

Stakeholder Orientation and Financial Misconduct

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This Draft: July 2023

Abstract: We use the staggered adoption of constituency statutes by the U.S. states as an exogenous shock to stakeholder orientation and empirically investigate the impact of stakeholder orientation on financial misconduct. We show a strong mitigating effect of stakeholder orientation on financial misconduct. We find that firms incorporated in states that passed stakeholder constituency statutes have lower likelihood of opportunistic insider trading. Additionally, opportunistic purchases in firms incorporated in states with constituency statutes are less profitable. We also show that stakeholder orientation has a mitigating effect on other measures of financial misconduct like securities class action lawsuits and financial misstatements.

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1. Introduction

How does firm stakeholder orientation influence managers' financial misbehavior? Since 1930s, the debate between primacy of stakeholders vs shareholders has been of fundamental importance to the corporation's purpose in society (Berle (1931), Bainbridge (1991), Allen, Jacobs, and Strine (2002)). There is also a growing body of evidence that stakeholder orientation which introduces a broader set of constituencies in the corporate board's decision-making plays a vital role in shaping corporate outcomes (Flammer and Kacperczyk (2016), Chowdhury, Doukas, and Park (2021)). However, to the best of our knowledge, there have been no studies investigating the relationship between stakeholder orientation and financial misconduct. In this paper, we fill a gap in the literature by examining the impact of variation in the state-level stakeholder constituency statutes on financial misconduct.

We use staggered adoption of the constituency statutes in different U.S. states as an exogenous shock to stakeholder orientation and investigate the associated changes in managers' financial misconduct. Financial misconduct like financial misrepresentation (Karpoff, Lee, and Martin (2008)) or insider trading (Alexander and Cumming (2020)) can be extremely costly and any mechanisms that could reduce its incidence merit further examination. To broaden our coverage, we employ several measures of financial misconduct, namely opportunistic insider trading (Ali and Hirshleifer (2017)), along with firm financial misstatements (Dechow et al. (2011)) and securities class action lawsuits. We find a significant decrease in managerial financial misbehavior using different measures of financial misconduct in firms incorporated in the states that adopted stakeholder-oriented constituency statutes.

Theoretically, the association between stakeholder orientation and financial misconduct is somewhat ambiguous. There is some evidence that stakeholder orientation increases board

oversight over managerial behavior (Flammer and Kacperczyk (2016)) which could make it harder to engage in opportunistic misconduct. A stronger stakeholder presence on the board after the adoption of constituency statutes by the state can help stakeholders to better perform a monitoring role over the managers (Chowdhury, Doukas, and Park (2021)). This heightened monitoring effect can mitigate managers' opportunistic behavior, specifically financial misbehavior. Moreover, firms have higher CSR ratings after the adoption of constituency statutes (Mayberry and Watson (2021)), and insiders from more corporate social responsibility (CSR) conscious firms are less likely to engage in informed trading and have lower insider profits due to the reputational effects (Gao, Lisic, and Zhang (2014)). Therefore, one can expect stakeholder orientation to induce the firm to commit more resources to social good and increase its corporate social responsibility (CSR) engagement which in turn is associated with a lower incidence of insider trading.

On the other hand, stakeholder orientation induces long-termism in the board and managerial decision-making (Chowdhury, Doukas, and Park (2023), Flammer and Kacperczyk (2016)), which makes monitoring the short-term managerial activity less effective. Furthermore, stakeholder orientation may induce misaligned incentives among diverse stakeholders leading to a decreased efficiency of the board monitoring function and hence less oversight of short-term managerial behavior (Fich and Shivdasani (2006), Liu et al. (2020)). Moreover, stakeholder orientation may provide self-interested managers with incentives to collude with stakeholders to act opportunistically and extract private benefits (Bertrand and Mullainathan (2003), Pagano and Volpin (2005), Friedman (2007), Cronqvist et al. (2009), Masulis and Reza (2015)).

We use several proxies of financial misconduct, although our main focus is on the insider trading given that there are only a few managerial behaviors that are as directly observable as

insider trading⁴. Our main proxy for financial misconduct is opportunistic insider trading from Ali and Hirshleifer (2017), who link it with various kinds of firm and managerial misconduct such as financial restatements, U.S. Securities and Exchange Commission (SEC) enforcement actions, shareholder litigation, and executive compensation. Our empirical findings show that the adoption of stakeholder-oriented constituency statutes helps to mitigate opportunistic insider trading. We show a statistically significant and economically strong effect of constituency statutes on financial misbehavior. Our main variable of interest in our tests is *Constituency Statutes* which takes the value of one if the incorporation state of a firm adopted constituency statutes and the value of zero otherwise. For example, a one-standard-deviation increase in *Constituency Statutes* leads to a 9.7% (9%) decrease in the probability of all opportunistic trades (opportunistic sales) when we examine opportunistic trades of managers before earnings announcements. We obtain similar results when we focus on opportunistic trades before the filing of 8K forms and before the filing of 8k forms with litigious sentiment classification.

We also have a series of robustness checks and additional tests highlighting the mitigating effect of shareholder orientation, following the adoption of constituency statutes, on financial misbehavior. Prior literature indicates a higher level of unethical behavior and financial misconduct when there is a more pervasive corruption culture or local corruption or when there is lower or no analyst coverage. This suggests a stronger effect of constituency statutes in reducing opportunistic insider trading in areas with more corruption or firms with no analyst coverage. For example, a one-standard-deviation increase in *Constituency Statutes* is associated with a 15 % decrease in the probability of all opportunistic trades in states with more corruption, whereas there

⁴ As of August 29, 2002, the U.S. Securities and Exchange Commission (SEC) requires managers of public companies to report their transactions in company securities within two calendar days using SEC Form 4 filings (<http://www.sec.gov/rules/final/34-46421.htm>).

is a statistically insignificant effect of *Constituency Statutes* on all opportunistic trades made by insiders in firms headquartered in states with less corruption. Similarly, a one-standard-deviation increase in *Constituency Statutes* leads to a 14.7 % decrease in the probability of all opportunistic trades in firms with no analyst coverage, while a one-standard-deviation increase in *Constituency Statutes* is associated with only a 6.3 % decrease in the probability of all opportunistic trades in firms with analyst coverage. These findings provide additional evidence supporting the mitigating effect of stakeholder-oriented policies on financial misconduct.

When we focus on the insider trading profitability tests, we find evidence that incorporation in a state that adopted constituency statutes reduces the 3-day cumulative abnormal return (CAR) of purchases. This finding provides evidence of the mitigating effect of *Constituency Statutes* on the short-term profitability of insider trading, consistent with our other findings of fewer opportunistic trades in constituency statutes states.

We also find a pronounced impact of *Constituency Statutes* on other forms of financial misconduct. For example, the adoption of constituency statutes is associated with a reduction of the likelihood of securities fraud. A one-standard-deviation increase in *Constituency Statutes* leads to a 12.8% decrease in the probability of securities class action lawsuits. Similarly, we examine the effect of constituency statutes on financial misstatements by using the Dechow et al. (2011) data on the Accounting and Auditing Enforcement Releases (AAERs) with alleged financial misstatements and show that a one-standard-deviation increase in *Constituency Statutes* is associated with a 14.6% decrease in the probability of financial misstatement. These findings present additional evidence highlighting the effect of constituency statutes in reducing financial misconduct.

Stakeholder versus shareholder debate over the purpose and goals of the firm in the wider social context dates back to the 1930s (Berle (1931), Dodd (1932)). The shareholder view of the firm's legal obligations highlighted the primacy of the fiduciary duty to the shareholders and was also the courts' primary stance in the matter (Orts (1992)). On the other hand, the stakeholder view of the firm sought to change the corporate law to acknowledge the wide variety of non-shareholder constituencies with valid interests in the firm's activity (Bainbridge (1991), Springer (1999)).

This debate was reinvigorated during the 1980s with the introduction of the stakeholder management theories (Freeman (1984)) simultaneously with the staggered state-level implementation of the non-shareholder constituency statutes (Hale (2003)). The constituency statutes empower corporate board directors to consider the interests of non-shareholder constituencies and also provide the legal protection that has often since prevailed in courts (Geczy et al. (2015)). Moreover, constituency statutes have been adopted by over a half of the U.S. states in the span of 25 years, offering thus a unique opportunity to study the effects of a largely exogenous shock to the firm stakeholder orientation on corporate outcomes (Ni (2020)).

For instance, Chowdhury, Doukas, and Park (2021) study the effect of stakeholder orientation on the value of cash holdings and find a significant increase in the marginal value of cash following the passage of constituency statutes. In a follow-up paper, Chowdhury, Doukas, and Park (2023) find that greater stakeholder orientation increases labor investment efficiency, especially for firms with more pronounced potential managerial agency problems. Flammer and Kacperczyk (2016) examine the impact of stakeholder orientation on innovation using the enactment of state-level constituency statutes and find a significant increase in the number of patents and patent citations. Leung, Song, and Chen (2019) find that banks whose directors' legal duties are extended to consider stakeholder and long-term interests due to the enactment of

constituency statutes significantly reduce their risk-taking by increasing capital and shifting to safer borrowers. Li and Zhang (2020) use the staggered adoption of constituency statutes in the U.S. as an exogenous variation in stakeholder orientation and link it with lower stock price crash risk for the firms in the affected states. Ni (2020) find that greater stakeholder orientation due to the passage of non-shareholder constituency statutes significantly reduces discretionary accruals and curtails earnings management to some extent. Ni, Song, and Yao (2020) note that firms incorporated in states that have adopted constituency statutes reduce share repurchases. Gao, Li, and Ma (2021) discover a substantial decrease in loan spreads for firms incorporated in states that adopted non-shareholder constituency statutes relative to firms incorporated elsewhere. Li and Lu (2022) use the passage of the state-level constituency statutes as an exogenous shock to investigate the relationship between stakeholder orientation and operating cost stickiness.

Our paper contributes to the burgeoning literature on stakeholder orientation and corporate outcomes in several ways. First, our results demonstrate the mitigating effect of the stakeholder orientation on opportunistic insider trading, which might be of interest to corporate governance and legal professionals. Second, in our paper we document an attenuating effect of stakeholder orientation on factors like high local corruption and low analyst coverage that have been associated with higher levels of financial misconduct. Third, we show that stakeholder orientation mitigates other measures of financial misconduct as well, broadening the application of our results. We expect our findings to be a relevant argument in the development of a legal framework aimed at better corporate governance and a more responsible role of the firm in society.

The remainder of this paper is organized as follows. The next section provides a description of the data and the sample selection method we use, along with the summary statistics. Section 3

presents the empirical tests of the constituency statutes and insider trading. Section 4 provides a conclusion.

2. Data and Sample

Our sample runs from 1986 through 2021. We require available stock price data in CRSP and accounting data in COMPUSTAT databases. We obtain incorporation state data from Compustat. We define constituency states following Gao, Li, and Ma (2021). We obtain the historical headquarters data from Bai, Fairhurst, and Serfling (2020) for the pre-1993 period, who hand-collected it from the Moody's Manuals (later Mergent Manuals) and Dun & Bradstreet's Million Dollar Directory (later bought by Mergent). For the 1993-2021 period, we use the Python and SAS code⁵ from Gao, Leung, and Qiu (2021) to extract the business address from 10-X Header data file from the Notre Dame Software Repository for Accounting and Finance (SRAF)⁶ prepared by Loughran and McDonald (2016). 10-X Header file includes all of the information in the header section of 10-K/Qs (and all variants) filed on the Securities and Exchange Commission's (SEC) EDGAR database. If the business address is missing or invalid from parsing the headers, we use the Compustat data.

The insider trading data on open market sales and open market purchases is from the Thomson Reuters Insider Filings database. For our analysis, we focus on trades by managers and directors. We define managers as all insiders who are officers, officer-directors, or officer-shareholders⁷. We exclude trades made by blockholders who are not managers or directors. To identify opportunistic

⁵ <https://mingze-gao.com/posts/firm-historical-headquarter-state-from-10k/>

⁶ <https://sraf.nd.edu/data/augmented-10-x-header-data/>

⁷ We use the following position codes to identify officers (managers): AV, C, CB, CEO, CFO, CI, CO, COO, CT, EVP, GC, GM, GP, H, O, OB, OD, OE, OT, OX, P, SVP, TR, VC, and VP. We use the position code D to identify directors.

insider trades, we use the method proposed by Ali and Hirshleifer (2017), classifying a trade as opportunistic if it is conducted by an insider who falls within the top quintile of the profitability ranking of their past trades before quarterly earnings announcements (QEAs). For each QEA, we obtain an insider's open market buys and sales during the trading days -21 through -3 relative to the QEA day (day 0). We then calculate the profitability of each of these pre-QEA trades by determining the average market-adjusted return for the QEA period, spanning days -2 through +2 relative to the QEA day:

$$\text{Profit} = \sum_{j=-2}^{j=2} (r_{(i,t+j)} - r_{m,t+j}) / 5 \quad (1)$$

where t is the QEA date, $r_{i,t}$ is stock i 's return on day t , and $r_{m,t}$ is the return on the CRSP equal-weighted index on day t .

Then for each insider and for each year, we define the average profitability of the insider's past pre-QEA trades as:

$$\text{Average Profit} = (\sum^B \text{Profit}_{\text{Buy}} - \sum^S \text{Profit}_{\text{sell}}) / (B + S) \quad (2)$$

where B (S) is the total number of pre-QEA buy (sell) trades made by the insider prior to the start of the year. If an insider makes multiple trades in a particular pre-QEA period, we aggregate the trades and classify them as a buy (sell) trade if the number of shares bought is greater (less) than the number of shares sold by the insider during the pre-QEA period. At the beginning of each year, we rank insiders into quintiles based on their calculated Average Profit. Insiders falling within the top quintile are labeled as opportunistic, and their trades conducted in the ranking year are classified as opportunistic trades. Conversely, all other trades are considered non-opportunistic.

In further tests, we use alternative definitions of opportunistic trades using Form 8-K filing dates instead of QEA dates⁸. Form 8-K must be filed by firms with the SEC whenever there is material news that shareholders should know about. For each 8-K filing, we obtain an insider's open market buys and sales during trading days -21 through -3 relative to the 8-K filing date (day 0). We calculate the profitability of these trades during the five-day window around 8-K filing date and compute the average profitability of each insider's past pre-8-K trades using equations (1) and (2). Insiders in the top quintile of average profitability of pre-8-K trades are labeled as opportunistic, and their trades in the ranking year are classified as opportunistic trades. All other trades are considered non-opportunistic.

Finally, we focus only on 8-K filings with litigious language, arguing that these filings are likely to contain news about ongoing or impending litigation, providing greater opportunities for insiders to engage in opportunistic trading before the release of such information. We use the sentiment analysis table in the SEC Analytics database to obtain the proportion of litigious words in 8-K filings (Loughran-McDonald litigious word proportion) and classify an 8-K filing as litigious if it has a higher than median proportion of litigious words for all the 8-K filings made by all firms in that year. We then calculate the profitability of insider trades conducted before the filing date of such litigious 8-Ks (pre-litigious 8-K trades), using equations (1) and (2). Insiders in the top quintile of average profitability of pre-litigious 8-K trades are classified as opportunistic, and their trades in the ranking year are classified as opportunistic trades. All other trades are considered non-opportunistic.

Table 1 presents the descriptive statistics of our sample. Panel A and B report descriptive statistics for independent and dependent variables used in the main insider purchase and sales

⁸ Opportunistic trades defined based on 8-K filing dates cover the period 1996-2016, since the electronic filing of 8-K forms was not common before 1996, and the SEC Analytics Sentiment data available to us ends in 2016.

regressions. 2.5% of purchase transactions are classified as opportunistic using the QEA date, 5.6% using the 8-K filing date, and 2.2% using the litigious 8-K filing date. Opportunistic trades are more common in sales transactions; the figures are 5.5%, 7.9%, and 4.5% using QEA, 8-K, and litigious 8-K dates, respectively. Purchases are preceded by a negative past six-month return of -2.4% but met with a positive three-day cumulative abnormal return (CAR) of 1.2%, suggesting that managers tend to buy when they believe their stock is undervalued. On the other hand, sales are preceded by a positive past six-month return of 21.9% but receive a negative CAR of -0.1%, consistent with managers selling after a price run-up for diversification and rebalancing reasons. Sales transactions tend to be bigger in size, and CEOs are quite active in trading, accounting for 14.4% of purchases and 12.6% of sales. Firms in sales transactions tend to be large growth firms with higher analyst covering and a higher fraction of institutional ownership, consistent with managers in larger and potentially overvalued firms selling more. Overall, the results in Table 1 show that a small but significant number of trades are opportunistic trades, and they are more common in sales transactions. Additionally, a significant proportion of all the insider trades are in firms that are incorporated in constituency statutes states: 41.8% of firms in purchase transactions and 25.8% in sales transactions. The rest of the results are mostly in line with the literature (see, for example, Contreras, Korczak, and Korczak (2023)) and our expectations.

[Insert Table 1 Here]

3. Empirical Tests

3.1. Main Tests

Panel A of Table 2 presents our main results, where we use a logit model to examine the impact of *Constituency Statutes* on opportunistic insider trading. We expect that the stakeholder

orientation induced by the adoption of *Constituency Statutes* in the incorporation state of a firm will reduce the likelihood of opportunistic insider trades. The dependent variable is the opportunistic trade dummy, set to one if the trade is made by an insider who is in the top quintile of the profitability ranking of past trades before earnings announcements. Column 1 reports results for combined purchases and sales, whereas Column 2 (Column 3) presents results for purchases (sales) only.

[Insert Table 2 Here]

The main variable of interest is *Constituency Statutes*, which takes the value of one if the incorporation state of a firm adopted *Constituency Statutes* and zero otherwise. The dependent variables include factors known to influence insider trading, such as market capitalization and book-to-market ratio (both in log form), past return and volatility (measured over the past six months), change in volatility, log of trade size, and a dummy variable indicating whether the insider is the Chief Executive Officer (CEO). We also control for year and industry fixed effects.

Constituency Statutes has a negative and statistically significant coefficient in both Column 1 and Column 3, suggesting that the adoption of *Constituency Statutes* makes all opportunistic trades, especially opportunistic sales, less likely. The effect is also economically significant. In Column 1, a one-standard-deviation increase in *Constituency Statutes* leads to a 9.7% decrease in the probability of an opportunistic trade. In Column 3, a one-standard-deviation increase in *Constituency Statutes* is associated with a 9% decrease in the probability of an opportunistic sale.

In sum, our baseline regression in Panel A of Table 2 suggests that the adoption of *Constituency Statutes* leads to a reduction in the likelihood of opportunistic insider trades. This finding indicates

that the adoption of *Constituency Statutes* might help eliminate financial misbehavior related to insider trading.

In Panel B of Table 2, we focus on opportunistic trades based on the filing of 8-K forms. The dependent variable is the opportunistic trade dummy, set to one if made by an insider in the top quintile of the profitability ranking of past trades before Form 8-K filing dates. Our findings are similar to those in our main tests in Panel A. *Constituency Statutes* has a negative and statistically significant coefficient in both Column 1 and Column 2, suggesting that the adoption of *Constituency Statutes* leads to a reduction in the likelihood of all opportunistic trades, especially opportunistic purchases. The effect is also economically robust. In Column 1, a one-standard-deviation increase in *Constituency Statutes* leads to a 9% decrease in the probability of all opportunistic trades. In Column 2, a one-standard-deviation increase in *Constituency Statutes* is associated with a 9.4% decrease in the probability of opportunistic purchases. The results in Panel B provide additional evidence of the role of *Constituency Statutes* in reducing opportunistic insider trades.

Now, in Panel C of Table 2, we analyze opportunistic trades based on the filing of litigious 8-K forms. The dependent variable is the opportunistic trade dummy, set to one if made by an insider in the top quintile of the profitability ranking of past trades before litigious Form 8-K filing dates. A litigious Form 8-K is one that has a higher than median proportion of litigious words compared to all 8-K filings made by all firms in that year. Litigious word proportion data for 8-K forms comes from the SEC Analytics Database. Litigious 8-Ks are likely to contain information about impending or ongoing litigations involving the firm, presenting a greater opportunity for insiders to engage in opportunistic trading before the release of such information.

Our findings are similar to our earlier results. *Constituency Statutes* has a negative and statistically significant coefficient in both Column 1 and Column 3, indicating that the adoption of *Constituency Statutes* is associated with a reduction in the likelihood of all opportunistic trades, especially opportunistic sales. The effect of *Constituency Statutes* is economically significant too. In Column 1, a one-standard-deviation increase in *Constituency Statutes* leads to a 10.7% decrease in the probability of all opportunistic trades. In Column 3, a one-standard-deviation increase in *Constituency Statutes* is associated with a 9.9% decrease in the probability of opportunistic sales. Overall, our findings in Panel C provide additional support for the mitigating effect of *Constituency Statutes* on financial misbehavior.

3.2. Local Corruption Tests

Recent studies have highlighted the link between corporate and financial outcomes and corruption culture. Parsons, Sulaeman, and Titman (2018) analyze the impact of local unethical behavior on financial misconduct. Liu (2016) underlines the association between the corruption culture in the ancestral country of corporate managers and financial misconduct. Ucar and Staer (2020) show the impact of local corruption on corporate social responsibility (CSR). Prior literature suggests a positive association between unethical behavior particularly financial misconduct, and the corruption culture and local corruption. Therefore, one can expect a stronger effect of *Constituency Statutes* in reducing opportunistic insider trading when there is more prominent local corruption if the effect shown in our prior results is driven by the stakeholder orientation induced by *Constituency Statutes*. In this section, we examine this conjecture by re-examining our main tests for companies located in areas with high and low local corruption values. Following the related literature (e.g., Butler, Fauver, and Mortal (2009), Ucar and Staer (2020))

we use local federal corruption convictions per capita as a proxy for local corruption culture⁹, match the corruption data with our sample, and re-focus on our tests from Table 2. We divide our sample into high and low local corruption subsamples. Our sample firms located in states with corruption conviction per capita values lower than the sample median are in the Low Corruption subsample, while those with higher values are in the High Corruption subsample. We re-examine the main tests for these subsamples separately in Table 3.

[Insert Table 3 Here]

Panel A of Table 3 shows that *Constituency Statutes* mitigate opportunistic trading primarily for firms headquartered in high-corruption states. Coefficients for *Constituency Statutes* are negative and significant for all opportunistic trades and opportunistic sales in the high local corruption subsample in Columns 2 and 6, respectively. This is consistent with our earlier conjecture. The effect is also economically significant. In Column 2, a one-standard-deviation increase in *Constituency Statutes* is associated with a 15% decrease in the probability of all opportunistic trades in states with more corruption as measured by corruption conviction rates per capita. Similarly, in Column 6, a one-standard-deviation increase in *Constituency Statutes* leads to almost a 15% decrease in the probability of opportunistic sales in states with high corruption. On the other hand, in low local corruption states, *Constituency Statutes* do not seem to reduce opportunistic trading or selling; the coefficients have the expected sign (negative) but are insignificant in Columns 1 and 5.

These results provide additional support for the effect of the adoption of *Constituency Statutes* in mitigating financial misbehavior as measured by opportunistic insider trading.

⁹ We thank Alex Butler for making the updated state level corruption conviction data available on his website. (<http://butler.rice.edu/corruption/>). We winsorize the conviction per capita values at one percent level.

When we examine the results of opportunistic trades based on the filing of 8-K forms and litigious 8-K forms in Panels B and C, respectively, we find similar outcomes. In Panel B, while there is no statistically significant effect of *Constituency Statutes* on all opportunistic trades for the firms in the low local corruption subsample in Column 1, a one-standard-deviation increase in *Constituency Statutes* leads to a 9.1% decrease in the probability of all opportunistic trades in states with high corruption rates in Column 2. In Column 3, a one-standard-deviation increase in *Constituency Statutes* is associated with a 9.6% decrease in the probability of opportunistic purchases in states with low corruption rates, whereas in Column 4, the same increase leads to an 11% decrease in the probability of opportunistic purchases in states with high corruption rates. In Column 6, a one-standard-deviation increase in *Constituency Statutes* leads to almost an 8% decrease in the probability of opportunistic purchases in states with high corruption rates, while there is no statistically significant effect of *Constituency Statutes* on opportunistic sales for the firms in the low local corruption subsample in Column 5.

When we examine opportunistic trades based on the filing of litigious 8-K forms, there are statistically significant and negative coefficient values for *Constituency Statutes* for the high local corruption subsample for all opportunistic trades and opportunistic sales in Columns 2 and 6, respectively. The effect is also economically strong. In Column 2, a one-standard-deviation increase in *Constituency Statutes* is associated with a 19.4% decrease in the probability of all opportunistic trades in states with high corruption rates, whereas there is no statistically significant effect of *Constituency Statutes* on all opportunistic trades for the firms in the low local corruption subsample in Column 1. In Column 6, a one-standard-deviation increase in *Constituency Statutes* leads to almost a 22% decrease in the probability of opportunistic sales in states with high corruption rates, but there is no statistically significant effect of *Constituency Statutes* on

opportunistic sales in states with low corruption rates in Column 5.

These results provide additional support for the effect of the adoption of *Constituency Statutes* in reducing financial misbehavior, as measured by opportunistic insider trading. In sum, the statistically significant and economically strong results in Table 3 are consistent with our earlier conjecture suggesting a stronger effect of *Constituency Statutes* on insider trading for the firms located in areas with a high local corruption culture. These results further support the notion that our earlier findings are driven by constituency statutes and the stakeholder orientation culture induced by the adoption of constituency statutes, which helps reduce financial misbehavior.

3.3. Institutional Ownership Tests

Prior literature indicates that institutional ownership can have a monitoring effect on firms. Hillegeist and Weng (2021) state that “recent studies using the Russell index setting conclude quasi-indexers are active monitors who have a positive effect on certain governance and corporate practices (e.g., Appel, Gormley, and Keim (2016), Boone and White (2015), Crane, Michenaud, and Weston (2016))”. Crane, Michenaud, and Weston (2016) emphasize the monitoring role of institutions on firm behavior. Appel, Gormley, and Keim (2016) point out that passive mutual funds influence firms' corporate governance, leading to more independent directors, removal of takeover defenses, and more equal voting rights. Boone and White (2015) suggest that higher institutional ownership leads to greater management disclosure, analyst following, liquidity, and lower information asymmetry. Hillegeist and Weng (2021) examine insider trading and show that higher quasi-indexer institutional ownership is associated with less insider trading (both buys and sells) and less profitable trades for sells.

Recent studies suggest a stronger monitoring effect of institutional ownership on insider

trading, and one can argue that constituency statutes might have a more pronounced effect in mitigating opportunistic insider trading when there is higher institutional ownership, assuming that the effect shown in our prior results from the main tests comes from constituency statutes. To investigate this conjecture, we re-focus on our main tests for firms with high and low institutional ownership separately in Table 4. We divide our sample into low (high) institutional ownership subsamples. A firm is designated as a low (high) institutional ownership firm if institutional investors hold less (more) than 50% of the shares outstanding. Institutional ownership data comes from Thomson Reuters' S34 database. We then repeat the main tests for low and high institutional ownership subsamples separately in Table 4.

[Insert Table 4 Here]

Results in Panel A of Table 4 generally point to a higher mitigating effect of constituency statutes on opportunistic trading for the low institutional ownership subsample. In Column 1, a one-standard-deviation increase in *Constituency Statutes* is associated with almost a 12% decrease in the probability of all opportunistic trades in firms with low institutional investor ownership, whereas in Column 2, the same change leads to only a 6.1% decrease in the probability of all opportunistic trades in firms with high institutional investor ownership. Similarly, a one-standard-deviation increase in *Constituency Statutes* is associated with almost an 11% decrease in the probability of opportunistic sales in firms with lower institutional investor ownership in Column 5 and only a 6.8% decrease in the probability of opportunistic sales in firms with high institutional investor ownership in Column 6. These findings in Panel A provide additional evidence supporting the role of *Constituency Statutes* in mitigating financial misbehavior proxied by opportunistic

insider trading.

Moving to the regression results of opportunistic trades based on the filing of 8-K forms and litigious 8-K forms in Panels B and C, respectively, we observe similar patterns, with the mitigating effect of *Constituency Statutes* mainly coming from low institutional ownership firms. In Column 1 of Panel B, a one-standard-deviation increase in *Constituency Statutes* leads to a 14.6% decrease in the probability of all opportunistic trades in firms with lower institutional investor ownership, whereas there is a statistically insignificant effect of *Constituency Statutes* on all opportunistic trades in firms with higher institutional investor ownership in Column 2. Likewise, while a one-standard-deviation increase in *Constituency Statutes* is associated with almost an 11.6% decrease in the probability of opportunistic purchases in firms with lower institutional investor ownership in Column 3, there is a statistically insignificant effect of *Constituency Statutes* on opportunistic purchases in firms with higher institutional investor ownership in Column 4. In Column 5, a one-standard-deviation increase in *Constituency Statutes* leads to almost a 16% decrease in the probability of opportunistic sales in firms with low institutional investor ownership, whereas there is a statistically insignificant effect of *Constituency Statutes* on opportunistic sales in firms with higher institutional investor ownership in Column 6.

When we examine opportunistic trades based on the filing of litigious 8-K forms in Panel C, a one-standard-deviation increase in *Constituency Statutes* leads to a 20.3% decrease in the probability of all opportunistic trades in firms with lower institutional investor ownership in Column 1, whereas there is a statistically insignificant effect of *Constituency Statutes* on all opportunistic trades in firms with higher institutional investor ownership in Column 2. Similarly, a one-standard-deviation increase in *Constituency Statutes* leads to almost a 21% decrease in the probability of opportunistic sales in firms with low institutional investor ownership in Column 5,

while there is a statistically insignificant effect of *Constituency Statutes* on opportunistic sales in firms with higher institutional investor ownership in Column 6.

Our empirical findings in Table 4 are consistent with our earlier conjecture and provide additional evidence on the impact of *Constituency Statutes* in mitigating financial misbehavior measured by opportunistic insider trading. This table further supports the notion that our main findings reported in Table 2 are driven by *Constituency Statutes*, and the stakeholder-oriented culture associated with the adoption of *Constituency Statutes* has a mitigating effect on financial misbehavior.

3.4. Analyst Coverage Tests

Previous literature suggests that analyst coverage has a monitoring effect on firms and can help to reduce financial misconduct. Yu (2008) shows a negative relationship between analyst coverage and earnings management. Chen, Harford, and Lin (2015) suggest that “financial analysts play an important governance role in scrutinizing management behavior.”, while Yang, Wang, and Xue (2021) find that analyst coverage reduces the likelihood of corporate misconduct. Prior literature suggests a higher level of financial misbehavior when there is less or no analyst coverage and a lower level of financial misconduct when there is some monitoring by financial analysts. One can argue that there should be a stronger effect of *Constituency Statutes* in reducing financial misbehavior in opportunistic insider trades in firms with no analyst coverage if the empirical findings in our main tests are driven by the adoption of *Constituency Statutes*. To investigate this conjecture, we divide our sample into two subsamples: firms with no analyst coverage and firms with analyst coverage and re-run our main tests.

In Panel A of Table 5, we find statistically significant and negative coefficient values for *Constituency Statutes* in all Columns except Column 4. The effect is much stronger for firms with no analyst coverage, consistent with our conjecture. In Column 1, a one-standard-deviation increase in *Constituency Statutes* leads to a 14.7% decrease in the probability of all opportunistic trades in firms with no analyst coverage, whereas in Column 2, a one-standard-deviation increase in *Constituency Statutes* is associated with only a 6.3% decrease in the probability of all opportunistic trades in firms with analyst coverage.

[Insert Table 5 Here]

In Column 3, a one-standard-deviation increase in *Constituency Statutes* is associated with a 20.5% decrease in the probability of opportunistic purchases in firms with no analyst coverage, while there is no statistically significant effect on opportunistic purchases for firms with analyst coverage. Additionally, in Column 5, a one-standard-deviation increase in *Constituency Statutes* leads to a 10.3% decrease in the probability of opportunistic sales in firms with no analyst coverage, whereas in Column 6, a one-standard-deviation increase in *Constituency Statutes* is associated with a 7.4% decrease in the probability of opportunistic sales in firms with analyst coverage.

When we focus on the results of opportunistic trades based on the filing of 8-K forms and litigious 8-K forms in Panels B and C, respectively, we have similar results. In Panel B, while there is a statistically insignificant effect of *Constituency Statutes* on all opportunistic trades for the firms with analyst coverage in Column 2, a one-standard-deviation increase in *Constituency Statutes* leads to a 13.2% decrease in the probability of all opportunistic trades for the firms with no analyst coverage in Column 1. Similarly, in Column 5, a one-standard-deviation increase in *Constituency*

Statutes leads to almost a 16% decrease in the probability of opportunistic sales in firms with no analyst coverage, whereas there is no statistically significant effect of *Constituency Statutes* on opportunistic sales for the firms with analyst coverage in Column 6.

We have similar findings in Panel C. While a one-standard-deviation increase in *Constituency Statutes* leads to a 21.7% decrease in the probability of all opportunistic trades in firms with no analyst coverage in Column 1, a one-standard-deviation increase in *Constituency Statutes* is associated with only a 7.7% decrease in the probability of all opportunistic trades in firms with analyst coverage in Column 2. In Column 5, a one-standard-deviation increase in *Constituency Statutes* leads to a 24.6% decrease in the probability of opportunistic sales in firms with no analyst coverage, whereas in Column 6, a one-standard-deviation increase in *Constituency Statutes* is associated with a 7.6% decrease in the probability of opportunistic sales in firms with analyst coverage.

The findings in Panels B and C, along with Panel A, provide more support for the effect of the adoption of constituency statutes in reducing financial misconduct measured by opportunistic insider trading. Table 5 presents robust findings in line with our earlier conjecture, suggesting a stronger effect of constituency statutes on insider trading for firms with no analyst coverage. This table indicates that our earlier results highlighted in our main tests are driven by constituency statutes, and stakeholder-oriented policies through the adoption of constituency statutes play an important role in reducing financial misbehavior.

3.5. Return Tests

In Table 6, we examine whether being incorporated in a constituency statutes state affects the profitability of insider trading by looking at all insider trades. Insider trading involves informed trading, so we expect insiders to use their private information about the value of the firm when trading to a certain extent. This suggests a positive price reaction to purchases (gains made) and a negative reaction to sales (losses avoided). We expect these profits to be reduced in firms incorporated in constituency states since insiders will find it less attractive to trade opportunistically. We use the three-day cumulative abnormal return net of the value-weighted market return to measure the profitability of each trade around the trading date.

Column 1 of Table 6 shows that being incorporated in a constituency statutes state reduces the 3-day CAR of purchases by 0.18%, and the effect is significant at the 1% level. For sales, the coefficient for *Constituency Statutes* has the expected sign (positive) but is insignificant. These results suggest that being incorporated in a constituency statutes state reduces the short-term profitability of insider trading by making insiders less willing to trade on private information, which is consistent with our earlier findings of fewer opportunistic trades in firms incorporated in constituency statutes states.

[Insert Table 6 Here]

3.6. Securities Class Action Filings Tests

Now, we focus on a different type of financial misconduct and examine securities class action lawsuits using the securities fraud litigation data from the Securities Class Action Clearinghouse database. This dataset includes securities class actions with filing dates, company tickers, and other relevant information. We match this dataset with the firms in our sample and identify the firms with securities class action filings for the years 1996-2021. For each firm-year, we construct a dummy variable, 'Class Action Filing,' which takes the value of one if there is a securities class action lawsuit filed in a year and zero otherwise. Next, we investigate the impact of constituency statutes on securities fraud litigation by running a logit regression with the dependent variable as 'Class Action Filing' and the variable of interest being '*Constituency Statutes*.'

As Column 1 of Table 7 indicates, there is a negative and statistically significant coefficient for *Constituency Statutes*. This suggests that the adoption of constituency statutes in the incorporation state of a firm reduces the likelihood of securities class action lawsuits. This result is also economically significant. A one-standard-deviation increase in *Constituency Statutes* leads to a 12.8% decrease in the probability of securities class action lawsuits. This suggests that the adoption of *Constituency Statutes* leads to a reduction in the likelihood of securities fraud. This table provides evidence supporting the role of stakeholder-oriented policies in reducing financial misbehavior.

[Insert Table 7 Here]

3.7. Financial Misstatements Tests

Next, we investigate the impact of adopting constituency statutes on financial misstatements. Recent studies have focused on the relationship between constituency statutes and earnings management. Gao, Li, and Ma (2021) show that constituency statutes limit earnings management, while Ni (2020) suggests that they decrease it. Building upon this research, we extend our analysis to explore the effect of constituency statutes on financial misstatements. We use the Dechow et al. (2011) data on the Accounting Enforcement Releases (AAERs) with alleged financial misstatements.¹⁰ Dechow et al. (2011) highlight the advantages of “using the SEC’s AAERs as a sample of misstatements” as follows: “the use of AAERs as a proxy for manipulation is a straightforward and consistent methodology”; and “AAERs are also likely to capture a group of economically significant manipulations as the SEC has limited resources and likely pursues the most important cases.” Dechow et al. (2011) also state that “...the SEC has issued Accounting and Auditing Enforcement Releases (AAERs) during or at the conclusion of an investigation against a company, an auditor, or an officer for alleged accounting and/or auditing misconduct. These releases provide varying degrees of detail on the nature of the misconduct, the individuals and entities involved, and the effect on the financial statements.”

We match the annual financial misstatement data with the firms in our sample for the years 1986-2019. For each firm-year, we construct a dummy variable, *AAER Misstatement*, which takes the value of one if there is a financial misstatement in a year, and zero otherwise. Next, we investigate the impact of constituency statutes on financial misstatements. We run a logit regression in which the dependent variable is *AAER Misstatement*, and the variable of interest is *Constituency Statutes*.

¹⁰ <https://sites.google.com/usc.edu/aaerdataset/home>

As shown in Column 1 of Table 8, the results reveal a negative and statistically significant coefficient for *Constituency Statutes*. The adoption of *Constituency Statutes* in a firm's incorporation state reduces the likelihood of financial misstatements. This result is also economically significant, as a one-standard-deviation increase in *Constituency Statutes* is associated with a 14.6% decrease in the probability of financial misstatement. These findings align with the recent literature, highlighting the effect of constituency statutes in reducing financial misbehavior.

[Insert Table 8 Here]

Overall, Table 8 provides additional evidence supporting the role of constituency statutes in mitigating financial misstatements, reinforcing the notion that the adoption of constituency statutes plays a vital role in reducing financial misbehavior.

4. Conclusion

In this paper, we explore the impact of stakeholder orientation on financial misconduct by employing staggered adoption of constituency statutes across different U.S. states as a measure of exogenous shock to stakeholder orientation. Constituency statutes allow directors to consider stakeholder interests in their decision-making without violating their fiduciary duties to the shareholders. We conjecture that increased stakeholder orientation via the adoption of state-level constituency statutes mitigates managerial financial misconduct.

Our findings provide evidence in favor of the mitigating role of stakeholder orientation induced by constituency statutes on financial misconduct. We find that firms incorporated in states that passed stakeholder constituency statutes show a lower likelihood of opportunistic insider

trading before earnings releases and the filings of 8K forms, including those with litigious sentiment. Our results also indicate that this reduction in opportunistic trading is more substantial in firms located in states with higher local corruption, indicating a significant role of constituency statutes in attenuating the effect of local corruption on managerial misbehavior. Furthermore, we observe a similar reduction in the probability of opportunistic insider trading associated with constituency statutes in firms with low institutional ownership and in firms with no analyst coverage, suggesting that constituency statutes mitigate insider trading in the absence of other disciplining mechanisms. These findings also provide support to the notion that the mitigating effect of constituency statutes on financial misconduct comes from stakeholder-oriented constituency statutes rather than other factors. Additionally, the opportunistic purchases conducted by insiders in firms incorporated in states with constituency statutes are significantly less profitable.

Analogous to our insider trading results, we find that constituency statutes exhibit a mitigating role using other measures of financial misconduct. We examine securities fraud litigation and find a lower likelihood of securities class action lawsuits in firms incorporated in states that adopted constituency statutes. We observe a similar association between the adoption of constituency statutes and the decreased probability of misconduct when we analyze financial misstatements.

Our empirical findings shed more light on the relationship between stakeholder orientation and financial misconduct. Our paper contributes to the vast literature on financial misconduct by providing a novel insight into the role of legal adoption of the stakeholder statutes as a mitigating mechanism for the managerial misconduct and, as such, will be of interest to policy makers and practitioners.

Appendix 1 Variable Definitions

Ln (B/M): log of the book to market ratio calculated using quarterly COMPUSTAT data items as follows: $bm = ceq / (cshoq * prccq)$. Data comes as of the fiscal quarter end immediately preceding the beginning of the current month (during which the trade takes place) minus three months. If $cshoq * prccq$ is missing, then market value of equity is calculated using CRSP data as price times number of shares outstanding. In Tables 7 and 8, data comes from the most recent fiscal quarter-end three-months before the beginning of the year.

Ln (Mcap): Log of market capitalization as of the trading date using the most recent month-end data for price and shares outstanding. In Tables 7 and 8, it is calculated at the end of the previous year.

Past Return: Stock return during the six-month period ending right before the beginning of the current month. In Tables 7 and 8, past return is the return for the last six-months of the preceding year.

Past Volatility: Annualized stock return volatility using daily returns during the six-month period preceding the current month. In Tables 7 and 8, stock volatility is the volatility for the last six-months of the preceding year.

Change in Volatility: Past Volatility minus the annualized stock return volatility using daily returns during six-month period preceding the month -6 relative to the current month (month 0). In Tables 7 and 8, change in volatility is the volatility for the last six-months of the preceding year, minus the volatility for the first six-months of the preceding year.

Ln (Trade Size): Log of the absolute dollar value of the trade (in 2022 dollars).

CEO: Dummy variable that is set to one if the insider is the Chief Executive officer (CEO).

Opportunistic trade based on Quarterly Earnings Announcement (QEA) date: Dummy variable showing if the trade belongs to an insider who is labeled as opportunistic for the year based on their trading in previous years before the QEA dates. An insider is labeled as opportunistic for a given year if they are in the top quintile of average profitability of all their insider trading during days -21 through -3 relative to the QEA dates in all of the previous years. For each of these pre-QEA trades, we calculate profitability as the average market-adjusted return for the QEA period (days -2 through +2 relative to the QEA day):

$$\text{Profit} = \sum_{j=-2}^{j=2} (r_{(i,t+j)} - r_{m,t+j}) / 5 \quad (1)$$

where t is the QEA date, $r_{i,t}$ is stock i 's return on day t , and $r_{m,t}$ is the return on the CRSP equal-weighted index on day t .

Then for each year and for each insider, we define the average profitability of the insider's past pre-QEA trades as:

$$\text{Average Profit} = (\sum^B \text{Profit}_{\text{buy}} - \sum^S \text{Profit}_{\text{sell}}) / (B + S) \quad (2)$$

where B (S) is the total number of pre-QEA buy (sell) trades made by the insider prior to the start of the year. If an insider makes multiple trades in a particular pre-QEA period, we aggregate the trades and classify them as a buy (sell) trade if the number of shares bought is greater (less) than the number of shares sold by the insider during the pre-QEA period.

Opportunistic trade based on 8K filing date: Dummy variable showing if the trade belongs to an insider who is labeled as opportunistic for the year based on the profitability of their trading in previous years before Form 8-K filing dates. Calculated similarly to opportunistic trade based on QEA date, the only difference is 8K filing date is used to identify the trades, instead of the QEA date.

Opportunistic trade based on Litigious 8K filing date: Dummy variable showing if the trade belongs to an insider who is labeled as opportunistic for the year based on the profitability of their trading in previous years before Litigious Form 8-K filing dates. Calculated similarly to opportunistic trade based on QEA date, the only difference is Litigious 8K filing date is used to identify the trades, instead of the QEA date. We classify an 8-K filing as litigious if it has higher than the median proportion of litigious words for all the 8-K filings made by all firms in that year. Litigious word proportion data comes from SEC Analytics Database.

Constituency Statutes: Dummy variable showing if the firm's state of incorporation is a constituency state in the current year. Data on the adoption of constituency statutes by the state is from Gao, Li and Ma (2021).

Fraction of Institutional Shareholders: Percentage of institutional shareholders, obtained from Thomson Reuters S34 database. It is measured as of the most recent fiscal quarter end immediately preceding the beginning of the year minus three months.

Number of Analysts: Number of analysts covering the firm, obtained from IBES database. It is measured as of the most recent month end immediately preceding the beginning of the year minus three months.

3-day Cumulative abnormal return around trade date: Cumulative abnormal return calculated net of the CRSP value-weighted index return during the three-day window (-1,+1) around the trading date (day 0).

Debt: Debt is calculated using quarterly COMPUSTAT data items as follows: debt in current liabilities (dlcq) plus total long-term debt (dlttq) divided by total assets (atq). It is measured as of the most recent fiscal quarter end immediately preceding beginning of the year minus three months.

Return on Equity: Return on Equity is calculated using quarterly COMPUSTAT data items as follows: operating income before depreciation (oibdpq) divided by 1-quarter-lagged book equity plus the carrying value of preferred stock (item pstk). It is measured as of the most recent fiscal quarter end immediately preceding the beginning of the year minus three months.

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Table 1 Descriptive statistics

This table presents the descriptive statistics for the variables used in the main regressions. Variable definitions are in Appendix 1. The insider trading sample includes all direct open market insider sales and purchases from 1986 through 2021. The sample for Accounting and Auditing Enforcement Release (AAER) Misstatements run from 1986-2019, and the sample for Class Action Lawsuit Filings run from 1996 to 2021. Class Action Lawsuit Filing data comes from Stanford Law School's Securities Class Action Clearinghouse (SCAC) and AAER data is from the University of Southern California's Leventhal School of Accounting.

	N	Mean	Std Dev	Q1	Median	Q3
Panel A: Purchases						
Opportunistic trade based on Quarterly Earnings Announcement (QEA) date	243,336	0.025	0.156	0.000	0.000	0.000
Opportunistic trade based on 8K filing date	196,518	0.056	0.229	0.000	0.000	0.000
Opportunistic trade based on Litigious 8K filing date	196,156	0.022	0.146	0.000	0.000	0.000
3-day Cumulative abnormal return around trade date	243,335	0.012	0.080	-0.020	0.005	0.034
Constituency State	243,336	0.418	0.493	0.000	0.000	1.000
Ln (Mcap)	243,336	12.307	2.081	10.863	12.228	13.615
Ln (B/M)	243,336	-0.541	0.899	-0.952	-0.450	-0.015
Past Return	243,336	-0.024	0.430	-0.241	-0.039	0.127
Past Volatility	243,336	0.600	0.444	0.305	0.474	0.757
Change in Volatility	243,336	0.023	0.327	-0.083	0.005	0.111
Ln (Trade Size)	243,336	9.715	1.917	8.558	9.793	10.968
CEO	243,336	0.144	0.351	0.000	0.000	0.000
Fraction of Institutional Shareholders	237,263	0.391	0.292	0.137	0.333	0.612
Number of Analysts	223,136	3.879	5.869	0.000	1.000	5.000
Panel B: Sales						
	N	Mean	Std Dev	Q1	Median	Q3
Opportunistic trade based on Quarterly Earnings Announcement (QEA) date	648,418	0.055	0.228	0.000	0.000	0.000
Opportunistic trade based on 8K filing date	487,761	0.079	0.270	0.000	0.000	0.000
Opportunistic trade based on Litigious 8K filing date	487,761	0.045	0.207	0.000	0.000	0.000
3-day Cumulative abnormal return around trade date	648,418	-0.001	0.051	-0.020	-0.001	0.017
Constituency State	648,418	0.258	0.437	0.000	0.000	1.000
Ln (Mcap)	648,418	14.330	2.102	13.016	14.369	15.706
Ln (B/M)	648,418	-1.171	0.905	-1.650	-1.058	-0.560
Past Return	648,418	0.219	0.601	-0.012	0.135	0.323
Past Volatility	648,418	0.459	0.321	0.269	0.379	0.552
Change in Volatility	648,418	-0.017	0.248	-0.091	-0.015	0.055
Ln (Trade Size)	648,418	11.971	1.911	10.779	12.074	13.261
CEO	648,418	0.126	0.332	0.000	0.000	0.000
Fraction of Institutional Shareholders	643,356	0.666	0.285	0.484	0.734	0.887
Number of Analysts	611,142	8.500	8.807	1.000	6.000	13.000
Panel C: Class Action Lawsuits and Misstatements						
	N	Mean	Std Dev	Q1	Median	Q3
Class Action Lawsuit Filings	98,923	0.031	0.174	0.000	0.000	0.000
AAER Misstatements	126,804	0.007	0.082	0.000	0.000	0.000

Table 2. Main Tests

The main variable of interest is *Constituency Statutes* dummy which is set to one if the firm's state of incorporation is a constituency statutes state for the current year. The dependent variable in Panel A is an opportunistic trade dummy which is set to one if it is made by an insider who is in the top quintile of the profitability ranking of past trades before earnings announcements. The dependent variable in Panel B is an opportunistic trade dummy which is set to one if it is made by an insider who is in the top quintile of the profitability ranking of past trades before Form 8K filing dates. The dependent variable in Panel C is an opportunistic trade dummy which is set to one if it is made by an insider who is in the top quintile of the profitability ranking of past trades before litigious Form 8K filing dates. A litigious Form 8K is one which has higher than the median proportion of litigious words for all the 8-K filings made by all firms in that year. Litigious word proportion data for 8K forms comes from SEC Analytics Database. Column 1 reports results for purchases and sales combined, column 2 for purchases only and column 3 for sales only. All other variable definitions are in Appendix 1. All the tests include industry and year dummy variables. Industries are defined using Fama-French 49 industries. Standard errors are adjusted for heteroskedasticity and clustered at the firm level. Robust *p*-values are in parentheses. ***, **, and * indicate significance at the 1%, 5%, and 10% levels respectively.

Panel A: Opportunistic Trades before Earnings Announcements			
Dep. Var.	(1) Opportunistic All Trades	(2) Opportunistic Purchases	(3) Opportunistic Sales
Constituency Statutes	-0.22337 (0.001)***	-0.07690 (0.454)	-0.21684 (0.005)***
Ln (Mcap)	0.00585 (0.698)	0.07348 (0.011)**	-0.04389 (0.010)***
Ln (B/M)	0.02483 (0.453)	0.08571 (0.180)	0.03337 (0.373)
Past Return	-0.03745 (0.093)*	-0.08412 (0.186)	-0.13359 (0.000)***
Past Volatility	0.20543 (0.005)***	-0.00165 (0.990)	0.38997 (0.000)***
Change in Volatility	-0.16510 (0.000)***	-0.02696 (0.776)	-0.20893 (0.000)***
Ln (Trade Size)	-0.01269 (0.271)	-0.04168 (0.133)	-0.02947 (0.011)**
CEO	0.35434 (0.000)***	0.58046 (0.000)***	0.36636 (0.000)***
Constant	-5.19845 (0.000)***	-5.50149 (0.000)***	-4.73410 (0.000)***
Fixed Effects	Yes	Yes	Yes
Observations	892,461	243,336	648,418
Pseudo R-squared	0.0379	0.0395	0.0405

Table 2. cont.

Panel B. Opportunistic Trades before the filing of 8K Forms			
Dep. Var.	(1)	(2)	(3)
	Opportunistic All Trades	Opportunistic Purchases	Opportunistic Sales
Constituency Statutes	-0.09456 (0.065)*	-0.19890 (0.025)**	-0.04750 (0.411)
Ln (Mcap)	-0.06437 (0.000)***	-0.04555 (0.032)**	-0.08394 (0.000)***
Ln (B/M)	-0.00016 (0.996)	-0.02504 (0.520)	0.00899 (0.811)
Past Return	0.02051 (0.291)	0.02446 (0.560)	-0.04927 (0.087)*
Past Volatility	0.56818 (0.000)***	0.33756 (0.001)***	0.80722 (0.000)***
Change in Volatility	-0.37579 (0.000)***	-0.18517 (0.005)***	-0.48825 (0.000)***
Ln (Trade Size)	-0.01435 (0.145)	-0.02874 (0.090)*	-0.02027 (0.063)*
CEO	0.31389 (0.000)***	0.39273 (0.000)***	0.30829 (0.000)***
Constant	-6.69107 (0.000)***	-5.76685 (0.000)***	-7.64186 (0.000)***
Fixed Effects	Yes	Yes	Yes
Observations	684,279	196,518	487,761
Pseudo R-squared	0.0707	0.0922	0.0676

Table 2. cont.

Panel C. Opportunistic Trades before the filing of Litigious 8-K Forms			
VARIABLES	(1) Opportunistic All Trades	(2) Opportunistic Purchases	(3) Opportunistic Sales
Constituency Statutes	-0.24229 (0.007)***	-0.19126 (0.276)	-0.23257 (0.020)**
Ln (Mcap)	0.02156 (0.322)	0.02724 (0.570)	-0.00977 (0.684)
Ln (B/M)	0.00620 (0.892)	0.03007 (0.633)	0.01282 (0.812)
Past Return	0.00845 (0.806)	-0.04926 (0.583)	-0.07785 (0.144)
Past Volatility	0.40269 (0.016)**	-0.06265 (0.801)	0.65014 (0.000)***
Change in Volatility	-0.26557 (0.000)***	-0.21739 (0.114)	-0.29460 (0.000)***
Ln (Trade Size)	-0.03377 (0.046)**	-0.06245 (0.034)**	-0.04157 (0.024)**
CEO	0.39780 (0.000)***	0.78372 (0.000)***	0.34273 (0.000)***
Constant	-10.88941 (0.000)***	-9.83063 (0.000)***	-10.97351 (0.000)***
Fixed Effects	Yes	Yes	Yes
Observations	684,279	196,156	487,761
Pseudo R-squared	0.0881	0.100	0.0854

Table 3. Local Corruption Tests

The main variable of interest is *Constituency Statutes* dummy which is set to one if the firm's state of incorporation is a constituency statutes state for the current year. The dependent variable in Panel A is an opportunistic trade dummy which is set to one if it is made by an insider who is in the top quintile of the profitability ranking of past trades before earnings announcements. The dependent variable in Panel B is an opportunistic trade dummy which is set to one if it is made by an insider who is in the top quintile of the profitability ranking of past trades before Form 8K filing dates. The dependent variable in Panel C is an opportunistic trade dummy which is set to one if it is made by an insider who is in the top quintile of the profitability ranking of past trades before litigious Form 8K filing dates. A litigious Form 8K is one which has higher than the median proportion of litigious words for all the 8-K filings made by all firms in that year. Litigious word proportion data for 8K forms comes from SEC Analytics Database. In this table, we re-examine the main tests in Table 2 for low and high corruption subsamples separately. Columns 1, 3 and 5 report results for purchases and sales combined, purchases only and sales only, for firms headquartered in low corruption states. Columns 2, 4 and 6 report the same results for firms headquartered in high corruption states. A state is designated as low (high) corruption state if conviction rates per capita in a given year are below (above) the median conviction rate per capita for all states in that year. We use state-level corruption data provided on Alex Butler's Website for conviction rate per capita. All other variable definitions are in Appendix 1. All the tests include industry and year dummy variables. Industries are defined using Fama-French 49 industries. Standard errors are adjusted for heteroskedasticity and clustered at the firm level. Robust *p*-values are in parentheses. ***, **, and * indicate significance at the 1%, 5%, and 10% levels respectively.

Panel A: Opportunistic Trades before Earnings Announcements

Dep. Var.	(1)	(2)	(3)	(4)	(5)	(6)
	Low Corruption	High Corruption	Low Corruption	High Corruption	Low Corruption	High Corruption
	Opp. All Trades		Opp. Purchases		Opp. Sales	
Constituency Statutes	-0.06965 (0.494)	-0.34186 (0.000)***	0.02932 (0.857)	-0.20222 (0.233)	-0.09013 (0.439)	-0.36085 (0.001)***
Ln (Mcap)	0.04330 (0.077)*	0.00934 (0.651)	0.13102 (0.001)***	0.04351 (0.325)	-0.00122 (0.966)	-0.02902 (0.214)
Ln (B/M)	0.02742 (0.646)	0.11906 (0.011)**	0.23476 (0.020)**	-0.00454 (0.958)	-0.04285 (0.536)	0.16772 (0.002)***
Past Return	-0.05499 (0.184)	0.01175 (0.775)	-0.24795 (0.005)***	0.05396 (0.571)	-0.05655 (0.186)	-0.12635 (0.019)**
Past Volatility	0.06998 (0.520)	0.18486 (0.079)*	0.06854 (0.663)	-0.07759 (0.735)	0.17174 (0.185)	0.38781 (0.001)***
Change in Volatility	-0.17103 (0.009)***	-0.19001 (0.014)**	-0.12694 (0.291)	0.03448 (0.865)	-0.18842 (0.013)**	-0.22846 (0.006)***
Ln (Trade Size)	-0.01872 (0.319)	-0.02111 (0.173)	-0.02667 (0.501)	-0.05846 (0.138)	-0.03222 (0.079)*	-0.03637 (0.029)**
CEO	0.51757 (0.000)***	0.37330 (0.000)***	0.67453 (0.000)***	0.52959 (0.001)***	0.50586 (0.000)***	0.37430 (0.000)***
Constant	-4.59010 (0.000)***	-6.02445 (0.000)***	-5.42733 (0.000)***	-5.94908 (0.000)***	-3.85510 (0.002)***	-5.58019 (0.000)***
Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
Observations	317,793	324,376	103,991	91,434	213,505	232,262
Pseudo R-squared	0.0470	0.0403	0.0603	0.0522	0.0518	0.0447

Table 3.cont.

Panel B. Opportunistic Trades based on the filing of 8K Forms						
	(1)	(2)	(3)	(4)	(5)	(6)
	Low Corruption	High Corruption	Low Corruption	High Corruption	Low Corruption	High Corruption
Dep. Var.	Opp. All Trades		Opp. Purchases		Opp. Sales	
Constituency Statutes	-0.01061 (0.893)	-0.20429 (0.005)***	-0.20807 (0.087)*	-0.23473 (0.054)*	0.09937 (0.275)	-0.18520 (0.028)**
Ln (Mcap)	-0.05879 (0.001)***	-0.03437 (0.056)*	-0.05968 (0.044)**	-0.01301 (0.674)	-0.07607 (0.001)***	-0.05196 (0.016)**
Ln (B/M)	-0.11261 (0.017)**	0.04275 (0.241)	-0.06516 (0.179)	-0.02827 (0.630)	-0.13934 (0.028)**	0.07090 (0.107)
Past Return	0.00981 (0.663)	0.04258 (0.221)	0.00664 (0.891)	0.05101 (0.493)	-0.02233 (0.461)	-0.05345 (0.235)
Past Volatility	0.37233 (0.000)***	0.66485 (0.000)***	0.22859 (0.085)*	0.41024 (0.006)***	0.51929 (0.000)***	0.94979 (0.000)***
Change in Volatility	-0.27257 (0.000)***	-0.47726 (0.000)***	-0.08127 (0.349)	-0.23819 (0.022)**	-0.38027 (0.000)***	-0.63212 (0.000)***
Ln (Trade Size)	-0.02572 (0.055)*	-0.01139 (0.346)	-0.05144 (0.032)**	-0.01121 (0.649)	-0.03616 (0.016)**	-0.02140 (0.110)
CEO	0.36178 (0.000)***	0.30071 (0.000)***	0.30624 (0.003)***	0.43642 (0.000)***	0.40379 (0.000)***	0.28388 (0.001)***
Constant	-7.50965 (0.000)***	-6.44288 (0.000)***	-5.75405 (0.000)***	-4.87455 (0.002)***	-6.18995 (0.000)***	-9.57278 (0.000)***
Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
Observations	283,722	305,185	92,626	85,182	190,927	220,003
Pseudo R-squared	0.0991	0.0589	0.121	0.0733	0.0958	0.0602

Table 3.cont.

Panel C. Opportunistic Trades based on the filing of Litigious 8-K Forms						
	(1)	(2)	(3)	(4)	(5)	(6)
	Low Corruption	High Corruption	Low Corruption	High Corruption	Low Corruption	High Corruption
Dep. Var.	Opp. All Trades		Opp. Purchases		Opp. Sales	
Constituency Statutes	-0.08086 (0.566)	-0.46153 (0.000)***	-0.12089 (0.592)	-0.15446 (0.477)	-0.06429 (0.694)	-0.55451 (0.000)***
Ln (Mcap)	0.03945 (0.208)	0.03982 (0.151)	-0.05407 (0.253)	0.14780 (0.035)**	0.04268 (0.245)	-0.00880 (0.772)
Ln (B/M)	-0.00677 (0.919)	-0.01040 (0.839)	0.02587 (0.784)	-0.02512 (0.762)	-0.01714 (0.839)	-0.00301 (0.961)
Past Return	-0.03471 (0.462)	0.05989 (0.345)	-0.12245 (0.273)	0.06019 (0.640)	-0.07899 (0.201)	-0.06978 (0.406)
Past Volatility	0.23291 (0.245)	0.30248 (0.065)*	-0.19091 (0.582)	0.12499 (0.633)	0.48424 (0.025)**	0.52732 (0.002)***
Change in Volatility	-0.23752 (0.014)**	-0.27221 (0.002)***	-0.14025 (0.446)	-0.36522 (0.020)**	-0.28345 (0.012)**	-0.27520 (0.006)***
Ln (Trade Size)	-0.03090 (0.213)	-0.04651 (0.021)**	-0.07535 (0.121)	-0.10386 (0.006)***	-0.03799 (0.178)	-0.04078 (0.067)*
CEO	0.46409 (0.000)***	0.41380 (0.000)***	0.63444 (0.001)***	0.95132 (0.000)***	0.43662 (0.003)***	0.30580 (0.017)**
Constant	-8.38496 (0.000)***	-10.30135 (0.000)***	-6.13047 (0.000)***	-4.33062 (0.002)***	-8.60395 (0.000)***	-10.23403 (0.000)***
Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
Observations	282,705	305,185	91,103	81,054	190,572	220,003
Pseudo R-squared	0.122	0.0761	0.139	0.0911	0.119	0.0760

Table 4.A. Institutional Ownership Tests

The main variable of interest is *Constituency Statutes* dummy which is set to one if the firm's state of incorporation is a constituency statutes state for the current year. The dependent variable in Panel A is an opportunistic trade dummy which is set to one if it is made by an insider who is in the top quintile of the profitability ranking of past trades before earnings announcements. The dependent variable in Panel B is an opportunistic trade dummy which is set to one if it is made by an insider who is in the top quintile of the profitability ranking of past trades before Form 8K filing dates. The dependent variable in Panel C is an opportunistic trade dummy which is set to one if it is made by an insider who is in the top quintile of the profitability ranking of past trades before litigious Form 8K filing dates. A litigious Form 8K is one which has higher than the median proportion of litigious words for all the 8-K filings made by all firms in that year. Litigious word proportion data for 8K forms comes from SEC Analytics Database. In this table, we re-examine the main tests in Table 2 for low and high institutional ownership subsamples separately. Columns 1, 3 and 5 report results for purchases and sales combined, purchases only and sales only, for firms headquartered in low institutional ownership firms. Columns 2, 4 and 6 report the same results for firms with high institutional ownership. A firm is designated as low (high) institutional ownership firm if institutional investors hold less (more) than 50% of the shares outstanding. Institutional ownership data comes from Thomson Reuters' S34 database. All other variable definitions are in Appendix 1. All the tests include industry and year dummy variables. Industries are defined using Fama-French 49 industries. Standard errors are adjusted for heteroskedasticity and clustered at the firm level. Robust *p*-values are in parentheses. ***, **, and * indicate significance at the 1%, 5%, and 10% levels respectively.

Panel A. Opportunistic Trades Based on Earnings Announcements

Dep. Var.	(1)	(2)	(3)	(4)	(5)	(6)
	Low Inst. Own.	High Inst. Own.	Low Inst. Own.	High Inst. Own.	Low Inst. Own.	High Inst. Own.
	Opp. All Trades		Opp. Purchases		Opp. Sales	
Constituency Statutes	-0.26042 (0.013)**	-0.14531 (0.076)*	-0.18052 (0.166)	0.18166 (0.183)	-0.24671 (0.077)*	-0.16515 (0.061)*
Ln (Mcap)	0.08133 (0.001)***	-0.07191 (0.000)***	0.14227 (0.000)***	-0.03470 (0.397)	0.02612 (0.365)	-0.09613 (0.000)***
Ln (B/M)	0.04004 (0.479)	-0.01663 (0.644)	0.17934 (0.032)**	-0.10192 (0.248)	-0.00679 (0.923)	0.02101 (0.594)
Past Return	-0.07295 (0.045)**	-0.04411 (0.177)	-0.07031 (0.322)	-0.14350 (0.125)	-0.15895 (0.002)***	-0.14608 (0.000)***
Past Volatility	0.09399 (0.371)	0.80173 (0.000)***	-0.01720 (0.914)	0.42676 (0.118)	0.21412 (0.062)*	0.99140 (0.000)***
Change in Volatility	-0.11553 (0.054)*	-0.44050 (0.000)***	-0.05210 (0.652)	-0.22658 (0.256)	-0.12262 (0.070)*	-0.44196 (0.000)***
Ln (Trade Size)	-0.05125 (0.018)**	-0.00556 (0.619)	-0.05469 (0.120)	-0.01855 (0.549)	-0.06765 (0.002)***	-0.02178 (0.060)*
CEO	0.28741 (0.008)***	0.37226 (0.000)***	0.43713 (0.005)***	0.78384 (0.000)***	0.29529 (0.039)**	0.36656 (0.000)***
Constant	-6.03015 (0.000)***	-3.40620 (0.002)***	-6.17335 (0.000)***	-4.38024 (0.003)***	-3.97446 (0.000)***	-2.81836 (0.020)**
Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
Observations	323,784	557,538	155,507	81,256	167,603	475,252
Pseudo R-squared	0.0476	0.0360	0.0547	0.0627	0.0635	0.0391

Table 4.cont.

Panel B. Opportunistic Trades based on the filing of 8K Forms						
	(1)	(2)	(3)	(4)	(5)	(6)
	Low Inst. Own.	High Inst. Own.	Low Inst. Own.	High Inst. Own.	Low Inst. Own.	High Inst. Own.
Dep. Var.	Opp. All Trades		Opp. Purchases		Opp. Sales	
Constituency Statutes	-0.32314 (0.000)***	0.05332 (0.379)	-0.24765 (0.033)**	-0.09862 (0.419)	-0.36914 (0.000)***	0.08108 (0.213)
Ln (Mcap)	-0.03904 (0.054)*	-0.10143 (0.000)***	-0.04836 (0.118)	-0.04713 (0.120)	-0.05747 (0.031)**	-0.11729 (0.000)***
Ln (B/M)	0.00741 (0.857)	-0.03805 (0.300)	-0.00772 (0.886)	-0.04835 (0.255)	0.02181 (0.687)	-0.02662 (0.531)
Past Return	0.01555 (0.509)	-0.00612 (0.878)	0.05019 (0.286)	-0.07096 (0.312)	-0.04638 (0.230)	-0.05721 (0.226)
Past Volatility	0.41068 (0.000)***	1.19102 (0.000)***	0.21084 (0.134)	1.05645 (0.000)***	0.60091 (0.000)***	1.31056 (0.000)***
Change in Volatility	-0.24734 (0.000)***	-0.77329 (0.000)***	-0.10801 (0.182)	-0.59914 (0.000)***	-0.33247 (0.000)***	-0.81521 (0.000)***
Ln (Trade Size)	-0.03322 (0.037)**	-0.00654 (0.529)	-0.01912 (0.399)	-0.04783 (0.032)**	-0.05819 (0.002)***	-0.00782 (0.483)
CEO	0.33156 (0.000)***	0.30389 (0.000)***	0.32008 (0.001)***	0.51449 (0.000)***	0.38761 (0.001)***	0.27472 (0.000)***
Constant	-6.11792 (0.000)***	-9.05606 (0.000)***	-5.26205 (0.000)***	-1.55319 (0.003)***	-6.95780 (0.000)***	-8.52184 (0.000)***
Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
Observations	259,457	417,625	128,105	61,926	131,352	353,212
Pseudo R-squared	0.107	0.0559	0.104	0.0742	0.123	0.0552

Table 4.cont.

Panel C. Opportunistic Trades based on the filing of Litigious 8-K Forms						
	(1)	(2)	(3)	(4)	(5)	(6)
	Low Inst. Own.	High Inst. Own.	Low Inst. Own.	High Inst. Own.	Low Inst. Own.	High Inst. Own.
Dep. Var.	Opp. All Trades		Opp. Purchases		Opp. Sales	
Constituency Statutes	-0.46502*** (0.004)	-0.12355 (0.228)	-0.32195 (0.235)	0.08285 (0.611)	-0.49745*** (0.006)	-0.13755 (0.215)
Ln (Mcap)	0.00532 (0.882)	-0.01761 (0.513)	-0.03253 (0.574)	0.06615 (0.384)	-0.01821 (0.679)	-0.04286 (0.145)
Ln (B/M)	0.03661 (0.605)	-0.04048 (0.408)	0.08291 (0.379)	-0.05997 (0.429)	0.01671 (0.857)	-0.01560 (0.775)
Past Return	0.04506 (0.254)	0.00132 (0.978)	0.05516 (0.605)	-0.21468* (0.075)	-0.03095 (0.592)	-0.07123 (0.226)
Past Volatility	0.15104 (0.603)	0.78726*** (0.000)	-0.36030 (0.329)	0.54898** (0.013)	0.45532 (0.102)	0.92386*** (0.000)
Change in Volatility	-0.14432 (0.281)	-0.48293*** (0.000)	-0.16317 (0.400)	-0.46728*** (0.004)	-0.15624 (0.343)	-0.46980*** (0.000)
Ln (Trade Size)	-0.08827*** (0.007)	-0.01783 (0.296)	-0.07939* (0.072)	-0.05004 (0.164)	-0.11294*** (0.001)	-0.02471 (0.177)
CEO	0.54221*** (0.000)	0.33887*** (0.000)	0.77224*** (0.000)	0.75856*** (0.000)	0.43541** (0.035)	0.31312*** (0.003)
Constant	-10.34564*** (0.000)	-10.03396*** (0.000)	-8.18545*** (0.000)	-4.29088*** (0.000)	-1.43381* (0.089)	-9.33201*** (0.000)
Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
Observations	259,457	417,625	126,433	61,411	120,315	353,212
Pseudo R-squared	0.1320	0.0653	0.1176	0.0855	0.1535	0.0651

Table 5. Analyst Coverage Tests

The main variable of interest is *Constituency Statutes* dummy which is set to one if the firm's state of incorporation is a constituency statutes state for the current year. The dependent variable in Panel A is an opportunistic trade dummy which is set to one if it is made by an insider who is in the top quintile of the profitability ranking of past trades before earnings announcements. The dependent variable in Panel B is an opportunistic trade dummy which is set to one if it is made by an insider who is in the top quintile of the profitability ranking of past trades before Form 8K filing dates. The dependent variable in Panel C is an opportunistic trade dummy which is set to one if it is made by an insider who is in the top quintile of the profitability ranking of past trades before litigious Form 8K filing dates. A litigious Form 8K is one which has higher than the median proportion of litigious words for all the 8-K filings made by all firms in that year. Litigious word proportion data for 8K forms comes from SEC Analytics Database. In this table, we re-examine the main tests in Table 2 for firms with no analyst coverage and firms with analyst coverage subsamples separately. Columns 1, 3 and 5 report results for purchases and sales combined, purchases only and sales only, for firms with analyst coverage. Columns 2, 4 and 6 report the same results for firms with no analyst coverage. Analyst coverage data comes from IBES database. All other variable definitions are in Appendix 1. All the tests include industry and year dummy variables. Industries are defined using Fama-French 49 industries. Standard errors are adjusted for heteroskedasticity and clustered at the firm level. Robust *p*-values are in parentheses. ***, **, and * indicate significance at the 1%, 5%, and 10% levels respectively.

Panel A. Opportunistic Trades Based on Earnings Announcements

Dep. Var.	(1)	(2)	(3)	(4)	(5)	(6)
	No Analyst Cvg	Analyst Cvg	No Analyst Cvg	Analyst Cvg	No Analyst Cvg	Analyst Cvg
	Opp. All Trades		Opp. Purchases		Opp. Sales	
Constituency Statutes	-0.34308 (0.002)***	-0.14410 (0.055)*	-0.46395 (0.008)***	0.10081 (0.368)	-0.25449 (0.052)*	-0.17602 (0.036)**
Ln (Mcap)	0.04930 (0.077)*	-0.02453 (0.177)	0.13798 (0.008)***	0.01371 (0.718)	-0.01016 (0.746)	-0.05877 (0.004)***
Ln (B/M)	0.09725 (0.062)*	0.02713 (0.516)	0.23567 (0.004)***	0.05156 (0.527)	0.09152 (0.132)	0.03277 (0.476)
Past Return	-0.08570 (0.053)*	-0.04833 (0.096)*	-0.12669 (0.209)	-0.04608 (0.510)	-0.20826 (0.001)***	-0.14809 (0.000)***
Past Volatility	0.17370 (0.191)	0.50582 (0.000)***	-0.03889 (0.857)	0.28382 (0.112)	0.39684 (0.005)***	0.74380 (0.000)***
Change in Volatility	-0.10829 (0.114)	-0.31173 (0.000)***	0.10047 (0.556)	-0.18837 (0.119)	-0.18962 (0.009)***	-0.38491 (0.000)***
Ln (Trade Size)	0.01172 (0.520)	-0.02243 (0.093)*	-0.04765 (0.234)	-0.04857 (0.143)	-0.01223 (0.534)	-0.03323 (0.011)**
CEO	0.43866 (0.000)***	0.32246 (0.000)***	0.67140 (0.000)***	0.58451 (0.000)***	0.48009 (0.000)***	0.30817 (0.000)***
Constant	-7.79569 (0.000)***	-3.79511 (0.000)***	-6.65253 (0.000)***	-4.08718 (0.000)***	-4.91510 (0.000)***	-3.47159 (0.002)***
Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
Observations	219,416	613,230	78,272	143,357	139,653	468,895
Pseudo R-squared	0.0637	0.0384	0.0659	0.0442	0.0587	0.0435

Table 5.cont.

Panel B. Opportunistic Trades based on the filing of 8K Forms						
Dep. Var.	(1)	(2)	(3)	(4)	(5)	(6)
	No Analyst Cvg	Analyst Cvg	No Analyst Cvg	Analyst Cvg	No Analyst Cvg	Analyst Cvg
	Opp. All Trades		Opp. Purchases		Opp. Sales	
Constituency Statutes	-0.29293 (0.005)***	-0.02653 (0.636)	-0.21001 (0.157)	-0.15472 (0.114)	-0.37819 (0.004)***	0.01526 (0.806)
Ln (Mcap)	-0.03320 (0.240)	-0.07993 (0.000)***	-0.07517 (0.105)	-0.05050 (0.067)*	-0.05039 (0.181)	-0.09328 (0.000)***
Ln (B/M)	0.05341 (0.311)	-0.00033 (0.993)	-0.00870 (0.892)	-0.02374 (0.594)	0.08627 (0.242)	0.00457 (0.912)
Past Return	0.01476 (0.706)	-0.00111 (0.963)	0.15220 (0.027)**	-0.03856 (0.391)	-0.12283 (0.086)*	-0.05704 (0.082)*
Past Volatility	0.24593 (0.037)**	0.87226 (0.000)***	0.20484 (0.116)	0.41999 (0.006)***	0.31512 (0.094)*	1.14705 (0.000)***
Change in Volatility	-0.11602 (0.116)	-0.56614 (0.000)***	-0.08534 (0.334)	-0.25784 (0.009)***	-0.13234 (0.237)	-0.69131 (0.000)***
Ln (Trade Size)	-0.04564 (0.024)**	-0.00801 (0.437)	-0.03786 (0.159)	-0.01657 (0.375)	-0.06468 (0.008)***	-0.01596 (0.157)
CEO	0.37968 (0.000)***	0.31146 (0.000)***	0.25558 (0.043)**	0.47370 (0.000)***	0.54433 (0.001)***	0.28617 (0.000)***
Constant	-6.57417 (0.000)***	-7.45912 (0.000)***	-4.94244 (0.000)***	-8.18266 (0.000)***	-8.65139 (0.000)***	-7.12523 (0.000)***
Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
Observations	104,892	550,999	54,766	128,916	49,740	422,083
Pseudo R-squared	0.0902	0.0734	0.0963	0.108	0.107	0.0684

Table 5.cont.

Panel C. Opportunistic Trades based on the filing of Litigious 8-K Forms						
	(1)	(2)	(3)	(4)	(5)	(6)
	No Analyst Cvg	Analyst Cvg	No Analyst Cvg	Analyst Cvg	No Analyst Cvg	Analyst Cvg
Dep. Var.	Opp. All Trades		Opp. Purchases		Opp. Sales	
Constituency Statutes	-0.50741 (0.003)***	-0.17598 (0.065)*	-0.32871 (0.214)	-0.11290 (0.578)	-0.61489 (0.003)***	-0.18096 (0.080)*
Ln (Mcap)	0.04890 (0.302)	-0.00074 (0.976)	-0.03368 (0.660)	0.00177 (0.978)	0.02440 (0.657)	-0.02454 (0.357)
Ln (B/M)	0.10367 (0.191)	0.01682 (0.743)	0.12465 (0.189)	0.02777 (0.729)	0.05906 (0.596)	0.02327 (0.685)
Past Return	0.02691 (0.791)	-0.01230 (0.753)	0.07437 (0.733)	-0.07408 (0.341)	-0.09222 (0.539)	-0.09562 (0.116)
Past Volatility	0.23430 (0.379)	0.52848 (0.013)**	-0.30724 (0.199)	0.09566 (0.760)	0.55854 (0.058)*	0.77393 (0.002)***
Change in Volatility	-0.21606 (0.089)*	-0.30578 (0.000)***	-0.19304 (0.264)	-0.22187 (0.198)	-0.27491 (0.079)*	-0.32769 (0.001)***
Ln (Trade Size)	-0.09312 (0.006)***	-0.02827 (0.116)	-0.03160 (0.573)	-0.07800 (0.019)**	-0.14605 (0.000)***	-0.03042 (0.107)
CEO	0.73526 (0.000)***	0.36134 (0.000)***	0.75129 (0.001)***	0.85088 (0.000)***	0.81965 (0.001)***	0.29445 (0.004)***
Constant	-8.95319 (0.000)***	-8.20130 (0.000)***	-7.39105 (0.000)***	-2.45598 (0.020)**	-3.45976 (0.005)***	-7.52492 (0.000)***
Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
Observations	103,730	550,542	53,849	119,991	42,852	421,756
Pseudo R-squared	0.147	0.0845	0.138	0.0933	0.160	0.0828

Table 6. Profitability of Insider Trading in Constituency Statutes States

The dependent variable CAR3vw is the three day (-1,+1) cumulative abnormal around an insider trade (where the trade day is day 0), market-adjusted using the CRSP value-weighted index. The main variable of interest is *Constituency Statutes* dummy which is set to one if the firm's state of incorporation is a constituency statutes state for the current year. Column 1 reports returns for insider purchases and column 2 for insider sales. All other variable definitions are in Appendix 1. All the tests include industry and year dummy variables. Industries are defined using Fama-French 49 industries. Standard errors are adjusted for heteroskedasticity and clustered at the firm level. Robust *p*-values are in parentheses. ***, **, and * indicate significance at the 1%, 5%, and 10% levels respectively.

	(1)	(2)
	Purchases	Sales
Dep. Var.	CAR3vw	CAR3vw
Constituency Statutes	-0.00181*** (0.002)	0.00023 (0.304)
Ln (Mcap)	0.00002 (0.914)	0.00049*** (0.000)
Ln (B/M)	-0.00262*** (0.000)	-0.00159*** (0.000)
Past Return	-0.00510*** (0.000)	-0.00145** (0.020)
Past Volatility	0.02015*** (0.000)	-0.00015 (0.885)
Change in Volatility	-0.00379*** (0.009)	-0.00056 (0.533)
Ln (Trade Size)	0.00144*** (0.000)	-0.00019*** (0.001)
CEO	0.00042 (0.471)	0.00026 (0.231)
Constant	-0.02674*** (0.000)	-0.00514** (0.030)
Fixed Effects	Yes	Yes
Observations	243,343	649,153
R-squared	0.022	0.002

Table 7. Class Action Filings

The dependent variable is *Class Action Filing*, which takes the value of one if there is a securities class action lawsuit filed in a year, and zero otherwise. Class Action Filing data comes from Stanford Law School's Securities Class Action Clearinghouse (SCAC). The main variable of interest is *Constituency Statutes* dummy which is set to one if the firm's state of incorporation is a constituency statutes state for the current year. All other variable definitions are in Appendix 1. The regression includes industry and year dummy variables. Industries are defined using Fama-French 49 industries. Standard errors are adjusted for heteroskedasticity and clustered at the firm level. Robust *p*-values are in parentheses. ***, **, and * indicate significance at the 1%, 5%, and 10% levels respectively.

Dep. Var.	Class Action Filing
Constituency Statutes	-0.29334*** (0.000)
Ln (Mcap)	0.27277*** (0.000)
Ln (B/M)	-0.06678*** (0.004)
Past Return	-0.41227*** (0.000)
Past Volatility	0.57952*** (0.000)
Change in Volatility	-0.07561* (0.087)
Debt	0.18617* (0.094)
Return on Equity	-0.32740** (0.020)
Constant	-8.33558*** (0.000)
Fixed Effects	Yes
Observations	98,923
Pseudo R-squared	0.0881

Table 8. Financial Misstatements

The dependent variable is *AAER Misstatement* which takes the value of one if there is a financial misstatement in a year, and zero otherwise. AAER data is from the University of Southern California's Leventhal School of Accounting and runs from 1986 to 2019. The main variable of interest is *Constituency Statutes* dummy which is set to one if the firm's state of incorporation is a constituency statutes state for the current year. All other variable definitions are in Appendix 1. The regression includes industry and year dummy variables. Industries are defined using Fama-French 49 industries. Standard errors are adjusted for heteroskedasticity and clustered at the firm level. Robust *p*-values are in parentheses. ***, **, and * indicate significance at the 1%, 5%, and 10% levels respectively.

Dep. Var.	AAER Misstatement
Constituency Statutes	-0.33951** (0.027)
Ln (Mcap)	0.28454*** (0.000)
Ln (B/M)	0.03125 (0.614)
Past Return	0.14502*** (0.009)
Past Volatility	0.17651 (0.255)
Change in Volatility	-0.08666 (0.311)
Debt	1.14119*** (0.000)
Return on Equity	0.02187 (0.339)
Constant	-9.38893*** (0.000)
Fixed Effects	Yes
Observations	126,804
Pseudo R-Squared	0.0939