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The Politics of Bank Opacity

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ABSTRACT

The distribution of power in the political system shapes the financial reporting opacity of banks. Specifically, banks located in states with senators on the Senate Banking Committee (BC senators) have greater abnormal loan loss provisions than banks in other states. The result is stronger for larger banks and banks with higher risk. In addition, BC senators have a negative effect on the likelihood of banks in their home states receiving enforcement actions, and, more importantly, this effect is stronger for more opaque banks. These findings suggest that politicians, regulators, and banks use opaque financial reporting to facilitate regulatory forbearance. Moreover, we show that opacity is a significant channel through which BC senators increase bank risk. During economic downturns, however, BC senators appear to promote bank opacity to encourage bank lending and create liquidity. Finally, the capital market does not penalize the reporting opacity of banks in states with BC senators.

Keywords: Bank opacity, politicians, loan loss provisions, regulatory forbearance, real effects, market discipline

JEL Codes: G18, G21, G28, M41

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The distribution of power in the political system shapes the financial reporting opacity of banks. Specifically, banks located in states with senators on the Senate Banking Committee (BC senators) have greater abnormal loan loss provisions than banks in other states. The result is stronger for larger banks and banks with higher risk. In addition, BC senators have a negative effect on the likelihood of banks in their home states receiving enforcement actions, and, more importantly, this effect is stronger for more opaque banks. These findings suggest that politicians, regulators, and banks use opaque financial reporting to facilitate regulatory forbearance. Moreover, we show that opacity is a significant channel through which BC senators increase bank risk. During economic downturns, however, BC senators appear to promote bank opacity to encourage bank lending and create liquidity. Finally, the capital market does not penalize the reporting opacity of banks in states with BC senators.

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1. Introduction

The banking system is at the heart of a country's financial infrastructure, and the system's effective functioning is critical to resource allocation and economic stability and prosperity. Transparent financial reporting can promote the effective functioning of the banking system by facilitating corporate governance, government supervision, and market discipline (e.g., Acharya and Ryan, 2016; Bushman, 2014). Therefore, it is important to understand the potential factors that influence bank transparency or opacity. In this study, we examine whether and how politics affects bank financial reporting opacity.

The relation between financial institutions and political institutions is a central theme in the political economy literature. For example, Calomiris and Haber (2014) regard modern banking as a partnership between the government and a group of bankers. The authors argue that the partnership is shaped by the institutions that govern the distribution of power in the political system. They analyze the historical distribution of banking crises around the world and conclude that these crises, including the US subprime debacle of 2007–2009, originated from political institutions. Surprisingly, however, the accounting literature has paid little attention to how the political power shapes the financial reporting of banks. Our research fills this void.

This study explores the cross-sectional and time-series distribution of political power that governs the banking sector. In particular, we examine how the presence of a senator on the influential US Senate Committee on Banking, Housing, and Urban Affairs (i.e., Senate Banking Committee) affects the financial reporting opacity of banks headquartered in the senator's home state. The Senate Banking Committee has jurisdiction over matters related to banks and financial institutions, deposit insurance, monetary and credit policy, financial aid, and economic stabilization, among others.

According to congressional control theory (e.g., Weingast and Moran, 1983), the senators on the Senate Banking Committee (BC senators) can influence the actions of banking regulators via various monitoring, rewarding, and punitive mechanisms, such as budgetary appropriation confirmation and oversight and investigative hearings on the performance of banking regulators (McCubbins and Schwartz, 1984). BC senators can also influence bank regulators via their advice and consent power to confirm these officials (Kostovetsky, 2015; Short, 2021).

Bank failures can impose substantial negative externalities on the economy, especially the economy of the states where banks are located (e.g., Liu and Ngo 2014),[1] dimming the career prospects of politicians.[2] Due to political career concerns, BC senators have incentives to use their power to mitigate the negative consequences of bank failures in their home states. This can have two opposite effects on bank opacity. On one hand, to reduce the probability of bank failures in their home state, BC senators can pressure bank regulators to closely monitor those banks to ensure safe and sound banking practices. Since financial reporting quality is important in banking governance and monitoring, bank regulators will intervene with banks with opaque financial reporting (e.g., Costello, Granja, and Weber, 2019). This argument suggests that BC senators have a negative effect on the financial reporting opacity of banks in their home states.

On the other hand, BC senators may have a positive effect on bank opacity through the interactions of banks, senators, and regulators. During periods of financial distress, BC senators have incentives to press government officials to give preferential treatment to banks in their home states in the allocation of bailout funds. For example, during the

[1] For example, Liu and Ngo (2014) suggest that the costs associated with bank failures, such as losses to uninsured depositors and shareholders, bank job losses, and potential reductions in economic activity, are likely to be concentrated in the state where the failed banks operate.

[2] According to political science theory, voters' personal wealth concerns determine their voting behavior (e.g., Hibbing and Alford 1982). For example, voters experiencing economic losses from bank failure may blame and penalize the BC senators of their states for not ensuring effective regulatory oversight on those failed banks.

2007–2009 financial crisis, powerful politicians appeared to use their leverage to direct millions of Troubled Asset Relief Program (TARP) money toward banks in their home states (e.g., Paletta and Enrich, 2009). Anticipating BC senators' strong ability and incentive to save them during financial distress, banks will take more risks, which might be considered excessive by regulators or market participants (e.g., Kostovetsky, 2015). To shield themselves from disciplinary actions by the regulators or the market, these banks have incentives to make their financial reports more opaque (Acharya and Ryan, 2016; Beatty and Liao, 2014; Bushman, 2014). Moreover, interest group theory suggests that banks might influence BC senators to impose political pressure on bank regulators to practice forbearance once the banks get into trouble (e.g., Brown and Dinç, 2005). In 1987, for instance, several senators successfully urged bank regulators to back off taking enforcement actions against a California-based bank, Lincoln, which had violated federal regulations because of rapid, high-risk growth.[3] In this scenario, BC senators and regulators both prefer banks to be more opaque, to prevent market participants and taxpayers from detecting and constraining regulatory forbearance (Bushman and Landsman, 2010; Gallemore, 2021; Kane, 1989). Essentially, bank opacity is a tool used by politicians, regulators, and banks to collude and disguise loosening regulatory discipline over bank risk taking.

We empirically test the effects of BC senators on bank opacity. To measure bank opacity, we focus on loan loss provisions, which are accounting estimates of loan losses. Loan loss provisions are the largest accruals of banks and the most important mechanism for banks for managing earnings and regulatory capital (Beatty and Liao, 2014; Huizinga and Laeven, 2012). Following prior literature (e.g., Jiang, Levine, and Lin, 2016), we estimate discretionary loan loss provisions as the residual from Beatty and Liao's (2014) preferred loan loss provision model. Our first measure of bank opacity is the absolute

[3] Appendix A provides a detailed case study of the enforcement actions on Lincoln.

value of quarterly discretionary loan loss provisions. To address the potential measurement issue from accrual reversal and seasonal effects, we construct a second measure of opacity as the moving sum of discretionary loan loss provisions over the past four quarters, in the spirit of Hutton, Marcus, and Tehranian (2009).

Using a large sample of bank–quarters over the period 1995 to 2017, we find that banks headquartered in states with BC senators have significantly higher levels of discretionary loan loss provisions than their peers in states without BC senators. The results are robust to controlling for firm and time fixed effects, as well as various time-varying firm- and state-level characteristics. Moreover, in a difference-in-differences analysis exploiting plausibly exogenous departures of BC senators, we show that bank opacity decreases after banks experience the loss of BC senators. In cross-sectional analyses, we find that the effect of BC senators on bank opacity is more pronounced for banks that are larger, suggesting that senators care more about the fate of economically important banks in their home states. The impact of BC senators on bank opacity is also stronger for banks with larger increases in financial leverage and higher stock volatility, suggesting that banks with higher risks have stronger incentives to conceal their risk-taking behavior.

We next examine regulatory forbearance as the potential mechanism behind the positive relation between BC senators and bank opacity. Consistent with our argument and anecdotal evidence that BC senators have the ability and incentive to pressure regulators to practice forbearance, we find that banks headquartered in states with BC senators have a lower likelihood of being the subject of formal enforcement actions. More importantly, we show that the impact of BC senators on the likelihood of enforcement actions is stronger for banks with more opaque financial reporting, suggesting that bank opacity facilitates regulatory forbearance by inhibiting outside monitoring. Interestingly, however, we find that opaque banks located in states without BC senators are more likely

to be subject to enforcement actions, suggesting that opacity alone is unlikely to be effective in avoiding regulatory enforcement, possibly because regulators are sophisticated enough to see through banks' efforts to manage earnings and regulatory capital.

The political influence of individual BC senators is likely to be heterogeneous (e.g., Gropper, Jahera, and Park, 2013). Although the US Constitution does not mandate differences in rights, Senate rules give more power to senators with more seniority (e.g., Goodwin, 1959). For example, senior senators have priority in choosing committee assignments, and the committee chairpersonship is traditionally given to the most senior senator of the majority party serving on the committee, so long as the senator is not already holding the chairpersonship of another committee. Moreover, a leadership analysis of congresspersons suggests that more senior members of Congress tend to have higher leadership scores, defined as the frequency of other congressional members cosponsoring their bills (Tauberer, 2012).[4] Consistent with senior senators wielding more political clout, we find that senior BC senators have a stronger effect on bank opacity than other BC senators, particularly when these senior senators hold the chairpersonship of the Senate Banking Committee. Regarding bank enforcement actions, we show that the interactive effect of BC senators and opacity on formal enforcement actions is more pronounced for senior BC senators who hold the committee chairpersonship. These results add further credence to our theory that political clout affects bank opacity.

Loosened regulatory oversight and handicapped market discipline can encourage imprudent lending and make banks in BC senators' home states less sound. Consistent with this conjecture, we find that banks headquartered in states with BC senators have a significantly higher risk of insolvency and more actual loan losses than their peers in

[4] The idea behind a leadership score is that if X cosponsors Y's bills but Y does not cosponsor X's bills, then X is a follower relative to Y being a leader.

states without BC senators. More importantly, using a path analysis, we show that opacity is an important channel through which BC senators affect bank real outcomes.

Although bank transparency is central to market and nonmarket discipline over bank risk taking in economic good times, academics and policy makers argue that financial reporting opacity in bad economic conditions can be helpful in mitigating bank runs, encouraging bank lending, and maintaining financial stability (Acharya and Ryan, 2016; Leuz, 2009). Therefore, if BC senators hold similar ideas, they should have stronger incentives to promote bank opacity during economic downturns. To provide evidence for this argument, we examine how the impact of BC senators on bank opacity varies with measures of economic conditions. We find that the impact of BC senators on bank opacity is more pronounced during periods of recession with inadequate capital supply, poor state economy, and a weaker state banking sector. Moreover, we find that, during difficult economic conditions, the growth of the loan supply is greater in states with BC senators than in those without. Taken together, it appears that bank opacity in states with BC senators leads to greater credit supply during economic downturns.

In a final analysis, we find that the adverse effect of bank opacity on credit ratings and bond spreads is significantly weaker for banks located in states with BC senators, suggesting that the opaque financial reporting of these banks is penalized to a lesser extent or not at all by the capital market. One potential interpretation of this result is that market participants, particularly creditors, expect these banks to be bailed out should they encounter financial difficulties. Therefore, they have fewer incentives to monitor bank risk taking and rely less on financial reports.

Our results contribute to the literature on bank transparency or opacity, which has attracted renewed attention due to the 2007–2009 financial crisis. The results reported by Bushman and Williams (2015) imply substantial cross-sectional and time-series

variations in the quality of bank financial reporting. Beatty and Liao (2014) and Bushman (2014) call for more research on the determinants of bank accounting quality. Recent studies have examined the effects of auditing and internal controls (Altamuro and Beatty, 2010; Kanagaretnam, Krishnan, and Lobo, 2010; Nicoletti, 2018), corporate governance and ownership structure (Nichols, Wahlen, and Wieland, 2009; Vyas, 2011), bank regulation and credit competition (Bushman, Hendricks, and Williams, 2016; Dou, Ryan, and Zou, 2018; Jiang et al., 2016), asset quality (Huizinga and Laeven, 2012), and national culture (Kanagaretnam, Lim, and Lobo, 2013) on bank reporting quality. Our research contributes to this growing and important literature by documenting how the distribution of political power shapes bank opacity. Moreover, we explore the important interrelations among politicians and their political clout, regulatory forbearance, bank opacity, and financial stability (Acharya and Ryan, 2016; Gallemore, 2021). Given the significant role of politics and regulation in the banking sector, our study represents a meaningful addition to the literature.

Our study also adds to the accounting and finance literature that examines the effect of politics or politicians on firm behavior or outcomes (e.g., Chaney, Faccio, and Parsley, 2011; Gropper et al., 2013; Hope, Yue, and Zhong, 2020; Kim and Zhang, 2016; Kostovetsky, 2015; Lambert, 2019; Mehta, Srinivasan, and Zhao, 2020; Mehta and Zhao, 2020; Papadimitri et al., 2021). While most of these studies focus on nonfinancial firms, some recent studies examine how politics impacts bank decisions or real outcomes. Gropper et al. (2013) and Papadimitri et al. (2021) show that banks in states with a congressperson serving as the chairman of the congressional banking committees have better performance and a lower probability of receiving formal enforcement actions, respectively. Kostovetsky (2015) focuses on BC senators and find that BC senators have a positive effect on the risk exposure of banks. However, during the 2008 financial crisis, BC senators are (weakly) associated with improved stock returns and reduced bankruptcy

probability. Our study extends this line of research by examining the effect of politics on banks' financial reporting opacity. Moreover, we show that bank opacity is an important channel through which BC senators affect bank real outcomes.

In a closely related study, Chaney et al. (2011) examine the effect of politicians on financial reporting quality. However, our research is different in several important dimensions. First, Chaney et al. focus on firms' choice of establishing connections with the government by hiring past politicians, whereas our study explores the distribution of power of incumbent politicians, largely exogenous to firm decisions. Second, Chaney et al. examine non-US nonfinancial firms, the results of which are unlikely generalizable to US financial firms because of the unique political environment of the United States and the unique status of the banking system in the economy. Finally, our study offers more insights on how politicians impact regulatory forbearance and banks' real decisions.

2. Institutional background

In this section, we first review the political science literature on the mechanisms of congressional control of regulators' decision making. Then, we develop our empirical predictions and provide anecdotal evidence of individual BC senators' interference in bank enforcement and bailouts.

2.1 The politics of regulation

The creation and enforcement of regulations are the joint product of actions by various decision makers in government agencies, legislatures, and executive offices, as well as representatives from business and nongovernmental organizations (Carrigan and Coglianese, 2011). An important stream of the political science literature examines the relationships between electorally accountable institutions and the unelected, ostensibly autonomous regulators who draft and enforce binding rules. In particular, the so-called new institutionalism or congressional control theory focuses on the mechanisms by which

Congress seeks to control the actions of regulatory agencies. According to the theory, politicians can exercise control over regulators through oversight mechanisms within the congressional committee system (e.g., McCubbins and Schwartz, 1984).

In particular, congressional oversight committees can influence regulatory agencies by a variety of subtle control devices (e.g., Short, 2021; Weingast, 1984). First, regulatory agencies have incentives to expand or maintain their programs, which require congressional support in terms of budgets and rulings. Therefore, these agencies have incentives to accommodate requests from politicians on congressional oversight committees in exchange for budgetary or legislative favors. Second, congressional committees have numerous avenues for direct regulatory intervention. Armstrong (1959), Cary (1967), and Fenno (1973), among others, document substantial costs of congressional harassment during congressional hearings and investigations of various regulatory agencies. These ex post sanctions create ex ante incentives for bureaucrats to serve the needs of the congressperson. Finally, and perhaps most importantly, the congressional oversight committees control the appointment, reappointment, and replacement of the leadership at regulatory agencies.[5] Politicians on these committees are more likely to support the appointment of top bureaucratic officials who have greater ex ante potential to provide them political favors. Moreover, the threat of ex post replacement provides bureaucrats with ex ante incentives to satisfy the interests of powerful congresspersons due to career concerns. As Barke and Riker (1982, 78) note, "[administrators'] best chance of success, therefore, lies in proper obedience to legislative directives. Whatever ultimate objectives administrators may have, their immediate instrumental goal is probably that of pleasing or at least of not displeasing their constitutional masters."

[5] Besides confirmation hearings, Congress also plays a crucial role in selecting the nominees in most cases (Weingast and Moran, 1983).

The empirical evidence in the political science literature generally supports the view that there is substantial congressional influence over the implementation and enforcement of regulations.[6] For example, Weingast and Moran (1983) show that the turnover in relevant congressional committees had a significant impact on the Federal Trade Commission's antitrust enforcement in the 1970s. Wood and Waterman (1991) find that congressional oversight and appropriation decisions are important predictors of the activity levels at the Environmental Protection Agency. Shipan (2004) shows that the volume of Food and Drug Administration inspections over a 50-year period ending in 1995 was substantially impacted by the ideological views of the relevant congressional oversight committee. Mehta et al. (2020) show that congresspersons serving on committees with antitrust regulatory oversight constrain the ability of antitrust regulators to provide independent antitrust reviews of merger transactions. Overall, there appears to be broad consensus in the political science literature that politics matter in regulatory enforcement and compliance (Haines, 2011; Short, 2021).

2.2 Bank regulation: Politicians, regulatory forbearance, and bank opacity

Bank regulation and supervision are critical tools for the promotion of stability and soundness in the financial sector. In the United States, banking is regulated and supervised at both the federal and state levels. Depending on the type of charter and organizational structure of a banking organization, its primary federal regulator could be the Federal Reserve Board (Fed), the Federal Deposit Insurance Corporation (FDIC), or the Office of Comptroller of the Currency (OCC). For example, the primary federal regulator for federally charted banks is the OCC, and the primary federal regulator for state-charted banks is the Fed (for Fed-member banks) or the FDIC (for non-Fed member banks). The Fed is also the primary federal regulator for all bank holding companies.

[6] See Carrigan and Coglianese (2011) and Short (2021) for a review of the literature.

State-charted banks are also subject to the regulations of the state in which they were chartered, in addition to federal regulations.

The main objective of bank regulation and supervision is to ensure banks follow safe and sound banking practices and comply with banking laws and regulations. Specifically, banking supervision involves activities such as evaluating risk management process, assessing internal controls, and identifying risks to a bank's continued financial health and viability (Hirtle, Kovner, and Plosser, 2020). More importantly, bank supervision includes taking actions to ensure that problematic banks remediate deficiencies, such as imprudent lending practices, in the form of informal private or formal public enforcement actions or to close the banks if the deficiencies are irremediable.

Although the intention of enforcement actions is to correct unsafe or unsound practices and prevent future (systematic) bank failures, these actions can impose substantial costs on individual banks, such as growth or expansion constraints, direct costs of revamping risk management and control systems, loss of reputation and market value, and even bank runs (Boot and Thakor, 1993; Eisenbach et al., 2017; Morrison and White, 2013; Pereira et al., 2019; Slovin, Suskha, and Polonchek, 1999). For example, in a recent enforcement action, the Fed capped Wells Fargo's growth for three years, and the bank has spent billions of dollars remaking its risk and control system (Eisen, 2021). Therefore, banks have incentives to interfere in the regulatory process to avoid formal enforcement actions and the associated costs. For example, Lambert (2019) finds that banks actively lobby regulators to shield themselves from the costs associated with enforcement actions.

According to congressional control theory, Congress tends to use a fire-alarm mechanism of oversight, which relies on interest groups to alert politicians on relevant committees when problems arise in the regulatory process, to focus members' attention

on the most important constituents (McCubbins and Schwartz, 1984). Therefore, banks, as important interest groups, could obtain preferential regulatory treatment by seeking help from their connected committee members who have power to impose political pressure on regulators. Numerous studies on congressional distributive politics suggest that re-election–minded congresspersons serving on relevant committees have substantial incentives to ensure that regulatory agencies provide benefits to their constituents in their home states (e.g., Atlas et al., 1995; Hoover and Pecorino, 2005; Weingast, 1984).

In the context of bank regulation, the relevant congressional committees include the Senate Banking Committee and the US House Committee on Financial Services. In this study, we focus our attention on the Senate Banking Committee, mainly because senators, relative to representatives, have exclusive confirmation power in the presidential appointment of the leadership at regulatory agencies, such as the governors of the Fed.[7] According to the political science literature, the most important channel of congressional control is via the appointment and reappointment of agency leaders (Weingast and Moran, 1983). Moreover, individual senators are generally considered more powerful and influential than individual representatives, because of the smaller number of senators in Congress and their relatively longer terms and higher seniority.[8] For example, Hoover and Pecorino (2005) show that states with higher Senate representation, rather than House representation, receive more federal spending per capita. In addition, prior studies find that the Senate Banking Committee has a stronger influence on monetary policies than the House Committee on Financial Services (e.g., Grier, 1991).

[7] See https://www.banking.senate.gov/legislative-calendar/nominations.
[8] The Senate Banking Committee has an average of 20 members.

Drawing on the theory and empirical evidence in the political science literature, we argue that BC senators have both the incentive and ability to facilitate regulatory forbearance on troubled banks in their home states. However, due to the largely behind-the-scenes nature of political intervention, it is often difficult to observe direct evidence of BC senators' influence over bank supervision, particularly enforcement actions. Fortunately, a relatively egregious case revealed during the savings and loan crisis of the 1980s and 1990s provides a lens to examine evidence of political intervention. In the case detailed in Appendix A, several senators successfully convinced bank regulators to back off taking enforcement actions against a California-based bank, Lincoln, which had violated a rule limiting the risky investment practices of savings and loan companies in the 1980s. In Lincoln's case, Alan Cranston, the then Democrat Senator of California and a senior member of the Senate Banking Committee, played the leading role in imposing political pressure on bank regulators to exercise regulatory forbearance.

Although bank regulators can bend to the political pressure of BC senators and agree to practice forbearance, some non-regulator bank stakeholders (e.g., depositors, creditors, shareholders, employees, financial analysts, and taxpayers in general) can take actions to hinder a regulator's ability to successfully practice forbearance if they observe a bank's deteriorating financial situation (e.g., Bushman, 2014; Bushman and Landsman, 2010; Gallemore, 2021; Huizinga and Laeven, 2012; Rochet, 2005). Therefore, BC senators, regulators, and banks have incentives to increase bank opacity and undermine non-regulator monitors' ability to understand a bank's true financial situation and limit regulatory forbearance. In a sense, bank opacity is an essential tool used by politicians, regulators, and banks to collude in practicing forbearance. For example, during the savings and loan crisis, it is reported that authorities were tempted to become accessories in a cover-up scheme with insolvent institutions to disguise adverse information (Kane, 1989). Empirically, Gallemore (2021) shows that financial reporting opacity facilitates

regulatory forbearance. Therefore, we expect that banks in states with BC senators are likely to produce opaque financial reports to shield themselves from non-regulator stakeholders' or the market's discipline for excessive risk taking and to facilitate forbearance.

2.3 Politics of bank bailout and bank opacity

Banks tend to take risks that are higher than socially optimal levels due to the externality of bank failures and the expectation of government bailouts. Although the goal of government bailouts is generally to help banks that are important and healthy enough to survive and lend, the actual process of deciding which banks will receive cash is often secretive and opaque. During the 2007–2009 financial crisis, powerful politicians appeared to have used their leverage to direct millions of federal funds toward banks in their home states (e.g., Paletta and Enrich, 2009). For example, 12 Ohio banks received funds after Ohio's congressional delegation sent dozens of letters to Comptroller of the Currency John Dugan and Treasury Secretary Henry Paulson and threatened to hold hearings on how the Treasury had supposedly wrecked a bank they said was not in immediate danger of collapsing. In contrast, in neighboring Michigan, which was hurt similarly by the crisis, only two banks received federal infusions.[9] Although it is difficult to prove a direct link between powerful politicians and the allocation of bailout funds, some banking officials appear to believe it exists. For example, John Harrison, Alabama's banking superintendent, said that Alabama Senator Richard Shelby, the ranking Republican on the Senate Banking Committee, "has been a big proponent for Alabama state-charted banks … and he was really concerned that the TARP money went here" (Paletta and Enrich, 2009). In the political economy literature, there is substantial evidence that powerful politicians have the incentive and ability to direct government

[9] Senator Sherrod Brown from Ohio was a BC senator in the 111th Congress. There was no BC senator from Michigan, although two Michigan representatives were serving on the House Committee on Financial Services.

investments to their home states (e.g., Atlas et al., 1995; Cuny, Kim, and Mehta, 2020; Duchin and Sosyura, 2012; Hoover and Pecorino, 2005; Levitt and Porterba, 1999).

Expectations of preferential treatment in government bailout programs during periods of financial distress can encourage banks in states with BC senators to take more risks (e.g., Kostovetsky, 2015). To insulate themselves from disciplinary actions by regulators or non-regulator stakeholders, these banks have incentives to make their financial reports more opaque. However, we argue that regulators are likely to be able to see through the opacity because of their various monitoring activities, such as on-site inspections. Therefore, it is more likely that bank regulators, with political pressure from BC senators, cooperate with banks in using opaque financial reports to alleviate outside stakeholders' and taxpayers' scrutiny of bank risk taking.

3. Data and measurements

3.1 Sample and data

Our primary sample contains all Compustat banks with necessary quarterly data during the period of 1995 to 2017.[10] In the main analyses of discretionary loan loss provisions, we use a sample of 43,034 bank–quarter observations that represent 1,560 banks with non-missing control variables. The sample sizes in the other analyses vary due to data availability. We obtain stock return data from the Center for Research in Security Prices and bond pricing data from the WRDS Bond Database.[11]

[10] To estimate discretionary loan loss provision measures, we require banks to have information for all variables in the loan loss provision model. In addition, we require bank-quarter observations have nonnegative total assets or book value of equity (e.g., Laux and Rauter, 2017).

[11] The WRDS Bond Database provides cleaned datasets of corporate bond transactions, sourced from TRACE Standard and TRACE Enhanced datasets, along with a separate dataset for monthly price, return, coupon, and yield information for all corporate bonds traded since July 2002. Importantly, this database provides a unique and essential linking table that maps all bonds and equity issues for all firms.

We manually collect the historical data on the membership of the Senate Banking Committee from the annual volumes of the Official Congressional Directory.[12] The Congressional Directory lists the names and home states of each senator on each Senate committee. We collect information from the 104th to the 115th Congress, which corresponds to the years 1995 to 2017. For each bank–quarter observation, we set the dummy variable *SENATOR* as equal to one if the bank is headquartered in a state with a BC senator in that year–quarter, and zero otherwise. Figure 1 presents the time-series distribution of BC senators by state. During the 104th to 115th Congress, seven states never had a senator serving on the Senate Banking Committee, whereas one state (Alabama) always had one. Therefore, most states experienced changes in BC senator status during our sample period. Rhode Island had two BC senators (Senators Lincoln D. Chafee and Jack Reed) in the 108th Congress, and both Alabama (Senators Richard Shelby and Doug Jones) and Nevada (Senators Dean Heller and Catherine Cortez Masto) had two senators in the 115th Congress. Thus, it is rare for a state to have two BC senators in the same Congress. Panel A of Table 1 presents the sample distribution by state, together with the mean value of *SENATOR*. In Panel A, there is no clear pattern that our sample is concentrated in states with BC senators, except for New York, which contributes 3,020 observations to the full sample and had a BC senator during most of the sample period.[13]

We obtain information for bank enforcement actions from Standard & Poor's (S&P) Global Market Intelligence's SNL Bank Regulatory dataset. State-level variables are collected from various sources. The returns on the Case-Shiller Real Estate Index are from Robert Shiller's website (http://www.econ.yale.edu/~shiller/data.htm), the gross domestic

[12] The directory can be found at the US Government Publishing Office website at https://www.gpo.gov/fdsys/browse/collection.action?collectionCode=CDIR&browsePath=113%2F2014-02-18%2FF1&isCollapsed=false&leafLevelBrowse=false&isDocumentResults=true&ycord=351.

[13] All results are robust if we drop banks from New York.

product (GDP) data are from the Bureau of Economic Analysis, and the unemployment data are from Bureau of Labor Statistics.

3.2 Measurement of bank opacity

Following the banking literature (e.g., Beatty and Liao 2014; Jiang et al. 2016), we measure bank opacity based on discretionary loan loss provisions. Loan loss provisions are accounting estimates of loan losses. According to Beatty and Liao (2014), loan loss provisions are the most important bank accruals that managers use to manage earnings or circumvent capital adequacy requirements. Discretionary loan loss provisions are also the primary focus of the literature that examines the financial reporting quality of banks. Specifically, we estimate the following loan loss provision model:

$$\begin{aligned} LLP_t = & \propto_0 + \propto_1 \Delta NPA_{t+1} + \propto_2 \Delta NPA_t + \propto_3 \Delta NPA_{t-1} + \propto_4 \Delta NPA_{t-2} + \propto_5 SIZE_{t-1} + \\ & \propto_6 \Delta LOAN_t + \propto_7 SENATOR_t + \propto_8 SENATOR_t \times \Delta NPA_{t+1} + \propto_9 SENATOR_t \\ & \times \Delta NPA_t + \propto_{10} SENATOR_t \times \Delta NPA_{t-1} + \propto_{11} SENATOR_t \\ & \times \Delta NPA_{t-2} + \propto_{12} SENATOR_t \times SIZE_{t-1} + \propto_{13} SENATOR_t \\ & \times \Delta LOAN_t + \propto_{14} CSRET_t + \propto_{15} \Delta GDP_t + \propto_{16} \Delta UNEMP_t + STATE + \varepsilon_t \end{aligned} \quad (1)$$

where the dependent variable (LLP_t) is loan loss provisions, scaled by lagged total loans, and ΔNPA_t is the change in nonperforming assets from quarters t - 1 to t, divided by total loans in quarter t - 1. Following Bushman and Williams (2012), we include the changes in nonperforming assets in the current quarter, the next quarter, and the previous two quarters. The logic is that banks might use current, forward-looking, and historical information on nonperforming assets when determining loss provisions. The variable $SIZE_{t-1}$ is the natural logarithm of total assets in quarter t - 1. The strength of regulation may vary with bank size. The term $\Delta LOAN_t$ is the change in total loans over quarter t, scaled by total loans in the last quarter. Banks with rapid loan expansion may recognize fewer loan loss provisions. Following the spirit of Jiang et al. (2016), we include

SENATOR and its interaction terms with other firm-level determinants of loan loss provisions to control for potential systematic differences in modeling errors between treatment and control states. In other words, we seek to separate *discretionary* provisions from systematic modeling errors.[14]

We include three macro variables: the Case-Shiller Real Estate Index ($CSRET_t$), the change in GDP (ΔGDP_t), and the change in the state's unemployment rate ($\Delta UNEMP_t$). These macro variables have been found to have significant effects on banks' loan loss provisions (e.g., Beatty and Liao 2014). We also include state fixed effects to account for any time-invariant state characteristics that affect the estimation of loan loss provisions.[15]

According to the analyses of Beatty and Liao (2014), the above model is the preferred model, in the sense that it is the most effective at identifying the discretionary part of loan loss provisions. Following Jiang et al. (2016), we estimate the model and use the natural logarithm of the absolute values of the error term (*DLLP*) as our first measure of bank opacity; a larger *DLLP* indicates a higher level of bank opacity. The use of absolute values of the error term is appropriate for measuring the opacity (i.e., upward or downward distortions of the actual loan loss provisions). Since *DLLP* may be affected by the reversion of accruals from previous periods, in the spirit of Hutton et al. (2009), we also use the four-quarter moving sum of *DLLP* as our second measure (*DLLP_MS*). The measure using the moving sum is more likely to reflect bank policy on loss provisions. Appendix B presents the estimation results for Eq. (1). The coefficients on the determinants of loan loss provisions all have the expected signs and are comparable to those in previous studies (Beatty and Liao, 2014). The adjusted *R*-squared is 20.5%, suggesting that the model has a reasonable capability to describe the variation in loan loss provisions.

[14] Our results are robust if we do not include *SENATOR* interaction terms in the estimation model (Online Appendix Table OA1).
[15] Following the banking literature, we do not include time fixed effects in the estimate model. Our results, however, are robust if we do (see Online Appendix Table OA2).

3.3 Descriptive statistics

Table 1, Panel B, presents the descriptive statistics for our main test sample. Appendix C defines all the major variables used in this study. The variable *SENATOR* has a mean of 0.483, suggesting that 48.3% of bank–quarters have BC senators. On average, loan loss provisions (*LLP*) are 0.13% of the total loans, similar to the number reported in Beatty and Liao (2014). The total assets of banks in our sample have a mean of $9.2 billion and a median of $1.1 billion. Given the skewed distribution of total size, we use the logarithm of total assets (*SIZE*) in the regression analyses. Approximately 8% of bank–quarters have negative earnings. Our first measure of bank opacity is discretionary loan loss provisions (*DLLP*), defined as the natural logarithm of the absolute value of the error terms from Eq. (1). The variable *DLLP* has a mean of -2.733, which translates into 0.065% ($e^{-2.733}/100$) of the total loans. The variable *DLLP_MS*, the four-quarter moving sum of *DLLP*, has a mean of -10.952, representing an average quarterly discretionary loan loss provisions of 0.064% ($e^{-10.952/4}/100$) of the total loans. Due to data availability, our main regression includes 38,509 observations when we use *DLLP_MS* as the measure of bank opacity.

4. Main results

In this section, we present our main analysis of the effect of BC senators on bank opacity. In addition, we examine regulatory forbearance as a potential mechanism for the effect of BC senators and explore how the effects of BC senators on bank opacity and forbearance vary with their political power.

4.1 BC senators and bank opacity

To examine the effect of BC senators on discretionary loan loss provisions, we run the following regression:

$$OPACITY_t = \beta_0 + \beta_1 SENATOR_t + \beta_2 SIZE_t + \beta_3 LLP_{t-1} + \beta_4 CAP_t + \beta_5 LOSS_t + \beta_6 TIER_t + \beta_7 EBP_t + Macro_t + YQtr + BANK + \varepsilon_t, \quad (2)$$

where the dependent variable is bank opacity, measured as discretionary loan loss provisions ($DLLP_t$), or the four-quarter moving sum of discretionary loan loss provisions ($DLLP\_MS_t$). The variable *SENATOR* is the variable of interest and indicates whether the bank is located in a state with a BC senator. Following Jiang et al. (2016) and Kanagaretnam et al. (2010), we include the following control variables: *SIZE* is the natural logarithm of total assets; LLP_{t-1} is the loan loss provisions in the previous quarter, which captures possible reversal of accruals over time; *CAP* is the ratio of shareholder equity to total assets; *LOSS* is an indicator variable equal to one if the bank reports negative net income in the quarter; *TIER* is tier 1 risk-adjusted capital ratio; and *EBP* is earnings before loan loss provisions and taxes, scaled by lagged total loans. We also use three state-level variables to control for time-varying state economic conditions (*CSRET,* ΔGDP*,* and $\Delta UNEMP$). We include year–quarter fixed effects ($YQtr$) and bank fixed effects ($BANK$). The standard errors are clustered at the bank level.

Table 2 presents the results. In column (1), we use $DLLP_t$ as the dependent variable and include only *SENATOR* as the independent variable; in column (2), we include all the control variables. The coefficients of *SENATOR* are both positive (0.0634 and 0.0680, respectively) and significant at the 1% level. In columns (3) and (4), we use $DLLP\_MS_t$ as the dependent variable. The coefficients of *SENATOR* are also positive (0.2850 and 0.2763, respectively) and significant at the 1% level. The results are consistent with the prediction that banks in states with BC senators exert more accounting discretion in loan loss provisions and provide more opaque financial information. On average, banks in states with BC senators have about 6% (7% = 28%/4) more discretionary loan loss provisions

(quarterly) than states without BC senators.[16] The results for the control variables are comparable to previous research (e.g., Jiang et al., 2016).[17]

4.2 Identification

Our main regression exploits the time-series and cross-state variations in BC senators, which is largely exogenous to firm decisions (Kostovetsky, 2015).[18] Moreover, we use bank fixed effects to control for potential unobservable omitted variables. Nonetheless, to further address potential endogeneity issues, we conduct an event study by focusing on plausibly exogenous BC senator departures (e.g., Mehta and Zhao 2020). First, we identify 49 BC senator turnovers. From these, we remove 12 cases in which a senator from the same state took the position. Second, we use Charles Stewart's website and Google search to carefully examine the reasons for each turnover case. Following Mehta and Zhao (2020) and Mehta et al. (2020), we identify 21 cases as exogenous departures: 18 senators transferred to other Senate committees and three resigned from Congress. Other senators either left the Banking Committee because of re-election failure (6 cases) or retirement (10 cases).[19]

In our analysis, treated firms are those from states with exogenous BC senator departures. We use a propensity score method to identify the control sample and require these firms to be located in states without BC senator turnovers around the BC senator departure years of the treated firms. The propensity score is estimated using firm size, leverage, the tier 1 risk-adjusted capital ratio, the return on assets, cash holding, growth rate, net charge-offs, non-performing assets, loan loss provisions, change in non-

[16] As discussed in Section 2, we focus on BC senators because of their exclusive confirmation power in the presidential appointment and reappointment of agency leaders and their higher seniority than that of representatives. Our results are robust if we control for the potential effect of representatives of the House Committee on Financial Services (Table OA3).
[17] Our results are robust to including additional measures of risks, such as stock volatility or change in leverage.
[18] Kostovetsky (2015) runs probit regressions of BC senators on bank characteristics and finds no significant relation.
[19] We find no cases of close election failure.

performing assets, and liquidity, as well as three macro variables, namely, the Case-Shiller Real Estate Index ($CSRET_t$), the change in GDP (ΔGDP_t), and the change in the state's unemployment rate ($\Delta UNEMP_t$). For each turnover case, we include two years prior to and two years after the turnover year for both the treated and control firms. Then, we run the following regression:

$$OPACITY_t = \beta_0 + \beta_1 DEPARTURE \times POST + \beta_2 DEPARTURE + \beta_3 POST + Controls + Fixed\ Effects + \varepsilon_t, \quad (3)$$

where the dependent variable is bank opacity, measured as discretionary loan loss provisions ($DLLP_t$), or the four-quarter moving sum of discretionary loan loss provisions ($DLLP\_MS_t$); *DEPARTURE* indicates whether the bank is in a state with a departing BC senator; and *POST* indicates whether the observation is in the period after the turnover event. The interaction term *DEPARTURE*×*POST* is the variable of interest, whose coefficient captures the change in opacity for treated banks around BC senator departure relative to control banks without BC senator turnover. The control variables are the same as in Eq. (2).

Table 3 presents the results. In both columns (1) and (2), the coefficient of *DEPARTURE*×*POST* is negative (-0.1449 and -0.5264, respectively) and significant at the 5% level, suggesting that banks located in states with BC senators significantly reduce reporting opacity after the senators' departure from the Banking Committee. In a dynamic analysis (Table OA4), we find that banks start to significantly reduce opacity one quarter after the departure of BC senators, suggesting that banks can swiftly change their discretionary accounting choices (e.g., Jiang et al., 2016). Moreover, there is no discernable patterns in the changes of opacity immediately before the departures.

4.3 Moderating effect of bank characteristics

The incentives of BC senators to bail out banks or avoid bank enforcement actions stem from their political career concerns, because bank failures and formal enforcement actions are costly to both banks and the local economy. Therefore, we expect economically important banks to matter more to politicians, and the effect of BC senators on bank opacity should be stronger for these banks. Moreover, important banks have more influence on senators.

To examine the moderating effect of relative bank importance, we adjust Eq. (2) and include an interaction term between *IMPORT* and *SENATOR*. The indicator variable *IMPORT* takes the value of one if the ratio of a bank's total assets to the sum of the total assets of all banks headquartered in the same state is greater than the median ratio of all banks in the year–quarter, and zero otherwise. Columns (1) and (2) of Table 4 report the results. The variable of interest, *IMPORT*×*SENATOR*, has a coefficient of 0.1042 (0.4150) when *DLLP* (*DLLP_MS*) is the dependent variable and is significant at the 5% level, suggesting that the effect of BC senators on bank opacity is more pronounced for relatively important banks in the state.

The main purpose of banks being opaque is to conceal excessive risk taking to avoid regulatory intervention or to facilitate regulatory forbearance. Therefore, the effect of BC senators on bank opacity should be more pronounced for banks that already have high risk, because these banks are more likely to be scrutinized by regulators or market participants. To test this conjecture, we adapt Eq. (2) by including the interaction terms between measures of risk and *SENATOR*. The first measure of risk is the volatility of stock returns, defined as the standard deviation of daily returns over a quarter. The second measure is change in leverage, where leverage is defined as long-term debt scaled by total assets. Columns (3) to (6) of Table 4 present the results. Consistent with our prediction, the effect of BC senators on bank opacity is more pronounced for banks with

higher risk, supporting the argument that these banks have a greater need or incentive to hide excessive risk.

4.4 BC senators, bank opacity, and enforcement actions

This section investigates the relation between BC senators and bank enforcement actions and the role of opacity in this relation. The purpose of this investigation is to provide evidence on regulatory forbearance as the potential mechanism through which BC senators affect bank opacity. Under this mechanism, BC senators, regulators, and banks all have incentives to increase bank opacity and dampen the ability of market participants and taxpayers to detect or constrain regulatory forbearance.

We first match the formal enforcement data from the SNL Bank Regulatory dataset to our main sample using parent firms' unique regulatory IDs. We then exclude enforcement actions against individuals, since they were not issued because of a bank's deteriorating financial health and do not have a direct impact on bank operations (Delis, Staikouras, and Tsoumas, 2017; Lambert, 2019). In our final sample, approximately 0.6% of bank–quarter observations (232 bank–quarters) are associated with at least one formal enforcement action.[20] Among them, 22 bank–quarters received two or more enforcement actions. Using this sample, we run the following regression[21]:

$$EA_t = \beta_0 + \beta_1 OPACITY_t \times SENATOR_t + \beta_2 SENATOR_t + \beta_3 OPACITY_t + Controls + Fixed\ Effects + \varepsilon_t \quad (4)$$

[20] In Kleymenova and Tomy's (2020) sample of both public and private banks, about 0.26% of bank–quarters were the subject of formal enforcement actions over the period 1987 to 1997. For a sample of public and private banks during the financial crisis, Gallemore (2021) reports that about 4% of bank-years (translating into about 1% of bank quarters) were the subject of formal enforcement actions because enforcement actions are generally more frequent during crisis periods.

[21] The results are robust if we include interaction terms between *SENATOR* and all control variables in the model.

where the dependent variable *EA* is the number of enforcement actions that the bank has been subject to during the quarter, or a dummy variable indicating whether the bank was subject to enforcement action during the quarter. The independent variables include the measure of opacity (*DLLP* or *DLLP_MS*), the BC senator indicator variable (*SENATOR*), and the interaction term of these two variables. Following prior literature (e.g., Kleymenova and Tomy, 2020; Lambert, 2019), we use a set of control variables, including the bank size (*SIZE*), leverage ratio (*LEV*), tier 1 risk-adjusted capital ratio (*TIER*), nonperforming assets (*NPA*), return on equity (*ROE*), total deposits (*DEPOSIT*), changes in the amount of loans (*△LOAN*), and changes in liquidity (*△LIQUIDITY*).

Table 5 presents the results.[22] In columns (1) and (2), we use the number of enforcement actions as the dependent variable and include time and bank fixed effects in the ordinary least squares (OLS) regression models. We find that the coefficients of *SENATOR* are negative and significant, suggesting that banks headquartered in states with BC senators have a lower likelihood of being the subject of formal enforcement actions. More importantly, we find that the coefficients of the interaction term of *OPACITY* and *SENATOR* are significant and negative, suggesting that the negative effect of BC senators on the likelihood of bank enforcement actions is strengthened by bank opacity. This result is consistent with our argument that BC senators and banks employ financial reporting opacity to facilitate regulatory forbearance. Using a sample of banks during the recent financial crisis, Gallemore (2021) finds that bank opacity is negatively associated with the likelihood of regulatory intervention, suggesting that regulators have strong incentives to use opacity to facilitate regulatory forbearance during crises. Interestingly, however, for our broader sample, opaque banks without BC senators are the subject of more enforcement actions (as indicated by the significantly positive

[22] Our results are similar if we use bootstrapped standard errors for regressions with *OPACITY* as one of the independent variables.

coefficients of *OPACITY*), suggesting that opacity alone is unlikely to mitigate regulatory interventions without politicians' influence. This argument is consistent with the findings of Costello et al. (2019), which shows that strict regulators on average are associated with lower bank opacity.

Since few banks are subject to more than one enforcement action in any one particular quarter, we also use a logit model to examine the joint effect of BC senators and bank opacity on bank enforcement. Previous literature (e.g., Lancaster, 2000; Neyman and Scott, 1948) suggests that estimating nonlinear regression with firm fixed effects introduces an incidental parameters problem. Therefore, in columns (3) and (4) of Table 5, we include only time fixed effects in logit regressions. The results are consistent with those using OLS models. Finally, to check robustness, in columns (5) and (6), we use a conditional logit model to operationalize firm fixed effects. Due to the large number of banks without enforcement actions throughout our sample period, the sample size is reduced significantly to 9,388 and 8,821 observations in columns (5) and (6), respectively. Nonetheless, the results continue to hold in the conditional logit regressions.[23]

4.5 The political power of BC senators

In this section, we examine how the effect of BC senators on bank opacity and regulatory forbearance varies with their political clout. Specifically, we focus on the seniority of BC senators. The seniority system of Congress, which has existed for over 100 years, tends to give congresspersons with longer congressional service more privileges and power. For example, the chairpersonship of congressional committees is determined almost entirely by seniority, although there have been occasional deviations from this rule

[23] We also examine whether BC senators condition the impact of key financial statement variables on enforcement actions (see Online Appendix Table OA 5). We find that the effects of capital ratios, nonperforming assets, profitability, and liquidity on bank enforcement are marginally weakened by BC senators. In this study, we argue that politicians and banks use opaque financial reporting to conceal regulatory forbearance, which suggests that the reported financial statement numbers of troubled banks forborne by regulators may appear to be sound. Therefore, the conditioning effect of BC senators on these accounting variables is not clear.

in more recent years. As Galloway (1953, 367) states, "*in no other place, perhaps, does seniority or length of service carry so much weight as it does in the Congress of the United States*." Consistent with a positive relation between seniority and power, Levitt and Poterba (1999) find that states with very senior congresspersons have higher growth rates than states with more junior ones. Mehta et al. (2020) and Mehta and Zhao (2020) show that the seniority of the congressperson serving on relevant committees is negatively related to the enforcement of misconduct and antitrust regulations. Gropper et al. (2013) show that banks headquartered in states with congressional banking committee chairpersonships outperform banks in other states. The chair effect, however, disappears or even becomes negative when the chair is less senior.

We collect US Congressional member details from Charles Stewart's website and construct the dummy variable *Senior*, which takes the value of one if the BC senator's length of service in the Senate is within the top decile among all senators in the year, and zero otherwise.[24] In addition to seniority, we examine whether the senior senator is the chair of the Banking Committee, since chairpersonship gives senators formal power to set the committee's agenda. However, we argue that senior BC senators without chairpersonship also wield substantial power, because of their extensive political network and personal ability to bring individual senators together to reach compromises, as evidenced by Senator Cranston in Lincoln's case.[25]

Table 6, Panel A, presents the results of how differences in the political power of BC senators affect bank opacity. In column (1), where *DLLP* is the dependent variable, we find that the coefficient of *Senior* is positive and significant at the 5% level, and in column (2), where *DLLP_MS* is the dependent variable, the coefficient of *Senior* is also positive

[24] Our results are robust if we measure seniority based on the total number of years served on the Banking Committee.

[25] Moreover, some senior members of congressional committees often served as past chairs of the same committees. In our bailout example, for instance, Senator Richard Shelby was not the chair of the Banking Committee during the financial crisis, but was the chair from 2003 to 2007.

and significant at the 10% level. These results suggest that senior BC senators have a stronger effect on bank opacity than other BC senators.

In columns (3) and (4), we include the dummy variable *Senior Chair*, which indicates that a BC senator is both a senior senator and the chair of the Senate Banking Committee, and the dummy variable *Senior Member*, which indicates the BC senator is senior but not the chair. We find that the coefficient of *Senior Chair* is significant in both columns (3) and (4), and the coefficient of *Senior Member* is significant in only column (3). The coefficients of *Senior Chair* are economically larger than those of *Senior Member*, suggesting that senior senators with chairmanship likely have stronger political power and thus a stronger effect on bank opacity.[26]

Panel B of Table 6 presents the results of similar analysis of BC senator power for bank enforcement actions.[27] In columns (1) and (2), we find no evidence that the interactive effect of BC senator and opacity on bank enforcement actions is more pronounced for senior BC senators than for other senators. However, in columns (3) and (4), we show that the interactive effect is statistically and economically stronger for senior BC senators holding the chairpersonship of the Senate Banking Committee than other BC senators.[28] These results suggest that the joint effect of opacity and BC senators on regulatory forbearance varies predictably with the political clout of individual BC senators.[29]

[26] The coefficients of *Senior Chair* and *Senior Member* are not statistically different.

[27] For this test, we use a logit model with time fixed effects. Perhaps due to the limited within-firm variations of the dependent variable, we do not find significant senior senator effects if we use a conditional logit model with bank fixed effects.

[28] The coefficients of interaction terms of *Senior Chair* and *Senior Member* are statistically different in column 3 (p-value = 0.13) and column 4 (p-value = 0.06).

[29] In an additional analysis, we also examine how the political environment, in terms of party alignments, affects the power of senior senators. Table OA6 shows that the effect of BC senators on bank opacity and the interactive effect of BC senators and opacity on enforcement actions are more pronounced for senior BC senators who are members of either the Senate majority party, the majority party of both chambers, or the same party as the president.

In summary, the evidence in this section strengthens our arguments that BC senators have the political power to influence bank regulators, which leads banks to increase opacity to conceal excessive risk taking and facilitate regulatory forbearance.

5. Real effects and macroeconomic conditions

We have established that BC senators have an overall positive effect on bank opacity and that banks and politicians use opacity to facilitate regulatory forbearance and hinder market and taxpayer scrutiny of bank risk taking. In this section, we examine whether BC senators have any direct effect and indirect effect via opacity on the real outcomes of banks. In addition, we examine whether BC senators have stronger incentives to promote bank opacity and encourage lending during economic downturns.

5.1 Real effects

BC senator and bank opacity could encourage more imprudent lending activities, which could lead to more loan losses and less banking stability. In this section, we examine whether BC senators affect bank real outcomes, and more importantly, whether bank opacity is an important channel through which BC senators affect bank outcomes. Specifically, we estimate the following structural mediation model:

$$Opacity_t = \beta_0 + \beta_1 SENATOR_t + Controls + YQtr + BANK + \varepsilon_t, \tag{5A}$$

$$RealEffect_{t+1} = \gamma_0 + \gamma_1 Opacity_t + \gamma_2 SENATOR_t + Controls + YQtr + BANK + \varepsilon_t, \tag{5B}$$

where *Real Effect* is bank insolvency risk or actual loan losses. Following Laeven and Levine (2009), we measure bank insolvency risk using each bank's *z*-score, which is the return on assets plus the capital adequacy ratio divided by the standard deviation of asset returns. Because the *z*-score is inversely related to the probability of bank insolvency and highly skewed, we define our first variable, *Insolvency Risk,* as the negative of the natural

logarithm of the *z*-score. Specifically, *Insolvency Risk* equals -ln((*ROA* + *CAR*)/std(*ROA*)), where *ROA* is the rate of return on assets, *CAR* is capital adequacy ratio, and std(*ROA*) is the standard deviation of the rate of return on assets. In addition, we measure actual loan losses using loan charge-offs. Specifically, our second measure of the real effect is *Loan Loss*, which equals net loan charge-offs divided by total loans (e.g., Cantrell, McInnis, and Yust, 2014; Jiang et al., 2016). We include standard control variables following prior literature, as well as bank and time fixed effects.

Table 7 reports the structural estimation results. Panel A presents the results of insolvency risk and panel B presents the results of actual loan losses. We focus our discussion on the result in column (1) of Panel A, where *DLLP* is the measure of opacity and insolvency risk is the measure of real effects. We find that BC senators have a significant direct effect on insolvency risk (*path coefficient* = 0.0652, z = 2.32). The path coefficient between BC senators and opacity is positive and significant, consistent with the results reported in Table 2. The path coefficient between opacity and insolvency risk is positive and significant, suggesting that bank opacity is associated with higher insolvency risk. More importantly, the total mediation path for opacity is positive and significant (*path coefficient* = 0.0015, *z* = 2.52), suggesting that there is a significant indirect effect of BC senators on insolvency risk through the channel of bank opacity. The results in column (2) of panel A and both columns of panel B show similar direct and indirect effect (via opacity) of BC senators on real outcomes. Overall, we find that BC senators have a significant and positive direct effect on bank insolvency risk and loan losses and a significant and positive indirect effect on these outcomes through bank opacity.

5.2 Macroeconomic conditions

Transparent financial reporting facilitates market and nonmarket discipline over bank risk taking, which deters banks from accumulating excessive leverage and risky

assets during good times. However, some academics argue that bank transparency can be detrimental in economic downturns. For example, Goldstein and Sapra (2014) argue that the disclosure of stress tests could result in panic-based bank runs. Hanson, Kashyap, and Stein (2011) suggest that transparent disclosure may induce market pressure and cause a negative spiral, including a decrease in lending, a decline in deposits, and fire sales, exacerbating the economic downturn. Therefore, if politicians hold a similar view, we should expect them to have even stronger incentives to promote bank opacity and encourage bank lending in economic downturns.

To test this conjecture, we adapt Eq. (2) and include the interaction terms between measures of economic conditions (*EC*) and *SENATOR*. We measure economic conditions using three variables. The first measure is an indicator variable (*IDQC*) that equals one if the observation is in a recession period (i.e., 2001Q2–2001Q4 or 2008Q1–2009Q2) and the bank has a tier 1 risk-adjusted capital ratio in the bottom decile, and zero otherwise. Our second measure is an indicator variable (*POOR*) that takes the value of one if the state's GDP growth is below the sample median, and zero otherwise. The third measure is an indicator variable (*WBS*) that equals one if the percentage of banks that were or would be closed without assistance in the state is above the sample median, and zero otherwise.[30]

Table 8 presents the results. The variable of interest, *EC*×*SENATOR*, has significant and positive coefficients in all regression models. The results suggest that the impact of BC senators on bank opacity is more pronounced during downturns of the local economy. The evidence supports our conjecture that BC senators have stronger incentives to promote bank opacity during downturns, perhaps with the intention of avoiding panic runs and encouraging bank lending.

[30] Bank closure data are from the FDIC (https://www.fdic.gov/).

A natural follow-up question is whether BC senators can indeed help encourage bank lending during economic downturns. To examine this question, we regress future loan growth on the interaction term of economic conditions (proxied by *IDQC, POOR,* or *WBS*) and *SENATOR*, as well as standard control variables (e.g., Beatty and Liao, 2011; Bhat, Ryan, and Vyas, 2019; Gallemore, Mayberry, and Wilde, 2017). We find that local economic conditions are negatively associated with future loan growth, suggesting that bad economic conditions lead to less bank lending (Table OA7). More importantly, we find that BC senators mitigate bank disinvestment and encourage liquidity provision in economic downturns. Some researchers (e.g., Acharya and Ryan, 2016; Leuz, 2009) propose making financial (regulatory) reporting rules "countercyclically transparent" for the benefit of financial stability. Our evidence suggests that the interactions among banks, politicians, and regulators can result in some sort of countercyclical transparency and more bank lending in downturns, which can be taken as a bright side of the politics of bank opacity.

6. Capital market consequences

Our arguments mainly focus on BC senators, regulators, and banks. It is interesting to examine the market perceptions of opacity and the role of BC senators. If market participants, such as current shareholders and creditors, believe that banks in states with BC senators are more likely to receive governmental bailouts or forbearance in case of trouble, they will have reduced incentives to monitor or discipline these banks and will not penalize bank opacity.

To provide evidence on market consequences, we examine whether market participants regard discretionary loan loss provisions differently for banks in states with and without BC senators. Specifically, we run the following regression:

$$BOND_t = \beta_0 + \beta_1 SENATOR_t \times OPACITY_t + \beta_2 OPACITY_t + \beta_3 SENATOR_t + \beta_4 SIZE_t + \beta_5 LEV_t + \beta_6 TIER_t + \beta_7 EBP_t + \beta_8 LOAN_t + \beta_9 VOLATILITY_t + \beta_{10} MB_t + \beta_{11} MATURITY_t + \beta_{12} MATURITY_t^2 + \beta_{13} AMOUNT_t + \beta_{14} SUBORDINATE_t + Fixed\ Effects + \varepsilon_t, \quad (6)$$

where the dependent variable (*BOND*) is either the bond rating or bond yield for each bond of banks. The bond rating (*RATING*) is defined as the average bond rating score assigned by S&P, Moody's, and Fitch, where higher values indicate lower credit quality. The bond yield (*YIELD*) is the bond yield minus the risk-free rate, which represents investor expected abnormal returns for the bond. We use the two variables to capture how market participants view bank opacity.

The key independent variable of interest is the interaction term between *SENATOR* and *OPACITY*. Follow prior literature (e.g., Becker and Milbourn, 2011; Jiang, Stanford, and Xie, 2012), we also include a set of firm- and bond-specific characteristics that have been found to explain bond ratings or bond yields. Following Becker and Milbourn (2011), we use ordered probit regression where *RATING* is the dependent variable.[31]

Columns (1) and (2) of Table 9 report the results using *RATING* as the dependent variable. In both columns, the coefficient of *DLLP* (*DLLP_MS*) is positive and significant, suggesting that bond rating agencies regard bank opacity as a bad signal for credit risk and assign a lower credit rating to more opaque banks. More importantly, we find that the interaction term between *SENATOR* and *DLLP* (or *DLLP_MS*) is negative and significant at the 1% level, suggesting that bank opacity is penalized less by the rating agencies if the banks are in states with BC senators.

Columns (3) and (4) of Table 9 report the results of OLS regression with *YIELD* as the dependent variable. We find that the interaction term between *SENATOR* and *DLLP*

[31] As Becker and Milbourn (2011) point out, an ordered probit regression permits each cutoff to be estimated and implicitly allows the effect of dependent variables to vary across different parts of the ratings scale, for more efficient data utilization.

(or *DLLP_MS*) is negative and significant at the 1% (5%) level. The evidence is consistent with the argument that bondholders care less about the reporting opacity of banks in states with BC senators. One potential interpretation for the results is that market participants, particularly creditors, expect these banks to be bailed out should they encounter financial difficulties. Therefore, they have fewer incentives to monitor bank risk taking and rely less on financial reports.

7. Additional analysis

7.1 The ideology of BC senators

The impact of BC senators on bank opacity stems from their incentives and ability to facilitate the regulatory bailout and forbearance of troubled banks. The political economy literature, however, suggests that politicians' actions can also be affected by their ideological positions (Poole and Rosenthal, 2011). Conservatives tend to oppose spending public resources on private sector bailouts, whereas liberals prefer more government intervention (Bischof, Daske, and Sextroh 2020). For example, Wen (2011) shows that Republicans tended to vote against the TARP bill during the 2008–2009 financial crisis. If banks expect a lower likelihood of bailouts from conservatives, we would expect the effect of BC senators on bank opacity to be more pronounced for banks in states with liberal senators. Moreover, conservatives are more likely to leave banks to the disciplinary power of the free market and are thus less likely to shield banks from market discipline. By the same token, however, conservatives may prefer less regulation ex ante than liberals and thus enforce regulations less strictly ex post.[32] Therefore, it is not clear how the political ideology of BC senators affects bank opacity, and we examine this question empirically.

[32] However, Shleifer and Vishny (1993, 601) argue that "an important reason why many of these permits and regulations exist is probably to give officials the power to deny them and to collect bribes in return for providing the permits."

We measure ideology using the first dimension of the DW-NOMINATE score of Lewis et al. (2019), which is derived from politicians' past roll call voting records in Congress.[33] Then, we classify all BC senators as either conservative (*CONSERVATIVE*) or liberal (*LIBERAL*) according to the ideology score and re-estimate Eq. (2). We find that the coefficients of *LIBERAL* are positive and significant at the 1% level in all specifications, whereas the coefficients of *CONSERVATIVE* are nonsignificant. The results suggest that the ideology of BC senators matters for bank opacity (see Table OA8).

7.2 Publicly listed banks and privately held banks

Our main data source is Compustat, which contains financial statement information on all publicly listed banks. Besides the availability of pricing data necessary for some variables, we focus on publicly listed banks also because these banks are generally larger, more visible, and under more intense public scrutiny. Moreover, an important type of market discipline is that stakeholders can act upon market price signals, which, in turn, are affected by financial reporting. The central argument of our theory is that politicians and banks use opaque financial reports to shield risk taking and forbearance from market and public discipline. Therefore, our theory is more relevant to public banks. Nevertheless, we examine whether our results hold after including both public and private banks in our sample. To do so, we collect financial information from all banks' call reports and re-estimate Eq. (2). The results continue to hold. Moreover, we find that the effect of BC senators on bank opacity is significantly stronger for publicly listed banks than for nonpublic banks (see Online Appendix Table OA9).

8. Conclusions

This study investigates how the distribution of political power shapes the financial reporting opacity of the banking sector. We show that banks located in states with

[33] See https://voteview.com.

senators on the powerful Senate Banking Committee produce more opaque financial reports than banks located in states without these powerful politicians. The results are stronger when banks are relatively important in a state and when banks take more risks. Consistent with the argument that BC senators and opacity facilitate regulatory forbearance, we show that BC senators have a negative effect on the likelihood of banks in their home states being subject to regulatory intervention, and the effect is stronger for more opaque banks. The effect of BC senators on bank opacity and regulatory forbearance is stronger when they wield more political clout.

In addition, we show that BC senators have a positive effect on bank insolvency risk and actual loan losses, and, more importantly, that bank opacity is an important channel through which BC senators have real effects. Moreover, we find evidence that the effect of politicians on bank opacity is more pronounced during periods of economic downturns, and the politicians appear to increase bank opacity to create liquidity in times of need. Finally, we find that the reporting opacity of banks located in states with BC senators is penalized less by the capital market than banks in other states. Overall, our research identifies politics or politicians as an important determinant of bank opacity and provides evidence on major mechanisms and real effects.

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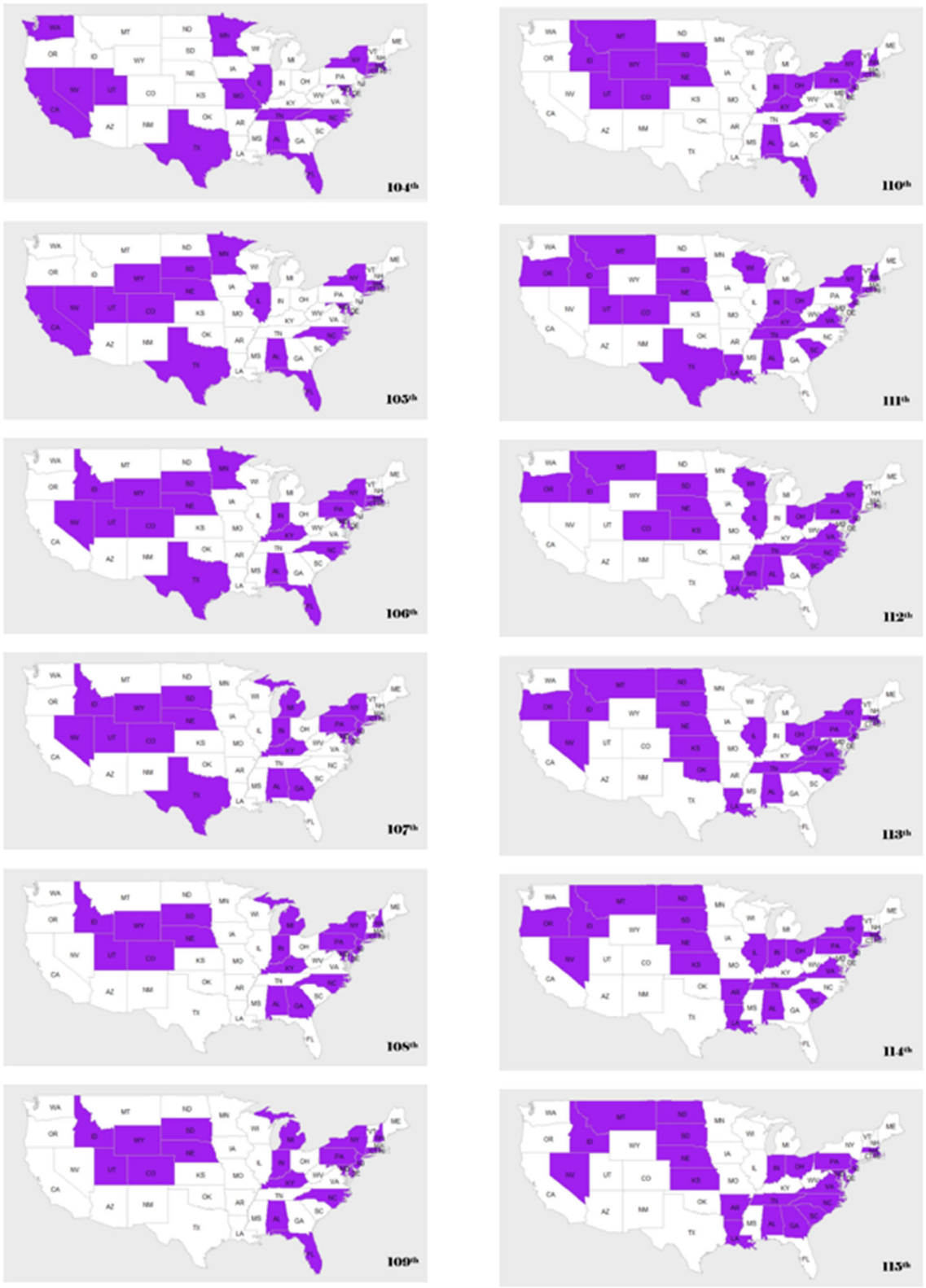
Figure 1. Distribution of BC Senators by State (104th–115th Congress)



Note: States with BC senators are colored.

Table 1. Descriptive Statistics

Panel A. Sample distribution by state

State	#Observations	% *SENATOR* = 1
AK	119	0.00
AL	598	1.00
AR	311	0.15
AZ	50	0.00
CA	4251	0.17
CO	209	0.61
CT	870	0.70
DC	102	0.00
DE	232	0.41
FL	1034	0.48
GA	1287	0.24
HI	245	0.39
IA	410	0.00
ID	36	0.94
IL	1779	0.40
IN	1856	0.66
KS	197	0.32
KY	836	0.52
LA	509	0.53
MA	1600	0.49
MD	1070	0.51
ME	273	0.00
MI	1367	0.28
MN	323	0.39
MO	887	0.11
MS	555	0.13
MT	164	0.59
NC	1594	0.73
ND	137	0.28
NE	81	0.88
NH	194	0.35
NJ	2141	0.77
NM	38	0.00
NV	45	0.13
NY	3020	0.97
OH	2435	0.47
OK	256	0.09
OR	396	0.32
PA	3974	0.76
RI	185	0.98
SC	697	0.31
SD	134	0.89
TN	560	0.48
TX	1109	0.43
UT	121	0.69
VA	2055	0.49

VT	241	0.00
WA	1073	0.04
WI	747	0.18
WV	631	0.09
Total	43034	0.48

Panel B. Descriptive statistics of main variables

				Percentile		
	N	Mean	SD	P25	P50	P75
$SENATOR_t$	43034	0.483	0.500	0.000	0.000	1.000
$DLLP_t$	43034	-2.733	1.198	-3.285	-2.557	-2.010
$DLLP\_MS_t$	38509	-10.952	3.416	-13.107	-10.744	-8.680
ASSET	43034	9258	33852	542	1148	3455
$SIZE_t$	43034	7.368	1.558	6.296	7.046	8.148
LLP_{t-1}	43034	0.130	0.220	0.025	0.066	0.136
CAP_t	43034	9.553	3.113	7.589	9.115	10.895
$LOSS_t$	43034	0.080	0.271	0.000	0.000	0.000
$TIER_t$	43034	11.665	3.322	9.420	11.320	13.420
EBP_t	43034	0.607	0.391	0.403	0.586	0.796
$CSRET_t$	43034	0.913	2.023	-0.037	1.300	2.269
$\triangle GDP_t$	43034	2.146	2.406	0.900	2.200	3.600
$\triangle UNEMP_t$	43034	-0.006	0.337	-0.200	-0.067	0.100

Notes:
This table reports the sample distributions and descriptive statistics of the main variables. The sample period spans 1995Q1 to 2017Q4. Our primary sample contains all banks with necessary quarterly data available from Compustat. Variable definitions are presented in Appendix C. All continuous variables are winsorized at the 1st and 99th percentiles to mitigate the effects of outliers.

Table 2. BC Senator and Bank Opacity

	DLLP		*DLLP_MS*	
	(1)	(2)	(3)	(4)
SENATOR$_t$	***0.0634****	***0.0680****	***0.2850****	***0.2763****
	(2.67)	***(2.95)***	***(2.95)***	***(2.96)***
SIZE$_t$		0.0337		0.0009
		(1.07)		(0.01)
LLP$_{t-1}$		0.4504***		3.1931***
		(9.56)		(19.55)
CAP$_t$		-0.0025		-0.0228
		(-0.48)		(-1.07)
LOSS$_t$		0.8663***		1.0477***
		(26.21)		(12.86)
TIER$_t$		0.0092**		0.0489**
		(1.99)		(2.55)
EBP$_t$		0.2021***		0.0782
		(5.90)		(0.67)
CSRET$_t$		-0.0177**		-0.0190*
		(-2.27)		(-1.71)
△GDP$_t$		-0.0463***		-0.1189***
		(-9.96)		(-7.32)
△UNEMP$_t$		0.0688***		-0.0028
		(2.73)		(-0.04)
Constant	-2.9627***	-3.3203***	-12.0060***	-12.3762***
	(-60.37)	(-15.47)	(-56.33)	(-13.25)
Time Fixed Effects	Yes	Yes	Yes	Yes
Bank Fixed Effects	Yes	Yes	Yes	Yes
Observations	43034	43034	38509	38509
Adjusted R^2	0.218	0.258	0.433	0.476

Notes:
This table presents the results of OLS regressions of bank opacity on BC senators, as follows:

$$OPACITY_t = \beta_0 + \beta_1 SENATOR_t + \beta_2 SIZE_t + \beta_3 LLP_{t-1} + \beta_4 CAP_t + \beta_5 LOSS_t + \beta_6 TIER_t + \beta_7 EBP_t + Macro_t + YQtr + BANK + \varepsilon_t$$

The dependent variable is bank opacity, measured as discretionary loan loss provisions (*DLLP*), or the four-quarter moving sum of discretionary loan loss provisions (*DLLP_MS*). The variable *SENATOR* is an indicator variable equal to one if the bank is headquartered in a state with a senator on the Banking Committee. The sample period is from 1995Q1 to 2017Q4. Variable definitions are presented in Appendix C. We control for year and quarter fixed effects and bank fixed effects in all specifications. The *t*-statistics in parentheses are based on standard errors clustered at the bank level. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels for two-tailed tests, respectively.

Table 3. Identification Using the Exogenous Departures of BC Senators

	DLLP	*DLLP_MS*
	(1)	(2)
DEPARTURE×POST	***-0.1449****	***-0.5264****
	(-2.12)	***(-2.11)***
DEPARTURE	0.0714	0.2581
	(1.07)	(0.96)
POST	0.0272	0.1461
	(0.51)	(0.73)
$SIZE_t$	0.1208	0.3985
	(1.38)	(1.18)
LLP_{t-1}	0.2643***	2.3018***
	(3.23)	(9.93)
CAP_t	-0.0149	-0.1159**
	(-1.18)	(-2.40)
$LOSS_t$	0.7941***	0.7388***
	(10.13)	(4.11)
$TIER_t$	0.0171	0.0711*
	(1.50)	(1.88)
EBP_t	0.2567***	0.2119
	(3.25)	(0.99)
$CSRET_t$	-0.0151	0.0888***
	(-0.87)	(3.37)
$\triangle GDP_t$	-0.0488***	-0.0815*
	(-4.06)	(-1.96)
$\triangle UNEMP_t$	0.0620	0.1218
	(1.03)	(0.80)
Constant	-3.9347***	-14.8810***
	(-6.25)	(-6.16)
Time Fixed Effects	Yes	Yes
Bank Fixed Effects	Yes	Yes
Observations	7593	7039
Adjusted R^2	0.309	0.596

Notes:
This table examines the impact of the unexpected departures of BC senators on bank opacity. The variable *DEPARTURE* is an indicator variable equal to one if the bank experienced a plausibly exogenous departure of their BC senator because of a committee transfer or resignation, and *POST* is an indicator variable equal to one if the year–quarter is after the departure. The regression includes a matched sample of banks that did not experience BC senator turnovers. The dependent variable is bank opacity, measured as discretionary loan loss provisions (*DLLP*), or the four-quarter moving sum of discretionary loan loss provisions (*DLLP_MS*). Variable definitions are presented in Appendix C. We control for year and quarter fixed effects and bank fixed effects in all specifications. Note that the dummy variables *Departure* and *POST* are not subsumed by fixed effects because this is a stacked event study design. The *t*-statistics in parentheses are based on standard errors clustered at the bank level. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels for two-tailed tests, respectively.

Table 4. Effects of Bank Characteristics

	IMPORT		*VOLATILITY*		*△LEV*	
	DLLP	*DLLP_MS*	*DLLP*	*DLLP_MS*	*DLLP*	*DLLP_MS*
	(1)	(2)	(3)	(4)	(5)	(6)
$SENATOR_t$	0.0062	0.0252	-0.0243	0.0130	0.0673***	0.2775***
	(0.19)	(0.19)	(-0.48)	(0.07)	(2.92)	(2.97)
$CONDITION_t \times SENATOR_t$	***0.1042****	***0.4150****	***5.3796*****	***15.8847****	***1.2692*****	***1.1000***
	(2.51)	***(2.50)***	***(2.62)***	***(2.20)***	***(2.98)***	***(1.29)***
$SIZE_t$	-0.0040	-0.1642	0.0607	0.1550	0.0334	-0.0026
	(-0.11)	(-1.06)	(1.59)	(1.00)	(1.06)	(-0.02)
LLP_{t-1}	0.4424***	3.1163***	0.1934	3.0345***	0.4548***	3.1952***
	(7.55)	(15.76)	(1.43)	(6.86)	(9.69)	(19.52)
CAP_t	-0.0050	-0.0277	0.0048	0.0276	-0.0022	-0.0225
	(-0.81)	(-1.08)	(0.51)	(0.75)	(-0.41)	(-1.05)
$LOSS_t$	0.8318***	1.0496***	0.7245***	1.0672***	0.8653***	1.0468***
	(17.68)	(9.66)	(7.37)	(4.12)	(26.14)	(12.84)
$TIER_t$	0.0081	0.0380*	0.0046	0.0358	0.0095**	0.0494**
	(1.36)	(1.65)	(0.53)	(1.12)	(2.06)	(2.57)
EBP_t	0.1819***	-0.0888	0.0695	0.0376	0.2012***	0.0788
	(4.10)	(-0.58)	(0.85)	(0.14)	(5.89)	(0.67)
$CONDITION_t$	-0.4603**	-1.9689**	5.3564	76.3955***	-1.0269	-0.8168
	(-2.25)	(-2.38)	(0.73)	(2.74)	(-0.72)	(-0.26)
$CONDITION_t \times SIZE_t$	0.0497**	0.2039**	-1.3061	-7.8750***	0.0675	0.0824
	(2.00)	(2.03)	(-1.62)	(-2.60)	(0.44)	(0.23)
$CONDITION_t \times LLP_{t-1}$	0.0105	0.1546	8.8788**	5.0260	2.6464**	1.0238
	(0.13)	(0.56)	(2.00)	(0.36)	(2.46)	(0.40)
$CONDITION_t \times CAP_t$	0.0028	0.0036	-0.4548	-2.6702*	-0.1097	-0.2925
	(0.33)	(0.11)	(-1.21)	(-1.88)	(-1.46)	(-1.64)
$CONDITION_t \times LOSS_t$	0.0690	-0.0210	7.3808**	1.0128	-0.3596	-2.2388
	(1.06)	(-0.13)	(2.02)	(0.10)	(-0.33)	(-1.01)
$CONDITION_t \times TIER_t$	0.0014	0.0167	0.2345	1.1167	0.0046	0.2029
	(0.18)	(0.55)	(0.63)	(0.84)	(0.06)	(1.20)
$CONDITION_t \times EBP_t$	0.0398	0.2919	6.5967**	4.0368	0.4214	0.3879
	(0.67)	(1.37)	(2.03)	(0.37)	(0.75)	(0.27)

$CSRET_t$	-0.0178**	-0.0195*	-0.0157*	-0.0187	-0.0183**	-0.0193*
	(-2.28)	(-1.76)	(-1.89)	(-1.63)	(-2.36)	(-1.73)
$\triangle GDP_t$	-0.0456***	-0.1167***	-0.0451***	-0.1178***	-0.0463***	-0.1186***
	(-9.76)	(-7.16)	(-8.84)	(-6.66)	(-9.97)	(-7.31)
$\triangle UNEMP_t$	0.0699***	0.0013	0.0576**	-0.0644	0.0694***	-0.0028
	(2.77)	(0.02)	(2.14)	(-0.93)	(2.76)	(-0.04)
Constant	-2.9913***	-10.8866***	-3.4220***	-14.0144***	-3.3249***	-12.3611***
	(-11.73)	(-10.27)	(-11.76)	(-11.72)	(-15.48)	(-13.22)
Time Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
Bank Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
Observations	43034	38509	38005	34421	43004	38486
Adjusted R^2	0.258	0.477	0.260	0.476	0.258	0.476

Notes:
This table presents the results of the moderating effects of bank characteristics. The conditional variable (*CONDITION*) in columns (1) and (2) is an indicator variable for the bank's relative importance (*IMPORT*). We calculate the total assets of the bank divided by the sum of the total assets of all banks headquartered in the same state. If the ratio is larger than the median value of the ratio in the year–quarter, then we set *IMPORT* equal to one, and zero otherwise. The conditional variable in columns (3) and (4) is the volatility of stock returns (*VOLATILITY*), defined as the standard deviation of daily returns over a quarter. The conditional variable in columns (5) and (6) is change in leverage (*△LEV*), where leverage is defined as long-term debt scaled by total assets. The dependent variable is bank opacity, measured as discretionary loan loss provisions (*DLLP*), or the four-quarter moving sum of discretionary loan loss provisions (*DLLP_MS*). The sample period is from 1995Q1 to 2017Q4. Variable definitions are presented in Appendix C. We control for year and quarter fixed effects and bank fixed effects in all specifications. The *t*-statistics in parentheses are based on standard errors clustered at the bank level. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels for two-tailed tests, respectively.

Table 5. BC Senators, Bank Opacity, and Enforcement Action

	No. of EA		EA Dummy			
	OLS		Logit		Conditional Logit	
	(1)	(2)	(3)	(4)	(5)	(6)
DLLP×SENATOR	***-0.0027*** ***		***-0.2701*** ***		***-0.2206****	
	(-2.25)		***(-2.14)***		***(-1.76)***	
DLLP_MS×SENATOR		***-0.0012*** ***		***-0.0987*****		***-0.1013*** ***
		(-2.40)		***(-2.68)***		***(-2.15)***
SENATOR	-0.0085**	-0.0136**	-0.8494**	-1.1690***	-0.7049*	-1.1499**
	(-2.30)	(-2.31)	(-2.56)	(-2.95)	(-1.89)	(-2.24)
DLLP	0.0019**		0.1798*		0.1779**	
	(2.42)		(1.79)		(1.97)	
DLLP_MS		0.0010***		0.0695***		0.0977***
		(2.70)		(2.58)		(2.74)
SIZE	0.0031*	0.0034	0.4426***	0.4239***	0.4248	0.4174
	(1.65)	(1.61)	(10.19)	(9.88)	(1.23)	(1.13)
LEV	0.0009	-0.0000	-1.4418	-1.6532	-0.4900	-0.6465
	(0.08)	(-0.00)	(-1.14)	(-1.26)	(-0.23)	(-0.29)
TIER	-0.0003	-0.0003	-0.0485	-0.0389	-0.0464	-0.0285
	(-1.07)	(-0.82)	(-1.57)	(-1.24)	(-1.17)	(-0.71)
NPA	0.1216**	0.0999*	7.5578***	6.0299*	3.3959	0.5740
	(2.06)	(1.65)	(2.60)	(1.89)	(0.75)	(0.12)
ROE	-0.0983**	-0.0912*	-4.3166**	-4.2721**	-3.7371	-3.0321
	(-1.98)	(-1.80)	(-2.02)	(-2.01)	(-1.42)	(-1.12)
DEPOSIT	0.0009	0.0003	1.1235	0.7753	-1.0696	-1.3601
	(0.06)	(0.02)	(0.96)	(0.66)	(-0.48)	(-0.59)
△LOAN	-0.0088	-0.0101	-0.9117	-1.4367	-0.7594	-1.5345
	(-0.70)	(-0.74)	(-0.58)	(-0.85)	(-0.49)	(-0.89)
△LIQUIDITY	-0.0038	0.0035	0.9682	0.8368	0.8407	0.9917
	(-0.17)	(0.16)	(0.34)	(0.29)	(0.29)	(0.33)
Constant	-0.0123	-0.0107	-8.9950***	-8.3875***		
	(-0.68)	(-0.52)	(-7.69)	(-5.81)		
Time Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
Bank Fixed Effects	Yes	Yes	No	No	Yes	Yes
Observations	38100	34586	36291	33032	9388	8821
Adjusted R^2/Pseudo R^2	0.008	0.008	0.082	0.077	0.088	0.088

Notes:
This table examines the role of bank opacity in facilitating regulatory forbearance. The regression model is as follows:

$$EA_t = \beta_0 + \beta_1 OPACITY_t \times SENATOR_t + \beta_2 SENATOR_t + \beta_3 OPACITY_t + Controls + Fixed\ Effects + \varepsilon_t$$

The dependent variable *EA* represents enforcement actions the bank has been the subject of during the quarter. In columns (1) and (2), we use the number of enforcement actions that a bank has received during the quarter and fit OLS models. In columns (3) to (6), the dummy variable equals one if the bank has been the subject of enforcement action during the quarter, and zero otherwise. We fit the logit/conditional logit model in columns (3) to (6). The variable of interest is the interaction between bank opacity (*DLLP* or *DLLP_MS*) and BC senators (*SENATOR*). The sample period is from 1995Q1 to 2017Q4. Variable definitions are presented in Appendix C. We control for year and quarter fixed effects in all regressions and bank fixed effects in OLS specifications and conditional logit model. The *z*-/*t*-statistics in parentheses are based on standard errors clustered at the bank level. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels for two-tailed tests, respectively.

Table 6. Political Clout of BC Senators

Panel A. BC Senators and Bank Opacity

	DLLP	*DLLP_MS*	*DLLP*	*DLLP_MS*
	(1)	(2)	(3)	(4)
Senior	0.1348**	0.4026*		
	(2.46)	(1.79)		
Senior Chair			0.1796**	0.6330*
			(2.07)	(1.67)
Senior Member			0.1218**	0.3278
			(2.07)	(1.42)
$SENATOR_t$	0.0606**	0.2452***	0.0604**	0.2437***
	(2.56)	(2.62)	(2.55)	(2.60)
Control Variables	Yes	Yes	Yes	Yes
Time Fixed Effects	Yes	Yes	Yes	Yes
Bank Fixed Effects	Yes	Yes	Yes	Yes
Observations	43034	38509	43034	38509
Adjusted R2	0.258	0.475	0.258	0.475

Panel B. BC Senators and Enforcement Actions

	Enforcement Action			
	DLLP	*DLLP_MS*	*DLLP*	*DLLP_MS*
	(1)	(2)	(3)	(4)
Opacity×Senior	-0.1084	-0.0973		
	(-0.50)	(-1.02)		
Opacity×Senior Chair			-0.5255**	-0.3144***
			(-2.55)	(-4.24)
Opacity×Senior Member			0.0593	0.0059
			(0.12)	(0.03)
Opacity×SENATOR	-0.2632**	-0.0912**	-0.2647**	-0.0915**
	(-2.02)	(-2.38)	(-2.03)	(-2.40)
SENATOR	-0.8417**	-1.0950***	-0.8458**	-1.0986***
	(-2.43)	(-2.65)	(-2.44)	(-2.67)
Senior	-0.1250	-0.9184		
	(-0.23)	(-0.89)		
Senior Chair			-0.3769	-2.0182**
			(-0.49)	(-2.05)
Senior Member			-0.1336	-0.4847
			(-0.13)	(-0.25)
Opacity (DLLP/DLLP_MS)	0.1802*	0.0691**	0.1828*	0.0704***
	(1.79)	(2.56)	(1.81)	(2.61)
Control Variables	Yes	Yes	Yes	Yes
Time Fixed Effects	Yes	Yes	Yes	Yes
Bank Fixed Effects	No	No	No	No
Observations	36291	33032	36291	33032
Pseudo R^2	0.082	0.077	0.084	0.080

Notes:

This table presents the results of the moderating effects of BC senators' political clout. We collect details on US Congressional members from Charles Stewart's website (http://web.mit.edu/17.251/www/data_page.html). In columns (1) and (2), we include an indicator variable (*Senior*) equal to one if the BC senator has chamber seniority in the top decile. Chamber

seniority is measured as the number of years the senator has served in the Senate. In columns (3) and (4), we include variables to indicate whether the senior senator is also chairperson of the Banking Committee (*Senior Chair*) or not (*Senior Member*). In Panel A, the dependent variable is bank opacity, measured as discretionary loan loss provisions (*DLLP*) or the four-quarter moving sum of discretionary loan loss provisions (*DLLP_MS*), and we control for year and quarter fixed effects and bank fixed effects in all specifications. In Panel B, the dependent variable is a dummy variable equal to one if the bank has been the subject of enforcement action in the quarter, and we fit a logit model with year and quarter fixed effects. The sample period is from 1995Q1 to 2017Q4. Variable definitions are presented in Appendix C. The z/t-statistics in parentheses are based on standard errors clustered at the bank level. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels for two-tailed tests, respectively.

Table 7. Direct and Indirect Effect of BC Senators on Bank Real Outcomes

Panel A. Insolvency Risk

	Opacity = DLLP		*Opacity = DLLP_MS*	
	Coefficient	z-statistics	Coefficient	z-statistics
Total Effects	0.0667**	2.37	0.0662**	2.25
Direct Path				
p (SENATOR, Insolvency Risk)	0.0652**	2.32	0.0597**	2.04
Mediated Path for Opacity				
p (SENATOR, Opacity)	0.0680***	2.95	0.2783***	2.94
p (Opacity, Insolvency Risk)	0.0216***	4.58	0.0233***	7.56
Total Mediated Path for Opacity	0.0015**	2.52	0.0065***	2.80

Panel B. Loan Loss

	Opacity = DLLP		*Opacity = DLLP_MS*	
	Coefficient	z-statistics	Coefficient	z-statistics
Total Effects	0.0095**	2.22	0.0075*	1.71
Direct Path				
p (SENATOR, Loan Loss)	0.0087**	2.07	0.0054	1.28
Mediated Path for Opacity				
p (SENATOR, Opacity)	0.0645***	2.91	0.2452***	2.70
p (Opacity, Loan Loss)	0.0120***	9.28	0.0084***	11.58
Total Mediated Path for Opacity	0.0008***	2.73	0.0021***	2.61

Notes:
This table examines the real effects of BC senators. We estimate the structural models as follows: $Opacity_t = \beta_0 + \beta_1 SENATOR_t + Controls + YQtr + BANK + \varepsilon_t$, (5A)

$RealEffect_{t+1} = \gamma_0 + \gamma_1 Opacity_t + \gamma_2 SENATOR_t + Controls + YQtr + BANK + \varepsilon_t$, (5B)

In Panel A, bank insolvency risk is measured using *Insolvency Risk*, calculated as –ln((*ROA* + *CAR*)/std(*ROA*)). In Panel B, *Loan Loss* is calculated as net charge-offs divided by total loans. Both variables are measured in quarter $t + 1$. The variable *SENATOR* is an indicator variable equal to one if the bank is headquartered in a state with a senator on the Banking Committee. The coefficient γ_2 is the magnitude of direct path from *SENATOR* to real effects, the coefficient $\beta_1 \times \gamma_1$ is the magnitude of indirect path from *SENATOR* to real effects. The sample period is from 1995Q1 to 2017Q4. The list of control variables include *SIZE*, *GROWTH*, *TBTF* (too-big-too-fail), *LOSS*, and ΔNPA in the current and previous two periods. Details of variable definitions are presented in Appendix C. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels for two-tailed tests, respectively.

Table 8. Macroeconomic Conditions

	EC = Inadequate capital during recession (*IDQC*)		*EC* = Poor state economy (*POOR*)		*EC* = Weak state banking sector (*WBS*)	
	DLLP	*DLLP_MS*	*DLLP*	*DLLP_MS*	*DLLP*	*DLLP_MS*
	(1)	(2)	(3)	(4)	(5)	(6)
$SENATOR_t$	0.0644***	0.2641***	0.0362	0.1351	0.0567**	0.2469**
	(2.77)	(2.81)	(1.35)	(1.29)	(2.38)	(2.58)
$EC_t \times SENATOR_t$	***0.2843*****	***1.0054*****	***0.0645****	***0.2985*****	***0.1162*****	***0.3125*****
	(2.64)	***(2.87)***	***(2.26)***	***(2.85)***	***(2.88)***	***(2.62)***
$SIZE_t$	0.0346	0.0090	0.0375	0.0129	0.0339	0.0022
	(1.10)	(0.07)	(1.18)	(0.09)	(1.07)	(0.02)
LLP_{t-1}	0.4629***	3.2540***	0.6207***	3.7613***	0.4730***	3.2199***
	(9.61)	(19.48)	(9.57)	(16.36)	(8.10)	(15.49)
CAP_t	-0.0021	-0.0207	-0.0039	-0.0269	-0.0008	-0.0173
	(-0.39)	(-0.97)	(-0.67)	(-1.12)	(-0.14)	(-0.80)
$LOSS_t$	0.8724***	1.0607***	0.9088***	1.1264***	0.8149***	0.9861***
	(26.05)	(12.72)	(19.71)	(9.62)	(21.61)	(10.72)
$TIER_t$	0.0092**	0.0491**	0.0121**	0.0666***	0.0081*	0.0473**
	(1.98)	(2.56)	(2.32)	(3.22)	(1.71)	(2.42)
EBP_t	0.2050***	0.0729	0.2259***	0.0548	0.1934***	0.0913
	(5.96)	(0.63)	(5.64)	(0.38)	(5.44)	(0.74)
RC_t	0.3585	6.1935***	0.2072**	0.7960**	0.0338	0.3029
	(0.63)	(3.50)	(2.20)	(2.29)	(0.23)	(0.62)
$EC_t \times SIZE_t$	-0.0786**	-0.4464***	-0.0109	-0.0457	-0.0204	-0.0380
	(-2.00)	(-3.42)	(-1.16)	(-1.31)	(-1.31)	(-0.75)
$EC_t \times LLP_{t-1}$	-0.1876	-1.1302***	-0.3245***	-1.0495***	-0.0810	-0.0871
	(-1.11)	(-3.21)	(-4.37)	(-4.40)	(-1.13)	(-0.42)
$EC_t \times CAP_t$	-0.0265	-0.0757	0.0019	0.0065	-0.0135*	-0.0401*
	(-1.00)	(-0.74)	(0.37)	(0.32)	(-1.87)	(-1.76)
$EC_t \times LOSS_t$	-0.2123	-0.1028	-0.0768	-0.1181	0.2190***	0.2266
	(-1.19)	(-0.26)	(-1.26)	(-0.77)	(3.30)	(1.47)
$EC_t \times TIER_t$	0.0804	-0.3180	-0.0049	-0.0341*	0.0145*	0.0227
	(0.99)	(-1.33)	(-0.95)	(-1.79)	(1.90)	(0.98)
$EC_t \times EBP_t$	-0.1369	0.3706	-0.0572	0.0397	0.0350	-0.1134

	(-1.07)	(1.02)	(-1.30)	(0.27)	(0.59)	(-0.72)
$CSRET_t$	-0.0176**	-0.0186*	-0.0182**	-0.0199*	-0.0182**	-0.0194*
	(-2.25)	(-1.68)	(-2.34)	(-1.80)	(-2.34)	(-1.76)
$\triangle GDP_t$	-0.0466***	-0.1199***	-0.0409***	-0.0954***	-0.0461***	-0.1191***
	(-10.01)	(-7.39)	(-6.64)	(-4.45)	(-10.00)	(-7.39)
$\triangle UNEMP_t$	0.0697***	0.0033	0.0712***	0.0103	0.0686***	-0.0020
	(2.75)	(0.05)	(2.85)	(0.16)	(2.71)	(-0.03)
Constant	-3.3308***	-12.4447***	-3.4295***	-12.7821***	-3.3212***	-12.4018***
	(-15.52)	(-13.32)	(-15.69)	(-13.71)	(-15.38)	(-13.23)
Time Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
Bank Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
Observations	43034	38509	43034	38509	43034	38509
Adjusted R^2	0.258	0.477	0.259	0.478	0.259	0.476

Notes:
This table examines the moderating effects of economic conditions on the relation between BC senators and bank opacity. In columns (1) and (2), we measure economic conditions using an indicator variable (*IDQC*) equal to one when banks have inadequate capital during the recession, and zero otherwise. In columns (3) and (4), we measure economic conditions using an indicator variable (*POOR*) for poor state economy equal to one if the state's GDP growth is below the sample median, and zero otherwise. In columns (5) and (6), we measure economic conditions using an indicator variable (*WBS*) for a weak state banking sector that equals one if the percentage of state banks that were or would be closed without assistance is above the sample median, and zero otherwise. The dependent variable is bank opacity, measured as discretionary loan loss provisions (*DLLP*), or the four-quarter moving sum of discretionary loan loss provisions (*DLLP_MS*). The sample period is from 1995Q1 to 2017Q4. Variable definitions are presented in Appendix C. We control for year and quarter fixed effects and bank fixed effects in all specifications. The *t*-statistics in parentheses are based on standard errors clustered at the bank level. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels for two-tailed tests, respectively.

Table 9. Capital Market Consequences

	RATING		*YIELD*	
	(1)	(2)	(3)	(4)
SENATOR×DLLP	***-0.1205******		***-0.0930*****	
	(-5.97)		***(-2.81)***	
DLLP	0.0965***		0.0140	
	(4.57)		(0.56)	
SENATOR×DLLP_MS		***-0.0457*****		***-0.0272****
		(-6.90)		***(-2.11)***
DLLP_MS		0.0411***		-0.0028
		(5.67)		(-0.25)
SENATOR	-0.2984***	-0.4543***	-0.1124	-0.1570
	(-4.66)	(-6.26)	(-1.24)	(-1.25)
SIZE	-0.8859***	-0.8976***	-0.3982***	-0.3962***
	(-10.06)	(-13.88)	(-2.86)	(-2.85)
LEV	0.9185	0.8373	4.3868***	4.6319***
	(1.25)	(1.29)	(4.48)	(4.71)
TIER	0.1184***	0.1073***	0.0604***	0.0628***
	(6.20)	(5.82)	(3.82)	(3.65)
EBP	-0.3097***	-0.3024***	-0.1451***	-0.1328***
	(-10.25)	(-11.10)	(-3.91)	(-3.48)
LOAN	1.0439***	1.0041***	-0.8899*	-1.0400*
	(5.02)	(5.23)	(-1.65)	(-1.95)
VOLATILITY	51.4389***	51.7587***	62.6036***	64.9515***
	(9.19)	(10.08)	(11.39)	(11.62)
MB	-1.2610***	-1.2705***	-0.3868***	-0.3869***
	(-15.53)	(-18.77)	(-3.66)	(-3.62)
MATURITY	0.0057	0.0061	-0.0171	-0.0204
	(0.53)	(0.62)	(-0.33)	(-0.39)
$MATURITY^2$	0.0228***	0.0236***	0.1161***	0.1151***
	(3.03)	(4.00)	(5.23)	(5.16)
AMOUNT	0.0386***	0.0380***		
	(3.45)	(3.77)		
SUBORDINATE	0.7805***	0.8070***		
	(15.46)	(18.38)		
Constant			3.9293*	3.7924*
			(1.93)	(1.87)
Time Fixed Effects	Yes	Yes	Yes	Yes
Bond Fixed Effects	No	No	Yes	Yes
Observations	68992	68898	62866	62773
Pseudo R^2 /Adjusted R^2	0.220	0.215	0.678	0.678

Notes:
This table examines market perceptions of opacity and the role of BC senators. The regression model is as follows:

$$BOND_t = \beta_0 + \beta_1 SENATOR_t \times OPACITY_t + \beta_2 OPACITY_t + \beta_3 SENATOR_t + \beta_4 SIZE_t + \beta_5 LEV_t + \beta_6 TIER_t + \beta_7 EBP_t + \beta_8 LOAN_t + \beta_9 VOLATILITY_t + \beta_{10} MB_t + \beta_{11} MATURITY_t + \beta_{12} MATURITY_t^2 + \beta_{13} AMOUNT_t + \beta_{14} SUBORDINATE_t + Fixed\ Effects + \varepsilon_t$$

In columns (1) and (2), the dependent variable is *RATING*, defined as the average of the bond rating scores assigned by S&P, Moody's, and Fitch, where higher values indicate lower credit quality. We fit an ordered probit model because *RATING* is not a continuous variable. In columns (3) and (4), the dependent variable is *YIELD*, which is the bond yield minus the maturity-matched US Treasury yield (%). We fit an OLS model. The variable of interest is the interaction of bank opacity (*OPACITY*) and BC senators (*SENATOR*). The variable *OPACITY* is measured as *DLLP* in columns (1) and (3), and *DLLP_MS* in columns (2) and (4). Our sample period is from July 2002

to December 2017 due to data availability. Variable definitions are presented in Appendix C. We control for fixed effects in all specifications. The *z*-/*t*-statistics in parentheses are based on standard errors clustered at the bond level. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels for two-tailed tests, respectively.

APPENDIX A. The Lincoln Case

In 1985, Edwin J. Gray, chair of the Federal Home Loan Bank Board (FHLBB), instituted the rule that savings associations could hold no more than 10% of their assets in direct investments. The regulation was in response to the savings industry's increasing risky investment practices in the 1980s, which exposed the government's insurance funds to huge losses. In 1986, the FHLBB investigated the investment practices of the Lincoln Savings and Loan Association of Irvine, California, and found that Lincoln had directed FDIC-insured accounts into commercial real estate ventures and surpassed the regulated direct investment limit by $600 million. Moreover, the company had hidden losses of $135 million. The regulators recommended that Lincoln be seized by the government for insolvency.

Lincoln's chairman, Charles Keating, had several senators help him convince the federal regulators to take no enforcement actions. Among the senators, he pushed Alan Cranston, the then Democrat Senator of California and a senior member on the Senate Banking Committee of the 100th Congress, to remove Gray from any FHLBB discussions regarding Lincoln's case. In March 1987, Donald W. Riegle, Jr., the then Democrat Senator of Michigan and also a senior member on the Senate Banking Committee, told Gray that "some senators out west are very concerned about the way the bank board is regulating Lincoln Savings."[34] In April 1987, the Senators held two secret meetings with FHLBB regulators (one with Gray and the other with members of FHLBB's San Francisco branch) in the office of Dennis DeConcini, the then Democrat senator of Arizona, to discuss the government's investigation of Lincoln.[35] During the meetings, the senators threatened to cripple a bill that contained a provision to restore FHLBB's full conservatorship powers and give the agency the funds to close more of the worst frauds if it refused to accept the deal the senators proposed.[36] The regulators later said they felt pressured and in some cases intimidated. After the April 1987 meetings, Cranston and DeConcini continued intervening on behalf of Keating, applying political pressure on both Danny Wall, Gray's successor, California state regulators, and the FDIC. Because of these interventions, the FHLBB San Francisco branch was removed from the Lincoln investigation in September 1987, and, in May 1988, FHLBB signed an agreement with Lincoln that included not proceeding with a criminal referral to the Department of Justice. Lincoln stayed in business from mid-1987 to April 1989 and its assets grew from $3.91 billion to $5.46 billion during the same period. It finally collapsed in 1989, at a cost of over $2 billion to taxpayers.[37]

After Lincoln's failure, former FHLBB chair Gray went public about the senators' intervention and said that they had sought "to directly subvert the regulatory process" to benefit Keating in the April 1987 meetings.[38] In 1991, the Senate Ethics Committee ruled that Cranston, DeConcini, and Riegle had substantially and improperly interfered with the FHLBB's investigation of Lincoln Savings, with Cranston receiving a formal reprimand. After the ruling, however, Cranston rebutted his reprimand on the floor of the

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[34] Binstein, Michael, and Bowden, Charles (1993). *Trust Me: Charles Keating and the Missing Billions*. Random House.

[35] Riegle's constituency connection to Keating was that Keating's Hotel Pontchartrain was located in Michigan, and DeConcini considered Keating a constituent because Keating lived in Arizona.

[36] Black, William (2012). "We Were Regulators Once: Ed Gray's Finest Hour." *New Economic Perspectives*, April 1.

[37] FDIC (2002). "The S&L Crisis: A Chrono-Bibliography." December 20, https://www.fdic.gov/bank/historical/sandl.

[38] Dougherty, John (1993). "DeConcini & Keating." *Phoenix New Times,* July 14.

Senate, stating that, if he was guilty of wrongdoing, then so was the entire Senate.[39] DeConcini said that he would continue to be aggressive in representing his constituents in their affairs with federal regulators. Cranston's attorney argued that "the real problem for the 'Keating Three' who were most involved was that they had been caught."[40] These arguments suggest that senators' intervention in the regulatory process is likely common.

[39] Berke, Richard (1991). "Cranston Rebuked by Ethics Panel." *The New York Times*, November 21.

[40] Gould, Lewis J. (2005). *The Most Exclusive Club: A History of the Modern United States Senate*. Basic Books.

APPENDIX B. Estimation Results of the Loan Loss Provision Model

In this appendix, we present estimates from the OLS regression that we use to extract the discretionary loan loss provisions. The regression model is as follows:

$$LLP_t = \propto_0 + \propto_1 \Delta NPA_{t+1} + \propto_2 \Delta NPA_t + \propto_3 \Delta NPA_{t-1} + \propto_4 \Delta NPA_{t-2} + \propto_5 SIZE_{t-1} + \propto_6 \Delta LOAN_t + \propto_7 SENATOR_t + \propto_8 SENATOR_t \times \Delta NPA_{t+1} + \propto_9 SENATOR_t \times \Delta NPA_t + \propto_{10} SENATOR_t \times \Delta NPA_{t-1} + \propto_{11} SENATOR_t \times \Delta NPA_{t-2} + \propto_{12} SENATOR_t \times SIZE_{t-1} + \propto_{13} SENATOR_t \times \Delta LOAN_t + \propto_{14} CSRET_t + \propto_{15} \Delta GDP_t + \propto_{16} \Delta UNEMP_t + STATE + \varepsilon_t$$

The dependent variable LLP_t is loan loss provisions. Details of variable definitions are presented in Appendix C. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels for two-tailed tests, respectively.

	Dependent Variable = LLP_t
$\triangle NPA_{t+1}$	0.0124***
	(5.03)
$\triangle NPA_t$	0.0604***
	(23.82)
$\triangle NPA_{t-1}$	0.0718***
	(28.18)
$\triangle NPA_{t-2}$	0.0734***
	(28.63)
$SIZE_{t-1}$	0.0123***
	(14.26)
$\triangle LOAN_t$	-0.3919***
	(-16.43)
SENATOR	-0.0031
	(-0.36)
$SENATOR \times \triangle NPA_{t+1}$	-0.0079*
	(-2.20)
$SENATOR \times \triangle NPA_t$	-0.0234***
	(-6.41)
$SENATOR \times \triangle NPA_{t-1}$	-0.0292***
	(-8.02)
$SENATOR \times \triangle NPA_{t-2}$	-0.0203***
	(-5.57)
$SENATOR \times SIZE_{t-1}$	0.0016
	(1.31)
$SENATOR \times \triangle LOAN_t$	0.0161
	(0.47)
$CSRET_t$	-0.0147***
	(-30.29)
$\triangle GDP_t$	-0.0104***
	(-23.44)
$\triangle UNEMP_t$	0.0337***
	(10.62)
Constant	0.0681***
	(3.84)
State Fixed effects	Yes
Observations	49341
Adjusted R^2	0.205

APPENDIX C. Variable Definitions

Variable	Definition
LLP	Loan loss provisions (pllq) scaled by lagged total loans (lntalq). We multiply by 100 for presentation.
SENATOR	Indicator variable, equal to 1 if the bank is headquartered in a state with a senator representative on the Banking Committee in that year–quarter, and 0 otherwise.
NPA	Nonperforming assets (naptq) divided by lagged total loans.
⊿NPA	Change in nonperforming assets divided by lagged total loans. We multiply by 100 for presentation.
SIZE	The natural logarithm of total assets (atq).
LOAN	Total loans divided by total assets.
⊿LOAN	Change in total loans divided by lagged total loans.
CSRET	The return on the Case-Shiller Real Estate Index over the quarter. We multiply by 100 for presentation.
⊿GDP	Percent change in GDP by state.
⊿UNEMP	Change in state unemployment percentages over the quarter.
DLLP	Discretionary loan loss provisions, equal to the natural logarithm of the absolute values of the residuals estimated from Eq. (1) (see Appendix B for the regression results).
DLLP_MS	Four-quarter moving sum of *DLLP* (Hutton et al., 2009).
CAP	Book value of equity over total assets. We multiply by 100 for presentation.
LOSS	Indicator variable for loss firm, equal to 1 if the bank reports negative net income (niq) in the quarter, and 0 otherwise.
TIER	Tier 1 risk-adjusted capital ratio (capr1q).
⊿TIER	Change in *TIER* over the quarter, where *TIER* is defined above.
EBP	Earnings before loan loss provisions and taxes (piq + pllq) scaled by lagged total loans. We multiply by 100 for presentation.
IMPORT	Indicator variable for the bank's relative importance. We first calculate the bank's relative importance as its total assets divided by the sum of the total assets of all banks headquartered in the same state. If the bank's relative importance is larger than the median value of the year–quarter, then *IMPORT* equals 1, and otherwise it equals 0.
VOLATILITY	Volatility of stock returns, defined as the standard deviation of daily returns over a quarter. We require at least 20 observations to estimate the variable.
LEV	Long-term debt (dlttq) divided by total assets.
⊿LEV	Change in *LEV* over the quarter, where *LEV* is defined above.
EA	Enforcement actions the bank has been the subject of during the quarter (not including those against individuals).

ROE	Return on equity, calculated as earnings before loan loss provisions, divided by equity.
DEPOSIT	The ratio of total deposits (dptcq) to total assets.
⊿DEPOSIT	Change in total deposits over the quarter, scaled by total assets at the beginning of the quarter.
⊿LIQUIDITY	Change in the ratio of cash to total deposits.
Senior	Indicator variable for a senior senator, equal to 1 if the BC senator has a chamber seniority in the top decile, where chamber seniority is measured as the number of years the senator has served in the Senate.
Senior Chair	Indicator variable equal to 1 if a senior senator is also the chair of the Banking Committee.
Senior Member	Indicator variable equal to 1 if a senior senator is not the chair of the Banking Committee.
Insolvency Risk	Banks' risk taking measure, calculated as -1 multiplied by ln((*ROA* + *CAR*)/std(*ROA*)), where *ROA* is the rate of return on assets, *CAR* is the capital adequacy ratio, and std(*ROA*) is an estimate of the standard deviation of the rate of return on assets. A larger value indicates higher bank risk.
Loan Loss	Banks' risk taking measure, defined as the net charge-offs divided by the total loans. A higher amount of credit charge-offs represents higher bank risk.
GROWTH	Asset growth in the quarter.
TBTF	Dummy variable equal to 1 if the bank's share of the state's total deposits exceeds 10%.
IDQC	Indicator variable for banks with inadequate capital during a recession. Tier 1 risk-adjusted capital ratios in the quarterly bottom decile are deemed inadequate for banks. Recession indicates periods between 2001Q2 and 2001Q4, and periods between 2008Q1 and 2009Q2, and 0 otherwise;
POOR	Indicator variable for a poor state economy, equal to 1 if the state's GDP growth is below the sample median, and 0 otherwise.
WBS	Indicator variable for a weak state banking sector, equal to 1 if the percentage of banks that were or would be closed without assistance in the state is above the sample median, and 0 otherwise.
RATING	Bond ratings, defined as the average of the bond rating scores assigned by S&P, Moody's and Fitch. Higher values indicate lower credit quality.
YIELD	Bond yield minus the maturity-matched US Treasury yield (%). The daily Treasury constant maturity rates are provided by the Board of Governors of the Federal Reserve System. We interpolate (or extrapolate, where necessary) the risk-free rate associated with each bond based upon the number of months remaining until the debt matures.
MB	Market-to-book ratio, calculated as the market value of equity divided by the book value of equity.
MATURITY	The natural logarithm of the number of years to maturity.

AMOUNT	The natural logarithm of the offering amount of the bond.
SUBORDINATE	Indicator variable for a subordinated bond, equal to 1 if the bond is subordinated, and 0 otherwise.

ONLINE APPENDIX

(NOT INTENDED FOR PUBLICATION)

Table OA1. Robustness: Measuring Opacity without Senator Interaction Items

	DLLP		*DLLP_MS*	
	(1)	(2)	(3)	(4)
SENATORt	***0.0747****	***0.0790****	***0.3127****	***0.3042****
	(3.21)	***(3.51)***	***(3.31)***	***(3.34)***
$SIZE_t$		0.0314		0.0148
		(0.99)		(0.11)
LLP_{t-1}		0.4612***		3.1612***
		(9.85)		(19.37)
CAP_t		-0.0016		-0.0265
		(-0.31)		(-1.26)
$LOSS_t$		0.8584***		1.0271***
		(25.72)		(12.43)
$TIER_t$		0.0081*		0.0505***
		(1.77)		(2.66)
EBP_t		0.1884***		0.0469
		(5.47)		(0.39)
$CSRET_t$		-0.0165**		-0.0156
		(-2.14)		(-1.41)
$\triangle GDP_t$		-0.0458***		-0.1188***
		(-9.81)		(-7.43)
$\triangle UNEMP_t$		0.0637**		-0.0283
		(2.30)		(-0.43)
Constant	-2.9702***	-3.3011***	-12.0200***	-12.4362***
	(-61.48)	(-15.47)	(-57.20)	(-13.38)
Time Fixed Effects	Yes	Yes	Yes	Yes
Bank Fixed Effects	Yes	Yes	Yes	Yes
Observations	43034	43034	38509	38509
Adjusted R^2	0.222	0.263	0.438	0.481

Notes: This table presents the results of OLS regressions of bank opacity on BC senator. The model is as follows:

$$OPACITY_t = \beta_0 + \beta_1 SENATOR_t + \beta_2 SIZE_t + \beta_3 LLP_{t-1} + \beta_4 CAP_t + \beta_5 LOSS_t + \beta_6 TIER_t + \beta_7 EBP_t + Macro_t + YQtr + BANK + \varepsilon_t$$

The dependent variable is bank opacity, measured as discretionary loan loss provisions (*DLLP*), or the four quarter moving sum of discretionary loan loss provisions (*DLLP_MS*). The measurement is different from Table 2 in that we do not include senator interaction items when estimating the *DLLP* model. *SENATOR* is an indicator variable equal to 1 if the bank is headquartered in a state with senator representative on the Banking Committee. The sample period is from 1995Q1 to 2017Q4. Details of variable definitions are presented in Appendix C. We control for year and quarter fixed effects and bank fixed effects in all specifications. The t-statistics in parentheses are based on standard errors clustered at the bank level. *, **, *** indicate statistical significance at the 10 percent, 5 percent, and 1 percent levels for two-tailed tests, respectively.

Table OA2. Robustness: Measuring Opacity with Year Fixed Effects

	DLLP		*DLLP_MS*	
	(1)	(2)	(3)	(4)
SENATOR$_t$	***0.0495****	***0.0555****	***0.2285****	***0.2217****
	(2.00)	***(2.23)***	***(2.25)***	***(2.20)***
SIZE$_t$		0.0196		-0.0563
		(0.59)		(-0.39)
LLP$_{t-1}$		0.1699***		2.0857***
		(3.09)		(10.13)
CAP$_t$		0.0128**		0.0317
		(2.19)		(1.27)
LOSS$_t$		0.7053***		0.9594***
		(18.93)		(10.03)
TIER$_t$		-0.0010		0.0125
		(-0.18)		(0.55)
EBP$_t$		0.1755***		0.0448
		(4.44)		(0.33)
CSRET$_t$		0.0026		0.0647***
		(0.42)		(6.71)
△GDP$_t$		-0.0235***		-0.0626***
		(-5.33)		(-3.83)
△UNEMP$_t$		0.0193		0.2673***
		(0.80)		(3.83)
Constant	-3.1089***	-3.4166***	-12.2835***	-12.4038***
	(-57.78)	(-15.20)	(-53.45)	(-12.86)
Time Fixed Effects	Yes	Yes	Yes	Yes
Bank Fixed Effects	Yes	Yes	Yes	Yes
Observations	43034	43034	38509	38509
Adjusted R^2	0.297	0.314	0.508	0.525

Notes: This table presents the results of OLS regressions of bank opacity on BC senator. The model is as follows:

$$OPACITY_t = \beta_0 + \beta_1 SENATOR_t + \beta_2 SIZE_t + \beta_3 LLP_{t-1} + \beta_4 CAP_t + \beta_5 LOSS_t + \beta_6 TIER_t + \beta_7 EBP_t + Macro_t + YQtr + BANK + \varepsilon_t$$

The dependent variable is bank opacity, measured as discretionary loan loss provisions (*DLLP*), or the four quarter moving sum of discretionary loan loss provisions (*DLLP_MS*). The measurement is different from Table 2 in that we include time fixed effects when estimating the *DLLP* model. *SENATOR* is an indicator variable equal to 1 if the bank is headquartered in a state with senator representative on the Banking Committee. The sample period is from 1995Q1 to 2017Q4. Details of variable definitions are presented in Appendix C. We control for year and quarter fixed effects and bank fixed effects in all specifications. The t-statistics in parentheses are based on standard errors clustered at the bank level. *, **, *** indicate statistical significance at the 10 percent, 5 percent, and 1 percent levels for two-tailed tests, respectively.

Table OA3. Controlling for Representatives of the House Committee on Financial Services

	DLLP	*DLLP_MS*
	(1)	(2)
House Chair$_t$	***0.0935***	***0.3854****
	(1.60)	***(1.69)***
House Member$_t$	***-0.0072***	***-0.0363***
	(-0.21)	***(-0.27)***
SENATOR$_t$	0.0747***	0.2965***
	(3.21)	(3.24)
SIZE$_t$	0.0298	-0.0173
	(0.95)	(-0.13)
LLP$_{t-1}$	0.4499***	2.9372***
	(9.54)	(19.91)
CAP$_t$	-0.0028	-0.0219
	(-0.53)	(-1.05)
LOSS$_t$	0.8670***	1.0012***
	(26.21)	(12.52)
TIER$_t$	0.0090*	0.0462**
	(1.94)	(2.47)
EBP$_t$	0.2040***	0.0716
	(5.96)	(0.63)
CSRET$_t$	-0.0177**	-0.0212*
	(-2.28)	(-1.95)
△GDP$_t$	-0.0463***	-0.1196***
	(-9.93)	(-7.57)
△UNEMP$_t$	0.0688***	0.0173
	(2.73)	(0.27)
Constant	-3.2894***	-12.1527***
	(-15.35)	(-13.38)
Time Fixed Effects	Yes	Yes
Bank Fixed Effects	Yes	Yes
Observations	43034	38509
Adjusted R^2	0.258	0.475

Notes: This table examines whether the House representatives of the Banking Committee have similar effects on bank opacity. We manually collect historical membership of the House Committee on Financial Services from annual volumes of the Official Congressional Directory. *House Chair* indicates whether the bank is headquartered in a state with a House representative who is the chair of the House Committee on Financial Services, and *House Member* indicates whether the bank is headquartered in a state with a House representative who is a member of the House Committee on Financial Services. The dependent variable is bank opacity, measured as discretionary loan loss provisions (*DLLP*), or the four-quarter moving sum of discretionary loan loss provisions (*DLLP_MS*). The sample period is from 1995Q1 to 2017Q4. Details of variable definitions are presented in Appendix C. We control for year and quarter fixed effects and bank fixed effects in all specifications. The t-statistics in parentheses are based on standard errors clustered at the bank level. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels for two-tailed tests, respectively.

Table OA4. Change of Opacity around the Exogenous Departure of BC Senator

	DLLP
DEPARTRUE×QTR+1	-0.2968**
	(-2.49)
DEPARTRUE×QTR+2	-0.1834*
	(-1.67)
DEPARTRUE×QTR+3	-0.1902*
	(-1.91)
DEPARTRUE×QTR+4	-0.0771
	(-0.80)
DEPARTRUE×QTR+5	-0.1069
	(-0.99)
DEPARTRUE×QTR+6	-0.3183***
	(-2.71)
DEPARTRUE×QTR+7	-0.2802**
	(-2.45)
DEPARTRUE×QTR+8	-0.1487
	(-1.14)
DEPARTRUE×QTR-1	-0.0709
	(-0.75)
DEPARTRUE×QTR-2	-0.1332
	(-1.32)
DEPARTRUE×QTR-3	-0.0740
	(-0.63)
DEPARTRUE×QTR-4	-0.0485
	(-0.48)
DEPARTRUE×QTR-5	0.0039
	(0.05)
DEPARTRUE×QTR-6	0.0310
	(0.52)
DEPARTRUE×QTR-7	-0.0918
	(-1.50)
Controls	Yes
Time Fixed Effects	Yes
Bank Fixed Effects	Yes
Observations	7593
Adjusted R^2	0.309

Notes: This table examines the change of bank opacity around the unexpected departures of BC senators. The variable *Departure* is an indicator variable equal to one if the bank experienced a plausibly exogenous departure of their BC senator because of a committee transfer or resignation, and *QTR+t* (*-t*) is an indicator variable equal to one if the year–quarter is t quarters after (before) the departure. The regression includes a matched sample of banks that did not experience BC senator turnovers. The dependent variable is bank opacity, measured as discretionary loan loss provisions (*DLLP*). Variable definitions are presented in Appendix C. We control for time fixed effects and bank fixed effects. The *t*-statistics in parentheses are based on standard errors clustered at the bank level. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels for two-tailed tests, respectively.

Table OA5. The effect of BC Senator on the Relation between Financial Indicators and Enforcement

	Enforcement Action			
	(1)	(2)	(3)	(4)
LowCAR×senator	***-0.3312***			
	(-1.13)			
LowCAR	0.5341**			
	(2.20)			
LowQuality×senator		***-0.4273***		
		(-1.61)		
LowQuality		0.5178**		
		(2.33)		
LowProfit×senator			***-0.2274***	
			(-0.85)	
LowProfit			0.0382	
			(0.19)	
LowLiquid×senator				***-0.4594****
				(-1.74)
LowLiquid				-0.0377
				(-0.20)
SENATOR	-0.0193	0.0730	-0.0875	0.0081
	(-0.09)	(0.33)	(-0.43)	(0.04)
SIZE	0.4516***	0.4540***	0.4473***	0.4422***
	(10.67)	(10.72)	(10.49)	(10.30)
LEV	-0.8943	-0.8607	-0.8903	-0.8289
	(-0.72)	(-0.70)	(-0.73)	(-0.66)
TIER	0.0047	-0.0446	-0.0409	-0.0465
	(0.13)	(-1.53)	(-1.41)	(-1.59)
NPA	8.1635***	6.7931**	8.2932***	7.8657***
	(3.13)	(2.45)	(3.21)	(3.00)
ROE	-3.4236*	-3.3873*	-3.8198	-3.2290
	(-1.71)	(-1.69)	(-1.55)	(-1.61)
DEPOSIT	1.4138	1.4776	1.3018	1.2424
	(1.22)	(1.29)	(1.13)	(1.06)
△LOAN	-1.3167	-1.2951	-1.2821	-1.2500
	(-0.82)	(-0.82)	(-0.80)	(-0.79)
△LIQUIDITY	1.3674	1.4526	1.3762	0.4542
	(0.51)	(0.53)	(0.51)	(0.17)
Constant	-10.6725***	-10.1958***	-9.7777***	-9.6508***
	(-8.20)	(-8.75)	(-8.25)	(-8.23)
Time Fixed Effects	Yes	Yes	Yes	Yes
Observations	37243	37243	37243	37243
Pseudo R^2	0.080	0.080	0.079	0.080

Notes: This table examines whether BC senators affect enforcement actions conditional on other key financial statement variables. The dependent variable is a dummy variable, which equals to 1 if the bank has received enforcement action during the quarter, and 0 otherwise. We fit the logit model with time fixed effects. *LowCAR* is an indicator variable, equal to 1 if the tier 1 risk-adjusted capital ratio is below sample median, and 0 otherwise; *LowQuality* is an indicator variable, equal to 1 if *NPA* is above sample median, and 0 otherwise; *LowProfit* is an indicator variable, equal to 1 if *ROE* is below sample median, and 0 otherwise; *LowLiquid* is an indicator variable, equal to 1 if the ratio of cash to deposits is below sample median, and 0 otherwise. The sample period is from 1995Q1 to 2017Q4. Details of other variable definitions are presented in Appendix C. The z-statistics in parentheses are based on standard errors clustered at the bank level. *, **, *** indicate statistical significance at the 10 percent, 5 percent, and 1 percent levels for two-tailed tests, respectively.

Table OA6. The Political Environments of BC Senators

Panel A. BC Senators and Bank Opacity

	DLLP	*DLLP_MS*	*DLLP*	*DLLP_MS*	*DLLP*	*DLLP_MS*
	(1)	(2)	(3)	(4)	(5)	(6)
Senior Majority	0.1505*	0.6573**				
	(1.84)	(1.98)				
Senior Minority	0.1250*	0.2287				
	(1.95)	(0.96)				
Senior HouseALG			0.1920*	1.0899***		
			(1.66)	(2.76)		
Senior nonHouseALG			0.1214**	0.2200		
			(2.01)	(0.94)		
Senior PresidentALG					0.1056	0.6275**
					(1.50)	(2.19)
Senior nonPresidentALG					0.1552**	0.2526
					(2.38)	(0.98)
$SENATOR_t$	0.0606**	0.2433***	0.0605**	0.2427***	0.0605**	0.2459***
	(2.56)	(2.60)	(2.55)	(2.59)	(2.55)	(2.63)
Control Variables	Yes	Yes	Yes	Yes	Yes	Yes
Time Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
Bank Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
Observations	43034	38509	43034	38509	43034	38509
Adjusted R2	0.258	0.475	0.258	0.475	0.258	0.475
Test the different effects of political environments	*Senior Majority vs Senior Minority*		*Senior HouseALG vs. nonHouseALG*		*Senior PresidentALG vs. Senior nonPresidentALG*	
P-value	0.40	0.12	0.29	0.02	0.27	0.10

Panel B. BC Senators and Enforcement Actions

	DLLP	*DLLP_MS*	*DLLP*	*DLLP_MS*	*DLLP*	*DLLP_MS*
	(1)	(2)	(3)	(4)	(5)	(6)
Opacity×Senior Majority	-0.4515**	-0.3123***				
	(-2.21)	(-4.24)				
Opacity×Senior Minority	0.0598	0.0173				
	(0.14)	(0.10)				
Opacity×Senior HouseALG			0.3153	-0.1382*		
			(1.53)	(-1.68)		
Opacity×Senior nonHouseALG			-0.0888	-0.0827		
			(-0.42)	(-0.82)		
Opacity×Senior PresidentALG					-0.6242***	-0.5893***
					(-3.92)	(-4.89)
Opacity×Senior nonPresidentALG					0.1671	0.0049
					(0.68)	(0.07)
Opacity×SENATOR	-0.2639**	-0.0914**	-0.2625**	-0.0911**	-0.2625**	-0.0912**
	(-2.02)	(-2.39)	(-2.02)	(-2.38)	(-2.02)	(-2.38)
SENATOR	-0.8428**	-1.0963***	-0.8401**	-1.0943***	-0.8404**	-1.0970***
	(-2.43)	(-2.66)	(-2.43)	(-2.65)	(-2.43)	(-2.66)
Senior Majority	-0.6102	-2.4157**				
	(-0.81)	(-2.41)				
Senior Minority	0.0268	-0.2269				
	(0.03)	(-0.13)				
Senior HouseALG			0.0891	-1.6051		
			(0.10)	(-1.59)		
Senior nonHouseALG			0.0636	-0.6855		
			(0.12)	(-0.61)		
Senior PresidentALG					-2.1798*	-8.3961***
					(-1.72)	(-5.13)
Senior nonPresidentALG					0.7689	0.4292
					(1.53)	(0.68)
Opacity (DLLP/DLLP_MS)	0.1815*	0.0700***	0.1792*	0.0690**	0.1798*	0.0692**
	(1.80)	(2.59)	(1.78)	(2.56)	(1.79)	(2.56)
Control Variables	Yes	Yes	Yes	Yes	Yes	Yes
Time Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
Bank Fixed Effects	No	No	No	No	No	No

Observations	36291	33032	36291	33032	36291	33032
Pseudo R^2	0.083	0.079	0.082	0.077	0.083	0.079
Test the different effects of political environments	*Senior Majority vs Senior Minority*		*Senior HouseALG vs. nonHouseALG*		*Senior PresidentALG vs. Senior nonPresidentALG*	
P-value	0.14	0.05	0.07	0.35	0.01	0.01

Notes: This table presents the results of the moderating effects of BC senators' political environments. We collect details on US Congressional members from Charles Stewart's website (http://web.mit.edu/17.251/www/data_page.html). In columns (1) and (2), we include variables to indicate whether the senior senator is a member of the majority party (*Senior Majority*) or not (*Senior Minority*). In columns (3) and (4), we include variables to indicate whether the senior senator is a member of the party that controls both chambers (*Senior HouseALG*) or not (*Senior nonHouseALG*). In columns (5) and (6), we include variables to indicate whether the senior senator is from the same party as the president (*Senior PresidentALG*) or not (*Senior nonPresidentALG*). In Panel A, the dependent variable is bank opacity, measured as discretionary loan loss provisions (*DLLP*) or the four-quarter moving sum of discretionary loan loss provisions (*DLLP_MS*), and we control for year and quarter fixed effects and bank fixed effects in all specifications. In Panel B, the dependent variable is a dummy variable equal to one if the bank has been the subject of enforcement action in the quarter, and we fit a logit model with year and quarter fixed effects. The sample period is from 1995Q1 to 2017Q4. Variable definitions are presented in Appendix C. The *z*/*t*-statistics in parentheses are based on standard errors clustered at the bank level. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels for two-tailed tests, respectively.

Table OA7. Macroeconomic Conditions and Liquidity Creation

	Future Loan Growth (LG_{t+1})		
	IDQC	*POOR*	*WBS*
	(1)	(2)	(3)
***SENATOR**$_t$×**EC**$_t$*	0.0081***	0.0024***	0.0025**
	(2.67)	(3.08)	(2.26)
EC_t	-0.0136***	-0.0031***	-0.0044***
	(-6.24)	(-5.26)	(-4.96)
$SENATOR_t$	-0.0004	-0.0014*	-0.0005
	(-0.54)	(-1.87)	(-0.83)
$SIZE_t$	-0.0123***	-0.0122***	-0.0122***
	(-10.51)	(-10.32)	(-10.38)
LEV_t	-0.0001	0.0005	-0.0000
	(-0.02)	(0.08)	(-0.01)
$TIER_t$	0.0010***	0.0010***	0.0010***
	(6.65)	(6.93)	(6.88)
$\triangle UNEMP_t$	-0.0028***	-0.0028***	-0.0028***
	(-4.40)	(-4.37)	(-4.36)
$\triangle DEPOSITS_t$	0.0224***	0.0222***	0.0223***
	(4.13)	(4.08)	(4.12)
ROE_t	0.0619***	0.0636***	0.0652***
	(5.85)	(5.97)	(6.12)
$\triangle TIER_t$	-0.0005**	-0.0005*	-0.0005*
	(-2.07)	(-1.95)	(-1.94)
$CSRET_t$	0.0002	0.0003*	0.0003*
	(1.42)	(1.79)	(1.65)
Constant	0.0894***	0.0895***	0.0886***
	(11.39)	(11.33)	(11.22)
Time Fixed Effects	Yes	Yes	Yes
Bank Fixed Effects	Yes	Yes	Yes
Observations	41714	41714	41714
Adjusted R^2	0.192	0.192	0.192

Notes: This table examines the role of BC senators in encouraging bank lending and increasing liquidity under bad economic conditions. The dependent variable is future loan growth (LG_{t+1}). The variable of interest is the interaction between economic conditions (*EC*) and BC senators (*SENATOR*). Specifically, economic conditions are proxied by inadequate capital during recession (*IDQC*), a poor state economy (*POOR*), or a weak state banking sector (*WBS*) in columns (1) to (3), respectively. The sample period is from 1995Q1 to 2017Q4. Variable definitions are presented in Appendix C. We control for year and quarter fixed effects and bank fixed effects in all specifications. The *t*-statistics in parentheses are based on standard errors clustered at the bank level. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels for two-tailed tests, respectively.

Table OA8. BC Senator Ideology

	DLLP		*DLLP_MS*	
	(1)	(2)	(3)	(4)
CONSERVATIVE$_t$	***-0.0124***	***-0.0283***	***-0.0656***	***-0.1356***
	(-0.38)	***(-0.90)***	***(-0.48)***	***(-1.01)***
LIBERAL$_t$	***0.1108******	***0.1283******	***0.5044******	***0.5344******
	(3.96)	***(4.77)***	***(4.57)***	***(5.09)***
SIZE$_t$		0.0350		0.0054
		(1.12)		(0.04)
LLP$_{t-1}$		0.4530***		3.2105***
		(9.64)		(19.78)
CAP$_t$		-0.0017		-0.0187
		(-0.32)		(-0.88)
LOSS$_t$		0.8690***		1.0574***
		(26.39)		(13.05)
TIER$_t$		0.0090*		0.0476**
		(1.96)		(2.49)
EBP$_t$		0.2068***		0.0977
		(6.05)		(0.83)
CSRET$_t$		-0.0174**		-0.0180
		(-2.23)		(-1.62)
△GDP$_t$		-0.0470***		-0.1222***
		(-10.12)		(-7.51)
△UNEMP$_t$		0.0726***		0.0110
		(2.89)		(0.17)
Constant	-2.9546***	-3.3251***	-11.9740***	-12.3960***
	(-60.20)	(-15.61)	(-56.13)	(-13.36)
Time Fixed Effects	Yes	Yes	Yes	Yes
Bank Fixed Effects	Yes	Yes	Yes	Yes
Observations	43034	43034	38509	38509
Adjusted R^2	0.219	0.259	0.434	0.477

Notes: This table presents the results of the effects of BC senators' ideology on bank opacity. To measure ideology, we follow Bischof, Daske, and Sextroh (2020) and use the first dimension of DW-NOMINATE (ideology) provided by Lewis et al. (2019). The ideology score for each senator ranges from -1 to +1 and increases with the level of conservative ideology. The variable *CONSERVATIVE* is an indicator variable for a conservative BC senator, equal to one if the BC senator's ideology score is above the sample median, and zero otherwise; *LIBERAL* is an indicator variable for a liberal BC senator, equal to one if the BC senator's ideology score is below the sample median, and zero otherwise. The dependent variable is bank opacity, measured as discretionary loan loss provisions (*DLLP*), or the four-quarter moving sum of discretionary loan loss provisions (*DLLP_MS*). The sample period is from 1995Q1 to 2017Q4. Variable definitions are presented in Appendix C. We control for year–quarter fixed effects and bank fixed effects in all specifications. The *t*-statistics in parentheses are based on standard errors clustered at the bank level. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels for two-tailed tests, respectively.

Table OA9. Public vs. Private Banks

Panel A: All Banks

	DLLP		*DLLP_MS*	
	(1)	(2)	(3)	(4)
SENATOR$_t$	***0.0219****	***0.0281****	***0.0939****	***0.1052****
	(4.07)	***(5.72)***	***(4.45)***	***(5.52)***
SIZE$_t$		0.0479***		-0.0017
		(7.25)		(-0.06)
LLP$_{t-1}$		0.3450***		2.0899***
		(64.95)		(107.94)
CAP$_t$		-0.0037***		-0.0107**
		(-2.95)		(-2.19)
LOSS$_t$		0.6493***		0.9660***
		(60.04)		(34.77)
TIER$_t$		0.0071***		0.0314***
		(11.13)		(12.44)
EBP$_t$		0.0149***		-0.0178**
		(4.76)		(-2.21)
CSRET$_t$		-0.0280***		0.0316***
		(-15.97)		(10.82)
△GDP$_t$		-0.0568***		-0.1646***
		(-45.58)		(-41.35)
△UNEMP$_t$		0.0231***		0.1137***
		(3.61)		(7.58)
Constant	-1.8530***	-2.4680***	-7.9986***	-8.5940***
	(-237.01)	(-32.27)	(-268.97)	(-27.84)
Time Fixed Effects	Yes	Yes	Yes	Yes
Bank Fixed Effects	Yes	Yes	Yes	Yes
Observations	777611	777611	734694	734694
Adjusted R^2	0.216	0.262	0.400	0.479

Panel B: Public vs. Private Banks

	DLLP		*DLLP_MS*	
	(1)	(2)	(3)	(4)
PUBLIC×SENATOR$_t$	***0.0409****	***0.0300****	***0.1913*****	***0.1467****
	(2.47)	***(2.02)***	***(2.97)***	***(2.56)***
SENATOR$_t$	0.0173***	0.0247***	0.0722***	0.0883***
	(3.06)	(4.76)	(3.27)	(4.40)
PUBLIC$_t$	0.0551***	0.0366**	0.2122***	0.1558**
	(3.18)	(2.30)	(3.03)	(2.43)
SIZE$_t$		0.0445***		-0.0164
		(6.66)		(-0.61)
LLP$_{t-1}$		0.3449***		2.0892***
		(64.91)		(107.87)
CAP$_t$		-0.0042***		-0.0130***
		(-3.32)		(-2.62)
LOSS$_t$		0.6489***		0.9641***
		(60.01)		(34.69)
TIER$_t$		0.0072***		0.0321***
		(11.33)		(12.64)
EBP$_t$		0.0149***		-0.0176**
		(4.77)		(-2.19)
CSRET$_t$		-0.0280***		0.0316***
		(-15.96)		(10.82)
△GDP$_t$		-0.0567***		-0.1644***
		(-45.52)		(-41.29)
△UNEMP$_t$		0.0231***		0.1138***
		(3.61)		(7.58)
Constant	-1.8555***	-2.4294***	-8.0061***	-8.4262***
	(-234.89)	(-31.48)	(-266.49)	(-27.04)
Time Fixed Effects	Yes	Yes	Yes	Yes
Bank Fixed Effects	Yes	Yes	Yes	Yes
Observations	777611	777611	734694	734694
Adjusted R^2	0.216	0.262	0.400	0.480

Notes: This table examines the effects of BC senator on bank opacity using all public and non-public banks. The bank information is from the Call Reports provided by FDIC (https://www7.fdic.gov/sdi/download_large_list_outside.asp). The dependent variable is bank opacity, measured as discretionary loan loss provisions (*DLLP*), or the four quarter moving sum of discretionary loan loss provisions (*DLLP_MS*). *SENATOR* is an indicator variable equal to one if the bank is headquartered in a state with senator representative on the Banking Committee. The sample period is from 1995Q1 to 2017Q4. In Panel A, we use the same model as in Table 2. In Panel B, we include an indicator variable (*PUBLIC*), which equals to 1 if the bank is publicly listed, and the interaction of *PUBLIC* and *SENATOR*. Details of variable definitions are presented in Appendix C. We control for year and quarter fixed effects and bank fixed effects in all specifications. The t-statistics in parentheses are based on standard errors clustered at the bank level. *, **, *** indicate statistical significance at the 10 percent, 5 percent, and 1 percent levels for two-tailed tests, respectively.