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Guilty by Political Association: The Impact of Political Scandals on Connected Firms

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May 2023

Working Paper 20230504

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Keywords: Political Scandal, Political Connection, Reputational Penalty, Firm Valuation
JEL Classification: G14, G30

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First Draft: April 2020

Current Draft: April 2023

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1. Introduction

Received literature generally concludes that ties to politicians increase the value of firms whose management elects to become so connected.[2] The common measure of whether a firm is connected to a US politician is whether the firm's Political Action Committee (PAC) contributes to the politician's electoral campaign.[3] Presumably, management weighs the costs and benefits of establishing such a connection prior to doing so and, for those firms that choose to contribute, management concludes that the present value of the benefits outweighs the costs. For US congresspersons, the direct cost of establishing such a tie is easy to measure—it is a maximum of $5,000 for each candidate as established by Federal Campaign Finance Law and monitored by the Federal Election Commission (FEC). Given the apparently low direct cost, a reasonable expectation would be that every firm would establish such a tie with every congressperson.

However, according to the FEC, of the US firms with shares traded on an exchange during the period of 1992-2018, only 33% contributed through a PAC to *any* congressional campaign during a year in which a congressional election occurred. Moreover, conditional on a firm contributing to any congressional campaign, on average, the firm contributed to only 34 such campaigns out of a total of 469.[4] Potentially, the cost of ties to a congressperson goes beyond the direct costs of a campaign contribution. In this study, we propose that one such cost is the loss in

[2] See, for example, Snyder (1992), Agrawal and Knoeber (2001), Fisman (2001), Cull and Xu (2005), Faccio, Masulis, and McConnell (2006), Claessens, Feijen, and Laeven (2008), Faccio and Parsley (2009), Firth, Rui, and Wu (2011), Yu and Yu (2011), Amore and Bennedsen (2013), Goldman, Rocholl, and So (2013), Igan and Mishra (2014), Tahoun (2014), Lu, Pan, and Zhang (2015), and Fulmer, Knill, and Yu (2022).

[3] See, for example, Cooper, Gulen and Ovtchinnikov (2010), Duchin and Sosyura (2012), Correia (2014), Akey (2015), Hutton, Jiang, and Kumar (2015), and Kim and Zhang (2015), Jennings, Kartapanis, and Yu (2020).

[4] There are 435 representatives and 100 senators, but only one third of Senators are up for reelection in a given election year because the terms are staggered such that one-third of the seats are up for reelection each election year. Of course, a firm could contribute to more than one campaign in an election, thereby, giving rise to additional opportunities.

value to a US firm that maintains a political connection, through a PAC contribution, to a US congressperson who is ensnared in a scandal.

According to GovTrack.us, there were 172 instances during the period of 1992-2018, or about 6.6 instances per year, in which a congressperson became caught up in misconduct of one form or another. We label these "political scandals." As illustrated in Figure 1, on average, in any given year during that time period, 24.8% of the firms that contributed through a PAC to a congressional campaign did so to a congressperson who was involved in a scandal no later than two years after the year of the contribution. Thus, in general, the likelihood of a firm contributing to any congressperson's campaign is relatively modest, but, having done so, the likelihood of the firm having contributed to a congressperson who is caught up in a scandal is not inconsequential. Importantly, only 20.35% of the scandal-tainted politicians in our sample step down from office, leaving 79.65% to serve the remainder of their elected terms. While it is straight-forward to predict what would happen to firm values for the 20% of firms whose political connections are severed, it is less clear what happens to the 80% of firms for which political connections are *not* severed. We conjecture that an undocumented cost to a firm of an ongoing political connection is a reputational spillover effect that occurs when the congressperson is embroiled in wrongdoing. To wit: the damage to the congressperson's reputation imposes an indirect economic penalty on the connected firms' market value that comes about as customers, suppliers, and financiers "back-away" from the connected firm.

We begin by investigating the valuation consequences to firms connected to such US congresspersons. We consider a firm to be connected to a scandal-tainted congressperson if the firm contributes through its PAC during the two-year period preceding the calendar year of the

first published media report of the scandal or during the calendar year of the first published media report of the scandal.

To address this topic, we conduct three sets of tests. The first set of tests are panel regressions that examine the correlation between the change in a firm's Tobin's Q (henceforth, Q) in a year and whether a firm is connected to a scandal-tainted congressperson in that year. We find that firms connected to such a congressperson are associated with a 2.6% (p-value < 0.01) decrease in Q relative to firms that are connected to congresspersons not caught up in a scandal in the year in which the scandal is first reported by the published media. Furthermore, we find that firms connected to a greater number of scandal-tainted congresspersons are associated with an even greater decline in Q than the Q of firms connected to congresspersons not involved in a scandal. Specifically, a firm connected to one additional scandal-tainted congressperson is associated with a 0.6% (p-value = 0.02) further relative fall in Q in the year in which the scandals are first reported. Considering that the average market capitalization of connected firms is $13.8 billion, the 2.6% decline in Q translates to a loss of $359 million, and the second scandal adds $83 million to that loss.

The second set of tests are multiple event difference-in-differences analyses. These tests consider the difference in the change in Q from the years before to the years after the year of the first scandal in which the firm is connected to the scandal-tainted congressperson relative to the change in Q for contributing firms that are connected to congresspersons not involved in a scandal at any time during the sample period. These tests are designed to consider whether the relative declines in Q of firms connected to scandal-tainted congresspersons stem solely from severed political ties. Critically, we find that the relative decline in Q is 4.2% (p-value < 0.01) for firms connected to a scandal-tainted congressperson who does *not* step down from office following the

first published media report of the scandal in contrast with a lower relative decline in Q of 1.7% (p-value = 0.29) for firms connected to a scandal-tainted congressperson who publicly announces his/her resignation prior to the next election. Stepping down from office severs the tie between the firm and the congressperson. Thus, these results indicate that the decline in firm value is not due to the broken political tie; there is a more-pervasive negative shock to firms connected to the scandal-tainted congresspersons who do not step down. This negative shock represents a potential cost to firms of ongoing political connections. Estimates of such costs could tip the scales of a cost/benefit analysis of contributing politically to a negative expected value, which could explain, at least in part, why some firms choose not to contribute.

We, then, group the scandals according to the label attached to them by GovTrack.us. These include business-, crime-, ethics-, and sexual harassment-related scandals. We leverage these scandal characteristics to verify that the adverse consequences felt by firms connected to scandal-tainted congresspersons are due to a reputational spillover effect versus a broken political tie. In each grouping, we find that the relative declines in Q for firms connected to scandal-tainted congresspersons who do not step down from office are more pronounced than are the relative declines in Q for firms connected to scandal-tainted congresspersons who do step down following the first media report of the scandal. Thus, the more pronounced relative drop in value for congresspersons who remain in office is not due to a single type of scandal.

In addition, we find that the greater relative decline in Q for firms connected to scandal-tainted congresspersons who do not step down from office in comparison with the relative decline in Q of firms connected to scandal-tainted congresspersons who do step down is more pronounced when the scandal receives more media attention and involves congresspersons who are members of the Senate (henceforth, senators) as opposed to members of the House of Representatives

(henceforth, representatives). These findings suggest that a scandal is more detrimental to the market value of a connected firm when the scandal is more visible.

The third set of tests are event studies that investigate the cumulative abnormal stock return (CAR) of firms connected to scandal-tainted congresspersons around the first instance in which a published media outlet reports the scandal. The virtue of this set of tests is that they are tied to specific dates. The downside is that we do not know when a rumor of the scandal began to circulate either in Washington or the congressperson's home voting district, and neither do we know when the extent of the infraction was fully recognized by investors. We, thus, consider the one-month trading interval around the first published media report. We find that, on average, connected firms experience a CAR of -0.23% (p-value < 0.01) over the 21 days surrounding the first media report of a scandal. Further, for firms connected to scandal-tainted congresspersons who do not step down from office, the CAR of -0.29% (p-value < 0.01) is more negative than the CAR of -0.08% (p-value = 0.54) for firms connected to congresspersons who do step down from office. The results support the proposition that it is not just the broken tie to a congressperson that causes harm to the connected firms; the effect is more pronounced when the congressperson remains in office.

We, then, examine channels through which a reputational spillover could flow. Specifically, we investigate the effect of scandal-tainted congresspersons on connected firms' fundamental operating and financing prospects. We find that the decline in the market value of firms connected to scandal-tainted congresspersons is associated with a 2.4% (p-value < 0.01) decline in sales growth, a 7.2% (p-value = 0.02) decrease in net profit margin, and an 18.5% (p-value < 0.01) increase in the cost of debt following the year of the first scandal in which the firm is connected to the scandal-tainted congressperson relative to contributing firms not connected to a scandal-tainted congressperson. Furthermore, the relative fall in the sales growth rate and net profit margin, as

well as the relative increase in the cost of debt, are more pronounced for firms connected to congresspersons who do not step down from office following the first media report of a scandal in comparison with those connected to congresspersons who do step down from office. These findings suggest that the relative drop in the market values of connected firms derives from an expectation of future declines in the connected firm's fundamental operating and financing prospects. The greater changes for firms connected to congresspersons who do not step down from office further suggest that the drops in firm value go beyond the loss of a political connection.

In addition, we directly test the impact of political scandals on firm reputation using Fortune's "Most Admired Companies" reputation scores. Using these reputation scores, we find that firms connected to a scandal-tainted congressperson who remains in office experience a 2.8% (p-value = 0.05) decline in reputation score. The magnitude of this decline in reputation score increases to 3.0% (p-value = 0.04) for first scandal connections in which the scandal-tainted congressperson steps down from office. In contrast, the impact of a political scandal on reputation is statistically indistinguishable from zero when the politician leaves office, suggesting once again that this effect is not born out of a broken political tie.

Finally, we examine the change in connected firms' contributions to scandal-tainted congresspersons following the first media report. We find that connected firms relatively decrease their contributions to the scandal-tainted congresspersons by 45% (p-value < 0.01). This evidence is consistent with connected firms distancing themselves from scandal-tainted congresspersons, suggesting that the management of connected firms is aware of the negative effects of such connections on the firm's market value and future fundamental operating and financing prospects.

In sum, we interpret our findings to indicate that there exists a previously undocumented cost associated with ongoing corporate political connections: when a congressperson is involved

in a publicly-reported scandal, connected firms experience a relative loss in value that is especially severe when the scandal-tainted congressperson does not step down from office soon after the initial published media report of the scandal. We further find that the losses in value are related to a decrease in corporate reputation score and subsequent lower sales growth and profit margin and higher cost of debt financing for firms connected to scandal-tainted congresspersons than for firms connected to those not caught up in such scandals. We propose that this undocumented cost of ongoing political connections may offer, at least in part, an answer to the question posed by Ansolabehere, Figueiredo, and Snyder (2003), as to why there is so little corporate money in US politics. In particular, the *ex post* costs that we document are taken into account *ex ante* as one of the costs of being politically connected. Corporate managers apparently take these costs into account when making the decision to contribute (or not) to US politicians' campaigns.

2. Literature Review

A. Benefits and Costs of Corporate Political Connections

An extant body of literature examines the ways in which political connections benefit connected firms. Prior studies find that political connections positively influence firm sales (Amore and Bennedsen (2013), Goldman, Rocholl, and So (2013), Tahoun (2014)), leverage ratios (Claessens, Feijen, and Laeven (2008)), government bailouts and relief (Faccio, Masulis, and McConnell (2006), Duchin and Sosyura (2012)) and access to credit (Cull and Xu (2005), Claessens, Feijen, and Laeven (2008)). Moreover, politically-connected firms linked to political misconduct face a reduced likelihood of or delay in being investigated (Yu and Yu (2011), Correia (2014)), and the penalties assessed by enforcers are less severe (Fulmer, Knill, and Yu (2022), Heitz, Wang, and Wang (2021)).

The strand of literature on the benefits of political connections gives rise to a natural question: if political connections are inordinately beneficial, why do many firms choose not to be connected (Ansolabehere et al. (2003))? A set of studies attempts to address this question by identifying the downside of firms being so connected. These studies find that politically connected firms suffer from higher agency costs, which they attribute to managers increasing their personal political capital to be used in the event that they are caught expropriating from shareholders (Aggarwal, Meschke, and Wang (2012), Coates (2012), Dahan, Hadani, and Schuler (2013), Fisman and Wang (2015), and Fulmer et al. (2022)). However, if corporate political ties are, on average, beneficial to the connected firms' shareholders and if managers also consume more private benefits as a result of firms being politically connected, why do most US managers choose not to have their firms become connected? We address these questions by examining whether there is a further cost to a firm of being politically connected that comes about when the congressperson to whom a firm is connected is involved in a scandal and does not subsequently step down from office, i.e., the political connection is not severed.

B. Political Scandals and Contributing Firms

Our paper is not the first to examine the impact of political scandals on connected firms. Fan, Rui, and Zhao (2008) report a significant decline in stock prices of firms connected to corruption scandals involving high-level government bureaucrats in China. Liu, Shu, and Wei (2017) document that the Bo Xilai scandal, a widely known political scandal in China involving a powerful member of the Chinese Communist Party, caused a significant drop in the stock prices of firms connected to him. We, too, consider the effect of political scandals on connected firms. Our study differs from the prior studies in that prior studies attribute the deterioration in firm value and future performance in connected firms following political scandals to the broken political tie

and the associated loss in the benefits of such ties. Our paper is the first, of which we are aware, to examine the market value consequences of scandals when political ties are *not* severed. We study the reputational spillover effect from the scandal-tainted congressperson to the connected firms in the form of a deterioration in market value and operating and financing prospects.

C. Guilty by Association

It is a well-known phenomenon in U.S. politics that politicians will distance themselves from a scandal involving a campaign contributor. A recent example is found in the months leading up to the 2020 election, when Kevin McCarthy, House Minority Leader of the U.S. House of Representatives, said he would donate to charities the contributions he received from Igor Fruman and Lev Parnas, two donors that were indicted due to campaign finance fraud.[5] Why would politicians return or give away donations if the politician had nothing to do with the crime? The answer is that politicians do not want to be guilty by association, even though they had nothing to do with the scandal in question and, therefore, distance themselves from the individual(s) involved in the scandal. In this paper, we examine the reverse of this example.

The notion of "guilty by association" implies that the stigma leads to disgrace on all associated parties of a particular circumstance, regardless of guilt. Extant literature provides evidence consistent with stigma playing a role in innocent parties being penalized by a scandal. For example, Groysberg, Lin, Serafeim, and Abrahams (2016) find that employees who worked at a scandal-tainted company suffer job market penalties post-scandal (an average 4% compensation penalty), even though they were innocent of any wrongdoing. Kang (2008) finds that firms that have directors in common with fraudulent firms experience a reputational penalty spillover from the fraudulent firm, even when the director had nothing to do with the fraud. Beatty, Bunsis, and

[5] https://www.usatoday.com/story/news/politics/2019/10/10/impeachment-kevin-mccarthy-donation-igor-fruman-lev-parnas/3935813002/

Hand (1998) find that clients of underwriters who are investigated by the Securities and Exchange Commission face indirect penalties due to the reputational decline of their underwriter. Though attaching a stigma to parties that had nothing to do with the scandal may seem irrational, Bos, Pryor, Reeder, and Stutterheim (2013) suggest that stigma need not be rational. They explain that stigmas are more about enforcing norms and helping people to avoid contact with parties that are guilty by association – or "contaminated" by the scandal. In our context, the association becomes salient through corporate political contributions.

3. Scandals and Contributing Firms

A. Congressperson Scandals

The data source for congressperson scandals is the *Legislator Misconduct Database* (LMD), which is available at GovTrack.us. These data comprise instances of confirmed and alleged misconduct, to which we refer as political scandals, by members of the US Congress based on investigations and settlements, felony convictions, and official reprimands by Congress. Table 1 displays the characteristics and frequency of the scandals that occur within the sample period. Our sample consists of 172 scandals occurring between 1992 and 2018. In 137 of the scandals, the involved congressperson does not resign from office following the scandal and before the next election. We classify such congresspersons as *Stay*.[6] A congressperson is classified as *Non-stay* if he or she publicly announces a resignation from office prior to the next election. Appendix A.1 gives examples of scandals, the involved congressperson, the first-report date, and whether the congressperson remained in office.

[6] Congresspersons who do not resign from office may lose an election or choose not to run for office in the next election. We consider such cases in Section 7.B.

In addition to scandal characteristics and outcomes, LMD provides the date of the "first consequence" regarding the scandal.[7] With the LMD first consequence date as a starting point, we search the Factiva database to identify the date of the first news article about the scandal that appeared in a published outlet.[8,9] The median difference in days between the date of the first news article in Factiva and the date of the first consequence in LMD is 83, with the first consequence always appearing later than the first published media report. In the remainder of the paper, we refer to the date of the first news article in Factiva regarding the scandal as the first-report date. For our purposes, the first-report date is the critical date.

B. Contributing Firms

We assemble the sample of contributing firms, their corresponding political campaign contributions, and the years of their contributions from the FEC database, which covers all firms making campaign contributions through a PAC. We merge the sample with stock return data and financial reporting data from the *CRSP* and *Compustat* databases. The final sample comprises 1,064 firms that contribute through their PACs at least once to a congressperson's campaign during the period of 1992 through 2018 and for which data are available in *CRSP* and *Compustat*. We classify a firm as being connected to a scandal-tainted congressperson if the firm contributes through its PAC to the campaign of a congressperson involved in a scandal any time beginning two years prior to the first-report date of the scandal and ending at the end of the year in which the

[7] According to LMD, the first consequence includes "(1) all letters of reproval, censures, and expulsions from Congress; (2) all investigations by the House Office of Congressional Ethics (OCE) (2008–), the House Committee on Ethics (HCE) (1975–), and the Senate Select Committee on Ethics (SSCE) (1962–), and all Senate votes on "exclusion" related to personal misconduct; (3) some other investigations by a body of Congress and monetary settlements that involved alleged personal misconduct, e.g., settlements administered by Congress's Office of Compliance regarding sexual harassment claims, but most settlements are not known to the public."

[8] The scandal could have been reported in a television or radio outlet prior to the published report.

[9] The following is an example of the search syntax used in Factiva: (Chris Collins or Christopher Collins) and (scandal or indict or indicted or sentence or sentenced or investigation or investigated or conviction or convicted or committed or resign or guilty or charged or testify or probe or charge or charged or quit or perjury or accuse or accused or ethic or ethics or arrest or arrested or alcoholic or suspect).

first-report date of the scandal occurred.[10] The median number of publicly-listed contributing firms in the final sample connected to each of the 172 scandal-tainted congresspersons is 56, with a minimum of 2 and a maximum of 258. In total, 700 of the sample firms are connected to at least one scandal-tainted congressperson. Of these, 364 are connected to more than one scandal-tainted congressperson. The firms that contribute to a congressperson who is never enmeshed in a scandal during our sample period comprise the control group for our analyses. We, thus, compare firms that contribute to congresspersons caught up in a scandal with firms that contribute to congresspersons not caught up in a scandal.

4. Connected Firms, Scandal-tainted Congresspersons, and Firm Value

The primary research question of our study is whether being connected to a congressperson involved in a scandal, a scandal-tainted congressperson—especially those that remain in office—affects the firm's market value. We conduct three sets of tests to investigate that question: (1) panel regressions; (2) multiple events difference-in-differences analyses; and (3) event studies of stock returns.

A. Scandal Connection and Firm Value

We begin by estimating firm-year panel regressions of the form:

$$Q_{i,t} = \alpha_i + \alpha_t + \gamma X_{i,t} + \delta Scandal_{i,t} + \in_{i,t} \quad (1)$$

where i indexes firms, t indexes years, $Q_{i,t}$ is the dependent variable for firm i in year t, α_i and α_t are firm and year fixed effects, $X_{i,t}$ are control variables, and $\in_{i,t}$ is an error term. The dependent variable, $Q_{i,t}$, is calculated as total assets minus book value of equity plus stock price times shares outstanding divided by total assets of firm i at the end of year t. The independent variables of interest, $Scandal_{i,t}$, are indicators that identify whether a contributing firm i is connected to a

[10] Our results remain when we consider one year or three years preceding first-report date.

scandal-tainted congressperson in year *t*. The coefficient of $Scandal_{i,t}$, δ, estimates the relation between a scandal and the change in a connected firm's Q during the year of the first-report date. Through $X_{i,t}$, we include control variables that have been shown by prior research to be correlated with firm value. All variables, their definitions, and sources of data are given in Appendix A.2. In the analysis, all numerical control variables are winsorized at the 1% and 99% levels. Table 2 presents summary statistics of the firms in the analyses. In all regressions, except those in Section 7, standard errors are clustered at the firm level (Bertrand, Duflo, and Mullainathan (2004)). In Section 7, we cluster standard errors by congressperson.

To examine the correlation between the change in a firm's market value, as measured by its Q, and whether the firm is connected to a scandal-tainted congressperson, we estimate equation (1). Columns 1 and 2 of Table 3 report the coefficients where the independent variable of interest is $Scandal\ Year_{i,t}$. $Scandal\ Year_{i,t}$ is an indicator variable set to 1 if firm *i* is connected to at least one scandal-tainted congressperson in year *t*, and zero otherwise. Column 1 reports the results of a regression with firm and year fixed effects, but no control variables; column 2 reports the results of a regression with fixed effects and control variables. The coefficients of $Scandal\ Year_{i,t}$ are -0.039 and -0.026 (both p-values < 0.01). The coefficient in column 2 indicates that, after controlling for other factors, firms connected to scandal-tainted congresspersons are associated with a 2.6% relative decrease in Q during the year of the first-report date. The drop in Q for connected firms is relative to control firms that are connected to congresspersons not involved in a scandal. For the average firm in our sample, the relative drop in Q translates to a $359 million loss in market value. The results indicate that connections to scandal-tainted congresspersons are associated with a statistically significant decline in firm value.

To capture the effect of a firm being connected to multiple scandal-tainted congresspersons in the first-report year, we estimate equation (1) using *Number of Scandals*$_{i,t}$ as the independent variable of interest where *Number of Scandals*$_{i,t}$ is the number of scandals to which firm *i* is connected in year *t*. The results are reported in Table 3, column 3, with firm and year fixed effects, but no control variables, and column 4, with control variables. The coefficients of *Number of Scandals*$_{i,t}$ are -0.015 (p-value < 0.01) and -0.006 (p-value = 0.02), respectively. Taking into account the control variables, the 0.6% fall in Q translates to a loss of $82.8 million per additional scandal for the average firm in the year of the first-report date.

B. First Scandal Connection and Scandal Outcome

A potential concern with the findings in Table 3 is that rather than a reputational spillover effect from the scandal-tainted congressperson to the connected firms, the results could be explained as simply the consequence of a broken political tie. Specifically, if political connections provide economic value, then signals indicating that the likelihood of the congressperson stepping down from office have become elevated are likely to result in declines in connected firms' market values (Fisman (2001), Fan et al. (2008), Faccio and Parsley (2009), and Liu et al. (2017)).

To identify empirically whether the results in Table 3 stem solely from severed political ties, we classify firms based on the year of the first scandal in which the firm is connected to a scandal-tainted congressperson during our sample period (henceforth, first scandal connection). Following Bertrand and Mullainathan (2003), we use a multiple event difference-in-differences methodology to examine the difference in the change in Q from the year before to the year after the year of the first-report date. Such changes in Q are examined relative to the change in Q for contributing firms that are not connected to a scandal-tainted congressperson during that year. To identify whether the valuation effect depends upon the scandal-tainted congressperson remaining

in office following the scandal, we distinguish first scandal connections based on scandal outcome, where the outcome is whether the congressperson remains in office or steps down following the scandal. A more pronounced valuation effect for scandal outcomes involving congresspersons that remain in office would point to something beyond a broken political tie. We posit (and later test) that it is due to a scandal reputational spillover effect from the congressperson to the firm. To test whether the results in Table 3 are due to something beyond a broken political tie, we estimate the model:

$$Q_{i,t} = \alpha_i + \alpha_t + \gamma X_{i,t} + \delta \textit{First Scandal}_{i,t} + \in_{i,t} \quad (2)$$

where i indexes firms, t indexes years, $Q_{i,t}$ is total assets minus book value of equity plus stock price times shares outstanding divided by total assets of firm i at the end of year t, α_i and α_t are firm and year fixed effects, $X_{i,t}$ are control variables, and $\in_{i,t}$ is an error term. The variable *First Scandal*$_{i,t}$ is an indicator set to 1 if the year of observation is equal to or later than the year of the first scandal in which the firm is connected to the scandal-tainted congressperson. *First Stay Scandal*$_{i,t}$ is an indicator set to 1 if the year of observation is equal to or later than the year of the first scandal in which the firm is connected to the scandal-tainted congressperson who does not resign from office. Analogously, *First Non-stay Scandal*$_{i,t}$ is an indicator set to 1 if the year of observation is equal to or later than the year of the first scandal in which the firm is connected to the scandal-tainted congressperson who does step down from office prior to the following election cycle.

The coefficient of *First Scandal*$_{i,t}$, δ, estimates the effect of a firm's first scandal connection on the change in $Q_{i,t}$ from before to after the year of the first scandal in which firm i is connected to the scandal-tainted congressperson. The coefficients of *First Stay Scandal*$_{i,t}$ and *First Non-stay*

Scandal$_{i,t}$ have similar interpretations and refer to scandals in which the congressperson remains in office or steps down, respectively.

Table 4 presents the results. In column 1, the coefficient of *First Scandal*$_{i,t}$ is -0.043 (p-value < 0.01). This result indicates that relative to firms connected to a congressperson who is not scandal-tainted during our sample period, firms connected to a scandal-tainted congressperson experience a 4.3% decline in Q in the year of and in the years following the first-report date. Further, the coefficients of *First Stay Scandal*$_{i,t}$ in column 2 and *First Non-stay Scandal*$_{i,t}$ in column 3 are -0.042 (p-value = 0.01) and -0.017 (p-value = 0.29), respectively. These results show an average decline in Q of 4.2% for firms connected to a scandal-tainted congressperson who *does not* step down from office following the first-report date of the scandal. In contrast, firms connected to a scandal-tainted congressperson who *does* step down are associated with a lesser decline of 1.7% in Q (which, with a p-value of 0.29, is not significantly different from zero). Column 4 presents the results of including *First Stay Scandal*$_{i,t}$ and *First Non-stay Scandal*$_{i,t}$ in a single regression. The results are similar to those in columns 1 and 2, where the coefficient of *First Stay Scandal*$_{i,t}$ is -0.040 (p-value = 0.01), and the coefficient of *First Non-stay Scandal*$_{i,t}$ is -0.011 (p-value = 0.51). The 4.0% decline in Q translates into a loss of $552 million for the average contributing firm in the years following the first-report date.

Considering that the connection between a firm and a congressperson is severed when the outcome is that the congressperson steps down from office, the results in Table 4 show that a connection to a scandal-tainted congressperson can result in negative valuation consequences *beyond* the loss of a political tie. In particular, the detrimental effect on firm value is more pronounced when the outcome is that the congressperson remains in office following the scandal, suggesting that the negative effect is, at least in part, due to a reputational spillover from the

scandal-tainted congressperson to connected firms. We test the reputational spillover effect further in Sections 5 and 6 of the paper.

C. Firm Value and Scandals by Type of Scandal

Perhaps the effect of a scandal on value is related to the type of scandal. To address that concern, we investigate whether the valuation effect differs across various types of scandals. We examine four types of scandals where the type of scandal is assigned by GovTrack.us. They are: *Business, Crime, Ethics,* and *Sexual Harassment*. Note that the types of scandals are not mutually exclusive.

We re-estimate equation (2) for each type of scandal and use *First Stay Scandal*$_{i,t}$ and *First Non-stay Scandal*$_{i,t}$ as the key independent variables of interest. In total, eight regressions are estimated. One for each category of *Business, Crime, Ethics,* and *Sexual Harassment* and one for each category of *non-Business, non-Crime, non-Ethics,* and *non-Sexual Harassment*.

Table 5 reports the results. In each regression, the coefficient of *First Stay Scandal*$_{i,t}$ is more negative than the coefficient of *First Non-stay Scandal*$_{i,t}$. Further, six of the eight coefficients of *First Stay Scandal*$_{i,t}$ are significantly different from zero at the 0.10 level or better with four of the eight being significant at the 0.05 level or better. By comparison, only one of the coefficients of *First Non-stay Scandal*$_{i,t}$ is significantly different from zero at the 0.10 level, and none are significant at the 0.05 level. Moreover, three of the eight coefficients are positive. Also noteworthy is the fact that there are intuitive differences in the magnitude of the effect on *First Stay Scandal*$_{i,t}$, ranging from 2.9% for non-crimes to 10% for crimes. If this effect were due to broken political ties, we would expect to see little to no difference in the magnitude of the effect by scandal type. Instead, we see differences that are consistent with these effects being due to a reputational spillover effect.

These results indicate that, regardless of the type of scandal, the relative drops in Q for firms connected to scandal-tainted congresspersons who do not step down from office are more pronounced than are the drops in value for firms connected to scandal-tainted congresspersons who step down from office following the first-report date of the scandal. These findings show that the difference between the decline in value for firms connected to congresspersons who remain in office and those who step down from office is not isolated to a single type of scandal. They further show that the loss in value extends beyond the loss of a political connection, as the loss in value is less when the congressperson involved in the scandal steps down. Finally, the differences across the effects of different types of scandals are consistent with a reputational spillover.

D. Firm Value and Scandals by Scandal Visibility

In this section, we investigate whether the valuation consequence to the firm is related to the visibility of the scandal. The idea is that not all customers and suppliers are aware of a scandal at the first-report date and some potential scandals never reach the level of a congressional investigation. If so, the potential scandal, though covered in a news article, does not show up in our analyses. We construct samples using two proxies for the visibility of the scandals: (1) *High/Low Media Coverage* and (2) *Senator/Representative*.

The first proxy is the relative level of media coverage of the scandal. A firm is categorized as *High Media Coverage* (*Low Media Coverage*) if it is connected to scandal-tainted congresspersons that are covered in an above-sample median (below-sample median) number of total Factiva news articles in the 12-month period following the first-report date. A firm's Factiva news article count in year *t* is the count of all news articles published regarding the scandals to which firm *i* is connected in year *t*. Under the presumption that customers, suppliers, and financiers are more likely to learn of scandals that receive greater media coverage, we conjecture that firms

in the *High Media Coverage* sample that are connected to scandal-tainted congresspersons will experience a more pronounced negative valuation effect if the scandal-tainted congressperson remains in office following the scandal.

The second proxy for scandal visibility is based on whether the connected congressperson is a member of the Senate or the House of Representatives. A firm is categorized as *Senator* (*Representative*) if it is connected to a scandal-tainted congressperson who is a senator (representative) in the year of the first scandal in which the firm is connected to a scandal-tainted congressperson. Taking into consideration that there are 100 senators versus 435 representatives, as well as the length of their respective terms (six years for senators and two years for representatives), senators are likely to be more visible than representatives (see, e.g., Akey (2015), Akey and Lewellen (2017)). Under the presumption that scandals involving senators are more likely to be learned of by customers, suppliers, and financiers, we conjecture that firms in the senator sample will experience a more pronounced negative valuation consequence if the scandal-tainted congressperson remains in office following the scandal.

We re-estimate equation (2) using the level of media coverage and the office of the congressperson to construct the samples. We use *First Stay Scandal*$_{i,t}$ and *First Non-stay Scandal*$_{i,t}$ as the variables of interest. The results are reported in Table 6. Column 1 of Table 6 provides results for the *High Media Coverage* sample. After controlling for other factors and fixed effects, the coefficient of *First Stay Scandal*$_{i,t}$ is -0.070 (p-value < 0.01). This coefficient represents a 7.0% relative decline in Q for firms in the *High Media Coverage* sample following a *First Stay Scandal*$_{i,t}$. The coefficient of *First Non-stay Scandal*$_{i,t}$ is 0.023 (p-value = 0.41). Column 2 presents results for the *Low Media Coverage* sample. The coefficient of *First Stay Scandal*$_{i,t}$ is -0.034 (p-value = 0.08), and the coefficient of *First Non-stay Scandal*$_{i,t}$ is -0.028 (p-value = 0.16). In the *Low Media*

Coverage sample, the difference between the coefficient of *First Stay Scandal*$_{i,t}$ and *First Non-stay Scandal*$_{i,t}$ of -0.006 is less pronounced than the difference of -0.093 in the *High Media Coverage* sample.

Column 3 of Table 6 gives results for the *Senator* sample. Both the coefficients of *First Stay Scandal*$_{i,t}$ and *First Non-stay Scandal*$_{i,t}$ are negative and statistically significant. They are -0.091 (p-value < 0.01) and -0.050 (p-value = 0.05), respectively. The coefficient of *First Stay Scandal*$_{i,t}$ represents a 9.1% decline in Q for firms in the *Senator* sample following a *First Stay Scandal*. Column 4 of Table 6 gives the results for the *Representative* sample. Neither the coefficient of *First Stay Scandal*$_{i,t}$ nor of *First Non-stay Scandal*$_{i,t}$ is statistically different from zero (p-values = 0.26 and 0.86). In the *Representative* sample, the difference between the coefficients of *First Stay Scandal*$_{i,t}$ and *First Non-stay Scandal*$_{i,t}$ of -0.025 is less pronounced than the difference of -0.041 in the *Senator* sample.

The results in Table 6 serve as additional evidence that results are due to something beyond a broken political tie. They are consistent with the conjecture that scandals are more detrimental to the connected firms' market values when the firm's customers, suppliers and financiers are more likely to learn about them.

E. Event Study of Stock Returns

To further investigate the correlation between connected firms' valuation and their connections to scandal-tainted congresspersons, we conduct event studies that investigate the CAR of firms connected to scandal-tainted congresspersons around the first-report date. Specifically, we employ the market model with parameters estimated over the interval of 255 trading days ending 126 trading days prior to the event and using the value-weighted market index to examine the CAR of firms connected to scandal-tainted congresspersons. We require a minimum of 40

observations during the estimation interval to include the firm in the analysis. Because the day on which the rumor of the scandal begins to circulate is unknown, and because the seriousness of a scandal may take some time to be fully recognized, we examine stock returns for the one-month interval (i.e., 21 trading days) surrounding the first-report date.[11] It is important to note that the average elapsed time between the first-report date and the first consequence date is 83 days such that the question of whether the misconduct will rise to the level of investigation by a congressional committee is unknown at the first-report date. Unlike an earnings release or a dividend omission, for example, the news revelation at the first-report date may be partially known in advance, and/or an investigation may never materialize. Thus, the valuation effect at the first-report date may be muted.

The results are reported in Table 7. Each column of Table 7 indicates samples based on scandal type, whether the scandal received high or low media coverage, and whether the congressperson was a senator or a representative. The results in the panels are grouped according to whether the congressperson remained in office (*Stay*) or resigned (*Non-stay*), and all CARs are scaled by 100. The CAR for the full *Stay* sample, as shown in column 1 of Panel A, is -0.290% (p-value < 0.01). Considering that the average market capitalization of firms in the *Stay* sample is $39.1 billion, the -0.290% CAR translates to a loss of $113.4 million. In columns 2–5, the CARs for the *Business*, *Crime*, *Ethics*, and *Sexual Harassment* scandal types are reported. Each CAR is negative, and two of the four are statistically significant at the 0.05 level or better. They are -0.243% (p-value = 0.01), -0.413 (p-value = 0.28), -0.269 (p-value = 0.01), and -0.316 (p-value = 0.15). In columns 6 and 7, the CARs for the scandal characteristics of *High Media Coverage* and

[11] The results of the event study are qualitatively similar when we calculate the CAR using three-day, five-day, and eleven-day event windows around the first-report date of the scandal.

Senator are reported. Both are negative and significant at the 0.01 level. They are -0.393% (p-value < 0.01) and -0.270% (p-value = 0.01), respectively.

Panel B of Table 7 reports the results using the *Non-stay* sample. The CAR for the full *Non-stay* sample, as shown in column 1, is -0.076% and not statistically different from zero (p–value = 0.54). Similarly, in columns 2–7, albeit negative, none of the CARs for the scandal type, level of media coverage, or office of the congressperson is statistically significant. Compared with the CARs reported in Panel A, the results indicate that the negative economic consequences due to connections to a scandal-tainted congressperson with an outcome of *Stay* are worse than scandals with an outcome of *Non-stay*, indicating that the decline in connected firm value is not due entirely to a broken tie, but to adverse economic consequences resulting from a reputational spillover effect from the scandal-tainted congressperson to the connected firms. Panel A of Figure 2 plots the CAR for the full sample, and Panel B of Figure 2 plots the CARs for the Stay and Non-stay subsamples.

5. Operating and Financing Prospects of Connected Firms

The results in Tables 3 and 4 show that there is a negative relation between a firm's equity value and whether a congressperson to whom the firm is connected through a PAC contribution is involved in a scandal. The results in Tables 4 and 5 further show that the drop in the firm's equity value is more severe when the congressperson remains in office following the report of the scandal. Table 6 shows that the drop in a firm's equity value is more severe when the scandals are covered more by the media or involve more visible politicians. These results could come about because of the loss in the largesse that a political connection confers upon the connected firm or because the scandal causes customers, suppliers and financiers to back-away from the connected firm, which can happen when a firm's damaged reputation affects employee and customer loyalty, leading to

the loss of both human capital and a loss of sales revenue (Argenti and Druckenmiller (2004)). The fact that the loss in firm value is more severe when the congressperson to whom the firm is connected remains in office points in the direction of the second possibility.

To investigate that possibility more directly, we examine three variables that measure the future fundamental operating and financing prospects of connected firms: (1) *Sales Growth*$_{i,t}$, calculated as sales of firm *i* in year *t* divided by sales of firm *i* in year *t*-1; (2) *Net Profit Margin*$_{i,t}$, calculated as income of firm *i* before extraordinary items in year *t* divided by sales of firm *i* in year *t*; and (3) *Cost of Debt*$_{i,t}$, calculated as total interest and related expense of firm *i* during year *t*. Sales growth reflects the effect of the connection on the firm's customers; net profit margin captures the net effect of customers and suppliers; and cost of debt is a proxy for cost of capital. Adverse changes in any of these will negatively affect the firm's equity value. We are, as always, assessing those relative to firms connected to congresspersons who are not involved in scandals during the time interval covered by our analysis.

To undertake this analysis, we estimate regressions of the form in equation (2) with dependent variables of sales growth, net profit margin, and cost of debt. The results are reported in Table 8. Columns 1 and 2 of Table 8 present the estimated coefficients of equation (2), where y_{it} is the sales growth of firm *i* in year *t*. In column 1, the coefficient of *First Scandal*$_{i,t}$ is -0.024 (p-value < 0.01). This estimate indicates that, following the first instance in which a firm is connected to a congressperson involved in a scandal, the firm experiences a 2.4% relative decline in sales growth. In column 2, the coefficient of *First Stay Scandal*$_{i,t}$ is also negative and significant at -0.025 (p-value < 0.01) while the coefficient of *First Non-stay Scandal*$_{i,t}$ is negative and not significant at -0.007 (p-value = 0.40).

Columns 3 and 4 of Table 8 present the estimated coefficients of equation (2) where $y_{i,t}$ is the net profit margin of firm *i* in year *t*. In column 3, the coefficient of *First Scandal*$_{i,t}$ is -0.072 (p-value = 0.02). This estimate indicates that following the first instance in which a firm is connected to a congressperson involved in a scandal, the firm experiences a 7.2% relative decline in net profit margin. In column 4, the coefficient of *First Stay Scandal*$_{i,t}$ is also negative and significant at -0.072 (p-value = 0.01), while the coefficient of *First Non-stay Scandal*$_{i,t}$ is negative and not significant at -0.026 (p-value = 0.39).

Columns 5 and 6 of Table 8 give the coefficients of equation (2) when $y_{i,t}$ is the cost of debt of firm *i* in year *t*. In column 5, the coefficient of *First Scandal*$_{i,t}$ is 0.185 (p-value < 0.01). This estimate indicates that in the first instance in which a firm is connected to a congressperson involved in a scandal during the period of our analysis, the firm experiences an 18.5% relative increase in the cost of debt. In column 6, the coefficients of *First Stay Scandal*$_{i,t}$ and *First Non-stay Scandal*$_{i,t}$ are both positive and significant. But, at 0.193 (p-value < 0.01), the coefficient of *First Stay Scandal*$_{i,t}$ is more than twice the level of the coefficient of *First Non-stay Scandal*$_{i,t}$, which is 0.083 (p-value = 0.05).

Thus, the regressions reported in Table 8 show that a firm's sales growth rate and the net profit margin fall, and the cost of debt increases when a firm is connected to a congressperson who is involved in a scandal. Further, the drops in sales growth rate and net profit margin are greater when the congressperson remains in office following the scandal. As regards cost of debt, the increase is greater when the congressperson remains in office following the scandal, albeit regardless of whether the congressperson remains in office or steps down, the relative increase is significantly different from zero.

In general, the results of the regressions reported in Table 8 support the idea that firms connected to scandal-tainted congresspersons experience a reputational spillover effect from the scandal-tainted congressperson that flows from customers, suppliers, and financiers who pull away from firms connected to scandal-tainted congresspersons. The results indicate that the negative economic consequences are not simply due to broken political ties, but more pervasive subsequent declines in operating and financing prospects for firms connected to congresspersons involved in scandals, presumably due to a reputational spillover effect. We test this directly in the next section.

6. Firm Reputation, First Scandal Connection, and Scandal Outcome

Thus far, our evidence of a reputational spillover has been indirect, i.e., evidence consistent with a reputational penalty. Specifically, we have shown that: 1) there is a drop in the connected firm's equity value subsequent to a political scandal, 2) this drop in the firm's equity value is more severe when the congressperson remains in office following the report of the scandal, and 3) political scandals cause customers, suppliers, and financiers to edge-away from the connected firm, which can lead to the loss of both human capital and sales (Argenti and Druckenmiller (2004)).

Notwithstanding the fact that reputation is a somewhat abstract and difficult concept to measure, we attempt to test the impact of political scandals on connected firm reputation more directly through a proxy of reputation. To this end, we use *Fortune's* "Most Admired Companies" (MAC) reputation scores[12] to directly test the impact of political scandals on connected firm reputation. *Fortune* generates its MAC reputation scores using annual survey questionnaires sent to approximately 15,000 senior executives, outside directors, and industry analysts. The firms included in the survey come from the *Fortune 1000* listing and the *Global 500* listing, must have at least $10 billion in revenue, and rank among the largest by revenue within their industry. Each

[12] Results using rankings of *Fortune's* "Most Admired Companies" are qualitatively similar.

firm is rated from 1 to 10 on nine attributes, and the overall corporate reputation score is the average of these attribute scores. The firm with the highest (lowest) MAC reputation score each year is the most (least) reputable.[13] Firms not included in *Fortune's* MAC lists are dropped from the sample for this analysis.

Following Gormley and Matsa (2011), we use a multiple event stacked difference-in-differences methodology to examine the difference in the change in *Score* from the ten years before the scandal to the ten years after the year of the first media report. Using *Ln(Score)* as the key dependent variable of interest, we estimate the following model:

$$Ln(Score)_{i,t} = \alpha_i + \alpha_t + \gamma X_{i,t} + \delta First\ Scandal_{i,t} + \in_{i,t} \quad (3)$$

where *i* indexes firms, *t* indexes years, $Ln(Score)_{i,t}$ is the natural log of *Fortune's* MAC reputation score for firm i in year t, α_i and α_t are firm-by-cohort and year-by-cohort fixed effects, $X_{i,t}$ are control variables, and $\in_{i,t}$ is an error term. The independent variables of interest are $First\ Scandal_{i,t}$, $First\ Stay\ Scandal_{i,t}$, and $First\ Non\text{-}stay\ Scandal_{i,t}$. The coefficient of $First\ Scandal_{i,t}$, δ, estimates the effect of a firm's first scandal connection on the change in $Ln(Score)_{i,t}$ from before to after the year of the first scandal in which firm *i* is connected to the scandal-tainted congressperson. The coefficients of $First\ Stay\ Scandal_{i,t}$ and $First\ Non\text{-}stay\ Scandal_{i,t}$ have similar interpretations and refer to scandals in which the congressperson stays in office or steps down from office, respectively.

Table 9 presents the results of this analysis. In column 1, the coefficient of $First\ Scandal_{i,t}$ is -0.006 (p-value = 0.64). This result indicates that relative to firms connected to a congressperson who is not scandal-tainted during our sample period, the average firm connected to a scandal-tainted congressperson is not associated with a significant change in *Score* following the first-

[13] More details regarding *Fortune's* MAC reputation scores and methodology can be found here: https://www.kornferry.com/insights/this-week-in-leadership/fortune-worlds-most-admired-companies-2022. Also see Cheng et al. (2017).

report date of the scandal. Further, the coefficients of *First Stay Scandal*$_{i,t}$ in column 2 and *First Non-stay Scandal*$_{i,t}$ in column 3 are -0.028 (p-value = 0.05) and 0.001 (p-value = 0.95), respectively. These results translate to a 2.8% decline in *Score* for firms connected to a scandal-tainted congressperson who does not step down from office following the first-report date of the scandal. In contrast, firms connected to a scandal-tainted congressperson who steps down experience an insignificant change in *Score* following the first-report date of the scandal. Column 4 presents the results of including *First Stay Scandal*$_{i,t}$ and *First Non-stay Scandal*$_{i,t}$ in a single regression. The coefficient of *First Stay Scandal*$_{i,t}$ is -0.030 (p-value = 0.04). The coefficient of *First Non-stay Scandal*$_{i,t}$ is 0.007 (p-value = 0.55). This result implies a 3.0% decline in *Score* for a firm connected to a scandal-tainted congressperson who does not step down from office following the first-report date of the scandal.

The results in Table 9 provide direct evidence that firms connected to a scandal-tainted congressperson experience a reputational penalty. Moreover, the deleterious effect on a connected firm's reputation is most severe if the scandal-tainted congressperson remains in office following the first-report date of the scandal. This set of results provides evidence indicating that the negative valuation effect experienced by a firm connected to a scandal-tainted congressperson is, at least in part, due to a reputational spillover.

7. Connected Firms' Active Management of Political Contributions

Like congresspersons who distance themselves from donors who find themselves confronting legal difficulties, contributing firms may seek to distance themselves from scandal-tainted congresspersons. If they do so, such actions suggest that the management of firms recognize the negative economic fallout that can tarnish their firms when the congresspersons to whom the firm is connected become tarnished by scandal. To flesh out this possibility, we examine

post-scandal contributions received by such scandal-tainted congresspersons. Using the FEC congressperson-year-month panel data, we estimate the following logistic regression:

$$Pr\left(Reversal_{j,t} = 1 \mid Scandal_{j,t}\right) = \frac{exp\left(\beta_0 + \beta_1 Scandal_{j,t}\right)}{1 + exp\left(\beta_0 + \beta_1 Scandal_{j,t}\right)}$$

where *j* indexes congresspersons, *t* indexes year-months, and $Reversal_{j,t}$ is an indicator variable set to 1 if *congressperson j* has negative aggregate contributions (a net refund) in year-month *t* and is zero otherwise. Congresspersons can have negative aggregate contributions during a year-month if they refund more contributions than they receive. $Scandal_{i,t}$ is an indicator set to 1 if year *t* is equal to or later than the year-month in which congressperson *j* is initially connected to a scandal and is zero otherwise. The coefficient of $Scandal_{i,t}$, β_1, is the change in the log odds of $Reversal_{j,t}$ after a scandal. In each regression, we cluster observations at the congressperson level. The panel data set encompasses the years 1992-2018 and includes all US congresspersons whose campaigns received donations.

The results of equation (4) are reported in Panel A of Table 10. In the full sample, the coefficient of $Scandal_{j,t}$ is 0.854 (p-value < 0.01). The marginal effect of this estimate is 0.041, which is interpreted as the average change in the predicted probability of $Reversal_{j,t}$ following a scandal connection, holding all other variables constant. In other words, the predicted probability of congressperson *j* incurring a contribution reversal (a net refund) in year-month *t* increases by 4.1% following a scandal connection.

Column 2 reports the results of equation (4) for congresspersons who remain in office following the scandal. The coefficient of $Scandal_{i,t}$ is 0.692 (p-value < 0.01), and the marginal effect of this estimate is 0.033. Following a scandal, congressperson *j* experiences a 3.3% increase in the predicted probability of receiving a contribution reversal if they remain in office. Lastly,

column 3 reports the results for congresspersons that step down from office following the scandal. The coefficient of $Scandal_{i,t}$ is 1.824 (p-value < 0.01). The marginal effect of this estimate is 0.086, which represents an 8.6% increase in the predicted probability of incurring a contribution reversal following a scandal connection for congresspersons who step down from office.

Panel B of Table 10 reports the results of a slightly modified version of equation (4). In Panel B, the panel dataset is constructed at the congressperson-firm-year level. The results in Panel B are similar to those of Panel A.

In short, following the first-report date of a scandal, connected firms reduce or entirely discontinue contributions to the scandal-tainted congresspersons. The results indicate that scandal-tainted congresspersons experience an increased probability of contribution reversal following a scandal, especially if the involved congressperson steps down from office. The results of this section suggest that managers actively manage political contributions and are aware of the potential negative responses that can occur.

8. Robustness Analyses

A. Alternative Measures of Firm Valuation

In this section, we conduct a robustness check using alternative measures of firm valuation to investigate whether connections to a scandal-tainted congressperson can result in negative economic consequences for connected firms *beyond* the loss of a political tie. We do so by examining the impact of political scandals on the connected firms using three alternative measures of firm value: the firm's market-to-book value of equity ratio, dividends per share, and earnings per share. If firms connected to scandal-tainted congresspersons are associated with a relative decline in equity market value, they should also be associated with relative declines in market-to-book value of equity, dividends per share, and earnings per share. To be consistent with previous

results, the declines in connected firms' alternative measures of firm value should be greater if the scandal-tainted congressperson remains in office following the scandal. The regression models in this section follow the form of equation (2).

The results are reported in Table 11. Columns 1 and 2 present the coefficients of equation (2) where the dependent variable is the market-to-book value of equity of firm *i* at the end of year *t*. Similarly, columns 3 and 4 (5 and 6) examine dividends per share (earnings per share). The results show that first scandal connections, specifically those where the scandal-tainted congressperson does not step down from office, result in negative economic consequences for connected firms as measured by market-to-book value of equity, dividends per share, and earnings per share. In terms of economic significance, the coefficients of *First Stay Scandal*$_{i,t}$ in columns 2, 4, and 6 indicate that firms connected to scandal-tainted congresspersons with an outcome of *Stay* experience a relative annual decrease in market-to-book value of equity of 6.8%, dividends per share of $0.07, and earnings per share of $0.21 in the years following the first-report date. Each of these drops is statistically significant at the 0.05 level or better. Equally importantly, the coefficients of *First Non-stay Scandal*$_{i,t}$ are each negative, but none is significant at the 0.10 level. These results are consistent with a negative economic consequence that goes beyond the loss of a political connection and consistent with a reputational spillover effect.

B. Political Scandals and Reelection Outcomes

Thus far, the results provide evidence that *Stay* scandals result in a greater loss in market value for connected firms than *Non-stay* scandals. The reelection outcomes of congresspersons who seek reelection provide a further opportunity to consider the valuation effects of scandals. Arguably, the analysis of *Stay* scandals suggests that the reelection of scandal-tainted congresspersons should result in a negative valuation effect for firms connected to the reelected

congressperson. A counter-argument is that voters choose to reelect only congresspersons for whom the scandal is of little concern, and these modest concerns will have little effect on connected firms when the congressperson is reelected. To evaluate these possibilities, we separate the *Stay* scandals in the next election cycle according to the reelection outcome of the involved scandal-tainted congressperson. We then construct *First Stay Reelect Scandal* and *First Stay Non-Reelect Scandal* using the reelection outcome. Using these two variables, we examine the effect of the reelection outcome on the values of the connected firms.

The results are reported in Table 12. The effect of *First Stay Reelect Scandal* is more negative than that of both *First Stay Non-Reelect Scandal* and *First Non-stay Scandal*. These findings suggest that connected firms face a reputational spillover effect and the associated response from customers, suppliers, and financiers that give rise to a loss in market value. In terms of economic significance, the coefficient of *First Stay Reelect Scandal*$_{i,t}$ in column 4 indicates that firms connected to scandal-tainted congresspersons with an outcome of *Stay* and *Reelect* experience a relative decline in Q of 3.8% in comparison with a relative decline in Q of 0.9% for firms connected to scandal-tainted congresspersons with an outcome of *Stay* and *Non-Reelect* and with a relative decline in Q of 0.8% for firms connected to scandal-tainted congresspersons with an outcome of *Non-stay*. These findings suggest that when scandal-tainted congresspersons are reelected, connected firms have a more pronounced drop in value.

C. Heterogeneous Treatment Effects

Standard difference-in-difference regressions operate under the assumption that the treatment effects are constant across groups and time. This assumption is often violated when the difference-in-differences regression contains heterogeneous (staggered) treatment effects. Recent studies, such as Callaway and Sant'Anna (2021) and Goodman-Bacon (2021), show that

coefficients resulting from difference-in-differences models with both a heterogeneous treatment and a combination of group and period fixed effects may be biased (de Chaisemartin and D'Haultfoeuille (2020), Borusyak, Jaravel, and Spiess (2021), Sun and Abraham (2021), Athey and Imbens (2022), and de Chaisemartin and D'Haultfoeuille (2022)).

Under the parallel trends assumption, the difference-in-differences estimator is the weighted average of the treatment effect in each group and time period. The sum of the weights always equals 1.00, but some weights may be negative. The result can be an overall negative average treatment effect when, in fact, the majority of group and time treatment effects are estimated to be positive. This phenomenon only occurs when treatment effects are heterogeneous, which could be the case in this study when negative weights arise and the already-treated firms are part of the control group.

To examine the possibility of such a bias in our difference-in-differences estimates, we employ the Sun and Abraham (2021) fixed-effect (henceforth, FE) estimator, which is free of contamination and is more robust to treatment effects heterogeneity than standard staggered panel regressions. Figure 3 plots the FE estimates of a model similar to equation (2) using this alternative estimator proposed by Sun and Abraham (2021). The initial sample includes all publicly-listed US firms that made contributions to a US congressperson through its PAC and were connected to a congressional political scandal at some point between 1992 and 2018. To be included in the final model and figure, firms have at least half (at least 5) of the observations in the 10-year period. Period -1 is used as the reference point. Leads and lags are shown as two separate lines (as recommended by Borusyak, Jaravel, and Spiess (2021)), and the 90% confidence levels are plotted using the shaded red and blue regions. The model does not include firm control variables to ensure that we estimate a precise average treatment effect.

The results of Figure 3 provide evidence that the main results of this study are not biased due to treatment effect heterogeneity. In other words, the plotted average causal treatment effect is almost identical to the coefficient estimate of *First Scandal*$_{i,t}$, -0.043 (p-value < 0.01), in Table 4. Notably, the plotted FE estimates also provide clear evidence that the parallel trends assumption of our staggered difference in difference model is valid due to the insignificance of the FE estimates before treatment. Overall, we can confidently assume that the results of this study are not contaminated with the documented bias of difference-in-differences models with both a heterogeneous treatment and a combination of group and period fixed effects.

9. Conclusion

Using scandals occurring between 1992 and 2018 involving US congresspersons, publicly-listed US firms whose PAC contributed to a scandal-tainted congressperson are associated with a significant decline in Q during the year of the scandal and the subsequent years relative to firms that contributed to congresspersons not involved in scandals. Further, following the first media report of a congressperson's misconduct, firms connected to the congressperson, as measured by the firm's PAC contribution to the congressperson's campaigns, also experience a reduction in sales growth and net profit margin and an increase in the cost of debt all measured relative to firms connected to congresspersons not involved in scandals. Moreover, connections to scandal-tainted congresspersons result in a greater decline in the market value of connected firms when the involved congressperson *does not* step down from office following the scandal and when the scandal-tainted congressperson and the scandal receive greater media attention. Notably, the firms connected to a scandal-tainted congressperson who does not step down from office not only experience an indirect reputational penalty through stakeholders including customers, suppliers, and financiers, but they also experience a direct reputational penalty as measured by *Fortune's*

MAC reputation scores. Finally, we find that the connected firms substantially reduce their contributions to the scandal-tainted congresspersons following the first-report date of the scandal.

Collectively, these findings support the notion that the decline in firm value is not simply due to a broken political tie but also to a reputational spillover effect from the scandal-tainted congresspersons to the connected firms and, as a result, a negative shock to the operating and financing prospects of the connected firms. We interpret our findings to indicate that there exists an undocumented potential cost associated with corporate political connections: when a politician is involved in a scandal, the connected firms experience a reputational spillover effect that arises from the negative reactions by customers, suppliers, and financiers. These spillovers show up as a loss in firm value that occurs over the time period subsequent to the disclosure of the scandal. Thereby, our study helps to at least partially resolve the long-debated question as to why there is so little corporate money in US politics (Ansolabehere et al. (2003)).

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Appendix A.1. Examples of Scandals

This appendix presents examples of scandals. *Scandal Type* is a label assigned by the *Legislator Misconduct Database* at GovTrack.us. *First-Report Date* is the date of the first news article in Factiva regarding the scandal. *Stays in Office* describes whether the scandal-tainted congresspersons stay in office or step down from office following the scandal. *Contributing Firms* lists examples of large firms that contributed through a PAC to the congressperson's campaign as reported by FEC. *Media Citations* are obtained from Factiva.

Congressperson	Scandal Type	First-Report Date	Stays in Office	Contributing Firms	Media Citation
Ted Stevens (Representative)	Business: Failing to Properly Report Gifts	5/29/2007	Yes	Microsoft Corp., Honeywell International, Exxon Mobil Corp., Chevron Corp., and Waste Management	"Investigators eye remodeling at home of Sen. Ted Stevens," Associate Press Newswire
Chaka Fattah (Representative)	Business: Racketeering and Money Laundering	10/11/2013	No	Comcast Corp., Lockheed Martin Corp., Raytheon Co., AT&T Inc., Boeing Co., and Northrup Grumman Corp.	"FBI investigating Fattah for 7 years," Philadelphia Business Journal Online
Trey Radel (Senator)	Crime: Possession of Cocaine	11/19/2013	No	Pfizer Inc., Caterpillar Inc., Home Depot Inc., NextEra Energy Inc., and Honeywell International	"Florida Congressman Trey Radel charged with cocaine possession," Associated Press Newswires
Corrine Brown (Representative)	Business: Fraudulent Activity	3/4/2016	Yes	Union Pacific Corp., CSX Corp., Arcbest Corp., AT&T Inc., and Cubic Corp.	"House ethics panel investigating Democrat Corrine Brown," Reuters News
Chris Collins (Representative)	Business: Insider Trading	4/26/2017	No	AT&T Inc., Ford Motor Co., General Electric Co., and Boeing Co.	"Collins's ties to Australian pharma company under scrutiny," Hotline
Al Franken (Senator)	Sexual Harassment: Unwanted Groping	11/16/2017	No	General Motors Co., International Paper, T-Mobile USA Inc., Cisco Systems Inc., and Sprint Corp.	"Al Franken accused of kissing, groping woman," Market Watch

Appendix A.2. Variable Definitions

This appendix presents variable definitions and their sources. Panel A presents the scandal characteristics. Panel B presents congressperson outcomes and characteristics. Panel C gives firm characteristics. LMD/Govtrack.us refers to the *Legislative Misconduct Database* at Govtrack.us. FEC refers to Federal Election Commission.

Variable	Definition	Source
Panel A. Scandal Characteristics		
Business	An indicator that is set to 1 if the scandal is related to or involves money, and zero otherwise.	LMD
Crime	An indicator that is set to 1 if the scandal is related to tax evasion, murder, fraud, and other crimes (besides corruption and sexual harassment and abuse), and zero otherwise.	LMD
Ethics	An indicator that is set to 1 if the scandal is related to a violation of congressional rules that is not a crime, and zero otherwise.	LMD
Sexual Harassment	An indicator that is set to 1 if the scandal is related to sexual harassment or abuse, and zero otherwise.	LMD
High Media Coverage	An indicator that is set to 1 if a scandal has an above-median number of Factiva newspaper articles, and zero otherwise.	Factiva
Scandal Year	An indicator that is set to 1 if a firm is connected to at least one scandal-tainted congressperson in year *t*, and zero otherwise.	FEC/Factiva
Number of Scandals	The number of scandals to which a firm is connected to the scandal-tainted congresspersons in year *t*. Winsorized at 1% & 99%.	FEC/Factiva
First Scandal	An indicator that is set to 1 beginning in the year of the first scandal in which the firm is connected to the scandal-tainted congressperson, and zero otherwise.	FEC/Factiva
First Stay Scandal	An indicator that is set to 1 beginning in the year of the first scandal in which the firm is connected to the scandal-tainted congressperson who remains in office for the rest of his/her term, and zero otherwise.	FEC/Factiva
First Non-stay Scandal	An indicator that is set to 1 beginning in the year of the first scandal in which the firm is connected to the scandal-tainted congressperson who steps down from office before his/her term is completed, and zero otherwise.	FEC/Factiva
Scandal	An indicator that is set to 1 beginning in the first month that a congressperson is connected to a scandal, and zero otherwise.	FEC/Factiva
Panel B. Congressperson Outcomes and Characteristics		
Stay	An indicator that is set to 1 if the congressperson involved in the scandal stays in office until the end of his/her term, and zero otherwise. Congresspersons in this category do not resign nor get expelled from office.	Factiva/LMD
Non-stay	An indicator that is set to 1 if the congressperson involved in the scandal resigns or is expelled from office before the end of his/her term, and zero otherwise.	Factiva/LMD
Senator/Representative	An indicator that is set to 1 if the congressperson is a senator (Representative), and zero otherwise.	FEC/LMD

Appendix A.2. Continued

Panel B. Continued		
Reelect	An indicator that is set to 1 if the congressperson is reelected in the next election cycle, and zero otherwise.	Congress.gov
Non-Reelect	An indicator that is set to 1 if the congressperson is not reelected in the next election cycle, and zero otherwise.	Congress.gov
Reversal	An indicator that is set to 1 if congressperson *j* has negative total contributions (a net refund) in year-month *t*, and zero otherwise	FEC

Panel C. Firm Characteristics		
FEC Contributions	Total firm contributions to all congresspersons in year *t*. Winsorized at 1% & 99%.	FEC
Tobin's Q	$(AT_{i,t} - SEQ_{i,t} + PRCCC_{i,t} * CSHO_{i,t})/AT_{i,t}$, total assets minus book equity plus stock price times shares outstanding all divided by total assets at the end of year *t*.	Compustat
Market-to-Book Value of Equity (MTB)	$(PRCCC_{i,t} * CSHO_{i,t})/SEQ_{i,t}$, the product of stock price and shares outstanding in year *t* divided by book equity at the end of year *t*.	Compustat
Dividends per Share	$DVPSP_{i,t}$, dividends per share in calendar year *t*.	Compustat
Earnings per Share	$EPSPI_{i,t}$, earnings per share in year *t* - including extraordinary items.	Compustat
Sales Growth	$Ln(SALE_{i,t})/SALE_{i,t-1}$), the natural log of sales during year *t* divided by sales in year *t* minus 1.	Compustat
Net Profit Margin	The natural log of $IB_{i,t}/SALE_{i,t}$, income before extraordinary items in year *t* divided by sales in year *t*.	Compustat
Cost of Debt	The natural log of $XINT_{i,t}$, total interest and related expense in year *t*.	Compustat
Market Capitalization	$PRCCC_{i,t} * CSHO_{i,t}$, stock price in year *t* times shares outstanding at the end of year *t*. Winsorized at 1% & 99%.	Compustat
Firm Age	Year *t* minus the first year firm *i* appears in Compustat. Winsorized at 1% & 99%.	Compustat
Capital Expenditures	$CAPX_{i,t}/AT_{i,t}$, capital expenditures divided by total assets at the end of year *t*. Winsorized at 1% & 99%.	Compustat
Leverage	$(DLTT_{i,t} + DLC_{i,t})/AT_{i,t}$, long-term debt plus debt in current liabilities divided by total assets at the end of year *t*. Winsorized at 1% & 99%.	Compustat
Return on Assets	$OIBDP_{i,t}/AT_{i,t}$, operating income before depreciation divided by total assets at the end of year *t*. Winsorized at 1% & 99%.	Compustat
Tax	$TXT_{i,t}/EBIT_{i,t}$, income taxes divided by earnings before interest and taxes in year *t*. Winsorized at 1% & 99%.	Compustat
Research and Development Expense (R&D)	$XRD_{i,t}/AT_{i,t}$, research and development expense divided by total assets at the end of year *t*. Winsorized at 1% & 99%.	Compustat
Firm Return Variance	$ReturnVariance_{i,t-36}$, stock return variance during the past 36 months as of year *t*. Winsorized at 1% & 99%.	CRSP
Dividends Indicator	An indicator variable that is set to 1 for a firm that pays dividends in year *t*, and zero otherwise.	Compustat
Score	The *Fortune's* "Most Admired Companies" reputation score for firm *i* in year *t*.	Fortune

Table 1. Congressperson and Scandal Summary Statistics

This table presents the descriptive statistics of the 172 instances of misconduct involving US congresspersons from both the Senate and the House of Representatives during the period of 1992-2018 as reported by the *Legislator Misconduct Database* at GovTrack.us. Type of Scandal refers to the category assigned by the *Legislator Misconduct Database*. The types of scandals are not mutually exclusive. If the scandal outcome is that the involved congressperson does not resign from office following the scandal and before the next election, we classify such congresspersons as *Stay*. A congressperson is classified as *Non-stay* if the scandal outcome is that he or she publicly announces resignation from office prior to the next election.

	Number of Scandals		
	Stay	Non-stay	Full Sample
Scandal Outcome			
Business	19	97	116
Crime	8	10	18
Ethics	11	91	102
Sexual Harassment	11	7	18
Type of Scandal			
Senate	3	12	15
House	32	125	157
Observations	35	137	172

Table 2. Summary Statistics

This table presents the descriptive statistics for the panel data set of firm-year observations for the period of 1990 - 2020 for all publicly-listed US firms that made contributions to a US congressperson through its PAC. Panel A displays the number of observations (N), mean, standard deviation (Std. Dev.), first quartile (Q1), and third quartile (Q3). Panel B displays the mean of variables in the *Stay vs. Nonstay* sample. All variables are defined in Appendix A.2. All control variables are winsorized at 1% and 99%.

Panel A. Full Sample

	N	Mean	Std. Dev.	Q1	Q3
FEC Contributions ($ thousands)	19,658	105.217	204.077	1.500	103.650
Scandal Year	19,658	0.220	0.414	0	0
Number of Scandals	19,658	0.465	1.189	0	0
First Scandal	19,658	0.574	0.494	0	1
First Stay Scandal	19,658	0.536	0.499	0	1
First Non-stay Scandal	19,658	0.366	0.482	0	1
Tobin's Q	19,658	1.731	1.560	1.074	1.847
MTB	19,658	2.955	53.814	1.285	3.270
Dividends per Share	19,658	0.801	2.178	0.000	1.200
Earnings per Share	19,609	1.905	2.854	0.670	3.050
Sales Growth	19,518	0.069	0.249	-0.013	0.139
Net Profit Margin	19,596	-0.034	4.555	0.024	0.112
Cost of Debt ($ millions)	17,034	349.469	1882.150	16.713	224.311
Market Capitalization ($ billions)	19,658	13.823	30.624	0.732	10.487
Firm Age	19,658	31.968	18.342	16.000	46.000
Capital Expenditures	18,108	0.052	0.048	0.019	0.072
Leverage	19,561	0.271	0.182	0.131	0.375
Return on Assets	19,277	0.117	0.083	0.063	0.162
Tax	18,949	0.210	0.343	0.138	0.324
R&D	19,658	0.015	0.032	0.000	0.014
Firm Return Variance	19,549	0.012	0.015	0.004	0.014
Dividends Indicator	19,658	0.734	0.442	0.000	1.000
Score	3,576	6.733	11.839	6.010	7.130

Table 2. Continued

Panel B. Stay vs. Nonstay Sample

	Mean	
	Stay	Non-stay
FEC Contributions ($ thousands)	140.835	178.263
Scandal Year	0.297	0.357
Number Of Scandals	0.632	0.787
Tobin's Q	1.77	1.85
Market-to-Book	3.237	3.278
Dividends Per Share	0.891	0.967
Earnings Per Share	2.158	2.29
Sales Growth	0.066	0.066
Net Profit Margin	0.029	0.054
Cost of Debt	416.301	510.904
Market Capitalization ($ billions)	17.883	22.172
Firm Age	34.944	35.716
Capital Expenditures	0.052	0.052
Leverage	0.275	0.274
Return on Assets	0.123	0.127
Tax	0.213	0.215
Research and Development Expense	0.015	0.017
Firm Return Variance	0.011	0.011
Dividends Indicator	0.769	0.794
Score	6.795	6.835
Observations	14,359	10,883

Table 3. Panel Regressions of Firm Value and Political Scandals

This table presents the results of the following firm-year panel regression: $Ln(Tobin's\ Q)_{i,t} = \alpha_i + \alpha_t + \gamma X_{i,t} + \delta Scandal_{i,t} + \epsilon_{i,t}$. The sample includes all publicly-listed US firms that made contributions to a US congressperson through its PAC during the period of 1992-2018. The dependent variable in each column is *Ln(Tobin's Q)*, abbreviated in the table as *Ln(Q)*. *Scandal Year* is an indicator variable that is set to 1 if firm *i* has been connected to at least one scandal-tainted congressperson in year *t*, and zero otherwise. *Number of Scandals* is a categorical variable equal to the number of scandal-tainted congresspersons to whom firm *i* is connected in year *t*. The independent variable of interest in columns 1 and 2 is *Scandal Year*. The independent variable of interest in columns 3 and 4 is *Number of Scandals*. Each regression includes firm and year fixed effects (α_i, α_t) and the following control variables ($X_{i,t}$): *FEC Contributions*, *Ln(Market Capitalization)*, *Ln(Firm Age)*, *Capital Expenditures*, *Leverage*, *Return on Assets*, *Tax*, *R&D*, *Firm Return Variance*, and *Dividends Indicator*. All variables are defined in Appendix A.2. Standard errors are clustered at the firm level. The p-values are reported in parentheses. ***, **, and * indicate significance at 1%, 5%, and 10%, respectively.

	(1)	(2)	(3)	(4)
Dependent Variable	Ln(Q)	Ln(Q)	Ln(Q)	Ln(Q)
Scandal Year	-0.039***	-0.026***		
	[0.00]	[0.00]		
Number Of Scandals			-0.015***	-0.006**
			[0.00]	[0.02]
FEC Contributions		-0.236***		-0.239***
		[0.00]		[0.00]
Ln(Market Capitalization)		0.190***		0.190***
		[0.00]		[0.00]
Ln(Firm Age)		-0.212***		-0.213***
		[0.00]		[0.00]
Capital Expenditures		0.674***		0.674***
		[0.00]		[0.00]
Leverage		0.005		0.006
		[0.91]		[0.90]
Return on Assets		1.759***		1.759***
		[0.00]		[0.00]
Tax		0.010		0.010
		[0.15]		[0.15]
R&D		3.014***		3.018***
		[0.00]		[0.00]
Firm Return Variance		3.593***		3.593***
		[0.00]		[0.00]
Dividends Indicator		-0.075***		-0.075***
		[0.00]		[0.00]
Firm FE	YES	YES	YES	YES
Year FE	YES	YES	YES	YES
No. of Obs.	19,658	17,405	19,658	17,405
Adj. R^2	0.647	0.775	0.647	0.775

Table 4. Difference-in-Differences Analysis of Firm Value, First Scandal Connection, and Scandal Outcome
This table presents the results of the following multiple event and multiple treatment group difference-in-differences regression: $Ln(Tobin's\ Q)_{i,t} = \alpha_i + \alpha_t + \gamma X_{i,t} + \delta\ First\ Scandal_{i,t} + \epsilon_{i,t}$. The sample includes all publicly-listed US firms that made contributions to a US congressperson through its PAC during the period of 1992-2018. The dependent variable in each column is *Ln(Tobin's Q)*, abbreviated in the table as *Ln(*Q*)*. *First Scandal* is an indicator variable that is set to 1 if firm *i* is connected to a scandal-tainted congressperson in year *t* and remains 1 for all years following the scandal year, and is zero otherwise. *First Stay Scandal* is an indicator variable that is set to 1 if firm *i* is connected to a scandal-tainted congressperson with an outcome of *Stay* in year *t* and remains 1 for all years following the scandal year, and is zero otherwise. *First Non-stay Scandal* is an indicator variable that is set to 1 if firm *i* is connected to a scandal-tainted congressperson with an outcome of *Non-stay* in year *t* and remains 1 for all years following the scandal year, and is zero otherwise. Each regression includes firm and year fixed effects (α_i, α_t): *FEC Contributions*, *Ln(Market Capitalization)*, *Ln(Firm Age)*, *Capital Expenditures*, *Leverage*, *Return on Assets*, *Tax*, *R&D*, *Firm Return Variance*, and *Dividends Indicator*. All variables are defined in Appendix A.2. Standard errors are clustered at the firm level. The p-values are reported in parentheses. ***, **, and * indicate significance at 1%, 5%, and 10%, respectively.

	(1)	(2)	(3)	(4)
Dependent Variable	Ln(Q)	Ln(Q)	Ln(Q)	Ln(Q)
First Scandal	-0.043***			
	[0.00]			
First Stay Scandal		-0.042***		-0.040***
		[0.01]		[0.01]
First Non-stay Scandal			-0.017	-0.011
			[0.29]	[0.51]
Control Variables	YES	YES	YES	YES
Firm FE	YES	YES	YES	YES
Year FE	YES	YES	YES	YES
No. of Obs.	17,405	17,405	17,405	17,405
Adj. R^2	0.775	0.775	0.775	0.775

Table 5. Firm Value and Political Scandals by Type of Scandal

This table presents the results of the following multiple event and multiple treatment group difference-in-differences regression: $Ln(Tobin's\ Q)_{i,t} = \alpha_i + \alpha_t + \gamma X_{i,t} + \delta_1 First\ Stay\ Scandal_{i,t} + \delta_2 First\ Leave\ Scandal_{i,t} \in_{i,t}$. The sample includes all publicly-listed US firms that made contributions to a US congressperson through its PAC during the period of 1992-2018. The dependent variable in each column is *Ln(Tobin's Q)*, abbreviated in the table as *Ln(*Q*)*. *First Stay Scandal* is an indicator variable that is set to 1 if firm *i* is connected to a scandal-tainted congressperson with an outcome of *Stay* in year *t* and remains 1 for all years following the scandal year, and is zero otherwise. *First Non-stay Scandal* is an indicator variable that is set to 1 if firm *i* is connected to a scandal-tainted congressperson with an outcome of *Non-stay* in year *t* and remains 1 for all years following the scandal year, and is zero otherwise. The samples are constructed based on the type of scandal of each firm's first scandal connection, and they are denoted above each column number. The samples in columns 1 and 2 are constructed based on business and non-business scandal connections. The samples in columns 3 and 4 are based on crime and non-crime scandal connections. The samples in columns 5 and 6 are based on ethics and non-ethics scandal connections. The samples in columns 7 and 8 are based on sexual harassment and non-sexual harassment scandal connections. Each regression includes firm and year fixed effects (α_i, α_t) and the following control variables ($X_{i,t}$) (: *FEC Contributions*, *Ln(Market Capitalization)*, *Ln(Firm Age)*, *Capital Expenditures*, *Leverage*, *Return on Assets*, *Tax*, *R&D*, *Firm Return Variance*, and *Dividends Indicator*. All variables are defined in Appendix A.2. Standard errors are clustered at the firm level. The p-values are reported in parentheses. ***, **, and * indicate significance at 1%, 5%, and 10%, respectively.

	Business	Non-Business	Crime	Non-Crime	Ethics	Non-Ethics	Sexual Harassment	Non-Sexual Harassment
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Dependent Variable	Ln(Q)	Ln(Q)	Ln(Q)	Ln(Q)	Ln(Q)	Ln(Q)	Ln(Q)	Ln(Q)
First Stay Scandal	-0.042**	-0.036	-0.100**	-0.029*	-0.037*	-0.058**	-0.068	-0.044***
	[0.03]	[0.20]	[0.01]	[0.08]	[0.07]	[0.02]	[0.13]	[0.01]
First Non-stay Scandal	-0.023	0.000	-0.014	-0.011	-0.040*	0.024	0.055	-0.021
	[0.20]	[0.99]	[0.80]	[0.51]	[0.06]	[0.33]	[0.14]	[0.22]
Control Variables	YES	YES	YES	YES	YES	YES	YES	YES
Firm FE	YES	YES	YES	YES	YES	YES	YES	YES
Year FE	YES	YES	YES	YES	YES	YES	YES	YES
No. of Obs.	13,932	6,999	4,958	15,973	12,524	8,407	5,040	15,891
Adj. R^2	0.774	0.761	0.741	0.782	0.776	0.762	0.767	0.770

Table 6. Firm Value and Political Scandals by Scandal Visibility

This table presents the results of the following multiple event and multiple treatment group difference-in-differences regression: $Ln(Tobin's\ Q)_{i,t} = \alpha_i + \alpha_t + \gamma X_{i,t} + \delta_1 First\ Stay\ Scandal_{i,t} + \delta_2 First\ Leave\ Scandal_{i,t} \in_{i,t}$. The sample includes all publicly-listed US firms that made contributions to a US congressperson through its PAC during the period of 1992-2018. The dependent variable in each column is *Ln(Tobin's* Q*)* abbreviated in the table as *Ln(*Q*)*. *First Stay Scandal* is an indicator variable that is set to 1 if firm *i* is connected to a scandal-tainted congressperson with an outcome of *Stay* in year *t* and remains 1 for all years following the scandal year and is zero otherwise. *First Non-stay Scandal* is an indicator variable that is set to 1 if firm *i* is connected to a scandal-tainted congressperson with an outcome of *Non-stay* in year *t* and remains 1 for all years following the scandal year, and is zero otherwise. The samples are constructed based on the scandal characteristic of each firm's first scandal connection, and they are denoted above each column number. The samples in columns 1 and 2 are constructed based on Factiva media coverage levels. The samples in columns 3 and 4 are based on senator and representative scandal connections. Each regression includes firm and year fixed effects (α_i, α_t) and the following control variables ($X_{i,t}$): *FEC Contributions, Ln(Market Capitalization), Ln(Firm Age), Capital Expenditures, Leverage, Return on Assets, Tax, R&D, Firm Return Variance,* and *Dividends Indicator*. All variables are defined in Appendix A.2. Standard errors are clustered at the firm level. The p-values are reported in parentheses. ***, **, and * indicate significance at 1%, 5%, and 10%, respectively.

	High Media Coverage	Low Media Coverage	Senator	Representative
	(1)	(2)	(3)	(4)
Dependent Variable	Ln(Q)	Ln(Q)	Ln(Q)	Ln(Q)
First Stay Scandal	-0.070***	-0.034*	-0.091***	-0.021
	[0.00]	[0.08]	[0.00]	[0.26]
First Non-stay Scandal	0.023	-0.028	-0.050**	0.004
	[0.41]	[0.16]	[0.05]	[0.86]
Control Variables	YES	YES	YES	YES
Firm FE	YES	YES	YES	YES
Year FE	YES	YES	YES	YES
No. of Obs.	8,131	12,800	9,791	11,140
Adj. R^2	0.771	0.770	0.789	0.753

Table 7. Event Study of Stock Returns

This table presents the cumulative abnormal returns (CARs) of a market model for the (-10, +10) event window around the first-report date for all scandals and for various types and the visibility of scandals. Each CAR is scaled by 100. Day 0 is the date of the first instance in which a media outlet reports the scandal. We adopt a 255-trading day estimation window ending 126 trading days prior to the event date. For each stock, we require a minimum of 40 observations in the estimation window. All variables are defined in Appendix A.2. The p-values are reported in parentheses. ***, **, and * indicate significance at 1%, 5%, and 10%, respectively.

Panel A: Congressperson Stays in Office (*Stay* Sample)

	Full Sample	Business	Crime	Ethics	Sexual Harassment	High Media Coverage	Senator
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
CAR (%)	-0.290***	-0.243***	-0.413	-0.269***	-0.316	-0.393***	-0.270***
	[0.00]	[0.01]	[0.28]	[0.01]	[0.15]	[0.00]	[0.01]
No. of Obs.	6,579	5,605	379	4,495	938	4,181	4,069

Panel B: Congressperson Steps Down from Office (*Non-stay* Sample)

	Full Sample	Business	Crime	Ethics	Sexual Harassment	High Media Coverage	Senator
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
CAR (%)	-0.076	-0.209	-0.268	-0.139	-0.340	-0.041	-0.049
	[0.54]	[0.11]	[0.63]	[0.35]	[0.32]	[0.82]	[0.74]
No. of Obs.	2,426	2,079	126	1,706	373	1,421	1,597

Table 8. Political Scandals and Firm Operating and Financing Prospects

This table presents the results of the following multiple event and multiple treatment group difference-in-differences regression: $y_{i,t} = \alpha_i + \alpha_t + \gamma X_{i,t} + \delta First\ Scandal_{i,t} + \epsilon_{i,t}$. The sample includes all publicly-listed US firms that made contributions to a US congressperson through its PAC during the period of 1992-2018. The dependent variables are *Sales Growth*, *Net Profit Margin*, and *Cost of Debt*, respectively. *First Scandal* is an indicator variable that is set to 1 if firm *i* is connected to a scandal-tainted congressperson in year *t* and remains 1 for all years following the scandal year in the sample term and is zero otherwise. *First Stay Scandal* is an indicator variable that is set to 1 if firm *i* is connected to a scandal-tainted congressperson with an outcome of *Stay* in year *t* and remains 1 for all years following the scandal year and is zero otherwise. *First Non-stay Scandal* is an indicator variable that is set to 1 if firm *i* is connected to a scandal-tainted congressperson with an outcome of *Non-stay* in year *t* and remains 1 for all years following the scandal year, and is zero otherwise. Each regression includes firm and year fixed effects (α_i, α_t) and the following control variables ($X_{i,t}$): *FEC Contributions, Ln(Market Capitalization), Ln(Firm Age), Capital Expenditures*, *Leverage*, *Return on Assets*, *Tax*, *R&D*, *Firm Return Variance*, and *Dividends Indicator*. All variables are defined in Appendix A.2. Standard errors are clustered at the firm level. The p-values are reported in parentheses. ***, **, and * indicate significance at 1%, 5%, and 10%, respectively.

	(1)	(2)	(3)	(4)	(5)	(6)
Dependent Variable	Sales Growth	Sales Growth	Net Profit Margin	Net Profit Margin	Cost of Debt	Cost of Debt
First Scandal	-0.024***		-0.072**		0.185***	
	[0.00]		[0.02]		[0.00]	
First Stay Scandal		-0.025***		-0.072**		0.193***
		[0.00]		[0.01]		[0.00]
First Non-stay Scandal		-0.007		-0.026		0.083**
		[0.40]		[0.39]		[0.05]
Control Variables	YES	YES	YES	YES	YES	YES
Firm FE	YES	YES	YES	YES	YES	YES
Year FE	YES	YES	YES	YES	YES	YES
No. of Obs.	17,373	17,373	14,888	14,888	15,992	15,992
Adj. R^2	0.178	0.178	0.629	0.629	0.911	0.911

Table 9. Stacked Difference-in-Differences Analysis of Firm Reputation, First Scandal Connection, and Scandal Outcome

This table presents the results of the following multiple event stacked difference-in-differences regression: $Ln(Score)_{i,t} = \alpha_i + \alpha_t + \gamma X_{i,t} + \delta First\ Scandal_{i,t} + \epsilon_{i,t}$. The sample includes all publicly-listed US firms included in *Fortune's* Most Admired Companies (MAC) lists during the period of 1990-2020. The dependent variable in each column is *Ln(Score)*, which is equal to the natural log of *Fortune's* MAC reputation score for firm *i* in year *t*. *First Scandal* is an indicator variable that is set to 1 if firm *i* is connected to a scandal-tainted congressperson in year *t* and remains 1 for all years following the scandal year and is zero otherwise. *First Stay Scandal* is an indicator variable that is set to 1 if firm *i* is connected to a scandal-tainted congressperson with an outcome of *Stay* in year *t* and remains 1 for all years following the scandal year and is zero otherwise. *First Non-stay Scandal* is an indicator variable that is set to 1 if firm *i* is connected to a scandal-tainted congressperson with an outcome of *Non-stay* in year *t* and remains 1 for all years following the scandal year, and is zero otherwise. Each regression includes firm-by-cohort and year-by-cohort fixed effects (α_i, α_t): *FEC Contributions*, *Ln(Market Capitalization)*, *Ln(Firm Age)*, *Capital Expenditures*, *Leverage*, *Return on Assets*, *Tax*, *R&D*, *Firm Return Variance*, and *Dividends Indicator*. All variables are defined in Appendix A.2. The p-values are reported in parentheses. ***, **, and * indicate significance at 1%, 5%, and 10%, respectively.

	(1)	(2)	(3)	(4)
Dependent Variable	Ln(Score)	Ln(Score)	Ln(Score)	Ln(Score)
First Scandal	-0.006			
	[0.64]			
First Stay Scandal		-0.028**		-0.030**
		[0.05]		[0.04]
First Non-stay Scandal			0.001	0.007
			[0.95]	[0.55]
Control Variables	YES	YES	YES	YES
Firm-cohort FE	YES	YES	YES	YES
Year-cohort FE	YES	YES	YES	YES
No. of Obs.	4,431	4,431	4,431	4,431
Adj. R^2	0.709	0.709	0.709	0.709

Table 10. Political Scandals and Active Management of Political Contributions

This table presents the results of the following logistic regression:

$Pr(Reversal_{j,t} = 1|Scandal_{j,t}) = \frac{exp(\beta_0+\beta_1 Scandal_{j,t})}{1+exp(\beta_0+\beta_1 Scandal_{j,t})}$. In Panel A, the panel data set encompasses the years 1992-2018 and includes all US congresspersons that received political contributions. The dependent variable for each column is Reversal, an indicator variable equal to one if congressperson *j* has negative total contributions (a net refund) in year-month *t*, and zero otherwise. The independent variable of interest for each column is Scandal. Scandal is an indicator variable that is set to 1 if a congressperson is involved in a scandal in year-month *t* and remains 1 for all year-months following the scandal year-month in the sample and is zero otherwise. Column 1 includes the full sample of scandal-tainted congresspersons. Column 2 is limited to the sample of congresspersons that stay in office following the scandal. Column 3 is limited to the sample of congresspersons who step down from office following the scandal. Panel B is identical, except the panel dataset is constructed at the politician-firm-year level. All variables are defined in Appendix A.2. Standard errors are clustered at the congressperson level. The p-values are reported in parentheses. ***, **, and * indicate significance at 1%, 5%, and 10%, respectively.

Panel A: Politician Level

	Full Sample	Stay	Non-stay
	(1)	(2)	(3)
Dependent Variable		Reversal	
Scandal	0.854***	0.692***	1.824***
	[0.00]	[0.00]	[0.00]
No. of Obs.	164,252	160,378	146,209

Panel B: Politician-Firm Level

	Full Sample	Stay	Non-stay
	(1)	(2)	(3)
Dependent Variable		Reversal	
Scandal	0.552***	0.456***	0.928***
	[0.00]	[0.00]	[0.00]
No. of Obs.	583,178	570,860	532,335

Table 11. Political Scandals and Alternative Measures of Firm Value

This table presents the results of the following multiple event and multiple treatment group difference-in-differences regression: $y_{i,t} = \alpha_i + \alpha_t + \gamma X_{i,t} + \delta First\ Scandal_{i,t} + \epsilon_{i,t}$. The sample includes all publicly-listed US firms that made contributions to a US congressperson through its PAC during the period of 1992-2018. The dependent variables are *Ln(MTB)*, *Dividends per Share*, and *Earnings per Share*, respectively. *First Scandal* is an indicator variable that is set to 1 if firm *i* is connected to a scandal-tainted congressperson in year *t* and remains 1 for all years following the scandal year and is zero otherwise. *First Stay Scandal* is an indicator variable that is set to 1 if firm *i* is connected to a scandal-tainted congressperson with an outcome of *Stay* in year *t* and remains 1 for all years following the scandal year and is zero otherwise. *First Non-stay Scandal* is an indicator variable that is set to 1 if firm *i* is connected to a scandal-tainted congressperson with an outcome of *Non-stay* in year *t* and remains 1 for all years following the scandal year, and is zero otherwise. Each regression includes firm and year fixed effects (α_i, α_t) and the following control variables ($X_{i,t}$): *FEC Contributions*, *Ln(Market Capitalization)*, *Ln(Firm Age)*, *Capital Expenditures*, *Leverage*, *Return on Assets*, *Tax*, *R&D*, *Firm Return Variance*, and *Dividends Indicator*. All variables are defined in Appendix A.2. Standard errors are clustered at the firm level. The p-values are reported in parentheses. ***, **, and * indicate significance at 1%, 5%, and 10%, respectively.

	(1)	(2)	(3)	(4)	(5)	(6)
Dependent Variable	Ln(MTB)	Ln(MTB)	Dividends per Share	Dividends per Share	Earnings per Share	Earnings per Share
First Scandal	-0.075**		-0.085***		-0.205*	
	[0.01]		[0.01]		[0.05]	
First Stay Scandal		-0.068**		-0.069**		-0.213**
		[0.03]		[0.03]		[0.05]
First Non-stay Scandal		-0.017		-0.050		0.017
		[0.60]		[0.17]		[0.88]
Control Variables	YES	YES	YES	YES	YES	YES
Firm FE	YES	YES	YES	YES	YES	YES
Year FE	YES	YES	YES	YES	YES	YES
No. of Obs.	16,839	16,839	17,405	17,405	17,403	17,403
Adj. R^2	0.692	0.692	0.709	0.709	0.482	0.482

Table 12. Political Scandals, Reelection Outcomes, and Firm Value

This table presents the results of the following multiple event and multiple treatment group difference-in-differences regression: $Ln(Tobin's\ Q)_{i,t} = \alpha_i + \alpha_t + \gamma X_{i,t} + \delta\, First\ Scandal_{i,t} + \epsilon_{i,t}$. The sample includes all publicly-listed US firms that made contributions to a US congressperson through its PAC during the period of 1992-2018. The dependent variable in each column is *Ln(Tobin's Q)* abbreviated in the table as *Ln(*Q*)*. *First Scandal* is an indicator variable that is set to 1 if firm *i* is connected to a scandal-tainted congressperson in year *t* and remains 1 for all years following the scandal year and is zero otherwise. *First Stay Reelect Scandal* is an indicator variable that is set to 1 if firm *i* is connected to a scandal-tainted congressperson with an outcome of *Stay* and *Reelect* in year *t* and remains 1 for all years following the scandal year and is zero otherwise. *First Stay Non-Reelect Scandal* is an indicator variable that is set to 1 if firm *i* is connected to a scandal-tainted congressperson with an outcome of *Stay* and *Non-Reelect* in year *t* and remains 1 for all years following the scandal year and is zero otherwise. *First Non-stay Scandal* is an indicator variable that is set to 1 if firm *i* is connected to scandal-tainted congressperson with an outcome of *Non-stay* in year *t* and remains 1 for all years following the scandal year, and is zero otherwise. Each regression includes firm and year fixed effects (α_i, α_t) and the following control variables ($X_{i,t}$): *FEC Contributions*, *Ln(Market Capitalization)*, *Ln(Firm Age)*, *Capital Expenditures*, *Leverage*, *Return on Assets*, *Tax*, *R&D*, *Firm Return Variance*, and *Dividends Indicator*. All variables are defined in Appendix A.2. Standard errors are clustered at the firm level. The p-values are reported in parentheses. ***, **, and * indicate significance at 1%, 5%, and 10%, respectively.

	(1)	(2)	(3)	(4)
Dependent Variable	Ln(Q)	Ln(Q)	Ln(Q)	Ln(Q)
First Scandal	-0.043***			
	[0.00]			
First Stay Reelect Scandal		-0.039**		-0.038**
		[0.01]		[0.02]
First Stay Non-Reelect Scandal		-0.011		-0.009
		[0.50]		[0.55]
First Non-stay Scandal			-0.017	-0.008
			[0.29]	[0.60]
Control Variables	YES	YES	YES	YES
Firm FE	YES	YES	YES	YES
Year FE	YES	YES	YES	YES
No. of Obs.	17,405	17,405	17,405	17,405
Adj. R^2	0.775	0.775	0.775	0.775

Figure 1. The Number and Fraction of Firms Connected to a Scandal-Tainted Congressperson by Year
This figure reports the number and fraction of publicly-listed US contributing firms that are connected to at least one US congressperson embroiled in a scandal as reported by the *Legislator Misconduct Database* at Govtrack.us in a given year during the period of 1992-2018. Contributing firms are those that contribute to a US congressperson through its PAC during 1990-2018. There are 1,064 unique firms in the sample.

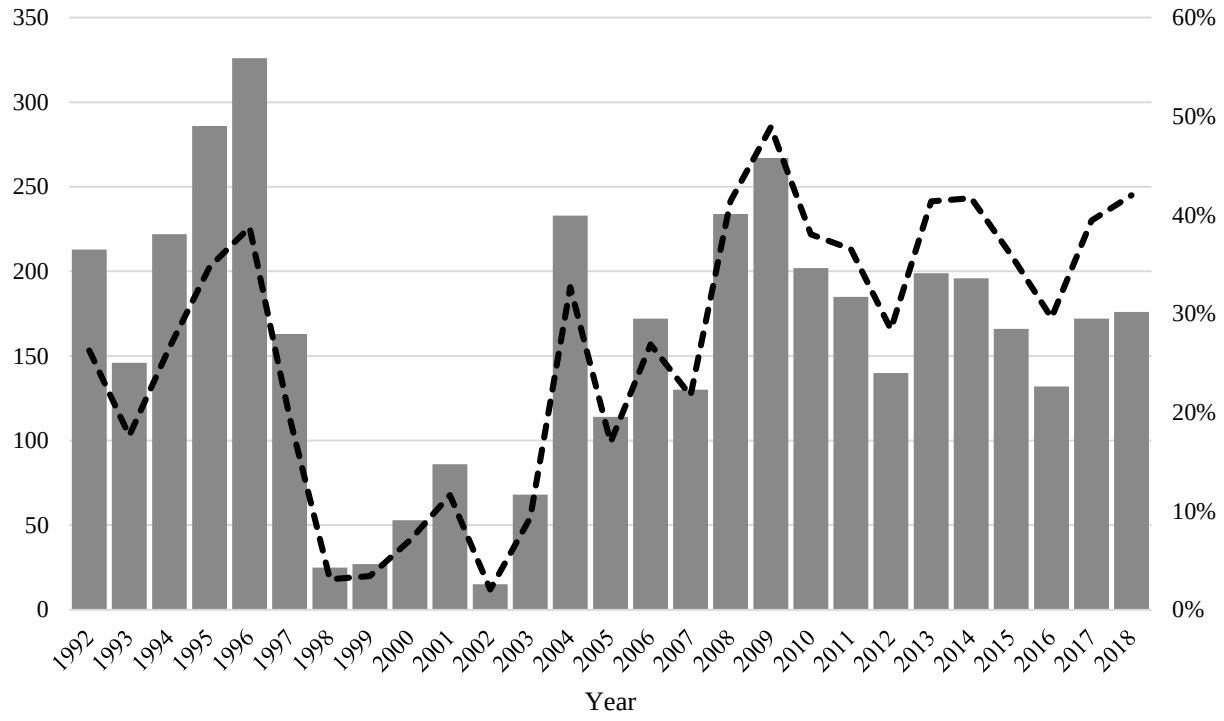
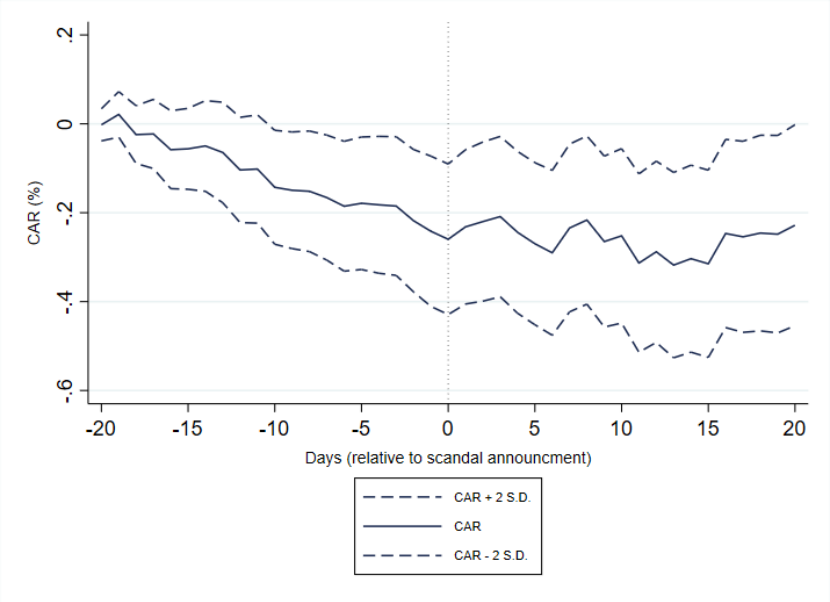


Figure 2. Cumulative Abnormal Returns Around Political Scandals

This figure plots the cumulative abnormal returns (CARs) of a market model for an event window around the first-report date for political scandals. Each CAR is scaled by 100. Day 0 is the date of the first instance in which a media outlet reports the scandal. We adopt a 255-trading day estimation window ending 126 trading days prior to the event date. For each stock, we require a minimum of 40 observations in the estimation window. Panel A plots the mean CAR and the two standard deviation confidence intervals of the mean CAR for the full sample. Panel B plots the mean CARs for the Stay and Non-stay subsample. All variables are defined in Appendix A.2.

Panel A: Full Sample CAR



Panel B: Stay vs. Non-stay CARs

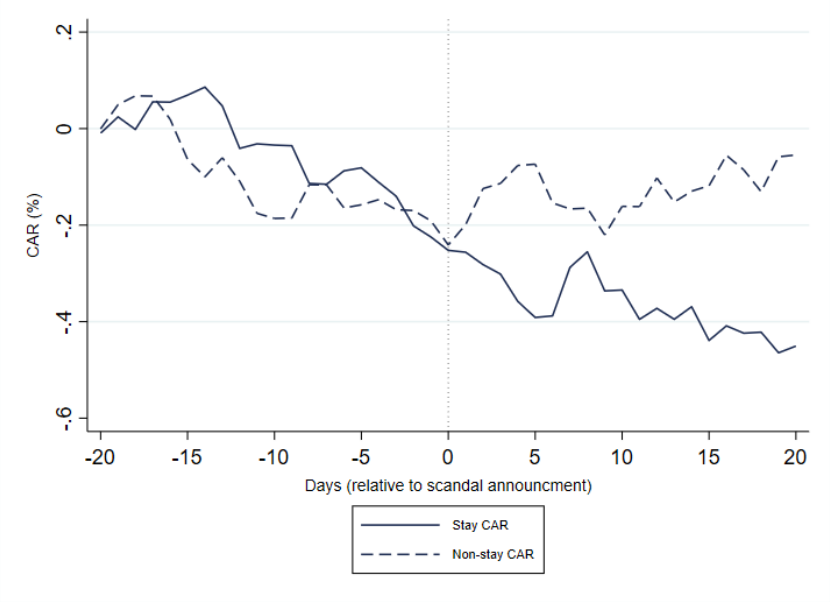


Figure 3. Sun and Abraham (2021) Fixed-Effect Difference-in-Differences Estimates of the Effects of Firm Value and Politicl Scandals

This figure plots the fixed-effect estimates of the following multiple event and multiple treatment group difference-in-differences regression using a ten-year event window and the Sun and Abraham (2021) methodology: $Ln(Tobin's\ Q)_{i,t} = \alpha_i + \alpha_t + \delta\, First\ Scandal_{i,t} + \in_{i,t}$. Period -1 is used as the reference point. Leads and lags are shown as two separate lines (as recommended by Borusyak, Jaravel, and Spiess (2021)), and the 90% confidence levels are plotted using the shaded red and blue regions. The initial sample includes all publicly-listed US firms that made contributions to a US congressperson through its PAC and were connected to a congressional political scandal at some point during the period of 1992-2018. To be included in the final model and figure, firms have at least half (at least 5) of the observations in the 10-year window. The dependent variable in each column is Ln(Tobin's Q), abbreviated in the table as Ln(Q). First Scandal, the treatment variable, is an indicator variable that is set to 1 if firm i is connected to a scandal-tainted congressperson in year t and remains 1 for all years following the scandal year, and is zero otherwise. All variables are defined in Appendix A.2. Standard errors are clustered at the firm level.