

# A Lobbying Approach to Evaluating the Sarbanes-Oxley Act of 2002\*

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## Abstract

This paper evaluates the net benefits of the Sarbanes-Oxley Act of 2002 (SOX) for shareholders by studying the lobbying behavior of investors and corporate insiders to affect the final implemented rules under the Act. We document that investors and investor groups lobbied overwhelmingly in favor of strict implementation of the provisions of SOX, while the majority of corporate insiders and business groups lobbied against strict implementation of the Act's provisions. To analyze the effects of the law on stock prices, we compare the returns of the firms likely to be more affected by SOX with those less affected. We identify the firms most affected by the law as those whose insiders lobbied against the provisions of SOX. We find that cumulative returns during the four and a half months leading up to passage of SOX were approximately 10 percent *higher* for corporations whose insiders lobbied *against* one or more of the SOX disclosure-related provisions than for non-lobbying firms with similar size, book-to-market and industry characteristics. These results are consistent with investors' positive perception of the effects of the law as expressed by their lobbying efforts. Analysis of returns and operating performance in the post-passage period of implementation indicates that investors' positive expectations with regards to the effects of the law were warranted for the enhanced disclosure provisions of SOX.

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Following the Enron/Arthur Andersen scandal in late 2001, the U.S. Congress came under increasing pressure to pass legislation that would make it more difficult and costly for corporate insiders to misrepresent company performance and divert resources for personal gain. Bills were introduced in the House by Representative Michael Oxley on February 13, 2002, and in the Senate by Senator Paul Sarbanes on May 8, 2002. The final bill, the Sarbanes-Oxley Act of 2002, was passed in the House and Senate on July 25, 2002.

There are two main competing views about the likely impact of the Sarbanes-Oxley Act (SOX) on shareholders. Proponents of the Act argue that it will lead to improved disclosure and corporate governance, thereby reducing misconduct of insiders, and that these benefits will outweigh the costs of compliance. Opponents argue either that SOX will be ineffective in preventing corporate wrongdoing and/or that any benefits of SOX will not be large enough to outweigh the compliance costs associated with it.

In this paper, we evaluate the net benefits of the Sarbanes-Oxley Act of 2002 for corporate shareholders. The central challenge to distinguishing between the two main views regarding the effect of SOX is the lack of a control group of publicly traded firms unaffected by the legislation. We employ two approaches in an attempt to circumvent the lack of a control group of comparable firms unaffected by SOX. Our methodology follows from the procedural process used in the implementation of the SOX legislation.

Following the passage of SOX in 2002, Congress delegated the drafting and implementation of the principles outlined by SOX to the Securities and Exchange Commission (SEC). The various sections of SOX were divided into separate rules by the SEC, which then solicited public comments regarding its proposing rule releases, prior to drafting the final adopting releases. Letters to the SEC commenting on the proposed rule releases were made publicly available on the SEC web site and through its public reference office.

Following the main compliance-related titles of SOX, we classify the rules on which the SEC solicited comments into groups, focusing on three major sets of rules: provisions related to enhanced financial disclosure, provisions related to corporate responsibility, and provisions related to auditor independence. Our first approach to evaluating the effect of SOX on shareholder value is to classify comment letters submitted to the SEC by individual investors and investor groups. We document that based on their letters to the SEC, individual investors were overwhelmingly in favor of strict implementation of SOX, across all three categories of proposed rules. Importantly, lobbying by

investor groups such as pension funds and labor unions, who presumably are more sophisticated than individual shareholders, was equally supportive. These findings allow us to speak to the perceived value of SOX for shareholders. To the extent that investors were sufficiently informed about SOX, this allows us to circumvent the lack of a control group of firms unaffected by SOX. The fact that, based on their comment letters, individual investors and investor groups were strongly in favor of SOX stands in stark contradiction to the conclusions of studies such as Zhang (2005), who argue that shareholder reactions to SOX were unfavorable based on the price movement of the market as a whole.

To provide additional evidence on the value of SOX, our second approach utilizes the comment letters from corporate insiders lobbying the SEC with regards to implementation of SOX's provisions. Our reading of letters to the SEC by corporate insiders reveals that an overwhelming majority of insiders in lobbying companies opposed strict implementation of SOX, and argued strongly for delays, exemptions and loopholes in its implementation. While lobbying by investors in favor of SOX is useful for distinguishing between the improved disclosure and corporate governance and the costly compliance views of SOX, lobbying by insiders is not informative for this purpose in and of itself. Corporate insiders may lobby against strict implementation of SOX both if SOX was expected to succeed in improving disclosure and governance or if the dominant effect of SOX was expected to be its high compliance costs.<sup>1</sup> However, lobbying by corporate insiders is still useful in that lobbying by an insider against strict implementation of SOX can be used as a proxy to identify companies more likely to be affected by the legislation. Under the improved disclosure and governance view, these more affected firms will be those for whom the governance gain will be greatest, thus, if SOX provides a net benefit in the form of improved disclosure and corporate governance for shareholders, companies that lobbied against strict implementation of SOX should have higher cumulative returns than otherwise similar non-lobbying companies in the period leading up to the passage of SOX, as the market adjusts its expectations of future cash flows for these companies relative to their matched, less-affected peers. Conversely, under the compliance cost view, where SOX is detrimental to shareholders because it imposes costs that outweigh any associated governance gains, the more affected companies will be those for whom the net costs are highest, and thus we would expect lobbyists to experience lower cumulative returns than non-lobbyers.

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<sup>1</sup>Under the improved disclosure and governance view, insiders lobby against strict implementation due to SOX's effect of reducing insiders' ability to divert resources to themselves. Under the compliance cost view, insiders may lobby against SOX either because they choose to lobby in the interest of company shareholders, or because they anticipate a possible reduction in diversion of resources.

One aspect of our research design, important for interpreting our findings, is that lobbying of the SEC with regards to implementation of SOX primarily occurred after the passage of the Act itself. For our identification strategy to be valid, it must be the case that the market could predict which firms would be most affected (and hence, which insiders would lobby against strict implementation of SOX) based on ex-ante observable characteristics of firms. To validate our empirical strategy, we provide direct evidence that lobbying was to some extent predictable based on variables publicly observable at the start of our sample. Furthermore, an event study of abnormal returns observed around the date of submission of a comment letter by a given company indicates that there was no discernable market reaction to the submission of the letter, suggesting that market participants were not surprised to see which firms lobbied.

Our portfolio analysis of returns reveals that during the period from February to July of 2002 leading up to passage of SOX, cumulative returns were approximately 10 percentage points higher for corporations whose insiders lobbied against one or more of the SOX 'Enhanced Disclosure' provisions than for non-lobbying firms with similar size, book-to-market and industry characteristics. Similarly, we find higher cumulative returns for corporations whose insiders lobbied against one or more of the SOX 'Corporate Responsibility' provisions and for corporations whose insiders lobbied against one or more of the SOX 'Auditor Independence' provisions than for comparable non-lobbying firms. However, many firms who lobbied against strict implementation of the 'Corporate Responsibility' or 'Auditor Independence' provisions also lobbied against strict implementation of one or more of the 'Enhanced Disclosure' provisions. We therefore proceed to estimate the separate abnormal returns associated with each of the three categories by running firm-level regressions. The results from our firm-level models imply a total abnormal excess return of approximately 10 percent during the period leading up to the passage of SOX for firms lobbying against the 'Enhanced Disclosure' provisions, but a total abnormal excess return of only 3 percent and 1 percent respectively for firms lobbying against 'Corporate Responsibility' or 'Auditor Independence' provisions, respectively. These relative returns suggest that while investors did not disapprove of the 'Corporate Responsibility' or 'Auditor Independence' provisions, the market expected SOX to mainly benefit the firms most affected by provisions related to 'Enhanced Disclosure', rather than those affected primarily by corporate responsibility provisions or auditor independence provisions.

In the second part of our analysis, we focus on the returns and operating performance of lobbying and non-lobbying firms during the period after the passage of SOX. If investors' positive expect-

tations regarding the overall effect of SOX were warranted, one would not expect any differences between the returns of lobbying and non-lobbying firms in the post-passage period; furthermore, the operating performance of lobbyists should improve relative to the operating performance of non-lobbyists. If, on the other hand, shareholders gradually became aware that the measures introduced by SOX did not in fact result in higher earnings, due, for example, either to a watering down of the rules during implementation or to high compliance costs, then one should observe abnormal negative returns for lobbying firms relative to non-lobbyists in the period following SOX passage and until investor expectations settle at a new, less optimistic level. In that scenario, one would not expect to see improvements in operating performance of lobbyists relative to non-lobbyists. On the contrary, one may even see a deterioration in the relative operating performance of lobbyists if compliance costs were higher than expected, and this may have been the case for lobbyists more so than for non-lobbying firms.

Our analysis of returns in the post-passage period indicate that the returns for firms who lobbied against an 'Enhanced Disclosure' rule were similar to the returns for their non-lobbying comparison group of firms, and thus that the increase in relative stock price experienced by lobbying firms did not tend to reverse during the post-passage period. Furthermore, a preliminary analysis of operating performance shows that lobbying firms experienced improvements in operating performance relative to non-lobbying firms. Firms that lobbied against an 'Enhanced Disclosure' rule experienced an improvement in operating income relative to initial market value of equity of about 5 percentage points, consistent with the returns results for these firms, suggesting that investors' positive expectations about the effect of SOX were warranted in the case of the 'Enhanced Disclosure' rules.

In sum, our study documents, first, that investors expected SOX to more closely align interests of insiders and shareholders; second, that (relative) returns during the period leading up to SOX passage are consistent with the views of investors; and third, that investors' positive expectations may have been warranted, based on returns and operating performance in the post-SOX period. Our results indicate that, in the eyes of public company shareholders, the most important and effective provisions in SOX were the 'Enhanced Disclosure' provisions, rather than the provisions related to 'Corporate Responsibility' and 'Auditor Independence'.

An obvious shortcoming of a research design which compares more affected firms to less affected firms, without have a comparable group of firms unaffected by the legislation studied, is that it

does not speak directly to the overall effect of SOX on the public equity market. We can only say that considering the full period from when serious discussions about the legislation first started in week 7 of 2002 to the end of 2004 (well into the implementation phase of SOX), the stocks of more affected firms (proxied for by lobbying firms) outperformed those of less affected firms (proxied for by non-lobbying firms). We cannot unambiguously say that the net benefit of SOX for either group is positive.

We argue, however, that our analysis of comment letters from investors and investor groups indicates that shareholders expect SOX to be value increasing on average across publicly traded firms. To our knowledge, shareholder support for SOX has not diminished since the period covered by the letters we analyze. Furthermore, based on industry estimates of SOX compliance costs and the relative performance of lobbyists and non-lobbyists, we suggest that the group of companies who lobbied against an enhanced disclosure provision of SOX may have experienced an overall net benefit as high as \$185 billion, and that in the presence of even a small gross benefit of SOX to non-lobbying firms, gains for the overall group of public shareholders may be substantial.

Additionally, an important caveat to our analysis is that we are not able to speak to the welfare effects of SOX, but rather only to the law's effects on shareholders. We cannot rule out that insiders lost an amount equal to or greater than what outside investors gained. We note, however, that if misconduct by insiders is distortionary, then our evidence is consistent with an overall positive welfare effect.<sup>2</sup>

Our study is related to an emerging literature attempting to evaluate the effects of SOX. An insightful review of this literature, which has not produced a general consensus on the effects or value of the Act, is presented in Coates (2006). Zhang (2005) examines the reaction of the overall U.S. stock market to legislative events leading to the passage of the Act. While Zhang (2005) finds significantly negative returns around legislative events leading to the passage of SOX, these returns might be due to other, confounding events unrelated to SOX. Rezaee and Jain (2003) also study the aggregate market reaction to SOX, reaching the opposite conclusion of Zhang (2005).

As in our paper, other studies seek to circumvent the lack of a control group of unaffected firms by use of alternative approaches. Cohen, Dey and Lys (2005) evaluate the impact of SOX by examining changes in earnings management behavior and in the informativeness of earnings announcements of firms around the passage of the Act. They find a decline in earnings management

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<sup>2</sup>Examples of distortionary behavior by insiders include empire building (negative NPV expansion projects) and perquisite consumption where the cost to the firm exceeds the private benefit to the insider.

activity following the passage of SOX. Engel, Hayes and Wang (2004) study firms' going-private decisions and find a modest increase in the number of firms going private after the passage of SOX. The paper closest to ours in approach is Chhaochharia and Grinstein (2005), who study the announcement effect of SOX on firm value. To overcome the lack of an unaffected control group, they sort firms into groups most and least compliant with certain proposed SOX provisions in the pre-SOX period. Based on a comparison of these two groups, their study finds a positive value effect associated with SOX for large firms, whereby firms that need to make the most changes in order to comply with the new rules outperform firms that require fewer changes over the announcement period. Conversely, they find a negative effect for small firms. While Chhaochharia and Grinstein (2005) study the perceived value of SOX for firms most affected by certain specific provisions of the Act, our approach allows us to expand on their work by examining shareholders' views regarding the full spectrum of SOX's provisions, and to separate the perceived effects of the Act as passed in Congress from the net effects resulting from the actual implementation of those rules.

Our paper is also related to a growing literature that uses the lobbying activities of corporations to examine the impact of regulation. King and O'Keefe (1986) examine the relationship between corporate lobbying and trading activities of corporate insiders surrounding proposed accounting standards that require firms to expense oil and gas exploration expenditures associated with dry holes. A more closely related study is that of Lo (2003), who examines the economic consequences of the 1992 revision of executive compensation disclosure rules using a lobbying approach quite similar to that employed in this study. Lo (2003) finds, in support of the value of increased disclosure, that corporations who lobbied the SEC *against* the proposed regulation had *positive* excess stock returns of about 6% over the 8-month period between the SEC's announcement that it would be pursuing reform and the adoption of the proposed regulation. In addition to addressing a different reform, a key difference between Lo (2003) and this study is that we study not only the opinions of corporations who lobby the SEC, but also the views of non-investor groups and of individual investors and investor groups.

The remainder of this paper is organized as follows. Section I presents an overview of the Sarbanes-Oxley Act, the time line of its adoption, and the role of lobbying in the design of the resulting rules. Section II details our hypotheses and research method. Section III presents and discusses our empirical findings. Section IV concludes.

## **I. The Sarbanes-Oxley Act Of 2002**

### **A. The Legislative Time-Line**

The collapse of Enron in October 2001, followed by the subsequent exposure of a string of accounting and governance scandals at Qwest Communications, Global Crossing, Worldcom, Adelphia and Tyco in the spring of 2002, triggered a flurry of legislative proposals to reform corporate business practices and improve governance and accounting systems for publicly traded companies.

The Sarbanes-Oxley Act resulted from the combination of reform bills introduced by Senator Paul Sarbanes, Democrat of Maryland, and Representative Michael Oxley, Republican of Ohio, in the Senate and House, respectively. Representative Oxley's reform bill was first introduced in the House on February 13th, 2002. Oxley's bill was passed in committee on April 16th, 2002, and was subsequently passed in the House on April 24th, 2002. In May of 2002, the Sarbanes reform bill was circulated in the Senate Banking Committee, which passed the bill on June 18th, 2002. The full Senate began debate on Sarbanes' bill on July 8th 2002, and passed the bill with overwhelming support on July 15th, 2002. On July 19th, 2002, the House and Senate formed a conference committee and began negotiations to merge the two bills. The final legislative bill, to be known as the Sarbanes-Oxley Act of 2002, was passed in Congress on July 25th, 2002, and was signed into law by the President on July 30th of that year.

SOX directed the SEC to immediately begin rule-making activities, and the SEC commenced such action in late August 2002. SOX-directed rule making activities continued throughout 2003 and into the beginning of 2004. The major rule-making activities were completed by June 2004.

### **B. The Content of the Act**

The Sarbanes-Oxley Act established the Public Company Accounting Oversight Board (PCAOB) and laid out new rules for and restrictions on corporations, corporate directors, auditors and other corporate entities. The Act is arranged into eleven titles.

The first four titles of the Act are the most relevant for issues of public company compliance. Title I of the Act establishes the PCAOB, which is charged with overseeing and registering public accounting firms and establishing standards related to auditing and internal controls. Title II of the Act covers issues related to auditor independence, and places restrictions on public accounting firms with regards to the provision of non-auditing services, as well as mandating periodic rotation of the coordinating and reviewing auditing partners. Title III of the Act deals with corporate re-

sponsibilities, including the independence of the auditing committee, improper influence on conduct of audits, executive certification of financial reports, penalties related to financial restatements, and rules of professional responsibility for attorneys. Title IV of the Act deals with enhanced financial disclosure, including disclosures in periodic reports, enhanced conflict of interest provisions, disclosure of transactions involving management or principal stockholders, the disclosure of the existence of an audit committee financial expert, and the much-discussed management assessment of internal controls.

The remaining titles of the Act primarily deal with issues unrelated to compliance by public firms, or set out criminal penalties and as such were (with two exceptions noted below) not subject to interpretation and implementation by the SEC. Title V of the Act deals with analyst conflicts of interest, Title VI deals with SEC resources and authority, and Title VII with studies and reports. Title VIII of the act deals with corporate and criminal fraud accountability, and Title IX with white collar crime penalty enhancements. Title X deals with the signing of corporate tax returns by chief executive officers, and Title XI with definitions of corporate fraud and accountability. Of these remaining titles only Title VIII, section 802, on criminal penalties for altering documents and Title IX, Section 906, on corporate responsibility for financial reports generated SEC rule-making. We group SEC rules related to Sections 802 and 906 with those related to Title III since they cover similar topics. Due to the SEC's lack of rule-making activities with regards to Title V, VI, VII, X and XI, we do not deal directly with these Titles of the Act.

We classify the rule-making activities of the SEC with regards to Titles I through IV of SOX into three broad categories. Rulemaking activities related to auditor independence, Title II of SOX, are classified as 'Auditor Independence' rules. Rulemaking activities related to corporate responsibilities, Title III of SOX, are classified as 'Corporate Responsibility' rules. Rulemaking related to issues of enhanced financial disclosure and the PCAOB, Titles IV and I of SOX, are classified as 'Enhanced Financial Disclosure' rules. We include Title I, which establishes the PCAOB, in the 'Enhanced Disclosure' rules category due to the close overlap between the PCAOB's responsibilities and rulemaking and the disclosure items mandated in Title IV. Indeed, a significant part of the PCAOB's purpose is to determine and regulate the standards for the enhanced disclosures mandated by Title IV.

In conjunction with the federal legislation, the major stock exchanges produced their own governance-related listing requirements. In February of 2002, the SEC called on the major stock

exchanges to review their governance requirements. NYSE’s and NASD’s boards adopted governance proposals and submitted them to the SEC for approval. The SEC solicited public comment on these proposals, and upon reviewing the comments, approved the NYSE and NASD proposals with some modifications. We include SEC rule-making related to the governance and listing standards of the NYSE and NASDAQ exchanges in the ‘Corporate Responsibilities’ category.

Additionally, contemporaneously with SOX rulemaking, the SEC issued a number of proposed rules on disclosure related issues which were either adopted or replaced by a SOX mandated rule. Due to the topics of these rules, they are included in the ‘Enhanced Financial Disclosure’ category. In the fall of 2003, the SEC proposed one further rule related to corporate responsibility, which was not part of SOX, and which eventually was not implemented. This rule relates to nominations of directors by security holders. We tabulate letters for this rule in Appendix A, but subsequently leave out firms that lobbied for or against this rule from our sets of lobbying and non-lobbying firms since the rule was not implemented.

### **C. The Role of Lobbying in the Design of the Rules**

Section 3A of the Sarbanes-Oxley Act grants authority to the Securities and Exchange Commission to “promulgate such rules and regulations, as may be necessary or appropriate in the public interest or for the protection of investors, and in furtherance of this Act.” The SEC started rulemaking activities in August 2002. The rulemaking activities directed by SOX continued into 2003 and 2004.

After the passage of SOX, the relevant sections of each title were broken down and drafted in a proposing release, which was then circulated by the SEC for public comment. At the end of the comment period, the SEC drafted and approved a final adopting release for each rule. In Appendix A we classify and briefly describe all of the SOX-related rules proposed by the SEC. We report the date of the proposing release, the date of the adopting release, the related SOX section, and whether the rule was adopted with or without amendments and further restrictions.<sup>3</sup>

For each of the proposed rules, the SEC solicited public comments that were to be submitted to the SEC after the proposing release date by a specific deadline prior to the adopting release date. Comment letters submitted to the SEC by electronic means are made available to the public on

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<sup>3</sup>Three of the proposing releases that we list as releases generated by SOX were issued before the actual passage of the law. These are cases where the content of the SEC’s proposed rule subsequently was mandated by SOX and adopted as such, or where the SEC’s proposed rule was augmented by a subsequent release under SOX and adopted as such.

the SEC website. Comment letters submitted in paper form were made available to us by request through the SEC public reference section. In Section III, we describe in detail the content of the letters submitted to the SEC.

The major event window we employ to understand the perceived value of SOX is the time period leading to the approval of the Sarbanes-Oxley Act. Our event window starts on February 8, 2002, and ends on July 26, 2002. The first week of our event window leading up to SOX passage is thus the week that includes February 13, 2002, when the SEC announced that it intended to propose several rules designed to improve disclosure and governance. The last week of the window includes July 25, 2002, when Congress passed the law.<sup>4</sup> Because most of the rule making activity is concentrated after the passage of the Act (after July 25th, 2002), the event window allows us to separate the perceived effect of the law from the information potentially generated by the submission of comments to the SEC.

To understand the effects of SOX as implemented, as opposed the perceived effects of the bill as passed by Congress, we also examine the period following the passage of the Act, from July 26th, 2002, to the end of 2004. By examining returns for lobbying and non-lobbying firms in the post-passage period, we can assess the net effect of the final SOX rules, given the strictness and effectiveness of the implementation, and the costs of compliance associated with such.

## II. Hypotheses and Research Method

There are two competing views of the likely impact of SOX. The view on which Congress based the act is that SOX would improve disclosure and governance, thereby decreasing misconduct by corporate insiders and increasing value for shareholders. Under this positive view of the act we would expect the following:

1. Lobbying: Shareholders should support SOX, while corporate insiders should oppose it.
2. Returns during the period leading up to passage of SOX: In the cross-section of firms, returns should be higher for firms with the largest required improvements in disclosure and governance, controlling for differences in compliance costs.<sup>5</sup>

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<sup>4</sup>While the president only signed the law on July 30, 2002, presidential approval was viewed as a foregone conclusion once the Act was passed in Congress.

<sup>5</sup>As the probability of legislation went from zero to one, the price of a given company should gradually move upward from  $P$  to  $P + \Delta P_{sox}$  where  $\Delta P_{sox}$  is the present value of the increase in dividends due to SOX. If  $\frac{\Delta P_{sox}}{P}$  differs in the cross-section, firms with large values will be observed to have abnormally good returns over this period.

3. Operating performance after SOX relative to pre-SOX: In the cross-section of firms, operating performance should improve for firms with the largest impact of increased disclosure and governance, relative to firms less affected by SOX.

The improved disclosure and governance view of the act also predicts that, on average, across firms, returns during the period leading up to passage should be abnormally positive (relative to a set of firms with no news about disclosure and governance), and average operating performance should improve in the post-SOX period. Given the lack of a control group of (comparable US) firms not impacted by SOX, these additional predictions are impossible to test, as they cannot be distinguished from aggregate shocks unrelated to SOX.

The alternative view of SOX is that the main impact of SOX would be to impose large compliance costs on firms with a negative net effect of the act on shareholder value. This view is based on the prior that SOX would be ineffective in diminishing any misconduct, and that compliance costs would be sufficiently large to outweigh any benefits. Proponents of this view would argue that private markets already lead to the shareholder value maximizing disclosure and governance structure, and that government interference leads to sub-optimally large amounts of resources being spent on disclosure and governance issues. Under the compliance cost view, one would expect the following:

1. Lobbying: Shareholders should oppose SOX. Corporate insiders should either oppose it (if they are acting on behalf of shareholders or if SOX has some ability to reduce insider misconduct), or be indifferent to it (if SOX is ineffective in reducing insider misconduct).
2. Returns during the period leading up to passage of SOX: In the cross-section of firms, returns should be lower for firms with the highest compliance costs, net of any benefits of SOX.
3. Operating performance after SOX relative to pre-SOX: In the cross-section of firms, operating performance should diminish most for those firms with the highest compliance costs, either via the direct effect of the costs or via indirect effects on firm competitiveness due to suboptimal disclosure and/or governance.

The compliance cost view also has predictions about the average effect of SOX across firms. Returns during the period leading up to passage should be abnormally negative (relative to a set of firms with no news about disclosure and governance), and operating performance should be worse

in the post-SOX period. Once again, given the lack of a control group of firms not impacted by SOX, these predictions are impossible to test.

From the above, it is clear that studying lobbying behavior is informative about the average effect (across companies) of SOX on shareholders. The views of shareholders are particularly informative, while lobbying by corporate insiders against SOX contains less *direct* evidence about SOX's average effect on shareholders, since insiders should oppose SOX under both the improved disclosure and governance view and the compliance cost view. Lobbying by insiders is however still useful for distinguishing between the two views of SOX, under the assumption that insiders are more likely to lobby in firms more affected (positively or negatively) by SOX. Under this assumption, firms can be split into groups based on whether the insiders lobbied against SOX or not, and this split can be used to test the cross-sectional predictions regarding returns during the period leading up to passage of SOX and operating performance after the passage of SOX relative to the pre-SOX period.

One aspect of our research design is important for interpreting our findings. The majority of lobbying occurs after the passage of SOX in congress on July 25th, 2002. Our approach to testing the predictions for stock returns during the period leading up to passage will therefore only be powerful if shareholders were aware which types of firms are likely to lobby. To validate our identification strategy, we document that (a) lobbying is to some extent predictable based on variables known at the start of our sample, and (b) a firm level event study reveals no abnormal returns for lobbying firms around the date of submission of a letter to the SEC, suggesting that lobbying does not come as a surprise to the market. These findings support our research design and the interpretability of our findings.

### **III. Results**

#### **A. Opinions of Letter Writers**

The opinions of commenters are tabulated in Table I. Overall, our study is based on 2610 letters. Panel A shows how the letters are distributed across various types of letter writers. Of the 2610 letters, 843 are from corporations (or more precisely, from corporate managers or directors). 253 are from non-investor groups such as the Business Roundtable and the American Society of Corporate Secretaries. 226 of the letters are from investor groups, typically pension funds (including union pension funds), and 542 are from individuals. The remaining 747 letters are from accountants

(individuals and groups), lawyers (individuals and groups), academics, or others (mainly church groups and governments). Around 92 percent of the letters were submitted after July 25th, 2002, the date of the approval of the Act, with 34 percent submitted in the remainder of 2002, 47 percent submitted in 2003 and 10 percent submitted in 2004.

We classify the letters into three categories. Letters classified as “Positive” are those who favored the rule commented on, or who called for stronger measures than those stated in the SEC’s proposing release. Letters classified as “Negative” are those who opposed the rule commented on. The last category, “Neutral”, is used for letters which commented on several of the sub-provisions in a particular proposing release and where the commenter was positive on some sub-provisions and negative on others. A small number of letters which were difficult to classify are also included in the neutral category.

The top panel of Table I shows for each type of commenter, and across all rules, the total number and percentage of positive letters, neutral letters, and negative letters. It is clear that individuals and investor groups were overwhelmingly in favor of the SOX provisions. 79 percent of letters from individuals and 82 percent of letters from investor groups were in favor of the rule commented on. An important feature of comment letters from individual and investor groups is that the opinions expressed are not specific to a particular firm. In other words, the letters most likely state the letter writer’s view of the average effect of the particular provision across stocks, as opposed to its effect on an individual firm. Of course, it is possible that some individuals may be motivated by particularly poor disclosure/governance for a particular firm whose stock they own. However, since the provisions of SOX apply to all publicly traded firms, it seems fair to consider opinions expressed as views about the total set of stocks the investor/investor group holds or intends to hold in the future. Under this assumption, the positive views expressed by the vast majority of individual investors and investor groups provide support for the improved disclosure and governance view of SOX.

The remainder of Table I tabulates opinions by the rule and major rule category commented on. We first present results for the major rule category ‘Enhanced Financial Disclosure and PCAOB’ (SOX Title IV and I)<sup>6</sup>, then turn to the results for ‘Corporate Responsibility’ (SOX Title III) and last the results for ‘Auditor Independence’ (SOX Title II). The ‘Auditor Independence’ rule generated much fewer comments, mainly from accountants and accounting firms.

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<sup>6</sup>For brevity we will refer to this category as ‘Enhanced Disclosure’ in what follows.

Approximately 80 percent of both individual investors and investor groups write in favor of the 'Enhanced Disclosure' rule they are commenting on, with similar results for individual investors and investor groups that comment on a 'Corporate Responsibility' rule. Investors thus appear to view both the disclosure and governance provisions of SOX as being value increasing, even after any compliance costs borne by shareholders.

The opinions of corporations and of non-investor groups contrast starkly with those of investors. Across all rules, 78 percent of letters written by corporations (corporate managers or directors) and 74 percent of letters written by non-investor groups argue against the rule they commented on. Roughly similar percentages of letters from corporations and non-investor groups express negative views about the rules in all three individual categories of SOX provisions.

Since both the improved disclosure and governance hypothesis and the compliance cost hypothesis predict that insiders should lobby against SOX, alternative theories are required to explain the 14 percent of corporations and 13 percent of non-investor groups who lobbied in favor of the rule commented on. At least one CEO of a large publicly traded firm stated that he was in favor of SOX because compliance costs were disproportionately large for smaller firms and therefore put these at a competitive disadvantage. An alternative story for positive lobbying by a minority of corporations and non-investor groups is that these CEOs acted on behalf of shareholders and thus expressed views in line with those of the majority of individuals and investor groups.

For data availability reasons, our subsequent analysis focuses on publicly traded corporations. A given letter may be signed by managers or directors of multiple companies. 71 percent of the 842 letters from corporations are signed by at least one manager/director from a publicly traded company. Letters that represent insiders of publicly traded firms are even more likely to express negative views about the rule commented on. 88 percent of such letters express negative views, compared to 47 percent for letters representing a non-publicly traded firm.

A given company's managers or directors may be signatories to multiple letters and a total of 384 publicly traded firms are represented among the corporate letters. To ease the interpretation of our results, in our groups of lobbying firms below we omit letters from corporations expressing neutral or positive opinions, as there are too few such letters to allow a separate analysis of these firms.<sup>7</sup> Of the 384 publicly traded firms that are represented among the corporate letters, 280 firms are thus classified as lobbying against 'Enhanced Disclosure' and/or 'Corporate Responsibility', and/or

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<sup>7</sup>If a firm submits comments on several rules within a major rule category (i.e. several rules within 'Enhanced Disclosure') we classify them as lobbying against this major rule category only if all submitted comments are negative.

'Auditor Independence'.<sup>8</sup>

With regards to the other types of letter writers, the majority of accountants and lawyers argue against the rules they commented on, while opinions of academics and others were more mixed. The negative views of accountants and lawyers often refer to cases where the letter writer points out practical complexities of the rule commented on, or for auditors lobby against regulation that restricted the advisory role of auditing firms.

## **B. Predictability Of Lobbying By Corporate Insiders**

Since most lobbying took place after the passage of SOX, our research design implicitly assumes that lobbying is, at least to some extent, predictable by investors. If not, we would not expect to observe different returns between lobbying firms and matched non-lobbying firms during the period leading up to passage of SOX. The fact that we do find different returns between the two groups by itself provides evidence that this assumption is reasonable.

We now provide evidence to show that: (a) lobbying is to some extent predictable based on variables known at the start of our sample, (b) a firm level event study reveals no abnormal returns for lobbying firms around the date of submission of a letter to the SEC, suggesting that lobbying does not come as a surprise to the market.

### **B.1. Probit Models of Lobbying**

First, we show that it is possible to predict (with a somewhat reasonable  $R^2$ ) which firms will lobby based on firm characteristics at the start of our sample. We run probit regressions where the dependent variable is an indicator variable taking the value of one if the firm lobbied, and zero otherwise. For brevity, we focus on firms lobbying against an 'Enhanced Disclosure' rule. In addition to firm size, as measured by the log of market capitalization at the end of week 6 of 2002, and the book-to-market equity ratio on the same date, we include a variety of variables that may predict lobbying.

Firms with more entrenched management may be more affected by SOX and may therefore be more likely to lobby. To capture this we include the governance index of Gompers, Ishii and Metrick (2002), as measure of managerial entrenchment. Higher values of this index indicate more managerial entrenchment. Similarly, firms with more resources for insiders to expropriate

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<sup>8</sup>The difference between the 384 and the 280 firms is driven by firms with neutral/positive letters and by the firms who only comment on the SEC's proposed rule on Security Holder Director Nominations discussed above.

may be more likely to lobby. Following Bloom and Van Reenen (2006), we construct measures of how competitive a firms' business environment is. We employ both a firm level measure and an industry level measure. The industry level measure, which is called a Lerner competition index, is the industry wide average of  $(1 - \text{net income}/\text{sales})$  calculated at the 3-digit SIC code level and excluding the firm itself. Our firm level equivalent of this index is simply  $1 - \text{net income}/\text{sales}$  for the firm. Net income and sales data are for the fiscal year ending in 2000.<sup>9</sup> Firms that have a political action committee (PAC) may tend to be involved in all types of political and lobbying activities. We therefore include an indicator variable equal to one if the firm has a political action committee which was registered with the Federal Election Commission at some point during the period 1999-2000. Similarly, evidence of past lobbying may be indicative of future lobbying. We include an indicator variable equal to one if the firm lobbied the SEC in regards to the 1992 compensation reform analyzed by Lo (2003), and an indicator variable equal to one if the firm lobbied the SEC in regard to a contemporaneous 1992 rule on proxy fights.<sup>10</sup> Since lobbying may be driven by compliance costs, we additionally include the log of audit fees paid in 2001.<sup>11</sup> High pre-SOX audit fees may be associated (positively or negatively) with SOX compliance costs. Finally, we include three additional variables that may indicate poor firm governance. Following Chhaochharia and Grinstein (2005), we include an indicator variable taking the value of one if the firm's CEO have sold a large amount of stock within the 3 month period leading up to a large reported drop in earnings, and an indicator variable for restated earnings during 1998-2001.<sup>12</sup> The last variable included is a measure of discretionary accruals calculated using the modified Jones (1991) model, which is intended to measure earnings management. Summary statistics for these variables are included in Table II.

Table III Panel A presents the results of the probit models for lobbying against an 'Enhanced Disclosure' rule. Some of the models are estimated with fewer observations due to lack of availability of the necessary data. We include size in all models since it is the strongest driver of lobbying. Given the summary statistics in Table II, it is not surprising that size is a strong predictor of lobbying. We are more interested in which variables other than size (the characteristic we always match on) may have predictive power for lobbying. When the additional variables are included

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<sup>9</sup>We do not use the 2001 values since these may not be known until well into 2002. We set the competition variables to missing if the calculated variables are in the top or bottom 2 percent.

<sup>10</sup>Data on both these variables was obtained from Kin Lo.

<sup>11</sup>Data on audit fees is obtained from Audit Analytics.

<sup>12</sup>Data for both these variables was provided by Yaniv Grinstein and Vidhi Chhaochharia.

individually, book-to-market equity, the Gompers, Ishii and Metrick index, the two competition indices, and the PAC indicator enter significantly. The last column includes all variables. In this model we set a variable to zero if data are missing and include indicator variables for missing data (the coefficients on these indicators are omitted from the table). When all variables are included jointly, the book-to-market equity ratio, the Gompers, Ishii and Metrick index, and the firm level index of competition retain their significance. The signs of these three variables are as expected and the magnitudes are economically substantial. Value firms (those with a higher book-to-market equity ratio) are more likely to lobbying, likely because these tend to be older firms that may have more entrenched management. An increase in the book-to-market equity ratio from its 10th to its 90th percentile increases the probability of lobbying against an 'Enhanced Disclosure' rule by 0.05 percentage points. For reference, 2.6 percent of the 7358 firms included in the regression lobby against an 'Enhanced Disclosure' rule. An increase in the Gompers, Ishii and Metrick index from its 10th to its 90th percentile increases the probability of lobbying against an 'Enhanced Disclosure' rule by 0.28 percentage points, while the increase in the firm level competition index from its 10th to its 90th percentile decreases the lobbying probability by 0.82 percentage points.

The pseudo  $R^2$  of the regression is 0.23 suggesting that lobbying overall is fairly predictable based on variables observable at the beginning of our sample. Furthermore, it is highly likely that market participants had much more detailed information about firm characteristics and thus that they were able to predict much more accurately than our probit models which firms would lobby. We therefore supplement the probit results with an event study of whether abnormal returns were observed around the date of the submission of a letter by a given company (and posting of the letter on the SEC web page or accessibility of the letter in the SEC's public reference room).

## **B.2. Event Study of Returns Around Date of Comment Letter**

Figure 1 illustrates our findings and includes results for all three types of lobbying. It shows results for the approach where abnormal returns are measured relative to a group of non-lobbying firms constructed based on 100 size-portfolios. The results based on matching on size and book-to-market equity or size and industry are similar. Each graph contains two lines. The line labelled 'No factor adjustment' is constructed as follows. We first average the excess returns for lobbying firms relative to their matched non-lobbying firms across the set of lobbying firms. This is done for each week in event time where date zero in event time is the week the letter was filed with the SEC. Average excess returns are then summed over time (in event time) starting 10 weeks before the event date,

and ending 10 weeks after the event date.<sup>13</sup> The line labelled ‘With factor adjustment’ follows the same approach except that the excess return for a given lobbying firm relative to its group of matched non-lobbying firms is replaced by the residual from a regression (run on the post-SOX period from week 31 of 2002 to the end of 2004) of the excess return on the market factor, size factor and book-to-market factor. If lobbying was not predictable by the market one would expect to see a positive or negative reaction to the submission of a letter. Figure 1 reveals no such reaction, suggesting that market participants were not surprised to learn which firms lobbied.

### **C. Returns of Lobbying and Non-Lobbying Firms During the Period Leading up to Passage of the Sarbanes-Oxley Act**

We now turn to the comparison of returns for lobbying and non-lobbying firms. Under the improved disclosure and governance hypothesis, returns should be larger for lobbying firms than for non-lobbying firms during the period leading up to passage of SOX. The compliance cost view of SOX has the opposite prediction.

#### **C.1. Portfolio Level Returns**

To test these two competing hypotheses, we must first decide precisely how the comparison between the two sets of firms should be made. The standard approach for this type of question is to calculate excess returns for a portfolio of the ‘affected’ firms (here lobbyists) over and above the returns for a portfolio of ‘control’ firms (here non-lobbyers). To do this calculation, one must decide on which characteristics lobbying and non-lobbying firms should be matched, and how fine a grid should be used to match along a given dimension.

A large literature documents that small firms and firms with high book-to-market equity ratios on average tend to outperform large firms and firms with low book-to-market ratios. Furthermore, in a particular time period, realized returns could differ systematically across firms with different size, book-to-market, industry, or other characteristics, and such patterns may be entirely unrelated to the effects of SOX. It is therefore important to compare lobbying and non-lobbying firms with similar characteristics along these dimensions. Of course, there is a limit to how many characteristics one should match lobbying and non-lobbying firms on. In the extreme, if one matched along all observable dimensions related to disclosure, governance and variables measuring likely SOX compliance costs, then it may be more or less random which firms of a particular set of such

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<sup>13</sup>In the construction of Figure 1 we omit letters filed within the first 10 weeks of SOX passage such that no parts of the figure are affected by the news of SOX passage itself.

characteristics decided to lobby the SEC. Such a matching scheme would then, by construction, find no different return patterns between lobbyists and non-lobbyists and would wrongly lead to the conclusion that SOX was irrelevant for firm value. Based on these considerations, we will consider a variety of approaches to match lobbying and non-lobbying firms on size, book-to-market, and industry (the leading variables known to be related to expected returns or likely to be related to realized returns for reasons not related to SOX), but will not match on variables related to disclosure, governance or likely compliance costs. Data on returns, industry and market capitalization are obtained from CRSP, while data on book equity values are obtained from COMPUSTAT.

To decide how best to do the matching on size, book-to-market, and industry, we begin in Table II by tabulating the characteristics of lobbying and non-lobbying firms. For each characteristic, we provide p-values for t-tests for equal means across the two groups. The statistics for non-lobbyists refer to firms who did not lobby for or against any SOX provision and are therefore identical for Panel A, which compares firms who lobbied against any of the 'Enhanced Disclosure' rules to non-lobbyists, Panel B, which compares firms who lobbied against any of the 'Corporate Responsibility' rules to non-lobbyists, and Panel C, which compares firms who lobbied against the 'Auditor Independence' rule to non-lobbyists.

The strongest difference between the three groups of lobbyists and the non-lobbyists is that lobbying firms tend to be much larger than non-lobbying firms. This could be due to a fixed cost element of lobbying, or due to the costs or benefits of SOX varying along the size dimension. Along the book-to-market equity dimension there is little difference between firms that lobby against 'Enhanced Disclosure' and non-lobbyists, while firms that lobby against 'Corporate Responsibility' or 'Auditor Independence' have significantly higher mean (but not median) book-to-market ratios than non-lobbyists. The industry composition of lobbyists and non-lobbyists differs somewhat, with significant differences for several industry categories in Panel A and also in Panel B. Together these statistics suggest that a fine grid along the size dimension is the most important for ensuring that the matched non-lobbying firms have characteristics similar to those of the lobbying firms. We therefore show results for three approaches, defined by how many comparison portfolios of non-lobbying firms we construct: (a) 100 size-sorted portfolios (with break points calculated using all NYSE, AMEX and NASDAQ firms), (b) 125 size and book-to-market sorted portfolios defined as the interaction of 25 size categories (with NYSE break points to get a finer grid at the top end) and 5 book-to-market categories, and (c) 250 size and industry sorted portfolios, defined as

the interaction of 25 size categories (with NYSE break points) and 10 1-digit SIC industry code categories.<sup>14</sup>

For each approach, we first calculate the weekly average portfolio returns for each of the 100/125/250 comparison groups of non-lobbying firms. We then calculate the average weekly excess return for lobbying firms over and above their matched non-lobbying firm portfolio as

$$\frac{1}{N_t} \sum_{i=1}^{N_t} (r_{i,t}^{Lobby} - r_{p,t}^{Non-Lobby})$$

where  $r_{i,t}^{Lobby}$  is the return on lobbying firm  $i$ 's stock in week  $t$ ,  $N_t$  is the number of lobbying firms for which returns are available for week  $t$ , and  $r_{p,t}^{Non-Lobby}$  is the average weekly return in week  $t$  on the portfolio of non-lobbying firms matched to firm  $i$ .

If the matching succeeds in lining up each lobbying firm with a set of non-lobbying firms with very similar size, book-to-market and industry characteristics, then the above excess return time series directly measures the abnormal performance ( $\alpha$ ) of lobbyists. If the match is less accurate, more precise measures of the abnormal part of any over- or under-performance of lobbyists can be obtained by estimating a factor model and analyzing the  $\alpha$  from such a model. We present both the results which do not use a factor model and the results which use a 3-factor model and regress the excess return of lobbyists on the weekly market factor (MKT), size factor (SMB), and book-to-market factor (HML) calculated from daily factor data from Ken French's web page:

$$\frac{1}{N_t} \sum_{i=1}^{N_t} (r_{i,t}^{Lobby} - r_{p,t}^{Non-Lobby}) = \alpha + \beta_{MKT}(r_{MKT,t} - r_{f,t}) + \beta_{SMB}r_{SMB,t} + \beta_{HML}r_{HML,t} + \epsilon_{i,t}$$

where  $r_f$  is the riskless (30-day T-bill) rate and  $\epsilon$  is an error term.<sup>15</sup> To the extent that results differ depending on whether a factor model is used, one would expect those from the factor model to be the most accurate.

Table IV Panel A shows the estimates of abnormal performance of lobbyists relative to non-lobbyists during the 24-week period leading up to passage of SOX, beginning in week 7 of 2002 and ending in week 30 of 2002 (February 8, 2002 to July 26, 2002). The top part of the panel shows strong evidence of *positive* abnormal returns for firms who lobbied *against* one of the 'Enhanced Disclosure' provisions, relative to their matched sample of non-lobbyists. Without factor controls,

<sup>14</sup>In all cases we define break points using the full set of lobbying and non-lobbying firms. Size is defined as market equity at the start of our sample (end of week 6 of 2002). Book-to-market equity is calculated using book equity for the prior calendar year from COMPUSTAT and market equity for the beginning of the year (with the exception that we for 2002 use market equity in week 6 of 2002).

<sup>15</sup>Weekly data are used as opposed to daily data to avoid any potential biases in factor loadings due to differential liquidity of the stocks of lobbying and non-lobbying firms. An alternative would be to use daily data but include lags of the factors as regressors.

the weekly alphas in columns (1), (5), and (9) are 0.0056, 0.0046, and 0.0037 across the three methods of matching. This corresponds to total abnormal returns for such lobbyists of 13.4, 11.0, and 8.9 percent over the 24-week period leading up to SOX passage. In each case, the alphas are significantly different from zero at the 1 percent level. Results are a bit weaker when a factor model is used (columns (2), (6) and (10)). A potentially important issue with the factor model is that the regressions in columns (2), (6) and (10) estimate the factor loadings using only 24 weeks of data. This could lead to overfitting and corresponding downward small sample bias in the estimated abnormal excess returns (alphas). In columns (4), (8), and (12) we instead use the full time period from week 7 of 2002 to the end of 2004 and allow for different alphas for the period leading up to SOX passage and the post-passage period. Across all three approaches to matching, the alphas now increase a bit relative to columns (2), (6) and (10), and imply total abnormal returns for such lobbyists of 11.5, 9.4, and 8.4 percent over the 24-week period leading up to SOX passage.<sup>16</sup>

Figure 1 illustrates the cumulative abnormal returns over time for firms that lobbied against an 'Enhanced Disclosure' provision of SOX. It is based on portfolio level returns and three sets of cumulative abnormal returns are shown. The first of the three is based on the size-matched control group of non-lobbying firms, the second on a size and book-to-market equity matched control group and the third on a size and industry-matched control group. In each graph, two lines are shown. The unadjusted cumulative abnormal return is calculated by averaging the excess returns over comparison group across lobbying firms in each week, and then summing these abnormal returns over time, starting in week 7 of year 2002. The factor-adjusted cumulative abnormal return is calculated by first regressing the excess return over the comparison group on the excess return on the market, and the Fama-French size and book-to-market factors. The regression is run using weekly data from week 7 of 2002 until the end of 2004, and the intercept (alpha) plus the residuals are averaged each week and then summed over time. The two vertical lines indicate the beginning and end of the 24-week period leading up to SOX passage. It is striking how the abnormal performance of lobbying firms relative to non-lobbying firms ends right around the time of the passage of SOX.

The middle and bottom parts of Table IV Panel A repeat the same regressions, but now focusing on firms who lobbied against a 'Corporate Responsibility' or 'Auditor Independence' rule. In each case there is evidence of abnormal positive excess returns for lobbying firms relative to their

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<sup>16</sup>We discuss the alphas for the post-passage period below.

matched non-lobbying firms though the results are statistically weaker than for firms who lobbied against an 'Enhanced Disclosure' rule. Because many of the firms that lobbied against a 'Corporate Responsibility' or 'Auditor Independence' rule also lobbied against 'Enhanced Disclosure', it is, however, unclear how to interpret the results.<sup>17</sup> We address this issue in Table IV Panel B where we estimate the separate abnormal returns associated with each of the three types of lobbying by running firm level return regressions.

## C.2. Firm Level Returns

We run firm level (as opposed to portfolio level) regressions of the following form:

$$\begin{aligned} \frac{1}{T} \sum_{t=1}^T (r_{i,t}^{Lobby} - r_{f,t}) &= \delta_0 + \gamma_1 I(\text{Lobbied Against Enhanced Disclosure Rules}) \\ &+ \gamma_2 I(\text{Lobbied Against Corporate Responsibility Rules}) \\ &+ \gamma_3 I(\text{Lobbied Against Auditor Independence Rule}) + X_i' \beta + u_i \end{aligned}$$

where  $I(\cdot)$  indicates a dummy variable,  $\delta_0$  is an intercept term,  $X$  is a set of control variables and  $u_i$  is an error term. The regression is run on the full set of firms, i.e. including both lobbyists and non-lobbyists, and has one data point per firm. In regressions (1), (2), and (3) of Table IV Panel B, the dependent variable is the average weekly excess return over the riskless rate during the period leading up to SOX passage. The regression coefficient  $\gamma$  on the dummy variable for a particular type of lobbying estimates how much the average weekly return during the period differs between that group of lobbying firms and a typical non-lobbying firm. Control variables are included to account for differences in size, book-to-market and industry between lobbying and non-lobbying firms. We control for size by including in  $X$  log market equity at the start of the sample (end of week 6 of 2002), for book-to-market equity by including book-to-market equity as of the same date, and for industry by including nine 1-digit SIC code dummy variables. For similarity with Panel A, we first control only for size, then for size and book-to-market, and finally for size and industry.

Regressions (1), (2) and (3) of Table IV Panel B indicate that the market expected SOX to benefit the firms most affected by its 'Enhanced Disclosure' provisions (as evidenced by their lobbying), with only small added shareholder value for firms most affected by its 'Corporate Responsibility' or 'Auditor Independence' provisions. The weekly abnormal excess return for firms lobbying against an 'Enhanced Disclosure' rule captured by the  $\gamma_1$  coefficient imply total abnormal excess

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<sup>17</sup>About a third of firms who lobbied against a 'Corporate Responsibility' rule also lobbied against an 'Enhanced Disclosure' rule. About half of firms who lobbied against an 'Auditor Independence' rule also lobbied against an 'Enhanced Disclosure' rule.

return for the lead-up period of between 9.1 percent and 13.7 percent across the three regressions. These effects are comparable (theoretically, and in magnitude) to the effects estimated based on the  $\alpha_{\text{Lead-Up}}$  coefficient in the top part of Panel A. The  $\gamma_2$  coefficient on lobbying against a 'Corporate Responsibility' rule in Panel B imply total abnormal excess return for the lead-up period of between 2.6 percent and 3.8 percent across the three regressions, but this effect is not statistically significant. The  $\gamma_3$  coefficient on lobbying against the 'Auditor Independence' rule in Panel B imply total abnormal excess return for the lead-up period of between 1.4 percent and 3.6 percent across the three regressions, again not statistically significant.

In sum, the results of Table IV support the positive view of SOX that this legislation will increase shareholder value. In particular, the return results indicate that firms most affected by the 'Enhanced Disclosure' provisions of SOX (as evidenced by their lobbying) experienced positive abnormal excess returns during the period leading up to SOX passage of around 10 percent relative to less affected (non-lobbying) firms with similar size, book-to-market and industry characteristics. Smaller effects of a few percentage points were documented for firms most affected by the 'Corporate Responsibility' and 'Auditor Independence' rules.

These findings are consistent with the overwhelmingly positive opinions expressed by individuals and investor groups in their letters to the SEC.

## **D. Returns and Operating Performance During the Period Following Passage of the Sarbanes-Oxley Act**

### **D.1. Returns**

From Figure 2, it is apparent that firms lobbying against one or more of the SOX 'Enhanced Disclosure' rules had returns during the post-SOX period that were similar to those of their matched comparison group of non-lobbying firms. Table IV Panel A and B confirms this result. Columns (3)-(4), (7)-(8), and (11)-(12) of Table IV Panel A estimate the portfolio level excess return regressions on the full period from week 7 of 2002 to the end of 2004, with separate intercepts ( $\alpha$ 's) for the leadup period and the post-passage period. In the top part of the panel that concerns 'Enhanced Disclosure,' the intercept for the post-passage period,  $\alpha_{\text{Post}}$ , is consistently close to zero in both economic and statistical terms. A similar result obtains in columns (4)-(6) of Table IV Panel B when the firm-level regressions are estimated for the post-passage period – the  $\gamma_1$  regression coefficient of the dummy variable equal to one for firms that lobbied against an 'Enhanced Disclosure' rule is close to zero. These findings indicate that the returns for firms that lobbied against an 'Enhanced

Disclosure' rule were similar to the returns for their non-lobbying comparison group of firms and thus that the increase in (relative) stock prices experienced by lobbying firms did not tend to reverse during the post-passage period.

As for firms lobbying against a 'Corporate Responsibility' rule, columns (4)-(6) of Table IV Panel B suggest that the small positive abnormal excess returns for these firms during the leadup-period reverse during the post passage period though none of these effects are statistically significant.

## **D.2. Operating Performance**

A preliminary analysis of operating performance shows that lobbying firms experience improvements in operating performance relative to non-lobbying firms. We measure changes in operating performance as  $(\text{Operating income in 2004} - \text{Operating income in 2001}) / (\text{Market value of equity at the end of week 6 of 2002})$ , where operating income is COMPUSTAT Item 13 (operating income before depreciation). The results are included in columns (1)-(3) of Table V. The regressions presented are firm level regressions with one observation per firm and with controls for size (column (1)), size and book-to-market (column (2)), or size and industry dummies (column (3)). To reduce the influence of outliers, all regressions in the table drop observations in the top two or bottom two percent in terms of the dependent variable.

Firms that lobbied against an 'Enhanced Disclosure' rule experience an improvement in operating income relative to initial market value of equity of about 5 percentage points, and this effect is statistically significant at the 1 percent level. This is consistent with the returns results for these lobbying firms and indicates that investors positive expectations about the effect of SOX were warranted in the case of the 'Enhanced Disclosure' rules.

Operating performance also seems to improve for the other two groups of lobbying firms (relative to non-lobbyers). This is somewhat surprising given the lack of consistent abnormal returns for these firms.

## **D.3. Discussion**

Following the passage of SOX, a heated debate has emerged about the high costs of complying with the 'Enhanced Disclosure' provisions of SOX, notably Section 404 on internal controls. It is widely believed that the compliance costs associated with SOX have been higher than initially expected. In June 2003, the SEC estimated the aggregate cost of implementing Section 404 alone on all registrants at approximately \$1.24 billion, or \$91,000 per registrant. In January 2004, Financial

Executives International (FEI) completed the first of a string of surveys estimating the cost of SOX, and Section 404 in particular. The survey placed the expected average total cost of SOX compliance at approximately \$1.93 million per company. Expected costs appeared to be increasing in firm size, with expected total compliance costs for larger firms (over \$5 billion in annual revenues) to reach \$4.6 million per company. A first follow-on survey by FEI in June 2004 raised these estimates to \$3.15 million and \$8 million per company, respectively. A second follow-on survey by FEI in March of 2005 raised the estimates to \$4.36 million and \$10 million, respectively.

How do these costs affect our analysis of the post-passage period? We note first that if compliance costs increased equally for all firms (as a fraction of market value), then our analysis of excess returns of lobbyists over non-lobbyists will be unaffected by the increase. This is an obvious shortcoming of a research design which compares more affected firms to less affected firms, without having a comparable group of firms unaffected by the legislation studied. We can only say that considering the full period from when serious discussions about the legislation first started in week 7 of 2002 to the end of 2004 (well into the implementation phase of SOX), the stocks more affected firms (defined as lobbying firms) outperformed those of less affected firms (defined as non-lobbying firms). We cannot unambiguously say that the net benefit of SOX for either group is positive.

What then can be said about the net benefit of SOX for lobbyists and/or non-lobbyists? Our analysis of comment letters from investors and investor groups indicated that shareholders expect SOX to be value increasing on average across publicly traded firms. To our knowledge, shareholder support for SOX has not diminished since the period covered by the letters we analyze. For example, at the SEC's "Roundtable Discussion on Second-Year Experiences with Internal Control Reporting and Auditing Provisions" held on May 10, 2006, several institutional investors expressed continued support for SOX, specifically for the section 404 on internal controls. In her statement dated March 1st, Ann Yerger from the Council of Institutional Investors (an association of more than 130 corporate, union, and public pensions plans with more the \$3 trillion in assets) wrote: "...the Council believes the benefits over time will far outweigh the costs and will be a positive for all involved in the U.S. capital markets. ... In closing, Section 404 is working."

Furthermore, under two simplifying assumptions, we believe the net benefit of SOX can be argued to be positive for lobbyists. Suppose that compliance costs relative to initial market value are similar across lobbyists and non-lobbyists for firms of similar size. Suppose furthermore, as a conservative assumption, that there was no (gross) benefit of SOX for non-lobbyists. If so, the

cumulative abnormal excess return of about 10 percent for firms lobbying against an 'Enhanced Disclosure' rule relative to their matched non-lobbying firms implies that the gross benefit of SOX for these lobbying firms was about 10 percent of their initial market value, or approximately \$308 billion in total.

It is unlikely that the present value of SOX compliance costs for lobbying firms is as high as 10 percent of these firms initial market value. From Table II Panel A, the mean market value for firms lobbying against an 'Enhanced Disclosure' rule is \$16 billion, while the median is \$2.6 billion. Suppose the typical such lobbying firm experienced a SOX compliance cost equal to the estimate of \$10 million for large firms from the March 2005 FEI survey discussed above. Using a discount rate of 10 percent, the present value of a typical lobbying firm's compliance costs is then \$100 million. This corresponds to 0.6 percent of the mean market value of \$16 billion and 3.8 percent of the median market value of \$2.6 billion.

This admittedly simplified calculation suggests that, at least for the set of firms lobbying against an 'Enhanced Disclosure' rule, SOX was a net benefit of between 6 and 9 percent of initial market value. We have data for 193 such firms with a total market value of  $193 \times \$16$  billion or about \$3 trillion. At a net benefit of 6 percent of market value, the total net benefit of SOX for these lobbying firms comes to \$185 billion. At a net benefit of 9 percent of market value, the total net benefit of SOX for these lobbying firms comes to \$278 billion.

Furthermore, in the March 2005 FEI survey, the total estimated annual compliance costs for the full set of US publicly traded firms of \$35 billion. Since then the FEI reports that average compliance cost have fallen 16 percent, bringing the total estimated annual compliance cost for the full set of US publicly traded firms down to \$29.4 billion. At a discount rate of 10 percent, the present value of these costs is \$294 billion, slightly less than the estimated gross benefit for lobbyists. This suggests that with even a small positive gross benefit of SOX for non-lobbyers, the net benefit of SOX for the overall US stock market could be substantial.

## **IV. Conclusion**

In this paper, we evaluate the impact of SOX on shareholders by analyzing the SOX-related lobbying behavior of corporations, individuals and organizations. We classify the rules on which the SEC solicited comments into three major categories: those related to 'Enhanced Disclosure', those related to 'Corporate Responsibility', and those related to 'Auditor Independence'. We then examine the

comment letters sent to the SEC during the drafting of the final SOX rules.

We document that individual investors, as well as large investor groups such as pension funds and labor unions, were overwhelmingly in favor of the SOX provisions they commented on, speaking to shareholders' perceived value of the legislation. In contrast, our reading of letters to the SEC by corporate insiders reveals that an overwhelming majority of insiders in lobbying companies opposed the SOX provision they commented on.

We then use lobbying by corporate insiders to distinguish between two views of SOX: the view that SOX improves governance and disclosure, and the view that SOX will not be beneficial due to high compliance costs outweighing any potential benefits. Our identifying assumption is that insiders in companies more affected by SOX were more likely to lobby.

Our study of returns reveals that during the 24-week period leading up to passage of SOX, returns were higher for corporations whose insiders lobbied against an 'Enhanced Disclosure' provision of SOX than for non-lobbying firms with similar size, book-to-market and industry characteristics. This lends support to the improved disclosure and governance hypothesis and suggests that corporate insiders lobbied to water down the implementation of SOX because SOX reduces insiders' ability to expropriate company resources. Cumulative returns were approximately 10 percent higher for corporations whose insiders lobbied against one or more of the SOX 'Enhanced Disclosure' provisions than for non-lobbying firms with similar size, book-to-market and industry characteristics. There is no evidence of differential returns between lobbyists and non-lobbyists in the post-passage period. Furthermore, a preliminary analysis of operating performance indicates that lobbying firms experienced improvements in operating performance relative to non-lobbying firms in the post-passage period.

In sum, our findings suggest that investors had overwhelmingly positive expectations about the effects of SOX, particularly those provisions related to 'Enhanced Disclosure', which includes management assessment of internal controls over financial reporting. These expectations appear to be warranted in the case of the 'Enhanced Disclosure' provisions of SOX, though not in the case of the 'Corporate Responsibility' or 'Auditor Independence' provisions.

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Table I:

### Opinions of Commenters, by Rule and Type of Commenter

The table reports the number of letters sent to the SEC and the opinions expressed in those letters for the provisions of the Sarbanes-Oxley Act and the NYSE/NASDAQ corporate governance rules for which comments were solicited by the SEC. The first panel presents the overall counts across all rules. Rules are then sorted into those that concern auditor independence (related to SOX Title II), Corporate Responsibility (related to SOX title III), and Enhanced Financial Disclosure and PCAOB (mostly related to SOX Title IV). The title of the rule (underlined) refers to the SEC initial proposal for each specific rule. For each rule we report the number of letters sent to the SEC and classify them by whether the letter is positive, neutral, or negative on the particular rule commented on. The neutral category includes letters that are positive on some, but negative on other sub-provisions, as well as letters that cannot be classified due to insufficient information. We classify commenters into the following categories: Corporations (including letters from a top manager or director), non-investor groups (e.g. business associations), investor groups (e.g. pension funds, asset management firms and foundations), individuals (excluding lawyers and accountants), accountants (associations, law firms, and individual lawyers), accountants (associations, accounting firms, and individual accountants), academics, and other (e.g. religious organizations, government representatives, and elected officials). When available, we report, in bracket parenthesis, the SOX Section corresponding to the proposal.

| Commenter:   | Total Letters Commenting on All Rules |                    |                |            |            |           |          |         |
|--|---------------------------------------|--------------------|----------------|------------|------------|-----------|----------|---------|
|  | Corporation                           | Non-Investor Group | Investor Group | Individual | Accountant | Lawyer    | Academic | Other   |
| No. of Letters   | 842                                   | 253                | 226            | 542        | 176        | 398       | 70       | 103     |
| No. Pos/Neu/Neg  | 115/69/643                            | 34/31/188          | 186/18/22      | 426/48/68  | 40/22/114  | 35/33/330 | 40/15/15 | 46/6/51 |
| Pct. Pos/Neu/Neg   | 14/8/78                               | 13/12/74           | 82/8/10        | 79/9/13    | 23/13/65   | 9/8/83    | 57/21/21 | 45/6/50 |
| <b>Totals Letters Commenting on Rules Related to Enhanced Financial Disclosure and PCAOB [SOX Titles IV and I]</b> |                                       |                    |                |            |            |           |          |         |
| No. of Letters   | 401                                   | 114                | 50             | 113        | 65         | 111       | 17       | 38      |
| No. Pos/Neu/Neg  | 36/53/312                             | 12/16/86           | 38/3/9         | 88/9/16    | 17/14/34   | 7/10/94   | 9/6/2    | 30/3/5  |
| Pct. Pos/Neu/Neg   | 9/13/78                               | 11/14/75           | 76/6/18        | 78/8/14    | 26/22/52   | 6/9/85    | 53/35/12 | 79/8/13 |
| Break-down of Letters Submitted on Enhanced Financial Disclosure Rules:  |                                       |                    |                |            |            |           |          |         |
| Disclosure In Management's Discussion And Analysis Of Critical Accounting Policies                                 |                                       |                    |                |            |            |           |          |         |
| No. of Letters   | 40                                    | 19                 | 4              | 0          | 7          | 0         | 1        | 0       |
| No. Pos/Neu/Neg  | 2/2/36                                | 2/0/17             | 3/1/1          | 0/0/0      | 0/0/7      | 0/0/0     | 0/1/0    | 0/0/0   |

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| <b>Committer:</b>   | <b>Corporation</b> | <b>Non-Investor Group</b>  | <b>Investor Group</b> | <b>Individual</b> | <b>Accountant</b> | <b>Lawyer</b> | <b>Academic</b> | <b>Other</b> |
|---|--------------------|--|-----------------------|-------------------|-------------------|---------------|-----------------|--------------|
| [SOX Section 401: Disclosure in Periodic Reports]   |                    |  |                       |                   |                   |               |                 |              |
| No. of Letters  | 14                 | Disclosure in Management's Discussion and Analysis of Off-Balance Sheet Arrangements |                       |                   |                   |               |                 |              |
| No. Pos/Neu/Neg   | 0/0/14             | 2/0/8  | 1/1/0                 | 10/1/2            | 0/1/6             | 0/1/8         | 0/0/0           | 1/0/0        |
| [SOX Section 401: Disclosure in Periodic Reports]   |                    |  |                       |                   |                   |               |                 |              |
| No. of Letters  | 54                 | Conditions for Use of Non-GAAP Financial Measures                                    |                       |                   |                   |               |                 |              |
| No. Pos/Neu/Neg   | 2/27/25            | 1/1/11   | 1/1/1                 | 4/0/1             | 7/4/2             | 13/0/2/11     | 0               | 2            |
| [SOX Section 401: Disclosure in Periodic Reports]   |                    |  |                       |                   |                   |               |                 |              |
| No. of Letters  | 7                  | Mandated Electronic Filing and Website Posting for Forms 3, 4 and 5                  |                       |                   |                   |               |                 |              |
| No. Pos/Neu/Neg   | 0/7/0              | 0/3/1  | 2/0/0                 | 1/0/0             | 0/1/0             | 1/5/0         | 0               | 0            |
| [SOX Section 403: Disclosures Of Transactions Involving Management and Principal Stockholders]                          |                    |  |                       |                   |                   |               |                 |              |
| No. of Letters  | 136                | Disclosure Required by Sections 404, 406 and 407 of the Sarbanes-Oxley Act of 2002   |                       |                   |                   |               |                 |              |
| No. Pos/Neu/Neg   | 4/6/126            | 2/4/30   | 2/0/2                 | 8/4/7             | 3/4/9             | 0/2/31        | 6               | 4            |
| [SOX Section 404: Management Assessment of Internal Controls]   |                    |  |                       |                   |                   |               |                 |              |
| [SOX Section 406: Code Of Ethics For Senior Financial Officers]   |                    |  |                       |                   |                   |               |                 |              |
| [SOX Section 407: Disclosure of Audit Committee Financial Expert]   |                    |  |                       |                   |                   |               |                 |              |
| No. of Letters  | 47                 | Additional Form 8-K Disclosure Requirements and Acceleration of Filing Date          |                       |                   |                   |               |                 |              |
| No. Pos/Neu/Neg   | 7/1/39             | 4/1/6  | 1/0/0                 | 4/0/0             | 0/0/7             | 1/0/14        | 1               | 3            |
| [SOX Section 409: Real-Time Issuer Disclosures]   |                    |  |                       |                   |                   |               |                 |              |
| Letters Commenting on Other Disclosure Related SEC Rules (Not Part of SOX Itself):                                      |                    |  |                       |                   |                   |               |                 |              |
| Disclosure Regarding Nominating Committee Functions And Communications Between Security Holders and Boards of Directors |                    |  |                       |                   |                   |               |                 |              |
| No. of Letters  | 29                 | 8  | 26                    | 57                | 3                 | 13            | 6               | 27           |
| No. Pos/Neu/Neg   | 16/1/12            | 4/1/3  | 23/0/3                | 51/3/3            | 3/0/0             | 4/0/9         | 5/1/0           | 25/2/0       |
| Form 8-K Disclosure of Certain Management Transactions  |                    |  |                       |                   |                   |               |                 |              |
| No. of Letters  | 57                 | 10   | 7                     | 14                | 0                 | 15            | 2               | 0            |
| No. Pos/Neu/Neg   | 4/5/48             | 0/1/9  | 5/0/2                 | 10/1/3            | -                 | 1/0/14        | 1/1/0           | -            |
| Individual PCAOB Rules  |                    |  |                       |                   |                   |               |                 |              |

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| Commenter:   | Corporation | Non-Investor Group | Investor Group | Individual | Accountant | Lawyer    | Academic | Other   |
|--|-------------|--------------------|----------------|------------|------------|-----------|----------|---------|
| No. of Letters   | 0           | 0                  | 0              | 0          | 5          | 0         | 0        | 0       |
| No. Pos/Neu/Neg  | -           | -                  | -              | -          | 4/1/0      | -         | -        | -       |
| [SOX Section 101: Establishment; Administrative Provisions]                          |             |                    |                |            |            |           |          |         |
| [SOX Section 103: Auditing, Quality Control, and Independence Standards and Rules]   |             |                    |                |            |            |           |          |         |
| [SOX Section 107: Commission Oversight of the Board]                                 |             |                    |                |            |            |           |          |         |
| PCAOB Auditing Standard No. 1  |             |                    |                |            |            |           |          |         |
| No. of Letters   | 17          | 3                  | 0              | 0          | 12         | 0         | 1        | 0       |
| No. Pos/Neu/Neg  | 1/4/12      | 1/1/1              | -              | -          | 6/3/3      | -         | 0/1/0    | -       |
| PCAOB Auditing Standard No. 2  |             |                    |                |            |            |           |          |         |
| <b>Total Letters Commenting on Rules on Corporate Responsibility [SOX Title III]</b> |             |                    |                |            |            |           |          |         |
| No. of Letters   | 393         | 123                | 170            | 420        | 42         | 276       | 48       | 60      |
| No. Pos/Neu/Neg  | 70/15/293   | 20/14/89           | 143/15/12      | 333/38/49  | 16/5/21    | 25/23/228 | 28/8/12  | 14/3/43 |
| Pct. Pos/Neu/Neg   | 18/4/77     | 16/11/72           | 84/9/7         | 79/9/12    | 38/12/50   | 9/8/83    | 58/17/25 | 23/5/72 |
| Break-down of Letters Submitted on Corporate Responsibility Rules:                   |             |                    |                |            |            |           |          |         |
| Standards Relating To Listed Company Audit Committees                                |             |                    |                |            |            |           |          |         |
| No. of Letters   | 80          | 24                 | 9              | 5          | 13         | 26        | 1        | 15      |
| No. Pos/Neu/Neg  | 4/4/72      | 4/1/19             | 8/1/0          | 4/0/1      | 4/4/5      | 1/3/22    | 1/0/0    | 2/1/12  |
| [SOX Section 301: Public Company Audit Committees]                                   |             |                    |                |            |            |           |          |         |
| Certification of Disclosure in Companies' Quarterly and Annual Reports               |             |                    |                |            |            |           |          |         |
| No. of Letters   | 19          | 15                 | 1              | 52         | 4          | 24        | 1        | 3       |
| No. Pos/Neu/Neg  | 4/1/14      | 3/0/12             | 0/0/1          | 49/2/1     | 1/1/2      | 3/2/19    | 1/0/0    | 0/0/3   |
| [SOX Section 302: Corporate Responsibility For Financial Reports]                    |             |                    |                |            |            |           |          |         |
| Certification of Disclosure in Certain Exchange Act Reports                          |             |                    |                |            |            |           |          |         |
| No. of Letters   | 1           | 1                  | 0              | 0          | 1          | 4         | 1        | 0       |
| No. Pos/Neu/Neg  | 0/0/1       | 0/0/1              | -              | -          | 1/0/0      | 1/1/2     | 1/0/0    | -       |
| [SOX Section 302: Corporate Responsibility for Financial Reports]                    |             |                    |                |            |            |           |          |         |
| [SOX Section 906: Corporate Responsibility for Financial Reports]                    |             |                    |                |            |            |           |          |         |
| Improper Influence on Conduct of Audits  |             |                    |                |            |            |           |          |         |
| No. of Letters   | 7           | 8                  | 2              | 14         | 9          | 8         | 0        | 1       |
| No. Pos/Neu/Neg  | 1/1/5       | 1/1/6              | 2/0/0          | 14/0/0     | 6/0/3      | 0/0/8     | -        | 0/0/1   |
| [SOX Section 303: Improper Influence on Conduct of Audits]                           |             |                    |                |            |            |           |          |         |

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| Commenter:   | Corporation | Non-Investor Group | Investor Group | Individual | Accountant | Lawyer | Academic | Other |
|--|-------------|--------------------|----------------|------------|------------|--------|----------|-------|
| No. of Letters   | 2           |                    |                |            |            |        |          |       |
| No. Pos/Neu/Neg  | 2/0/0       |                    |                |            |            |        |          |       |
| [SOX Section 802: Criminal Penalties for Altering Documents]                       |             |                    |                |            |            |        |          |       |
|  |             |                    |                |            |            |        |          |       |
| No. of Letters   | 3           |                    |                |            |            |        |          |       |
| No. Pos/Neu/Neg  | 1/1/1       |                    |                |            |            |        |          |       |
| [SOX Section 306: Insider Trades During Pension Fund Blackout]                     |             |                    |                |            |            |        |          |       |
|  |             |                    |                |            |            |        |          |       |
| No. of Letters   | 8           |                    |                |            |            |        |          |       |
| No. Pos/Neu/Neg  | 3/2/20      |                    |                |            |            |        |          |       |
| [SOX Section 307: Rules Of Professional Responsibility for Attorneys]              |             |                    |                |            |            |        |          |       |
|  |             |                    |                |            |            |        |          |       |
| No. of Letters   | 23          |                    |                |            |            |        |          |       |
| No. Pos/Neu/Neg  | 2/2/19      |                    |                |            |            |        |          |       |
| [SOX Section 307: Rules of Professional Responsibility for Attorneys]              |             |                    |                |            |            |        |          |       |
|  |             |                    |                |            |            |        |          |       |
| No. of Letters   | 4           |                    |                |            |            |        |          |       |
| No. Pos/Neu/Neg  | 0/0/4       |                    |                |            |            |        |          |       |
| [SOX Section 307: Rules of Professional Responsibility for Attorneys]              |             |                    |                |            |            |        |          |       |
|  |             |                    |                |            |            |        |          |       |
| No. of Letters   | 18          |                    |                |            |            |        |          |       |
| No. Pos/Neu/Neg  | 8/3/18      |                    |                |            |            |        |          |       |
| [SOX Section 307: Rules of Professional Responsibility for Attorneys]              |             |                    |                |            |            |        |          |       |
|  |             |                    |                |            |            |        |          |       |
| No. of Letters   | 4           |                    |                |            |            |        |          |       |
| No. Pos/Neu/Neg  | 0/1/3       |                    |                |            |            |        |          |       |
| [SOX Section 103: Auditing, Quality Control, and Independence Standards and Rules] |             |                    |                |            |            |        |          |       |
| [SOX Section 404: Management Assessment of Internal Controls]                      |             |                    |                |            |            |        |          |       |

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| Commenter:   | Corporation | Non-Investor Group   | Investor Group | Individual | Accountant | Lawyer  | Academic | Other   |
|--|-------------|--|----------------|------------|------------|---------|----------|---------|
| Total Letters Commenting on Rules on Auditor Independence [SOX Title II] |             |  |                |            |            |         |          |         |
| No. of Letters   | 48          | 16   | 6              | 9          | 69         | 11      | 5        | 5       |
| No. Pos/Neu/Neg  | 9/1/38      | 2/1/13   | 5/0/1          | 5/1/3      | 7/3/59     | 3/0/8   | 3/1/1    | 2/0/3   |
| Pct. Pos/Neu/Neg   | 19/2/79     | 13/6/81  | 83/0/17        | 56/11/33   | 10/4/86    | 27/0/73 | 60/20/20 | 40/5/60 |
| [SOX: Section 201-207; Auditor Independence]                             |             |  |                |            |            |         |          |         |
|  |             | Strengthening The Commission's Requirements Regarding Auditor Independence |                |            |            |         |          |         |

Table II:

### **Characteristics of Publicly Traded Firms that Lobbied the SEC and Firms that did not Lobby the SEC**

This table presents firm characteristics for companies who did and did not lobby against the proposed SOX-related SEC rule releases. Panel A examines the characteristics of both lobbying and non-lobbying companies with regards to the rules on Enhanced Financial Disclosure and PCAOB proposed and implemented by the SEC. Panel B examines the characteristics of both lobbying and non-lobbying companies with regards to the corporate responsibility rules proposed and implemented by the SEC. Panel C examines the characteristics of both lobbying and non-lobbying companies with regards to Auditor Independence rules proposed and implemented by the SEC. We present the mean, standard deviation and the p-value for a t-test for no differences in means between lobbyists and non-lobbyers. Firm market capitalization is expressed in MM \$ and calculated for the end of week 6 of 2002 (Friday, February 8th); book-to-market equity is calculated using book equity for the fiscal year ending in 2001 and market equity for the end of week 6 of 2002; Governance Index is the firm's Gompers, Ishi and Metrick (2003) index calculated in year 2000; Firm-level Lerner Competition Index is  $(1 - netincome/sales)$  calculated in year 2000; Industry Level Lerner Competition Index is  $(1netincome/sales)$  calculated as the average across the entire firm level database in 2000, excluding each firm itself (see Bloom and Van Reenen, 2006); PAC is an indicator variable equal to one if the firm has a Political Action Committee that was registered with the Federal Election Commission's during the 1999-2000 period; Past Lobbying on Compensation Rules is an indicator variable if the firm has lobbied against the 1992 revision of executive compensation disclosure rules adopted by the SEC (See Lo, 2003); Past Lobbying on Proxy Rules is an indicator variable if the firm has lobbied against the new rules on proxy fights adopted by the SEC in 1992 (See Lo, 2003); both the firm's audit fees, expressed in MM \$, and the firm's ratio of audit fees over sales are calculated in year 2001; Discretionary Accruals are calculated in year 2001 following Jones (2001) model; Restated Earnings is an indicator variable if the firm restated its earnings in the period 1998-2001; Insider Sales Prior to Earnings Drop is an indicator variable equal to one if the CEO sold a large amount of his stocks within the 3 months prior to a large reported drop in earnings. Finally, the table reports the summary statistics for Standard Industrial Classification code (indicator variables).

Panel A: Enhanced Financial Disclosure and PCAOB

|  | Lobbyers |        |        |           | Non-Lobbyers |        |        |           | p-values |
|--|----------|--------|--------|-----------|--------------|--------|--------|-----------|----------|
|  | N        | Median | Mean   | Std. Dev. | N            | Median | Mean   | Std. Dev. |          |
| Market Capitalization (\$M)                              | 193      | 2,604  | 16,004 | 38,318    | 6,990        | 119    | 1,103  | 6,169     | 0.000    |
| Book-to-Market Ratio                                     | 182      | 0.509  | 1.550  | 4.634     | 5,881        | 0.647  | 1.392  | 3.420     | 0.545    |
| Agriculture, Forestry, And Fishing (SIC=0)               | 193      | 0      | 0      | 0         | 6,990        | 0      | 0.002  | 0.046     | 0.519    |
| Mining (SIC=1)   | 193      | 0      | 0.047  | 0.211     | 6,990        | 0      | 0.046  | 0.211     | 0.993    |
| Construction (SIC=2)                                     | 193      | 0      | 0.161  | 0.368     | 6,990        | 0      | 0.112  | 0.316     | 0.038    |
| Manufacturing (SIC=3)                                    | 193      | 0      | 0.181  | 0.386     | 6,990        | 0      | 0.226  | 0.418     | 0.144    |
| Transp., Commun., Elec., Gas, and Sanitary Serv. (SIC=4) | 193      | 0      | 0.088  | 0.284     | 6,990        | 0      | 0.080  | 0.271     | 0.688    |
| Wholesale Trade (SIC=5)                                  | 193      | 0      | 0.057  | 0.232     | 6,990        | 0      | 0.083  | 0.276     | 0.195    |
| Retail Trade (SIC=6)                                     | 193      | 0      | 0.399  | 0.491     | 6,990        | 0      | 0.264  | 0.441     | 0.000    |
| Finance, Insurance, And Real Estate (SIC=7)              | 193      | 0      | 0.057  | 0.232     | 6,990        | 0      | 0.139  | 0.346     | 0.001    |
| Services (SIC=8)   | 193      | 0      | 0.010  | 0.102     | 6,990        | 0      | 0.047  | 0.211     | 0.017    |
| Public Administration (SIC=9)                            | 193      | 0      | 0      | 0         | 6,990        | 0      | 0.000  | 0.012     | 0.868    |
| Governance Index   | 109      | 10     | 9.807  | 2.774     | 1,201        | 9      | 8.850  | 2.691     | 0.000    |
| Firm-level Lerner Competition Index                      | 174      | 0.904  | 0.885  | 0.118     | 5,129        | 0.967  | 1.627  | 5.093     | 0.055    |
| Industry-level Lerner Competition Index                  | 190      | 0.947  | 1.264  | 1.254     | 6,722        | 0.991  | 1.554  | 1.510     | 0.009    |
| Political Action Committee (PAC) (indicator)             | 193      | 0      | 0.420  | 0.495     | 6,990        | 0      | 0.075  | 0.264     | 0.000    |
| Past Lobbying on Compensation Rules (indicator)          | 193      | 0      | 0.119  | 0.325     | 6,990        | 0      | 0.011  | 0.104     | 0.000    |
| Past Lobbying on Proxy Rules (indicator)                 | 193      | 0      | 0.078  | 0.268     | 6,990        | 0      | 0.005  | 0.074     | 0.000    |
| Audit Fees in 2001 (\$M)                                 | 159      | 0.706  | 2.208  | 3.768     | 5,124        | 0.168  | 0.403  | 0.985     | 0.000    |
| Audit Fees over sales in 2001                            | 159      | 0.026  | 0.081  | 0.288     | 5,124        | 0.106  | 0.391  | 1.038     | 0.000    |
| Discretionary Accruals                                   | 107      | 0.001  | -0.001 | 0.044     | 3,711        | 0.002  | -0.001 | 0.115     | 0.985    |
| Restated Earnings (indicator)                            | 188      | 0      | 0.059  | 0.235     | 6,102        | 0      | 0.053  | 0.224     | 0.729    |
| Insider Sales Prior to Earnings Drop (indicator)         | 188      | 0      | 0.021  | 0.145     | 6,102        | 0      | 0.010  | 0.099     | 0.124    |

Panel B: Corporate Responsibility

|  | Lobbyers |        |        |           | Non-Lobbyers |        |        |           | p-values |
|--|----------|--------|--------|-----------|--------------|--------|--------|-----------|----------|
|  | N        | Median | Mean   | Std. Dev. | N            | Median | Mean   | Std. Dev. |          |
| Market Capitalization (\$M)                              | 90       | 2.662  | 22.245 | 58.921    | 6,990        | 119    | 1,103  | 6,169     | 0.000    |
| Book-to-Market Ratio                                     | 76       | 0.646  | 4.627  | 9.759     | 5,881        | 0.647  | 1.392  | 3.420     | 0.000    |
| Agriculture, Forestry, And Fishing (SIC=0)               | 90       | 0      | 0      | 0         | 6,990        | 0      | 0.002  | 0.046     | 0.660    |
| Mining (SIC=1)   | 90       | 0      | 0.067  | 0.251     | 6,990        | 0      | 0.046  | 0.211     | 0.368    |
| Construction (SIC=2)                                     | 90       | 0      | 0.156  | 0.364     | 6,990        | 0      | 0.112  | 0.316     | 0.199    |
| Manufacturing (SIC=3)                                    | 90       | 0      | 0.267  | 0.445     | 6,990        | 0      | 0.226  | 0.418     | 0.359    |
| Transp., Commun., Elec., Gas, and Sanitary Serv. (SIC=4) | 90       | 0      | 0.167  | 0.375     | 6,990        | 0      | 0.080  | 0.271     | 0.003    |
| Wholesale Trade (SIC=5)                                  | 90       | 0      | 0.044  | 0.207     | 6,990        | 0      | 0.083  | 0.276     | 0.187    |
| Retail Trade (SIC=6)                                     | 90       | 0      | 0.256  | 0.439     | 6,990        | 0      | 0.264  | 0.441     | 0.862    |
| Finance, Insurance, And Real Estate (SIC=7)              | 90       | 0      | 0.044  | 0.207     | 6,990        | 0      | 0.139  | 0.346     | 0.010    |
| Services (SIC=8)   | 90       | 0      | 0      | 0         | 6,990        | 0      | 0.047  | 0.211     | 0.036    |
| Public Administration (SIC=9)                            | 90       | 0      | 0      | 0         | 6,990        | 0      | 0.000  | 0.012     | 0.910    |
| Governance Index   | 31       | 10     | 9.774  | 2.432     | 1,201        | 9      | 8.850  | 2.691     | 0.059    |
| Firm-level Lerner Competition Index                      | 76       | 0.912  | 0.901  | 0.110     | 5,129        | 0.967  | 1.627  | 5.093     | 0.214    |
| Industry-level Lerner Competition Index                  | 89       | 0.972  | 1.344  | 1.271     | 6,722        | 0.991  | 1.554  | 1.510     | 0.192    |
| Political Action Committee (PAC) (indicator)             | 90       | 0      | 0.367  | 0.485     | 6,990        | 0      | 0.075  | 0.264     | 0.000    |
| Past Lobbying on Compensation Rules (indicator)          | 90       | 0      | 0.133  | 0.342     | 6,990        | 0      | 0.011  | 0.104     | 0.000    |
| Past Lobbying on Proxy Rules (indicator)                 | 90       | 0      | 0.144  | 0.354     | 6,990        | 0      | 0.005  | 0.074     | 0.000    |
| Audit Fees in 2001 (\$M)                                 | 42       | 2.678  | 4.956  | 5.953     | 5,124        | 0.168  | 0.403  | 0.985     | 0.000    |
| Audit Fees over sales in 2001                            | 42       | 0.023  | 0.033  | 0.031     | 5,124        | 0.106  | 0.391  | 1.038     | 0.026    |
| Discretionary Accruals                                   | 54       | -0.001 | 0.003  | 0.049     | 3,711        | 0.002  | -0.001 | 0.115     | 0.781    |
| Restated Earnings (indicator)                            | 86       | 0      | 0.023  | 0.152     | 6,102        | 0      | 0.053  | 0.224     | 0.222    |
| Insider Sales Prior to Earnings Drop (indicator)         | 86       | 0      | 0.047  | 0.212     | 6,102        | 0      | 0.010  | 0.099     | 0.001    |

Panel C: Auditor Independence

|  | Lobbyers |        |        |           | Non-Lobbyers |        |        |           | p-values |
|--|----------|--------|--------|-----------|--------------|--------|--------|-----------|----------|
|  | N        | Median | Mean   | Std. Dev. | N            | Median | Mean   | Std. Dev. |          |
| Market Capitalization (\$M)                              | 23       | 4,295  | 32,844 | 63,730    | 6,990        | 119    | 1,103  | 6,169     | 0.000    |
| Book-to-Market Ratio                                     | 21       | 0.644  | 4.100  | 9.856     | 5,881        | 0.647  | 1.392  | 3.420     | 0.000    |
| Agriculture, Forestry, And Fishing (SIC=0)               | 23       | 0      | 0      | 0         | 6,990        | 0      | 0.002  | 0.046     | 0.824    |
| Mining (SIC=1)   | 23       | 0      | 0      | 0         | 6,990        | 0      | 0.046  | 0.211     | 0.290    |
| Construction (SIC=2)                                     | 23       | 0      | 0.174  | 0.388     | 6,990        | 0      | 0.112  | 0.316     | 0.352    |
| Manufacturing (SIC=3)                                    | 23       | 0      | 0.261  | 0.449     | 6,990        | 0      | 0.226  | 0.418     | 0.689    |
| Transp., Commun., Elec., Gas, and Sanitary Serv. (SIC=4) | 23       | 0      | 0.043  | 0.209     | 6,990        | 0      | 0.080  | 0.271     | 0.518    |
| Wholesale Trade (SIC=5)                                  | 23       | 0      | 0.043  | 0.209     | 6,990        | 0      | 0.083  | 0.276     | 0.493    |
| Retail Trade (SIC=6)                                     | 23       | 0      | 0.391  | 0.499     | 6,990        | 0      | 0.264  | 0.441     | 0.166    |
| Finance, Insurance, And Real Estate (SIC=7)              | 23       | 0      | 0.087  | 0.288     | 6,990        | 0      | 0.139  | 0.346     | 0.469    |
| Services (SIC=8)   | 23       | 0      | 0      | 0         | 6,990        | 0      | 0.047  | 0.211     | 0.288    |
| Public Administration (SIC=9)                            | 23       | 0      | 0      | 0         | 6,990        | 0      | 0.000  | 0.012     | 0.954    |
| Governance Index   | 13       | 11     | 10.769 | 2.279     | 1,201        | 9      | 8.850  | 2.691     | 0.011    |
| Firm-level Lerner Competition Index                      | 19       | 0.899  | 0.891  | 0.134     | 5,129        | 0.967  | 1.627  | 5.093     | 0.529    |
| Industry-level Lerner Competition Index                  | 23       | 0.972  | 1.851  | 2.072     | 6,722        | 0.991  | 1.554  | 1.510     | 0.347    |
| Political Action Committee (PAC) (indicator)             | 23       | 1      | 0.565  | 0.507     | 6,990        | 0      | 0.075  | 0.264     | 0.000    |
| Past Lobbying on Compensation Rules (indicator)          | 23       | 0      | 0.174  | 0.388     | 6,990        | 0      | 0.011  | 0.104     | 0.000    |
| Past Lobbying on Proxy Rules (indicator)                 | 23       | 0      | 0.130  | 0.344     | 6,990        | 0      | 0.005  | 0.074     | 0.000    |
| Audit Fees in 2001 (\$M)                                 | 14       | 2.779  | 3.510  | 2.749     | 5,124        | 0.168  | 0.403  | 0.985     | 0.000    |
| Audit Fees over sales in 2001                            | 14       | 0.012  | 0.031  | 0.032     | 5,124        | 0.106  | 0.391  | 1.038     | 0.196    |
| Discretionary Accruals                                   | 13       | 0.000  | -0.003 | 0.097     | 3,711        | 0.002  | -0.001 | 0.115     | 0.959    |
| Restated Earnings (indicator)                            | 23       | 0      | 0.087  | 0.288     | 6,102        | 0      | 0.053  | 0.224     | 0.465    |
| Insider Sales Prior to Earnings Drop (indicator)         | 23       | 0      | 0.043  | 0.209     | 6,102        | 0      | 0.010  | 0.099     | 0.105    |

Table III:

### Predictability of Lobbying by Corporate Insiders

The table presents the results of probit analysis of the likelihood of a company lobbying against SOX-related SEC rule releases: the dependent variable is an indicator taking the value of one if the firm lobbied against one or more of the rules on Enhanced Financial Disclosure and PCAOB proposed and implemented by the SEC, and zero otherwise. Log of Market Capitalization is calculated at the end of week 6 of 2002 (Friday, February 8th); Book-to-Market Ratio is calculated using book equity for the fiscal year ending in 2001 and market equity for the end of week 6 of 2002 (Friday, February 8th); Governance Index is the firm's Gompers, Ishi and Metrick (2003) index calculated in year 2000 (Higher values of the governance index indicate more entrenched management and lower shareholder power); Firm-level Lerner Competition Index is  $(1 - \text{netincome}/\text{sales})$  calculated in year 2000; Industry Level Lerner Competition Index is  $(1\text{netincome}/\text{sales})$  calculated as the average across the entire firm level database in 2000, excluding each firm itself (see Bloom and Van Reenen, 2006); PAC is an indicator variable equal to one if the firm has a Political Action Committee that was registered with the Federal Election Commission's during the 1999-2000 period; Past Lobbying on Compensation Rules is an indicator variable if the firm has lobbied against the 1992 revision of executive compensation disclosure rules adopted by the SEC (See Lo, 2003); Past Lobbying on Proxy Rules is an indicator variable if the firm has lobbied against the new rules on proxy fights adopted by the SEC in 1992 (See Lo, 2003); the logarithm of the firm's audit fees are calculated in year 2001; Insider Sales Prior to Earnings Drop is an indicator variable equal to one if the CEO sold a large amount of his stocks within the 3 months prior to a large reported drop in earnings; Restated Earnings is an indicator variable if the firm restated its earnings in the period 1998-2001; Discretionary Accruals are calculated in year 2001 following Jones (2001) model. All tests use White (1980) heteroscedasticity-consistent robust standard errors.

|   | (1)                   | (2)                   | (3)                    | (4)                   | (5)                   | (6)                   | (7)                   | (8)                   | (9)                   | (10)                   |
|---|-----------------------|-----------------------|------------------------|-----------------------|-----------------------|-----------------------|-----------------------|-----------------------|-----------------------|------------------------|
| Log of Market Capitalization                        | 0.0094***<br>(0.0008) | 0.0315***<br>(0.0034) | 0.0016*<br>(0.0008)    | 0.0085***<br>(0.0007) | 0.0077***<br>(0.0007) | 0.0084***<br>(0.0007) | 0.0085***<br>(0.0007) | 0.0089***<br>(0.0010) | 0.0081***<br>(0.0009) | 0.0017***<br>(0.0007)  |
| Book-to-Market Ratio                                | 0.0010***<br>(0.0003) |                       |                        |                       |                       |                       |                       |                       |                       | 0.0002**<br>(0.0001)   |
| Governance Index                                    |                       | 0.0059***<br>(0.0021) |                        |                       |                       |                       |                       |                       |                       | 0.0003*<br>(0.0002)    |
| Firm-level Lerner                                   |                       |                       | -0.0071***<br>(0.0022) |                       |                       |                       |                       |                       |                       | -0.0086***<br>(0.0017) |
| Competition Index                                   |                       |                       |                        |                       |                       |                       |                       |                       |                       | -0.0002<br>(0.0003)    |
| Industry-level Lerner                               |                       |                       |                        |                       |                       |                       |                       |                       |                       | 0.0027<br>(0.0017)     |
| Competition Index                                   |                       |                       |                        |                       |                       |                       |                       |                       |                       | 0.0025<br>(0.0030)     |
| Political Action Committee<br>(PAC) (indicator)     |                       |                       |                        |                       | 0.0142***<br>(0.0053) |                       |                       |                       |                       | -0.0003<br>(0.0017)    |
| Past Lobbying on Compensation<br>Rules (indicator)  |                       |                       |                        |                       |                       | 0.0140<br>(0.0094)    |                       |                       |                       | 0.0002<br>(0.0003)     |
| Past Lobbying<br>on Proxy Rules (indicator)         |                       |                       |                        |                       |                       |                       | 0.0103<br>(0.0100)    |                       |                       | 0.0002<br>(0.0003)     |
| Log of Audit Fees in 2001                           |                       |                       |                        |                       |                       |                       |                       | 0.0016<br>(0.0015)    |                       | -0.0017<br>(0.0011)    |
| Insider Sales Prior<br>to Earnings Drop (indicator) |                       |                       |                        |                       |                       |                       |                       |                       | -0.0058<br>(0.0042)   | -0.0008<br>(0.0010)    |
| Restated Earnings<br>(indicator)                    |                       |                       |                        |                       |                       |                       |                       |                       | -0.0067**<br>(0.0031) | -0.0048<br>(0.0060)    |
| Discretionary Accruals                              |                       |                       |                        |                       |                       |                       |                       |                       | -0.0033<br>(0.0144)   |                        |
| Observations  | 6227                  | 1404                  | 5450                   | 7086                  | 7358                  | 7358                  | 7358                  | 5413                  | 3922                  | 7358                   |

Table IV:

**Abnormal Excess Returns During Period Leading Up to Passage of the Sarbanes-Oxley Act of 2002 and the Period from Passage to the End of 2004**

The table presents the abnormal excess returns for firms that lobbied against SOX related rules relative to non-lobbying firms. Panel A reports results for weekly excess returns averaged across lobbying firms. The first section of the table presents the results for firms that lobbied against enhanced financial disclosure and PCAOB rules; the second section of the table presents the results for firms that lobbied against corporate responsibility rules; the third section of the table presents the results for firms that lobbied against auditor independence rules. Excess returns are calculated for each lobbying firm by subtracting the return on a portfolio of non-lobbying firms of similar size (columns (1)-(4)) or of similar size and book-to-market equity (columns (5)-(8)) or of similar size and in the same 1-digit industry category (columns (9)-(12)). Excess returns are then averaged for each week across the set of lobbying firms. These average excess returns are then regressed either just on a constant or on a constant and the three market, size and book-to-market factors. This is done first for the 24-week period from week 7 to 30 of 2002 leading up to passage of SOX only (columns (1)-(2), (5)-6) and (9)-(10)) and then for the period starting with week 7 of 2002 and ending in the last week of 2004 (columns (3)-(4), (7)-(8), and (11)-(12)) with different constant terms allowed for the lead-up period and for the post-SOX period. Panel B reports results for the excess returns at the firm level. In the first three columns the dependent variable is the firm's excess return during the lead-up period, while in the last three columns is the firm's excess return in the post-SOX period. Lobbied Against Enhanced Financial Disclosure and PCAOB Rules is an indicator variable equal to one if the firm lobbied against the SEC rules related to SOX Section IV; Lobbied Against Corporate Responsibility Rules is an indicator variable equal to one if the firm lobbied against the SEC rules related to SOX Section III; Lobbied Against Auditors Independence Rules is an indicator variable equal to one if the firm lobbied against the SEC rules related to SOX Section IV. Log of Market Capitalization is calculated at the end of week 6 of 2002 (Friday, February 8th); Book-to-Market Ratio is calculated using book equity for the fiscal year ending in 2001 and market equity for the end of week 6 of 2002 (Friday, February 8th).

Panel A:

Dependent variable:  $r_t^{\text{Lobbying Firm Group}} - r_t^{\text{Matched Non-Lobbying Firm Group}}$

|  | Comparison Group<br>Based On 100 Size<br>Portfolios |                      |                       |                        | Comparison Group<br>Based On 25 Size And<br>5 Book-To-Market<br>Portfolios |                      |                       |                        | Comparison Group<br>Based On 25 Size And<br>10 1-Digit Industry<br>Portfolios |                      |                       |                        |
|--|---|----------------------|-----------------------|------------------------|--|----------------------|-----------------------|------------------------|---|----------------------|-----------------------|------------------------|
|  | (1)   | (2)                  | (3)                   | (4)                    | (5)  | (6)                  | (7)                   | (8)                    | (9)   | (10)                 | (11)                  | (12)                   |
| <b>Enhanced Financial Disclosure and PCAOB</b> |   |                      |                       |                        |  |                      |                       |                        |   |                      |                       |                        |
| $\alpha_{\text{Lead-Up}}$                      | 0.0056***<br>(0.0015)                               | 0.0043**<br>(0.0017) | 0.0056***<br>(0.0015) | 0.0048***<br>(0.0015)  | 0.0046***<br>(0.0014)  | 0.0034**<br>(0.0014) | 0.0046***<br>(0.0014) | 0.0039***<br>(0.0014)  | 0.0037***<br>(0.0011)   | 0.0034**<br>(0.0013) | 0.0037***<br>(0.0011) | 0.0035***<br>(0.0012)  |
| $\alpha_{\text{Post}}$                         |   |                      | -0.0001<br>(0.0005)   | 0.0003<br>(0.0004)     |  |                      | -0.0002<br>(0.0005)   | 0.0003<br>(0.0004)     |   |                      | -0.0000<br>(0.0004)   | 0.0001<br>(0.0003)     |
| $\beta_{\text{Market}}$                        |   | -0.0537<br>(0.0699)  |                       | -0.0879***<br>(0.0270) |  | -0.1016<br>(0.0597)  |                       | -0.1124***<br>(0.0243) |   | 0.0170<br>(0.0506)   |                       | -0.0255<br>(0.0212)    |
| $\beta_{\text{SMB}}$                           |   | 0.1246<br>(0.0727)   |                       | -0.1044***<br>(0.0361) |  | 0.0986<br>(0.0717)   |                       | -0.1019***<br>(0.0352) |   | 0.1193*<br>(0.0666)  |                       | -0.0523*<br>(0.0277)   |
| $\beta_{\text{HML}}$                           |   | 0.1213<br>(0.1609)   |                       | 0.0711<br>(0.0560)     |  | 0.0090<br>(0.1352)   |                       | -0.0089<br>(0.0515)    |   | 0.0477<br>(0.1114)   |                       | 0.0348<br>(0.0404)     |
| $N$ (Weeks)                                    | 24  | 24                   | 151                   | 151                    | 24   | 24                   | 151                   | 151                    | 24  | 24                   | 151                   | 151                    |
| $R^2$  | 0.379   | 0.511                | 0.125                 | 0.295                  | 0.323  | 0.490                | 0.097                 | 0.307                  | 0.336   | 0.421                | 0.105                 | 0.153                  |
| <b>Corporate Responsibility</b>                |   |                      |                       |                        |  |                      |                       |                        |   |                      |                       |                        |
| $\alpha_{\text{Lead-Up}}$                      | 0.0027<br>(0.0019)                                  | 0.0027<br>(0.0026)   | 0.0027<br>(0.0019)    | 0.0035*<br>(0.0021)    | 0.0026*<br>(0.0014)  | 0.0026<br>(0.0016)   | 0.0026*<br>(0.0014)   | 0.0033**<br>(0.0014)   | 0.0030*<br>(0.0016)   | 0.0033<br>(0.0020)   | 0.0030*<br>(0.0016)   | 0.0040**<br>(0.0017)   |
| $\alpha_{\text{Post}}$                         |   |                      | -0.0006<br>(0.0006)   | -0.0005<br>(0.0006)    |  |                      | -0.0012*<br>(0.0006)  | -0.0007<br>(0.0006)    |   |                      | -0.0010<br>(0.0006)   | -0.0007<br>(0.0006)    |
| $\beta_{\text{Market}}$                        |   | -0.0054<br>(0.0764)  |                       | 0.0365<br>(0.0297)     |  | -0.0765<br>(0.0539)  |                       | -0.0342<br>(0.0280)    |   | -0.0253<br>(0.0575)  |                       | 0.0220<br>(0.0281)     |
| $\beta_{\text{SMB}}$                           |   | -0.1883<br>(0.1957)  |                       | -0.2095***<br>(0.0501) |  | -0.2304<br>(0.1424)  |                       | -0.1985***<br>(0.0457) |   | -0.2009<br>(0.1618)  |                       | -0.2187***<br>(0.0487) |
| $\beta_{\text{HML}}$                           |   | 0.1485<br>(0.2142)   |                       | 0.0384<br>(0.0784)     |  | -0.0284<br>(0.1276)  |                       | -0.1534**<br>(0.0708)  |   | 0.0178<br>(0.1591)   |                       | -0.0657<br>(0.0705)    |
| $N$ (Weeks)                                    | 24  | 24                   | 151                   | 151                    | 24   | 24                   | 151                   | 151                    | 24  | 24                   | 151                   | 151                    |
| $R^2$  | 0.079   | 0.181                | 0.027                 | 0.153                  | 0.122  | 0.357                | 0.044                 | 0.216                  | 0.138   | 0.262                | 0.044                 | 0.199                  |
| <b>Auditor Independence</b>                    |   |                      |                       |                        |  |                      |                       |                        |   |                      |                       |                        |
| $\alpha_{\text{Lead-Up}}$                      | 0.0039*<br>(0.0019)                                 | 0.0038<br>(0.0023)   | 0.0039**<br>(0.0019)  | 0.0060**<br>(0.0024)   | 0.0046**<br>(0.0019)   | 0.0048*<br>(0.0026)  | 0.0046**<br>(0.0019)  | 0.0070***<br>(0.0025)  | 0.0031<br>(0.0020)  | 0.0031<br>(0.0025)   | 0.0031<br>(0.0019)    | 0.0050**<br>(0.0024)   |
| $\alpha_{\text{Post}}$                         |   |                      | -0.0003<br>(0.0010)   | -0.0003<br>(0.0009)    |  |                      | -0.0005<br>(0.0011)   | -0.0002<br>(0.0009)    |   |                      | -0.0001<br>(0.0009)   | 0.0001<br>(0.0009)     |
| $\beta_{\text{Market}}$                        |   | 0.0477<br>(0.0670)   |                       | 0.1156***<br>(0.0396)  |  | -0.0185<br>(0.0652)  |                       | 0.0611<br>(0.0419)     |   | 0.0392<br>(0.0718)   |                       | 0.0833**<br>(0.0413)   |
| $\beta_{\text{SMB}}$                           |   | -0.0124<br>(0.1320)  |                       | -0.1711**<br>(0.0721)  |  | -0.0307<br>(0.1293)  |                       | -0.1422*<br>(0.0808)   |   | -0.0246<br>(0.1393)  |                       | -0.2105***<br>(0.0799) |
| $\beta_{\text{HML}}$                           |   | 0.1630<br>(0.2028)   |                       | -0.1704*<br>(0.0990)   |  | -0.0722<br>(0.2431)  |                       | -0.4013***<br>(0.1119) |   | 0.1380<br>(0.2151)   |                       | -0.1446<br>(0.0951)    |
| $N$ (Weeks)                                    | 24  | 24                   | 151                   | 151                    | 24   | 24                   | 151                   | 151                    | 24  | 24                   | 151                   | 151                    |
| $R^2$  | 0.152   | 0.198                | 0.022                 | 0.159                  | 0.202  | 0.212                | 0.027                 | 0.208                  | 0.101   | 0.134                | 0.014                 | 0.136                  |

**Panel B:**

|  | Average weekly excess return<br>over the riskless rate<br>during the leadup period |                        |                        | Average weekly excess return<br>over the riskless rate<br>during the post period |                        |                        |
|--|--|------------------------|------------------------|--|------------------------|------------------------|
|  | (1)  | (2)                    | (3)                    | (4)  | (5)                    | (6)                    |
| I(Lobbied Against Enhanced Financial Disclosure and PCAOB Rules) | 0.0052***<br>(0.0009)  | 0.0057***<br>(0.0010)  | 0.0038***<br>(0.0009)  | 0.0002<br>(0.0005)   | -0.0000<br>(0.0005)    | 0.0005<br>(0.0005)     |
| I(Lobbied Against Corporate Responsibility Rules)                | 0.0011<br>(0.0012)   | 0.0013<br>(0.0014)     | 0.0016<br>(0.0012)     | -0.0003<br>(0.0004)  | -0.0002<br>(0.0005)    | -0.0004<br>(0.0004)    |
| I(Lobbied Against Auditor Independence Rules)                    | 0.0008<br>(0.0016)   | 0.0015<br>(0.0017)     | 0.0006<br>(0.0017)     | -0.0001<br>(0.0005)  | -0.0000<br>(0.0005)    | 0.0002<br>(0.0006)     |
| Log of Market Capitalization (\$M)                               | -0.0008***<br>(0.0002)   | -0.0009***<br>(0.0001) | -0.0008***<br>(0.0001) | -0.0005***<br>(0.0002)   | -0.0006***<br>(0.0002) | -0.0005***<br>(0.0002) |
| Book-to-Market Ratio   |  | 0.0001<br>(0.0001)     |                        |  | -0.0000<br>(0.0001)    |                        |
| Industry Dummies   | NO   | NO                     | YES                    | NO   | NO                     | YES                    |
| Observations   | 7252   | 6125                   | 7252                   | 6915   | 5915                   | 6915                   |
| R-squared  | 0.093  | 0.109                  | 0.149                  | 0.077  | 0.095                  | 0.083                  |

Table V:

### Changes in Operating Performance from 2001 to 2004

The table shows the results of firm level regressions of the change in operating performance from 2001 to 2004. The dependent variable is the the difference between operating income in 2004 and operating income in 2001 divided by the market value of equity at the start of the period (end of week 6 of 2002 (Friday, February 8th)). Operating income is COMPUTSTAT Item 13 (operating income before depreciation). Lobbied Against Enhanced Financial Disclosure and PCAOB Rules is an indicator variable equal to one if the firm lobbied against the SEC rules related to SOX Section IV; Lobbied Against Corporate Responsibility Responsibility Rules is an indicator variable equal to one if the firm lobbied against the SEC rules related to SOX Section III; Lobbied Against Auditors Independence Rules is an indicator variable equal to one if the firm lobbied against the SEC rules related to SOX Section IV. Log of Market Capitalization is calculated at the end of week 6 of 2002 (Friday, February 8th); Book-to-Market Ratio is calculated using book equity for the fiscal year ending in 2001 and market equity for the end of week 6 of 2002 (Friday, February 8th). In column (3) and (6) the regressions include 1-digit SIC code dummies. To reduce the influence of outliers, all regressions in the table drop observations in the top two or bottom two percent in terms of the dependent variable and (when included) in terms of the book-to-market equity ratio. Regressions that involve book equity are restricted to firms with positive book equity.

|  | Change in Operating Performance<br>Between 2001 and 2004 |                        |                        |
|--|--|------------------------|------------------------|
|  | (4)  | (5)                    | (6)                    |
| Lobbied Against Enhanced<br>Financial Disclosure and PCAOB Rules | 0.0532***<br>(0.0192)                                    | 0.0400**<br>(0.0181)   | 0.0593***<br>(0.0193)  |
| Lobbied Against Corporate Responsibility<br>Responsibility Rules | 0.0559**<br>(0.0219)                                     | 0.0407*<br>(0.0222)    | 0.0546**<br>(0.0215)   |
| Lobbied Against Auditors<br>Independence Rules                   | 0.0361<br>(0.0288)                                       | 0.0084<br>(0.0263)     | 0.0490<br>(0.0312)     |
| Log of Market Capitalization (\$M)                               | -0.0281***<br>(0.0021)                                   | -0.0137***<br>(0.0021) | -0.0284***<br>(0.0021) |
| Book-to-Market Ratio   |  | 0.0881***<br>(0.0113)  |                        |
| Constant   | 0.2537***<br>(0.0138)                                    | 0.1056***<br>(0.0170)  | 0.1525***<br>(0.0378)  |
| Industry Dummies   | NO   | NO                     | YES                    |
| Observations   | 4274   | 4018                   | 4274                   |
| R-squared  | 0.192  | 0.211                  | 0.209                  |

## Appendix A. Description of the Rules

The following table describes the main features of each rule adopted or proposed by the SEC, the date of proposing release, the date of adopting release if available, and whether the rule was adopted with or without amendments.

| Proposing Release Date                                      | Adopting Release Date   | Description  | Adopted/Pending/Not Adopted                          |
|---|---|--|--|
| <b>SOX Title II: Auditor Independence</b>                   |   |  |  |
| 12/2/2002<br>(No. 33-8154)                                  | 1/28/2003<br>(No. 33-8183)<br>Amended<br>3/26/2003 (No. 33-8183a) | Strengthening the Commission's Requirements Regarding Auditor Independence<br>Change the requirements regarding auditor independence to enhance the independence of accountants that audit and review financial statements and prepare attestation reports filed with the Commission. Include regulation related to non audit services. Prohibit partners on the audit engagement team from providing audit services to the issuer for more than five consecutive years.<br>[SOX: Section 201-207; Auditor Independence]   | Adopted<br>(with amendment)                          |
| <b>SOX Title III: Corporate Responsibility</b>              |   |  |  |
| 1/8/2003<br>(No. 34-47137)                                  | 4/9/2003<br>(No. 33-8220)   | Standards Relating To Listed Company Audit Committees<br>It requires national securities exchanges and national securities associations to prohibit the listing of any security of an issuer that is not in compliance in the audit committee requirements mandated by the Sarbanes-Oxley Act of 2002 (the independence of audit committee members, the audit committee's responsibility to select and oversee the issuer's independent accountant, procedures for handling complaints regarding the issuer's accounting practices, the authority of the audit committee to engage advisors; and funding for the independent auditor and any outside advisors engaged by the audit committee).<br>[SOX Section 301: Public Company Audit Committees] | Adopted (less restrictive) and then amended 8-Apr-03 |
| 6/17/2002<br>(No. 34-46079) Updated 8/2/2002 (No. 34-46300) | 8/29/2002<br>(No. 33-8124)  | Certification of Disclosure in Companies' Quarterly and Annual Reports<br>It requires an issuer's principal executive and financial officers each to certify the financial and other information contained in the issuer's quarterly and annual reports. The rules also require these officers to certify that: they are responsible for establishing, maintaining issuer's internal controls.<br>[SOX Section 302: Corporate Responsibility For Financial Reports]  | Adopted  |
| 3/21/2003<br>(No. 33-8212)                                  | 6/5/2003<br>(included in No. 33-8238)                             | Certification of Disclosure in Certain Exchange Act Reports<br>Extend requirements to provide the certifications required by Sections 302 and 906 of the Sarbanes-Oxley Act of 2002 to reports other than annual and quarterly reports.<br>[SOX Section 302: Corporate Responsibility For Financial Reports]<br>[SOX Section 906: Corporate Responsibility For Financial Reports]  | Adopted  |
| 10/18/2002<br>(No. 34-46685)                                | 5/20/2003<br>(No. 34-47890)                                       | Improper Influence On Conduct Of Audits<br>The rule has to implement the SOX prohibition to officers and directors of an issuer, and persons acting under the direction of an officer or director, from taking any action to fraudulently influence, coerce, manipulate or mislead the auditor of the issuer's financial statements for the purpose of rendering the financial statements materially misleading.   | Adopted  |

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| Proposing Release Date                                 | Adopting Release Date       | Description  | Adopted/Pending/Not Adopted             |
|--|-----------------------------|--|---|
|  |                             | [SOX Section 303: Improper Influence On Conduct Of Audits]   |   |
| 11/21/2002<br>(No. 33-8151)                            | 1/24/2003<br>(No. 33-8180)  | Retention of Records Relevant to Audits and Reviews<br>It requires accountants who audit or review an issuer's financial statements to retain certain records relevant to that audit or review for a period of seven years from the end of the fiscal year in which an audit or review was concluded.<br>[SOX Section 802: Criminal Penalties For Altering Documents]  | Adopted<br>(more restrictive)           |
| 11/6/2002<br>(No. 34-46778)                            | 1/22/2003<br>(No. 34-47225) | Insider Trades During Pension Fund Blackout Periods<br>It prohibits any director or executive officer of an issuer of any equity security from, directly or indirectly, purchasing, selling or otherwise acquiring or transferring any equity security of the issuer during a pension plan blackout period that temporarily prevents plan participants or beneficiaries from engaging in equity securities transactions through their plan accounts, if the director or executive officer acquired the equity security in connection with his or her service or employment as a director or executive officer.<br>[SOX Section 306: Insider Trades During Pension Fund Blackout]   | Adopted                                 |
| 11/21/2002<br>(No. 33-8150)                            | 1/29/2003<br>(No. 33-8185)  | Implementation of Standards of Professional Conduct for Attorneys: Up the Ladder Provision<br>Establishes an up-the-ladder reporting system for attorneys who appear and practice before the Commission on behalf of public companies. It requires attorneys to report evidence of a material violation of the securities laws, a material breach of a fiduciary duty, or a similar material violation by a company or any of its agents to its chief legal counsel (CLO) or to both its CLO and chief executive officer (CEO); and if the CLO or CEO does not respond appropriately to the evidence, report this evidence to the audit committee, other independent committee, or the board of directors.<br>[SOX Section 307: Rules Of Professional Responsibility For Attorneys]  | Adopted                                 |
| 1/29/2003<br>(No. 33-8186)                             | Pending                     | Implementation of Standards of Professional Conduct for Attorney: Noisy-Withdrawal<br>Requires that, in certain circumstances, an attorney withdraw from representing an issuer and report that withdrawal to the Commission.<br>[SOX Section 307: Rules Of Professional Responsibility For Attorneys]   | Pending                                 |
| Related NYSE And NASDAQ Rules (Not Part Of SOX Itself) |                             |  |   |
| 8/16/2002<br>(Original Proposal)                       | 11/4/2003<br>(No. 34-48745) | NYSE and NASD Rulemaking: New Standards And Changes In Corporate Governance And Practices Of Listed Companies<br>NYSE requires for each listed company: (1) that the board of directors consists of a majority of independent directors; (2) that the non-management directors should meet at regularly scheduled executive sessions without management; (3) to have a nominating/corporate governance committee composed entirely of independent directors; (4) to have a compensation committee composed entirely of independent directors; (5) to have a minimum three-person audit committee composed entirely of directors that meet the independence standards; (6) that the audit committee has a written audit committee charter; (7) to have an internal audit function; (8) to adopt and disclose corporate governance guidelines; (9) to adopt and disclose a code of business conduct and ethics for directors, officers and employees; (10) to have the CEO certify to the NYSE each year that he or she is not aware of any violation by the company of the NYSE's corporate governance listing standards. Similar rules for NASD. | Adopted<br>(with various modifications) |

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| <u>Proposing Release Date</u>   | <u>Adopting Release Date</u>               | <u>Description</u>   | <u>Adopted/Pending/Not Adopted</u>                        |
|---|--|--|---|
| 10/8/2002<br>(No. 34-46620)<br>Corrected<br>10/21/2002<br>(No. 34-46620A) | 6/30/2003<br>(No. 34-48108)                | NYSE and NASD Rulemaking: Shareholder Approval of Equity Compensation Plans and the Voting of Proxies<br>It requires shareholder approval of all equity-compensation plans and material revisions to such plans, subject to limited exemptions for issuers listed in NASD and NYSE   | Adopted   |
| <u>Related SEC Rules (Not Part Of SOX Itself)</u>                         |  |  |   |
| 10/14/2003<br>(No. 34-48626)  | Pending                                    | Security Holder Director Nominations<br>Require, under certain circumstances, that nominees of long-term security holders, or groups of long-term security holders, with significant holdings are included in company proxy materials.   | Pending   |
| <b>SOX Title IV And Title I: Enhanced Financial Disclosure And PCAOB</b>  |  |  |   |
| 5/10/2002<br>(No. 33-8098)  | None                                       | Disclosure In Management's Discussion And Analysis Of Critical Accounting Policies<br>Disclosure requirements that regard application of companies' critical accounting policies in two areas: accounting estimates a company makes in applying its accounting policies and the initial adoption by a company of an accounting policy that has a material impact on its financial presentation.<br>[SOX Section 401: Disclosure In Periodic Reports]   | Not Adopted<br>(proposed rule replaced by the rule below) |
| 11/4/2002<br>(No. 33-8144)  | 1/27/2003<br>(No. 33-8182)                 | Disclosure In Management's Discussion And Analysis Of Off-Balance Sheet Arrangements Contractual Obligations and Contingent Liabilities And Commitments<br>It requires disclosure of off-balance sheet transactions, arrangements, obligations, that have, or may have, a material effect on financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.<br>[SOX Section 401: Disclosure In Periodic Reports]  | Adopted   |
| 11/5/2002<br>(No. 33-8145)  | 1/22/2003<br>(No. 33-8176 and No. 33-8216) | Conditions For Use Of Non-GAAP Financial Measures<br>It requires public companies that disclose or release these non-GAAP financial measures to include, in that disclosure or release, a presentation of the most comparable GAAP financial measure and a reconciliation of the disclosed non-GAAP financial measure to the most comparable GAAP financial measure.<br>[SOX Section 401: Disclosure In Periodic Reports]  | Adopted   |
| 12/20/2002<br>(No. 33-8170)   | 5/7/2003<br>(No. 33-8230)                  | Mandated Electronic Filing and Website Posting for Forms 3, 4 and 5<br>It mandates the electronic filing, and website posting by issuers with corporate websites, of beneficial ownership reports filed by officers, directors and principal security holders<br>[SOX Section 403: Disclosures Of Transactions Involving Management And Principal Stockholders]  | Adopted   |
| 10/22/2002<br>(No. 33-8138)   | 6/5/2003<br>(No. 33-8238)                  | Disclosure Required By Section 404 Of Sarbanes-Oxley On Internal Controls<br>It requires issuers to include in their annual reports a report of management on the company's internal control over financial reporting including: a statement of management's responsibility for establishing and maintaining adequate internal control; management's assessment of the effectiveness of the company's internal control; a statement identifying the framework used to evaluate the effectiveness of the internal controls a statement that the registered public accounting firm that audited the company's financial statements has issued an attestation report on management's assessment of the company's internal control over financial reporting. The registered public accounting firm that audited the financial statements has issued an attestation report on management's assessment of the company's internal control over financial reporting. | Adopted   |

| Proposing Release Date  | Adopting Release Date   | Description   | Adopted/Pending/Not Adopted   |
|---|---|---|---|
| 10/22/2002<br>(No. 33-8138)                                       | 1/22/2003<br>(No. 33-8177)<br>Amended<br>3/26/2003 (No. 33-8177a) | [SOX Section 404: Management assessment of internal controls]<br><br>Disclosure Required By Sections 406 And 407 Of Sarbanes-Oxley On Audit Committee Financial Expert and Code of Ethics<br>It requires a company to disclose whether its audit committee includes at least one member who is a financial expert; also require disclosure of whether the company has adopted a code of ethics for its senior financial officers and if not why it has not done so.<br>[SOX Section 406: Code Of Ethics For Senior Financial Officers]<br>[SOX Section 407: Disclosure Of Audit Committee Financial Expert] | Adopted<br>(with amendment)   |
| 6/17/2002<br>(No. 33-8106)  | 3/16/2004<br>(No. 34-49424)                                       | Additional Form 8-K Disclosure Requirements And Acceleration Of Filing Date<br>Add eight more events that need to be reported on Form 8-K under the Securities Exchange Act of 1934. Also, transfer two items from the periodic reports and expand disclosures under two existing Form 8-K items.<br>[SOX Section 409: Real time issuer disclosures]  | Adopted<br>(less restrictive)   |
| <b>Related SEC Rules (Not Part Of SOX Itself)</b>                 |   |   |   |
| 8/8/2003<br>(No. 34-48301)  | 11/24/2003<br>(No. 33-8340)                                       | Disclosure Regarding Nominating Committee Functions And Communications Between Security Holders And Boards Of Directors<br>The rule enhances disclosure requirements regarding the operation of board nominating committees and introduces a new disclosure requirement concerning the means, if any, by which security holders may communicate with members of the board of directors.   | Adopted   |
| 4/12/2002<br>(No. 33-8090)  | None  | Form 8-K Disclosure Of Certain Management Transactions<br>It proposes that some public companies have to file current reports describing: directors' and executive officers' transactions in company equity securities, directors' and executive officers' arrangements for the purchase and sale of company equity securities, and loans of money to a director or executive officer made or guaranteed by the company or an affiliate of the company.   | Not Adopted<br>(proposed rule likely replaced by SOX rule No. 33-8106 listed above) |
| <b>Individual PCAOB Rules</b>                                     |   |   |   |
| 4/6/2004<br>(No. 34-49528)  | 5/14/2004<br>(No. 34-49707)                                       | PCAOB Auditing Standard No. 1<br>It requires registered public accounting firms to refer to the standards of the PCAOB in their audit reports, rather than to U.S. generally accepted auditing standards, or "GAAS."<br>[SOX Section 101: Establishment; administrative provisions]<br>[SOX Section 103: Auditing, quality control, and independence standards and rules]<br>[SOX Section 107: Commission oversight of the Board]   | Adopted   |
| 4/8/2004<br>(No. 34-49544) Corrected 4/13/2004<br>(No. 34-49544A) | 6/17/2004<br>(No. 34-49884)                                       | PCAOB Auditing Standard No. 2<br>Consists of an auditing standard applicable to audits of internal control over financial reporting of issuers by registered public accounting firms and five appendices containing example reports and additional guidance.  | Adopted   |

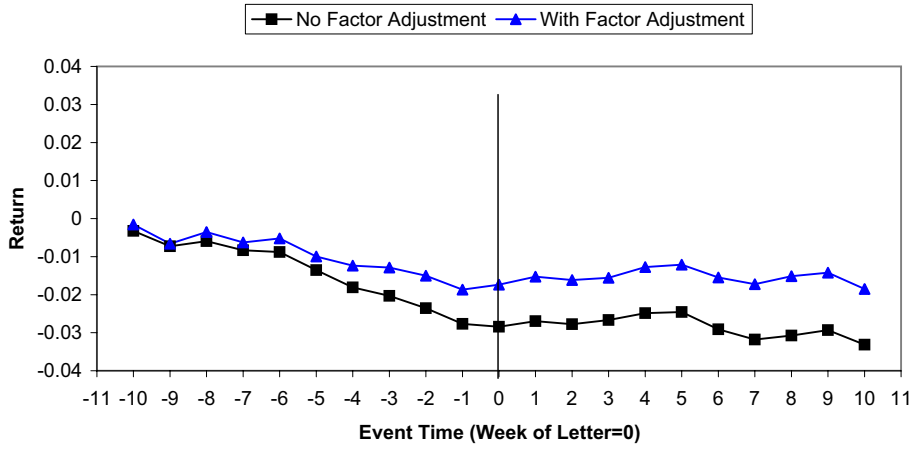
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| Proposing Release Date | Adopting Release Date | Description  | Adopted/Pending/Not Adopted |
|------------------------|-----------------------|--|-----------------------------|
|                        |                       | [SOX Section 103: Auditing, quality control, and independence standards and rules] |                             |
|                        |                       | [SOX Section 404: Management assessment of internal controls]                      |                             |

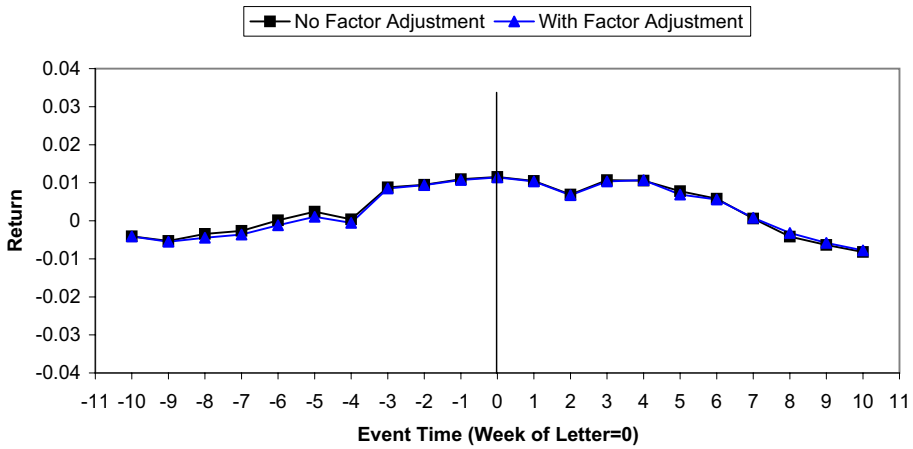
## Figure 1. Cumulative Excess Returns around Date of Filing Lobbying Letter with Negative Opinion

The figures show the cumulative excess returns for companies who lobby the SEC around the date of SEC receipt of the lobbying letter. Results are shown separately for firms lobbying against one of the SOX enhanced disclosure rules, corporate responsibility rules, and auditor independence rules, and are based exclusively on letters expressing negative opinions about the particular rule. In each graph, results are shown for two different definitions of excess returns. The lines labelled “No factor adjustment” are based on excess returns defined as (return on lobbying firm stock)-(return on a size-matched comparison group). The lines labelled “With factor adjustment” are based on excess returns defined as the residual from a regression (run on weekly data from week 31 of 2002 to the end of 2004) of (return on lobbying firm stock)-(return on size-matched comparison group) on a constant, the excess return on the market, and Fama and French’s the size and book-to-market factors SMB and HML. For each approach excess returns are averaged across lobbying firms for each week in event time, and then summed over time, starting 10 weeks before the week of the letter and ending 20 weeks after the week of the letter. Results are based only on letters filed at least 10 weeks after the passage of SOX on 7/30/2002 so that no point in the figures overlap with the period leading up to passage of SOX.

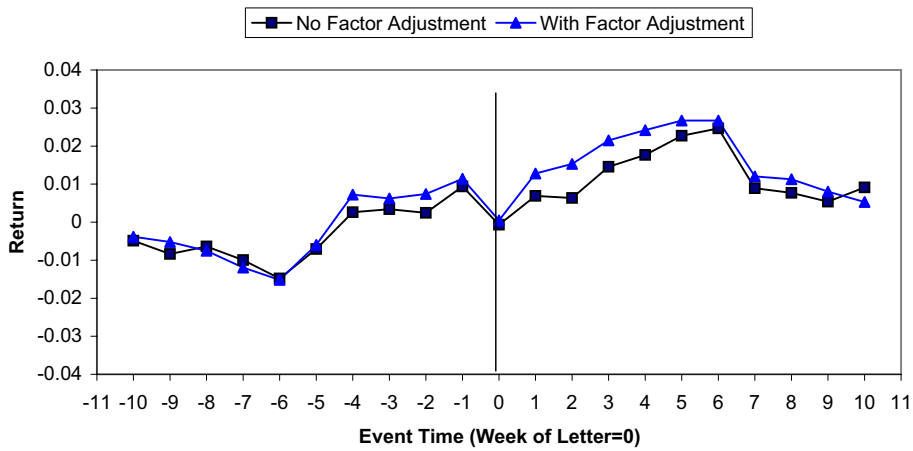
**Panel A: Enhanced Financial Disclosure [SOX Title IV and I]**



**Panel B: Corporate Responsibility [SOX Title III]**



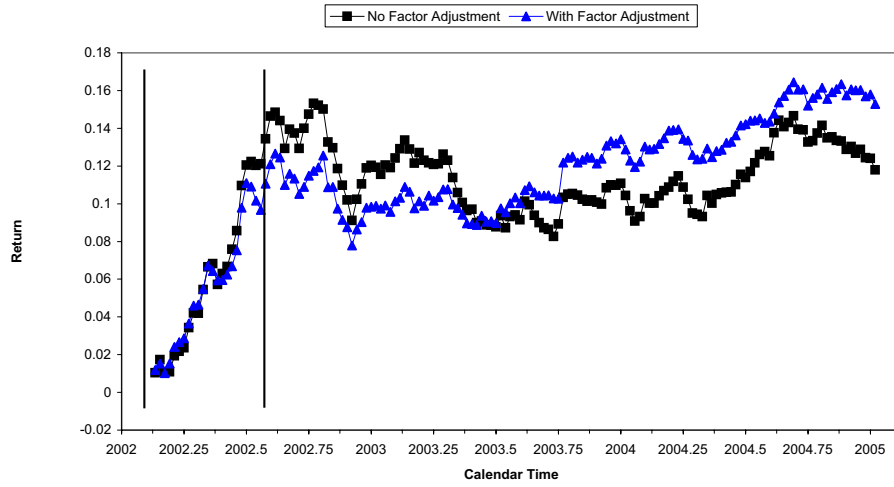
**Panel C: Auditor Independence [SOX Title II]**



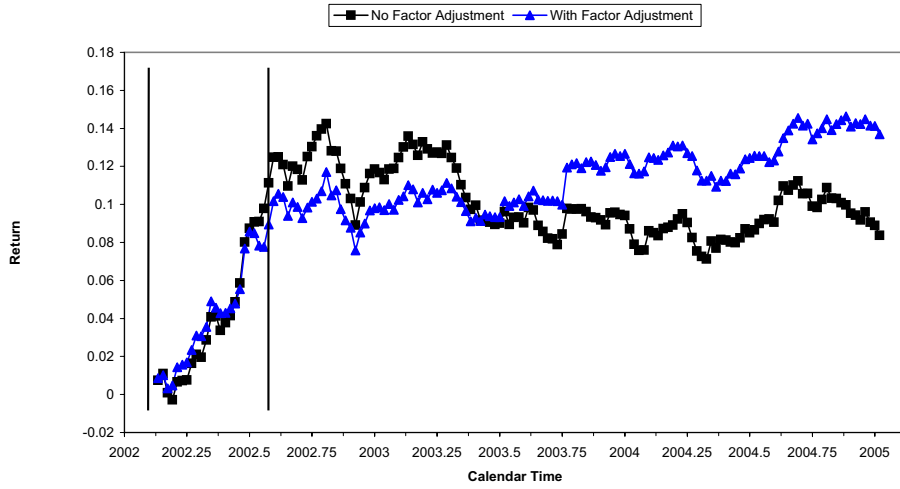
## Figure 2. Cumulative Excess Returns during Years 2002-2004 for Publicly Traded Firms that Lobbied the SEC

The figure shows the cumulative excess returns of firms lobbying firms against one or more of the 'Enhanced Disclosure' provisions of SOX over and above their matched comparison groups starting in week 7 of 2002. Three sets of cumulative excess returns are shown. Panel A is based on a size-matched (100 size portfolios) control group of non-lobbying firms. Panel B is based on a size and book-to-market equity (25 size portfolios and 5 book-to-market portfolios) matched control group. Panel C is based on a size and industry-matched (25 size portfolios and 10 industry portfolios) control group. In each graph, two lines are shown. The unadjusted cumulative excess return is calculated by averaging the excess returns over the comparison group across lobbying firms in each week, and then summing these excess returns over time, starting in week 7 of year 2002. The factor-adjusted cumulative excess return is calculated by first regressing the excess return over the comparison group on the excess return on the market and the Fama-French size and book-to-market factors. The regression is run using weekly data from week 7 of 2002 until the end of 2004, and the alpha plus the residuals are averaged each week and then summed over time. The leftmost vertical lines indicates the beginning of serious negotiations about SOX in Congress while the rightmost vertical line indicates the week SOX was passed in Congress.

Panel A: Comparison Group Based on 100 Size Portfolios



Panel B: Comparison Group Based on 25 Size Portfolios and 5 Book-to-Market Portfolios



Panel C: Comparison Group Based on 25 Size Portfolios and 10 1-Digit Industry Portfolios

