Transparency of corporate political disclosure and the cost of debt

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Abstract

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Key words: political risk, corporate political disclosure, cost of debt, transparency

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1. Introduction

Anecdotal evidence and recent research provide ample evidence that firms donate extensively to political campaigns, trade associations, and lobbying organizations (e.g., Akey and Lewellen 2017; Hansen et al. 2005). However, firms' corporate political disclosure (CPD, hereafter) remains voluntary, with some firms disclosing expansively and others parsimoniously. Whether the disclosure of political activities should be made mandatory is a highly controversial issue that has attracted a great deal of attention from businesses, policy makers, investment professionals, and academics (Chartered Financial Analyst (CFA) 2014; Stein and Maxell 2016).

Proponents of mandatory disclosure assert that increased disclosure can reduce the agency problems associated with executives using a firm's resources to pursue personal political agendas and allow investors to decide whether a firm's political activities are in the best interests of stakeholders (e.g., Bebchuk and Jackson 2013; Citizens United v. Federal Election Commission 2010).[1] In contrast, opponents of mandatory disclosure argue that public disclosure of political activities does not help businesses but instead "seems more directed at exerting societal pressure on companies to change behavior, rather than to disclose financial information that primarily informs investment decisions."[2] In his comment letter to the SEC, Mr. Quaadman, the president of the Center for Capital Markets Competitiveness of the U.S. Chamber of Commerce, suggests

1. Several other public figures have pushed for mandating the public disclosure of political spending by firms. For example, Robert Menendez, a member of the Senate Banking Committee, who has been pushing the SEC to issue rules on the disclosure of corporate political contributions, points out in an interview that "it is important to shareholders and investors to know how their money is being spent…. It casts a bright light on dark money. It would ultimately have a chilling effect on the use of corporate money in elections if companies had to disclose what they were spending and who they were spending it on (Stein and Maxwell 2016)."

2. https://www.bloomberg.com/politics/articles/2015-08-31/democrats-pressure-sec-to-force-disclosure-of-political-spending, retrieved on January 10, 2017

that political spending information is immaterial and that mandating such disclosure "will overload investors with information that few find to be useful when evaluating a company's financial and operational performance."[3]

As firms' political activities are non-trivial and intertwined with firms' investment, financing, and operating decisions (Goldman et al. 2013; Houston et al. 2014; Kim and Zhang 2016), it is important to determine whether and how CPD transparency affects investors. In this study, we use the CPD transparency index, jointly developed by the Center for Political Accountability (CPA) and the Carol and Lawrence Zicklin Center for Business Ethics Research of the Wharton School of the University of Pennsylvania (CPA–Zicklin index), to empirically examine the relation between CPD transparency and the cost of debt in the syndicated loan market.[4] We focus on the syndicated loan market because this market is an important source of corporate financing (Graham et al. 2008; Kim et al. 2011b; Sufi 2007) and the benefits and costs of disclosure transparency can be captured by the cost of debt (Li et al. 2015; Sengupta 1998). We argue that more transparent disclosure of corporate political activities lowers the cost of debt because such disclosure reduces the political uncertainty associated with firms' political activities and also enhances corporate accountability in political spending, thereby resulting in lower agency costs. Specifically, we argue that firms' political activities are a double-edged sword. On the one hand, a firm's political activities may benefit the firm if the candidates it sponsors win the contested seat or the trade unions or lobbying organizations it donates to are successful in their lobbying efforts. On the other hand, such activities could hurt the firm if the

3. The comment letter is available at https://www.sec.gov/comments/s7-06-16/s70616-173.pdf, retrieved on March 21, 2017.

4. CPD transparency measures the extent of firms' disclosure of their overall political activities, including spending, policies, and oversight. However, CPD transparency by itself is not an independent measure of the level of political spending, nor does it measure the extent of firms' political connectedness. We discuss this index in detail in section 4.2.

lobbying activities are unsuccessful or the political parties it sponsors lose (Kim et al. 2012).[5] Transparent disclosure of political activities can provide information about the parties or trade organizations the firm sponsors, and therefore lower the political activity uncertainty lenders face, leading to a lower cost of debt. In addition, enhancing CPD transparency provides corporate managers with strong incentives to be more accountable for their political investment activities and mitigates lenders' concerns about corporate resources being wasted on value-destroying political activities. Accordingly, we predict that the cost of debt is negatively associated with CPD transparency.

Our analysis of the relationship between cost of debt and CPD transparency index scores for a sample of Standard & Poor's 500 firms in the 2012–2015 period provides strong evidence that firms' CPD transparency is negatively associated with cost of debt. The reduction in borrowing costs is 12–19 basis points when a firm's CPD transparency increases from the first quintile to the third quintile, which is about 11% to 17% of the basis points charged on the sample firms' debt. The baseline results are robust to an instrumental variable approach that addresses the potential endogeneity bias that may result from firms' non-random decision to disclose political activities. In cross-sectional analyses, we document that the negative association between cost of debt and CPD transparency is more pronounced for firms that are more sensitive to government economic policy, have entrenched CEOs, and are smaller. These results are consistent with our arguments that greater CPD transparency reduces the uncertainty and agency costs associated with firms' political activities. Furthermore, our results remain

5. The 2016 U.S. presidential election provides impetus for this as many lobbying efforts and political gambles impacted firm equity values and had serious implications for those firms and industries that bet on the wrong candidate (see news reports available at http://time.com/money/page/2016-presidential-election-clinton-trump-affect-finances/, https://www.forbes.com/sites/steveschaefer/2016/11/05/election-day-clinton-trump-2016-markets/#5854181543e8, or https://www.washingtonpost.com/posteverything/wp/2016/11/09/stock-futures-tanked-on-news-that-trump-was-winning-what-does-that-tell-us/?utm_term=.da54d86634b9, retrieved on March 27, 2017).

qualitatively similar after we control for firms' financial reporting quality, measured by the level of abnormal accruals, and their non-financial disclosure quality, measured by the Environment, Social, and Governance disclosure (ESG) score provided by Bloomberg. This suggests that CPD represents a distinct dimension of a firm's non-financial disclosure that reduces creditors' political risk uncertainty.

To the best of our knowledge, our study is the first to examine the economic consequences of CPD transparency on capital markets. It makes three contributions to the literature. First, we inform the current debate over whether mandatory disclosure of political spending is desirable.[6] Our findings suggest that CPD reduces political uncertainty and agency costs, and thus support the claim that mandatory CPD enhances corporate transparency and is beneficial to investors. Second, we provide insight into the growing literature on the effect of political risk on firm value (e.g., Kelly et al. 2016; Kim et al. 2012). While existing studies mainly focus on how firms' political geographical alignment (Kim et al. 2012) and political connections (e.g., Kim and Zhang 2016) reduce political risk, our evidence suggests that CPD transparency mitigates the risk associated with political uncertainty, particularly for firms facing greater political uncertainty. Third, we contribute to the literature on the implications of non-financial disclosure for the level of information asymmetry in the capital markets (e.g., Dhaliwal et al. 2011, 2014; Du et al. 2015; Ge and Liu 2015; Jung et al. 2016). We show that while CPD transparency is positively associated with firms' non-financial disclosure and financial reporting

6. For example, in 2015, 44 senate Democrats penned a letter to SEC Chairwoman Mary Jo White encouraging her to take action on disclosure rules for corporate political contributions Ms. White was unable to address this call due to a regulatory restriction contained in a 2015 federal spending bill that does not allow the SEC to "finalize, issue or implement" a rule on the disclosure of political contributions, or contributions to trade associations and other tax-exempt organizations through the fiscal year 2016. However, that restriction should lapse at the end of fiscal year 2016 and allow Ms. White to tackle the issue of disclosure rules in 2017.

quality, CPD transparency has a statistically significant incremental effect on the cost of debt, indicating that CPD plays an important role in capital markets and should not be overlooked.

The rest of this paper is organized as follows. Section 2 reviews the related literature and develops our hypotheses. Section 3 presents our research design and sample selection. Section 4 reports our empirical results. Section 5 presents the results of our sensitivity tests. Section 6 offers our conclusions.

2. Institutional background, literature review, and hypothesis development

Corporate disclosure of political activities

In the U.S., for an extended period of time, there was little concern over corporate political disclosure transparency, as the 1907 Tillman Act banned corporations from funding federal campaigns, and the ban was extended to labor unions under the Taft–Hartley Act of 1947.[7] However, recent changes that allow firms to make unlimited political contributions have alerted investors, public advisory groups, and regulators to the (lack of) transparency in political spending disclosure.[8] As of now, the U.S. Stock Exchange Commission (SEC) has not promulgated any formal rules for corporate disclosure of political contributions, and such disclosures remain voluntary. Companies are adopting political disclosure policies through corporate governance engagement. This information is publicly available through the websites of companies that voluntarily disclose their political contributions, but investors often have to go

7. In 1971, the Federal Election Campaign Act (FECA) required the disclosure of campaign expenditures and contributions. FECA severely limited the amount of contributions and funding a corporation could give an individual or campaign. In 1976, the expenditure limits were struck down by the Supreme Court's decision in Buckely vs. Valeo 424 U.S. 1 (1976), but the severe limits on contributions were left intact. Throughout this period, these laws proved unwieldy and difficult to enforce.

8. In January 2010, the Supreme Court issued its landmark's decision in Citizens United vs. FEC that permits corporations to spend unlimited sums to influence federal elections. Since then, the amount of money spent by political groups, which do not reveal their donors' identity, increased from $100 million in 2008 to $300 million in 2012, according to the Center for Responsive Politics, a Washington-based research group (Available at http://www.nj.com/politics/index.ssf/2016/09/should_companies_disclose_their_political_spending.html, retrieved on December 16, 2016).

through a maze of different sources to obtain the information, which is often presented inconsistently. Moreover, the voluntary disclosures are issued inconsistently over time and across companies, and are often incomplete due to the lack of enforcement mechanisms.[9] As noted in the Wall Street Journal (Stein and Maxwell 2016), "One thing that frustrates investors is the lack of a central repository for data on corporate giving. Finding out how much a company gave to politicians, causes and trade groups would require searches of dozens of databases, and even that might not yield a complete record."

Although there is very limited regulation of CPD, there is political pressure from numerous advocacy groups and elected officials to adopt comprehensive CPD policies, including full disclosure of firms' donations. For example, JP Morgan Chase's shareholders required that the company disclose how and why it used company money to engage in political action at their annual meeting in 2006 (Tambe 2006). Bruce Freed, president and founder of the Center for Political Accountability, which advocates greater disclosure of corporate political contribution, indicates that investors' want to make sure corporate involvement in politics is aligned with a company's stated visions, and suggests that disclosure bolsters accountability. Timothy Smith, director of environmental, social, and governance shareowner engagement at Walden Asset Management, which manages about $2.7 billion of assets, points out that "what we are asking for in disclosure is that a company be upfront and explain why such spending is important for the company's strategy" (Stein and Maxwell 2016). New York City Comptroller Scott Stringer, who manages the city's pension funds and is pressing the issue at several companies, states that "We want to ensure that any corporate political spending advances the long-term interests of the company and its shareowners, not the personal political preferences of a particular executive

9. Our select review of firms' websites and disclosures suggests that CPD practices vary greatly between firms. Some firms provide transparency hubs with key CPD information prominently displayed; others bury information deep in their websites many clicks from the homepage.

with access to the corporate purse strings" (Stein and Maxwell 2016). Such demands for CPD transparency are also echoed by leaders of companies such as Merck, Capital One, Noble Energy, Exelon, Prudential, and Microsoft, who recognize that disclosure protects not only the company but also its stakeholders (Bagley et al. 2015).

However, the U.S. Chamber of Commerce and the Business Roundtable, among the largest recipients of corporate funds, have actively campaigned against efforts to get their members to open up about political spending on the grounds that such disclosure would exert unnecessary pressure on firms' business decisions.[10] It is argued that the pressure on business to increase corporate political spending disclosure transparency could be driven by the private interests of a small group of investors rather than by the interests of shareholders in general. Baloria et al. (2013) find that it is the discrepancies in political ideologies that are likely to prompt pension funds to demand that firms make more disclosure of political spending, and that the implementation of such disclosure is associated with negative stock returns.

Hypothesis development

The literature on the economic consequences of voluntary disclosure suggests that transparent voluntary disclosure signals management's openness, reflects management's discretionary choice about how much information to share with parties outside the firm, and improves the confidence of capital providers, thereby resulting in a lower cost of debt (e.g., Bharath et al. 2008; Cho et al. 2013; Graham et al. 2005, 2008; Kim et al. 2011b; Sengupta 1998). We argue that greater CPD transparency lowers borrowing firms' cost of debt because it reduces the political uncertainty and agency costs associated with political activities and assuages lenders' concerns about the possible adverse effects of such activities. Specifically,

10. https://www.bloomberg.com/politics/articles/2015-08-31/democrats-pressure-sec-to-force-disclosure-of-political-spending, retrieved on January 10, 2017

lenders face uncertainty due to the risky nature of their borrowers' corporate political activities because such activities require significant resource commitments without guaranteeing a favorable policy change or a positive impact on borrowers' future profitability (Aggarwal et al. 2012; Getz 2002; Gordon and Hafer 2005; Rehbein and Schuler 1999).[11] Moreover, increased disclosure of political spending provides corporate managers with stronger incentives to engage in more accountable political activities and constrains managerial opportunism such as diverting corporate resources for their own personal gain, which could lower default risk (Black et al. 2014; Denis et al. 2002; Desai et al. 2007; Kim et al. 2011a, b). Based on the foregoing arguments, we posit that greater CPD transparency lowers lenders' concerns about political uncertainty and constrains managerial opportunism, leading to a lower cost of debt. We state our first hypothesis in the alternative form, as follows:

HYPOTHESIS 1. *All else being equal, firms with more transparent CPD are charged lower loan interest spreads than firms with less transparent CPD.*

3. Sample selection and research design

Data and sample selection

Our sample includes S&P 500 firms with available CPD scores that received syndicated loans between 2012 and 2015. Our loan sample starts from 2012 because 2011 is the first year in which CPD scores are publicly available for S&P 500 firms; the sample stops in 2015 because 2015 is the last year for which complete loan information is available.[12] We obtain loan pricing and non-pricing data from the Dealscan database. Dealscan contains complete information about

11. Coates (2010) finds that firms that are politically active through controlling political committees, registered lobbying, or both, have lower price/book ratios than industry peers that are not politically active. Aggarwal et al. (2012) show that companies making soft money donations to parties or donations to Section 527 committees from 1991 to 2004 have more free cash, and are growing slower and investing less. They also show that the amount of contributions of these firms is negatively correlated with long-term, firm-specific stock market performance.

origination date, amount, maturity, collateral requirements, covenants, purposes, and costs of loans for each loan package and facility. We focus on loan facilities rather than loan packages because loan pricing terms are different for different facilities within a loan package.

Measures of CPD transparency

We collect corporate political disclosure and accountability (CPD&A) disclosure index scores for the 2011–2014 period using a new and unique dataset that is the result of a joint initiative between the Center for Political Accountability (CPA) and the Carol and Lawrence Zicklin Center for Business Ethics Research of The Wharton School of the University of Pennsylvania (CPA–Zicklin index). The index measures the CPD policies and the practices related to political spending of S&P 500 companies in the United States. We construct four CPD transparency measures using the following four scoring items in the CPA–Zicklin index: disclosure percentage (*PCT_DIS*), policy percentage (*PCT_POLICY*), oversight percentage (*PCT_OVER*), and overall CPD transparency percentage (*PERCENTAGE*).

Disclosure percentage (*PCT_DIS*) measures the transparency of voluntary corporate disclosure on both the amount and the identity of the recipients of the political contribution, and the titles and names of the executives who authorize the spending. Specifically, *PCT_DIS* is a firm's summed raw score for nine voluntary disclosure transparency-related items divided by the possible 36 points in Zicklin's disclosure category; the nine questions used in the scoring are given below.[13] The disclosure of such information not only makes corporate political activities more transparent, it also holds management accountable for their corporate political contribution decisions.

MAX

12. We use *CPD* in year $t-1$ to predict its effect on the cost of loans borrowed in year *t*.
13. Source: The 2014 CPA–Zicklin Index of Corporate Political Disclosure and Accountability. Available at politicalaccountability.net/index (retrieved on December 15, 2016)

D1	Does the company publicly disclose corporate contributions to political candidates, parties, and committees, including recipient names and amounts given?	4
D2.	Does the company publicly disclose payments to 527 groups, such as governors associations and super PACs, including recipient names and amounts given?	4
D3.	Does the company publicly disclose independent political expenditures made in direct support of or opposition to a campaign, including recipient names and amounts given?	4
D4.	Does the company publicly disclose payments to trade associations that the recipient organization may use for political purposes?	6
D5.	Does the company publicly disclose payments to other tax-exempt organizations that the recipient may use for political purposes?	6
D6.	Does the company publicly disclose a list of the amounts and recipients of payments made by trade associations or other tax exempt organizations of which the company is either a member or donor?	2
D7.	Does the company publicly disclose payments made to influence the outcome of ballot measures, including recipient names and amounts given?	4
D8.	Does the company publicly disclose the company's senior managers (by position/title of the individuals involved) who have final authority over the company's political spending decisions?	2
D9.	Does the company publicly disclose an archive of each political expenditure report, including all direct and indirect contributions, for each year since the company began disclosing the information (or at least for the past five years)?	4

Policy percentage (*PCT_POLICY*) measures the transparency of the voluntary corporate disclosure of the policies that mandate directors and officers to regularly monitor the firm's political spending to ensure that such spending is consistent with the company's public policy position, and advances the long-term interests of the company rather than advancing any individual manager's personal preference. Specifically, *PCT_POLICY* is a firm's summed raw score for six CPD policy scoring items divided by the possible 16 points in Zicklin's policy category, which are scored based on the following six questions.

		MAX
P1	Does the company disclose a detailed policy governing its political expenditures from corporate funds?	6
P2	Does the company have a publicly available policy stating that all of its contributions will promote the interests of the company and will be made without regard for the private political preferences of executives?	2
P3	Does the company publicly describe the types of entities considered to be proper recipients of the company's political spending?	2
P4	Does the company publicly describe its public policy positions that become the basis for its spending decisions with corporate funds?	2
P5	Does the company have a public policy requiring senior managers to oversee and have final authority over all of the company's political spending?	2
P6	Does the company have a publicly available policy that the board of directors regularly	2

oversees the company's corporate political activity?

Oversight percentage (*PCT_OVER*) measures the transparency of the voluntary corporate disclosure of the existence and effectiveness of board oversight over political spending through a specified committee. Specifically, *PCT_OVER* is a firm's summed raw score for two oversight-related scoring items divided by the possible 4 points in Zicklin's policy category, which are scored based on the following two questions.

		MAX
O1	Does the company have a specified board committee that reviews the company's policy on political expenditures?	2
O2	Does the company have a specified board committee, composed entirely of outside directors, that oversees its political activity?	2

Overall CPD transparency (*PERCENTAGE*) measures the aggregated transparency of corporate disclosure, corporate policies, and board oversight over political spending activities. *PERCENTAGE* is a summed total raw score for a firm's CPD disclosure (D1–D9), CPD policies (P1–P6), and CPD oversight (O1–O2), divided by the possible 56 points in the scoring items in the CPA–Zicklin index. *PERCENTAGE* provides a comprehensive assessment of a firm's CPD transparency and can assess creditors' political risk related to corporate political contributions.

Research design

To test our hypothesis, we estimate the following regression model:

$$AISD_{i,t} = \beta_0 + \beta_1 CPDTRANSPARENCY_{i,t-1} + \beta_2 Loan\ Specific\ Characteristics_{i,t} + \beta_3 Borrower\ Specific\ Characteristics_{i,t-1} + Industry\ \&\ Year\ Fixed\ Effect + \varepsilon_t\ , \quad (1)$$

where the dependent variable, *AISD*, is the cost of debt, measured as the total spread (including associated annual fees, if any) paid over the London Interbank Offered Rate (LIBOR) on the amount of loans borrowed in a loan contract for borrower *i* in year *t*. The independent variable, *CPDTRANSPARENCY*, is a placeholder for our four measures of CPD transparency

(*PERCENTAGE*, *PCT_DIS*, *PCT_POLICY*, and *PCT_OVER*, defined in section 3.2) for borrower *i* in year *t−1*. By relating the lagged value of *CPDTRANSPARENCY* to the current value of *AISD*, we are better able to attribute the cost of debt to the transparency of CPD. Following previous studies (e.g., Bharath et al. 2008; Dennis et al. 2000; Ge et al. 2016; Houston et al. 2014; Kim et al. 2011c), we include a set of loan-specific control variables that are related to loan contracting terms. These control variables include the following: natural logarithm of loan maturity (*LnMaturity)*; natural logarithm of loan amount *(LnLoanSize)*; indicator for secured loan *(Secured*); indicator for term loan *(TermLoan)*; and indicator for relationship loan *(Rel_Dum).* We also control for borrower-specific variables that are known to affect loan contract terms, including the natural logarithm of firm assets (*Lat*), leverage ratio *(Levg*), profitability ratio (*Prof*), ratio of tangible assets to total assets (*Tang*), Altman's Z-score (*Zscore),* an indicator for S&P crediting rating, and the natural logarithm of the number of financial and non-financial covenants (*Lfcov* and *Lnfcov)*. We also include indicator variables for year and for 4-digit SIC industry codes to control for year and industry fixed effects, and use White standard errors corrected for firm and year clustering for our statistical tests. The variable definitions are presented in the Appendix A. Hypothesis 1 predicts that the coefficient of *CPDTRANSPARENCY* is negative. That is, more transparent CPD is associated with lower loan interest spread.

4. Empirical analyses

Descriptive statistics of the sample

Table 1 panel A presents the distribution of our sample by year. The number of firm-loans increases from 52 in 2012 to 182 in 2015, mainly due to an increase in the available CPD data. Panel B presents the descriptive statistics of the firm and loan characteristics. The mean and

median scores of *PERCENTAGE* are 49.23 and 53.95, respectively, with some firms achieving 100. The average (median) loan spread is 117 (113) basis points, similar to the spread for the S&P 500 firms in Houston et al. (2014). The average (median) loan size of about 1.6 (1.8) billion USD is also consistent with the loan amount documented in Houston et al. (2014). Panel C presents the correlations of the main variable of interest. Consistent with our expectation, *AISD* is negatively associated with all four measures of CPD at the 5% level or better.

<< Please Insert Table 1 Here>>

Test of Hypothesis 1: Relation between CPD transparency and loan interest spread

In Hypothesis 1, we predict that loan spread is negatively associated with the CPD score, as voluntary disclosure potentially mitigates a firm's information asymmetry and lowers the lender's perceived credit risk. We report the estimation results in Table 2. As predicted, the coefficients on all four measures of CPD are negative and statistically significant at the 1% level. Specifically, the coefficients on *PERCENTAGE*, *PCT_DIS*, *PCT_POLICY*, and *PCT_OVER* are −0.338, −0.237, −0.445, and −0.222 and the t-statistics are −12.853, −5.891, −5.088, and −5.479, respectively, which suggests that firms with more transparent political disclosure incur lower cost of debt. The effect of political transparency on cost of debt is also economically significant. Specifically, an increase in disclosure transparency from the first quintile to the third quintile is accompanied by a reduction in the cost of debt in the range of 12 to 19 basis points, which is about 10% to 17% of the average basis points charged for the sample firms. The coefficients on the other control variables are in general consistent with prior studies. For example, larger firms and less leveraged firms are charged a lower cost of debt.

<< Please Insert Table 2 Here>>

Instrumental variable approach

As a firm's CPD transparency could be affected by unobservable factors such as the firm's overall attitude toward transparency, it is unclear whether the observed reduction in the cost of debt can be directly attributed to CPD transparency. In this section, we use an instrumental variable approach to analyze the relation between CPD transparency and the cost of debt. To implement the instrumental variable approach, we first identify an instrumental variable that is correlated with a firm's CPD transparency, but that does not affect the firm's cost of debt directly. We then employ a two-stage least squares (2SLS) regression, which uses the predicted value of *CPD TRANSPARENCY* obtained in the first stage to examine the relationship between cost of debt and CPD transparency in the second stage. Specifically, following Laeven and Levine (2007), we use the industry average (excluding the firm itself) *CPDTRANSPARENCY* as an instrument. Although an individual firm's disclosure practices are highly correlated with the disclosure practices of its industry, the industry-level disclosure score should not affect the individual firm's cost of debt. We calculate the predicted value of *CPDTRANSPARENCY* for each firm and use the predicted *CPDTRANSPARENCY* (*PREDICTED_PERCENTAGE*) as the independent variable in the second stage.[14]

We present the two-stage regression results in Table 3. Column (1) reports the results for the first stage regression. Consistent with our expectation, individual firms' CPD is positively associated with industry CPD and the association is significant at the 1% level. The second stage results, presented in column (2), show a negative and significant coefficient on *PREDICTED_PERCENTAGE (coefficient = −0.522; t-statistic = −2.444)*, which suggests that our results are robust to the instrumental variable approach, and that the negative relationship between cost of debt and CPD transparency is not due to unobservable factors.

14. For the sake of brevity, we only report the results using *PERCENTAGE* as a measure of CPD transparency. The results using the other three measures of CPD transparency are qualitatively similar. The results are available upon request.

<< Please Insert Table 3 Here>>

Cross-sectional analyses

We contend that CPD transparency is related to firms' cost of debt because it lowers lenders' concerns about the uncertainty associated with firms' political activities and the agency costs of such activities. To explore the mechanisms through which CPD relates to cost of debt, we investigate the moderating effects of political uncertainty and the internal monitoring of corporate political activities on the relationship between CPD transparency and cost of debt. Specifically, we classify firms based on their sensitivity to government economic policies, their internal monitoring of political activities, and the transparency of their overall informational environment. Then we analyze whether the effect of CPD transparency is more pronounced in settings where political uncertainty or corporate governance is a concern.

Political sensitivity

Businesses operate in complex political environments. Government policy affects firms' value through tax reform and by enacting and enforcing investment and competition regulations (Hansen et al. 2005), and this can motivate firms to engage in political activities. Kelly et al. (2016) show that political uncertainty impacts firms' credit rating in the debt market and risk premium in the equity market. Akey and Lewellen (2017) find that firms with a higher sensitivity to policy uncertainty (such as firms in real estate and healthcare) are likely to be more politically active. However, firms that engage in extensive political activities may also be subject to adverse publicity when their sponsored political intermediaries engage in activities not consistent with stakeholders' interests or when their activities fail to achieve the desired outcomes.

We argue that lenders are more concerned about the CPD transparency of more politically sensitive companies, as these creditors face heightened risks associated with more

uncertainty regarding the financial benefits of firms' extensive political activities. Accordingly, we predict that CPD transparency plays a more important role in firms with higher political sensitivity. Empirically, we specify the following regression model to test the moderating effect of political sensitivity.

$$AISD_{i,t} = \gamma_0 + \gamma_1 CPDTRANSPARENCY_{i,t-1} + \gamma_2 PS\_High_{i,t-1}$$
$$+\gamma_3 PS\_High_{i,t-1} * CPDTRANSPARENCY_{i,t-1} + \gamma_4 Loan\ Specific\ Characteristics_{i,t}$$
$$+ \gamma_5 Borrower\ Specific\ Characteristics_{i,t-1} + Industry\ \&\ Year\ Effects + \varepsilon, \quad (2)$$

where *PS_HIGH* is an indicator variable that equals 1 if a firm exhibits high sensitivity to economic policy uncertainty, and 0 otherwise. We follow Akey and Lewellen (2017) and define politically sensitive firms as firms whose stock returns vary significantly with economic policy uncertainty (Baker et al. 2016). Specifically, we regress monthly stock returns on the monthly economic policy uncertainty index for each firm over a period of 36 months prior to the loan syndication year; we define a firm as being sensitive to economic policy uncertainty if the p-value is less than or equal to 0.1. All of the other variables are as defined in equation (1).

We report the results of this analysis in Table 4. First, we show that the coefficients on the interaction between *PS_HIGH* and all four measures of disclosure transparency are negative and statistically significant at the 10% level or better. Specifically, the coefficients on *PS_High* × *PERCENTAGE*, *PS_High* × *PCT_DIS*, *PS_High* × *PCT_POLICY*, and *PS_High* × *PCT_OVER* are −0.550, −0.441, −0.670, and −0.317 and the t-statistics are −2.464, −1.910, −3.365, and −1.749, respectively. These results suggest that CPD transparency is more important for policy-sensitive firms that are likely to be more engaged in political activities. The coefficients on *PERCENTAGE*, *PCT_DIS*, *PCT_POLICY*, and *PCT_OVER* are negative and significant, suggesting that CPD transparency also lowers the cost of debt for firms with lower policy sensitivity. Additionally, the coefficients on *PS_HIGH* are positive and statistically significant in

all four models, which indicates that politically sensitive firms pay a higher cost of debt. This result is in contrast with the findings in the political connection literature that politically connected firms incur a lower cost of debt (e.g., Houston et al. 2014). Our results suggest that political connection and political sensitivity could be capturing different political dimensions of firms.

<< Please Insert Table 4 Here>>

Internal monitoring of corporate political activities

In Hypothesis 1, we argue that CPD transparency leads to lower cost of debt because greater CPD transparency constrains managerial opportunism. To further substantiate this argument, we explore whether the strength of internal corporate governance alters the relation between CPD transparency and cost of debt. If CPD transparency reduces lenders' concerns about managerial opportunism, we expect that the impact of CPD transparency on cost of debt will be more pronounced in firms with weaker board monitoring over these activities. We use CEO duality as a proxy for the strength of a firm's internal monitoring, because CEO duality is associated with higher managerial opportunism and risk-taking behavior (e.g., Hambrick and D'Aveni 1992 ; Harris and Helfat 1998; Li and Tang 2010; Worrell et al. 1997). We predict a negative coefficient on the interaction term between CPD and CEO duality. We collect CEO duality data from Bloomberg and create an indicator variable *CEO_Chair* that equals 1 if the CEO is also the chairman of the board, and 0 otherwise. We then estimate equation (2) after replacing *PS_High* with *CEO_Chair*.

We report the estimation results in Table 5. The coefficients on the interaction term between CEO duality and the CPD transparency measures are negative and statistically significant at the 10% level or better. The coefficient on *CEO_CHAIR* is positive but statistically

significant only in the *PERCENTAGE* regression. Overall, the results in Table 5 suggest that the effect of CPD on cost of debt is more pronounced when internal corporate governance, as proxied by CEO duality, is weak.

<< Please Insert Table 5 Here>>

Effect of firm information environment

Next, we examine how CPD transparency interacts with the firm's overall information environment. We contend that smaller companies have a poorer information environment because they are less likely to have extensive media coverage or analyst following. As a result, lenders might rely more on CPD transparency when assessing political risk.[15] Empirically, this implies that the impact of CPD transparency on cost of debt is stronger for smaller firms. We create an indicator variable *SML* that equals 1 if a firm's assets are smaller than the sample median, and 0 otherwise; we then interact *SML* with the four measures of CPD and estimate equation (2) with *PS_High* replaced with *SM*L.

Table 6 reports the estimation results. As expected, the coefficients on the interaction term between measures of CPD transparency and the indicator for smaller firms are negative and statistically significant at the 5% level or better. The coefficient on *SML* is positive and statistically significant, which is consistent with the findings of prior research that smaller firms incur higher cost of debt (e.g., Fang et al. 2016; Ge et al. 2016). The negative coefficient on the interaction term *SML* × *CPD TRANSPARENCY* suggests that CPD transparency reduces the cost of debt more for small firms than for large firms.

<< Please Insert Table 6 Here>>

Additional sensitivity tests

15. We acknowledge that the firms in our sample are large S&P 500 firms, and therefore this classification may work against detecting the moderating effect of size.

Effects of non-financial disclosure quality and financial reporting quality

It is possible that a firm's political disclosure strategy is associated with its overall reporting transparency. Thus, firms with higher CPD transparency could be firms that also have higher non-financial disclosure quality and financial reporting quality (e.g., Francis et al. 2008; Lennox and Park 2006), which may subsume the effect of CPD transparency on the cost of debt. To assess whether CPD transparency is related to the cost of debt in addition to the effects of non-financial disclosure quality and financial reporting quality, we first perform a correlation analysis of these three variables. We use the average of the Environmental, Social, and Governance (ESG) scores provided by Bloomberg to proxy for firms' non-financial disclosure quality.[16] To proxy for financial reporting quality, we use performance-matched discretionary accruals (Kothari et al 2005) estimated for each 2-digit SIC industry. The results reported in Table 7 panel A show that firms with higher CPD transparency have both higher financial reporting quality and non-financial disclosure quality. Next, we include measures of financial reporting quality and non-financial disclosure quality in equation (1) and investigate whether CPD transparency has a distinct effect on the cost of debt. We report these results in panels B and C of Table 7.

The results in panel B show that the cost of debt still decreases with CPD transparency and the coefficients on *PERCENTAGE* (coefficient = −0.197; t-statistic = −2.602) and

16. ESG scores are a much broader measure of a firm's non-financial information environment, which incorporate over 900 data items. Bloomberg collects environmental, social, and governance information from corporate CSR reports, annual reports, and websites and uses a proprietary scoring system to score firms' environmental, social, and governance disclosure. Environmental information (E) relates to information about emissions, water, waste, energy, and operational policies that have an environmental impact. Social information (S) relates primarily to information about employees, products, and the firms' impact on communities. Governance information (G) relates to information about board structure and function, firms' political involvement, and executive compensation. The disclosure scores range from 0.1 (lowest) to 100 (highest). The penetration of Bloomberg's Environmental, Social and Governance (ESG) data has grown from 1,545 unique users in 2009 to over 12,000 users in 2015. (https://www.bloomberg.com/bcause/customers-using-esg-data, retrieved on March 18, 2017).

PCT_POLICY (coefficient = −0.316; statistic = −3.808) are negative and significant after controlling for non-financial disclosure quality. In the *PCT_DIS* regression, the coefficient is −0.127 and the t-value is −1.535. In panel C, we report the results after controlling for abnormal accruals. We remove financial and utility firms from this analysis because of the specialized nature of the reporting models in those industries. We show that the coefficients on all four measures of disclosure quality are negative and statistically significant at least at the 5% level. These results confirm that CPD transparency is negatively related to the cost of debt even after controlling for differences in nonfinancial disclosure quality and financial reporting quality.

<< Please Insert Table 7 Here>>

Removing financial and utility firms

Table 8 reports the results after removing the regulated firms in the financial and utilities industries. The results show that cost of debt decreases with CPD transparency across all four CPD transparency measures. Consistent with the results in Table 2 for the full sample, the coefficients on all four CPD transparency measures are significant at the 5% level or better. This demonstrates that the results are not sensitive to the inclusion of regulated industries in the sample.

<< Please Insert Table 8 Here>>

5. Conclusions

Using a unique dataset (CPA–Zicklin index) to construct measures of CPD transparency, we examine the relation between CPD transparency and the cost of debt. We find that firms with more transparent CPD incur a lower cost of debt. We further show that the impact of CPD transparency on the cost of debt is even more pronounced for companies that are more sensitive to government economic policy uncertainty, have weaker internal monitoring over corporate

political contribution, and that have a less transparent overall information environment. Overall, our empirical findings suggest that bank lenders perceive CPD transparency as an incrementally important information risk factor, beyond traditional borrower-specific credit risk factors (e.g., profitability, growth, liquidity, etc.) and financial reporting quality. The information risk embedded in CPD cannot be removed by lenders' superior access to borrowers' information or the ability to better monitor borrower's operations, and is relevant and important in determining the cost of debt.

To the best of our knowledge, this study is the first to examine the economic consequences of CPD transparency for the cost of debt. Given the controversy over mandating political disclosure, our study provides the first piece of empirical evidence on the risk-reducing role of CPD transparency. Our evidence suggests that CPD transparency has economically significant benefits, and that such benefits are more significant for firms that are more politically sensitive, smaller, and have entrenched CEOs.

Appendix A: Variable Definitions

Variables	Definitions
AISD	Cost of borrowing, measured by the basis points above the LIBOR for loans borrowed.
PERCENTAGE	The sum of the raw scores for 17 scoring items used to construct *PCT_DIS*, *PCT_POLICY*, and *PCT_OVER*, divided by a possible 56 points in the scoring items in CPA–Zicklin index.
PCT_DIS	A firm's summed raw score for nine transparency-related scoring items divided by a possible 36 points in Zicklin's disclosure category.
PCT_POLICY	A firm's summed raw score for six CPD policy scoring items divided by a possible 16 points in Zicklin's policy category.
PCT_OVER	A firm's summed raw score for two oversight-related scoring items divided by a possible 4 points in Zicklin's policy category.
AB_TACC	The signed abnormal accruals (abnormal accruals = total accruals – normal accruals), where normal accruals are estimated for each 2-digist SIC industry using the performance-matched discretionary accruals model (Kothari et al. 2005).
ESG	The average of the Environmental, Social and Governance (ESG) scores provided by Bloomberg.
CEO_CHAIR	An indicator variable that equals 1 if the CEO is also the chairman of the board; 0 otherwise.
Credit rating dummies	A vector of dummy variables for S&P credit rating.
Levg	Borrower's book value of total debt divided by market value of equity: ((dltt+dlc)/(prcc_f×csho)).
Lat	Natural logarithm of total assets at year *t*.
Lfcov	Natural logarithm of (1+ the total number of financial covenants).
Lnfcov	Natural logarithm of (1+ the total number of non-financial covenants).
LnLoanSize	Natural logarithm of loan amount.
LnMaturity	Natural logarithm of loan maturity.
PS_HIGH	An indicator variable that equals 1 if a firm is more sensitive to economic policy uncertainty, and 0 otherwise. The Akey and Lewellen (2017) methodology is used to classify firms as more or less sensitive to economic policy uncertainty. A more sensitive firm is a firm whose stock returns vary significantly with the economic policy uncertainty index (Baker et al. 2016). Specifically, the monthly economic policy uncertainty index is regressed on monthly stock returns for each firm over a period of 36 months prior to the loan syndication year. A firm is defined as being sensitive to economic policy uncertainty if the p-value is less than or equal to 0.1.
Prof	Profitability, calculated as net income divided by total assets.
Rel_Dum	An indicator variable that equals 1 if the loan syndicate contains at least one relationship lead lender, and 0 otherwise. Relationship lead lenders are defined as lenders that have lent money to the borrower within the previous 5 years.
Secured	An indicator variable equal to 1 if a loan requires collateral, and 0 otherwise
SML	An indicator variable equal to 1 if firm assets are below the sample median, and 0 otherwise
Tang	Tangibility, measured as net property, plant, and equipment, divided by total assets: (ppent/at).
TermLoan	An indicator variable equal to 1 if the loan is a term loan, and 0 otherwise
Zscore	Altman's Z-score = 1.2×wcap/at+1.4×re/at+3.3×ebit/at+0.6×(prcc_f×csho)/lt+sale/at.

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TABLE 1
Descriptive statistics
Panel A: Yearly distribution

Loan Issue Year	Freq.	Percent	Cum.
2012	52	11.5	11.5
2013	104	23.01	34.51
2014	114	25.22	59.73
2015	182	40.27	100
Total	452	100	

Panel B: Descriptive statistics

Variables	N	mean	SD	p25	p50	p75	min	max
PERCENTAGE	452	49.23	29.23	24.29	53.95	75.71	0	100
PCT_DIS	452	43.26	33.28	5.56	44.44	72.22	0	100
PCT_POLICY	452	69.33	29.80	50	81.25	93.75	0	100
PCT_OVER	452	43.05	30.47	11.11	44.44	66.67	0	100
Lat	452	10.36	0.79	9.79	10.49	11.03	8.04	11.31
Levg	452	0.22	0.12	0.15	0.21	0.30	0	0.64
Prof	452	0.07	0.05	0.04	0.07	0.10	−0.10	0.27
Tang	452	0.31	0.26	0.08	0.21	0.58	0.01	0.86
Zscore	452	1.77	1.20	0.80	1.70	2.34	−1.11	5.82
AISD	452	116.86	58.22	87.50	112.5	125	15	525
LnMaturity	452	3.65	0.70	3.30	4.09	4.09	1.79	4.43
LnLoanSize	452	21.18	0.93	20.72	21.30	21.82	17.91	23.21
TermLoan	452	0.12	0.32	0	0	0	0	1
Secured	452	0.07	0.25	0	0	0	0	1
Rel_Dum	452	0.96	0.20	1	1	1	0	1
Lfcov	452	0.44	0.43	0	0.69	0.69	0	1.39
Lnfcov	452	1.43	0.11	1.39	1.39	1.39	1.39	1.95
Notrated	452	0.60	0.49	0	1	1	0	1

Panel C: Correlation analysis

		1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17
1	*AISD*	1																
2	*PERCENTAGE*	−0.13	1															
		0.00																
3	*PCT_DIS*	−0.10	0.95	1														
		0.03	0.00															
4	*PCT_POLICY*	−0.17	0.89	0.74	1													
		0.00	0.00	0.00														
5	*PCT_OVER*	−0.12	0.90	0.74	0.83	1												
		0.01	0	0	0													
6	*Lat*	−0.07	0.26	0.17	0.33	0.30	1											
		0.15	0	0	0	0												
7	*Levg*	0.10	0.09	0.08	0.04	0.11	−0.01	1										
		0.03	0.06	0.09	0.39	0.02	0.76											
8	*Prof*	−0.20	0.04	0.06	0.03	0.00	−0.43	−0.18	1									
		0.00	0.37	0.22	0.53	0.92	0	0										
9	*Tang*	0.08	−0.05	−0.07	−0.05	0	0.21	0.23	−0.29	1								
		0.11	0.28	0.14	0.31	0.96	0	0	0									
#	*Zscore*	−0.03	−0.07	−0.09	0.00	−0.08	−0.41	−0.38	0.47	−0.35	1							
		0.55	0.12	0.05	0.93	0.08	0	0	0	0								
#	*LnMaturity*	0.06	−0.11	−0.11	−0.09	−0.07	−0.09	−0.01	−0.07	0.10	−0.03	1						
		0.18	0.02	0.02	0.05	0.12	0.06	0.83	0.13	0.03	0.57							
#	*LnLoanSize*	−0.17	0.20	0.14	0.26	0.19	0.38	0.06	0.01	−0.07	−0.15	−0.15	1					
		0.00	0.00	0.00	0.00	0.00	0.00	0.18	0.77	0.17	0	0						
#	*TermLoan*	0.27	−0.06	−0.05	−0.08	−0.06	−0.11	0.04	−0.05	−0.06	0.12	0.02	−0.13	1				
		0.00	0.19	0.33	0.11	0.22	0.02	0.43	0.32	0.18	0.01	0.60	0.01					
#	*Secured*	0.52	−0.07	−0.07	−0.05	−0.05	−0.09	−0.01	−0.07	−0.02	0.08	−0.01	−0.12	0.18	1			
		0.00	0.16	0.13	0.25	0.33	0.05	0.76	0.13	0.71	0.10	0.77	0.01	0.00				
#	*Rel_Dum*	0.03	0.00	0.01	0.00	−0.04	0.09	0.16	−0.11	0.07	−0.07	0.05	0.13	0.04	0.01	1		
		0.56	0.98	0.77	0.99	0.45	0.06	0.00	0.02	0.15	0.13	0.25	0.01	0.38	0.81			
#	*Lfcov*	0.12	−0.08	−0.06	−0.13	−0.08	−0.32	0.18	−0.03	0.03	−0.12	0.12	−0.01	0.07	0.10	0.04	1	
		0.01	0.08	0.18	0.00	0.10	0.00	0.00	0.52	0.54	0.01	0.01	0.75	0.11	0.03	0.40		
#	*Lnfcov*	0.26	0.05	0.01	0.05	0.09	−0.18	0.15	−0.04	0.08	−0.01	−0.12	0.05	0.06	0.48	0.06	0.34	1
		0.00	0.33	0.90	0.27	0.05	0.00	0.00	0.35	0.10	0.90	0.01	0.33	0.21	0.00	0.18	0	

Notes: This table presents the descriptive statistics of the S&P 500 firms that have political disclosure scores and also borrowed money from syndicated loan market in the 2012–2015 period. Panel A presents the yearly distribution of the sample by the year of loan issuance. Panels B and C present the descriptive statistics and correlation analysis of the main variables used in the multivariate regressions.

TABLE 2
CPD and cost of debt

VARIABLES	(1) *PERCENTAGE*	(2) *PCT_DIS*	(3) *PCT_POLICY*	(4) *PCT_OVER*
PERCENTAGE	−0.338***			
	[−12.853]			
PCT_DIS		−0.237***		
		[−5.891]		
PCT_POLICY			−0.445***	
			[−5.088]	
PCT_OVER				−0.222***
				[−5.479]
Lat	−15.655***	−17.346***	−13.841***	−17.667***
	[−5.013]	[−5.534]	[−4.832]	[−4.609]
Levg	67.022***	62.151***	66.994***	64.065***
	[4.602]	[4.233]	[4.381]	[4.177]
Prof	−27.150	−20.437	−58.391***	−8.551
	[−1.093]	[−0.701]	[−3.223]	[−0.238]
Tang	−16.039	−7.773	−22.928	−19.492
	[−0.456]	[−0.228]	[−0.651]	[−0.580]
Zscore	−7.293	−7.845*	−5.773	−8.251*
	[−1.530]	[−1.654]	[−1.342]	[−1.812]
Secured	52.908***	54.574***	51.327***	53.567***
	[3.434]	[3.615]	[3.298]	[3.573]
LnMaturity	−0.289	−0.337	−0.031	−0.098
	[−0.095]	[−0.112]	[−0.010]	[−0.032]
LnLoanSize	−2.198	−2.380	−1.525	−2.055
	[−0.710]	[−0.774]	[−0.511]	[−0.662]
TermLoan	11.185*	11.451*	10.265	12.429*
	[1.726]	[1.782]	[1.541]	[1.852]
Lfcov	−11.808***	−11.511***	−12.946***	−11.113***
	[−3.364]	[−3.385]	[−3.871]	[−3.122]
Lnfcov	49.610***	43.592**	59.057***	44.757*
	[3.033]	[2.546]	[4.288]	[1.943]
Rel_Dum	−15.000***	−13.440***	−17.413***	−16.105***
	[−3.537]	[−3.292]	[−5.203]	[−3.178]
Constant	281.339***	299.301***	246.099	292.391***
	[11.043]	[9.064]	[.]	[10.816]
Loan purpose fixed effects	Yes	Yes	Yes	Yes
Credit rating fixed effects	Yes	Yes	Yes	Yes
Industry and year fixed effects	Yes	Yes	Yes	Yes
Observations	452	452	452	452
Adjusted R-square	0.747	0.744	0.753	0.741

Notes: This table presents the multi-variate regression results estimating the effects of *CPD* on cost of debt. The dependent variable is all-in-spread drawn (*AISD*). The measures of *CPD* include the total political transparency percentage (*PERCENTAGE*), disclosure percentage (*PCT_DIS*), policy percentage (*PCT_POLICY*), and oversight percentage (*PCT_OVER*). Variable descriptions for all of the variables are provided in Appendix A. Standard errors are clustered at firm and year with robust and clustered t-statistics provided in parentheses. *, **, and *** represent significance levels of 0.10, 0.05, and 0.01, respectively.

TABLE 3
2SLS Instrumental variable estimation

VARIABLES	(1) First stage	(2) Second stage
INDUSTRY_PERCENTAGE	0.632***	
	[3.931]	
PREDICTED_PERCENTAGE		−0.522**
		[−2.444]
Lat	11.538***	1.431
	[3.196]	[0.204]
Levg	21.021	29.957**
	[0.953]	[2.421]
Prof	−23.363	−132.953***
	[−0.496]	[−4.651]
Tang	2.975	13.574
	[0.280]	[1.564]
Zscore	1.160	0.166
	[0.420]	[0.047]
Secured	−13.395	80.888***
	[−1.284]	[3.449]
LnMaturity	−1.073	2.143
	[−0.510]	[0.631]
LnLoanSize	0.964	−5.251
	[0.532]	[−1.324]
TermLoan	−0.640	16.944**
	[−0.152]	[2.240]
Lfcov	−6.204	10.989***
	[−1.268]	[3.655]
Lnfcov	23.480	−55.493
	[1.334]	[−1.448]
Rel_Dum	2.756	−9.955***
	[0.369]	[−3.222]
Constant	−164.850***	288.317***
	[−2.705]	[5.022]
Loan purpose fixed effects	Yes	Yes
Credit rating fixed effects	Yes	Yes
Year fixed effects	Yes	Yes
Observations	452	452
Adjusted R-square	0.313	0.489

Notes**:** This table reports the instrumental variable estimation results using 2SLS regression to account for the endogeneity of *CPD*. In the first stage, the measure of *CPD* (*PERCENTAGE*) is regressed on the instrumental variable, industry average of *CPD* (*INDUSTRY_PERCENTAGE*), and other independent variables included in the second stage. *INDUSTRY_PERCENTAGE* is calculated as the average *CPD* of all of the firms (excluding the firm itself) in each 2-digit SIC code industry. In the second stage, *AISD* is regressed on the predicted *CPD PERCENTAGE* (*PREDICTED PERCENTAGE*) obtained from the first stage and other independent variables. Column (1) reports the first stage regression results and column (2) reports the second stage regression results. Variable descriptions for all variables are provided in Appendix A. Standard errors are clustered at firm and year. *, **, and *** represent significance levels of 0.10, 0.05, and 0.01, respectively, using two-tailed tests. Robust and clustered t-statistics are provided in parentheses.

TABLE 4
Cross-sectional analysis: Firm's political sensitivity

VARIABLES	(1) *PERCENTAGE*	(2) *PCT_DIS*	(3) *PCT_POLICY*	(4) *PCT_OVER*
PERCENTAGE	−0.282***			
	[−7.143]			
PS_High×PERCENTAGE	−0.550**			
	[−2.464]			
PCT_DIS		−0.186***		
		[−3.383]		
PS_High×PCT_DIS		−0.441*		
		[−1.910]		
PCT_POLICY			−0.354***	
			[−4.386]	
PS_High×PCT_POLICY			−0.670***	
			[−3.365]	
PCT_OVER				−0.211***
				[−5.285]
PS_High×PCT_OVER				−0.317*
				[−1.749]
PS_High	46.603***	36.821***	66.915***	35.888**
	[3.117]	[2.586]	[4.025]	[2.444]
Lat	−15.259***	−17.900***	−13.104***	−16.867***
	[−5.876]	[−6.905]	[−4.139]	[−5.101]
Levg	52.630***	51.406***	49.536***	51.922***
	[3.114]	[2.972]	[2.763]	[2.767]
Prof	−80.459***	−77.547**	−111.942***	−60.698**
	[−3.281]	[−2.512]	[−13.389]	[−2.136]
Tang	−8.990	−1.048	−14.913	−18.455
	[−0.236]	[−0.029]	[−0.408]	[−0.533]
Zscore	−8.660*	−9.314*	−6.559*	−9.995**
	[−1.892]	[−1.935]	[−1.699]	[−2.253]
Secured	52.973***	55.553***	50.079***	54.406***
	[2.935]	[3.096]	[2.779]	[3.000]
LnMaturity	−0.425	−0.551	0.082	−0.463
	[−0.143]	[−0.178]	[0.029]	[−0.154]
LnLoanSize	−1.171	−1.141	−0.652	−1.073
	[−0.406]	[−0.404]	[−0.235]	[−0.354]
TermLoan	7.579	9.147	4.950	9.255
	[1.176]	[1.476]	[0.683]	[1.387]
Lfcov	−5.725	−5.516	−6.824*	−5.709
	[−1.373]	[−1.373]	[−1.711]	[−1.452]
Lnfcov	25.730	17.189	34.666*	21.298
	[1.364]	[0.833]	[1.891]	[0.926]
Rel_Dum	−18.305***	−17.128***	−20.240***	−18.575***
	[−3.317]	[−3.470]	[−4.064]	[−3.396]
Constant	295.211	328.931	252.710	329.631
	[.]	[.]	[.]	[.]
Loan purpose fixed effects	Yes	Yes	Yes	Yes
Credit rating fixed effects	Yes	Yes	Yes	Yes
Industry and year fixed effects	Yes	Yes	Yes	Yes
Observations	442	442	442	442
Adjusted R-square	0.765	0.760	0.774	0.758

Notes: This table presents the multi-variate regression results estimating the effects of *CPD* on the cost of debt for more and less politically sensitive firms. The dependent variable is all-in-spread drawn (*AISD*). The measures of *CPD* include the total political transparency percentage (*PERCENTAGE*), disclosure percentage (*PCT_DIS*), policy percentage (*PCT_POLICY*), and oversight percentage (*PCT_OVER*). *PS_High* is an indicator variable that equals 1 if a firm is more politically sensitive, and 0 otherwise. More politically sensitive firms are firms whose stock returns vary significantly with political uncertainty index (Baker et al. 2016). *PS_High* × *PERCENTAGE*, *PS_High* × *PCT_DIS*, *PS_High* × *PCT_POLICY*, and *PS_High* × *PCT_OVER* are the interaction terms between the *PS_High* and the four measures of *CPD*, respectively. Variable descriptions for all of the variables are provided in Appendix A. Standard errors are clustered at firm and year. *, **, and *** represent significance levels of 0.10, 0.05, and 0.01, respectively, using two-tailed tests. Robust and clustered t-statistics are provided in parentheses.

TABLE 5
Cross-sectional analysis: CEO chair, CPD, and cost of debt

VARIABLES	(1) *PERCENTAGE*	(2) *PCT_DIS*	(3) *PCT_POLICY*	(4) *PCT_OVER*
PERCENTAGE	−0.163***			
	[−3.042]			
CEO_CHAIR×PERCENTAGE	−0.285***			
	[−3.438]			
PCT_DIS		−0.140**		
		[−2.279]		
CEO_CHAIR×PCT_DIS		−0.165**		
		[−2.264]		
PCT_POLICY			−0.275***	
			[−4.139]	
CEO_CHAIR×PCT_POLICY			−0.258*	
			[−1.902]	
PCT_OVER				0.000
				[0.005]
CEO_CHAIR×PCT_OVER				−0.395***
				[−3.286]
CEO_CHAIR	13.524*	7.423	14.794	17.047
	[1.679]	[1.075]	[1.196]	[1.619]
Lat	−15.366***	−16.921***	−14.260***	−16.853***
	[−5.144]	[−5.584]	[−4.715]	[−3.206]
Levg	69.663***	62.816***	73.252***	66.823**
	[4.516]	[4.151]	[4.386]	[2.548]
Prof	−36.249	−27.189	−65.259***	−16.807
	[−1.407]	[−0.958]	[−3.395]	[−0.176]
Tang	−13.447	−4.220	−21.139	−24.426
	[−0.352]	[−0.114]	[−0.590]	[−0.839]
Zscore	−6.597	−7.301	−5.169	−7.869
	[−1.488]	[−1.641]	[−1.277]	[−1.196]
Secured	53.853***	54.977***	53.395***	53.770***
	[3.342]	[3.584]	[3.261]	[2.935]
LnMaturity	−0.379	−0.481	−0.017	0.004
	[−0.124]	[−0.160]	[−0.006]	[0.001]
LnLoanSize	−1.818	−2.155	−1.085	−1.804
	[−0.610]	[−0.715]	[−0.386]	[−0.575]
TermLoan	11.438*	11.578*	10.457	12.930
	[1.787]	[1.797]	[1.627]	[1.536]
Lfcov	−12.398***	−11.654***	−13.590***	−12.893
	[−3.222]	[−3.155]	[−3.882]	[−1.626]
Lnfcov	51.333***	44.607**	59.199***	50.247
	[3.018]	[2.489]	[4.123]	[1.180]

Rel_Dum	−14.132***	−12.798***	−17.248***	−14.501
	[−3.617]	[−3.217]	[−5.789]	[−1.369]
Constant	264.223	292.983***	233.196	276.974***
	[.]	[25.996]	[.]	[3.511]
Loan purpose fixed effects	Yes	Yes	Yes	Yes
Credit rating fixed effects	Yes	Yes	Yes	Yes
Industry and year fixed effects	Yes	Yes	Yes	Yes
Observations	452	452	452	452
Adjusted R-square	0.750	0.745	0.755	0.747

Notes: This table presents the multi-variate regression results estimating the effects of CPD on the cost of debt conditional on the duality of CEO chair (*CEO_Chair*). The dependent variable is all-in-spread drawn (*AISD*). The measures of CPD include the total political transparency percentage (*PERCENTAG*E), disclosure percentage (*PCT_DIS*), policy percentage (*PCT_POLICY*), and oversight percentage (*PCT_OVER*). *CEO_Chair* is an indicator variable that equals 1 if the CEO is also the chair of the board. *CEO_Chair* × *PERCENTAGE*, *CEO_Chair* × *PCT_DIS*, *CEO_Chair* × *PCT_POLICY*, and *CEO_Chair* × *PCT_OVER* are the interaction terms between the *CEO_Chair* and the four measures of firm political transparency, respectively. Variable descriptions for all of the variables are provided in Appendix A. Standard errors are clustered at firm and year. *, **, and *** represent significance levels of 0.10, 0.05, and 0.01, respectively, using two-tailed tests. Robust and clustered t-statistics are provided in parentheses.

TABLE 6
Cross-sectional analysis: Firms' information environment, CPD, and cost of debt

VARIABLES	(1) *PERCENTAGE*	(2) *PCT_DIS*	(3) *PCT_POLICY*	(4) *PCT_OVER*
PERCENTAGE	-0.197*** [-3.165]			
SML×PERCENTAGE	-0.374*** [-3.714]			
PCT_DIS		-0.169** [-2.063]		
SML×PCT_DIS		-0.251** [-2.060]		
PCT_POLICY			-0.239*** [-3.274]	
SML×PCT_POLICY			-0.478*** [-7.057]	
PCT_OVER				-0.123 [-1.303]
SML×PCT_OVER				-0.344** [-2.124]
SML	31.302*** [2.742]	25.362** [2.254]	45.622*** [3.515]	29.886*** [3.726]
Levg	70.608*** [6.598]	60.928*** [5.479]	63.491*** [6.685]	63.940** [2.204]
Prof	-36.314 [-1.621]	-21.056 [-0.794]	-80.625*** [-6.236]	-13.108 [-0.131]
Tang	7.004 [0.267]	3.034 [0.080]	-9.285 [-0.270]	-10.322 [-0.360]
Zscore×Levg	-6.025 [-1.378]	-6.615 [-1.601]	-5.084 [-1.340]	-7.306 [-1.108]
Secured	48.350*** [2.828]	50.655*** [3.128]	45.048*** [2.763]	49.124*** [2.599]
LnMaturity	1.033 [0.290]	0.899 [0.247]	0.859 [0.241]	1.223 [0.392]
LnLoanSize	-3.184 [-1.135]	-3.580 [-1.246]	-2.683 [-1.010]	-3.292 [-1.072]
TermLoan	9.927 [1.544]	11.097* [1.669]	8.612 [1.314]	11.358 [1.364]
Lfcov	-7.861** [-2.401]	-7.348** [-2.254]	-8.234*** [-2.669]	-6.904 [-0.876]
Lnfcov	53.815*** [3.249]	50.681*** [2.992]	56.287*** [4.164]	50.990 [1.274]
Rel_Dum	-14.254*** [-5.425]	-12.795*** [-3.960]	-15.404*** [-20.400]	-15.231 [-1.563]

Constant	124.497 [.]	127.494 [.]	114.525 [.]	122.030** [2.340]
Loan purpose fixed effects	Yes	Yes	Yes	Yes
Credit rating fixed effects	Yes	Yes	Yes	Yes
Industry and year fixed effects	Yes	Yes	Yes	Yes
Observations	452	452	452	452
Adjusted R-square	0.747	0.743	0.757	0.741

Notes: This table presents the multi-variate regression results estimating the effects of CPD on the cost of debt for large and small firms. The dependent variable is all-in-spread drawn (*AISD*). The measures of CPD include the total political transparency percentage (*PERCENTAGE*), disclosure percentage (*PCT_DIS*), policy percentage (*PCT_POLICY*), and oversight percentage (*PCT_OVER*). SML is an indicator variable that equals 1 if log(assets) is smaller than the sample median, and 0 otherwise. *SML* × *PERCENTAGE, SML* × *PCT_DIS, SML* × *PCT_POLICY,* and *SML* × *PCT_OVER* are the interaction terms between the *SML* and the four measures of CPD, respectively. Variable descriptions for all of the variables are provided in Appendix A. Standard errors are clustered at firm and year. *, **, and *** represent significance levels of 0.10, 0.05, and 0.01, respectively, using two-tailed tests. Robust and clustered t-statistics are provided in parentheses.

TABLE 7
Relations between CPD transparency, financial reporting quality, and non-financial disclosure quality
Panel A: Correlation of CPD transparency, financial reporting quality, and non-financial disclosure quality

	PERCENTAGE	*PCT_DIS*	*PCT_POLICY*	*PCT_OVER*
ESG	0.2158	0.2309	0.1967	0.1416
	(0.000)	(0.000)	(0.000)	(0.005)
AB_TACC	−0.1471	−0.1755	−0.0768	−0.1044
	(0.0257)	(0.008)	(0.246)	(0.114)

Panel B: Robustness tests: Controlling non-financial disclosure quality (ESGS)

VARIABLES	(1) *PERCENTAGE*	(2) *PCT_DIS*	(3) *PCT_POLICY*	(4) *PCT_OVER*
PERCENTAGE	−0.197***			
	[−2.602]			
PCT_DIS		−0.127		
		[−1.535]		
PCT_POLICY			−0.316***	
			[−3.808]	
PCT_OVER				−0.054
				[−0.634]
ESG	−0.172	−0.202	−0.106	−0.319
	[−0.578]	[−0.635]	[−0.456]	[−1.084]
Lat	−14.685**	−15.546***	−13.378**	−16.226***
	[−2.394]	[−2.621]	[−2.251]	[−2.604]
Levg	61.264**	57.368**	63.635**	53.469*
	[2.192]	[2.059]	[2.128]	[1.871]
Prof	−117.648***	−114.592***	−142.806***	−105.362***
	[−10.779]	[−7.031]	[−12.795]	[−4.005]
Tang	−12.033	−5.274	−21.389	−4.040
	[−0.288]	[−0.130]	[−0.555]	[−0.101]
Zscore	1.580	1.420	2.467	1.470
	[0.528]	[0.496]	[0.826]	[0.516]
Secured	40.707***	41.484***	39.723***	40.712***
	[2.940]	[3.005]	[2.783]	[3.271]
LnMaturity	3.527	3.598	3.563	3.829*
	[1.523]	[1.563]	[1.501]	[1.668]
LnLoanSize	−3.886	−3.908	−3.467	−3.515
	[−1.068]	[−1.101]	[−0.961]	[−0.967]
TermLoan	12.681	12.785	11.758	13.479
	[1.511]	[1.550]	[1.339]	[1.547]
Lfcov	−6.295	−5.958	−7.027	−5.350
	[−1.274]	[−1.214]	[−1.412]	[−0.963]
Lnfcov	50.047**	45.599**	58.320***	42.905*
	[2.480]	[2.293]	[3.075]	[1.689]
Rel_Dum	−13.314***	−12.175**	−15.495***	−12.723**
	[−2.761]	[−2.569]	[−4.085]	[−2.128]
Constant	206.145***	214.383***	185.399***	213.307***
	[4.352]	[4.621]	[5.716]	[4.554]
Loan purpose fixed effects	Yes	Yes	Yes	Yes
Credit rating fixed effects	Yes	Yes	Yes	Yes
Industry and year fixed effects	Yes	Yes	Yes	Yes
Observations	401	401	401	401
Adjusted R-square	0.778	0.777	0.782	0.776

Panel C: Robustness tests: Controlling for financial reporting quality

VARIABLES	(1) *PERCENTAGE*	(2) *PCT_DIS*	(3) *PCT_POLICY*	(4) *PCT_OVER*
PERCENTAGE	−0.228***			
	[−2.858]			
PCT_DIS		−0.196**		
		[−2.014]		
PCT_POLICY			−0.268***	
			[−10.752]	
PCT_OVER				−0.144***
				[−2.904]
AB_TACC	9.544	9.662	4.098	18.989
	[0.521]	[0.570]	[0.195]	[1.006]
Lat	−18.575***	−19.258***	−17.265***	−19.948***
	[−5.579]	[−5.528]	[−7.233]	[−7.360]
Levg	184.703***	182.022***	184.309***	186.828***
	[5.177]	[4.912]	[5.052]	[5.299]
Prof	−39.779	−35.878	−50.603	−44.892
	[−0.758]	[−0.695]	[−0.995]	[−0.850]
Tang	16.059	20.798	11.732	16.650
	[0.639]	[0.902]	[0.461]	[0.623]
Zscore	−12.368***	−12.158***	−12.995***	−13.508***
	[−3.425]	[−3.229]	[−3.372]	[−3.486]
Secured	72.389***	71.541***	72.844***	78.290***
	[7.507]	[6.511]	[11.157]	[7.574]
LnMaturity	1.484**	0.956	1.972***	2.011***
	[2.181]	[1.080]	[3.450]	[3.000]
LnLoanSize	1.131	0.964	1.454	0.960
	[0.327]	[0.283]	[0.418]	[0.272]
TermLoan	−7.612*	−7.628*	−7.815*	−7.666*
	[−1.730]	[−1.811]	[−1.750]	[−1.735]
Lfcov	−7.880	−7.002	−9.229*	−6.703
	[−1.281]	[−1.146]	[−1.651]	[−1.086]
Lnfcov	31.415	25.032	38.976	23.201
	[1.103]	[0.854]	[1.502]	[0.898]
Rel_Dum	−15.525**	−15.912**	−13.322**	−15.134**
	[−2.302]	[−2.355]	[−2.097]	[−2.124]
Constant	206.660***	224.928***	180.919***	230.862***
	[6.411]	[7.605]	[5.700]	[5.982]
Loan purpose fixed effects	Yes	Yes	Yes	Yes
Credit rating fixed effects	Yes	Yes	Yes	Yes
Industry and year fixed effects	Yes	Yes	Yes	Yes
Observations	185	185	185	185
Adjusted R-square	0.902	0.902	0.903	0.900

Notes: This table presents the effect of CPD transparency on the cost of debt after controlling for non-financial disclosure and financial reporting quality. Panel A presents the correlation analysis for the four measures of CPD transparency, and the measures of non-financial disclosure and financial reporting quality. Non-financial disclosure quality is measured by the average of the environmental disclosure score, social responsibility disclosure score, and governance disclosure score provided by Bloomberg (*ESG*). Financial reporting quality is measured by abnormal accruals based on the performance matched accrual model (Kothari et al., 2005). Panels B and C present the multi-variate regression results after controlling for non-financial disclosure quality (*ESG*) and financial reporting quality (*AB_TACC*), respectively. The dependent variable is all-in-spread drawn (AISD). The measures of CPD includes the total political transparency percentage, disclosure percentage, policy percentage, and oversight percentage. Variable descriptions for all of the variables are provided in Appendix A. *, **, and *** represent significance levels of 0.10, 0.05, and 0.01, respectively, using two-tailed tests. Robust and clustered t-statistics are provided in parentheses.

Table 8
Robustness tests: Removing firms in financial and utility industries

VARIABLES	(1) *PERCENTAGE*	(2) *PCT_DIS*	(3) *PCT_POLICY*	(4) *PCT_OVER*
PERCENTAGE	−0.420***			
	[−3.946]			
PCT_DIS		−0.308***		
		[−4.171]		
PCT_POLICY			−0.483***	
			[−3.207]	
PCT_OVER				−0.292**
				[−2.222]
Lat	−14.914**	−16.932***	−13.833***	−16.404***
	[−2.513]	[−3.376]	[−2.774]	[−2.613]
Levg	109.660***	104.552***	105.517***	106.388***
	[4.439]	[10.567]	[12.896]	[11.742]
Prof	−30.935	−23.022	−62.933*	−7.373
	[−0.311]	[−0.466]	[−1.716]	[−0.139]
Tang	12.043	21.130	6.597	10.642
	[0.431]	[0.901]	[0.240]	[0.384]
Zscore	−7.294	−7.948	−7.373	−8.384*
	[−1.041]	[−1.551]	[−1.508]	[−1.672]
Secured	65.473***	67.380***	64.787***	66.536***
	[5.528]	[7.169]	[5.818]	[6.479]
LnMaturity	0.744	0.489	1.480	0.942
	[0.221]	[0.115]	[0.355]	[0.222]
LnLoanSize	−2.380	−2.630	−1.968	−2.847
	[−0.690]	[−0.901]	[−0.707]	[−1.009]
TermLoan	16.725**	17.188***	15.050***	17.340***
	[2.092]	[3.335]	[3.244]	[3.304]
Lfcov	−14.147*	−13.159***	−15.414***	−14.112***
	[−1.668]	[−3.725]	[−4.531]	[−3.422]
Lnfcov	77.432	69.879	82.051*	71.482
	[1.586]	[1.589]	[1.908]	[1.439]
Rel_Dum	−27.796***	−25.975***	−28.598***	−28.366***
	[−3.282]	[−25.746]	[−10.257]	[−6.172]
Constant	246.124***	203.674**	227.812***	264.953***
	[2.789]	[2.532]	[4.635]	[3.177]
Loan purpose fixed effects	Yes	Yes	Yes	Yes
Credit rating fixed effects	Yes	Yes	Yes	Yes
Industry and year fixed effects	Yes	Yes	Yes	Yes
Observations	355	355	355	355
Adjusted R-square	0.784	0.781	0.790	0.778

Notes: This table presents the multi-variate regression results estimating the effects of CPD on the cost of debt for the sample excluding financial and utility firms. The dependent variable is all-in-spread drawn (*AISD*). The measures of CPD include the total political transparency percentage (*PERCENTAGE*), disclosure percentage (*PCT_DIS*), policy percentage (*PCT_POLICY*), and oversight percentage (*PCT_OVER*). Variable descriptions for all of the variables are provided in Appendix A. Standard errors are clustered at firm and year with robust and clustered t-statistics provided in parentheses. *, **, and *** represent significance levels of 0.10, 0.05, and 0.01, respectively, using two-tailed tests.