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Accounting information as political currency

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Accounting information as political currency*

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Abstract

We test whether accounting can be used as political currency. Our setting is the US congressional election of 2004, where outsourcing of US jobs was a campaign issue. We find that the largest corporate donors to principal candidates in closely watched congressional races manage earnings downwards in the two quarters immediately preceding the 2004 election. We find no evidence of such downwards earnings management among corporate donors to candidates in all other congressional races. Election outcomes for candidates are also systematically associated with the extent of donors' downwards earnings management in closely watched races, but not all other races. The findings are consistent with firms managing accounting information in circumstances where this is likely to benefit allied politicians.

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1. Introduction

We investigate whether firms manage accounting earnings in circumstances where this is likely to benefit allied politicians. We examine the accruals choices made by firms with links to politicians in closely watched US congressional races in the 2004 elections, where outsourcing of US jobs was a major campaign issue.¹ We find that the largest corporate donors to principal candidates in closely watched races managed earnings downwards in the two calendar quarters immediately preceding the 2004 election. We also find that the election outcomes for candidates in closely watched races are associated with the extent of downwards earnings management by donor firms. Our findings are consistent with a "political currency" role for accounting.

It is well known that firms contribute money to politicians. It is also widely held that such money, in the form of campaign contributions and lobbying expenditures, is used to buy access to and/or favors from politicians (see for example, Hart, 2001). Firms and politicians establish relationships with one another and the value to firms of such relationships likely increases over time (Snyder, 1992; Kroszner and Stratmann, 2005). When a politician with a well-established relationship to a firm faces a tough election prospect, it is then in the firm's interest to secure that politician's future. One obvious way to do so is to make further monetary contributions directly to the politician's campaign (see for example, Poole and Romer, 1985; Levitt, 1998).² *A priori*, direct monetary contributions are not the only channel through which firms can deliver benefits to candidates during political campaigns. We investigate whether political contributions can take a non-cash form, specifically (accounting) information. In other words, can (accounting) information be used as political currency?

¹ Throughout the paper, we use "outsourcing" to refer to offshore (i.e., international) outsourcing. Later, we discuss the implications of this definition.

² The evidence on the effectiveness of such cash contributions on election outcomes is, however, mixed at best (see for example, Levitt, 1994; Stratmann, 2005). Another issue in the literature is why there is, on average, so little money in political campaigns (relative to the size of total government spending; see for example, Ansolabehere *et al.*, 2003).

The information environment in a political campaign can be crucial to a candidate's success. Candidates can be expected to actively manage information that affects their election prospects through spin, censorship, and strategic press leaks. If a firm with ties to a candidate has information that can affect the candidate's chances, it is in both the candidate's and firm's interest for the firm to manage that information. Firms have incentives to manage information to the advantage of affiliated candidates because this likely pre-empts future political costs resulting from the election of "unfriendly" candidates (i.e., candidates likely to bring regulatory attention to the firm). Such information management on part of the firm can be considered a form of political currency, similar to cash contributions.

To examine whether a firm's accounting decisions are affected by its desire to influence the prospects of affiliated political candidates, we identify a setting that allows us to form a clear directional prediction about accrual choices that are likely to be, on average, more beneficial to candidates. Our setting is the US congressional elections of 2004, and our expectation is that donor firms seeking to deliver benefits to affiliated political candidates will, on average, manage earnings downwards.³

Congressional elections in 2004 accompanied a presidential race, where the Democratic challenger, Sen. John Kerry, made outsourcing of US jobs a campaign issue. Sen. Kerry and his allies alleged that policies of the incumbent Republican president, George Bush, and the Republican-controlled Congress were facilitating the outsourcing of US jobs overseas (see for example, *Fox News*, 2004 and *New York Times*, 2004a). The issue of outsourcing—and campaign contributions received from alleged outsourcers—entered the debate in specific

³ For simplicity, we focus on the whether the net effect of accounting choices is to increase or decrease net income. In any given fiscal period, there are potentially a large number of factors influencing whether a political candidate benefits from income-increasing or income-decreasing choices by donor firms. Our setting enables us to predict that in 2004, the donor-firm accounting choices most likely to generate *benefits* for affiliated politicians were income *decreasing* in nature.

congressional races as well. For example, the *Dayton Daily News* reported in October 2004 on challenger Jane Mitakides' (Democrat) attempts to highlight Rep. Mike Turner's (R-OH) involvement with outsourcers: "...Jane Mitakides (D) said Mike Turner's (R) support for outsourced jobs is seen in the political contributions his campaign has received from ... Raj Soin, founder of Dayton-based Modern Technologies Corp... Soin denies the claim that his company outsources jobs." Democratic candidates and non-incumbents were not immune to outsourcing-related criticism. In an October 2004 article titled "In House Race, Accusations Fly Over Outsourcing," the *Tulsa World* reported: "... Rep. John Sullivan [R-OK] has accused Democrat Doug Dodd of investing in a company that outsources jobs ..." Stagnant job growth in the years leading up to 2004 likely helped fuel the outsourcing issue. The media reported widely on it, and even prominent economists weighed in on the debate (see for example, Bhagwati *et al.*, 2004 and Samuelson, 2004).

The prevailing notion in 2004 was that firms were generating additional profits by sending corporate jobs abroad via their outsourcing activities (Taylor, 2005). Further, these profits were perceived as being concentrated in the hands of a few. We hypothesize that political candidates regardless of party affiliation or incumbency status were likely to benefit from donor firms underreporting profits during the election season, particularly if the donor firms were suspected outsourcers. If donor firms' accounting decisions are affected by their desire to influence the prospects of affiliated political candidates, we expect the donor firms in question made accruals choices to understate reported income in quarters preceding the 2004 election.⁴

⁴ It is also possible that donor firms made income-decreasing accruals choices to avoid increased scrutiny on themselves during the election season. We do not rule out this possibility (in fact, we expect it to also be the case), but certain results in the paper (as will be discussed) are only consistent with accounting decisions being affected by firms' desires to influence the prospects of affiliated political candidates.

In each congressional election race in 2004 (i.e., elections to the 109th Congress), we focus our attention on the Democratic and Republican candidates (principal candidates). We identify corporate donors to these candidates through records of cash contributions via political action committees (PACs). Consistent with the proposition that large cash giving can be used to establish links between politicians and firms (see for example, Stratmann, 2005), we focus only on corporate donors giving at least \$10,000 to a candidate.

We expect that the identified donor firms are more likely to reduce reported income when their beneficiary candidates are more likely to value such reductions. To that end, we distinguish candidates participating in election races with greater uncertainty and higher visibility, hereafter, "closely watched races." We expect candidates in closely watched races to be particularly vulnerable to political attacks exploiting unfavorable information, such as the outsourcing profits of donor firms. Given the relevance of outsourcing to the election environment in 2004, we expect that identified corporate donors to candidates in closely watched races are more likely (than corporate donors to all other candidates) to understate income via downward earnings management in financial reports released prior to the election.

The hypothesis that firms' accounting decisions are affected by their desire to influence the prospects of affiliated political candidates also predicts that income understatement via downward earnings management is associated with favorable outcomes for the beneficiary candidates. We measure favorable outcomes using the proportion of votes the candidates obtain in the congressional elections. We predict that the vote shares will be positively associated with the extent of income understatement by corporate donors, particularly for candidates in closely watched races, where the benefits from understated net income are likely to be the most relevant.

We measure income understatement using performance-matched discretionary accruals (Kothari *et al.*, 2005).⁵

To test our predictions, we perform two sets of tests. In the first set, we examine whether there is evidence of corporate donors making strategic income decreasing accrual choices in the second and third calendar quarters of 2004, since these quarters immediately preceded the November elections. We use the corporate donors' own recognition practices in four two-quarter periods centered around our quarters of interest as benchmarks (i.e., our quarters of interest are Q2'04&Q3'04 and our benchmark quarters are: Q2'03&Q3'03, Q4'03&Q1'04, Q4'04&Q1'05, and Q2'05&Q3'05). We do not find any evidence of downwards earnings management in the quarters of interest (relative to benchmark quarters) among donor firms not contributing to candidates in closely watched races. On the other hand, firms that contribute to candidates in closely watched races exhibit statistically significant evidence of downwards earnings management in the quarters of interest, consistent with the predictions of a political currency role for accounting. To substantiate the result above, we investigate whether firms contributing to candidates in closely watched races reduce disclosures related to outsourcing activities. We find decreases in mentions of the word-stem "outsourc" in the 10-Ks and 10-Qs of these firms during the quarters of interest (relative to benchmark quarters), consistent again with the predictions of a political currency role for accounting and financial statement disclosures.

Our second set of tests is at the candidate level. Here, we test for cross-sectional variation between donor firms' performance-matched discretionary accruals and principal candidates' election outcomes. For candidates not in closely watched races, we find no association between

⁵ In a given fiscal period, there are likely several agency-based incentives shaping a firm's accounting choices (*Fields et al.*, 2001). We identify a setting and sample where incentives to deliver benefits to affiliated political candidates are likely prevalent. It is likely that other agency incentives also shape accounting choices in our sample, but we do not expect such incentives to be systematic.

election outcomes and donor earnings management. On the other hand, for candidates in closely watched races, we find the proportion of votes secured increases as the average performance-matched discretionary accruals of donor firms decreases. For the average candidate in a closely watched race, a two standard-deviation decrease in donors' mean performance-matched discretionary accruals is associated with a 5% increase in votes obtained. Given that the average candidate in a closely watched race receives a vote share of 52.7%, the results suggest that on the margin, donor firms' earnings management can be associated with an election victory.

The results from the candidate-level tests are consistent with the results from the firm-level tests. Collectively, the two sets of results suggest that during the second and third calendar quarters of 2004, firms contributing to candidates in closely watched election races managed reported income downwards, and that the downward earnings management was associated with more favorable election outcomes for the candidates. The results are consistent with a "political currency" hypothesis.⁶

This paper attempts to broaden our understanding of the relation between accounting and the political process beyond the political cost hypothesis as specified by Watts and Zimmerman (1978, 1986). That hypothesis was originally formulated as follows: *ceteris paribus*, larger firms are more likely to choose accounting procedures that defer reported earnings from current to future periods. The intuition is that large firms, being more visible, are more likely to attract public attention when they declare large profits. Such public attention, in turn, is likely to result in higher taxes and costly regulatory oversight. By deferring earnings from current to future periods, large firms avoid the costs associated with high visibility and large profits. An extension (corollary) of the political cost hypothesis was developed by Jones (1991) who found that firms

⁶ The results of the first set of tests are consistent with accounting decisions being motivated by firms' desires to both influence the prospects of affiliated political candidates and avoid increased scrutiny during the election season. The results of the second set of tests are consistent with the former hypothesis only.

likely to benefit from government-sponsored import relief attempted to manage earnings downwards during import relief investigations. The basic premise in Jones is similar to that in Watts and Zimmerman: firms manage earnings in order to *extract* first-order benefits (or avoid first-order costs) from regulators. We develop and test a distinct and complementary political hypothesis: firms manage reported earnings in order to *supply* first-order benefits to regulators. In doing so, firms likely assist in the election of friendly regulators and ensure their ability to extract first-order benefits (or avoid first-order costs) in future periods.

The remainder of this paper is organized as follows. Section 2 describes our choice of the setting and sample, and defines key variables. Section 3 provides evidence on sample firms' management of information relating to outsourcing in 2004. Section 4 provides evidence on the association of this information management with election outcomes in 2004. Section 5 concludes.

2. Setting, sample, and key definitions

Our hypothesis is that firms use accounting information as a form of political contribution. This potential political role for accounting information, however, is likely balanced against other incentives that shape accounting and financial reporting (see for example, the vast literature on agency-related incentives and accounting choice, Fields *et al.*, 2001). Thus, testing our hypothesis requires identifying a relatively high-powered setting and sample where we can make clear directional predictions on the association between dependent and independent variables. For the setting, we identify an election season where corporate policies were a major part of the political debate—the 2004 US elections when outsourcing by US firms was heavily

discussed. For the sample, we focus on Democratic and Republican candidates in the 2004 congressional races.

2.1. Setting

The year 2004 was a presidential election year with a hotly contested race for the White House. Democratic presidential challenger, Sen. John Kerry, and allied political groups made outsourcing of US jobs a key theme in their campaigns. They alleged that policies of the incumbent Republican president, George Bush, and the Republican-controlled Congress were facilitating the outsourcing of US jobs overseas (see for example, *Fox News*, 2004 and *New York Times*, 2004a). The issue of outsourcing—and campaign contributions received from alleged outsourcers—entered the debate in specific congressional races as well, as evidenced from the examples in the introduction. Stagnant to slow job growth in the years leading up to the 2004 election helped support the claims against outsourcing. Taylor (2005, p. 367) notes how "'outsourcing' became a political dirty word during the 2004 election campaign." The media widely reported on the outsourcing issue and it became part of the information environment in the 2004 election (a Factiva search for articles in the *New York Times* and the *Wall Street Journal* between January 1, 2004 and Election Day, 2004 that contained both "outsourc" and "election" returned 191 unique stories).

The information environment in a political campaign can be crucial to a candidate's success. Candidates can be expected to actively manage information that affects their election prospects. If a firm with ties to a candidate has information that can affect the candidate's chances, it is in the candidate's and firm's interest for the firm to manage that information. The

firm can "contribute" to the candidate's election by managing information, in anticipation of favorable treatment in the future from affiliated political candidates in office.

In the 2004 election, with outsourcing of US jobs being a key issue, we expect candidates with ties to firms that were outsourcing were likely to benefit from firm-actions that *minimized* disclosure of this information. Further, we expect that candidates valued the benefits from minimized disclosures about donor firms' outsourcing activities irrespective of their party affiliation or incumbency status. Accordingly, in the case of accounting information related to outsourcing (our focus), we test for income-*decreasing* accruals management.

In any given fiscal period, there are potentially a large number of factors influencing whether a political candidate benefits from income-increasing or income-decreasing choices by donor firms. Our setting—the 2004 elections—enables us to predict that, given the widespread attention devoted to corporate outsourcing during that time, the donor-firm accounting choices most likely to generate benefits for affiliated politicians were income-decreasing in nature. The underlying assumption is that outsourcing, if any, is net profitable and thus, the use of income-decreasing accruals management enables donor firms to deflect public scrutiny of both the firm and the political candidate over outsourcing. The assumption that outsourcing is net-profitable is reasonable because if outsourcing is not cheaper than producing in-house, a firm would not choose to outsource. Later, we describe and explain our choice of empirical proxies for income-decreasing accruals management.

2.2. *Sample*

We focus on Democratic and Republican candidates in the 2004 congressional races. Third-party candidates, candidates in Louisiana, and candidates in races for non-voting House

delegates are excluded.⁷ These criteria give us a beginning sample of 836 congressional candidates. For these candidates, we obtain data on the largest twenty cash donors (in terms of PAC contributions) over the years 2000 through 2004. The largest twenty cash donors to the 836 congressional candidates represent 5,458 unique organizations. Of these organizations, we retain only for-profit corporate donors who contributed at least \$10,000 over the four-year period and who are included on COMPUSTAT (ideological and special-interest groups, law firms other private companies, unions, universities, etc. are excluded). There are 338 such corporate donors.

From the 836 congressional candidates we begin our analysis with, we eliminate 263 candidates who do not receive donations from any of the 338 corporate donors described above. This leaves us with 573 candidates to follow (Table 1, Panel A). We use the existence of cash contributions in excess of \$10,000 from the 338 corporate donors to the 573 candidates in the four-year period leading up to 2004 as evidence of a relationship between the donors and candidates. This is consistent with the proposition that large cash giving can be used to establish links between politicians and firms (see for example, Stratmann, 2005). Given the relevance of outsourcing to the election environment in 2004, we test whether the identified corporate donors manage information related to outsourcing in the election year (via earnings understatement), and whether the information management is associated with the candidates' election outcomes. We assume that cash and information are complementary forms of political contributions, i.e., the relations established through large cash donations are complemented by information management. It is possible that information management is a substitute to cash as a form of political currency. If this is so, we are unlikely to find results consistent with our predictions.

As noted earlier, we expect that the identified corporate donors are more likely to reduce reported income when their beneficiary candidates are more likely to value such reductions. To

⁷ We exclude races in Louisiana because these races can include multiple candidates from the same party.

that end, we identify which of the 573 candidates participated in election races with greater uncertainty and higher visibility. We use data compiled by The Green Papers, a non-partisan election-related website, to make this identification. We classify races with no incumbents and races with "close, interesting, or contradictory information" being reported by pollsters (compiled by The Green Papers five days prior to Election Day, November 2, 2004) as "closely watched races." We expect candidates in these races to be particularly vulnerable to political attacks exploiting unfavorable information, such as the outsourcing profits of donor firms. We refer to candidates in "closely watched races" as "candidates to watch" and create an associated indicator variable, *CTW*.

Ninety-five of the 573 candidates we follow are "candidates to watch" per the definition above. Panel B of Table 1 reports on their properties. Thirty-seven of the 95 "candidates to watch" are Democrats; the proportion of Democrats among "candidates to watch" is not statistically distinguishable from the proportion of Democrats among all other candidates. Seventy-four of the 95 "candidates to watch" participate in House races; the proportion of House contenders among "candidates to watch" is statistically lower than the proportion of House contenders among all other candidates (chi-square probability <0.001). Sixty-nine of the 95 "candidates to watch" are non-incumbents; the proportion of non-incumbents among "candidates to watch" is statistically greater than the proportion of non-incumbents among all other candidates (chi-square probability <0.001). In later multivariate tests, we control for these observed differences between "candidates to watch" and all other candidates.

2.3. Key definitions

As noted earlier, our principal proxy for the management of information among identified corporate donors is income-decreasing accruals management. We measure income-decreasing accruals management using performance-matched discretionary accruals (Kothari *et al.*, 2005). We test for lower performance-matched discretionary accruals during the second and third quarters of 2004, since these quarters immediately preceded the November elections. The firms' own performance-matched discretionary accruals in four two-quarter intervals immediately surrounding our quarters of interest are used as benchmarks. Our benchmark quarters are thus: Q2'03&Q3'03, Q4'03&Q1'04, Q4'04&Q1'05, and Q2'05&Q3'05.

Since we are interested in discretionary accounting decisions that are not reflective of fundamental economic performance, estimating performance-matched accruals is appropriate in the context of our study (Kothari *et al.*, 2005). To obtain performance-matched discretionary accruals for a given sample firm-quarter, we first calculate abnormal accruals for that firm-quarter. The abnormal accruals for a firm-quarter are the residual (ϵ) from the following regression run quarterly within the firm's 3-digit NAICS-defined industry.

$$\text{Acc} = \beta_0 * \text{Intercept} + \beta_1 * \Delta \text{Sales} + \beta_2 * \text{PPE} + \epsilon \quad (1)$$

In the above equation, Acc is defined (using COMPUSTAT Industrial Quarterly definitions) as $(\text{data8} - \text{data108}) / \text{lag}(\text{data44})$, in other words, the difference between income before extraordinary items and operating cash flows, over lagged period assets. The intercept is defined as $1/\text{lag}(\text{data44})$, the inverse of lagged period assets. ΔSales is defined as $(\text{data2} - \text{lag}(\text{data2})) / \text{lag}(\text{data44})$, the one-period change in sales over lagged period assets. PPE is

defined as defined as $\text{lag}(\text{data42}) / \text{lag}(\text{data44})$, lagged period net property, plant, and equipment over lagged period assets. All ratios are winsorized at the 1st and 99th percentile level of quarterly observations.

To obtain performance-matched discretionary accruals for a firm-year observation, we match that observation to one within its 3-digit NAICS-defined industry that is closest to it in terms of return-on-sales. Return-on-sales is defined as the ratio of lagged period income-before-extraordinary-items to lagged period sales. The excess of a sample firm-year's abnormal accruals (ϵ) over its matched firm-year's abnormal accruals is its performance-matched discretionary accruals number.

Using income-decreasing accruals management as a proxy for the management of information related to outsourcing assumes that all donor firms in our sample were involved in at least some overseas outsourcing. This is a reasonable assumption given the relatively large size of our sample firms (to be discussed in the next section) and the broad political definition of outsourcing that existed during the 2004 election (for example, Bhagwati *et al.*, 2004, p. 94, note how the definition of outsourcing during the 2004 election "leap[ed] beyond purchases of offshore arm's-length services to include ... phenomena such as offshore purchases of manufactured components and even direct foreign investment by firms"). Nevertheless, an *ex ante* measure of outsourcing that picks up on cross sectional variation within sample firms can add power to our tests. We attempt to develop such a measure below.

Since the main political concern with outsourcing has been workforce reduction within the United States, our proxy for *ex ante* outsourcing activities is based on the unexpected decrease in employment among firms. Specifically, our firm-level measure of outsourcing is

based on the negative of the residual from the following regression estimated annually within the firm's 3-digit NAICS-defined industry.⁸

$$\Delta\text{Employees} = \gamma_0 * \text{Intercept} + \gamma_1 * \Delta\text{Sales} + \delta \quad (2)$$

In the above equation, $\Delta\text{Employees}$ is defined (using COMPUSTAT Industrial Annual definitions) as $(\text{data29} - \text{lag}(\text{data29})) / \text{lag}(\text{data6})$, in other words, the one period increase in the number of employees, scaled by lagged assets. The intercept and ΔSales are defined as in equation (1), except using annual data (i.e., Intercept is $1/\text{lag}(\text{data6})$ and ΔSales is $(\text{data12} - \text{lag}(\text{data12})) / \text{lag}(\text{data6})$). The residual δ represents the unexpected change in employment for a given year. Negative values of this residual are associated with decreases in employment after controlling for sales changes and are, we argue, a proxy for outsourced operations. To allow for the proxy to *increase* with the level of outsourcing, we multiply it by -1. To allow for the proxy to be an *ex ante* measure of outsourcing we compute its two-year historical average. We call the resulting variable, a measure of outsourcing-related workforce reduction, WF_RED . Thus, our measure for outsourcing for all quarters in a given year "t," i.e., WF_RED_t , is computed as follows.

$$WF_RED_t = -1 * (\delta_{t-1} + \delta_{t-2})/2 \quad (3)$$

In subsequent tests using performance-matched discretionary accruals, we use WF_RED_t as a firm-level weight that captures cross-sectional differences in outsourcing.

⁸ Data on the number of employees is available only at the annual level in COMPUSTAT.

3. Management of information related to outsourcing in 2004

In this section, we report on evidence of donor firms making strategic accruals choices in our quarters of interest, i.e., the second and third calendar quarters of 2004 (hereafter, "MID-2004"). As noted above, we use as a benchmark the corporate donors' own recognition practices in the following two-quarter periods: Q2'2003&Q3'2003 (hereafter, "MID-2003"), Q4'2003&Q1'2004 (hereafter, "2003-04"), Q4'2004&Q1'2005 (hereafter, "2004-05"), and Q2'2005&Q3'2005 (hereafter, "MID-2005"). We first report formal statistical tests using performance-matched discretionary accruals as a proxy for the management of information related to outsourcing. We perform these tests on the entire sample of identified corporate donors. Then, for the sub-sample of corporate donors giving to candidates in closely watched elections, we report patterns in firm disclosure, specifically, reductions in references to outsourcing (measured by mentions of the word-stem "outsourc") among corporate donors' 10-Ks and 10-Qs. The disclosure patterns are intended to corroborate conclusions from the accruals tests.

3.1 Results using performance-matched discretionary accruals

Table 2 provides summary statistics on the corporate donor firms that contribute a \$10,000 minimum to at least one political candidate in a closely watched race (Panel A) and donors firms that contribute the same minimum amount to at least one candidate in any other race (Panel B). For comparison, we provide data from the two quarter periods starting MID-2003 through MID-2005. As Panel A reports, the mean sample firm contributing to candidates in closely watched races has about \$24 billion in assets in the test period, suggesting that sample firms are larger, on average, than COMPUSTAT firms. This is expected given their relatively

large political donations (assuming donation size increases with firm size). Panel A firms also show an increase in sales growth between MID-2003 to MID-2004, from 2.6% to 2.9%, consistent with improved economic activity during this period: US GDP growth increased from 4.7% in 2003 to 6.6% in 2004 (Source: Bureau of Economic Analysis).

Performance-matched discretionary accruals in Panel A of Table 2 show a decline in MID-2004 relative to the benchmark periods. The mean values of performance-matched discretionary accruals are -0.0082 in MID-2003; -0.0012 in 2003-04; -0.0145 in MID-2004; -0.0079 in 2004-05; and -0.0074 in MID-2005. If performance-matched discretionary accruals are a good proxy for the management of information related to outsourcing, there is some evidence of such information management among donors to candidates in closely watched elections in 2004, as seen in Panel A of Table 2. The table also reports sample firms' return-on-sales over the period MID-2003 through MID-2005. Unlike in the case of performance-matched discretionary accruals, return-on-sales is not the lowest in MID-2004—indeed it is higher than values in three out of the four benchmark periods.

Descriptive statistics for firms that contribute to candidates in races not classified as closely watched are reported in Panel B. These firms tend to be smaller than Panel A firms, with mean assets of \$14 billion in 2004, but these firms, like Panel A firms, also experience increase in sales growth from MID-2003 to MID-2004. Firms in Panel B do not exhibit a decline in performance matched accruals during MID-2004. In both Panels A and B of Table 2, we report on the time-series trend in our *ex ante* measure of outsourcing, *WF_RED*. In both panels, *WF_RED* is seen increasing over time, consistent with increased outsourcing activity over the sample period.

Table 3 presents more formal evidence on the trend in performance-matched discretionary accruals across firms in the sample. The dependent variable in Table 3 is performance-matched discretionary accruals, while the independent variables include a fourth-fiscal-quarter dummy (to control for end-of-fiscal-year effects, e.g., Mendenhall and Nichols, 1988) and dummies for the five two-quarter periods from MID-2003 through MID-2005. Since regression data in Table 3 include multiple observations from sample firms, all standard errors are clustered at the firm level. Further, intercepts are suppressed in all Table 3 regressions.

Panel A of Table 3 reports the results of the regression specification described above. The coefficient on the MID-2004 indicator is negative but statistically insignificant. In Panel B we introduce an indicator variable, *CTWGiver*, which is set equal to one if a sample firm has contributed to a political candidate in a closely watched race during the four years leading up to the 2004 elections. *CTWGiver* is also interacted with each of the dummies for the two-quarter periods from MID-2003 through MID-2005. The coefficient on the interacted variable *MID-2004*CTWGiver* in Panel B captures any systematic change in the performance-matched discretionary accruals in MID-2004 for firms contributing to candidates in closely watched races. The coefficient on *MID-2004*CTWGIVER* is negative and statistically significant at the 90% confidence level, consistent with downwards earnings management in MID-2004 among donors to candidates in closely watched races. The coefficient on *MID-2004* (un-interacted) remains statistically insignificant, indicating that firms contributing to candidates not in closely watched races do not exhibit evidence of downwards earnings management in MID-2004.

We expect that donor firms with greater outsourcing activities in the years leading up to 2004 had higher incentives to manage earnings down, particularly when associated with candidates in closely watched races. In Panel C of Table 3, we investigate whether firms with

greater *ex ante* outsourcing activities exhibit more negative performance-matched discretionary accruals. Recall that we develop a measure of workforce reduction, *WF_RED*, to proxy for historical outsourcing activities. In Panel C, we interact this variable with each of the substantive variables in the Panel B specification. The coefficient on *MID-2004*CTWGiver*WF_RED* in Panel C captures the relation between MID-2004 performance-matched discretionary accruals and greater workforce reduction for firms contributing to candidates running in closely watched races. The coefficient is negative and statistically significant at the 90% confidence level, suggesting that firms contributing to closely-watched candidates exhibited more downwards earnings management in MID-2004 if they engaged in greater outsourcing. The coefficient on *MID-2004*CTWGiver* in Panel C is also negative and significant at the 90% confidence level, consistent with the results and interpretation in Panel B (i.e., MID-2004 downwards earnings management, on average, among donors to candidates in closely watched races). The coefficient on *MID-2004*WF_RED* is positive and insignificant, indicating that for firms contributing to candidates not running in closely watched races, greater outsourcing is not associated with more downwards earnings management.

Overall, the evidence in Table 3 is consistent with the hypothesis that donor firms engage in downward earnings management when their affiliated candidates are contesting in closely watched election races (and thus likely value the informational benefits from earnings management), but not otherwise.

3.2 Outsourcing references in firm disclosures

In this sub-section, we concentrate on firms contributing to candidates in closely watched races. We investigate whether in addition to downwards earnings management, these firms

reduced direct references to outsourcing in their disclosures, as part of an overall strategic response to the increased concerns in 2004 about profits being generated via outsourcing activities. The results in this sub-section are intended to corroborate the results from the preceding accruals tests.

We measure donor firms' disclosure management using reductions in mentions of the word-stem "outsourc" among 10-Ks and 10-Qs. We measure reductions in mentions of "outsourc" by counting the incidences of "outsourc" in 10-Ks and 10-Qs across the quarters of interests (MID-2004) and the benchmark quarters (MID-2003, 2003-04, 2004-05, and MID-2005). Then, the sample's own disclosure practices in the benchmark quarters are used to evaluate its practices in MID-2004. We use "outsourc" because it encompasses common word usages like "outsourc," "outsourcs," "outsourcd," "outsourcing," etc.

Outsourcing usually refers to the act of procuring goods or services through a contract with an outside supplier (Merriam-Webster Dictionary). It does not in itself refer to *overseas* outsourcing (sometimes called offshoring). However, during the 2004 election campaign, the term "outsourcing" was often used in the context of overseas activities (see for example, the Kerry-Edwards campaign commercial "10 Million Jobs," *New York Times*, 2004b, and the Democratic National Convention acceptance speeches of John Kerry and John Edwards, *Washington Post*, 2004a, b). Taylor (2005, p. 368) suggests that the popular definition of outsourcing during the 2004 election "effectively include[d] all imports." Thus, if corporate donors managed information disclosures related to "outsourcing," it is unlikely such information management was conditioned on whether the outsourcing was in fact domestic or overseas in nature. Thus, we test for declines in incidences of "outsourc" and not words like "overseas outsourcing," "offshoring," etc.

Figure 1 presents the total number of mentions of the word-stem "outsourc" in sample-firms' 10-Ks and 10-Qs over the periods of interest. There were 268 occurrences of "outsourc" in MID-2003; 287 in 2003-04; 199 in MID-2004; 300 in 2004-05; and 319 in MID-2005. Thus, an otherwise secular increase in the number of mentions of "outsourc" over the periods studied is interrupted by a dip in MID-2004. Figure 2 presents the number of unique 10-Ks and 10-Qs among the sample-firms that mention the word-stem "outsourc." The number of unique 10-Ks and 10-Qs mentioning "outsourc" was 40 in MID-2003, 61 in 2003-04, 25 in MID-2004, 62 in 2004-05, and 46 in MID-2005. Thus, similar to Figure 1, a dip in MID-2004 is seen in Figure 2. Overall, there is some descriptive evidence consistent with the proposition that sample firms decreased outsourcing-related disclosure in mandatory financial reports in 2004.

To summarize the results in this section, we find: (1) statistical evidence of lower performance-matched discretionary accruals in MID-2004 among donor firms to candidates in closely watched races, (2) no evidence of lower performance-matched discretionary accruals in MID-2004 among donor firms to all other candidates, and (3) descriptive evidence of reduced disclosure of the word-stem "outsourc" in the 10-Ks and 10-Qs of donor firms to candidates in closely watched races during the MID-2004 period. Overall, the evidence in this section is consistent with donor firms to candidates in closely watched races making strategic reporting and disclosure choices prior to the elections in 2004.

4. Association of firms' information management with election outcomes in 2004

In this section, we report on tests of whether donor firms' lower performance-matched discretionary accruals in MID-2004 are associated with election outcomes of related candidates. We conduct a series of multivariate tests at the candidate level and use the *CTW* (candidate to

watch) indicator as an independent variable that distinguishes candidates that compete in closely watched races from those that do not.

The dependent variable in the tests is a censored continuous variable measuring the percentage of votes obtained by candidates in the sample.⁹ Parameters estimates in this regression specification are obtained through maximum likelihood estimation and results are reported in Tables 4 and 5.

The independent variables include candidate-specific characteristics such as: an indicator for whether the candidate is an incumbent (*Incumbent*), an indicator for whether the candidate is a Republican (*Republican*), an indicator for whether the candidate is competing in a Senate race (*Senate*), and an indicator for whether the candidate supported outsourcing-based legislation in the period leading up to the 2004 election (*SponsorMember*). The incumbent indicator controls for the result that incumbents are more likely to win an election (see for example, Gelman and King, 1990). The Republican indicator controls for the possibility of a systematic party association with election outcomes in our sample. The Senate race indicator controls for procedural differences in Senate and House-of-Representative races. The outsourcing legislation variable is constructed by searching for members of Congress who sponsored or co-sponsored legislation to regulate outsourcing during the 108th Congress (2002-2004). This variable controls for any systematic relation between *ex ante* opposition to outsourcing and election outcomes (e.g., the possibility that particularly vulnerable politicians oppose outsourcing as part of a broader populist agenda).¹⁰

Also among independent variables, we include a variable that captures the proportion of votes a candidate receives in her primary election, *PrimaryPct* (if the candidate did not face a

⁹ The dependent variable is censored at zero and one because the percentage of votes obtained in an election cannot be below zero and above one.

¹⁰ Note that this variable can only take the value one if the incumbent dummy is one.

primary challenge, we assume the proportion of primary votes obtained is one). Additionally, we include a variable that captures the number of candidates in the general election, *NumGenCand* (more candidates can be an indication of an incumbent's vulnerability or an indication of a fractured opposition and thus an indication of an incumbent's strength). Finally, we include a variable that measures the percentage vote received in 2004 by President Bush in the state in which the candidate is running (*Pct_BushVote*). This variable is intended to capture constituency-based voter preferences.

Since our regression analyses are at the candidate level, and since more than one firm in our donor sample could have contributed to a given candidate, the firm-based independent variables in our regressions are either *aggregates* or *averages* of firm-level values (i.e., aggregated or averaged across all firms contributing to a given candidate). We have two such firm-based independent variables. The first is a control variable—an aggregate measure of dollar contributions received by candidates from donor firms. The second is our test variable—an average measure of the performance-matched discretionary accruals of donor firms in MID-2004, that is, over the second and third calendar quarters of 2004. These are described in detail below.

Election outcomes are conceivably associated with the dollar contributions received by candidates from the top donor firms. To control for this possibility, we include as an explanatory variable the log of the sum of PAC dollar contributions received by candidates from donor firms over the period 2000-2004. We denote this variable *log(Contribution)*.

We have two different average measures of donor firms' performance-matched discretionary accruals in MID-2004. The first is a simple average across all firms contributing to a given candidate (*MeanPerfAcc*). This measure assumes that earnings management by all

donors to a given candidate is equally important (i.e., all donors have been equally involved in outsourcing activities). Our second measure is based on our *ex ante* measure of outsourcing. If donor firms with a greater workforce reduction in the two years leading up to 2004 are of greatest concern to candidates, lower performance-matched discretionary accruals among such firms are more likely to be associated with election outcomes. Accordingly, we construct a *weighted* average measure of the performance-matched discretionary accruals of all firms contributing to a given candidate, where the weights are the donor firms' average workforce reduction over 2002 and 2003. We call this measure *WF_REDPerfAcc*. We report results using *MeanPerfAcc* in Panels A of our results tables (i.e., Tables 4 and 5) and results using *WF_REDPerfAcc* in Panels B of those tables.

To distinguish the relation between election outcomes and earnings management for candidates in closely watched races, we interact our two proxies of average performance-matched discretionary accruals by the *CTW* indicator. Thus, in Panel A of Table 4, *MeanPerfAcc*CTW* captures the incremental association between election outcomes and earnings management for candidates in closely watched races, while in Panel B, *WF_REDPerfAcc*CTW* captures that incremental association.

In Panel A of Table 4, the coefficient on *MeanPerfAcc* is statistically insignificant, while the coefficient on *MeanPerfAcc*CTW* is negative and statistically significant (95% confidence level). This is consistent with lower performance-matched discretionary accruals among corporate donors being associated with a higher proportion of votes received only for candidates in closely watched races. Results in Panel B are similar to the ones above: the coefficient on *WF_REDPerfAcc* is statistically insignificant, while the coefficient on *WF_REDPerfAcc*CTW* is negative and statistically significant (95% confidence level). To interpret the substantive

significance of these results, consider the following. A two-standard-deviation decrease in *MeanPerfAcc* (*WF_REDPerfAcc*) is associated with a 5% (8.4%) increase in the percentage of votes obtained by candidates-to-watch in our sample. The average candidate-to-watch in our sample received a vote share of 52.7%, suggesting that on the margin, a two-standard-deviation decrease in donor firms' average performance-matched discretionary accruals can be associated with an election victory. The higher marginal effect of *WF_REDPerfAcc*CTW* relative to *MeanPerfAcc*CTW* suggests that the relation between earnings management and election outcomes is particularly strong when donor firms have experienced significant workforce reductions in previous years. Collectively, the results in Table 4 are consistent with the predictions of a "political currency" hypothesis.

Turning to the other independent variables in our regressions, the incumbent dummy and *log(Contributions)* are significantly positive at the 95% confidence level across both panels of Tables 4, indicating that incumbents and candidates receiving more PAC contributions are associated with larger vote shares. Further, we find a significantly negative coefficient on *NumGenCand*, consistent with vote shares being negatively associated with the number of candidates in the race. Finally, we also find significantly lower general-election vote shares for candidates receiving larger primary vote shares and candidates belonging to the Republican Party. The former result is consistent with the proposition that candidates who are more likely to face competitive general elections are less likely to face contested primaries.

In Table 5, we re-estimate the results of the regression in Table 4, but restrict the sample to only those candidates running for the House of Representatives. Procedural differences between House and Senate races can confound the results in Table 4 (where both races are pooled), so the Table 5 analysis is intended to test the robustness of the Table 4 results (we

cannot perform a similar analysis for Senate-only races due to the small sample size). In Panel A of Table 5, the coefficient on *MeanPerfAcc* is statistically insignificant, while the coefficient on *MeanPerfAcc*CTW* is negative and statistically significant (95% confidence level). In Panel B of Table 5, the coefficient on *WF_REDPefAcc* is statistically insignificant, while the coefficient on *WF_REDPefAcc*CTW* is negative and statistically significant (95% confidence level). A two-standard-deviation decrease in *MeanPerfAcc* (*WF_REDPefAcc*) is associated with a 7.6% (10.2%) increase in the percentage of votes obtained by candidates-to-watch in this sub-sample (i.e., House races). The average candidate-to-watch in the House sub-sample received a vote share of 53.9%.

Collectively, the results in Table 5 are consistent with those in Table 4. Specifically, lower average performance-matched discretionary accruals among donor firms are associated with greater vote shares for affiliated candidates; and the results are robust to, and are indeed generally stronger on, weighting the average performance matched discretionary accruals by the degree of outsourcing, as measured by *WF_RED*.

5. Conclusion

The study of accounting and the political process has long been viewed through the political cost hypothesis (Watts and Zimmerman, 1978, 1986). The basic premise of that hypothesis is firms manage earnings in order to *extract* first-order benefits (or avoid first-order costs) from regulators. In this paper, we develop and test a distinct, yet likely, complementary hypothesis: firms manage reported earnings in order to *supply* first-order benefits to regulators. We test whether the management of accounting information is in some circumstances akin to a political contribution from firms to politicians: in other words, whether accounting information

can be used as political currency. By doing so, firms likely assist in the election of friendly regulators and ensure their ability to extract first-order benefits (or avoid first-order costs) in future periods.

To test the political currency hypothesis, we identify a setting in which we are able to form clear directional predictions on firms' management of accounting information for the benefit of allied politicians. Our setting is the US congressional elections of 2004, a presidential election year when the Democratic presidential challenger, Sen. John Kerry, and allied political groups made outsourcing of US jobs a key issue. Stagnant to slow job growth in the years leading up to 2004 helped support that claim. The media picked up on the issue, and quickly corporate outsourcing of US jobs became an important part of the information environment during the election.

We focus on Democratic and Republican candidates in congressional races in 2004. For each candidate, we obtain data on for-profit corporations giving at least \$10,000 that are among the largest twenty donors to the candidate. We use the existence of large cash contributions from the for-profit corporate donors to the identified candidates as evidence of a relationship between the two groups. We partition our sample of candidates into those in closely watched races and those not. Closely watched races are races with no incumbents or with "close, interesting, or contradictory information" being reported by pollsters, according to data compiled by The Green Papers, a non-partisan election-related website. We expect candidates in closely watched races to be particularly vulnerable to political attacks exploiting unfavorable information, such as the outsourcing profits of donor firms. Thus, under the political currency hypothesis, we predict the identified corporate donors to candidates in closely watched races will manage information

related to their outsourcing (therein providing benefits to the candidates in closely watched races).¹¹

While corporate donors *in general* do not exhibit evidence of downward earnings management, corporate donors to candidates in *closely watched races* exhibit significant evidence of downward earnings management in the second and third calendar quarters of 2004. The evidence of downward earnings management is stronger for firms likely to have greater outsourcing activities. Further, donors in this latter set also reduce disclosure of outsourcing-related activities in their 10-Ks and 10-Qs during the second and third calendar quarters of 2004. Additionally, we find that election outcomes for candidates in closely watched races in 2004 are associated with the extent of downward earnings management by donor firms. Specifically, for the average principal candidate, the proportion of votes won increases by about 5% as the average performance-matched discretionary accruals of donor firms decreases by two standard deviations. The association between votes won and earnings management is stronger for firms that show more *ex ante* evidence of outsourcing (on average, a two-standard-deviation decrease in outsourcing-weighted performance-matched discretionary accruals is associated with a 8.4% increase in votes won). Our findings are consistent with firms managing accounting information in circumstances where this is likely to benefit allied politicians, and support the idea of a "political currency" hypothesis.

It is well known that firms contribute money to politicians. It is also widely held that such money, in the form of campaign contributions and lobbying expenditures, is used to buy access to and/or favors from politicians (see for example, Hart, 2001). Firms and politicians establish relationships with one another and the value to firms of such relationships likely increases over

¹¹ It is also possible that donor firms manage information related to their outsourcing to avoid increased scrutiny on themselves during the election season.

time (Snyder, 1992; Kroszner and Stratmann, 2005). When a politician with a well-established relationship to a firm faces a tough election prospect, it is then in the firm's interest to secure that politician's future. One way to do so is to increase monetary contributions to the politician's campaign (see for example, Poole and Romer, 1985; Levitt, 1998). Our findings on the role of (accounting) information as political currency suggest the existence of an alternate way to do so.

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Figure 1: Total number of mentions of the word-stem "outsourc" in 10-Ks and 10-Qs of firms donating to candidates in closely watched races

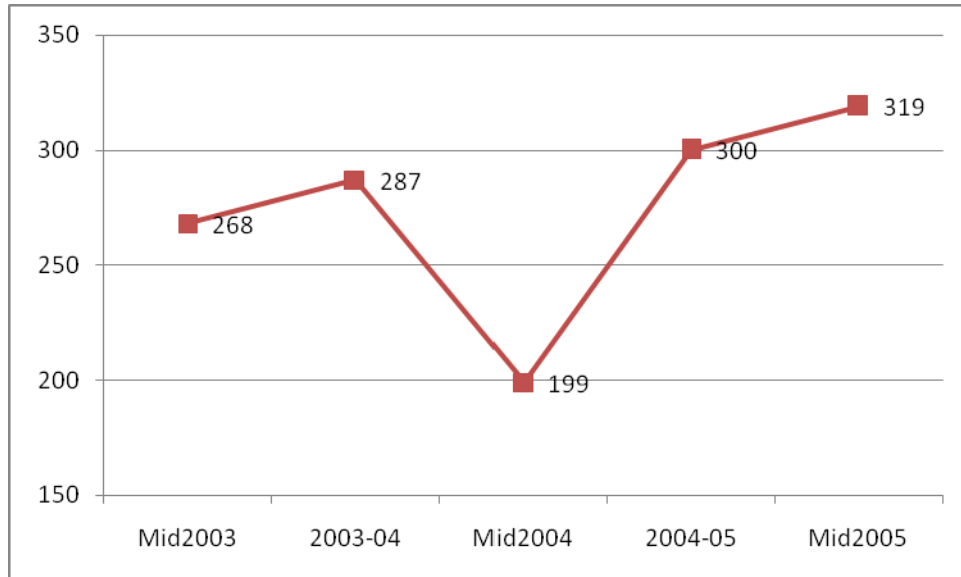
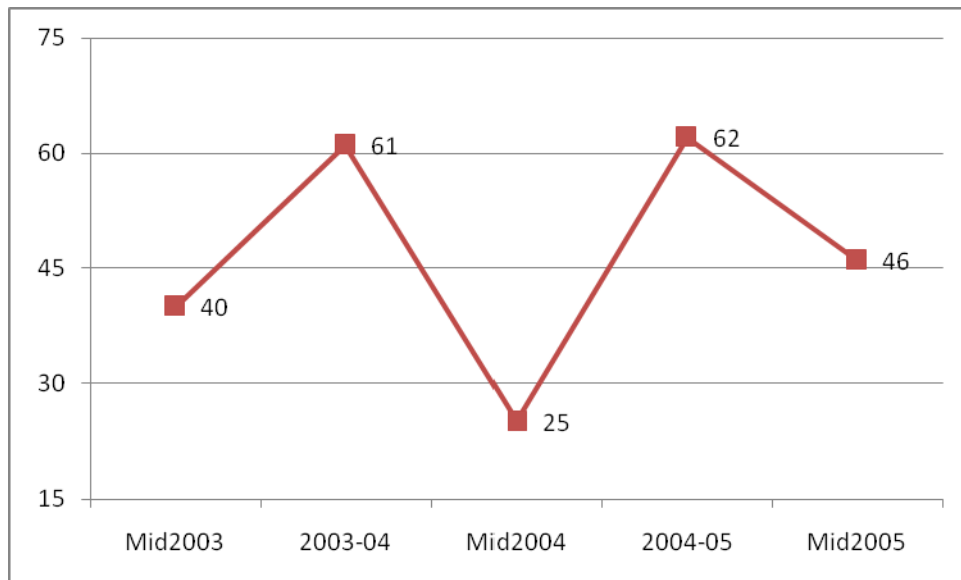


Figure 2: Number of unique 10-Ks and 10-Qs mentioning the word-stem "outsourc" among firms donating to candidates in closely watched races



See Tables 1 and 2 for a description of the sample. The sample period spans the following two-quarter periods: Q2'2003&Q3'2003 ("MID-2003"), Q4'2003&Q1'2004 ("2003-04"), Q2'2004&Q3'2004 ("MID-2004"), Q4'2004&Q1'2005 ("2004-05"), and Q2'2005&Q3'2005 ("MID-2005").

Table 1
Candidate properties

Panel A

Democratic and Republican congressional candidates from states other than Louisiana 836

Less: Candidates without COMPUSTAT corporations among their "top donor lists" 263

Candidates followed 573

Panel B

	<i>CTW = 0</i>	<i>CTW = 1</i>	<i>Total</i>
<i>Democrats</i>	209	37	246
<i>Republicans</i>	269	58	327
<i>House Candidates</i>	444	74	518
<i>Senate Candidates</i>	34	21	55
<i>Non-incumbents</i>	113	69	182
<i>Incumbents</i>	365	26	391
<i>TOTAL</i>	478	95	573

A candidate's "top donor list" is her/his top-20 donors that give at least \$10,000 in the four years leading up to the 2004 election. CTW is "Candidates to Watch," i.e., candidates in congressional races with no incumbents or with "close, interesting, or contradictory information" being reported by pollsters, according to data compiled by The Green Papers, a non-partisan election-related website. The chi-square probabilities for the three sub-panels in Panel B are 0.3903, <0.001, and <0.001, respectively.

Table 2
Summary statistics on sample firms

Panel A: CTWGiver = 1

	MID-2003	2003-04	MID-2004	2004-05	MID-2005
<i>Assets</i>	21,413	23,850	23,941	26,163	26,427
<i>ΔSales</i>	0.0263	0.0266	0.0288	0.0294	0.0309
<i>Return-on-Sales</i>	0.0282	0.0278	0.0432	0.0759	-0.2180
<i>Accruals</i>	-0.0546	-0.0551	-0.0505	-0.0517	-0.0509
<i>Abn. Accruals</i>	-0.0220	-0.0173	-0.0211	-0.0165	-0.0233
<i>PerfAcc</i>	-0.0082	-0.0012	-0.0145	-0.0079	-0.0074
<i>WF_RED</i>	-0.0003	-0.0002	-0.0001	0.0000	0.0000
<i>N</i>	232	235	234	237	230

Panel B: CTWGiver = 0

	MID-2003	2003-04	MID-2004	2004-05	MID-2005
<i>Assets</i>	12,086	13,788	14,119	15,426	15,692
<i>ΔSales</i>	0.0262	0.0338	0.0412	0.0300	0.0249
<i>Return-on-Sales</i>	0.0045	0.0284	0.0338	0.0087	0.0497
<i>Accruals</i>	-0.0394	-0.0371	-0.0352	-0.0445	-0.0387
<i>Abn. Accruals</i>	-0.0150	-0.0065	-0.0151	-0.0159	-0.0207
<i>PerfAcc</i>	0.0000	0.0001	0.0010	-0.0044	-0.0006
<i>WF_RED</i>	-0.0003	-0.0002	-0.0001	0.0000	0.0002
<i>N</i>	318	321	319	319	311

Sample firms are all Compustat firms in the top donor lists of candidates followed. "Candidates followed" and "top donor lists" are defined in Table 1. CTWGiver is a dummy variable coded as one if the sample firm gave at least \$10,000 to a "candidate to watch" in the four years leading up to the 2004 election. "Candidates to watch" are defined in Table 1. Abn. Accruals are abnormal accruals; PerfAcc are performance-matched discretionary accruals; WF_RED is an employment-based measure of outsourcing; all three variables are defined in detail in section 2 of the text. Our sample period spans the following two-quarter periods: Q2'2003&Q3'2003 ("MID-2003"), Q4'2003&Q1'2004 ("2003-04"), Q2'2004&Q3'2004 ("MID-2004"), Q4'2004&Q1'2005 ("2004-05"), and Q2'2005&Q3'2005 ("MID-2005").

Table 3
Trend in performance-matched discretionary accruals across firm-periods in the sample

Panel A

Parameter	Estimate	StdErr	Pr > t
<i>QTR4</i>	0.002	0.006	0.800
<i>MID-2003</i>	-0.004	0.005	0.502
<i>2003-04</i>	-0.001	0.006	0.848
<i>MID-2004</i>	-0.006	0.005	0.223
<i>2004-05</i>	-0.007	0.005	0.167
<i>MID-2005</i>	-0.004	0.006	0.535

Panel B

Parameter	Estimate	StdErr	Pr > t
<i>QTR4</i>	0.001	0.006	0.816
<i>MID-2003</i>	0.000	0.007	0.981
<i>2003-04</i>	-0.001	0.008	0.948
<i>MID-2004</i>	0.001	0.007	0.894
<i>2004-05</i>	-0.005	0.006	0.430
<i>MID-2005</i>	-0.001	0.008	0.924
<i>MID-2003*CTWGiver</i>	-0.008	0.011	0.461
<i>2003-04*CTWGiver</i>	-0.001	0.012	0.918
<i>MID-2004*CTWGiver</i>	-0.015	0.009	0.091
<i>2004-05*CTWGiver</i>	-0.003	0.009	0.710
<i>MID-2005*CTWGiver</i>	-0.007	0.012	0.568

Panel C

Parameter	Estimate	StdErr	Pr > t
<i>QTR4</i>	0.002	0.006	0.702
<i>MID-2003</i>	-0.003	0.008	0.719
<i>2003-04</i>	-0.001	0.009	0.894
<i>MID-2004</i>	0.002	0.007	0.820
<i>2004-05</i>	-0.008	0.007	0.232
<i>MID-2005</i>	0.001	0.008	0.944
<i>MID-2003*CTWGiver</i>	-0.003	0.012	0.795
<i>2003-04*CTWGiver</i>	0.000	0.013	0.983
<i>MID-2004*CTWGiver</i>	-0.017	0.009	0.072
<i>2004-05*CTWGiver</i>	-0.005	0.009	0.592
<i>MID-2005*CTWGiver</i>	-0.014	0.011	0.195
<i>MID-2003*WF_RED</i>	-4.043	3.620	0.265
<i>2003-04*WF_RED</i>	0.177	5.417	0.974
<i>MID-2004*WF_RED</i>	1.914	5.073	0.706
<i>2004-05*WF_RED</i>	-8.645	6.175	0.163
<i>MID-2005*WF_RED</i>	4.122	5.452	0.450
<i>MID-2003*CTWGiver*WF_RED</i>	8.421	10.187	0.409
<i>2003-04*CTWGiver*WF_RED</i>	8.826	11.378	0.439
<i>MID-2004*CTWGiver*WF_RED</i>	-15.737	8.363	0.061
<i>2004-05*CTWGiver*WF_RED</i>	15.058	12.638	0.235
<i>MID-2005*CTWGiver*WF_RED</i>	9.847	10.880	0.366

The sample and *CTWGiver* are defined in Table 2. The explanatory variables include a fourth-fiscal-quarter indicator and indicator variables representing the following two-quarter periods: Q2'2003&Q3'2003 ("MID-2003"), Q4'2003&Q1'2004 ("2003-04"), Q2'2004&Q3'2004 ("MID-2004"), Q4'2004&Q1'2005 ("2004-05"), and Q2'2005&Q3'2005 ("MID-2005"). *WF_RED* is an employment-based measure of outsourcing defined in detail in section 2 of the text. Standard errors are clustered at the firm level.

Table 4

Censored regression: Dependent variable is percentage of votes obtained by the candidate

Panel A

Parameter	Estimate	StdErr	Pr > t
<i>Intercept</i>	0.374	0.066	<.0001
<i>Incumbent</i>	0.245	0.020	<.0001
<i>SponsorMember</i>	-0.003	0.023	0.883
<i>Republican</i>	-0.050	0.011	<.0001
<i>Senate</i>	-0.031	0.021	0.149
<i>PrimaryPct</i>	-0.127	0.034	0.000
<i>NumGenCand</i>	-0.027	0.005	<.0001
<i>Pct_BushVote</i>	0.061	0.073	0.407
<i>CTW</i>	-0.002	0.018	0.914
<i>log(Contributions)</i>	0.026	0.005	<.0001
<i>MeanPerfAcc</i>	0.106	0.133	0.422
<i>MeanPerfAcc *CTW</i>	-0.682	0.335	0.042
<i>Sigma</i>	0.118	0.004	<.0001
		LL	351.43

Panel B

Parameter	Estimate	StdErr	Pr > t
<i>Intercept</i>	0.331	0.082	<.0001
<i>Incumbent</i>	0.233	0.024	<.0001
<i>SponsorMember</i>	0.002	0.030	0.938
<i>Republican</i>	-0.037	0.013	0.005
<i>Senate</i>	-0.018	0.025	0.479
<i>PrimaryPct</i>	-0.089	0.040	0.029
<i>NumGenCand</i>	-0.025	0.005	<.0001
<i>Pct_BushVote</i>	0.132	0.084	0.117
<i>CTW</i>	-0.027	0.022	0.211
<i>log(Contributions)</i>	0.022	0.007	0.001
<i>WF_REDPerfAcc</i>	0.063	0.119	0.597
<i>WF_REDPerfAcc*CTW</i>	-1.040	0.419	0.013
<i>Sigma</i>	0.117	0.004	<.0001
		LL	264.36

The sample is the set of 573 candidates followed described in Table 1. *Incumbent* is an indicator for whether the candidate was a member of the 108th Congress (2002-2004). *SponsorMember* is a dummy variable coded one if the candidate sponsored or co-sponsored legislation to regulate outsourcing during the 108th Congress, zero otherwise. *Republican* is an indicator for whether the candidate is a Republican. *Senate* is an indicator for whether the candidate is contesting in a

US Senate race. *PrimaryPct* captures the proportion of votes the candidate received in her/his primary election (if the candidate did not face a primary challenge, we assume the proportion of primary votes obtained is one). *NumGenCand* captures the number of candidates in the race being examined. *Pct_BushVote* is the year 2004 percentage vote share received by President Bush in the state in which the candidate is running. *CTW* is "candidate to watch" defined in Table 1. *log(Contributions)* is the log of the sum of dollar amounts contributed by sample firms (defined in Table 2) to a given candidate. Proxies for performance-matched discretionary accruals are defined in detail in section 2 of the paper.

Table 5
Censored regression for candidates running for the House of Representatives: Dependent variable is percentage of votes obtained by the candidate

Panel A

Parameter	Estimate	StdErr	Pr > t
<i>Intercept</i>	0.474	0.070	<.0001
<i>Incumbent</i>	0.262	0.021	<.0001
<i>SponsorMember</i>	0.007	0.025	0.773
<i>Republican</i>	-0.052	0.012	<.0001
<i>PrimaryPct</i>	-0.158	0.037	<.0001
<i>NumGenCand</i>	-0.050	0.006	<.0001
<i>Pct_BushVote</i>	0.060	0.076	0.429
<i>CTW</i>	-0.003	0.019	0.871
<i>log(Contributions)</i>	0.024	0.006	<.0001
<i>MeanPerfAcc</i>	0.111	0.134	0.408
<i>MeanPerfAcc *CTW</i>	-0.828	0.386	0.032
<i>Sigma</i>	0.116	0.004	<.0001
		LL	324.21

Panel B

Parameter	Estimate	StdErr	Pr > t
<i>Intercept</i>	0.437	0.085	<.0001
<i>Incumbent</i>	0.249	0.025	<.0001
<i>SponsorMember</i>	0.028	0.034	0.402
<i>Republican</i>	-0.037	0.013	0.006
<i>PrimaryPct</i>	-0.110	0.043	0.010
<i>NumGenCand</i>	-0.053	0.007	<.0001
<i>Pct_BushVote</i>	0.147	0.086	0.089
<i>CTW</i>	-0.028	0.023	0.234
<i>log(Contributions)</i>	0.019	0.007	0.006
<i>WF_REDPerfAcc</i>	0.104	0.124	0.400
<i>WF_REDPerfAcc*CTW</i>	-1.082	0.461	0.019
<i>Sigma</i>	0.114	0.004	<.0001
		LL	246.78

See Table 4 for variable definitions.