The Impact of Political Connectedness on Cash Holdings: Evidence from *Citizens United*

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Abstract

What motivates a company to become politically connected and what impact does political connectedness have on corporate policies? To address this question, we exploit an exogenous Supreme Court decision (*Citizens United*) that lifted all restrictions on corporate political contributions. We find a significant increase in the cash holdings levels of historically politically connected firms relative to both before the event and relative to historically non-politically connected firms. This result is exacerbated by poor corporate governance quality, characterized by busy board members, excessive CEO compensation, and a lack of investor involvement in politically-oriented governing policies. We further document a significantly negative market reaction to politically connected firms surrounding *Citizens United*. These findings are consistent with a positive association between agency costs and political connectedness.

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"At bottom, the Court's opinion [in Citizens United] is thus a rejection of the common sense of the American people, who have recognized a need to prevent corporations from undermining self-government since the founding, and who have fought against the distinctive corrupting potential of corporate electioneering since the days of Theodore Roosevelt. It is a strange time to repudiate that common sense. While American democracy is imperfect, few outside the majority of this Court would have thought its flaws included a dearth of corporate money in politics."
– Dissenting opinion of Supreme Court Justice John Paul Stevens[1]

I. INTRODUCTION

Does a firm's political connectedness influence corporate policies? The degree of political connectedness of a corporation may indeed significantly influence the way in which its finances and operations are managed. However, existing insights into political connectedness in relation to corporate policies are relatively scarce and inconclusive, likely owed at least in part to endogeneity concerns. Specifically, because they are jointly determined, political connectedness and corporate policies are endogeneously related. A valid method to minimize endogeneity problems is to pose a research question in the context of a natural experiment. Natural experiments offer a highly desirable empirical setting in which an exogenous shock enables the researcher to exploit variation in the relationship of interest (i.e., corporate policies and political connectedness) while better controlling for factors that might otherwise undermine the reliability of statistical inferences. By exploiting exogenous and unanticipated variation in corporate political connectedness associated with a landmark Supreme Court ruling, *Citizens United v. Federal Election Commission* (hereafter, "*Citizens United*"), we are able to help fill a gap in the literature with regard to how political connectedness affects a firm's corporate policies. In particular, we evaluate for whether political connections affect corporate cash holdings policies.

All else equal, it is reasonable to expect that the cash holdings of a politically connected firm will differ from those of a non-politically connected firm. Specifically, it may be the case

[1] Citizens United v. FEC, 130 S. Ct. 876 (2010), (Stevens, J., dissenting).

that the primary benefit to be derived from political connections is liquidity (e.g., Faccio 2010; Faccio, Masulis, and McConnell 2006). For example, politically connected firms are significantly more likely to be bailed out by the government in times of distress relative to non-politically connected firms (Faccio, Masulis, and McConnell 2006), and are also able to secure preferential access to financing (e.g., Bathon 2012; Mildenberg and Robison 2011) as well as profit from generous tax breaks (e.g., Walters 2012). Under this view, a politically connected firm is characterized by fewer liquidity constraints and can be expected to hold less cash relative to a non-politically connected firm (Liquidity Hypothesis).

A competing view indicates that the political connectedness of a company is driven by its managers' political agenda – an agenda that diverges from that of the company's stakeholders. Under this hypothesis, political connectedness generates an additional avenue through which managers can pursue personal benefits at the expense of shareholders. As agency costs are associated with higher cash holdings (e.g., Jensen 1986; Stulz 1990), this view predicts that politically connected firms are more likely to hoard cash (Agency Cost Hypothesis).

To test these competing hypotheses, we exploit the exogenous variation in corporate political connectedness associated with a landmark Supreme Court ruling, *Citizens United v. Federal Election Commission*. Decided in January 2010, *Citizens United* lifted all limits on corporate political contributions. However, the verdict was unanticipated and did not come easily, as the issue was accompanied by considerable disagreement (e.g., Bravin 2010; Barnes 2010b). The 5-4 vote in favor of its passing further verified division amongst members of the Court.[2]

[2] Soon after the ruling, President Barack Obama voiced vigorous criticism, declaring the decision "a green light to a new stampede of special interest money" (Barnes and Eggen 2010). The majority vote adamantly defended their belief that corporate political contributions are a form of free speech and, as such, constitutional under the First Amendment. Not surprisingly, the months following passage of *Citizens United* have been marked by controversy

The controversial and uncertain nature of *Citizens United* offers an ideal research setting to examine the effect of political connectedness on corporate policies. Specifically, much of the extant, related literature relies on a simple, cross-sectional research design that is subject to endogeneity concerns. Since predicting the likely outcome of *Citizens United* was highly infeasible (e.g., Barnes 2010a; Eggen 2010), it is difficult to argue that corporations were able to anticipate its favorable vote and proactively adjust their behaviors accordingly. The surprise nature of *Citizens United* lends to its credibility as a valid natural experimental setting.

A primary channel through which corporations become politically connected is through campaign contributions to candidates for office. We follow Aggarwal, Meschke, and Wang (2012), Goldman, Rocholl, and So (2009) and others in basing our definition of political connectedness on corporate campaign contributions, as reported in the Center for Responsive Politics. Specifically, we define a firm as politically connected if its median firm-level, pre-*Citizens United* political contributions (scaled by net total assets) falls in the top quartile.

By operationalizing the political connectedness measure in the natural experiment of *Citizens United*, this paper provides novel evidence on the impact of political activism on corporate cash holdings. Specifically, we utilize a difference-in-differences approach to capture differences between firms of differing political connectedness and during different periods of time (i.e., pre- versus post-*Citizens United*). After controlling for traditional determinants of cash holdings, we find that switching from non-politically connected status to politically connected

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and turmoil, with some lawmakers and investors urgently pleading that the Supreme Court reconsider the expansive and profuse provisions accompanying *Citizens United*, in addition to urging the Securities and Exchange Commission to consider adopting disclosure requirements for corporate political contributions. Notably, in June 2012, the Supreme Court refused a request to reconsider its *Citizens United* decision (Bravin 2012). As of November 2012, advocates for campaign finance reform were pushing the SEC to begin mandating disclosure of corporate political contributions (Bogardus 2012). On a micro level, NorthStar Asset Management has drafted numerous proposals requiring shareholder input on whether their approval should precede a corporation's political spending decisions. A first round of such proposals filed in 2011 at Home Depot, FedEx, and Procter & Gamble received little shareholder support. A second round of proposals was filed in 2012 at Chubb, Ecolab, Google, Home Depot, and Johnson & Johnson, among others (Goodridge and Jantz 2012).

status results in an incremental increase in corporate cash holdings of almost 20% following passage of *Citizens* United. Poor corporate governance quality also exacerbates the agency problems inherent to politically connected firms. Specifically, firms with busy boards of directors and overcompensated CEOs retain even more cash relative to their well-governed counterparts. Collectively, these findings favor the Agency Cost Hypothesis.

Our paper also offers insights into the impact of investor activism on agency conflicts. In particular, we investigate whether the mere entertaining of a politically-oriented shareholder proposal acts as a monitoring mechanism and, by extension, reduces the agency conflicts inherent to politically connected firms. We find that entertaining a politically-oriented shareholder proposal indeed provides an incremental reduction in the cash holdings of politically connected firms. The effect is more prominent for shareholder proposals entertained in the post Citizens United period. Overall, these findings support the existence of agency costs in politically connected firms.

Our findings also reveal a value-decreasing effect of political connectedness. Specifically, for historically politically connected firms, we document an abnormal price drop of –0.475% on announcement date and a cumulative abnormal loss of –1.219% five days after announcement date. In contrast, historically non-politically connected firms enjoy positive returns on announcement date in the order of 0.269%. The difference between the announcement date reactions of politically connected firms and non-politically connected firms is highly statistically significant. These results further support to the notion that political connectedness enhances agency problems.

This paper is related to extant literature that examines the impact of political connectedness on corporate policies. Previous studies have shown that political connectedness is

significantly related to executive compensation (Aslan and Grinstein 2012), leverage (Boubakri, Cosset, and Saffar 2012; Faccio 2010; Hutton, Jiang, and Kumar 2011), and liquidity (Boubakri, El Ghoul, and Saffar 2012; Hill, Fuller, Kelly, and Washam 2010). With regard to cash holdings, Boubakri, El Ghoul, and Saffar (2012) find that politically connected firms hold more cash relative to non-politically connected firms, suggestive of agency costs. Also consistent with agency conflicts affecting politically connected firms are the results of Aggarwal, Meschke, and Wang (2012), who find that an increase in political contributions is associated with a decrease in excess returns, particularly for poorly-governed firms. In a study of political *lobbying* expenditures, Hill, Fuller, Kelly, and Washam (2010) observe an inverse relation between cash holdings and lobbying costs, thus favoring a liquidity story. However, with the exception of Hutton et al. (2011), none of the aforementioned studies utilize a significant and exogenous macroeconomic shift in the corporate political connectedness landscape in an effort to draw more accurate inferences. That is, these studies almost exclusively rely on cross-sectional data, and inferences drawn from cross-sectional data are subject to endogeneity problems. In direct contrast, the primary focus and findings of our paper revolve around a natural experiment, thus significantly alleviating endogeneity concerns such that a link between political connectedness and corporate policies can be established.

This paper also contributes to studies on the determinants of cash holdings. Mikkelson and Partch (2003) find that larger cash holdings promote investment while Opler, Pinkowitz, Stulz, and Williamson (1999) show that larger cash holdings can help offset the riskiness of cash flows. Precautionary motives behind the buildup of cash reserves are also highlighted in work by Han and Qiu (2007). Foley, Hartzell, Titman, and Twite (2007) find that tax costs associated with the repatriating of foreign income provide further motivation to hold more cash, while insights

offered by Dittmar and Mahrt-Smith (2007) and Harford, Mansi, and Maxwell (2008) reveal a link between governance quality and corporate savings. We contribute to this literature by showing that political connectedness also influences a firm's cash holdings, and that poor corporate governance quality enhances this relation.

Our paper also adds to emerging literature on the value-decreasing effects of political connections. In a study of the effects of *Citizens United*, Coates (2012) finds that political connectedness is negatively related to shareholder value and shareholder rights by utilizing Tobin's Q ratio. However, previous studies show that Tobin's Q ratio is correlated with several other factors (e.g., growth opportunities, capital structure) which do not fully reflect shareholder value (Anderson and Reeb 2003; Hail and Leuz 2009). Instead, we offer a more direct examination of shareholder value by making use of event study methodology. For politically connected firms in France, Bertrand, Kramarz, Schoar, and Thesmar (2006) find that political connectedness translates into lower profitability. In a study of newly privatized firms in China, Fan, Wong, and Zhang (2007) document a value-decreasing effect of politically connected CEOs. Political connectedness is also known to be associated with greater information asymmetry between managers and investors (Chen, Ding, and Kim 2010) as well as lower quality earnings (Chaney, Faccio, and Parsley 2011). These results suggest that political connectedness increases systematic risk. Our study contributes to this stream of literature by documenting a link between political connectedness and agency conflicts that is magnified by poor corporate governance quality.

The remainder of the paper is organized as follows. A discussion of *Citizens United* is presented in the next section. Section III presents our hypotheses and related literature. Section

IV describes the sampling procedure, and our empirical analysis is offered in section V. We conclude in section VI.

II. BACKGROUND

Historically, corporations were prohibited from actively campaigning on behalf of politicians through donations of independent expenditures, which were strictly forbidden during the period from World War II through 2010.[3] In a landmark Supreme Court decision handed down in January 2010, such prohibitive laws were rendered unconstitutional under the First Amendment and corporations were effectively freed to engage in political activities of this nature and essentially of all other varieties to the extent of their choosing. Some aspects of the regulatory environment surrounding corporate political activism did remain unchanged following *Citizens United*. Notably, corporations are still prohibited from contributing corporate funds directly to a political candidate. Instead, corporations derive a large proportion of their political connectedness through Political Action Committee (PAC) contributions. Managers, employees, and shareholders can contribute to their company's PAC, and subsequently the PAC will channel the said funds to a political candidate. Interestingly, corporations are permitted to use internal funds to finance to fundraising efforts of PACs. Despite these regulatory consistencies, a logical yet relatively unexplored implication of *Citizens United* is an increase in corporate political activism through all means available, and not just through channels that were previously off limits.

[3] Independent expenditures are defined as funds "expressly advocating the election of or defeat of a clearly identified candidate who is not made in cooperation, consultation, or concert with, or at the request or suggestion of, a candidate, a candidate's authorized committee, or their agents, or a political party or its agents" (11 CFR 100.16(a)). An example of an independent expenditure would be a corporation's decision to finance television commercials endorsing the candidate of their choosing.

Election spending reached new highs following passage of *Citizens United*. The estimated $6 billion spent on the year 2012 election represents a new record and exceeds the cost of the second most expensive election by more than $700 million (Center for Responsive Politics 2012). While corporations have never been barred from political activism in an attempt to influence lawmakers or reform policies, passage of *Citizens United* essentially opened the floodgates for corporations to take an active, direct, and economically meaningful role in campaigning for preferred political candidates. Moreover, given the previously-documented complementary nature of the various types of political activism, *Citizens United* stimulated corporate political involvement of all forms, even those types that were allowed to be used prior to its passage (Coates 2012).

It is important to recognize that many forms of corporate campaign activity need not be disclosed. This reality complicates studies of political connectedness, since corporations can choose to strategically disguise their political activism. For example, a firm can avoid disclosure altogether by channeling political contributions through a separate entity (i.e., a "conduit", or "independent" organization). In the case that the independent entity subsequently contributes said funds to a political campaign, it may be required to disclose the identity of its donors. However, if the entity restricts its contributions to independent expenditures, no disclosure is required. These strategic yet unobservable channels of political activism were utilized even more in the post-*Citizens United* period. Specifically, the identities of donors who sourced more than 50 percent of the $266.4 million contributed by outside groups in 2010 remain unknown (Public Citizen 2010). The unobservable nature of some forms of corporate political activity results in conservative estimates of political contributions and should only bias against our ability to document a link between political connectedness and corporate policies.

A distinction of this paper is its focus on *Citizens United*, a powerful and controversial decision but one whose effects are limited to the United States. That is, our focus differs from broad, cross-country studies (e.g., Boubakri, El Ghoul, and Saffar 2012) in that we focus on a specific country (the United States) and the impact of a specific exogenous shock (*Citizens United*). Restricting our focus to a single country enables us to hold important within-country factors constant, such as cultural values, political views, and government structure. That is, it is difficult to control for cross-country effects arising through country-specific corporate governance mechanism, political regimes, and cultural values. Our within-country research design overcomes these potential identification problems.

III. HYPOTHESIS DEVELOPMENT

Liquidity Hypothesis

Do politically connected firms enjoy liquidity? Faccio, Masulis, and McConnell (2006) find that politically connected firms are significantly more likely to be bailed out by the government in times of distress relative to non-politically connected firms. This implicit guarantee tends to disincentivize a firm from retaining excess cash. For example, Solyndra, a former manufacturer of solar panels, is thought to have reaped significant financial benefits in response to its political connections. Specifically, in 2009, the company received a $535 million loan guarantee from the Department of Energy (DOE). In August 2011, Solyndra filed for bankruptcy, with the government projected to recoup a mere 19 cents on the dollar (Bathon 2012). A twist in this story originates in George Kaiser, an extremely wealthy Oklahoma oilman whose foundation owned one-third of the company. Kaiser is reported to have raised between $50,000 and $100,000 for President Barack Obama's 2008 campaign for presidency. One might conclude that Kaiser's loyalty to the President paid off in a big way; namely, some have suggested that the

Solyndra plant built in Kaiser's hometown of Tulsa, Oklahoma, was secured through his generous political contributions (Mildenberg and Robison 2011).

Another instance of politicians catering to the liquidity preferences of their donors arises through the combined efforts of congressional representatives Brian Bilbray, Erik Paulsen, and Jim Gerlach, who in June 2012 voted against a 2.3% excise tax on medical devices (H.R. 436) that went on to pass by a vote of 270-146. An examination of the legislators' contribution inflows reveals clear political motives, with PACs of leading health care companies such as Abbott Laboratories, Life Technologies Corporation, and the Medical Device Manufacturers Association topping Bilbray's list of major donors (Walters 2012). A politician's decision to promote the profitability of his donors (in this case, through tax breaks) represents a clear channel through which firms can use political contributions to enhance their financial stability.

According to the Liquidity Hypothesis, politically connected firms enjoy liquidity and soft-budget constraints that effectively free up the flow of cash (e.g., Boubakri, Cosset, and Saffar 2012). In particular, under this view, politically connected firms' preferential access to financing theoretically promotes an absence of financial constraints. In contrast, non-politically connected firms are compelled to hold more cash to make up for their financially constrained position. Hence, according to the Liquidity Hypothesis, politically connected firms should hold *less* cash relative to their less-connected counterparts. Moreover, the Liquidity Hypothesis predicts a positive market reaction to politically connected firms surrounding the passage of *Citizens United*.

Agency Cost Hypothesis

As illustrated next, several sources have presented arguments for why the political motives of managers create or further exacerbate existing conflicts with stakeholders. Notably, the

potential negative consequences in this context are perhaps best identified through the testimony of Columbia law professor John C. Coffee, Jr. before the U.S. House Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises, who noted the following:

> "…The goal, however, has to be not only to increase transparency and disclosure, but to give shareholders an effective remedy by which to challenge decisions of which they disapprove, because this is a world in which shareholder and managerial interests are not well aligned. There may be perfectly legitimate corporate contributions, but for every dollar contributed by a corporation that maximizes shareholder wealth, there are other dollars that are contributed to pursue the personal, political, or ideological agenda of senior managers, all of that is hidden… [*Citizens United*] assumes that shareholders have practical remedies by which to contest decisions of managers to make contributions. In fact, they have very few rights." (Corporate Governance after *Citizens United* 2010)

As an example of a response related to Professor Coffee's and others' pleas, in June 2011, shareholders of Home Depot entertained a proposal that would have allotted them the right to vote for or against campaign contributions. In turn, corporate executives are purported to have strongly encouraged shareholders to vote against the proposal and, as such, shareholders soundly rejected the proposal, with only about 5% of shareholders voting in favor of its passing. The proposal was filed by NorthStar Asset Management – a firm known for its socially responsible investing – with the hope that greater transparency and more empowered shareholders would better align the values of NorthStar and Home Depot (Bogle 2011).

More recent headlines directly tied to *Citizens United* involve incidents in which top-level corporate executives use their stature to influence the political leanings and voting decisions of lower-level employees, consistent with the presence of agency problems. For example, an October 2012 article posted to *The New York Times* website reveals that Dave Robertson, president of Koch Industries, distributed a politically-motivated information packet – complete with a list of endorsed candidates – to more than 30,000 employees of its subsidiary, Georgia-Pacific (Greenhouse 2012). These instances of political coercion are only becoming more

common in the post-*Citizens United* period, as the freedoms imparted by the law have left many managing directors to believe that money is not the only unrestricted resource to be used for political means, but that employees can be used, too (e.g., Paarlberg 2012, Charles 2012, McCarthy 2012).

According to the Agency Cost Hypothesis, politically connected firms suffer from agency problems that stem from a lack of alignment between manager and stakeholder incentives. This tension leads management to pursue their own interests, often at the cost of those they serve and potentially opening the door for a politician to use the politically connected corporation to advance his own agenda. Moreover, agency costs are known to be strongly associated with the retention of excess cash (e.g., Chaney, Faccio, and Parsley 2011; Jensen 1986; Stulz 1990). Thus, according to the Agency Cost Hypothesis, politically connected firms should hold *more* cash relative to their less-connected counterparts, and this effect should be exacerbated by weak corporate governance. Moreover, the Agency Cost Hypothesis predicts a negative market reaction to politically connected firms surrounding the passage of *Citizens United*.

IV. SAMPLE

Political contributions data are gathered from the Center for Responsive Politics (CRP). The CRP provides numerous data sets that can be used to gauge political activism, including campaign finance, lobbying, and the personal financial conditions of members of Congress. The focus of this paper is on corporate campaign finance activity, as gathered from the CRP and originating through Federal Election Commission (FEC) records. Major subsets of the campaign finance data include individual contributions and political action committee (PAC) contributions, both to candidates and to committees. Any individual contributing more than $200 is required by

law to report the contribution, as well as to disclose their employer and occupation to the FEC. The stringency of this requirement sheds light on the importance of employee-level contributions as a measure of a company's political activism.

To compute a measure of corporate campaign finance activity, we gather contribution-level observations for contributions made to candidates by PACs and by employees, both those tied to parent and to wholly-owned subsidiary companies.[4] Subsequently, we pool all contributions at the parent-level each fiscal year. PAC committee names and identifying information are gathered from the FEC and then matched to contribution-level observations in the CRP data. Employee contributions are identified by company name within the CRP data.[5] Consistent with Goldman, Rocholl, and So (2009) and Hill, Fuller, Kelly, and Washam (2010), we restrict the sample to S&P 500 firms.[6] Financial statement data are gathered from the Compustat Fundamentals Annual file, stock returns are collected from CRSP, and names of subsidiary companies are retrieved from Mergent Online. We pull governance data from the RiskMetrics Directors database, RiskMetrics Shareholders Proposals file, and Execucomp Annual

[4] Consistent with recommendations offered in the Center for Responsive Politics' OpenSecrets user's guide, we impose several exclusions. In the employee subsample, the following contribution-level observations are excluded: noncontributions (RealCode beginning with "Z9"), contributions to committees (RecipID beginning with "N"), and contributions to PACs (RecipID beginning with "P"). In the PAC subsample, the following contribution-level observations are excluded: noncontributions (RealCode beginning with "Z9") and transfers between committees as well as contributions to joint fundraising committees (RealCode beginning with "Z4").

[5] To match by company (employer) name, we conduct a series of wildcard searches using SAS statistical software. The wildcard we use most frequently is the percentage symbol (%), which represents 0 or more characters within a given character string. We use wildcards in place of certain words such as "the", "and", "international", "corporation", "compan[ies]", and "inc[orporated]" to account for the possibility that an employee purports to work at, e.g., "Anheuser-Busch" versus "Anheuser-Busch Companies" versus "Anheuser-Busch Companies Inc." versus "The Anheuser-Busch Companies Inc.", etc. We also convert all symbols to wildcards to allow for possibilities such as "Johnson & Johnson" versus "Johnson and Johnson." We also conduct searches by compressing company names such that stray or missing spaces do not affect our search results (e.g., transforming "Fannie Mae" into "FannieMae"). As a final pass, we use a combination of the SOUNDEX and COMPGED functions in SAS. SOUNDEX (a "sounds like" operator) is helpful in identifying relevant observations that were otherwise not picked up in the wildcard searches, such as cases where the company name is misspelled or letters are transposed. COMPGED is then used on the SOUNDEX results to identify the minimum generalized edit distance between the resulting matching company names and the actual company names. Results of all "fuzzy" searches are manually reviewed for actual matches, and coded accordingly.

[6] A firm that entered and/or departed the S&P 500 during the sample period is included in the analysis during the years in which they belonged to the index.

Compensation database. Our sample spans federal election cycle years 2006, 2008, 2010, and 2012, or fiscal years 2005 to 2011.[7,8,9] To be included in the sample, a firm must appear in the data set in at least one pre-*Citizens United* year (2005, 2006, 2007, or 2008), and at least one post-*Citizens United* year (2010 or 2011).

V. EMPIRICAL ANALYSIS

Table 1 depicts the distributional properties of cash holdings levels and their determinants. Descriptive statistics of political contributions and key variables presented by degree of political connectedness are also provided. The mean (median) of firm-level political contributions is $142,448 ($57,225) across all firms, $24,703 ($4,800) for historically non-politically connected firms, and $297,735 ($169,170) for historically politically connected firms. When considering the sample in the aggregate, PAC contributions represent about 53% of the 373,391 contribution-level observations in our data set, but 67% of the sample-wide total contributions of slightly more than $440 million dollars. Non-executive employee contributions represent 35% of all contributions by count and 23% by dollar value, while executive contributions constitute 12% of all contributions by count and 9% by dollar value.

Table 2 provides univariate tests of cash holdings for firms exhibiting varying degrees of pre-*Citizens United* political connectedness. The most politically connected firms (upper quartile) hold significantly larger cash balances than less politically connected firms (lower quartile) in

[7] Our RiskMetrics Shareholder Proposals and RiskMetrics Directors databases span the period 2007-2011, while data used to estimate a CEO's excess compensation are gathered from the Execucomp Annual Compensation database and are available for the period 2005-2011.

[8] Data for the 2012 election cycle were not available in full at time of this draft. As such, we restrict the upper bound of the sample to fiscal year 2011. Since most of our statistical analyses utilize a measure of *historical* political activism, defined in terms of political contributions during years 2005-2008, we do not require political contributions for year 2012, even if those data were available.

[9] To provide a cleaner test, fiscal year 2009 observations (i.e., those immediately preceding passage of *Citizens United*) are excluded. The main results of the paper are qualitatively very similar if this restriction is not imposed.

both the pre- and post-*Citizens United* periods. This initial evidence supports the Agency Cost Hypothesis. Comparing cash holdings levels in the pre- and post-*Citizens United* periods within each quartile, we find that most politically connected firms report larger cash balances (as a proportion of net total assets) in the post-*Citizens United* period. That is, politically connected firms significantly increased their cash holdings from the pre- to post-*Citizens United* periods, whereas the difference in cash holdings (pre- versus post-*Citizens United*) of the lower quartile of firms based on political connectedness is not statistically significant.

Most importantly, we find no significant difference between the most politically connected firms (upper quartile) and least politically connected firms (lower quartile, ignoring non-politically active firms) on important, traditional determinants of cash holdings. Specifically, in the post-*Citizens United* period, these politically connected firms do not significantly differ from non-politically connected firms on the basis of size (either in terms of Net Total Assets or Sales), leverage, profitability, or the propensity to pay dividends. Additionally, regarding governance quality, these groups of firms do not significantly differ on the basis of busy board representation or investor involvement in political matters. Moreover, within quartiles of historical political connectedness, very few firm characteristics or measures of governance quality significantly differ in the post-*Citizens United* period relative to the pre-*Citizens United* period.

Evaluating the potential impact of political connectedness on cash holdings requires that we incorporate a measure of political activism. To examine how cash holdings changed as a function of the change in political contributions in the post-*Citizens United* period relative to the pre-*Citizens United* period for our S&P 500 firms, we estimate the following specification:

$$\Delta\text{Log(Cash/NTA)}_i = \beta_0 + \beta_1 \Delta\text{Contributions/NTA}_i + \beta_2 \Delta \mathbf{X_i} + \varepsilon_i \quad (1)$$

where Contributions/NTA is our measure of political involvement, $\mathbf{X_i}$ is vector of traditional determinants of cash holdings, and changes are computed as the value in 2010 (post-*Citizens United*) relative to the value in 2008 (pre-*Citizens United*).[10] If the level of corporate cash holdings is decreasing in the degree of political connectedness (Liquidity Hypothesis), we expect to find a negative β_1 coefficient. If instead the level of corporate cash holdings is increasing in the degree of political connectedness (Agency Cost Hypothesis), we expect to find a positive β_1 coefficient. In modeling the determinants of cash holdings, we control for several firm characteristics. Specifically, consistent with Opler, Pinkowitz, Stulz, and Williamson (1999), Harford, Mansi, and Maxwell (2008) and others, we control for firm size (using the natural logarithm of net total assets, where net total assets is total assets net of cash and cash equivalents), leverage, growth opportunities, contemporaneous cash flows, the standard deviation of cash flows, net working capital, R&D expenditures, capital expenditures, and the propensity to pay dividends. Although this model does not consider historical political activism, it provides a preliminary look into whether and, if so, how these two amounts differed in 2010 relative to 2008. In particular, a positive (negative) relationship would favor the Agency Cost Hypothesis (Liquidity Hypothesis).

From Table 3, we find a positive and significant coefficient on ΔContributions/NTA (p-value = 0.043). That is, as political contributions increased from the pre- to post-*Citizens United* periods, so did corporate cash holdings. This evidence lends support to the Agency Cost Hypothesis.

We also investigate how political contributions changed in the post-*Citizens United* period and as a function of *historical* political connectedness. Specifically, we estimate the following model during the post-*Citizens United* period (2010-2011):

[10] For precise definitions of variables, see the Appendix.

$$\text{Contributions/NTA}_{i,t} = \beta_0 + \beta_1 \text{Political Dummy}_i + \beta_2 \mathbf{X_{i,}}_{t-1} + \varepsilon_{i,t} \quad (2)$$

where Political Dummy is a measure of historical political activism, [11] and $\mathbf{X_i}$ is vector of traditional determinants of cash holdings. We use lagged values of control variables to overcome a potentially endogenous relationship between contemporaneous values of cash holdings and firm characteristics. A positive (negative) β_1 coefficient would suggest that historically politically connected firms increased (decreased) their political contributions following the *Citizens United* decision. We note that our main interest is not in the amount in which historically politically connected firms contribute following *Citizens United*, but rather in their cash management policies surrounding this exogenous shock.

Table 4 provides the results of this equation estimated just for fiscal years 2010-2011. The positive and statistically significant coefficient on the Political Dummy (our measure of historical political activism) suggests that politically connected firms increased their political contributions following *Citizens United*.

Tests of hypothesis

The main focus of this paper is to determine whether the cash management practices of historically politically connected firms significantly differ from those of historically non-politically connected firms following passage of *Citizens United*. We use a difference-in-differences research design to test our prediction. In this test, the differences stem from (1) a measure of *historical* political activism, and (2) pre- versus post-*Citizens United* periods. We model cash holdings as a function of historical political activism in the pre- versus post-*Citizens United* periods:

[11] Political Dummy is based on median firm-level pre-*Citizens United* contributions (scaled by NTA), set equal to 1 for firms in the fourth quartile and equal to 0 for firms in the first quartile and for historically non-politically active firms.

$$\text{Log(Cash/NTA)}_{i,t} = \beta_0 + \beta_1 \text{Political Dummy}_i + \beta_2 \text{Post-}\textit{Citizens United}\text{ Dummy}_{i,t} + \beta_3 (\text{Political Dummy}_i * \text{Post-}\textit{Citizens United}\text{ Dummy}_{i,t}) + \beta_4 \mathbf{X_{i,}}_{t-1} + \varepsilon_{i,t} \quad (3)$$

where Post-*Citizens United* Dummy is set to 1 for fiscal years 2010 and 2011 (0 otherwise), and all other variables are as defined previously. Regarding equation 4, β_1 measures the relation between cash holdings and political connectedness, while β_3 measures the *differential* relation between cash holdings and political connectedness during the post-*Citizens United* period. The test of our hypothesis becomes $\beta_3 \neq 0$. That is, we expect those firms that were politically active prior to passage of *Citizens United* to exhibit a relation between cash holdings and political connectedness that significantly differs from those firms that were politically *in*active in the pre-*Citizens United* period. In particular, a result of $\beta_3 < 0$ would favor the Liquidity Hypothesis, suggesting that previously politically active firms chose to hold less cash relative to their less-connected counterparts following passage of *Citizens United* compared to before its passage. In contrast, a result of $\beta_3 > 0$ would favor the Agency Cost Hypothesis, suggesting that previously politically active firms chose to hold more cash relative to their less-connected counterparts following passage of *Citizens United* compared to before its passage.

In terms of our hypothesis, if the cash holdings of historically politically connected firms significantly differ from those of historically non-politically connected firms in the pre- versus post-*Citizens United* periods, we expect to find a significant difference on the interaction term (β_3). Specifically, in reference to equation 3, $\beta_3 < 0$ (> 0) would favor the Liquidity Hypothesis (Agency Cost Hypothesis), suggesting that previously politically active firms chose to hold less (more) cash relative to their less-connected counterparts following passage of *Citizens United* compared to before its passage.

Table 5 provides the main test of this hypothesis by examining the relation between firms' cash holdings and their traditional determinants in the pre-*Citizens United* period relative to the post-*Citizens United* period while also incorporating a measure of historical political connectedness. Consistent with prior literature (e.g., Opler et al. 1999; Harford et al. 2008), all traditional determinants of cash holdings enter with the expected signs. Specifically, current year cash holdings are positively associated with last year's cash holdings, the market-to-book ratio, cash flow, cash flow volatility, and R&D expense. Current year cash holdings are negatively related to size, leverage, net working capital, capital expenditures, and the propensity to pay dividends.

The evidence shown in Table 5 lends support to the main prediction of this paper in favor of the Agency Cost Hypothesis. Specifically, we find that the relation between cash holdings and our measure of historical political connectedness significantly increased during the post-*Citizens United* period relative to the pre-*Citizens United* period (p-value = 0.059). In contrast, cash holdings of historically non-politically connected firms fell following *Citizens United*, although this finding is not statistically significant. In terms of economic significance, switching from non-politically connected status to politically connected status results in an incremental increase in corporate cash holdings of 19.84% following passage of *Citizens* United.[12] Taken as a whole, these findings imply that politically connected firms suffer from agency problems (indicated by the retention of excess cash), but their less politically connected counterparts do not.

Corporate governance quality and political connections

The evidence presented so far in this paper supports the hypothesis that politically connected firms are characterized by agency problems. In this section, we examine whether

[12] The incremental and economic effect of politically connected status in the post-*Citizens United* period = $e^{0.181} - 1 = 0.1984$.

corporate governance quality incrementally affects this overall finding. Existing evidence suggests that poor corporate governance quality magnifies agency conflicts between managers and stakeholders and diminishes the value of cash holdings (Dittmar, Mahrt-Smith, and Servaes 2003; Dittmar and Mahrt-Smith 2007; Harford, Mansi, and Maxwell 2008). Our purpose is to investigate whether poorly-governed, historically politically connected firms exhibit greater agency problems relative to well-governed and/or historically non-politically connected firms.

We capture governance quality through three measures. The first measure is the external involvement of board members. Busy boards, defined here as the proportion of independent directors that serve on three or more boards, tend to become distracted and are less effective monitors because their attention is diverted away from the "home" corporation (Fich and Shivdasani 2006). The second measure of governance quality is defined in terms of excess CEO compensation. Excessive CEO compensation is more common in corporations with poor corporate governance structures (Core, Holthausen, and Larcker 1999). Since governance quality is decreasing in both of these measures, we predict that the agency conflicts plaguing politically connected firms will be amplified when the proportion of busy board members and level of excess CEO compensation are high.

Our third measure of corporate governance quality addresses the role of investor activism as a monitoring mechanism. In the context of corporate political contributions, we search the RiskMetrics Shareholder Proposals database for politically-oriented shareholder proposals. We are not necessarily interested in determining the fate of these proposals, but instead consider the mere knowledge that a proposal is being considered to act as a monitoring mechanism and, as such, impose restraints on a manager's selfish tendencies.

To test our predictions, we augment the cash holdings difference-in-differences model (equation 3) by incorporating measures of corporate governance:

$$\begin{aligned}\text{Log(Cash/NTA)}_{i,t} = {} & \beta_0 + \beta_1 \text{Political Dummy}_i + \beta_2 \text{Post-}\textit{Citizens United}\ \text{Dummy}_{i,t} \\ & + \beta_3 \text{Governance}_{i,t} + \beta_4 (\text{Political Dummy}_i * \text{Post-}\textit{Citizens United}\ \text{Dummy}_{i,t}) \\ & + \beta_5 (\text{Political Dummy}_i * \text{Governance}_{i,t}) \\ & + \beta_6 (\text{Post-}\textit{Citizens United}\ \text{Dummy}_{i,t} * \text{Governance}_{i,t}) \\ & + \beta_7 (\text{Political Dummy}_i * \text{Post-}\textit{Citizens United}\ \text{Dummy}_{i,t} * \text{Governance}_{i,t}) \\ & + \beta_8 \mathbf{X}_{\mathbf{i},\,t-1} + \varepsilon_{i,t} \end{aligned} \quad (4)$$

where Governance is one of the three measures of corporate governance quality mentioned previously.[13] Since we take governance quality to be worsening in the magnitude of both the busy-ness of directors and excessive compensation to CEOs, we posit that the agency problems (as captured by a build-up of cash) of historically politically connected firms in the post-*Citizens United* period are more severe when the proportion of busy board members and excessive compensation to the CEO are high; that is, for these two proxies of governance quality, our prediction becomes $\beta_7 > 0$. Additionally, we consider governance quality to be worse when a corporation is not required to entertain a politically-oriented shareholder proposal. Politically-oriented shareholder proposals should mitigate agency problems (and reduce cash hoarding behavior) more so for historically politically connected firms relative to historically non-politically connected firms, as it is a politically active firm that should benefit more from such a monitoring mechanism. Moreover, this differential impact should be most evident in the post- relative to pre-*Citizens United* period, as it was following the *Citizens United* decision that

[13] Specifically, Governance takes on the following definitions: "Busy Directors", defined as the proportion of independent directors who serve on three or more boards, measured in year *t*; "Compensation Dummy", an indicator variable set equal to 1 when a CEO's excess compensation in year *t* is positive and 0 otherwise, where excess compensation is the residual from a regression of the logarithm of CEO compensation on the logarithm of sales, two-digit SIC industry effects, and year fixed effects (Cheng, Hong, and Scheinkman 2010); or "Shareholder Inactivism Dummy", an indicator variable set to 1 when a firm has not entertained a shareholder proposal pertaining to political contributions, 0 otherwise.

essentially all limits on the extent of corporate political connectedness were lifted. Thus, for purposes of our shareholder proposal metric, our prediction is also $\beta_7 > 0$.

Table 6 provides results of our first two tests of the impact of governance quality on the agency implications of corporate political connections. Column I (II) provides estimates of equation 4 using the first two proxies of governance quality. The results are consistent with agency costs of politically connected firms. Specifically, we find that the busy-ness of boards is associated with larger cash holdings for historically politically connected firms in the post-*Citizens United* period (p-value = 0.075). Similarly, an excessively compensated CEO is associated with an incremental enhancement of agency problems in historically politically connected firms following the *Citizens United* decision (p-value = 0.016). Taken together, the results in Table 6 are consistent with the prediction that weak governance exacerbates agency problems in politically connected firms.

Our third measure of corporate governance quality is whether the firm entertained a politically-oriented shareholder proposal. We expect politically-oriented shareholder proposals to mitigate agency problems (and reduce cash hoarding behavior) more so for historically politically connected firms relative to historically non-politically connected firms. Moreover, we expect this relation to be most pronounced during the post-*Citizens United* period, i.e., after restrictions on corporate political activism had been lifted and the importance of shareholder monitoring had increased. In terms of equation 4, we predict that $\beta_7 > 0$.

Table 7 provides the results of estimating equation 4 using the busy board and excess compensation measures of governance quality. Consistent with expectations, we find that entertaining a politically-oriented shareholder proposal during either the 2007-2008 (pre-*Citizens United*) or 2010-2011 (post-*Citizens United*) periods results in an incremental decrease in the cash

holdings of historically politically connected firms relative to historically non-politically connected firms in the post-*Citizens United* period relative to the pre-*Citizens United* period (p-value = 0.019). This finding supports a positive association between political connections and agency costs.

We next investigate whether the impact of entertaining a shareholder proposal differs based on the period in which it is considered (either pre- or post-*Citizens United*). We expect that any existing agency conflicts of politically connected firms would only be amplified following passage of a rule that lifted all restrictions on corporate political activism. Therefore, a proposal entertained during the post-*Citizens United* period is likely to pose a more significant monitoring role on management than a proposal entertained during the pre-*Citizens United* period. To test our prediction, we redefine Shareholder Inactivism Dummy based on whether the shareholder proposal was considered during the pre-*Citizens United* period (column 2 of Table 7) or post-*Citizens United* period (column 3 of Table 7). We find that the incremental decrease in agency problems (and cash holdings) is much greater for politically-oriented shareholder proposals entertained during the post-*Citizens United* period (p-value = 0.046) relative to those considered during the pre-*Citizens United* period.

Executives' political connectedness and *Citizens United*

At a fundamental level, a corporation can derive political connectedness through the contributions of PACs and employees, both at the parent- and subsidiary-levels. While *Citizens United* effectively lifted all restrictions on corporate political activism, its provisions were more so targeted at the PAC- and corporate-level rather than the employee-level. Nonetheless, an implicit assumption behind our paper is that *Citizens United* brought a radical change to all channels of corporate political connectedness. Examples of such change might include a

corporation's decision to create a PAC, or an executive's decision to decrease her own contributions since bans on certain PAC-level contributions had now been lifted.

Thus, our goal now is to investigate whether the relation between corporate cash holdings and political contributions differs based on the type of contributor. Using *Citizens United* as an exogenous shock to this relation, we re-estimate equation 1 after decomposing political contributions into those made by executives,[14] non-executive employees, and PACs.[15] The evidence so far indicates that politically connected firms suffer from agency problems, as evidenced by the accumulation of excess cash. We largely attribute the agency problems to poor management and a lack of alignment between the goals of managers and of stakeholders. As such, we predict that the exogenous shock of *Citizens United* was accompanied by a statistically significant, positive relationship between cash holdings and the political contributions of executives.

Table 8 depicts the relationship between cash holdings and political connectedness based on the type of contributor (executives, non-executives, and PACs). We include earlier results from Table 3 in column 1, and subsequently decompose contributions into executive, non-executive, and PAC sub-samples in columns 2 through 4. The evidence indeed indicates that the change in corporate cash holdings as a function of the change in political contributions differed based on the identity of the contributor. With respect to the change in contributions made by executives, corporate cash holdings significantly increased following passage of *Citizens United* relative to before its passage (p-value = 0.053). The relation between the change in cash holdings

[14] To identify executive contributions, we search our data sets for the following employee titles: "CEO", "CFO", "CHIEF", "PRESIDENT", "VP", "DIRECTOR", "MANAGER", "MANAGING", "CHAIRMAN", "CHAIRPERSON", and "CHAIRWOMAN". We conduct this search using wildcards in SAS such that slight variations in these titles are also picked up in our data set.

[15] As a reminder to the reader, equation 1 took the following form: $\Delta\text{Log(Cash/NTA)}_i = \beta_0 + \beta_1\Delta\text{Contributions/NTA}_i + \beta_2\Delta X_i + \varepsilon_i$. This change specification was estimated as the difference between 2010 (post-*Citizens United*) and 2008 (pre-*Citizens United*) values.

and change in contributions is positive but insignificant for the non-executive employee sub-sample, and negative and insignificant for the PAC sub-sample. Managers are more inclined to hoard cash following passage of *Citizens United* relative to before its passage, possibly because of the ruling's relaxing of restrictions on other channels through which a corporation can become politically connected (such as PACs). In fact, the mean (median) level of employee contributions *decreased* from $68,816 ($31,578) in 2008 to $37,124 ($19,800) in 2010, while the mean (median) level of PAC contributions *increased* from $116,463 ($39,375) in 2008 to $129,270 ($40,025) in 2010. In aggregate terms, sample-wide employee contributions *decreased* from $16.5 million to $9.2 million, while sample-wide PAC contributions *increased* from $27.9 million in 2008 to $32.0 million in 2010, suggesting an element of substitutability between employee and PAC contributions. We take these results as further evidence in support of the Agency Cost Hypothesis.

Market reaction to *Citizens United*

January 21, 2010 marked a significant day of change in corporate political activism. Specifically, the Supreme Court's controversial decision in favor of *Citizens United* effectively lifted all limits on the political contributions of corporations. The evidence presented so far in this paper lends support to the notion that politically connected firms suffer from agency problems. Given the well-established value-decreasing effects of agency conflicts (e.g., Harford 1999, Lie 2000), it is reasonable to expect that the market reaction to *Citizens United* will differ based on the political connectedness of a firm. In particular, in the presence of agency problems, historically politically connected firms are likely to realize (1) negative abnormal returns surrounding the announcement of the Supreme Court ruling, and (2) significantly lower abnormal returns than those tied to their less-connected counterparts.

Evaluating the market reaction to *Citizens United* is complicated by the fact that all sample firms have the same event date (January 21, 2010). Event clustering in calendar time induces cross-correlation in estimates of abnormal returns which creates downward-biased standard errors and upward-biased test statistics. As such, rather than use standard event study methodology, we instead estimate each sample firm's reaction to the ruling through a seemingly unrelated regression (SUR). The SUR framework simultaneously estimates a set of firm-specific equations that include cross-correlated error terms:

$$R_i = \alpha_i + \beta_i R_m + \delta_i Event + \varepsilon_i \quad (5)$$

where R_i is the return series for individual firm *i*, R_m is the return series for the CRSP value-weighted index (including dividends), and *Event* is a dummy variable that equals 1 on days included in the event window (0 otherwise). For example, for the (0,+1) window, *Event* is set to one on January 21, 2010 and January 22, 2010, and is zero otherwise. Daily returns are measured between April 1, 2008, and March 31, 2010, and are retrieved from the CRSP daily returns file. The SUR methodology was developed by Schipper and Thompson (1983) and has since become increasingly utilized in corporate finance research (e.g., Doidge and Dyck 2012; Fernandes, Lel, and Miller 2010). This method enables us to measure the overall stock market reaction to *Citizens United*, while also accounting for cross-correlation in abnormal returns. Our main interest is in firm-specific estimates of $\hat{\delta}_i$ and, in particular, whether (1) the estimates jointly and significantly differ from zero, and (2) the estimates significantly differ across our firms having varying degrees of political connectedness.

Table 9 documents the market reaction to *Citizens United* for our sample of historically politically connected firms ("POLITICAL") and historically non-politically connected firms ("NEUTRAL"). Since $\hat{\delta}_i$ represents the average abnormal return for firm *i*, we multiply the

average value of $\hat{\delta}_i$ estimates in each event window by increments of 100% for each day in the event window to obtain the cumulative abnormal return (CAR).[16] Panel A provides univariate tests of CARs. Results indicate a negative market reaction to historically politically connected firms persisting for ten days beyond the announcement date, with a statistically significant negative reaction noted for all event windows considered [(0, 0), (0,+1), (0,+2), and (0,+5)]. On the announcement date, the average abnormal return to politically connected firms is –0.475% (p-value = 0.028), with an average cumulative loss of –1.219% five days after announcement date (p-value = 0.005). In contrast, historically *non*-politically connected firms exhibit a positive but insignificant market reaction over all event windows studied. For example, on announcement date, this "neutral" sub-sample realized an average abnormal return of 0.269% (p-value = 0.141), and an average cumulative abnormal return of 0.265% five days after announcement date (p-value = 0.325). Tests for differences in means are statistically significant for the (0, 0) and (0,+1) windows (p-values = 0.008 and 0.010, respectively). Overall, the results in Panel A of Table 9 suggest that politically connected firms face an unfavorable market reaction to *Citizens United*. This result further supports our finding of agency conflicts in politically connected corporations.

As a formal test of our prediction that the market reacted differently to *Citizens United* based on whether the firm was politically connected, we examine how the estimated CARs (average $\hat{\delta}_i$ from equation 5, expressed as percentage returns) differ with regard to a measure of historical political connectedness. To do so, we estimate the following regression model using ordinary least squares:

$$\hat{\delta}_i = \beta_0 + \beta_1 \text{Political Dummy}_i + \beta_2 \mathbf{X_i} + \varepsilon_i \quad (6)$$

[16] For example, CAR(0,+2) is computed as the average value of $\hat{\delta}_i$ estimates resulting from a SUR regression where *Event* = 1 on days 0, +1, and +2, multiplied by 300% for the three days in the event window.

where $\hat{\delta}_i$ originates from the SUR estimation in equation 5 and $\mathbf{X_i}$ is a vector of control variables measured in fiscal year 2009.

Panel B of Table 9 reports the coefficient estimates corresponding to equation 6. After controlling for size, market-to-book ratio, and leverage, we find that the coefficient on Political Dummy is negative in all four event windows studied and statistically significant in the (0,0), (0,+2), and (0,+5) windows (p-values = 0.006, 0.015, and 0.055, respectively). This evidence continues to be consistent with a positive association between agency problems and political connectedness.

Robustness checks

Cash holdings surrounding Citizens United. It is important to address the possibility that the cash management practices of our sample of S&P 500 firms significantly differ from those of an average firm in corporate America during the pre- and post-*Citizens United* periods. We estimate the following equation:

$$\text{Log(Cash/NTA)}_{i,t} = \beta_0 + \beta_1 \text{Post-}Citizens\ United\ \text{Dummy}_{i,t} + \beta_2 \mathbf{X_i}_{,t-1} + \varepsilon_{i,t} \quad (7)$$

where $\mathbf{X_i}$ is a vector of lagged values of traditional determinants of cash holdings. We first estimate equation 7 over all firms in the Compustat Fundamentals Annual file for the period 2005-2011, excluding the financial and utilities industries. Subsequently, we estimate equation 7 for S&P 500 firms. Industry fixed effects, based on two-digit SIC codes, are included when estimating this pooled model for the entire Compustat universe. The coefficient of interest is β_1, which captures corporate cash holdings as a function of the pre- and post-*Citizens United* periods. If there was a significant shift in the cash holdings of corporations in the post-*Citizens United* period, then we expect to find a significant coefficient on the Post-*Citizens United* Dummy.

Results are provided in Table 10. When estimated for the entire Compustat universe, the indicator variable enters with a positive and significant coefficient (p-value = 0.091), suggesting that corporations were inclined to accumulate more cash in the years following passage of *Citizens United* relative to the period before its passage. This statistically significant increase in cash holdings levels noted for the post- relative to pre-*Citizens United* periods also holds for our sample of S&P 500 firms (p-value = 0.065). In terms of economic significance, an average firm in the Compustat sample increased its cash-to-net-assets ratio by 2.53% in the post- relative to pre-*Citizens United* periods, while an average firm in our S&P 500 sample increased its cash ratio by 6.71% over the same period.[17] We take comfort in this result, as it suggests that our sample exhibits a similar shift in cash holdings as to that observed for the entire universe of Compustat firms. Moreover, while we acknowledge the fact that significant macroeconomic events during our sample period may have affected corporate policies, the impact felt by our sample firms is comparable to that experienced by an average firm drawn from the Compustat universe. Thus, findings based on Compustat firms also support the Agency Cost Hypothesis.

VI. CONCLUSION

Political connections may incentivize a manager to adopt corporate policies that differ from those that he otherwise would take on. However, very little attention has been given to this possibility in extant literature. Through a study of corporate cash holdings, we explore whether politically connected firms are better characterized by liquidity or agency costs. In an effort to provide clear insights that are not influenced by confounding factors, we pose the question in the

[17] When our dependent variable (but not independent variable) is measured in log form, results on economic significance are calculated as $e^{\text{coefficient}} - 1$. For the Compustat sample, $2.53\% = e^{0.025} - 1$For the S&P 500 sample, $6.71\% = e^{0.065} - 1$.

context of *Citizens United*, a landmark Supreme Court case decided in January 2010 that lifted essentially all limits on corporate political contributions.

The findings in this paper reveal a connection between political activism and corporate policies. Specifically, we find that politically connected firms increased their cash holdings following passage of *Citizens United relative* to before its passage. This significant difference supports the view that politically connected firms suffer from agency problems.

We also find that poor corporate governance quality, captured by busy board members and excessive remuneration to the CEO, aggravates the existing agency conflicts within politically connected firms, as evidenced by an incrementally and significantly greater level of cash holdings. However, we also show that investor activism, evidenced by a firm obligated to entertain a politically-oriented shareholder proposal, offers an incremental and significant *decrease* in the agency conflicts of politically connected firms.

When considering contributor type (executive, non-executive, and PAC), we find that the differential impact of political connectedness on cash holdings to be particularly strong for executive contributions. This evidence suggests that management's cash hoarding tendencies are only magnified following the *Citizens United* decision. Finally, we document a value-decreasing effect of political connections, as evidenced by a significantly negative market reaction to the *Citizens United* decision. Collectively, these findings are consistent with the existence of agency problems in politically connected firms.

Unfortunately, it seems that *Citizens United* has only further aggravated the agency problems of politically connected firms, as instances of managing directors attempting to influence the political leanings and voting decisions of non-managing employees have come to light. With a focus on agency problems between managers and various stakeholder groups, future

research could attempt to isolate and analyze the impact of the degree of political connectedness of firms' managing directors.

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Appendix
Variable Definitions
(with Compustat Fundamentals Annual variable names shown in parentheses, where applicable):

Panel A: Traditional Determinants of Corporate Cash Holdings

Log(Cash/NTA)	The logarithm of Cash & Cash Equivalents (CHE) / [Total Assets (AT) – Cash & Cash Equivalents (CHE)], measured in year *t*
Log(Net Total Assets)	The logarithm of [Total Assets (AT) – Cash & Cash Equivalents (CHE)], measured in year *t*
Debt/NTA	[Long-term Debt (DLTT) + Debt in Current Liabilities (DLC)] / [Total Assets (AT) – Cash & Cash Equivalents (CHE)], measured in year *t*
Market-to-Book	[Market Value of Equity (CSHO * PRCC_F) + Total Liabilities (LT)] / [Total Assets (AT) – Cash & Cash Equivalents (CHE)], measured in year *t*
Cash Flow/NTA	[Operating Income before Depreciation (OIBDP) – Interest Expense (DP) – Taxes (TXT) – Common Dividends (DVC)] / [Total Assets (AT) – Cash & Cash Equivalents (CHE)], measured in year *t*
Std(Cash Flow/NTA)	The trailing volatility of cash flow (OIBDP), computed over a minimum (maximum) of 5 (10) years ending in year *t–1*
Net Working Capital/NTA	[Working Capital (WCAP) – Cash & Cash Equivalents (CHE)] / [Total Assets (AT) – Cash & Cash Equivalents (CHE)], measured in year *t*
R&D/Sales	Research and Development Expenditures (XRD) / Sales (SALE), measured in year *t* (and set to 0 if missing)
R&D Missing Dummy	An indicator variable equal to 1 if the firm does not report Research & Development Expenditures (XRD) in year *t*, 0 otherwise
Capital Expenditures/NTA	Capital Expenditures (CAPX) / [Total Assets (AT) – Cash & Cash Equivalents (CHE)], measured in year *t*
Dividend Dummy	An indicator variable equal to 1 if the firm paid common dividends (DVC) in year *t*, 0 otherwise

Panel B: Political Connectedness	
Contributions/NTA	Annual Political Contributions / [Total Assets (AT) – Cash & Cash Equivalents (CHE)] computed at the parent-level and measured in year *t*, where political contributions include donations made by PACs and employees associated with parent and wholly-owned subsidiary companies, unless indicated otherwise
Post-*Citizens United* Dummy	An indicator variable equal to 1 for fiscal years 2010 and 2011, 0 otherwise
Political Dummy	An indicator variable to capture the degree of historical political connectedness as determined by median firm-level pre-*Citizens United* contributions (scaled by Net Total Assets), set equal to 1 for firms in the fourth quartile and equal to 0 for firms in the first quartile and for historically non-politically active firms
Panel C: Corporate Governance	
Busy Directors	The proportion of independent directors who serve on three or more boards in year *t*
Compensation Dummy	An indicator variable equal to 1 when a CEO's excess compensation in year *t* (defined as the residual from a regression of the logarithm of total CEO compensation on Log(Sales), two-digit SIC industry effects, and year fixed effects,[18] where total compensation is set equal to TDC1 in the Execucomp database) is positive; 0 otherwise
Shareholder Inactivism Dummy	An indicator variable equal to 1 when a firm does *not* entertain a shareholder proposal pertaining to political contributions in year *t*, 0 otherwise

[18] See Cheng, Hong, and Scheinkman (2010).

Table 1. Descriptive statistics (N = 1,378).

Panel A: All firm-year observations

Variable	Mean	Std Dev	Lower Quartile	Median	Upper Quartile
Total Assets ($ millions)	25,178	34,080	6,108	13,879	30,600
Cash & Cash Equivalents ($ millions)	2,548	4,694	381	957	2,331
Political Contributions (unscaled)	142,448	215,406	11,950	57,225	182,214
Log(Cash/NTA)	–2.557	1.329	–3.429	–2.545	–1.597
Log(Net Total Assets)	9.404	1.134	8.586	9.399	10.238
Debt/NTA	0.267	0.155	0.169	0.257	0.357
Market–to–Book	2.324	1.540	1.374	1.851	2.746
Cash Flow/NTA	0.114	0.070	0.066	0.101	0.144
Std(Cash Flow/NTA)	0.036	0.038	0.015	0.023	0.040
Net Working Capital/NTA	0.002	0.137	–0.060	–0.003	0.073
R&D/Sales	0.037	0.064	0.000	0.003	0.037
R&D Missing Dummy	0.370	0.483	0.000	0.000	1.000
Capital Expenditures/NTA	0.056	0.041	0.027	0.046	0.072
Dividend Dummy	0.839	0.368	1.000	1.000	1.000

Panel B: Aggregate statistics for politically connected sub-sample (2005-2011)[a]

	Total	Executives	Non-Executives	PACs
No. of contributions	373,391	45,313	130,587	197,491
Percent of total sample	100%	12.14%	34.97%	52.89%
Aggregate dollar amount	$441,088,864	$41,410,621	$102,535,472	$297,142,771
Percent of total sample	100%	9.39%	23.25%	67.36%

[a] For comparability with subsequent statistical tests, fiscal year 2009 observations have been omitted.

Table 2. Univariate Analysis.

		Not Politically Active in pre-*Citizens United* period		Political Contribution Quartiles									
				1		2		3		4			
		N	Mean	N	Mean	N	Mean	N	Mean	N	Mean	(1) – (4)	t-statistic
Log(Cash/NTA)	Pre-*Citizens United*	21	–2.384	217	–2.818	224	–2.718	220	–2.761	210	–2.295	–0.523***	–4.127
	Post-*Citizens United*	32	–1.984	111	–2.619	115	–2.414	112	–2.650	116	–2.025	–0.594***	–3.462
	Pre – Post		–0.400		–0.199		–0.304**		–0.111		–0.269*		
	t-statistic		–1.162		–1.389		–2.068		–0.710		–1.691		
Log(Net Total Assets)	Pre-*Citizens United*	21	8.474	217	9.146	224	9.338	220	9.732	210	9.260	–0.114	–1.063
	Post-*Citizens United*	32	8.613	111	9.392	115	9.414	112	9.949	116	9.512	–0.120	–0.812
	Pre – Post		–0.139		–0.246*		–0.075		–0.217**		–0.252*		
	t-statistic		–0.579		–1.892		–0.519		–2.061		–1.961		
Log(Sales)	Pre-*Citizens United*	21	8.497	217	9.140	224	9.271	220	9.568	210	9.295	–0.154	–1.473
	Post-*Citizens United*	32	8.916	111	9.296	115	9.308	112	9.671	116	9.469	–0.173	–1.183
	Pre – Post		–0.419		–0.155		–0.037		–0.102		–0.174		
	t-statistic		–1.361		–1.264		–0.249		–1.129		–1.335		
Debt/NTA	Pre-*Citizens United*	21	0.308	217	0.242	224	0.272	220	0.273	209	0.230	0.012	0.858
	Post-*Citizens United*	32	0.330	111	0.250	115	0.312	112	0.306	116	0.268	–0.017	–0.923
	Pre – Post		–0.022		–0.008		–0.041**		–0.033*		–0.038**		
	t-statistic		–0.508		–0.481		–2.104		–1.941		–2.187		
Market-to-Book	Pre-*Citizens United*	21	2.213	217	2.128	224	2.220	220	2.374	210	2.815	–0.687***	–4.680
	Post-*Citizens United*	32	3.177	111	1.963	115	2.146	112	2.114	116	2.418	–0.454***	–2.889
	Pre – Post		–0.964*		0.165		0.075		0.259		0.398**		
	t-statistic		–1.693		1.303		0.496		1.239		2.051		
Cash Flow/NTA	Pre-*Citizens United*	21	0.107	216	0.109	223	0.111	220	0.103	207	0.130	–0.021***	–3.200
	Post-*Citizens United*	32	0.141	111	0.109	113	0.115	112	0.106	114	0.119	–0.010	–1.056
	Pre – Post		–0.034		0.000		–0.004		–0.003		0.011		
	t-statistic		–1.604		0.018		–0.624		–0.345		1.265		
Std(Cash Flow/NTA)	Pre-*Citizens United*	21	0.030	217	0.032	224	0.034	220	0.034	210	0.043	–0.011***	–2.761
	Post-*Citizens United*	32	0.046	111	0.027	115	0.036	112	0.035	116	0.041	–0.014***	–3.521
	Pre – Post		–0.016		0.005		–0.002		–0.001		0.002		
	t-statistic		–1.427		1.439		–0.586		–0.113		0.481		
Net Working Capital/NTA	Pre-*Citizens United*	21	0.006	217	0.039	224	–0.002	220	–0.001	210	–0.032	0.071***	5.368
	Post-*Citizens United*	32	–0.057	111	0.040	115	0.006	112	–0.001	116	–0.010	0.050***	3.042
	Pre – Post		0.063		–0.001		–0.009		0.000		–0.022		
	t-statistic		1.025		–0.054		–0.513		–0.023		–1.291		
R&D/Sales	Pre-*Citizens United*	21	0.032	217	0.026	224	0.036	220	0.034	210	0.056	–0.030***	–4.563
	Post-*Citizens United*	32	0.059	111	0.024	115	0.029	112	0.034	116	0.051	–0.027***	–3.187
	Pre – Post		–0.027		0.001		0.006		0.000		0.005		
	t-statistic		–1.434		0.216		0.892		0.039		0.553		

R&D Missing Dummy	Pre-*Citizens United*	21	0.381	217	0.327	224	0.362	220	0.432	210	0.352	–0.025	–0.548
	Post-*Citizens United*	32	0.438	111	0.306	115	0.365	112	0.438	116	0.362	–0.056	–0.888
	Pre – Post		–0.057		0.021		–0.004		–0.006		–0.010		
	t-statistic		–0.401		0.383		–0.065		–0.098		–0.174		
Capital Expenditures/NTA	Pre-*Citizens United*	21	0.034	217	0.066	224	0.060	220	0.057	210	0.054	0.012***	2.764
	Post-*Citizens United*	32	0.028	111	0.059	115	0.053	112	0.054	116	0.040	0.018***	3.507
	Pre – Post		0.006*		0.007		0.007		0.003		0.014***		
	t-statistic		1.931		1.224		1.316		0.956		3.881		
Dividend Dummy	Pre-*Citizens United*	21	0.952	217	0.848	224	0.813	220	0.841	210	0.843	0.005	0.145
	Post-*Citizens United*	32	0.625	111	0.856	115	0.817	112	0.857	116	0.888	–0.032	–0.721
	Pre – Post		0.327***		–0.008		–0.005		–0.016		–0.045		
	t-statistic		2.863		–0.190		–0.109		–0.387		–1.118		
Proportion of Busy Directors	Pre-*Citizens United*	7	0.117	74	0.173	86	0.167	79	0.162	88	0.201	–0.028	–1.224
	Post-*Citizens United*	23	0.119	88	0.114	97	0.137	95	0.142	100	0.134	–0.020	–1.259
	Pre – Post		–0.001		0.059***		0.031		0.019		0.067***		
	t-statistic		–0.023		3.005		1.526		0.846		3.591		
Excess CEO Compensation	Pre-*Citizens United*	87	–0.131	199	–0.185	204	0.107	197	–0.026	202	0.156	–0.340***	–3.062
	Post-*Citizens United*	64	0.030	104	–0.168	109	–0.096	106	0.126	102	0.125	–0.293**	–2.480
	Pre – Post		–0.161		–0.017		0.203*		–0.152		0.030		
	t-statistic		–0.957		–0.144		1.965		–1.233		0.226		
Shareholder Inactivism Dummy	Pre-*Citizens United*	1	1.000	51	0.667	63	0.746	74	0.378	63	0.540	0.127	1.373
	Post-*Citizens United*	13	0.769	45	0.600	56	0.750	71	0.451	65	0.554	0.046	0.477
	Pre – Post		0.231		0.067		–0.004		–0.072		–0.014		
	t-statistic		0.507		0.672		–0.049		–0.880		–0.160		

Table 3. The change in cash holdings modeled as a function of the change in political contributions as computed in year 2010 (post-*Citizens United*) relative to year 2008 (pre-*Citizens United*).

Variable	Coef. (p-value)
ΔContributions/NTA	0.017** (0.043)
ΔLog(Net Total Assets)	–0.820*** (0.000)
ΔDebt/NTA	1.745*** (0.004)
ΔMarket-to-Book	0.172** (0.020)
ΔCash Flow/NTA	1.401 (0.102)
ΔStd(Cash Flow/NTA)	1.914 (0.454)
ΔNet Working Capital/NTA	–0.339 (0.583)
ΔR&D/Sales	1.759 (0.593)
ΔR&D Missing Dummy	–0.502 (0.162)
ΔCapital Expenditures/NTA	–4.885** (0.015)
ΔDividend Dummy	0.191 (0.640)
Adj. R^2	0.186
N	236

The results represent pooled regressions of 236 firm-level differences computed as observed values in 2010 (post-*Citizens United*) less observed values in 2008 (pre-*Citizens United*). The dependent variable is ΔLog(Cash/NTA). To provide a cleaner test, fiscal year 2009 observations (i.e., those immediately preceding passage of *Citizens United*) are excluded. Net Total Assets (NTA) is computed as Total Assets less Cash & Cash Equivalents. See the Appendix for other variable definitions. All continuous variables are winsorized at the 1st and 99th percentiles. p-values are shown in parentheses. *, **, *** indicates significance at the 0.10, 0.05, 0.01 level for a two-tailed t-test.

Table 4. The differential relation in political contributions for historically politically connected firms relative to historically non-politically connected firms in the post-*Citizens United* period

Variable	Coef. (p-value)
Political Dummy	1.556* (0.075)
Contributions/NTA	0.808*** (0.000)
Log(Net Total Assets)	–0.234 (0.536)
Debt/NTA	–2.148 (0.392)
Market-to-Book	0.035 (0.930)
Cash Flow/NTA	–2.603 (0.719)
Std(Cash Flow/NTA)	3.465 (0.789)
Net Working Capital/NTA	–0.870 (0.770)
R&D/Sales	–3.649 (0.622)
R&D Missing Dummy	0.399 (0.659)
Capital Expenditures/NTA	–12.201 (0.299)
Dividend Dummy	–0.756 (0.487)
Adj. R^2	0.776
N	259

The results represent pooled regressions of Political Contributions/NTA on traditional determinants of cash holdings and a measure of historical political connectedness (Political Dummy), and are estimated for the period 2010-2011 for which sufficient data are available. All traditional determinants of cash holdings are lagged in an effort to alleviate endogeneity. To provide a cleaner test, fiscal year 2009 observations (i.e., those immediately preceding passage of *Citizens United*) are excluded. Net Total Assets (NTA) is computed as Total Assets less Cash & Cash Equivalents. Political Dummy is a measure of historical political connectedness and is based on median firm-level pre-*Citizens United* contributions (scaled by NTA), set equal to 1 for firms in the fourth quartile and equal to 0 for firms in the first quartile and for historically non-politically active firms. See the Appendix for other variable definitions. All continuous variables are winsorized at the 1st and 99th percentiles. p-values are shown in parentheses. *, **, *** indicates significance at the 0.10, 0.05, 0.01 level for a two-tailed t-test.

Table 5. The differential relation in cash holdings for historically politically connected firms relative to historically non-politically connected firms in the post-*Citizens United* relative to pre-*Citizens United* periods.

Variable	Coef. (p-value)
Political Dummy	–0.017
	(0.780)
Post-*Citizens United* Dummy	–0.038
	(0.559)
Political Dummy * Post-*Citizens United* Dummy	0.181*
	(0.059)
Log(Cash/NTA)	0.771***
	(0.000)
Log(Net Total Assets)	–0.013
	(0.602)
Debt/NTA	–0.308*
	(0.072)
Market-to-Book	0.022
	(0.354)
Cash Flow/NTA	0.713
	(0.154)
Std(Cash Flow/NTA)	1.390*
	(0.054)
Net Working Capital/NTA	–0.089
	(0.637)
R&D/Sales	0.704
	(0.149)
R&D Missing Dummy	–0.089
	(0.117)
Capital Expenditures/NTA	–2.134***
	(0.001)
Dividend Dummy	–0.151**
	(0.038)
Adj. R^2	0.792
N	707

The results represent a regression of Log(Cash/NTA) on traditional determinants of cash holdings and a measure of historical political connectedness (Political Dummy), and are estimated for the period 2005-2011 for which sufficient data are available. All traditional determinants of cash holdings are lagged in an effort to alleviate endogeneity. To provide a cleaner test, fiscal year 2009 observations (i.e., those immediately preceding passage of *Citizens United*) are excluded. Net Total Assets (NTA) is computed as Total Assets less Cash & Cash Equivalents. Political Dummy is a measure of historical political connectedness and is based on median firm-level pre-*Citizens United* contributions (scaled by NTA), set equal to 1 for firms in the fourth quartile and equal to 0 for firms in the first quartile and for historically non-politically active firms. See the Appendix for other variable definitions. All continuous variables are winsorized at the 1st and 99th percentiles. p-values are shown in parentheses. *, **, *** indicates significance at the 0.10, 0.05, 0.01 level for a two-tailed t-test.

Table 6. The differential relation in corporate cash holdings with respect to political connectedness and governance quality in the post-*Citizens United* relative to pre-*Citizens United* periods.

Variable	**I. Busy Boards** Coef. (p-value)	**II. High Compensation** Coef. (p-value)
Political Dummy	0.156	0.061
	(0.266)	(0.472)
Post-*Citizens United* Dummy	0.199	0.155*
	(0.104)	(0.089)
Political Dummy * Post-*Citizens United* Dummy	–0.168	–0.049
	(0.351)	(0.713)
Busy Directors	0.738*	
	(0.095)	
Political Dummy * Busy Directors	–0.863	
	(0.152)	
Post-*Citizens United* Dummy * Busy Directors	–0.727	
	(0.260)	
Political Dummy * Post-*Citizens United* Dummy * Busy Directors	1.646*	
	(0.075)	
Compensation Dummy		0.106
		(0.182)
Political Dummy * Compensation Dummy		–0.152
		(0.192)
Post-*Citizens United* Dummy * Compensation Dummy		–0.390***
		(0.003)
Political Dummy * Post-*Citizens United* Dummy * Compensation Dummy		0.462**
		(0.016)
Log(Cash/NTA)	0.799***	0.773***
	(0.000)	(0.000)
Log(Net Total Assets)	–0.018	–0.013
	(0.553)	(0.602)
Debt/NTA	–0.390*	–0.305*
	(0.060)	(0.077)
Market-to-Book	0.022	0.021
	(0.571)	(0.363)
Cash Flow/NTA	0.988	0.798
	(0.135)	(0.112)
Std(Cash Flow/NTA)	1.547	1.256*
	(0.133)	(0.087)
Net Working Capital/NTA	–0.068	–0.054
	(0.794)	(0.774)
R&D/Sales	0.219	0.753
	(0.709)	(0.123)
R&D Missing Dummy	–0.106	–0.079
	(0.126)	(0.160)
Capital Expenditures/NTA	–2.391***	–2.249***
	(0.005)	(0.001)
Dividend Dummy	–0.107	–0.154**
	(0.266)	(0.034)
Adj. R^2	0.827	0.794
N	380	705

The results represent a regression of Log(Cash/NTA) on traditional determinants of cash holdings, a measure of historical political connectedness (Political Dummy), a measure of corporate governance (either Busy Directors or Compensation

Dummy), and are estimated for the period 2005-2011 for which sufficient data are available.[19] All traditional determinants of cash holdings are lagged in an effort to alleviate endogeneity. To provide a cleaner test, fiscal year 2009 observations (i.e., those immediately preceding passage of *Citizens United*) are excluded. Net Total Assets (NTA) is computed as Total Assets less Cash & Cash Equivalents. Political Dummy is a measure of historical political connectedness and is based on median firm-level pre-*Citizens United* contributions (scaled by NTA), set equal to 1 for firms in the fourth quartile and equal to 0 for firms in the first quartile and for historically non-politically active firms. See the Appendix for other variable definitions. All continuous variables are winsorized at the 1st and 99th percentiles. p-values are shown in parentheses. *, **, *** indicates significance at the 0.10, 0.05, 0.01 level for a two-tailed t-test.

[19] Data used to estimate the Busy Board Dummy are derived from RiskMetrics and available for the period 2007-2011. Data used to estimate the Compensation Dummy are derived from Execucomp and available for the period 2005-2011.

Table 7. The differential relation in corporate cash holdings with respect to political connectedness and politically-oriented shareholder proposals in the post-*Citizens United* relative to pre-*Citizens United* periods.

Variable	**Proposal Entertained during 2007-2008 or 2010-2011** Coef. (p-value)	**Proposal Entertained during 2007-2008** Coef. (p-value)	**Proposal Entertained during 2010-2011** Coef. (p-value)
Political Dummy	0.111	–0.129	0.043
	(0.506)	(0.614)	(0.773)
Post-*Citizens United* Dummy	0.241	–0.044	0.258
	(0.157)	(0.851)	(0.126)
Shareholder Inactivism Dummy	–0.065	–0.140	–0.070
	(0.702)	(0.534)	(0.636)
Political Dummy * Post-*Citizens United* Dummy	–0.299	0.112	–0.263
	(0.172)	(0.709)	(0.227)
Political Dummy * Shareholder Inactivism Dummy	–0.236	0.129	–0.135
	(0.260)	(0.646)	(0.508)
Post-*Citizens United* Dummy * Shareholder Inactivism Dummy	–0.253	0.134	–0.249
	(0.230)	(0.613)	(0.243)
Political Dummy * Post-*C.U.* Dummy * Shareholder Inactivism Dummy	0.658**	–0.011	0.566**
	(0.019)	(0.975)	(0.046)
Log(Cash/NTA)	0.800***	0.798***	0.804***
	(0.000)	(0.000)	(0.000)
Log(Net Total Assets)	–0.082*	–0.039	–0.059
	(0.087)	(0.357)	(0.164)
Debt/NTA	–0.608*	–0.589*	–0.582*
	(0.061)	(0.075)	(0.074)
Market-to-Book	0.031	0.041	0.035
	(0.556)	(0.442)	(0.497)
Cash Flow/NTA	0.088	0.235	0.062
	(0.927)	(0.806)	(0.949)
Std(Cash Flow/NTA)	1.774	1.202	1.456
	(0.176)	(0.369)	(0.261)
Net Working Capital/NTA	–0.252	–0.216	–0.294
	(0.440)	(0.509)	(0.370)
R&D/Sales	0.577	0.810	0.749
	(0.460)	(0.326)	(0.340)
R&D Missing Dummy	–0.079	–0.038	–0.086
	(0.361)	(0.662)	(0.330)
Capital Expenditures/NTA	–3.316***	–3.303***	–3.188***
	(0.002)	(0.002)	(0.004)
Dividend Dummy	–0.105	–0.094	–0.091
	(0.359)	(0.421)	(0.426)
Adj. R^2	0.854	0.849	0.853
N	238	238	238

The results represent a regression of Log(Cash/NTA) on traditional determinants of cash holdings, a measure of historical political connectedness (Political Dummy), a measure of corporate governance (Shareholder Inactivism Dummy), and are estimated for the period 2007-2011 for which sufficient data are available. All traditional determinants of cash holdings are lagged in an effort to alleviate endogeneity. To provide a cleaner test, fiscal year 2009 observations (i.e., those immediately preceding passage of *Citizens United*) are excluded. Net Total Assets (NTA) is computed as Total Assets less Cash & Cash Equivalents. Political Dummy is a measure of historical political connectedness and is based on median firm-level pre-*Citizens United* contributions (scaled by NTA), set equal to 1 for firms in the fourth quartile and equal to 0 for firms in the first quartile and for historically non-politically active firms. See the Appendix for other variable definitions. All continuous variables are winsorized at the 1st and 99th percentiles. p-values are shown in parentheses. *, **, *** indicates significance at the 0.10, 0.05, 0.01 level for a two-tailed t-test.

Table 8. The change in cash holdings modeled as a function of the change in political contributions as computed in year 2010 (post-*Citizens United*) relative to year 2008 (pre-*Citizens United*).

Variable	**Full Sample**	**Executives**	**Non-Executives**	**PACs**
ΔContributions/NTA	0.017**	0.072*	0.013	–0.002
	(0.043)	(0.053)	(0.211)	(0.894)
ΔLog(Net Total Assets)	–0.820***	–0.845***	–0.903***	–0.370*
	(0.000)	(0.000)	(0.000)	(0.071)
ΔDebt/NTA	1.745***	1.846***	1.571**	–0.677
	(0.004)	(0.003)	(0.010)	(0.316)
ΔMarket-to-Book	0.172**	0.157**	0.167**	0.044
	(0.020)	(0.034)	(0.026)	(0.635)
ΔCash Flow/NTA	1.401	1.581*	1.672*	0.348
	(0.102)	(0.063)	(0.051)	(0.692)
ΔStd(Cash Flow/NTA)	1.914	1.698	1.638	1.424
	(0.454)	(0.507)	(0.524)	(0.726)
ΔNet Working Capital/NTA	–0.339	–0.373	–0.524	–2.047***
	(0.583)	(0.547)	(0.400)	(0.009)
ΔR&D/Sales	1.759	1.960	2.428	–1.219
	(0.593)	(0.550)	(0.460)	(0.645)
ΔR&D Missing Dummy	–0.502	–0.521	–0.510	–0.292
	(0.162)	(0.147)	(0.158)	(0.343)
ΔCapital Expenditures/NTA	–4.885**	–4.697**	–4.700**	–9.441***
	(0.015)	(0.019)	(0.020)	(0.000)
ΔDividend Dummy	0.191	0.190	0.156	–0.028
	(0.640)	(0.642)	(0.704)	(0.920)
Adj. R^2	0.186	0.184	0.177	0.092
N	236	236	236	272

The results represent pooled regressions of 236 firm-level differences computed as observed values in 2010 (post-*Citizens United*) less observed values in 2008 (pre-*Citizens United*). The dependent variable is ΔLog(Cash/NTA). Results are presented according to the identity of the contributor (executive, non-executive, or PAC). To provide a cleaner test, fiscal year 2009 observations (i.e., those immediately preceding passage of *Citizens United*) are excluded. Net Total Assets (NTA) is computed as Total Assets less Cash & Cash Equivalents. See the Appendix for other variable definitions. All continuous variables are winsorized at the 1st and 99th percentiles. p-values are shown in parentheses. *, **, *** indicates significance at the 0.10, 0.05, 0.01 level for a two-tailed t-test.

Table 9. The market reaction to *Citizens United*.

Panel A: Univariate results for sub-samples of political connectedness.

	POLITICAL (N = 60)		NEUTRAL (N = 70)		Difference (p-value)	
	Mean $\hat{\delta}$ (%)	p-value	Mean $\hat{\delta}$ (%)	p-value	POLITICAL – NEUTRAL	
CAR(0,0)	–0.475**	0.028	0.269	0.141	–0.744***	(0.008)
CAR(0,+1)	–0.482*	0.082	0.098	0.684	–0.182	(0.113)
CAR(0,+2)	–0.633***	0.005	0.265	0.325	–0.182	(0.232)
CAR(0,+5)	–1.219**	0.028	0.054	0.882	–0.898**	(0.010)

Panel B: Cross-sectional determinants of firm-level responses to Citizens United.

Variable	CAR(0,0)	CAR(0,+1)	CAR(0,+2)	CAR(0,+5)
Political Dummy	–0.779***	–0.003	–0.893**	–1.272*
	(0.006)	(0.159)	(0.015)	(0.055)
Log(Net Total Assets)	–0.033	–0.001	–0.028	0.004
	(0.802)	(0.384)	(0.871)	(0.989)
Market-to-Book	0.279**	0.000	0.069	0.120
	(0.018)	(0.878)	(0.650)	(0.662)
Debt/NTA	0.173	0.003	0.418	1.112
	(0.845)	(0.641)	(0.719)	(0.596)
R^2	0.109	0.030	0.052	0.034
N	130	130	130	130

Panel A presents summary statistics and univariate tests of average $\hat{\delta}$ estimates, where the parameter $\hat{\delta}$ is derived from the seemingly unrelated regression (SUR), $R_i = \alpha_i + \beta_i R_m + \delta_i Event + \varepsilon_i$ where R_i is the return series for individual firm i, R_m is the return series for CRSP value-weighted index (including dividends), and *Event* is a dummy variable that equals 1 on days included in the event window (0 otherwise). Daily returns are measured between April 1, 2008, and March 31, 2010, and are retrieved from the CRSP daily returns file. The event parameter estimate $\hat{\delta}$ corresponds to the average abnormal return for firm i in a given event window, and is multiplied by increments of 100% for each day in the event window to obtain the cumulative abnormal return (CAR). "POLITICAL" refers to our sample of historically politically connected firms, defined as firms in the fourth quartile of median firm-level pre-*Citizens United* contributions (scaled by NTA). "NEUTRAL" refers to our sample of historically non-politically connected firms, defined as firms in the first quartile of median firm-level pre-*Citizens United* contributions (scaled by NTA), as well as firms that did not contribute to political campaigns prior to *Citizens United*. // Panel B provides estimates from a multivariate ordinary least squares regression where average $\hat{\delta}$ estimates are regressed on a measure of historical political connectedness (Political Dummy) and control variables. Control variables are measured as of fiscal year-end 2009 and are winsorized at the 1st and 99th percentiles. Net Total Assets (NTA) is computed as Total Assets less Cash & Cash Equivalents. Standard errors are corrected for contemporaneous cross-correlation in the residuals through use of the SUR methodology. p-values are shown in parentheses. *, **, *** indicates significance at the 0.10, 0.05, 0.01 level for a two-tailed t-test.

Table 10. Determinants of cash holdings as a function of the pre-*Citizens United* and post-*Citizens United* periods.

Variable	**All Compustat Firms**	**S&P 500 Firms**
Post-*Citizens United* Dummy	0.025*	0.065*
	(0.091)	(0.065)
Log(Cash/NTA)	0.779***	0.780***
	(0.000)	(0.000)
Log(Net Total Assets)	–0.028***	–0.007
	(0.000)	(0.703)
Debt/NTA	–0.041***	–0.284**
	(0.000)	(0.014)
Market-to-Book	–0.000	0.026
	(0.187)	(0.109)
Cash Flow/NTA	0.010**	0.149
	(0.021)	(0.687)
Std(Cash Flow/NTA)	–0.002	1.646***
	(0.180)	(0.002)
Net Working Capital/NTA	–0.024***	–0.018
	(0.000)	(0.893)
R&D/Sales	0.021***	1.072***
	(0.000)	(0.002)
R&D Missing Dummy	–0.127***	–0.039
	(0.000)	(0.314)
Capital Expenditures/NTA	–0.803***	–1.494***
	(0.000)	(0.001)
Dividend Dummy	–0.066***	–0.074
	(0.000)	(0.136)
Adj. R^2	0.691	0.799
N	22,542	1,378

The results represent pooled regressions of 22,542 firm-year observations in the Compustat universe (first column) and 1,378 firm-year observations in the S&P 500 (second column), during the period 2005-2011 for which sufficient data are available. The dependent variable is Log(Cash/NTA). All continuous variables are lagged in an effort to alleviate endogeneity. To provide a cleaner test, fiscal year 2009 observations (i.e., those immediately preceding passage of *Citizens United*) are excluded. Financial firms (SIC 6000-6999) as well as utilities (SIC 4900-4949) are excluded from the Compustat sample. The regression for the entire Compustat universe includes industry fixed effects based on two-digit SIC code classifications. See the Appendix for variable definitions. All continuous variables are winsorized at the 1st and 99th percentiles. p-values are shown in parentheses. *, **, *** indicates significance at the 0.10, 0.05, 0.01 level for a two-tailed t-test.