017  | 0.128 | 0.000  | 0.000  | 0.000 | 27,227 |
| <i>Key independent variables</i>           |        |       |        |        |       |        |
| Misalignment(TV)                           | 0.302  | 0.459 | 0.000  | 0.000  | 1.000 | 27,227 |
| Misalignment(TIV)                          | 0.312  | 0.463 | 0.000  | 0.000  | 1.000 | 27,227 |
| <i>Control variables</i>                   |        |       |        |        |       |        |
| Size                                       | 7.555  | 1.818 | 6.280  | 7.473  | 8.742 | 27,106 |
| BM   | 0.531  | 0.458 | 0.276  | 0.458  | 0.697 | 26,317 |
| Leverage                                   | 0.557  | 0.249 | 0.379  | 0.553  | 0.721 | 27,032 |
| ROA  | 0.033  | 0.106 | 0.010  | 0.040  | 0.079 | 27,087 |
| Analyst Following                          | 1.703  | 1.212 | 0.000  | 1.946  | 2.708 | 27,227 |
| DACC                                       | -0.017 | 0.640 | -0.101 | -0.005 | 0.084 | 25,427 |
| Distance to SEC                            | 4.461  | 1.712 | 3.399  | 4.629  | 5.930 | 26,064 |
| SP500                                      | 0.258  | 0.438 | 0.000  | 0.000  | 1.000 | 27,227 |
| PAC Contri SEC-Relevant (non-zero '000 \$) | 124    | 239   | 12     | 38     | 125   | 7,178  |
| Stock Return                               | 0.141  | 0.584 | -0.172 | 0.070  | 0.319 | 26,011 |
| Idiosyncratic Volatility                   | 0.024  | 0.014 | 0.014  | 0.020  | 0.029 | 25,850 |
| <i>Cross-sectional variables</i>           |        |       |        |        |       |        |
| Stronger-Ideology Firm <sub>1</sub>        | 0.261  | 0.439 | 0.000  | 0.000  | 1.000 | 27,227 |
| Stronger-Ideology Firm <sub>2</sub>        | 0.055  | 0.228 | 0.000  | 0.000  | 0.000 | 27,227 |
| Young SEC                                  | 0.556  | 0.497 | 0.000  | 1.000  | 1.000 | 27,227 |

## Panel B: Monetary enforcement penalties (\$ thousands)

|                       | Mean   | SD     | Q1  | Median | Q3     | N   |
|-----------------------|--------|--------|-----|--------|--------|-----|
| Civil Penalty         | 15,432 | 49,489 | 90  | 300    | 6,600  | 177 |
| Disgorgement          | 9,335  | 29,659 | 87  | 455    | 4,000  | 117 |
| Prejudgement Interest | 1,053  | 2,952  | 31  | 84     | 620    | 74  |
| Total Penalty         | 30,247 | 96,745 | 210 | 1,477  | 10,595 | 202 |

*Notes.* Unit of observation is firm-year. For descriptive purposes, PAC contribution to politicians serving on SEC-relevant congressional committees (*PAC Contri SEC-relevant*) is reported for non-zero contribution amounts in thousands of dollars (Panel A). Panel B reports the monetary enforcement penalties for non-zero penalty amounts in thousands of dollars. All variables are defined in Appendix A.

Table 2: Correlation matrix

|                                     | [1]   | [2]   | [3]   | [4]   | [5]   | [6]   | [7]   | [8]   | [9]   | [10]  | [11]  | [12]  | [13]  | [14]  | [15]  | [16]  | [17]  | [18]  | [19] | [20] |
|-------------------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|------|------|
| [1]SEC Investigation <sub>t+1</sub> | 1.00  |       |       |       |       |       |       |       |       |       |       |       |       |       |       |       |       |       |      |      |
| [2]AAER <sub>t+1</sub>              | 0.03  | 1.00  |       |       |       |       |       |       |       |       |       |       |       |       |       |       |       |       |      |      |
| [3]CivPen <sub>t+1</sub>            | 0.03  | 0.73  | 1.00  |       |       |       |       |       |       |       |       |       |       |       |       |       |       |       |      |      |
| [4]Disg <sub>t+1</sub>              | 0.02  | 0.59  | 0.64  | 1.00  |       |       |       |       |       |       |       |       |       |       |       |       |       |       |      |      |
| [5]PreInt <sub>t+1</sub>            | 0.02  | 0.48  | 0.54  | 0.78  | 1.00  |       |       |       |       |       |       |       |       |       |       |       |       |       |      |      |
| [6]TotalPen <sub>t+1</sub>          | 0.03  | 0.78  | 0.93  | 0.77  | 0.61  | 1.00  |       |       |       |       |       |       |       |       |       |       |       |       |      |      |
| [7]Misreporting <sub>t+1</sub>      | 0.01  | -0.01 | -0.00 | -0.00 | -0.00 | -0.00 | 1.00  |       |       |       |       |       |       |       |       |       |       |       |      |      |
| [8]Misalignment(TV)                 | 0.02  | -0.00 | 0.00  | 0.01  | 0.01  | 0.00  | -0.01 | 1.00  |       |       |       |       |       |       |       |       |       |       |      |      |
| [9]Misalignment(TIV)                | 0.02  | 0.00  | 0.01  | 0.02  | 0.02  | 0.01  | -0.01 | 0.79  | 1.00  |       |       |       |       |       |       |       |       |       |      |      |
| [10]Size                            | 0.09  | 0.06  | 0.05  | 0.04  | 0.03  | 0.06  | -0.02 | 0.08  | 0.10  | 1.00  |       |       |       |       |       |       |       |       |      |      |
| [11]BM                              | -0.02 | -0.00 | 0.00  | -0.00 | -0.01 | 0.00  | 0.02  | -0.01 | 0.00  | 0.03  | 1.00  |       |       |       |       |       |       |       |      |      |
| [12]Leverage                        | 0.01  | 0.04  | 0.04  | 0.02  | 0.01  | 0.04  | -0.00 | 0.03  | 0.03  | 0.48  | -0.09 | 1.00  |       |       |       |       |       |       |      |      |
| [13]ROA                             | 0.01  | -0.01 | -0.02 | -0.00 | 0.01  | -0.01 | -0.01 | 0.02  | 0.02  | 0.09  | -0.22 | -0.20 | 1.00  |       |       |       |       |       |      |      |
| [14]Analyst Following               | 0.05  | 0.00  | 0.00  | 0.00  | 0.00  | 0.00  | -0.03 | 0.04  | 0.06  | 0.30  | -0.13 | -0.03 | 0.17  | 1.00  |       |       |       |       |      |      |
| [15]DACC                            | 0.01  | -0.00 | -0.00 | 0.00  | 0.01  | 0.00  | 0.00  | -0.01 | -0.01 | -0.00 | 0.01  | -0.00 | -0.00 | -0.01 | 1.00  |       |       |       |      |      |
| [16]Distance to SEC                 | -0.02 | -0.01 | -0.01 | -0.01 | -0.00 | -0.00 | 0.01  | -0.01 | -0.00 | -0.01 | 0.02  | 0.04  | 0.04  | -0.01 | 0.01  | 1.00  |       |       |      |      |
| [17]SP500                           | 0.09  | 0.06  | 0.06  | 0.05  | 0.04  | 0.06  | -0.02 | 0.06  | 0.06  | 0.64  | -0.11 | 0.17  | 0.10  | 0.30  | 0.00  | -0.05 | 1.00  |       |      |      |
| [18]PAC Contri SEC-Relevant         | -0.00 | -0.01 | -0.00 | -0.00 | -0.00 | -0.00 | -0.00 | 0.01  | 0.01  | 0.01  | -0.02 | 0.00  | 0.03  | 0.02  | -0.00 | 0.01  | 0.02  | 1.00  |      |      |
| [19]Stock Return                    | -0.01 | 0.00  | -0.00 | 0.01  | 0.00  | -0.00 | 0.01  | 0.03  | 0.03  | -0.09 | -0.19 | -0.02 | 0.12  | -0.04 | -0.02 | 0.00  | -0.06 | 0.00  | 1.00 |      |
| [20]Idiosyncratic Volatility        | 0.00  | 0.01  | 0.01  | 0.01  | -0.00 | 0.01  | 0.04  | -0.06 | -0.07 | -0.45 | 0.16  | -0.08 | -0.40 | -0.25 | -0.00 | -0.02 | -0.26 | -0.03 | 0.02 | 1.00 |

*Notes.* This table reports correlation coefficients (Pearson) between key dependent and independent variables used in our analysis. *Misalignment (TV)* uses time-varying measure of firm ideology, and *Misalignment (TIV)* uses time-invariant measure of firm ideology. All variables are defined in Appendix A.

Table 3: Ideological misalignment and SEC investigations

| Dep. var. =<br>Firm ideology = | SEC Investigation <sub>t+1</sub> |                       |                       |                     |                       |                       |
|--------------------------------|----------------------------------|-----------------------|-----------------------|---------------------|-----------------------|-----------------------|
|                                | Time-varying                     |                       |                       | Time-invariant      |                       |                       |
|                                | (1)                              | (2)                   | (3)                   | (4)                 | (5)                   | (6)                   |
| Misalignment                   | 0.011***<br>(3.248)              | 0.010***<br>(2.800)   | 0.177***<br>(2.735)   | 0.014***<br>(4.078) | 0.013***<br>(3.540)   | 0.231***<br>(3.658)   |
| Size                           |                                  | 0.021***<br>(9.715)   | 0.356***<br>(10.395)  |                     | 0.021***<br>(9.653)   | 0.353***<br>(10.325)  |
| BM                             |                                  | -0.006<br>(-1.443)    | -0.102<br>(-1.429)    |                     | -0.006<br>(-1.447)    | -0.102<br>(-1.424)    |
| Leverage                       |                                  | -0.031***<br>(-2.793) | -0.555***<br>(-2.657) |                     | -0.031***<br>(-2.769) | -0.547***<br>(-2.617) |
| ROA                            |                                  | 0.044**<br>(2.224)    | 0.946**<br>(2.348)    |                     | 0.044**<br>(2.230)    | 0.945**<br>(2.345)    |
| Analyst Following              |                                  | 0.003*<br>(1.728)     | 0.066**<br>(2.281)    |                     | 0.003*<br>(1.707)     | 0.066**<br>(2.268)    |
| DACC                           |                                  | 0.003<br>(1.066)      | 0.045<br>(0.956)      |                     | 0.003<br>(1.080)      | 0.046<br>(0.969)      |
| Distance to SEC                |                                  | -0.001<br>(-1.240)    | -0.023<br>(-1.159)    |                     | -0.001<br>(-1.274)    | -0.022<br>(-1.147)    |
| SP500                          |                                  | 0.012**<br>(2.093)    | 0.174*<br>(1.863)     |                     | 0.012**<br>(2.155)    | 0.180*<br>(1.930)     |
| PAC Contri SEC-Relevant        |                                  | -0.685**<br>(-2.014)  | -21.442<br>(-1.232)   |                     | -0.698**<br>(-2.022)  | -22.540<br>(-1.272)   |
| Stock Return                   |                                  | -0.005<br>(-1.604)    | -0.096*<br>(-1.686)   |                     | -0.005<br>(-1.590)    | -0.096*<br>(-1.690)   |
| Idiosyncratic Volatility       |                                  | 1.934***<br>(10.412)  | 34.475***<br>(12.276) |                     | 1.929***<br>(10.383)  | 34.364***<br>(12.238) |
| Mean dep. var                  | 0.054                            | 0.058                 |                       | 0.054               | 0.058                 |                       |
| Year FE                        | Yes                              | Yes                   | Yes                   | Yes                 | Yes                   | Yes                   |
| Industry FE                    | Yes                              | Yes                   | Yes                   | Yes                 | Yes                   | Yes                   |
| Model                          | OLS                              | OLS                   | Logit                 | OLS                 | OLS                   | Logit                 |
| Obs.                           | 27,227                           | 23,176                | 23,085                | 27,227              | 23,176                | 23,085                |
| Adj.(Pseudo) R <sup>2</sup>    | 0.013                            | 0.032                 | 0.078                 | 0.013               | 0.033                 | 0.078                 |

*Notes.* This table examines whether the SEC is more likely to investigate firms misaligned with the SEC's political ideology. Unit of observation is firm-year. *Misalignment* is an indicator for firms whose political ideology does not match the (majority) political ideology of the SEC. Firm's political ideology is Republican (Democratic) if the firm's CEO contributes more to the political campaigns of the Republican (Democratic) party. SEC's political ideology is Republican (Democratic) if the party affiliation of majority of the SEC commissioners is Republican (Democratic). Independent commissioners are assigned the party affiliation of the appointing president. *SEC Investigation<sub>t+1</sub>* is an indicator that equals one if the SEC opens an investigation against the firm next year. *t* (*z*)-stats in parentheses for OLS (logit) models are based on standard errors clustered by firm. \*\*\*, \*\*, and \* indicate statistical significance (two-sided) at the 0.01, 0.05, and 0.10 levels, respectively. All variables are defined in Appendix A.

Table 4: Stronger firm ideology, ideological misalignment, and SEC investigations

| Dep. var. =<br>Firm ideology =                     | SEC Investigation <sub>t+1</sub> |                    |                    |                    |                     |                     |                     |                     |
|--|----------------------------------|--------------------|--------------------|--------------------|---------------------|---------------------|---------------------|---------------------|
|  | Time-varying                     |                    |                    |                    | Time-invariant      |                     |                     |                     |
|  | (1)                              | (2)                | (3)                | (4)                | (5)                 | (6)                 | (7)                 | (8)                 |
| Misalignment × Stronger-Ideology Firm <sub>1</sub> | 0.017***<br>(2.654)              | 0.284**<br>(2.418) |                    |                    | 0.020***<br>(3.216) | 0.361***<br>(3.177) |                     |                     |
| Misalignment × Weaker-Ideology Firm <sub>1</sub>   | 0.008*<br>(1.799)                | 0.137*<br>(1.817)  |                    |                    | 0.010**<br>(2.379)  | 0.182**<br>(2.462)  |                     |                     |
| Misalignment × Stronger-Ideology Firm <sub>2</sub> |                                  |                    | 0.030**<br>(2.366) | 0.702**<br>(2.333) |                     |                     | 0.035***<br>(2.721) | 0.825***<br>(2.729) |
| Misalignment × Weaker-Ideology Firm <sub>2</sub>   |                                  |                    | 0.010**<br>(2.566) | 0.162**<br>(2.448) |                     |                     | 0.012***<br>(3.260) | 0.212***<br>(3.319) |
| P-value of coef. diff.                             | 0.104                            | 0.141              | 0.060              | 0.040              | 0.081               | 0.088               | 0.042               | 0.023               |
| Controls   | Yes                              | Yes                | Yes                | Yes                | Yes                 | Yes                 | Yes                 | Yes                 |
| Year FE  | Yes                              | Yes                | Yes                | Yes                | Yes                 | Yes                 | Yes                 | Yes                 |
| Industry FE  | Yes                              | Yes                | Yes                | Yes                | Yes                 | Yes                 | Yes                 | Yes                 |
| Model  | OLS                              | Logit              | OLS                | Logit              | OLS                 | Logit               | OLS                 | Logit               |
| Obs.   | 23,176                           | 23,085             | 23,176             | 23,085             | 23,176              | 23,085              | 23,176              | 23,085              |
| Adj.(Pseudo) R <sup>2</sup>                        | 0.032                            | 0.078              | 0.033              | 0.080              | 0.033               | 0.079               | 0.033               | 0.081               |

*Notes.* This table examines whether the relation between ideological misalignment and future SEC investigation is stronger for firms with stronger ideology. Unit of observation is firm-year. *Stronger-Ideology Firm<sub>1</sub>* is an indicator for firms whose CEO only contributes to one political party. *Weaker-Ideology Firm<sub>1</sub>* is an indicator for when *Stronger-Ideology Firm<sub>1</sub>* is zero. *Stronger-Ideology Firm<sub>2</sub>* is an indicator for firms whose party affiliation (based on CEO political contributions for at least six election cycles) stays the same during our sample period. *Weaker-Ideology Firm<sub>2</sub>* is an indicator for when *Stronger-Ideology Firm<sub>2</sub>* is zero. *Misalignment* is an indicator for firms whose CEO's political ideology does not match the (majority) political ideology of the SEC. *SEC Investigation<sub>t+1</sub>* is an indicator that equals one if the SEC opens an investigation against the firm next year. *t* (*z*)-stats in parentheses for OLS (logit) models are based on standard errors clustered by firm. p-value for test of difference in coefficients is one-tailed. \*\*\*, \*\*, and \* indicate statistical significance (two-sided) at the 0.01, 0.05, and 0.10 levels, respectively. All variables are defined in Appendix A.



Table 5: Ideological misalignment and SEC enforcement actions

Panel A: Likelihood of receiving an AAER

| Dep. var. =<br>Firm ideology = | AAER <sub>t+1</sub> |           |                |           |
|--------------------------------|---------------------|-----------|----------------|-----------|
|                                | Time-varying        |           | Time-invariant |           |
|                                | (1)                 | (2)       | (3)            | (4)       |
| Misalignment                   | -0.001              | -0.082    | 0.001          | 0.128     |
|                                | (-0.391)            | (-0.465)  | (0.633)        | (0.742)   |
| Size                           | 0.005***            | 0.333***  | 0.005***       | 0.329***  |
|                                | (3.759)             | (4.281)   | (3.741)        | (4.243)   |
| BM                             | 0.002               | 0.191     | 0.002          | 0.192     |
|                                | (0.653)             | (1.467)   | (0.674)        | (1.467)   |
| Leverage                       | 0.013**             | 1.276***  | 0.013**        | 1.295***  |
|                                | (2.312)             | (3.027)   | (2.332)        | (3.064)   |
| ROA                            | 0.003               | 0.172     | 0.003          | 0.189     |
|                                | (0.306)             | (0.264)   | (0.304)        | (0.289)   |
| Analyst Following              | -0.001              | -0.016    | -0.001         | -0.016    |
|                                | (-0.643)            | (-0.211)  | (-0.636)       | (-0.215)  |
| DACC                           | -0.000              | -0.014    | -0.000         | -0.014    |
|                                | (-0.063)            | (-0.147)  | (-0.050)       | (-0.144)  |
| Distance to SEC                | 0.000               | 0.039     | 0.000          | 0.043     |
|                                | (0.545)             | (0.829)   | (0.558)        | (0.906)   |
| SP500                          | 0.007*              | 0.464*    | 0.007*         | 0.463*    |
|                                | (1.957)             | (1.937)   | (1.953)        | (1.934)   |
| PAC Contri SEC-Relevant        | -0.211              | -169.506  | -0.214         | -171.746  |
|                                | (-1.572)            | (-1.551)  | (-1.557)       | (-1.570)  |
| Stock Return                   | 0.002               | 0.165*    | 0.002          | 0.166*    |
|                                | (1.338)             | (1.752)   | (1.341)        | (1.759)   |
| Idiosyncratic Volatility       | 0.404***            | 25.866*** | 0.401***       | 25.625*** |
|                                | (3.538)             | (4.545)   | (3.519)        | (4.502)   |
| Mean dep. var.                 | 0.012               |           | 0.012          |           |
| Year FE                        | Yes                 | Yes       | Yes            | Yes       |
| Industry FE                    | Yes                 | Yes       | Yes            | Yes       |
| Model                          | OLS                 | Logit     | OLS            | Logit     |
| Obs.                           | 23,176              | 20,733    | 23,176         | 20,733    |
| Adj.(Pseudo) R <sup>2</sup>    | 0.0128              | 0.104     | 0.0128         | 0.104     |

*Notes.* This table examines the relation between ideological misalignment and the likelihood of receiving an AAER and the size of the monetary enforcement penalty. Unit of observation is firm-year.  $AAER_{t+1}$  is an indicator that equals one if the SEC releases an AAER against the firm next year (Panel A).  $Civ Pen_{t+1}$ ,  $Disg_{t+1}$ ,  $PreInt_{t+1}$ ,  $TotalPen_{t+1}$  are natural logarithms of one plus dollar amounts of civil penalty, disgorgement, prejudgement interest, and total penalty, respectively, as per an AAER released next year (Panel B). Panels C1 and C2 replicate Panels A and B, respectively, after extending sample period through 2020.  $t$  ( $z$ )-stats in parentheses for OLS (logit) models are based on standard errors clustered by firm. \*\*\*, \*\*, and \* indicate statistical significance (two-sided) at the 0.01, 0.05, and 0.10 levels, respectively. All variables are defined in Appendix A.

Table 5: Ideological misalignment and SEC enforcement actions (Continued)

Panel B: Monetary enforcement penalty

| Firm ideology =          | Time-varying          |                     |                       |                         | Time-invariant        |                     |                       |                         |
|--------------------------|-----------------------|---------------------|-----------------------|-------------------------|-----------------------|---------------------|-----------------------|-------------------------|
|                          | (1)                   | (2)                 | (3)                   | (4)                     | (5)                   | (6)                 | (7)                   | (8)                     |
| Dep. var. =              | CivPen <sub>t+1</sub> | Disg <sub>t+1</sub> | PreInt <sub>t+1</sub> | TotalPen <sub>t+1</sub> | CivPen <sub>t+1</sub> | Disg <sub>t+1</sub> | PreInt <sub>t+1</sub> | TotalPen <sub>t+1</sub> |
| Misalignment             | -0.000                | 0.027               | 0.012                 | 0.000                   | 0.033                 | 0.042**             | 0.025**               | 0.039                   |
|                          | (-0.014)              | (1.558)             | (1.023)               | (0.002)                 | (1.488)               | (2.361)             | (2.036)               | (1.555)                 |
| Size                     | 0.030***              | 0.022*              | 0.009                 | 0.042***                | 0.029***              | 0.022*              | 0.008                 | 0.041***                |
|                          | (2.683)               | (1.830)             | (1.530)               | (2.868)                 | (2.629)               | (1.799)             | (1.466)               | (2.829)                 |
| BM                       | 0.031                 | 0.003               | 0.000                 | 0.020                   | 0.032                 | 0.004               | 0.000                 | 0.021                   |
|                          | (1.270)               | (0.252)             | (0.011)               | (0.773)                 | (1.297)               | (0.261)             | (0.032)               | (0.805)                 |
| leverage                 | 0.157***              | 0.069               | 0.038                 | 0.159**                 | 0.159***              | 0.070               | 0.038                 | 0.161**                 |
|                          | (2.770)               | (1.481)             | (1.333)               | (2.540)                 | (2.800)               | (1.508)             | (1.362)               | (2.574)                 |
| ROA                      | 0.013                 | 0.039               | 0.072**               | 0.041                   | 0.013                 | 0.039               | 0.073**               | 0.040                   |
|                          | (0.160)               | (0.566)             | (1.995)               | (0.441)                 | (0.158)               | (0.568)             | (1.995)               | (0.439)                 |
| Analyst Following        | -0.007                | -0.009              | -0.007                | -0.010                  | -0.007                | -0.009              | -0.007                | -0.010                  |
|                          | (-0.574)              | (-0.920)            | (-1.107)              | (-0.697)                | (-0.567)              | (-0.930)            | (-1.110)              | (-0.691)                |
| DACC                     | 0.000                 | 0.005               | 0.012                 | 0.011                   | 0.001                 | 0.005               | 0.012                 | 0.011                   |
|                          | (0.034)               | (0.540)             | (1.482)               | (0.823)                 | (0.055)               | (0.555)             | (1.495)               | (0.845)                 |
| Distance to SEC          | 0.000                 | -0.001              | 0.000                 | 0.001                   | 0.000                 | -0.001              | 0.000                 | 0.001                   |
|                          | (0.004)               | (-0.198)            | (0.083)               | (0.222)                 | (0.018)               | (-0.213)            | (0.076)               | (0.236)                 |
| SP500                    | 0.089***              | 0.058**             | 0.044***              | 0.095***                | 0.089***              | 0.059**             | 0.044***              | 0.096***                |
|                          | (2.984)               | (2.419)             | (2.702)               | (2.716)                 | (2.994)               | (2.454)             | (2.732)               | (2.723)                 |
| PAC Contri SEC-Relevant  | -1.451                | -1.505              | -0.759                | -1.983                  | -1.498                | -1.550              | -0.788                | -2.039                  |
|                          | (-1.221)              | (-1.445)            | (-1.271)              | (-1.327)                | (-1.205)              | (-1.436)            | (-1.268)              | (-1.307)                |
| Stock Return             | 0.013                 | 0.024               | 0.008                 | 0.018                   | 0.013                 | 0.024               | 0.008                 | 0.018                   |
|                          | (0.775)               | (1.585)             | (0.781)               | (1.000)                 | (0.782)               | (1.594)             | (0.789)               | (1.006)                 |
| Idiosyncratic Volatility | 3.044***              | 1.606               | 0.600                 | 3.915***                | 3.001***              | 1.582               | 0.581                 | 3.865***                |
|                          | (2.659)               | (1.492)             | (1.363)               | (2.712)                 | (2.632)               | (1.477)             | (1.316)               | (2.690)                 |
| Year FE                  | Yes                   | Yes                 | Yes                   | Yes                     | Yes                   | Yes                 | Yes                   | Yes                     |
| Industry FE              | Yes                   | Yes                 | Yes                   | Yes                     | Yes                   | Yes                 | Yes                   | Yes                     |
| Obs.                     | 23,176                | 23,176              | 23,176                | 23,176                  | 23,176                | 23,176              | 23,176                | 23,176                  |
| Adj. R <sup>2</sup>      | 0.009                 | 0.006               | 0.003                 | 0.010                   | 0.009                 | 0.006               | 0.003                 | 0.010                   |

Table 5: Ideological misalignment and SEC enforcement actions (Continued)

Panel C1: Sample extended through 2020 - Likelihood of receiving an AAER

| Dep. var. =<br>Firm ideology = | AAER <sub>t+1</sub> |                  |                  |                  |
|--------------------------------|---------------------|------------------|------------------|------------------|
|                                | Time-varying        |                  | Time-invariant   |                  |
|                                | (1)                 | (2)              | (3)              | (4)              |
| Misalignment                   | 0.000<br>(0.117)    | 0.006<br>(0.041) | 0.001<br>(0.634) | 0.109<br>(0.691) |
| Controls                       | Yes                 | Yes              | Yes              | Yes              |
| Year FE                        | Yes                 | Yes              | Yes              | Yes              |
| Industry FE                    | Yes                 | Yes              | Yes              | Yes              |
| Model                          | OLS                 | Logit            | OLS              | Logit            |
| Obs.                           | 29,868              | 27,203           | 29,868           | 27,203           |
| Adj.(Pseudo) R <sup>2</sup>    | 0.011               | 0.094            | 0.011            | 0.094            |

Panel C2: Sample extended through 2020 - Monetary enforcement penalty

| Firm ideology =     | Time-varying          |                     |                       |                         | Time-invariant        |                     |                       |                         |
|---------------------|-----------------------|---------------------|-----------------------|-------------------------|-----------------------|---------------------|-----------------------|-------------------------|
|                     | (1)                   | (2)                 | (3)                   | (4)                     | (5)                   | (6)                 | (7)                   | (8)                     |
| Dep. var. =         | CivPen <sub>t+1</sub> | Disg <sub>t+1</sub> | PreInt <sub>t+1</sub> | TotalPen <sub>t+1</sub> | CivPen <sub>t+1</sub> | Disg <sub>t+1</sub> | PreInt <sub>t+1</sub> | TotalPen <sub>t+1</sub> |
| Misalignment        | 0.008<br>(0.453)      | 0.028*<br>(1.809)   | 0.012<br>(1.120)      | 0.009<br>(0.420)        | 0.027<br>(1.374)      | 0.035**<br>(2.274)  | 0.019*<br>(1.735)     | 0.029<br>(1.330)        |
| Controls            | Yes                   | Yes                 | Yes                   | Yes                     | Yes                   | Yes                 | Yes                   | Yes                     |
| Year FE             | Yes                   | Yes                 | Yes                   | Yes                     | Yes                   | Yes                 | Yes                   | Yes                     |
| Industry FE         | Yes                   | Yes                 | Yes                   | Yes                     | Yes                   | Yes                 | Yes                   | Yes                     |
| Obs.                | 29,868                | 29,868              | 29,868                | 29,868                  | 29,868                | 29,868              | 29,868                | 29,868                  |
| Adj. R <sup>2</sup> | 0.007                 | 0.005               | 0.002                 | 0.008                   | 0.007                 | 0.005               | 0.002                 | 0.008                   |

Table 6: Career concerns of SEC commissioners

Panel A: SEC investigation

| Dep. var. =<br>Firm ideology = | SEC Investigation <sub>t+1</sub> |                     |                     |                     |
|--------------------------------|----------------------------------|---------------------|---------------------|---------------------|
|                                | Time-varying                     |                     | Time-invariant      |                     |
|                                | (1)                              | (2)                 | (3)                 | (4)                 |
| Misalignment × Young SEC       | 0.017***<br>(3.137)              | 0.279***<br>(3.172) | 0.018***<br>(3.287) | 0.307***<br>(3.513) |
| Misalignment × Old SEC         | 0.003<br>(0.671)                 | 0.056<br>(0.601)    | 0.007<br>(1.522)    | 0.141<br>(1.516)    |
| P-value of coef. diff.         | 0.031                            | 0.042               | 0.078               | 0.100               |
| Controls                       | Yes                              | Yes                 | Yes                 | Yes                 |
| Year FE                        | Yes                              | Yes                 | Yes                 | Yes                 |
| Industry FE                    | Yes                              | Yes                 | Yes                 | Yes                 |
| Model                          | OLS                              | Logit               | OLS                 | Logit               |
| Obs.                           | 23,176                           | 23,085              | 23,176              | 23,085              |
| Adj.(Pseudo) R <sup>2</sup>    | 0.032                            | 0.078               | 0.033               | 0.079               |

*Notes.* This table explores the career concerns channel of our partisan regulatory actions hypothesis. Unit of observation is firm-year. *Young (Old) SEC* is an indicator that equals 1 if the average age of the majority party Commissioners is below (above) the sample median, and zero otherwise. *Misalignment* is an indicator for firms whose CEO's political ideology does not match the (majority) political ideology of the SEC. Panel A examines SEC investigations. *SEC Investigation<sub>t+1</sub>* is an indicator that equals one if the SEC opens an investigation against the firm in the year *t+1*. Panel B examines monetary enforcement penalty. *Civ Pen<sub>t+1</sub>*, *Disg<sub>t+1</sub>*, *PreInt<sub>t+1</sub>*, *TotalPen<sub>t+1</sub>* are natural logarithms of one plus dollar amounts of civil penalty, disgorgement, prejudgement interest, and total penalty, respectively, as per an AAER released in the year *t+1*. *t(z)*-stats in parentheses for OLS (logit) models are based on standard errors clustered by firm. p-value for test of difference in coefficients is one-tailed. \*\*\*, \*\*, and \* indicate statistical significance (two-sided) at the 0.01, 0.05, and 0.10 levels, respectively. All variables are defined in Appendix A.

Table 6: Career concerns of SEC Commissioners (Continued)

Panel B: Monetary enforcement penalty

| Firm ideology =          | Time-varying          |                     |                       |                         | Time-invariant        |                     |                       |                         |
|--------------------------|-----------------------|---------------------|-----------------------|-------------------------|-----------------------|---------------------|-----------------------|-------------------------|
|                          | (1)                   | (2)                 | (3)                   | (4)                     | (5)                   | (6)                 | (7)                   | (8)                     |
| Dep. var. =              | CivPen <sub>t+1</sub> | Disg <sub>t+1</sub> | PreInt <sub>t+1</sub> | TotalPen <sub>t+1</sub> | CivPen <sub>t+1</sub> | Disg <sub>t+1</sub> | PreInt <sub>t+1</sub> | TotalPen <sub>t+1</sub> |
| Misalignment × Young SEC | 0.024                 | 0.042*              | 0.024                 | 0.030                   | 0.089***              | 0.064**             | 0.036*                | 0.098***                |
|                          | (0.824)               | (1.690)             | (1.251)               | (0.880)                 | (2.618)               | (2.449)             | (1.790)               | (2.593)                 |
| Misalignment × Old SEC   | -0.026                | 0.011               | 0.000                 | -0.031                  | -0.024                | 0.019               | 0.015                 | -0.021                  |
|                          | (-1.103)              | (0.574)             | (0.036)               | (-1.211)                | (-1.058)              | (1.023)             | (1.127)               | (-0.836)                |
| P-value of coef. diff.   | 0.064                 | 0.139               | 0.134                 | 0.053                   | 0.001                 | 0.062               | 0.179                 | 0.002                   |
| Controls                 | Yes                   | Yes                 | Yes                   | Yes                     | Yes                   | Yes                 | Yes                   | Yes                     |
| Year FE                  | Yes                   | Yes                 | Yes                   | Yes                     | Yes                   | Yes                 | Yes                   | Yes                     |
| Industry FE              | Yes                   | Yes                 | Yes                   | Yes                     | Yes                   | Yes                 | Yes                   | Yes                     |
| Obs.                     | 23,176                | 23,176              | 23,176                | 23,176                  | 23,176                | 23,176              | 23,176                | 23,176                  |
| Adj. R <sup>2</sup>      | 0.009                 | 0.006               | 0.003                 | 0.010                   | 0.009                 | 0.006               | 0.003                 | 0.011                   |

Table 7: Firm behavior – Misreporting

| Dep. var. =<br>Firm ideology = | Misreporting <sub>t+1</sub> |                       |                      |                       |
|--------------------------------|-----------------------------|-----------------------|----------------------|-----------------------|
|                                | Time-varying                |                       | Time-invariant       |                       |
|                                | (1)                         | (2)                   | (3)                  | (4)                   |
| Misalignment                   | 0.001<br>(0.460)            | 0.043<br>(0.393)      | 0.001<br>(0.376)     | 0.034<br>(0.304)      |
| Size                           | 0.001<br>(1.175)            | 0.067<br>(1.452)      | 0.001<br>(1.164)     | 0.067<br>(1.447)      |
| BM                             | 0.008***<br>(2.916)         | 0.350***<br>(3.237)   | 0.008***<br>(2.911)  | 0.349***<br>(3.230)   |
| Leverage                       | 0.002<br>(0.412)            | 0.052<br>(0.187)      | 0.002<br>(0.412)     | 0.052<br>(0.187)      |
| ROA                            | -0.002<br>(-0.237)          | -0.199<br>(-0.387)    | -0.002<br>(-0.237)   | -0.199<br>(-0.387)    |
| Analyst Following              | -0.001*<br>(-1.702)         | -0.076*<br>(-1.704)   | -0.001*<br>(-1.708)  | -0.077*<br>(-1.711)   |
| DACC                           | 0.000<br>(0.363)            | 0.030<br>(0.372)      | 0.000<br>(0.364)     | 0.030<br>(0.371)      |
| Distance to SEC                | 0.001<br>(1.437)            | 0.042<br>(1.428)      | 0.001<br>(1.429)     | 0.042<br>(1.422)      |
| SP500                          | -0.006**<br>(-2.505)        | -0.463***<br>(-2.767) | -0.006**<br>(-2.499) | -0.462***<br>(-2.761) |
| PAC Contri SEC-Relevant        | -0.234<br>(-0.998)          | -23.676<br>(-0.706)   | -0.234<br>(-0.999)   | -23.798<br>(-0.707)   |
| Stock Return                   | 0.004**<br>(2.000)          | 0.202**<br>(2.394)    | 0.004**<br>(2.001)   | 0.202**<br>(2.397)    |
| Idiosyncratic Volatility       | 0.059<br>(0.568)            | 2.084<br>(0.437)      | 0.059<br>(0.568)     | 2.108<br>(0.442)      |
| Mean dep. var.                 | 0.017                       |                       | 0.017                |                       |
| Year FE                        | Yes                         | Yes                   | Yes                  | Yes                   |
| Industry FE                    | Yes                         | Yes                   | Yes                  | Yes                   |
| Model                          | OLS                         | Logit                 | OLS                  | Logit                 |
| Obs.                           | 23,176                      | 22,633                | 23,176               | 22,633                |
| Adj.(Pseudo) R <sup>2</sup>    | 0.005                       | 0.041                 | 0.005                | 0.041                 |

*Notes.* This table examines whether firms ideologically misaligned with the SEC are any different in their likelihood of initiating financial misreporting. Unit of observation is firm-year. *Misreporting* equals one in the year the firm initiates financial misreporting, as identified through a subsequent income decreasing restatement. *t* (*z*)-stats in parentheses for OLS (logit) models are based on standard errors clustered by firm. \*\*\*, \*\*, and \* indicate statistical significance (two-sided) at the 0.01, 0.05, and 0.10 levels, respectively. All variables are defined in Appendix A.

Table 8: False Positive – No AAER following SEC investigation

| Dep. var. =<br>Firm ideology = | No AAER               |                       |                       |                       |
|--------------------------------|-----------------------|-----------------------|-----------------------|-----------------------|
|                                | Time-varying          |                       | Time-invariant        |                       |
|                                | (1)                   | (2)                   | (3)                   | (4)                   |
| Misalignment                   | 0.032<br>(1.566)      | 0.384*<br>(1.645)     | 0.044**<br>(2.130)    | 0.540**<br>(2.282)    |
| Size                           | -0.014<br>(-1.442)    | -0.187*<br>(-1.937)   | -0.014<br>(-1.465)    | -0.193**<br>(-1.984)  |
| BM                             | -0.038<br>(-1.373)    | -0.395*<br>(-1.654)   | -0.037<br>(-1.381)    | -0.387<br>(-1.630)    |
| Leverage                       | -0.208***<br>(-3.701) | -2.239***<br>(-4.205) | -0.211***<br>(-3.737) | -2.280***<br>(-4.294) |
| ROA                            | -0.025<br>(-0.300)    | -0.281<br>(-0.374)    | -0.030<br>(-0.355)    | -0.350<br>(-0.456)    |
| Analyst Following              | 0.005<br>(0.505)      | 0.047<br>(0.532)      | 0.004<br>(0.443)      | 0.043<br>(0.485)      |
| DACC                           | 0.007<br>(0.483)      | 0.050<br>(0.367)      | 0.007<br>(0.489)      | 0.047<br>(0.350)      |
| Distance to SEC                | -0.008<br>(-1.359)    | -0.091<br>(-1.498)    | -0.008<br>(-1.303)    | -0.087<br>(-1.435)    |
| SP500                          | 0.005<br>(0.145)      | 0.079<br>(0.243)      | 0.005<br>(0.146)      | 0.096<br>(0.298)      |
| PAC Contri SEC-Relevant        | 5.633<br>(1.519)      | 402.996*<br>(1.774)   | 5.319<br>(1.456)      | 394.873*<br>(1.733)   |
| Stock Return                   | 0.025<br>(1.491)      | 0.271<br>(1.379)      | 0.024<br>(1.470)      | 0.265<br>(1.335)      |
| Idiosyncratic Volatility       | -0.784<br>(-0.760)    | -8.276<br>(-0.848)    | -0.842<br>(-0.816)    | -9.214<br>(-0.935)    |
| Mean dep. var.                 | 0.879                 |                       | 0.879                 |                       |
| Year FE                        | Yes                   | Yes                   | Yes                   | Yes                   |
| Industry FE                    | Yes                   | Yes                   | Yes                   | Yes                   |
| Model                          | OLS                   | Logit                 | OLS                   | Logit                 |
| Obs.                           | 1,385                 | 1,217                 | 1,385                 | 1,217                 |
| Adj.(Pseudo) $R^2$             | 0.075                 | 0.155                 | 0.077                 | 0.158                 |

*Notes.* This table examines whether SEC investigations against misaligned firms are less likely to result in an AAER. Unit of observation is SEC investigation. *No AAER* equals one if SEC does not release an AAER against the firm during an SEC investigation.  $t$  ( $z$ )-stats in parentheses for OLS (logit) models are based on standard errors clustered by firm. \*\*\*, \*\*, and \* indicate statistical significance (two-sided) at the 0.01, 0.05, and 0.10 levels, respectively. All other variables are defined in Appendix A.

Table 9: False negatives – No SEC investigation following misreporting

| Dep. var. =                       | Not Detected         |                       |                       |                       |                      |                       |                       |                       |
|-----------------------------------|----------------------|-----------------------|-----------------------|-----------------------|----------------------|-----------------------|-----------------------|-----------------------|
|                                   | Time-varying         |                       |                       |                       | Time-invariant       |                       |                       |                       |
|                                   | (1)                  | (2)                   | (3)                   | (4)                   | (5)                  | (6)                   | (7)                   | (8)                   |
| Firm ideology =                   |                      |                       |                       |                       |                      |                       |                       |                       |
| Non-Misalignment                  | 0.043<br>(1.016)     | 0.188<br>(0.902)      |                       |                       | 0.090**<br>(2.256)   | 0.454**<br>(2.244)    |                       |                       |
| Non-Misalignment × High Misreport |                      |                       | 0.137*<br>(1.757)     | 0.754*<br>(1.748)     |                      |                       | 0.147*<br>(1.922)     | 0.825*<br>(1.917)     |
| Non-Misalignment × Low Misreport  |                      |                       | 0.008<br>(0.179)      | 0.005<br>(0.022)      |                      |                       | 0.066<br>(1.500)      | 0.330<br>(1.452)      |
| High Misreport                    |                      |                       | -0.250***<br>(-3.477) | -1.331***<br>(-3.285) |                      |                       | -0.216***<br>(-3.008) | -1.155***<br>(-2.824) |
| Size                              | -0.037*<br>(-1.839)  | -0.204*<br>(-1.944)   | -0.039*<br>(-1.943)   | -0.228**<br>(-2.146)  | -0.038*<br>(-1.919)  | -0.214**<br>(-2.039)  | -0.040**<br>(-2.026)  | -0.239**<br>(-2.252)  |
| BM                                | 0.035<br>(0.837)     | 0.168<br>(0.779)      | 0.021<br>(0.498)      | 0.072<br>(0.331)      | 0.036<br>(0.859)     | 0.170<br>(0.798)      | 0.023<br>(0.540)      | 0.081<br>(0.379)      |
| Leverage                          | 0.209*<br>(1.784)    | 1.080*<br>(1.855)     | 0.189*<br>(1.664)     | 1.044*<br>(1.849)     | 0.224*<br>(1.911)    | 1.162**<br>(1.987)    | 0.203*<br>(1.772)     | 1.115*<br>(1.950)     |
| ROA                               | 0.030<br>(0.157)     | 0.303<br>(0.328)      | 0.044<br>(0.230)      | 0.416<br>(0.445)      | 0.026<br>(0.136)     | 0.285<br>(0.307)      | 0.034<br>(0.176)      | 0.331<br>(0.354)      |
| Analyst Following                 | -0.016<br>(-0.897)   | -0.076<br>(-0.918)    | -0.010<br>(-0.590)    | -0.052<br>(-0.619)    | -0.015<br>(-0.844)   | -0.072<br>(-0.872)    | -0.009<br>(-0.528)    | -0.046<br>(-0.557)    |
| DACC                              | -0.023<br>(-0.753)   | -0.124<br>(-0.832)    | -0.014<br>(-0.455)    | -0.083<br>(-0.540)    | -0.020<br>(-0.678)   | -0.108<br>(-0.733)    | -0.014<br>(-0.451)    | -0.078<br>(-0.514)    |
| Distance to SEC                   | 0.001<br>(0.075)     | 0.009<br>(0.153)      | -0.004<br>(-0.360)    | -0.020<br>(-0.334)    | 0.001<br>(0.091)     | 0.009<br>(0.152)      | -0.004<br>(-0.370)    | -0.022<br>(-0.366)    |
| SP500                             | -0.020<br>(-0.316)   | -0.058<br>(-0.177)    | -0.017<br>(-0.255)    | -0.032<br>(-0.095)    | -0.017<br>(-0.265)   | -0.031<br>(-0.093)    | -0.015<br>(-0.229)    | -0.008<br>(-0.023)    |
| PAC Contri SEC-Relevant           | 5.985<br>(0.557)     | 25.777<br>(0.497)     | 5.759<br>(0.577)      | 26.843<br>(0.540)     | 6.406<br>(0.583)     | 27.876<br>(0.522)     | 6.512<br>(0.631)      | 31.094<br>(0.596)     |
| Stock Return                      | -0.025<br>(-0.930)   | -0.158<br>(-1.171)    | -0.019<br>(-0.692)    | -0.145<br>(-1.038)    | -0.024<br>(-0.868)   | -0.148<br>(-1.081)    | -0.019<br>(-0.688)    | -0.142<br>(-1.018)    |
| Idiosyncratic Volatility          | -4.498**<br>(-2.386) | -24.068**<br>(-2.475) | -3.541*<br>(-1.844)   | -20.444**<br>(-2.075) | -4.452**<br>(-2.382) | -23.847**<br>(-2.462) | -3.415*<br>(-1.787)   | -19.853**<br>(-2.012) |
| Mean dep. var.                    | 0.612                |                       |                       |                       | 0.612                |                       |                       |                       |
| P-value of coef. diff.            |                      |                       | 0.067                 | 0.054                 |                      |                       | 0.171                 | 0.144                 |
| Year FE                           | Yes                  | Yes                   | Yes                   | Yes                   | Yes                  | Yes                   | Yes                   | Yes                   |
| Industry FE                       | Yes                  | Yes                   | Yes                   | Yes                   | Yes                  | Yes                   | Yes                   | Yes                   |
| Model                             | OLS                  | Logit                 | OLS                   | Logit                 | OLS                  | Logit                 | OLS                   | Logit                 |
| Obs.                              | 851                  | 798                   | 836                   | 784                   | 851                  | 798                   | 836                   | 784                   |
| Adj.(Pseudo) $R^2$                | 0.113                | 0.137                 | 0.131                 | 0.154                 | 0.119                | 0.141                 | 0.134                 | 0.157                 |

*Notes.* This table examines whether SEC is less likely to open investigations against non-misaligned firms who misreport vs. misaligned firms who misreport. Unit of observation is income decreasing restatement. *Not Detected* equals one if SEC does not open an investigation against the firm within three years of the end of misreporting. *Non-Misalignment* is an indicator that equals one when *Misalignment* is zero. *High (Low) Misreport* is an indicator that equals one if the cumulative effect of the restatement on income is more (less) than 3% of the total assets in the year before the start of misreporting.  $t(z)$ -stats in parentheses for OLS (logit) models are based on standard errors clustered by firm. p-value for test of difference in coefficients is one-tailed. \*\*\*, \*\*, and \* indicate statistical significance (two-sided) at the 0.01, 0.05, and 0.10 levels, respectively. All other variables are defined in Appendix A.



Table 10: Career outcomes: Partisan SEC Commissioners

Panel A: Partisan enforcement and new (leadership) roles

| Dep. var. =<br>Firm ideology = | New Roles    |          |          |                |          |          | New Leadership Roles |          |          |                |          |          |
|--------------------------------|--------------|----------|----------|----------------|----------|----------|----------------------|----------|----------|----------------|----------|----------|
|                                | Time-varying |          |          | Time-invariant |          |          | Time-varying         |          |          | Time-invariant |          |          |
|                                | (1)          | (2)      | (3)      | (4)            | (5)      | (6)      | (7)                  | (8)      | (9)      | (10)           | (11)     | (12)     |
| Partisan Investigations        | 2.283*       |          |          | 1.749***       |          |          | 2.636**              |          |          | 1.694**        |          |          |
|                                | (1.952)      |          |          | (3.335)        |          |          | (2.509)              |          |          | (2.708)        |          |          |
| Partisan AAERs                 |              | 0.502    |          |                | 1.462**  |          |                      | 0.727    |          |                | 2.199**  |          |
|                                |              | (0.509)  |          |                | (2.362)  |          |                      | (0.683)  |          |                | (2.850)  |          |
| Partisan Penalty               |              |          | 0.145    |                |          | 0.508**  |                      |          | 0.231    |                |          | 0.620*** |
|                                |              |          | (0.670)  |                |          | (2.925)  |                      |          | (0.930)  |                |          | (4.748)  |
| Age                            | -1.376       | -1.578   | -1.522   | -1.740*        | -1.815   | -1.567*  | -0.842               | -1.154   | -1.105   | -1.184         | -1.525   | -1.080*  |
|                                | (-1.277)     | (-1.461) | (-1.739) | (-1.878)       | (-1.636) | (-2.094) | (-1.002)             | (-1.231) | (-1.282) | (-1.623)       | (-1.596) | (-1.910) |
| Obs.                           | 13           | 13       | 13       | 13             | 13       | 13       | 13                   | 13       | 13       | 13             | 13       | 13       |
| R <sup>2</sup>                 | 0.376        | 0.179    | 0.183    | 0.481          | 0.280    | 0.428    | 0.385                | 0.110    | 0.134    | 0.397          | 0.368    | 0.508    |

Notes. This table examines association between SEC Commissioners' partisan actions and their career outcomes. Unit of observation is SEC Commissioner. *New Roles* is the natural logarithm one plus the number of new roles in public or private sector the Commissioner takes on within two years of the end of their tenure. *New Leadership Roles* is same as *New Roles* except that it only counts new leadership roles in public or private sector, where we identify leadership roles as those that involve being a chairman, president, board of director, board of trustee, founder, or CEO. *Partisan Enforcement* for a Commissioner measures the cumulative SEC actions against misaligned firms minus the cumulative SEC actions against non-misaligned firms, scaled by the sum of the two numbers, during the Commissioner's tenure. *Partisan Enforcement* has three versions: (i) *Partisan Investigations* (based on number of SEC investigations), (ii) *Partisan AAERs* (based on number of AAERs released), and (iii) *Partisan Penalty* (based on total monetary enforcement penalties). *Partisan Penalty* has three additional versions corresponding to civil penalty (*Partisan Civil Penalty*), disgorgement (*Partisan Disgorgement*), and prejudgment interest (*Partisan Prejudgment Interest*). Misaligned firms are identified using time-varying and time-variant firm ideology. *Age* is the natural logarithm of the Commissioner's age when their tenure ends. *t*-stats in parentheses are based on heteroscedasticity robust standard errors. \*\*\*, \*\*, and \* indicate statistical significance (two-sided) at the 0.01, 0.05, and 0.10 levels, respectively.

Table 10: Career outcomes: Partisan SEC Commissioners (Continued)

Panel B: Partisan monetary enforcement penalty by category and new (leadership) roles

| Dep. var. =<br>Firm ideology = | New Roles    |          |          |                |          |          | New Leadership Roles |          |          |                |          |          |
|--------------------------------|--------------|----------|----------|----------------|----------|----------|----------------------|----------|----------|----------------|----------|----------|
|                                | Time-varying |          |          | Time-invariant |          |          | Time-varying         |          |          | Time-invariant |          |          |
|                                | (1)          | (2)      | (3)      | (4)            | (5)      | (6)      | (7)                  | (8)      | (9)      | (10)           | (11)     | (12)     |
| Partisan Civil Penalty         | 0.564*       |          |          | 0.441**        |          |          | 0.463                |          |          | 0.500**        |          |          |
|                                | (2.033)      |          |          | (2.648)        |          |          | (1.803)              |          |          | (2.834)        |          |          |
| Partisan Disgorgement          |              | 0.311    |          |                | 0.457**  |          |                      | 0.262    |          |                | 0.382    |          |
|                                |              | (1.597)  |          |                | (2.453)  |          |                      | (1.273)  |          |                | (1.753)  |          |
| Partisan Prejudgment Interest  |              |          | -0.122   |                |          | -0.208   |                      |          | -0.211   |                |          | -0.404   |
|                                |              |          | (-0.443) |                |          | (-0.722) |                      |          | (-1.184) |                |          | (-1.663) |
| Age                            | -1.668**     | -1.899*  | -1.218   | -1.424*        | -2.126** | -1.039   | -1.061               | -1.263   | -0.606   | -0.895         | -1.450*  | -0.239   |
|                                | (-2.617)     | (-2.116) | (-1.076) | (-1.944)       | (-2.549) | (-0.800) | (-1.479)             | (-1.482) | (-0.619) | (-1.260)       | (-1.844) | (-0.212) |
| Obs.                           | 13           | 13       | 13       | 13             | 13       | 13       | 13                   | 13       | 13       | 13             | 13       | 13       |
| R <sup>2</sup>                 | 0.395        | 0.324    | 0.173    | 0.401          | 0.438    | 0.205    | 0.237                | 0.192    | 0.113    | 0.408          | 0.279    | 0.258    |