

Close Elections, Campaign Contributions, and Financial Deregulation

November 16, 2021

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Abstract

This paper builds upon Igan and Mishra (2014) Igan and Mishra (2014) on vote switches towards financial deregulation by US legislators. I measure the effect of close elections on US legislators on switching their votes towards financial deregulation in Congress bills. I aim to distinguish between vote switches towards financial deregulation because of voters' general interests (especially after the Global Financial Crisis of 2007) versus the financial industry's special interests and the industry's campaign contributions and lobbying expenditures towards legislators in close elections.

Keywords Financial Deregulation, Close Elections

JEL codes D81, D91, E21

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The paper is the author's 2nd year paper for fulfillment to the PhD in Economics program at Johns Hopkins University, and also for Professor Christopher Carroll's Computational Methods course. I thank Professors Laurence Ball and Filipe Campante for comments and advice, and Deniz Igan and Prachi Mishra for sharing their data.

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1 Introduction



Figure 1 Two Channels in which Legislators in Close Elections Switch their Votes Toward Financial Deregulation

How do legislators in close elections vote differently on financial deregulation compared to legislators in sure elections? I use data from Igan and Mishra (2014) to answer this question.

2 The Problem

Legislators, to get reelected, have to respond to voters and special interests (in this paper, the financial industry)

Legislators in sure elections are less incentivized to switch their vote on bills on financial deregulation; they will still win their sure elections whether they vote for (if the legislator's constituent voters prefer deregulation) or against (if the legislator's constituent voters do not prefer deregulation). Legislators in sure elections are also less incentivized to switch their votes towards financial deregulation to satisfy the financial industry, as they will still have enough campaign finances to win their sure elections regardless of the additional campaign contributions from the financial industry. In short, legislators in sure elections would not be strongly incentivized to switch their votes on financial deregulation to get more votes or acquire more campaign contributions. Legislators in sure elections will be less responsive to additional lobbying expenditures or campaign contributions by the financial industry as well.

Table 1 Definition of the Main Dependent Variable, Vote Switch towards Deregulation

Value of S_iBR	Voted for deregulation in Bill B, R	Voted against deregulation in Bill B, R
Voted for deregulation in Bill $B, R - 1$	0	0
Voted for deregulation in Bill $B, R - 1$	1	0

Legislators in close elections may be more incentivized to switch their vote towards financial deregulation via the same two stakeholders. To attract more votes, legislators in close elections may be more responsive to voters’ needs for financial deregulation. To gather more campaign contributions, those legislators may also be more responsive to lobbying expenditures and campaign contributions from the financial industry. Legislators in close elections, through either mechanism, have a greater incentive to switch their votes towards financial deregulation in order to win reelection.

Igan and Mishra (2014) argue that their results, that lobbying expenditures make legislators more likely to switch their votes towards financial deregulation, is a correlational result and therefore cannot be taken as causation from either of these reasons. I attempt to provide at least a partial answer by introducing new variables, including one for whether a legislator has been in or will be facing a close election. I also include other variables to support the regression strategies that can differentiate between voters’ public scrutiny and the financial industry’s special interests.

There are two broad strategies that can be used; the first is to use a measure of “media congruence”, by Snyder and Stromberg (2010).

The second is to use the rapid change in public sentiment against financial deregulation shortly after the Global Financial Crisis and the resulting Great Recession.

2.1 Setup

3 Variables

3.1 Dependent Variable

3.2 Election Closeness

Compared to the original Igan and Mishra (2014) paper, I add the new variable of “Election Closeness” as the main focus of this paper. I define “election closeness” for each legislator i and bill BR , denoted as X_{iBR} , as the degree to which the legislator has faced (past) or will face (future) a close election. Note the two possible ways of looking at election closeness: through the past election(s) of the legislator, or to the (immediately next) future election of the legislator. Meanwhile, the measure of future

election closeness

Past election closeness is defined simply, in this paper, as the percentage margin of victory of the legislator in the last election before a vote on a bill BR . I denote this variable as X_{iBR}^P . As a concrete example, assume that legislator A won his/her last election with 49,000 votes against the runner-up, who got 47,000 votes in a congressional election of a total of 100,000 votes, and that the remaining 4,000 votes all went to third-party, independent, and write-in votes. In this case, legislator A 's margin of victory is $(49,000 - 47,000)/100,000 = 2\%$. There are two important characteristics of this variable: first, X_{iBR}^P must necessarily be greater than zero, as the legislator must have won at least one more vote than the runner-up. Second, X_{iBR}^P is the same across all bills BR during the same congress C , as legislator i has only one value of past election closeness at any given congress C and all the bills therein.

Ideally, future election closeness may be defined as the expected margin of victory in the next (future) election of the legislator. I denote this variable as X_{iBR}^F . The future expected margin of victory of an as-of-yet undecided election can be proxied by results of election polls. Since most future congressional elections at any given electoral cycle have at least one polling result, and in most cases more than one, X_{iBR}^F can differ across bills BR even in the same congress C .

3.3 Original Variables

4 Regressions

4.1 Regression A

Concretely, I write Regression A1 as:

$$S_{iBR} = \beta_1 L_{BR} + \beta_2 X_{iBR}^P + \beta_3 (L_{BR} \times X_{iBR}^P) + \alpha F_{BR} + \gamma T_{BR} + s_i \times t_c + v_B \times t_c + \mu_R \times t_c + \varepsilon_{iBR} \quad (1)$$

5 Conclusions

References

IGAN, DENIZ, AND PRACHI MISHRA (2014): "Wall Street, Capitol Hill, and K Street: Political Influence and Financial Regulation," *Journal of Law and Economics*, 57, 1063–1084.