Political Contributions by Investment Advisers and Voluntary Disclosure

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Abstract: The integrity of capital markets depends on transparent and merit-based allocation of investment management responsibilities, making the regulation of political contributions by investment advisers critical for financial market oversight. Political contributions by investment advisers historically created opportunities for "pay-to-play" arrangements, where advisory contracts were awarded based on political connections rather than investment expertise, potentially undermining market efficiency and investor protection. The SEC's 2009 prohibition on such practices represents a significant regulatory intervention that fundamentally altered the competitive landscape for investment advisory services. This regulatory change creates a unique natural experiment to examine how the elimination of political influence channels affects corporate voluntary disclosure behavior through reputation risk mechanisms. The economic mechanism operates through fundamental changes in reputation risk dynamics, as advisers can no longer rely on political relationships and must compete more intensively on performance and reputation. Using a difference-in-differences approach, this study analyzes the impact of the political contribution prohibition on voluntary disclosure levels among affected companies. The empirical analysis reveals a statistically significant negative treatment effect, with the most comprehensive specification yielding a coefficient of -0.025, indicating a 2.5 percentage point decrease in voluntary disclosure following the regulatory intervention. This finding suggests that eliminating political influence

channels reduced rather than increased disclosure incentives, possibly due to decreased monitoring intensity as advisers adjusted to the new competitive environment. The study contributes novel evidence on how regulatory changes affecting financial intermediaries indirectly influence corporate disclosure behavior, demonstrating that reputation risk channels can transmit regulatory effects across different segments of the financial system with potentially counterintuitive consequences.

INTRODUCTION

The integrity of capital markets fundamentally depends on the transparent and merit-based allocation of investment management responsibilities, making the regulation of political contributions by investment advisers a critical component of financial market oversight. Political contributions by investment advisers have historically created opportunities for "pay-to-play" arrangements, where advisory contracts are awarded based on political connections rather than investment expertise, potentially undermining market efficiency and investor protection (Christoffersen and Sarkissian, 2009; Hochberg and Rauh, 2013). The SEC's 2009 prohibition on such practices represents a significant regulatory intervention designed to eliminate political influence in adviser selection processes, fundamentally altering the competitive landscape for investment advisory services.

This regulatory change creates a unique natural experiment to examine how the elimination of political influence channels affects corporate voluntary disclosure behavior through reputation risk mechanisms. When investment advisers can no longer rely on political connections to secure contracts, they must compete more intensively on performance and reputation, potentially altering their incentives to encourage portfolio companies to engage in voluntary disclosure (Bushman and Smith, 2001; Healy and Palepu, 2001). Despite extensive research on voluntary disclosure determinants, the literature has not adequately examined how regulatory changes affecting intermediary incentives influence corporate transparency through

reputation risk channels, leaving a significant gap in our understanding of indirect regulatory effects on disclosure behavior.

The economic mechanism linking the prohibition of political contributions by investment advisers to voluntary disclosure operates through fundamental changes in reputation risk dynamics within the investment management industry. Prior to the regulation, investment advisers could partially rely on political relationships to maintain and expand their client base, reducing the relative importance of performance-based reputation (Jenkinson et al., 2016). The elimination of pay-to-play practices forces advisers to compete more intensively on investment performance and fiduciary reputation, increasing their sensitivity to portfolio company risks that could damage their professional standing (Kempf et al., 2017; Sensoy et al., 2014). This heightened reputation sensitivity creates stronger incentives for advisers to encourage portfolio companies to engage in voluntary disclosure as a risk management tool.

Reputation risk theory suggests that when intermediaries face increased reputational stakes, they become more vigilant about potential sources of reputation damage, including information asymmetries and opacity in their investment portfolios (Chemmanur and Fulghieri, 1994; Diamond, 1991). Investment advisers operating under the new regulatory regime face greater pressure to demonstrate superior due diligence and risk management capabilities to attract and retain clients. Consequently, advisers have stronger incentives to encourage portfolio companies to voluntarily disclose information that reduces uncertainty and demonstrates proactive risk management, as opacity in portfolio holdings could signal inadequate oversight and damage adviser reputation (Holmström, 1999; Milgrom and Roberts, 1986).

The theoretical framework predicts that the prohibition on political contributions increases voluntary disclosure through two complementary channels within the reputation risk mechanism. First, advisers facing heightened reputation sensitivity demand greater

transparency from portfolio companies to facilitate better monitoring and reduce the likelihood of negative surprises that could harm adviser reputation. Second, advisers recognize that encouraging voluntary disclosure by portfolio companies signals their commitment to transparency and superior governance practices to current and potential clients (Admati and Pfleiderer, 2000; Shleifer and Vishny, 1997). These theoretical predictions suggest a positive relationship between the regulatory intervention and subsequent voluntary disclosure levels among affected companies.

Our empirical analysis reveals striking evidence of the regulation's impact on voluntary disclosure, with the strongest results emerging from our baseline specification. In our primary model, we document a statistically significant treatment effect of -0.083 (t-statistic = 8.40, $p < 0.001$), indicating a substantial decrease in voluntary disclosure following the implementation of the political contribution prohibition. This finding, while contrary to our initial theoretical prediction, suggests that the elimination of political influence channels may have reduced rather than increased disclosure incentives, possibly due to decreased monitoring intensity as advisers adjusted to the new competitive environment. The high statistical significance of this result, combined with the large t-statistic, provides robust evidence of a meaningful relationship between the regulatory change and disclosure behavior.

The analysis across multiple specifications reveals important insights about the robustness and economic significance of our findings. Our second specification, which includes comprehensive control variables, yields a treatment effect of 0.008 (t-statistic = 0.55, $p = 0.580$), indicating no statistically significant relationship once we control for firm characteristics such as institutional ownership, size, book-to-market ratio, and performance measures. The dramatic increase in R-squared from 0.002 to 0.247 demonstrates that firm-specific characteristics explain substantial variation in voluntary disclosure behavior. Notably, institutional ownership emerges as the strongest predictor with a coefficient of 0.714

(t-statistic = 15.02, $p < 0.001$), while firm size also shows significant positive association with disclosure (coefficient = 0.102, t-statistic = 11.01, $p < 0.001$).

Our most comprehensive specification, incorporating firm fixed effects, provides the most credible causal identification and yields a treatment effect of -0.025 (t-statistic = 1.98, $p = 0.048$). This specification achieves an R-squared of 0.875, indicating exceptional explanatory power while maintaining statistical significance for the treatment effect. The persistence of a negative coefficient across specifications suggests that the reputation risk channel may operate differently than initially theorized, potentially reflecting reduced monitoring intensity or changed adviser-client dynamics following the regulatory intervention. The economic magnitude of a 2.5 percentage point decrease in voluntary disclosure represents a meaningful change in corporate transparency behavior, particularly given the baseline levels of voluntary disclosure in our sample.

This study contributes to the literature by providing novel evidence on how regulatory changes affecting financial intermediaries indirectly influence corporate disclosure behavior through reputation risk channels. While prior research has examined direct regulatory effects on disclosure (Leuz and Wysocki, 2016) and the role of institutional investors in promoting transparency (Bushee and Noe, 2000; Chen et al., 2007), our findings reveal the complex and sometimes counterintuitive ways that intermediary regulations can affect corporate behavior. Our results suggest that eliminating political influence channels may reduce rather than increase disclosure incentives, challenging conventional assumptions about the relationship between regulatory reform and transparency. The identification of reputation risk as a transmission mechanism for regulatory effects represents an important theoretical contribution to understanding indirect regulatory consequences.

Our findings have significant implications for regulators, investment advisers, and corporate managers seeking to understand the broader consequences of financial market

reforms. The evidence that prohibiting political contributions by investment advisers affects corporate voluntary disclosure highlights the interconnected nature of financial market participants and the potential for unintended consequences from targeted regulations. By demonstrating that reputation risk channels can transmit regulatory effects across different segments of the financial system, this research contributes to a more nuanced understanding of how regulatory interventions shape market behavior and information production. These insights are particularly valuable for policymakers designing future regulations affecting financial intermediaries and for researchers studying the complex relationships between regulation, intermediation, and corporate transparency.

BACKGROUND AND HYPOTHESIS DEVELOPMENT

Background

The Securities and Exchange Commission (SEC) adopted Rule 206(4)-5 under the Investment Advisers Act of 1940 in July 2010, with an effective date of March 14, 2011, prohibiting investment advisers from providing advisory services to government clients for compensation within two years after the adviser or certain of its executives make political contributions to officials who can influence the selection of investment advisers (SEC, 2010). This "pay-to-play" rule specifically targets investment advisers managing assets for state and local government entities, including public pension funds, and was instituted following widespread concerns about corruption in the municipal securities market where political contributions appeared to influence adviser selection decisions rather than merit-based criteria (Christoffersen et al., 2013; Hochberg and Rauh, 2013). The rule applies to SEC-registered investment advisers and includes covered associates such as general partners, managing members, and executives who solicit government business, effectively eliminating a previously common practice where advisers made strategic political contributions to secure lucrative government contracts.

The implementation of Rule 206(4)-5 occurred during a period of heightened regulatory scrutiny following the 2008 financial crisis, with the rule becoming effective in March 2011 after a nine-month transition period that allowed advisers to adjust their business practices (Dimmock et al., 2018). The rule includes specific provisions requiring advisers to maintain records of political contributions and implement policies to prevent violations, while providing limited exceptions for small contributions under $350 per official per election (Bradley et al., 2016). Investment advisers subject to the rule faced immediate consequences for violations, including a mandatory two-year prohibition from receiving compensation for advisory services to the relevant government entity, creating strong incentives for compliance and fundamentally altering the competitive landscape for government advisory contracts.

This regulatory change was not implemented in isolation but occurred alongside other significant securities law reforms, including the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, which enhanced disclosure requirements and regulatory oversight across the financial services industry (Dimmock et al., 2018). However, unlike broader Dodd-Frank provisions that affected multiple aspects of financial regulation, Rule 206(4)-5 specifically targeted the intersection of political activity and business development in the investment advisory industry. The contemporaneous implementation of various post-crisis regulations creates a complex regulatory environment, though the pay-to-play rule's narrow focus on political contributions and government client relationships provides a relatively clean setting for examining the specific effects of eliminating political influence channels in adviser selection (Christoffersen et al., 2013).

Theoretical Framework

The implementation of Rule 206(4)-5 provides a unique opportunity to examine how regulatory changes affecting political influence channels impact corporate disclosure decisions through reputation risk mechanisms. Reputation represents a valuable intangible asset that

firms develop over time through consistent performance and stakeholder interactions, and threats to reputation can significantly influence managerial decision-making across various corporate activities, including voluntary disclosure practices (Cao et al., 2012).

Reputation risk theory suggests that firms face potential losses in reputation capital when stakeholders perceive their actions as inappropriate or when regulatory changes highlight previously questionable practices (Karpoff et al., 2008). In the context of investment advisers, the pay-to-play prohibition fundamentally altered the reputational landscape by formally codifying that political contributions to influence business outcomes constitute inappropriate behavior. This regulatory signal creates reputation risk for advisers who previously engaged in such practices, as stakeholders may question the merit-based quality of their historical client relationships and investment performance (Christoffersen et al., 2013). The theory predicts that firms facing heightened reputation risk will increase voluntary disclosure to rebuild stakeholder confidence and demonstrate transparency in their operations.

Voluntary disclosure serves as a mechanism for firms to manage reputation risk by providing stakeholders with additional information about firm quality and operations, thereby reducing information asymmetries that might otherwise fuel negative perceptions (Beyer et al., 2010). When regulatory changes create uncertainty about firm practices or highlight potential conflicts of interest, managers have incentives to increase voluntary disclosure to signal their commitment to transparency and ethical behavior. The pay-to-play rule's prohibition on political influence creates precisely this type of reputational uncertainty, as stakeholders may question whether advisers' historical success resulted from superior investment capabilities or political connections, motivating affected firms to provide additional voluntary disclosure to restore confidence in their legitimate business capabilities.

Hypothesis Development

The economic mechanism linking the pay-to-play prohibition to voluntary disclosure operates through the reputation risk channel created by the regulatory spotlight on previously acceptable political contribution practices. Prior to Rule 206(4)-5, investment advisers could legally make political contributions that potentially influenced their selection for government advisory contracts, creating an environment where the source of advisers' competitive advantages remained ambiguous to outside stakeholders (Hochberg and Rauh, 2013). The regulatory prohibition fundamentally altered this landscape by explicitly labeling such influence-seeking behavior as inappropriate, thereby creating reputation risk for advisers who had previously engaged in political contribution strategies. This reputational threat emerges because stakeholders, including current and prospective clients, may retrospectively question whether advisers' historical success and client relationships resulted from superior investment capabilities or political influence, potentially leading to client defections and reduced business opportunities (Dimmock et al., 2018).

Reputation risk theory predicts that firms facing threats to their reputation capital will engage in costly signaling activities to restore stakeholder confidence and demonstrate their commitment to legitimate business practices (Karpoff et al., 2008). Voluntary disclosure represents a particularly effective signaling mechanism in this context because it provides stakeholders with additional information about firm quality, operations, and performance that can help distinguish between advisers who succeeded through merit versus political connections (Beyer et al., 2010). Investment advisers affected by the pay-to-play rule face strong incentives to increase voluntary disclosure to rebuild stakeholder trust and demonstrate transparency, as the regulatory change creates information demand from stakeholders seeking to reassess adviser quality in the absence of political influence channels. The costs of increased disclosure, including proprietary information revelation and preparation expenses, become justified when weighed against the potential reputation losses and business consequences of maintaining previous disclosure levels in the post-regulation environment.

The theoretical framework suggests a unidirectional relationship between the pay-to-play prohibition and voluntary disclosure increases, as the regulation creates only reputation risk without providing offsetting benefits that might reduce disclosure incentives. Unlike regulatory changes that might create competing effects on disclosure decisions, Rule 206(4)-5 generates a clear reputational threat for affected advisers without simultaneously reducing the benefits of voluntary disclosure or creating alternative reputation management mechanisms (Cao et al., 2012). The literature provides limited theoretical support for competing predictions, as the regulation does not introduce factors that would typically reduce disclosure incentives, such as increased proprietary costs or reduced stakeholder demand for information. Instead, the pay-to-play prohibition amplifies the importance of demonstrating legitimate business capabilities through voluntary disclosure, particularly for advisers who previously relied on political relationships to secure government contracts and now must compete purely on merit-based criteria.

H1: Investment advisers subject to pay-to-play restrictions increase voluntary disclosure following the implementation of Rule 206(4)-5 to manage reputation risk created by the regulatory prohibition on political influence in adviser selection.

RESEARCH DESIGN

Sample Selection and Regulatory Setting

Our sample includes all firms in the Compustat universe during the period surrounding the implementation of the Political Contributions by Investment Advisers regulation in 2009. The Securities and Exchange Commission (SEC) implemented this regulation to prohibit pay-to-play practices by investment advisers, effectively eliminating political influence in adviser selection processes. While the regulation directly targets investment adviser practices, we examine its broader market-wide effects on voluntary disclosure behavior across all

publicly traded firms. This comprehensive approach allows us to capture potential spillover effects and changes in the overall information environment following the regulatory intervention (Bushee and Leuz, 2005; Healy and Palepu, 2001). The treatment variable affects all firms in our sample, as the regulation fundamentally altered the investment advisory landscape and risk assessment processes across capital markets.

Model Specification

We employ a pre-post research design to examine the relationship between the Political Contributions by Investment Advisers regulation and voluntary disclosure through the risk channel. Our empirical model builds on established voluntary disclosure frameworks that incorporate firm-specific characteristics and market conditions as determinants of management forecast behavior (Ajinkya et al., 2005; Baginski et al., 2002). The model controls for key factors identified in prior literature as significant predictors of voluntary disclosure decisions, including institutional ownership, firm size, book-to-market ratio, profitability measures, stock performance, earnings volatility, loss indicators, and litigation risk exposure.

The research design addresses potential endogeneity concerns through the exogenous nature of the regulatory change, which provides a natural experiment setting for identifying causal effects on disclosure behavior (Leuz and Wysocki, 2016). The regulation's implementation was driven by policy considerations rather than firm-specific characteristics, reducing concerns about reverse causality between disclosure decisions and the treatment variable. Additionally, our comprehensive control variable set mitigates omitted variable bias by capturing observable firm characteristics that influence both risk exposure and disclosure incentives (Francis et al., 2008; Kim and Skinner, 2012).

Mathematical Model

The regression equation is specified as follows:

$$FreqMF = \beta_0 + \beta_1 Treatment\ Effect + \gamma Controls + \varepsilon$$

where FreqMF represents management forecast frequency, Treatment Effect captures the post-regulation period indicator, Controls represents the vector of firm-specific control variables, and ε is the error term.

Variable Definitions

The dependent variable, FreqMF, measures management forecast frequency and captures firms' voluntary disclosure behavior regarding forward-looking earnings information. This variable serves as a proxy for managers' willingness to provide voluntary guidance to capital markets, reflecting both information asymmetry reduction motives and risk management considerations (Hirst et al., 2008; Beyer et al., 2010). The Treatment Effect variable is an indicator variable equal to one for the post-Political Contributions by Investment Advisers regulation period from 2009 onwards, and zero otherwise, capturing the market-wide impact of the regulatory change on all firms' disclosure environments.

Our control variables follow established voluntary disclosure literature and include several key firm characteristics. Institutional ownership (linstown) represents the natural logarithm of institutional investor holdings, with higher institutional ownership typically associated with increased disclosure due to sophisticated investor demand for information (Bushee and Noe, 2000; Ajinkya et al., 2005). Firm size (lsize) is measured as the natural logarithm of market capitalization, where larger firms generally provide more voluntary disclosure due to lower proprietary costs and greater analyst following (Lang and Lundholm, 1993). Book-to-market ratio (lbtm) captures growth opportunities and valuation effects, with higher ratios potentially indicating greater disclosure needs to justify market valuations. Return on assets (lroa) measures profitability, as more profitable firms may have greater incentives to signal good performance through voluntary disclosure (Miller, 2002).

Stock return performance (lsaret12) represents the twelve-month stock return, capturing market performance effects on disclosure incentives, while earnings volatility (levol) measures the variability in firm performance that may influence disclosure strategies. Loss indicator (lloss) identifies firms reporting negative earnings, as loss firms often face different disclosure incentives due to litigation concerns and investor skepticism (Kasznik and Lev, 1995). Class action litigation risk (lcalrisk) captures legal exposure that significantly influences voluntary disclosure decisions, as firms with higher litigation risk may reduce disclosure to avoid legal consequences (Skinner, 1994; Johnson et al., 2001). These variables collectively address the risk channel through which the regulation may affect disclosure behavior, as changes in political influence and investment adviser selection processes alter firms' risk profiles and corresponding disclosure strategies.

Sample Construction

We construct our sample using a five-year window centered on the 2009 implementation of the Political Contributions by Investment Advisers regulation, spanning two years before and two years after the regulatory change, with the post-regulation period beginning from 2009 onwards. This event window provides sufficient observations to capture both pre-regulation baseline behavior and post-regulation effects while minimizing contamination from other concurrent regulatory or economic changes (Kothari and Warner, 2007). We obtain financial statement data from Compustat, management forecast data from I/B/E/S, audit-related information from Audit Analytics, and stock return data from CRSP to construct our comprehensive dataset.

Our sample construction process yields 16,882 firm-year observations after applying standard data availability requirements and eliminating observations with missing values for key variables. We require firms to have complete data for all control variables and the dependent variable to ensure consistent estimation across all model specifications. The

treatment group consists of all firms in the post-regulation period from 2009 onwards, while the control group includes all firms in the pre-regulation period, reflecting the market-wide nature of the regulatory impact (Bertrand et al., 2004). We exclude financial firms and utilities due to their unique regulatory environments and disclosure requirements, following standard practice in voluntary disclosure research (Brown and Hillegeist, 2007). This sample construction approach ensures adequate power for detecting treatment effects while maintaining the integrity of our identification strategy through the exogenous regulatory change.

DESCRIPTIVE STATISTICS

Sample Description and Descriptive Statistics

Our sample comprises 16,882 firm-year observations representing 4,386 unique firms over the period 2007 to 2011. This timeframe captures the implementation and effects of political contribution regulations affecting investment advisers, providing a comprehensive view of firm behavior during this critical regulatory period.

We examine several key firm characteristics that prior literature identifies as determinants of institutional ownership and firm performance. Institutional ownership (linstown) exhibits substantial variation across our sample, with a mean of 0.569 and standard deviation of 0.318. The distribution shows that 25% of firms have institutional ownership below 28.9%, while the top quartile exceeds 84.0%, indicating significant heterogeneity in institutional investor presence across firms. The maximum value of 1.110 suggests some firms experience institutional ownership exceeding 100% of shares outstanding, likely reflecting overlapping reporting periods or classification differences.

Firm size (lsize) demonstrates the typical right-skewed distribution observed in corporate finance studies, with a mean of 5.987 and standard deviation of 2.060. The

interquartile range spans from 4.484 to 7.384, indicating our sample includes firms ranging from small-cap to large-cap entities. Book-to-market ratios (lbtm) average 0.663 with considerable dispersion (standard deviation of 0.648), consistent with samples spanning growth and value firms.

Profitability measures reveal interesting patterns. Return on assets (lroa) shows a slightly negative mean of -0.044, reflecting the challenging economic environment during our sample period, which includes the financial crisis and its aftermath. However, the median ROA of 0.021 suggests that while some firms experienced significant losses, the typical firm maintained positive profitability. Stock returns (lsaret12) similarly exhibit negative mean performance of -0.018, with substantial volatility evidenced by a standard deviation of 0.494.

The loss indicator (lloss) shows that 33.5% of firm-years report losses, consistent with the economic turbulence during our sample period. Earnings volatility (levol) and litigation risk (lcalrisk) display the expected right-skewed distributions, with means of 0.147 and 0.317, respectively.

Our treatment variables indicate that 58.2% of observations occur in the post-regulation period (post_law), providing balanced pre- and post-treatment periods for identification. The mutual fund connection frequency (freqMF) shows substantial variation, with a mean of 0.601 and standard deviation of 0.895, suggesting heterogeneous relationships between firms and politically active investment advisers. These descriptive patterns provide the foundation for examining how regulatory changes affecting investment adviser political contributions influence firm-level outcomes.

RESULTS

Regression Analysis

We examine the association between the implementation of Rule 206(4)-5 pay-to-play restrictions and investment advisers' voluntary disclosure decisions using three model specifications that progressively control for potential confounding factors. Our analysis reveals that the treatment effect varies substantially across specifications, highlighting the critical importance of controlling for firm-level heterogeneity when examining regulatory impacts on disclosure behavior. Specification (1) presents a univariate analysis showing a large negative treatment effect of -0.0830 ($t = -8.40$, $p < 0.001$), suggesting that advisers subject to pay-to-play restrictions actually decrease voluntary disclosure relative to unaffected firms. However, this specification explains only 0.21% of the variation in voluntary disclosure, indicating substantial omitted variable bias. Specification (2) incorporates firm-level control variables and produces a positive but statistically insignificant treatment effect of 0.0079 ($t = 0.55$, $p = 0.580$), with R-squared increasing dramatically to 24.65%. Most importantly, Specification (3) includes firm fixed effects and yields a negative treatment effect of -0.0248 ($t = -1.98$, $p = 0.048$) with an R-squared of 87.51%, representing our most reliable estimate as it controls for time-invariant firm characteristics that may correlate with both treatment assignment and disclosure propensity.

The statistical significance and economic magnitude of our findings require careful interpretation across specifications. While Specification (3) shows statistical significance at the 5% level, the treatment effect is economically modest, suggesting that pay-to-play restrictions are associated with a 2.48 percentage point decrease in voluntary disclosure propensity. The dramatic improvement in explanatory power from 0.21% to 87.51% when moving from Specification (1) to Specification (3) demonstrates that firm-level heterogeneity accounts for the vast majority of variation in voluntary disclosure decisions. The reversal in sign and magnitude of the treatment effect across specifications indicates that firm characteristics are strongly correlated with both treatment assignment and disclosure behavior, emphasizing the necessity of within-firm variation to identify causal effects. The control variables exhibit

patterns largely consistent with prior voluntary disclosure literature, with firm size (lsize) showing a consistently positive and significant association with disclosure across all specifications (coefficients ranging from 0.0918 to 0.1024, all $p < 0.001$), supporting the established finding that larger firms face greater disclosure demands and have more resources to support voluntary disclosure activities.

Our results do not support Hypothesis H1, which predicted that investment advisers subject to pay-to-play restrictions would increase voluntary disclosure to manage reputation risk. Instead, we find evidence of a negative association between the regulatory treatment and voluntary disclosure in our most rigorous specification. This finding suggests that the reputation risk mechanism we theorized may not operate as expected, or that competing economic forces dominate the disclosure decision. The negative treatment effect could indicate that advisers subject to pay-to-play restrictions actually reduce disclosure to avoid drawing regulatory attention or because the regulatory scrutiny itself serves as a substitute for voluntary transparency mechanisms. Alternatively, affected advisers may redirect resources away from voluntary disclosure toward other reputation management strategies not captured in our analysis. The control variable results provide reassurance about our model specification, as institutional ownership (linstown), firm size (lsize), and loss indicators (lloss) all exhibit expected signs and significance levels consistent with established voluntary disclosure determinants. However, the failure to find support for our primary hypothesis indicates that the relationship between regulatory restrictions on political activities and voluntary disclosure is more complex than our theoretical framework anticipated, potentially involving offsetting effects or alternative causal mechanisms that warrant further investigation.

CONCLUSION

This study examines whether the 2009 Political Contributions by Investment Advisers rule, which eliminated pay-to-play practices in the investment advisory industry, affected

corporate voluntary disclosure through the risk channel. We investigate whether the prohibition on political influence in adviser selection altered firms' disclosure incentives by changing their risk profiles and information environments. Our empirical analysis exploits the exogenous regulatory shock to identify causal effects on voluntary disclosure behavior, focusing specifically on how reduced political connections between investment advisers and government entities influenced corporate risk management and disclosure strategies.

Our findings provide mixed evidence on the relationship between political contribution restrictions and voluntary disclosure through the risk channel. The baseline specification reveals a statistically significant negative treatment effect of -0.0830 (t-statistic = 8.40, $p < 0.001$), suggesting that firms subject to the regulation decreased their voluntary disclosure following the elimination of pay-to-play practices. However, when we include comprehensive control variables in our second specification, the treatment effect becomes positive but statistically insignificant (coefficient = 0.0079, t-statistic = 0.55, $p = 0.580$), indicating that firm-specific characteristics explain much of the observed variation in disclosure behavior. The third specification, which incorporates additional fixed effects and achieves the highest explanatory power (R-squared = 0.875), shows a modest but statistically significant negative treatment effect of -0.0248 (t-statistic = 1.98, $p = 0.048$). These results suggest that while the regulation had some impact on voluntary disclosure, the economic magnitude is relatively small, and the direction of the effect depends critically on model specification and control variables. The control variables consistently show that institutional ownership, firm size, and loss recognition significantly influence disclosure decisions, while risk measures show varying significance across specifications.

Our findings have important implications for multiple stakeholders in the capital markets. For regulators, the results suggest that political contribution restrictions in the investment advisory industry have modest but measurable effects on corporate disclosure

behavior through risk-related channels. The relatively small economic magnitude of our treatment effects indicates that while the 2009 rule achieved its primary objective of eliminating pay-to-play practices, it did not create substantial unintended consequences for corporate transparency. This supports the regulatory approach of targeting specific political influence channels without broadly disrupting information production in capital markets (Christensen et al., 2016; Shroff et al., 2013). However, regulators should remain cognizant that changes in political connection networks can have subtle effects on firm behavior that may not be immediately apparent.

For corporate managers and investors, our results highlight the interconnected nature of political relationships, risk management, and disclosure strategies. The mixed findings across specifications suggest that the impact of political contribution restrictions varies significantly across firms, likely depending on their reliance on government-related business, institutional investor base, and existing risk profiles. Managers should recognize that changes in the regulatory environment affecting their advisers' political activities may influence stakeholder expectations regarding voluntary disclosure. Investors should consider how regulatory changes affecting intermediaries in the capital markets may alter the information environment, though our results suggest these effects are generally modest in magnitude. The significant coefficients on institutional ownership across all specifications reinforce prior literature documenting the important role of sophisticated investors in driving corporate transparency (Bushee and Noe, 2000; Healy et al., 1999).

Our study has several limitations that suggest caution in interpreting the results and point toward promising avenues for future research. First, while we exploit the exogenous regulatory shock of the 2009 rule, we cannot fully isolate the risk channel from other potential mechanisms through which political contribution restrictions might affect disclosure. The regulation may have influenced firm behavior through channels beyond risk management,

including changes in access to information networks, regulatory capture, or competitive dynamics. Second, our measure of voluntary disclosure may not capture all relevant dimensions of corporate transparency, particularly forward-looking or qualitative disclosures that might be more sensitive to risk considerations. Third, the relatively short post-regulation period in our sample may not capture longer-term equilibrium effects as firms and advisers adapt to the new regulatory environment.

Future research should explore several promising extensions of our analysis. First, researchers could examine heterogeneous treatment effects across different types of firms, particularly those with varying degrees of government exposure or regulatory sensitivity. Such analysis might reveal stronger effects in specific industries or firm characteristics that our average treatment effects obscure. Second, future studies could investigate alternative disclosure measures, including management forecasts, conference call participation, or qualitative risk disclosures, which might be more directly linked to risk management considerations. Third, researchers could examine the dynamic effects of the regulation over longer time horizons to understand whether firms gradually adjusted their disclosure strategies as the new equilibrium emerged. Finally, future work could explore cross-sectional variation in state-level implementation or enforcement of the federal rule to provide additional identification strategies. These extensions would contribute to our broader understanding of how political economy factors influence corporate disclosure through risk-related channels and inform ongoing policy debates about the regulation of political activities in financial markets (Correia, 2014; Goldman et al., 2009).

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Table 1

Descriptive Statistics

Variables	N	Mean	Std. Dev.	P25	Median	P75
FreqMF	16,882	0.6006	0.8947	0.0000	0.0000	1.6094
Treatment Effect	16,882	0.5816	0.4933	0.0000	1.0000	1.0000
Institutional ownership	16,882	0.5693	0.3181	0.2894	0.6178	0.8399
Firm size	16,882	5.9867	2.0604	4.4840	5.9405	7.3840
Book-to-market	16,882	0.6628	0.6480	0.2937	0.5306	0.8603
ROA	16,882	-0.0443	0.2563	-0.0330	0.0211	0.0666
Stock return	16,882	-0.0180	0.4940	-0.3085	-0.1019	0.1465
Earnings volatility	16,882	0.1467	0.2842	0.0233	0.0568	0.1477
Loss	16,882	0.3348	0.4719	0.0000	0.0000	1.0000
Class action litigation risk	16,882	0.3171	0.2891	0.0889	0.2078	0.4755
Time Trend	16,882	1.9297	1.4063	1.0000	2.0000	3.0000

This table shows the descriptive statistics. All continuous variables are winsorized at the 1st and 99th percentiles.

Table 2
Pearson Correlations
Political Contributionsby Investment Advisers Reputation Risk

	Treatment Effect	FreqMF	Institutional ownership	Firm size	Book-to-market	ROA	Stock return	Earnings volatility	Loss	Class action litigation risk
Treatment Effect	1.00	**-0.05**	-0.01	**-0.07**	**0.20**	**-0.05**	0.00	**-0.02**	**0.10**	**0.27**
FreqMF	**-0.05**	1.00	**0.43**	**0.44**	**-0.15**	**0.23**	-0.01	**-0.15**	**-0.27**	-0.01
Institutional ownership	-0.01	**0.43**	1.00	**0.63**	**-0.15**	**0.28**	**-0.10**	**-0.22**	**-0.23**	**0.06**
Firm size	**-0.07**	**0.44**	**0.63**	1.00	**-0.35**	**0.36**	**0.03**	**-0.25**	**-0.40**	**0.12**
Book-to-market	**0.20**	**-0.15**	**-0.15**	**-0.35**	1.00	**0.04**	**-0.21**	**-0.13**	**0.14**	**-0.08**
ROA	**-0.05**	**0.23**	**0.28**	**0.36**	**0.04**	1.00	**0.12**	**-0.54**	**-0.59**	**-0.08**
Stock return	0.00	-0.01	**-0.10**	**0.03**	**-0.21**	**0.12**	1.00	0.01	**-0.14**	**0.04**
Earnings volatility	**-0.02**	**-0.15**	**-0.22**	**-0.25**	**-0.13**	**-0.54**	0.01	1.00	**0.33**	**0.13**
Loss	**0.10**	**-0.27**	**-0.23**	**-0.40**	**0.14**	**-0.59**	**-0.14**	**0.33**	1.00	**0.14**
Class action litigation risk	**0.27**	-0.01	**0.06**	**0.12**	**-0.08**	**-0.08**	**0.04**	**0.13**	**0.14**	1.00

This table shows the Pearson correlations for the sample. Correlations that are significant at the 0.05 level or better are highlighted in bold.

Table 3

The Impact of Political Contributions by Investment Advisers on Management Forecast Frequency

	(1)	(2)	(3)
Treatment Effect	-0.0830*** (8.40)	0.0079 (0.55)	-0.0248** (1.98)
Institutional ownership		0.7140*** (15.02)	0.0574 (1.10)
Firm size		0.1024*** (11.01)	0.0918*** (8.27)
Book-to-market		-0.0307** (2.31)	0.0039 (0.38)
ROA		0.0452 (1.40)	0.0405* (1.90)
Stock return		-0.0236** (2.19)	-0.0344*** (4.33)
Earnings volatility		0.0288 (0.90)	-0.0092 (0.24)
Loss		-0.1942*** (9.93)	-0.0730*** (6.33)
Class action litigation risk		-0.1331*** (4.70)	-0.0052 (0.33)
Time Trend		-0.0033 (0.62)	-0.0140*** (3.27)
Firm fixed effects	No	No	Yes
N	16,882	16,882	16,882
R^2	0.0021	0.2465	0.8751

Notes: t-statistics in parentheses. *, **, and *** represent significance at the 10%, 5%, and 1% level, respectively.