

Does Bank Stakeholder Orientation Enhance Financial Stability? Evidence from a Natural Experiment

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ABSTRACT

Using the staggered enactment of US state constituency statutes, which provides plausibly exogenous variations in directors' fiduciary duties, we find that stakeholder orientation significantly reduces bank risk. This relation cannot be explained by reverse causality, local economic conditions and coincidental state antitakeover laws and banking deregulation policies. Consistent with lower risk-taking, we find that banks reduce risk through increasing capital and lending to safer borrowers. Furthermore, stakeholder orientation improves bank performance only for those banks that take excessive risk. Finally, banks that previously received a statute passage fared significantly better during the crises. Overall, our findings highlight the importance of bank directors' fiduciary duties in safeguarding financial stability, and more broadly, support the increasing calls for greater emphasis on stakeholder interests in the current bank regulatory and governance reforms.

Keywords: Bank risk-taking; Stakeholder orientation; Constituency statutes; Fiduciary duties; Financial stability.

JEL Classification: G01; G21; G28; G32; M14.

1. Introduction

The 2007-09 financial crisis has cast doubt on the adequacy of the prevailing bank regulatory and governance frameworks, which focus primarily on shareholder value maximization (Senior Supervisors Group, 2009). In particular, recent studies document that banks with managers whose interests are better aligned with those of shareholders or banks with more shareholder-friendly boards incurred significantly greater losses during the crisis (Fahlenbrach and Stulz, 2011; Beltratti and Stulz, 2012). As noted by Mr. Klaus Schwab, the founding chairman of the World Economic Forum, “[t]he current crisis should be a warning shot for us to fundamentally rethink...the regulatory mechanisms that underpin our economy [and that] we need to embrace [the] stakeholder principle...” (The Wall Street Journal, 2010). Similarly, Macey and O’Hara (2003, p.92) argue that “[...]to safeguard the banking systems, bank directors’] duties should not run exclusively to shareholders.” Echoing these concerns, the current bank governance reform initiatives advocate that banks place greater emphasis on value creation for stakeholders to ensure the safety and soundness of the banking sectors (Laeven, 2013). It is perhaps surprising that, despite the increased calls for reconciling stakeholder interests, empirical evidence on the relevance of stakeholder orientation remains largely absent. In this article, we exploit the plausibly exogenous variations in directors’ fiduciary duties to examine whether there is a causal impact of stakeholder orientation on bank risk-taking, performance and stability.

Shareholders and stakeholders have different risk preferences and return expectations. Stakeholders such as creditors have less risk-taking incentives and tend to focus more on long-term stability than shareholders because they typically receive fixed income but bear significant downside risk. By contrast, shareholders due to their limited liability and asymmetric payoffs are prone to take greater risk than is desired by stakeholders (Jensen and Meckling, 1976). This conflict between shareholders and stakeholders, or asset-substitution problem, is especially severe among banks because they are highly leveraged (Jensen and Meckling, 1976) and informationally opaque (Morgan, 2002), face limited disciplining from insured depositors (Merton, 1977), and have implicit government guarantees (Gropp, Hakenes and Schnabel, 2011). These unique features of banks provide greater incentives and opportunities for shareholders and managers to invest in excessively risky assets and shift losses onto their stakeholders (Macey and O’Hara, 2003; Thakor, 2014; Acharya, Mehra and Thakor, 2016). These arguments amount to the view that the prevailing bank governance model, which focuses primarily on shareholder

value maximization, may promote asset-substitution problems and excessive risk-taking, thereby threatening systemic stability (Macey and O'Hara, 2003, 2016; Fahlenbrach and Stulz, 2011; Laeven, 2013).

From a governance perspective, directors' oversight of bank operations and risk-taking is important for mitigating excessive risk-taking and systemic risk (Adams and Ferreira, 2012; Ellul and Yerramilli, 2013). There has always been a strong demand from regulators, practitioners and the public for bank directors to consider stakeholder, long-term or social interests. For instance, Section 5000.1 of the Bank Holding Company Supervision Manual (Federal Reserve, 2016, p.1) states that "[t]he board of directors is responsible to the bank's depositors, other creditors, and shareholders for safeguarding their interests..."¹ The traditional fiduciary laws diverge from such expectations on bank boards and instead require bank directors to account for shareholder interests only (Herlihy and Makow, 2014). Since the shareholder primacy view prevails in court and the business community, such legal pressure discourages bank directors from questioning, challenging or even opposing bank policies that favor shareholders but could jeopardize bank stability and social interests (Macey and O'Hara, 2003). To mitigate this problem, Macey and O'Hara (2003, 2016) propose that the fiduciary duties of bank directors should be *broadened* to consider the long-term and stability implications of bank actions. On a similar note, Federal Reserve Governor, Daniel Tarullo (2014), highlights that modifying the fiduciary duties of boards of financial firms will "...make the boards of financial firms responsive to the broader interests implicated by their risk-taking decisions..." Based on these arguments, we hypothesize that an increase in bank directors' authority to consider stakeholder interests reduces bank risk-taking and contributes to financial stability.²

¹ Similarly, the Office of the Comptroller of the Currency (OCC) (1997, p.2) also demands that "[d]irectors of a national bank are accountable not only to their shareholders and depositors but also to their regulators." Furthermore, in their special report on governance of financial institutions, the Group of Thirty Working Group (2012, pp.39-40) recommends that "[g]iven the unique externalities of FIs [(Financial Institutions)], society's interests and well-being must always be a high priority for the board... Regardless of whom the primary stakeholder is, FI boards in every country ought to take a long-term view on strategy..."

² There are at least two reasons as to why bank directors may choose to consider stakeholder interests and financial stability. First, since banks are important financial intermediaries and their failures could have widespread negative consequences to many market participants, bank directors may feel that it is morally right for them to pursue banking policies favoring stakeholders or stability to safeguard financial stability. Second, since banking is a specialized, competitive and highly regulated industry, bank directors face severe reputation concerns in the labor markets, and thus would be willing to consider the broader impact of bank risk-taking on stakeholders and the society.

We test our hypothesis by exploiting a unique empirical setting of the staggered passage of constituency statutes across US states. Constituency statutes expand directors' fiduciary duties, which are traditionally owed to shareholders, to take into account the interests of a variety of stakeholders, including creditors, suppliers, employees, the government, the rest of society, etc. The motivation behind the development of the statutes is to provide directors with a legal mechanism for pursuing stakeholder interests or other *long-term* corporate objectives without violating their legal duties to shareholders (Hale, 2003). The statutes are legally enforceable and have been applied by courts in defending directors' considerations of stakeholder interests. Based on 30 years of case evidence, Geczy, Jeffers, Musto and Tucker (2015) conclude that the statutes are a "true expansion of directors' authority" to consider stakeholder interests.

Following Bertrand and Mullainathan (2003), we estimate a difference-in-differences model to explore the relation between stakeholder orientation and bank risk-taking. The treatment group comprises states that pass the constituency statutes and the control group comprises states that do not in a given year. Based on 939 publicly traded US Bank Holding Companies (BHCs) from 1986 to 2012, we find that the passage of constituency statutes reduces bank total risk and idiosyncratic risk by 6.6% and 7.9%, and increases Z-score by 15.4% (relative to the sample means). We run a series of robustness tests and confirm that the negative relation is robust to alternative fixed effects, standard errors, model specifications, estimation approaches and samples, and the use of an alternative measure of bank stakeholder orientation.

The key identifying assumption of our difference-in-differences tests is that the treated and control BHCs are on parallel trends prior to statute passages (Roberts and Whited, 2012). We find that the statute effects up to two years prior to the treatment are small and insignificant, suggesting that the differences in pre-trends between the two groups are indeed indistinguishable. The decrease in bank risk occurs after statute passage, which rules out reverse causality.

To ensure that our results are not driven by chance, we run three placebo tests. The first test maintains the distribution of enactment years but randomly assigns states into these years. The second test keeps the distribution of the treated states but randomizes their enactment years. The third test randomizes both the enactment years and treated states. In each test, we generate 5000 placebo samples and obtain a distribution of placebo regression estimates. Our true coefficient estimate is smaller than at least 90 percent of the placebo estimates.

A potential concern is that unobserved changes in local economic conditions which jointly determine the introduction of constituency statutes and bank risk-taking might have driven our results. To address this concern, we exploit the idea that local economic conditions are likely to be similar across adjacent states but the statute effect stops at the borderline, and analyze a subsample of treated and control BHCs that are just a border away, geographically close to each other and similar in size. We confirm that this concern does not explain our results.

Since some of the constituency statutes were passed at similar times as other state antitakeover laws and banking deregulation policies, a potential concern is that our results might have been driven by these confounding events. To address this concern, we exclude “contaminated” states in which the statute passage coincided with any one of the three major state antitakeover laws, finding that our baseline results hold. Further, when we jointly control for the antitakeover laws in the regressions, none of these laws except the constituency statutes are significant in reducing bank risk. Likewise, we account for the staggered *interstate* and *intrastate* banking deregulation policy changes and the *erection of entry barriers* to interstate banking and confirm that these banking policy changes have little effects on our results.

Next, we explore two channels through which banks could reduce risk-taking. First, to the extent that constituency statutes expand bank directors’ authority to pursue more prudent policies favoring stakeholders and stability, banks could increase their equity capital to reduce asset-substitution moral hazard problems or better absorb future losses (Jensen and Meckling, 1976; Macey and O’Hara, 2003; see Thakor, 2014, for a review). Consistent with this channel, we find that banks increase their capital-to-assets ratios by 6.9% (relative to the sample mean) after statute passage. Second, we explore the bank lending channel and present evidence consistent with banks shifting their lending from riskier to safer borrowers after statute passage.

An alternative explanation for our finding is that the constituency statutes might have been used primarily as takeover defenses. Facing reduced threat of takeover, bank managers may prefer a “quiet life” and avoid the difficult decisions and costly efforts associated with risk-taking (Bertrand and Mullainathan, 2003). To test this alternative explanation, we examine the heterogeneity in the statute effect on bank risk. Inconsistent with the takeover defenses argument, we find that the negative statute effect concentrates on those statutes which allow considerations of stakeholder interests to be outside of change-of-control situations. Further, additional tests show that the passage of constituency statutes has little effect on BHCs’ acquisition likelihood.

Having established the negative effect of stakeholder orientation on bank risk-taking, we now turn our attention to understanding its implications for bank performance. The effect of stakeholder orientation on bank performance is ambiguous. For instance, on the one hand, the reduction in loan risks and losses after statute passage may enhance bank profitability. On the other hand, the lower loan prices owing to the shift towards safer borrowers may hurt bank performance. We identify a setting in which the former effect is likely to dominate the latter. Theory suggests that banks with severe moral hazard problems have stronger incentives to invest in excessively risky and inefficient assets that are high-risk-low-return. For such banks, their inefficient risk-taking would make a shift from riskier to safer borrowers more desirable insofar as the gain from reducing loan losses more than offsets the reduction in loan interest income. However, for banks characterized by safer borrowers, such a shift would be less appealing because the marginal benefit from reducing loan losses is lower. Consistent with these predictions, we find that the impact of constituency statutes on bank performance is small and insignificant on average but significantly positive for high-risk banks.

Finally, we examine the longer-term value implications of stakeholder orientation by examining bank crisis performance. Recent studies document that “risk culture” determines a bank’s sensitivity to crises (Fahlenbrach, Prilmeier and Stulz, 2012; Ellul and Yerramilli, 2013). To the extent that the adoption of constituency statutes has influenced bank risk culture in favor of stakeholders and stability, one may expect the statute to have a persistent effect and mitigate bank losses during the subsequent crises. To shed some light on this issue, we trace the BHCs that have received a statute passage prior to the crises and examine their stock performance during the 1998 and 2007-08 crises relative to the size-location-matched control BHCs. The previously treated BHCs fared significantly better in both crises, with difference-in-differences estimates ranging from 6.5 to 9.7 percentage points for the 1998 crisis and from 13.8 to 33.8 percentage points for the 2007-08 crisis. Overall, stakeholder orientation plays an important role in mitigating losses during crises, thereby enhancing financial stability.

Our paper makes the following important contributions. To start with, we present the first empirical evidence in support of the widespread calls for greater emphasis on stakeholder interests in the bank regulatory and governance reforms to safeguard the banking system (Macey and O’Hara, 2003; Mehran, Morrison and Shapiro, 2011; Laeven, 2013). Our results suggest that stakeholder orientation reduces bank risk-taking, mitigates losses during crises, and in turn

improves financial stability. They also complement the existing literature on the incompatibility between shareholder value maximization and financial stability which finds that more shareholder-oriented banks have worse crisis performance, more severe moral hazard problems and greater systemic risk.³

Second, our paper specifically contributes to one of the most heated debates within the context of the current bank governance reforms on whether the fiduciary duties of bank directors should be heightened to consider the long-term, stability implications of bank decisions (Macey and O'Hara, 2003, 2016; Tarullo, 2014). While there is a great demand for bank directors to consider stakeholder, long-term or social interests, the traditional fiduciary laws stipulate that bank directors owe legal duties only to shareholders and have no obligations to mitigate systemic risk. Under this legal pressure to maximize shareholder profits, bank directors tend to tolerate risky bank policies, which potentially threatens stability (Macey and O'Hara, 2003, 2016). The constituency statutes, which alleviate such legal pressure and expand directors' duties to consider stakeholder interests, offer a unique empirical setting for testing these arguments. We show novel evidence that banks with directors whose duties are expanded after statute passage reduce risk-taking through adopting a less risky capital structure and lending to safer borrowers, lending support to their proposals.

Third, our paper relates to the literature on the economics of stakeholder theory. For instance, Allen, Carletti and Marquez (2015) incorporate the costs of layoffs for workers during bankruptcies into firm objective function and show that stakeholder firms are more valuable when the marginal cost uncertainty is greater than demand uncertainty. Although we do not focus on employees, our definition of stakeholder orientation is consistent with theirs as it reflects a focus on firm survival and stability. Magill, Quinzii and Rochet (2015) develop a model to justify the view that large corporations should take into account stakeholder interests in addition to those of shareholders. They argue that large firms face endogenous risks that generate negative externalities on their stakeholders which are not internalized by shareholders. The resulting under-investment problem in the prevention of such risks can be alleviated if firms' objectives are to maximize the total welfare of their stakeholders rather than only shareholder value. Other studies include Allen and Gale (2000, Chapter 12) and Allen (2005) who argue that

³ See, for example, John and Qian (2003), Bebchuk, Cohen and Spamann (2010), Fahlenbrach and Stulz (2011), Beltratti and Stulz (2012), Bannier, Feess and Packham (2013), Berger, Imbierowicz and Rauch (2016), etc.

the inclusion of stakeholder benefits in firm objective functions correct for market failures and improve social welfare. Our paper complements these studies by showing that stakeholder orientation improves bank stability and reduces negative externalities. Moreover, our paper adds to the management literature on whether it is socially desirable for firms to pursue stakeholder interests (see, e.g., Freeman, 1984; Cornell and Shapiro, 1987; Freeman, Wicks and Parmar, 2004). As Jensen (Agle et al., 2008) notes, "...[in] the debate about stakeholder theory versus stockholder theory...there is way too much noise, way too much sloppy thinking and way too *little* empirical evidence present". We are one of the few to provide evidence to this debate.

Fourth, our paper extends the banking literature (see, e.g., Keeley, 1990; Saunders Strock and Travlos, 1990; Hellmann, Murdock and Stiglitz, 2000; Laeven and Levine, 2009; Goetz, Laeven and Levine, 2016) by showing that directors' stakeholder orientation is an important determinant of bank risk-taking. Furthermore, since stakeholder orientation reflects corporate culture and attitudes, we contribute to the understanding of the significant role of bank "risk culture" and "business model" in affecting risk-taking (see, e.g., Fahlenbrach, Prilmeier and Stulz, 2012; Ellul and Yerramilli, 2013; Ho, Huang, Lin and Yen, 2016).

Finally, our paper is also linked to studies on whether and how stakeholders influence corporate policies.⁴ Particularly relevant to our paper is Lin, Schmid and Xuan (2016) who find that board employee representation reduces firm agency conflicts with creditors and results in lower costs of financing in Germany. While both their paper and ours are interested in boards' considerations of stakeholder interests, we focus on directors' legal authority to consider stakeholder interests whereas their paper focuses on the direct involvement and influence of employees on the boards. Furthermore, our paper relates to studies examining how constituency statutes or similar legal rulings affect corporate policies. For instance, Flammer and Kacperczyk (2016) and Atanossov (2013) find that the passage of constituency statutes has a positive impact on corporate innovation. Gao, Li and Ma (2016) document a reduction in the cost of debts after the adoption of constituency statutes. Exploiting the 1991 Delaware legal ruling, Becker and Strömberg (2012) show that fiduciary duties influence firm equity issues, investments and risk-taking. This paper differs from the aforementioned studies in that we derive policy implications relevant to the current bank regulatory and governance reforms and systemic stability.

⁴ For studies on employee treatment and protection, see, for example, Bae, Kang and Wang (2011), Simintzi, Vig and Volpin (2015), etc.

Our paper is organized as follows: Section 2 introduces the constituency statutes. Section 3 explains our sample and variables. Section 4 explains our empirical strategy and presents our empirical results and Section 5 concludes.

2. Background on Constituency Statutes

The origin of constituency statutes traces back to the 1930s debate on the fundamental nature of corporation and specifically on whether management had a duty to shareholders or to a broader group of stakeholders (Orts, 1992). Under the traditional US laws, corporate leaders were legally required to maximize shareholder value and were not allowed to consider stakeholder interests or other nonmonetary corporate objectives. Since this shareholder primacy view prevailed in court and was dominant in the business society, fearing opposition and litigation from shareholders, corporate leaders were reluctant to divert their attention from shareholder value maximization (Smith, 1998; Fisch, 2005). Nonetheless, a number of corporate policies, e.g., restructuring, liquidations and acquisitions, that favor shareholder interests may often adversely affect stakeholders (including managers) and impair their firm-specific investments that are not fully protected through explicit contracts (Gavis, 1990). Because corporate actions affect both shareholders and stakeholders, proponents of stakeholder theories argue that corporations should consider the interests of the latter in their strategies and actions.

This debate regained its popularity in the 1980s amidst the hostile takeover waves in the US. While takeovers could bring benefits to target firm shareholders, the associated changes in ownership often imposed significant costs and losses onto its stakeholders, including creditors, employees, customers, suppliers, the community, etc. There was widespread criticism from the public about the inability of the corporate laws in protecting stakeholder interests and the increasing debate on whether corporations should be allowed to consider stakeholder interests eventually led to the development of the constituency statutes. Although the introduction of the constituency statutes was initially triggered by the merger waves in the 1980s (Karpoff and Wittry, 2016), their applications were not limited to takeovers or change-of-control situations; in fact, over half of the statutes can be applied in general business decisions (Bainbridge, 1992; Oswald, 1998). As of 2012, 35 US states have passed the constituency statutes (Barzuza, 2009). Table 1 shows a timeline of the passage of constituency statutes.

Insert Table 1 about here

Although the constituency statutes differ across states, they share a common theme, that is, to permit directors or officers to consider the effects on various specified constituencies when making business decisions, without breaching their fiduciary duties to shareholders (Geczy, Jeffers, Musto and Tucker, 2015). For instance, the 1987 Minnesota statute (*MINN. STAT. ANN. § 302A.251*) stipulates that when considering the best interest of the company, a director may consider the interests of (1) its employees, customers, suppliers and creditors, (2) the state and national economy, and (3) the community and the rest of the society, as well as may consider (4) the long- and short-term interests of the corporation. The relevant clauses in the state legislatures of the 35 statutes are provided in Table IA.1 of the Internet Appendix.

The constituency statutes are legally enforceable and have been applied by courts to defend stakeholder interests. According to Geczy, Jeffers, Musto and Tucker (2015), over the 1983-2013 period, there are in total 47 federal and state court cases that discussed the constituency statutes. These cases range from mergers, liquidations, restructuring and other shareholder derivative suits. The authors have analyzed the courts' enforcement opinions and coded 20 cases as having a "Positive" opinion, 9 cases as "Positive/Neutral", 14 cases as "Neutral", and as few as 4 cases as "Neutral/Negative".⁵ Based on the 30 years of court opinions that are mostly positive and above neutral, the authors conclude that the constituency statutes are a "true expansion of directors' authority" to consider stakeholder interests.

Several empirical studies have established that the enactment of constituency statutes improves corporate stakeholder performance. For instance, Luoma and Goodstein (1999) find that constituency statutes are associated with greater board stakeholder representation. Both Flammer and Kacperczyk (2016) and Atanossov (2013) find that firms incorporated in states with statute passage adopt more stakeholder-friendly policies than states without passage. To shed further light on this, we examine (unreported) whether statute passage also improves bank stakeholder performance. First, we find that passing the statutes significantly lowers the

⁵ A case is coded as "Positive" when the constituency statute "was a determinative element in the court's ruling and the court...recognized directors' expanded ability to consider non-shareholder constituents, but did not create a private enforcement right in such non-shareholder constituents." A case is coded as "Positive/Neutral" for court opinions "where the court discussed the scope of constituency statutes both in terms of expanding director rights and declining to extend constituency statutes to create a positive right in non-shareholder constituents..." A case is coded as "Neutral" for court opinions "that cited, referenced by name, or included dicta regarding constituency statutes...". The "Neutral/Negative" category "reflects cases where the court discussed constituency statutes, but declined to recognize expanded director authority..." (see Geczy, Jeffers, Musto and Tucker, 2015, pp. 106-110).

likelihood of a large reduction in BHCs' employee number, consistent with greater job stability.⁶ Second, consistent with the view that banks engage with the rest of the society through greater tax transparency⁷, we find that statute passage significantly increases bank effective tax rates.⁸

Finally, because the constituency statutes do not likely reflect the bank's strategic decisions, the associated increase in stakeholder orientation is plausibly exogenous to its risk-taking. Given the staggered nature of statute passage, BHCs are exogenously shocked at different times, allowing us to setup a difference-in-differences model with multiple treatment groups and time periods for identification. This setting helps reduce the potential biases and noise associated with analysis with only a single exogenous shock (Roberts and Whited, 2012).

3. Sample Formation and Variable Construction

We start with all publicly traded US BHCs that filed FR Y-9C reports with the Federal Reserve during the 1986-2012 period. We download the BHCs' consolidated financial information from the Bank Regulatory database and their stock information from CRSP.⁹ We then supplement these data with additional firm attributes, such as states of location and incorporation, from Compustat. Our final sample consists of 9,248 bank-year observations from 939 BHCs. 166 of these BHCs received a statute enactment during our sample period (see Table 1).

Following Goetz, Laeven and Levine (2016), we construct three measures of bank risk. First, bank total risk is defined as the annualized standard deviation of daily stock returns for

⁶ Specifically, we find that the constituency statutes significantly lower the likelihood of having an economically significant reduction in the number of employees (significant at the 5% level). We define an economically significant reduction in the number of employees as any negative percentage changes that are less than its 10th percentile in our sample BHCs. These results can be found in Table IA.2 of the Internet Appendix.

⁷ For instance, in the 2014 global citizenship report, Citi Group (2014) wrote, "...our culture of responsible finance extends to our approach to paying taxes... We emphasize both strong internal controls and transparency with global taxing authorities..."; in the 2013 sustainability report, HSBC (2013) stated that, "By running a sustainable banking business, HSBC is able to make a valuable contribution to the global economy by...[paying] tax revenues to governments in the countries and territories where we operate...HSBC does not enter into or promote tax avoidance."

⁸ The effective tax rate is computed as the ratio of tax expense to pre-tax earnings. This measure is commonly used in the tax literature as a proxy for tax avoidance [see for a discussion of this measure in Hanlon and Heitzman (2010)]. These results can be found in Table IA.2 in the Internet Appendix.

⁹ The stock information is merged with the bank fundamentals, using the linking table provided by the New York Federal Reserve Bank. The linking table can be accessed at:

[http://www.newyorkfed.org/research/banking_research/datasets.html]

each year. Second, bank idiosyncratic risk (*IVol*) is defined as the annualized standard deviation of the residuals from the following model:

$$R_{it} = \alpha_i + \beta_{1i} R_{mkt,t} + \beta_{2i} INTEREST_t + \varepsilon_{it}. \quad (1)$$

where R_{it} is daily stock returns of BHC i , $R_{mkt,t}$ is excess market returns of the value-weighted CRSP market index, and $INTEREST_t$ is the changes in the three-month Treasury bill rates. Third, we compute a BHC's Z -score as follows:

$$Z\text{-score}_{it} = (ROA_{it} + Capital/TA_{it})/\sigma_{it} \quad (2)$$

where ROA_{it} is the return on assets, $Capital/TA_{it}$ is the capital to total asset ratio, and σ_{it} is the annualized standard deviation of daily stock returns over a year. Z -score can be interpreted as the number of standard deviations by which profit can decrease before a bank goes into bankruptcy, where a larger Z -score indicates greater bank stability and lower risk.

We control for several bank characteristics that may influence risk-taking. First, bank size is measured as the natural logarithm of the book value of deflated total assets. Bank profitability is measured by return on assets (ROA), which is calculated as earnings before taxes and extraordinary items divided by total assets. Income from nontraditional banking activities is measured by the ratio of non-interest income to assets ($Non\text{-}interest\ income/TA$). Liquidity risk is captured by the ratio of non-core deposits to assets ($Non\text{-}core\ deposits/TA$) and the ratio of total loans to assets ($Loans/TA$). Bank franchise value is captured by the market-to-book equity ratio ($Market\text{-}to\text{-}book\ equity\ ratio$) (Keeley, 1990).¹⁰ We control for the frequency of trading in BHC stocks ($FREQ$), defined as the average daily volume of shares traded divided by the number of shares outstanding. To account for the effect of macroeconomic conditions on bank risk-taking, we include state real GDP growth and the natural logarithm of state population in the model, which are both downloaded from the US Bureau of Economic Analysis (BEA). To reduce the effects of outliers, all bank variables are winsorized at the 1st and 99th percentiles.

Table 2 reports the summary statistics. We find that BHC size, as measured by deflated total assets, is highly skewed and ranges from a minimum of \$111 million to a maximum of

¹⁰ Our results are similar when we measure franchise value by Keeley's q (Keeley, 1990), computed as the sum of the market value of equity plus the book value of liabilities divided by the book value of total assets.

\$2.07 trillion¹¹ with a mean (median) of \$17.7 (\$1.4) billion. For bank risk-taking, the means (medians) of *Total risk*, *IVol* and *Z-score* are 40.9% (34.3%), 38.2% (31.9%) and 0.298 (0.273), respectively. For bank profitability, the mean (median) *ROA* and *Non-interest income/TA* are 1.1% (1.3%) and 1.2% (1%), respectively. As for the other bank variables, the average non-core deposits to total assets, loan-to-assets ratio, market-to-book equity ratio and frequency of trading are 12.6%, 64.9%, 1.48 and 0.2%, respectively.

Insert Table 2 about here

4. Empirical Results

4.1. Constituency Statutes and Bank Risk-Taking

To investigate whether stakeholder orientation affects bank risk-taking, we follow Bertrand and Mullainathan (2003) and formulate a difference-in-differences test design in a multiple treatment groups and time periods setting based on the staggered passage of constituency statutes across US states. The baseline full model is written as follows:

$$Risk_{islrt} = \alpha_t + \alpha_i + \alpha_r \times \alpha_t + \lambda \times Constituency\ Statute_{st} + \delta X_{islrt} + \gamma W_{lrt} + \varepsilon_{islrt}, \quad (3)$$

where i is a BHC, s is the state of incorporation, l is the state of location, r is the economic region and t is year. $Risk_{islrt}$ is *Total risk*, *IVol* or *Z-score*. $Constituency\ Statute_{st}$ is a treatment dummy variable, which equals one if a BHC is incorporated in state s that has passed a constituency statute by year t and zero otherwise. X_{islrt} and W_{lrt} are vectors of bank and state control variables, respectively (see Section 3). Bank (α_i) and year fixed effects (α_t) are included to control for unobservable time-invariant bank characteristics and economy-wide shocks on bank risk-taking. We also account for the effects of time-varying regional shocks on bank risk-taking by interacting a region indicator with the year dummies ($\alpha_r \times \alpha_t$) in the model. The BHCs are grouped into four regions—Northeast, South, Midwest or West—based on their states of location following the US Census Bureau. Standard errors are clustered at the state of incorporation level to account for serial correlation following the recommendations by Bertrand, Duflo and Mullainathan (2004) (our results are robust to the use of BHC-clustered robust standard errors and the two-step procedure to account for serial correlation following Bertrand, Duflo and Mullainathan (2004)).

¹¹ In our sample, the maximum total deflated assets of 2.07 trillion refers to Citigroup Inc. in 2007 while the minimum total deflated assets of 111 million refers to American Bancorporation in 1987.

The average treatment effect of stakeholder orientation on bank risk-taking is captured by the estimated coefficient on *Constituency Statute*, λ . Including the bank, year and region-year fixed effects allows λ to be estimated as the *within-state* differences before and after the passage of constituency statute as opposed to the before-after differences in states where there are no changes in statute in the same period (Imbens and Wooldridge, 2009).

To illustrate, assume that we are interested in estimating the effect of constituency statute in Indiana in 1989 on bank risk-taking, we can subtract the bank risk before 1989 from the bank risk after 1989 for BHCs incorporated in Indiana. However, it is difficult to identify the causal statute effect because bank risk-taking may also be influenced by other events or economy-wide shocks that occurred in about 1989. To control for these confounding effects, we can use a control state where there is no change in constituency statute in the same period. We then calculate the difference between the difference in bank risk in Indiana before and after 1989 with the same before-after difference in bank risk in the control state. This difference in the two differences is an estimate of the effect of constituency statute in Indiana. The regression framework extends this example to account for the fact that there are many constituency statutes staggered over time.

Table 3 reports the estimation results for equation (3). In columns (1), (4) and (7) where bank controls, bank and year fixed effects are included, the estimated coefficients of *Constituency Statute* are negative and statistically significant for *Total risk*, and *IVol* and is significantly positive for *Z-score*. The coefficient estimates for *Constituency Statute* remain similar in magnitude and statistical significance after we control for the state GDP growth and log population (see columns (2), (5) and (8)) and further controlling for region-year fixed effects (see columns (3), (6) and (9)). In addition, the statutes' negative effects on bank risk are economically significant. Specifically, the enactment of constituency statutes decreases bank total risk by 6.6% and idiosyncratic risk by 7.9%, and increases the Z-score by 15.4%, relative to the sample means. These findings are consistent with the hypothesis that stakeholder orientation reduces bank risk-taking.

Insert Table 3 about here

4.2. Robustness Tests

Table 4 presents the robustness tests. We use the same bank and state control variables as well as the fixed effects as described in equation (3), unless stated otherwise. For brevity, we report only

the estimated coefficients and standard errors for *Constituency Statute* and present them in rows rather than columns.¹²

First, we use alternative standard errors clustered at the BHC level and obtain similar results (see row (1)). Second, to account for serial correlations in the error terms, we use the two-step procedure following Bertrand, Duflo and Mullainathan (2004). In the first step, the bank risk measures are regressed on the bank and state controls as well as the fixed effects as described in equation (3) without the treatment dummy variable. We then extract the residuals from these regressions for the treated BHCs and then average these residuals for the pre-treatment and post-treatment periods to obtain a two-period panel data. In the second step, we regress these average residuals on *Constituency Statute* with White robust standard errors. The results remain qualitatively similar (see row (2)).

In row (3), we control for the state of incorporation fixed effects to account for any persistent differences across states, such as differences in the banking industry structure or differences in the relative market power of large versus small banks (Rice and Strahan, 2010), etc., that may influence bank risk-taking. Our results continue to hold.

In our sample, some states have more bank-year observations and treated BHCs than others, and hence, our results may be driven by the possible over-representation of these states. To address this concern, we estimate weighted least squares (WLS) regressions with weights calculated as the inverse of the number of bank-year observations in each state of incorporation, thus allowing each state to receive equal weights in the estimation. Our results are similar and have become slightly stronger in both magnitude and significance (see row (4)).

Next, we exclude 16 states (down to 5,696 observations) in which no constituency statutes were enacted to avoid potential concerns about selection—BHCs incorporated in states with statute passage may be different from those incorporated in states without statute passage, based on unobservable variables related to bank risk-taking—and estimate the regressions. As row (5) shows, our results remain robust.

A next concern is that Delaware-incorporated BHCs may be different from other BHCs incorporated elsewhere. A notable difference is that under the Delaware law, firms may consider stakeholder interests to the extent that such considerations maximize shareholder interests

¹² The unabridged version of these robustness results is available upon request.

(Barzuza, 2009). Likewise, the 1991 Delaware’s court ruling of the Credit Lyonnais case shifted the fiduciary duties of corporate directors towards creditors (from shareholders) for distressed firms (Becker and Strömberg, 2012). To ensure that our results are not driven by the Delaware-incorporated BHCs, we exclude them (down to 7,273 observations) and re-estimate the baseline models. As Row (6) shows, the subsample results remain similar despite being less significant.

Next, since the included bank and state control variables may also be influenced by the adoption of constituency statutes, we may have a problem of “bad controls” (see Angrist and Pischke, 2008). Row (7) reports regressions that only include the treatment variable and the fixed effects on the right hand side, yielding very similar results in both magnitude and significance.

Furthermore, economy-wide shocks may cause bank characteristics to affect risk-taking differently in different periods. Rows (8) to (14) examine whether the statute effects are sensitive to controlling for such differences. We interact bank control variables, one at each time, with the year dummies in the baseline model and find that our results hold.

Since the majority of the constituency statutes were enacted in the late 1980s (in 25 of 35 states between 1986 and 1990) and our sample covers the period 1986-2012, we have more “after treatment” than “before treatment” years. Rows (15) and (16) show that our results are similar in both magnitude and significance when we use subsamples ending in either 1995 or 2005.

Furthermore, the extant literature acknowledges that bank competition affects risk-taking. For instance, Martínez-Miera and Repullo (2010) show that a non-linear (“U-shaped”) relationship exists between bank competition and risk-taking.¹³ In row (17), we control for the Herfindahl Index (*H-index*) of loan concentration and its squared term in the baseline model and find that our results are unaffected.¹⁴

¹³ The non-linear relationship arises because of two competing effects. The first effect is the “risk-shifting” effect, whereby bank competition lowers loan rates, loan default probabilities, and bank risk. The second effect is the “margin” effect, whereby lower loan rates reduce the revenue from performing loans, which is a buffer for loan losses, thus resulting in riskier banks. As the risk-shifting effect dominates in concentrated markets, while the margin effect takes over as competition increases, a U-shaped relationship between competition and bank risk is found to capture their net effects.

¹⁴ Following Claessens and Laeven (2004), *H-index* is defined as the sum of BHCs’ squared market shares in total loans within the state of location in a given year. Our results remain robust when *H-index* is defined as the sum of BHCs’ squared market shares in total loans within the state of incorporation in a given year.

Finally, there are some inconsistencies in the legal literature about the enactment year of constituency statutes. For example, compared to those reported by Karpoff and Wittry (2016), 7 states in our sample have statutes enacted at different years, including Connecticut, Indiana, Kentucky, Maine, Missouri, Nebraska and Texas. To ensure that our results are not driven by such discrepancies, in row (18) we exclude all BHCs incorporated in these 7 states (down to 8,200 observations) and confirm that our baseline results are robust.

Insert Table 4 about here

4.3. Additional Endogeneity Tests

4.3.1. Dynamic Treatment Model

A potential endogeneity concern is reverse causality. For instance, lawmakers may respond to negative events owing to excessive risk-taking and enact policies favoring stakeholders. To address this concern, we estimate the dynamic treatment model as follows:

$$\begin{aligned} Risk_{islrt} = & \alpha_t + \alpha_i + \alpha_r \times a_t + \lambda_1 \times Before^{-2 \text{ or } -1}_{st} + \lambda_2 \times Current^0_{st} + \lambda_3 \times After^{+1}_{st} \\ & + \lambda_4 \times After^{>=+2}_{st} + \delta X_{islrt} + \gamma W_{lrt} + \varepsilon_{islrt}, \end{aligned} \quad (4)$$

where $Before^{-2 \text{ or } -1}_{st}$ is a dummy variable equal to one for each of the two years preceding enactment of a constituency statute, $Current^0_{st}$ is a dummy variable equal to one for years of statute enactment, $After^{+1}_{st}$ is a dummy variable equal to one for the year after statute enactment, and $After^{>=+2}_{st}$ is a dummy variable equal to one if it is two or more years after a statute enactment. The coefficient estimate for $Before^{-2 \text{ or } -1}_{st}$, λ_1 , is of particular interest as its magnitude and statistical significance indicate whether the pre-trends (in bank risk) are systematically different between the treated and control BHCs.

Table 5 reports the results of the dynamic treatment analysis. We find that the coefficient estimates for $Before^{-2 \text{ or } -1}_{st}$ are small and insignificant in general for all of the three risk measures, suggesting no systematic differences in pre-trends between the treated and control BHCs and that the parallel trend assumption is likely satisfied (Roberts and Whited, 2012). Compared to the pre-treatment years, we observe an increase in the negative statute effects on bank risk-taking at the year of statute enactment as shown by the considerably larger and significant (for *IVol* and *Z-score*) coefficient estimates for $Current^0_{st}$. In the one year after statute enactment, the negative statute effects generally become stronger, and the coefficient estimates for $After^{+1}_{st}$ are significant for *Total risk* (at the 10% level), *IVol* (at the 10% level) and *Z-score* (at the 1% level).

Finally, the coefficient estimates for $After^{>+2}_{st}$ are the largest compared to other periods and are significant for all models, suggesting that the negative statute effects have persisted in the longer-term and that reverse causality does not drive our results.

Insert Table 5 about here

4.3.2. Placebo Tests

We conduct three placebo tests that randomize the assignment of constituency statutes. In the first test, we keep the distribution of the enactment years unchanged and randomly assign states into each of these years (without replacement)¹⁵, allowing any unobservable shocks occurring at about the same time as the statute passage to remain in the analysis. The second test maintains the distribution of the treated states but randomizes their enactment years, allowing any persistent state effects to continue to drive our results. The third test randomizes both the enactment years and the states (with no replacement for states). Within each placebo sample, we estimate the baseline model of equation (3) and store the coefficient and standard error estimates for the placebo statute. We repeat this procedure 5,000 times to obtain a distribution of the placebo estimates for each test.

In unreported results, we find that the effect of the placebo statute is small and insignificant for all placebo tests. In the first placebo test, the actual estimate for *Constituency Statute* is larger than the placebo estimate in 4,995 out of 5,000 placebo samples (99.9%) for *Z-score*, implying a 0.1 of 100 chance of randomly observing the actual estimate when the null of no statute effect is in fact true (Rosenbaum, 2009). For the remaining risk measures, the actual estimate is larger than the placebo estimate in at least 4,638 of 5,000 (92.8%) cases. The second and third placebo tests yield similar and even more significant results. These unreported results can be found in Table IA.3 of the Internet Appendix.

Overall, the placebo tests show that our results could not have been driven by chance. In addition, unobserved market-wide shocks, persistent state effects and the imperfect structure in the standard error matrix of the regressions do not drive our results.

¹⁵ For instance, in 1990, the constituency statutes were passed in Mississippi, Pennsylvania and Rhode Island. In the remaining 48 states, we randomly choose three states and assign a treatment event to them. We do this for each year with at least one statute passage and are careful not to assign a treatment to states which have already been treated (i.e., with no replacement).

4.3.3. *Unobservable Confounding Local Economic Conditions*

A potential concern is that unobservable changes in local economic conditions, driving both the introduction of constituency statutes and bank risk-taking, may bias our results. A plausible example is that politicians tend to be more successful in introducing a constituency statute in a booming economy (Flammer and Kacperczyk, 2016), and such favorable economic conditions may also influence bank risk-taking. We perform two tests to address this concern.

First, we run a placebo test that uses the treated states' (pre-treatment) GDP-matched bordering states as placebo states. Given that the treated and placebo states likely experience similar economic conditions, if the coefficient estimate for the placebo constituency statute continues to be significant, our earlier results could not have been caused by the statute enactment. In unreported results, we find that the placebo statute has small coefficient estimates and is insignificant in all models. The details of the placebo states and these results are provided in Table IA.4 of the Internet Appendix.

Second, we exploit the discontinuity in the effects of constituency statutes on bank risk between the treated BHCs and the control BHCs located in adjacent states just across the border. Since local economic conditions tend to spill across state borders (Heider and Ljungqvist, 2015), it will therefore be the case that if the constituency statutes are driven by unobserved changes in local economic conditions and if these changes (rather than the statutes) also affect bank risk-taking, the treated and control BHCs in bordering states would spuriously appear to respond to the statutes. Thus, this concern predicts no significant differences in bank risk between the treated BHCs and the control BHCs in bordering states.

We match each treated BHC to a control BHC located in a bordering state without statute passage and is closest in size.¹⁶ For each matched BHC pair, we keep the year before and after the statute passage for the analysis. To ensure that the treated and control BHCs in bordering states are subject to similar local economic shocks, we remove all matched pairs with a distance greater than 500 miles (from 166 down to 130 pairs). We also further restrict the distances between the treated and control BHCs to be within 250 miles (down to 99 pairs) and 125 miles

¹⁶ Of the 166 treated BHCs, 10 are located and incorporated in different states. We match each of these 10 BHCs with a control BHC located in the same state of location but incorporated in another state. Our conclusions are unaffected if we match each of these 10 BHCs with a control BHC located in a bordering state.

(down to 44 pairs)¹⁷. The detailed diagnostics for these matched samples are provided in Table IA.5 of the Internet Appendix. We estimate equation (3) on the matched samples and report the results in Table 6.

Insert Table 6 about here

In Panel A, with a 500-mile distance restriction, the estimated coefficients for *Constituency Statute* are significant at the 5% level or better for all three models, again revealing a negative statute effect on bank risk-taking. Panels B and C restrict the distance to be within 250 and 125 miles, respectively. While the power of the tests becomes more constrained in the smaller samples, our results are nonetheless similar. In particular, in Panel C, where distance is restricted to be within 125 miles, we still find a negative and significant (for *Total risk* and *IVol*) statute effects on bank risk, suggesting that our results are not driven by unobservable confounding local economic conditions.

4.3.4. Coincidental State Antitakeover Laws

The existing literature presents evidence that after the adoption of state antitakeover laws, managers who are generally risk-averse and now face increased protection from the antitakeover laws would seek to reduce firm risk. For instance, Bertrand and Mullainathan (2003) find that takeover protection reduces plant births and deaths. Garvey and Hanka (1999) document that the passage of state antitakeover laws reduces firm leverage. Likewise, Low (2009) documents reduced firm risk after an exogenous increase in takeover protection in Delaware during the mid-1990s. Consequently, if some of the constituency statutes were passed at similar times with these other state antitakeover laws, the reduced bank risk we document might potentially be driven by these confounding antitakeover laws. To address this concern, we collect information on the timing of the passage of major state antitakeover laws from Bertrand and Mullainathan (2003) and show empirically that the effect of constituency statutes on bank risk is independent of those of the coincidental state antitakeover laws.

¹⁷ The restrictions of 250-mile and 125-mile correspond to the 75th and 50th percentiles of distance in the final matched sample. We do not further restrict the distance to be within 100 miles (the 25th percentile, observations drop to 124) to avoid the small sample problem.

Panel A of Table 7 compares the timing of the adoption of constituency statutes with those of three major state antitakeover laws, including the control share acquisition laws, business combination laws and the fair price laws. There are in total 14 constituency statutes which were enacted in the same years as the three major state antitakeover laws, which affects 56 treated BHCs (33.7% of the total treated BHCs). To be more stringent, we define a state as confounded by the other antitakeover laws if the constituency statute was enacted in the one year prior to, during the year of, and in the one year after a passage of any of the antitakeover laws. We identify 16 confounded states and 66 treated BHCs (39.8% of the total treated BHCs) incorporated in these 16 states. As a preliminary test, we estimate our baseline risk models on a subsample that has excluded these 16 confounded states (down to 6,796 observations). As Panel B shows, our baseline results remain very similar.

Insert Table 7 about here

Panel C presents a more formal test to distinguish the effect of constituency statutes from those of the antitakeover laws. Specifically, we construct an indicator variable for each of the three major antitakeover laws, which equals one after the law passage and zero otherwise. We then estimate the baseline risk models and jointly control for the three antitakeover law treatment variables in the regressions. Our results reveal that none of the state antitakeover laws exert a significant effect on bank risk. However, the passage of constituency statutes remains highly significant in reducing bank risk. Together, our results are unlikely be driven by the omitted variables problem relating to coincidental state antitakeover laws.

4.3.5. Coincidental Banking Policy Changes

Another potential concern is that the enactment of constituency statutes may have coincided with several US state banking deregulation policy changes which may affect bank competition and risk-taking, thus potentially driving our results.

During the 1970-1990s, the US states deregulated *interstate* banking and *intrastate* branching activities. These staggered banking policy changes across states and time may have influenced our results if the banks' increased geographical expansion owing to deregulation has affected their business models, competition and thus risk-taking. In addition, while the Interstate Banking and Branching Efficiency Act (IBBEA) (in 1999) removed all remaining federal

restrictions on interstate banking as of 1995, it also allowed states to have their own discretion to erect out-of-state entry barriers to interstate branching. Such staggered erection of entry barriers may also affect bank risk-taking through changing the competitive environments of the banking industry.

Comparing the timing of the passage of constituency statutes with these deregulation policy changes, Panel A of Table 8 shows that there are only three constituency statute enactments (Wisconsin in 1987; Louisiana in 1988; and Indiana in 1989) which were enacted in the same year as the *interstate* and *intrastate* deregulation policy changes, affecting 13 BHCs in total (7.8% of the total treated BHCs). As a first test, we exclude BHCs incorporated or located in 10 confounded states (2,051 observations excluded) in which the enactment of constituency statutes is either in the *one year before*, *during the year of*, or *in the one year after* a banking deregulation policy change, removing 30 treated BHCs in total (18.1% of the total treated BHCs). As shown in Panel B, our results remain significant and similar in magnitude.

Insert Table 8 about here

Further, we control for these coincidental banking policy changes in the regressions. Following Cornaggia, Mao, Tian and Wolfe (2015), we construct two indicator variables, *Inter* and *Intra*, which equal zero before the interstate and intrastate banking deregulations, and one otherwise. We use the Rice and Strahan (2010) index (*RS index*), which ranges from zero (the least restrictive) to four (the most restrictive), to measure the state branching restrictions.¹⁸ In Panel C, we jointly control for *Inter*, *Intra* and *RS index* in the models and find that our results hold. Considering these results together, we confirm that these coincidental banking policy changes have little effects on our results.

4.3.6. Using an Alternative Bank-Level Stakeholder Orientation Measure

This section investigates whether we can replicate our earlier results with an alternative bank-level measure of stakeholder orientation based on KLD data.

¹⁸ Following Rice and Strahan (2010), we add one to *RS index* if a state has any one of the following provisions, (i) the minimum age of the target institution, (ii) de novo interstate branching, (iii) the acquisition of individual branches, and (iv) a state-wide deposit cap.

KLD rates firms on how well they care for their stakeholders along several dimensions, such as community, employees, diversity, etc.¹⁹ Following Deng, Kang and Low (2013), we use a two-step procedure to construct an overall KLD rating (*KLD*) for each BHC.^{20, 21} The merged *KLD* sample comprises 314 BHCs (1,619 bank-year observations) over the period 1991-2010.²² We then regress the bank risk-taking measures on *KLD*, the bank and state controls and the fixed effects and cluster standard errors at the bank level. The results, which we do not report here, indicate a negative and significant association between *KLD* and bank risk, consistent with our difference-in-differences results. In addition, we address the potential concern that the relationship between bank stakeholder orientation and risk may be dynamically endogenous: past risk may influence both current risk and stakeholder engagement (see Wintoki, Linck, and Netter, 2012). To this end, we apply a dynamic panel system Generalized Method of Moments (GMM) estimator (Arellano and Bover, 1995; Blundell and Bond, 1998) that allows us to control for the lagged risk measures and use the BHCs' past information as instruments.²³ After we control for the lagged risk measures, *KLD* remains negatively and significantly associated with bank risk-taking. The Sargan tests of over-identifying restrictions under the null hypothesis of instrument validity cannot be rejected for all three models. These results are provided in Table IA.7 of the Internet Appendix.

¹⁹ For example, in the employee relations dimension, a rating of one is assigned to "Union Relations Strength" if a firm has a good union relationship that is beneficial to its employees, and zero otherwise. In the environment dimension, KLD assigns one to "Ozone Depleting Chemicals Concern" if a firm produces ozone-depleting chemicals that cause harm to the natural environment, and zero otherwise.

²⁰ First, in each of the five dimensions—community, natural environment, product quality, employees and diversity—we standardize the number of strengths and concerns by the corresponding number of strength and concern indicators. Second, we sum the standardized ratings across the five dimensions for strengths and concerns, respectively. *KLD* is the difference between the standardized total strength and the standardized total concern scores.

²¹ We check our results to alternative approaches in constructing *KLD*, including no standardization, the inclusion of the human rights and corporate governance dimensions and the use of indicator variables that are only available throughout our sample period, and confirm that our results are robust. These results are available upon request.

²² The summary statistics of this KLD-merged BHC sample are provided in Table IA.6 of the Internet Appendix.

²³ Under the system GMM approach, the model is estimated at both levels and first differences and uses instruments in first differences for the level regression and instruments in levels for the first-differenced regression. We treat all independent variables as endogenous (except the year dummy) and instrument them with the three-period lagged bank risk measure and the two-period lagged right-hand-side variables for the difference equation and their lagged differences for the regression in level.

4.4. *Constituency Statutes and Bank Risk-Taking: Further Evidence*

In previous sections, we document a significant reduction in bank risk after the enactment of constituency statutes and that this relationship is robust to an extensive set of robustness and endogeneity tests. To strengthen our causal interpretation, this section explores the channels through which BHCs reduce their risk-taking and specifically investigates whether the statute enactment influences bank corporate decisions relating to risk-taking.

4.4.1. *Constituency Statutes and Bank Capital*

An important way banks could lower risk-taking is to alter their capital structure. There is a widespread consensus in the literature that higher bank capital levels mitigate moral hazard (risk-shifting) problems and contribute positively to financial stability (see, e.g., Acharya, Mehran and Thakor, 2016; Thakor, 2015, for a review). First, banks may exploit the deposit insurance put option (Merton, 1977) or respond to the shareholder-stakeholder conflict (Jensen and Meckling, 1976; Macey and O'Hara, 2003) and choose to invest in excessively risky and potentially inefficient assets. Since these risk-shifting incentives would become more severe the more highly leveraged the bank is, increasing equity capital helps to curb bank excessive risk-taking (see, e.g., Merton, 1977; Coval and Thakor, 2005). Moreover, bank capital also helps banks to better absorb losses and economic shocks with their own resources, which prevents the banks from being insolvent and requiring government bailouts, thereby enhancing systemic stability and social welfare (Demirgüç-Kunt, Detragiache and Merrouche, 2013). To the extent that the enactment of constituency statutes expands bank directors' authority and discretion to pursue more prudent banking policies in favor of stakeholders and stability, these directors may encourage banks to reduce risk-taking through increasing their equity capital.

Insert Table 9 about here

Table 9 presents the baseline regressions that replace the bank risk variables with bank capital ratios. The same control variables and fixed effects as in the baseline models are used. To isolate the effect of constituency statutes on bank capital from those of other coincidental changes in state laws, we control for the state antitakeover laws and the banking deregulation policy variables. Standard errors are clustered at the state of incorporation level.

Columns (1) and (3) of Table 9 show that the enactment of constituency statutes significantly (at the 5% level or better) increases bank capital-to-assets ratios (*Capital/TA*) by

6.9% and capital-to-loans ratios (*Capital/TL*) by 7.7%, relative to their sample means. These findings are consistent with the view that BHCs reduce risk-taking through maintaining a higher capital level to buffer future losses and mitigate moral hazard conflicts. Columns (2) and (4) examine the dynamic treatment effects for both capital measures and show that the significant increases in bank capital occur one year after the statute enactment and become more significant in subsequent years. In addition, the statute effects in the two years prior to statute enactment are small and insignificant for both models, suggesting little differences in pre-trends between the treated and control BHCs and that the parallel trend assumption is likely satisfied.

Overall, these results provide more direct evidence that the enactment of constituency statutes reduce bank risk-taking in a causal sense. In particular, we show that banks reduce their risk-taking by adopting less risky capital structures, thereby enabling them to better absorb future losses and mitigate asset-substitution moral hazard problems.

4.4.2. Constituency Statutes and Bank Lending Activities

Next, we examine whether the enactment of constituency statutes also lower risk-taking through changing their lending activities. Broadly speaking, there are at least three ways in which banks could adjust their lending activities that are consistent with lower risk-taking. First, banks could reduce risky lending, which would be reflected by a reduction in total loan volume. Second, banks may choose not to reduce their lending volume but rather shift their lending from riskier to safer borrowers. If this is true, after statute enactment, we would find little changes in bank total loan volume, an improvement in loan quality and lower interest margins due to cheaper loan prices. Third, given that the statute enactment has expanded bank directors' responsibilities to consider more long-term results and be less tolerant to moral hazard problems, the increased risk oversight by these directors may lead to an improved lending quality or efficiency. If this is the case, we may expect to find little changes in bank total loan volume, improved loan quality and little decrease in bank interest margins. To distinguish between these explanations, we estimate the baseline and dynamic treatment models to examine how statute enactment influences bank total loans, loan quality and net interest margins. The same bank and state controls as in the baseline models as well as the state antitakeover laws and banking deregulation policies are included. Standard errors are clustered at the state of incorporation level.

Insert Table 10 about here

Column (1) of Table 10 shows that the enactment of constituency statutes is insignificant in explaining bank log total loans ($Ln(Loans)$). The dynamic treatment model of column (2) shows similar results in that the statute effects in all of the periods around the enactment are small and insignificant.²⁴ These results imply that the first explanation is unable to explain our results.

Next, we investigate whether the statute enactment influences bank loan quality. We measure loan quality by non-performing loans, defined as the sum of loans 30 days or more past due and nonaccrual loans, scaled by total assets (NPL/TA).²⁵ Note that since BHCs are only required to report these two data items in the FR Y-9C reports beginning from 1990, the tests on loan quality are performed on a subsample covering 1990-2012. This data issue reduces the number of treated BHCs to 31. To address potential selection issues, we follow the matching procedure as described in Section 4.3.5 and match each of the 31 treated BHCs with a control BHC that is located in a bordering state and closest in bank size in order to create a matched sample for the difference-in-differences analysis. The matching is satisfactory in removing the differences in the observables between the treatment and control groups (see Table IA.5 of the Internet Appendix).

Column (3) of Table 10 shows a significantly (at the 10% level) negative effect of constituency statutes on NPL/TA . To gauge the economic magnitude, passing the statutes reduces NPL/TA by 16.3% relative to the sample mean. Column (2) reports the results estimated on the size-location-matched sample, showing very similar results in both magnitude and significance (at the 5% level). In column (5), the dynamic treatment model shows that the significantly negative statute effects on NPL/TA occur at the year of and in the one year after the treatment. The pre-treatment statute effects are small and insignificant, suggesting little systematic differences in the pre-trends between the treatment and control groups. These findings consistently show that statute enactment improves bank loan quality, consistent with both the second and the third explanations.

Finally, to distinguish between the second and third explanations, we investigate whether the overall loan prices, as measured by the ratio of net interest income to total assets (*Net interest*

²⁴ In unreported results, we use $Loans/TA$ as an alternative loan measures and find similarly insignificant results.

²⁵ In unreported results, we scale non-performing loans by total loans and find qualitatively similar results.

income/TA) following Ho and Saunders (1981), have changed after statute passage. In column (6), the coefficient estimate for *Constituency Statute* is negative and significant at the 1% level, suggesting that constituency statutes significantly reduce loan prices. Specifically, enacting the constituency statutes reduces bank net interest margin by 3.1% relative to the sample mean. Column (7) presents the dynamic treatment model showing that the negative statute effect on interest margin is significant from the year of enactment onwards, whereas the statute effect in the two years prior to the enactment is small and insignificant. These results are most consistent with the second explanation that banks did not reduce risky lending but rather shifted their lending from riskier to safer borrowers.

4.5. *Alternative Explanation*

As discussed in Section 2, the passage of constituency statutes was initially triggered by the merger waves in the 1980s (Karpoff and Wittry, 2016). Although the statutes' application and implications were not limited to takeovers, one could argue that the constituency statutes might have been used as takeover defenses. Indeed, our finding of reduced bank risk after statute passage is somewhat consistent with an alternative explanation that following a reduction in takeover threat, bank managers may pursue a "quiet life" and avoid the difficult decisions and costly efforts associated with risk-taking (Bertrand and Mullainathan, 2003). However, existing empirical evidence suggests that this alternative explanation is unlikely to be valid. For instance, contrary to the view that constituency statutes reduce takeover threat, Gao, Li and Ma (2016) document that the passage of constituency statutes has little effect on the acquisition likelihood of non-financial firms. To test this alternative explanation, we perform two additional tests.

First, we divide the statutes according to whether they allow the considerations of stakeholder interests in *any* instance of business decision making as opposed to *only* change-of-control situations. If the statutes were primarily used as takeover defenses, one would not expect the statute effects to vary with their scope of application. In total, 11 of the 35 statutes permit the considerations of stakeholder interests in *only* change-of-control situations (see Table IA.1 of the Internet Appendix), whereas the remaining 24 statutes allow such considerations in *any* instance of business decisions.²⁶ In Table 11, Panel A shows that the reduction in bank risk concentrates

²⁶ We collect this information from Oswald (1998, p.5, see footnote 25) and then manually go through each statute for verification.

on those statutes that allow stakeholder interests to be considered in a *wider* range of business decision making, inconsistent with statutes being used solely as takeover defenses.

Insert Table 11 about here

Second, we follow Gao, Li and Ma (2016) and empirically test whether the enactment of constituency statutes affects the BHCs' likelihood of being acquired. We perform the analysis at the state level (1,149 state-year observations). Our first measure of acquisition likelihood is the total number of BHCs acquired in a state of incorporation.²⁷ Our second measure is the total number of BHCs acquired in a state of incorporation normalized by the total number of BHCs incorporated in the same state. State-averaged bank control variables, state controls, state antitakeover laws, state banking deregulation policies, state and region-year fixed effects are included in the regressions whereas standard errors are clustered at the state level. As shown in Panel B, the coefficients for *Constituency Statutes* are small and insignificant. This indicates that the enactment of constituency statutes has little effect on the BHCs' acquisition likelihood and thus the threat of takeover, which is inconsistent with the alternative explanation.

4.6. *Constituency Statutes and Bank Performance*

Thus far, we have shown that after the enactment of constituency statutes, banks reduce their risk-taking by adopting less risky capital structures and shifting their lending from riskier to safer borrowers. This section examines the value implications of the reduced risk-taking for the BHCs.

The effect of constituency statutes on bank performance is somewhat ambiguous. For instance, on the one hand, the passage of constituency statutes significantly enhances bank loan quality. The associated reduction in loan losses may add to bank profitability. However, on the other hand, the lower interest margins owing to the banks' lending to safer borrowers may hurt profitability and performance. Therefore, the overall effect of constituency statutes on bank performance may depend on the relative significance of the two effects aforementioned, which is therefore ultimately an empirical question to be addressed.

²⁷ The BHC mergers are collected from the Thomson One Banker. Our final merger sample is established based on the following criteria: (1) the target ultimate parent firms are public and have 3-digit SIC codes: 602 or 671; (2) deals are removed if they are classified as repurchases, liquidations, restructurings, divestitures, leverage buyouts, reserve takeovers, privatizations, bankruptcy acquisitions or going private transactions; (3) the company identifier, PERMCO, could be obtained from the CRSP/COMPUSTAT merged dataset. The final sample consists of 656 BHC mergers over the period from 1986 to 2012.

To test this hypothesis, we estimate the difference-in-differences regression of equation (3) with return on assets (*ROA*), bank stock annual returns (*Annual returns*) and log market-to-book equity ratio ($\ln(\text{Market-to-book equity ratio})$) as dependent variables. *Annual returns* is the buy-and-hold return on the BHC stock over a calendar year. In the performance regressions, we include the same set of bank and state control variables (except *ROA* and *Market-to-book equity ratios*) and fixed effects as in the baseline model. The market beta (*Market beta*) estimated from equation (1) is included to control for the bank stocks' exposure to systematic risk. We also control for the state antitakeover laws and banking deregulation policy changes to ensure that our results are not driven by these confounding state laws. Standard errors are clustered at the state of incorporation level. The results are reported in Table 12.

Insert Table 12 about here

The positive but statistically insignificant coefficient for *Constituency Statute* in column (1) indicates that there are little changes in bank profitability after the enactment of constituency statutes. In column (3), where *ROA* is replaced with *Annual returns*, we continue to find an insignificant coefficient for *Constituency Statute*. Finally, column (5) shows very similar results in that we find no significant statute effect on bank market-to-book equity ratio. These results show that the overall effect of stakeholder orientation on bank performance is rather small and insignificant.

We identify a setting in which the marginal benefits of reducing risk-taking are likely to exceed its marginal costs. In theory, banks with severe moral hazard problems have greater incentives to invest in excessively risky and inefficient assets that are high-risk-low-return. Such inefficiency likely makes a shift from riskier to safer borrowers more desirable because the gain from mitigating loan losses is likely to outweigh the reduction in loan interest income. By contrast, for banks characterized by safer borrowers, such a shift would be less appealing because of the lower marginal benefit from reducing loan losses. Therefore, we hypothesize that the enactment of constituency statutes significantly improves bank performance only for banks that take on excessive risk but may not affect or may even reduce performance for banks that do not.

To test this hypothesis, we construct a dummy variable, *High risk*, which equals one if a bank's *Total risk* is above the size-adjusted average *Total risk* and zero otherwise. To adjust for size, we annually sort the BHCs into quintile portfolios based on bank size and compute the

average portfolio riskiness. We posit that a *High risk* bank is more likely to engage in excessive risk-taking and would benefit more from a shift to safer borrowers. We augment the bank performance models by including the interaction between *Constituency Statute* and *High risk*.

In column (2), where *ROA* is the dependent variable, we find that the coefficient for *Constituency Statute*×*High risk* is positive and significant at the 5% level. This finding is consistent with the view that the enactment of constituency statute improves bank profitability only for banks that likely engage in excessive risk-taking. Economically, for *High risk* banks, enacting the constituency statute increases their *ROA* by 0.18 percentage points, corresponding to a 16.4% increase relative to the sample mean or a \$31.9 million increase in earnings (mean total assets is \$17.7 billion). As expected, the statute effect is insignificant for the low-risk banks.

In column (4) where *Annual returns* is the dependent variable, we again find that the coefficient for *Constituency Statute*×*High risk* is positive and statistically significant (at the 1% level). For *High risk* banks, the enactment of constituency statute increases their annual stock returns by 0.6 percentage points or 4.3% relative to the sample mean, whereas the statute effect is insignificant for the low-risk banks.

Column (6) shows very similar results for *Ln(Market-to-book equity ratio)* in that the coefficient for *Constituency Statute*×*High risk* is again significantly positive at the 5% level. For *High-risk* banks, enacting the statute increases market-to-book equity ratio by 4.2% relative to the sample mean.²⁸ Similarly, we find insignificant statute effects on bank market to book equity ratio for the low-risk banks.

Overall, the effect of stakeholder orientation on bank performance is small and insignificant on average. More importantly, we show that stakeholder orientation is value-enhancing only for banks that likely engage in excessive and inefficient risk-taking but not for banks that do not.

4.7. *Constituency Statutes and Crisis Performance*

Our results thus far show that the enactment of constituency statutes significantly reduces bank risk-taking because it induces banks to adopt less risky bank capital structures and lend to less risky borrowers. The previous section further shows that statute passage improves bank

²⁸ This is calculated as: $Exp(0.041)-1=0.0419$ or 4.2%.

performance only for banks that likely engage in excessive risk-taking. In this section, we explore the long-term value implications of stakeholder orientation by testing whether the reduced risk-taking translates into better performance during the subsequent financial crises.

Recent studies document that a bank's "risk culture" is important for determining its crisis performance. For instance, Fahlenbrach, Prilmeier and Stulz (2012) document that bank underperformance during the 1998 crisis predicts lower bank performance during the 2007-08 crisis, consistent with risk culture being persistent and making banks sensitive to crises. Ellul and Yerramilli (2013) also find that banks with more tail risk during the 1998 crisis continued to have poorer risk control, consistent with their risk culture being fairly rigid. To the extent that the constituency statutes have influenced the BHCs' risk culture in favor of stakeholders and stability, we hypothesize that BHCs that have previously received a statute passage incur smaller losses during the financial crises relative to control BHCs.

We examine bank stock performance during both the 1998 crisis and the 2007-08 crisis. Our sample for the 1998 crisis begins with all available BHCs (378 BHCs) over 1997-98. We include all BHCs that have been treated before 1998 (88 BHCs) as the treatment group. Similarly, for the 2007-08 crisis, we begin with all available BHCs (304 BHCs) over 2006-09 of which 42 of them have been treated before 2007. We then match each treated BHC with a control BHC that is incorporated in a state that has not passed or does not have a constituency statute and is closest in size before the crisis. We also require the control BHCs to be located in a bordering state of the treated BHC to increase the likelihood that the treated and control BHCs experience similar economic conditions. Following Fahlenbrach, Prilmeier and Stulz (2012), we define three measures of 1998 crisis returns as the buy-and-hold bank stock returns from 3rd August 1998 to the date on which it attains the lowest stock price ($Crisis_{1998} RET_1$), to 30th September 1998 ($Crisis_{1998} RET_2$), and to 30th October 1998 ($Crisis_{1998} RET_3$). For the 2007-08 crisis, we also define three crisis performance measures as the buy-and-hold bank stock returns from 1st July 2007 to the date on which a bank attains its lowest price ($Crisis_{07-08} RET_1$), to 31st December 2008 ($Crisis_{07-08} RET_2$), and to 31st December 2009 ($Crisis_{07-08} RET_3$).²⁹ We estimate the following regression model for each of the two crises:

²⁹ If a bank was delisted or merged during 1997-98 or 2007-08, we put the proceeds into a daily bank index until the end of 1998 or 2009, respectively, to avoid potential survivorship bias. The daily bank index is collected from French's data library under the 49-industry classification. Our results hold if we instead put the proceeds in a cash account.

$$\Delta RET_{isl} = \alpha + \beta \times Previously\ Treated_s + \delta X_{isl} + \gamma W_l + \varepsilon_{isl}. \quad (5)$$

where i is a bank, s is the state of incorporation and l is the state of location. ΔRET_{isl} is the changes in bank stock returns calculated as the crisis returns (*Crisis RET*) minus the pre-crisis bank stock returns (*Annual returns*). *Previously Treated_s* is a treatment dummy equals one for BHCs that have been treated prior to the crisis and zero otherwise. X_{isl} and W_l are vectors of pre-crisis bank and state controls, respectively, augmented by the pre-crisis market beta, the three state antitakeover laws, *RS index* and *Intra*.³⁰ White heteroscedasticity-robust standard errors are reported.³¹ β is a difference-in-differences estimate capturing the differences in the Crisis-minus-Pre-crisis bank stock returns between the treatment and control groups.

Insert Table 13 about here

In Table 13, Panel A compares the pre-crisis bank and state characteristics between the treatment and control groups for both crises. All bank and state characteristics are insignificantly different between the two groups except for non-interest income and state population for the 2007-08 crisis, suggesting that the matching is satisfactory in eliminating the differences in observables between the two groups and that the parallel trend assumption is likely satisfied (Robert and Whited, 2012).

Panel B presents the estimates for the Crisis-minus-Pre-crisis differences and difference-in-differences of the bank stock returns. For the 1998 (2007-08) crisis, the after-before differences in bank stock returns range from -76.8 to -91.9 (-36.0 to -58.0) percentage points for the treated BHCs and from -88.8 to 105.3 (-61.7 to -79.1) percentage points for the control BHCs. These after-before differences are all statistically significant at the 1% level, consistent with the stylized fact that banking firms suffered huge losses during both crises. The difference-in-differences (treatment-control) estimates range from 12.0 to 13.3 percentage points for the 1998 crisis and from 21.1 to 25.8 percentage points for the 2007-08 crisis, all of which are significant at the 5% level, revealing that the treated BHCs fared significantly better than the matched BHCs during both crises.

³⁰ We do not control for state interstate deregulation because all BHCs are located in deregulated states. Market beta is estimated using daily bank stock returns data using equation (1) and controls for a bank's market risk exposure.

³¹ The results are qualitatively similar when we instead cluster the standard errors at the bank level.

Panel C reports the difference-in-differences estimates after we control for the pre-crisis bank and state control variables. The difference-in-differences estimates range from 6.5 to 9.7 percentage points for the 1998 crisis (significant at the 10% level or better for *Crisis RET₁* and *Crisis RET₃*) and from 13.8 to 33.8 percentage points for the 2007-08 crisis (all three crisis performance measures are significant at the 1% level).

Overall, our results show that the reduced risk-taking due to the statute passage translates into significantly smaller losses during the subsequent crises, lending direct support to the view that stakeholder orientation enhances financial stability.

5. Conclusion

The 2007-09 financial crisis has raised widespread concern about whether the traditional shareholder primacy view in bank governance model is detrimental to financial stability. Theory suggests that induced by deposit insurance and due to limited liability, bank shareholders and managers have incentives to take excessive risk, which poses threat to the banking system (Jensen and Meckling, 1976; Merton, 1977; see Thakor, 2014, for a review). To reduce this negative externality, in the current banking regulatory and governance reforms, practitioners and scholars have advocated for a more stakeholder-oriented approach in bank governance and management (Laeven, 2013). To our best knowledge, our paper is the first to examine whether stakeholder orientation reduces bank risk-taking and enhances financial stability.

Our paper exploits the plausibly exogenous variation in stakeholder orientation arising from the staggered enactment of state constituency statutes, which expand corporate directors' fiduciary duties to consider stakeholder and long-term interests, and sets up a difference-in-differences model for identification (Bertrand and Mullainathan, 2003). We find a negative and significant causal effect of stakeholder orientation on bank risk. This relationship is robust to reverse causality and to the inclusion of controls for state antitakeover laws, banking policy changes and unobserved local economic conditions. We then explore the channels behind these results and find that after statute passage banks reduce risk-taking by increasing capital levels and shifting lending to safer borrowers. Further, we examine the value implications of stakeholder orientation and find that the effect of statute passage on bank performance is small and insignificant on average, but is significantly positive only for banks that take excessive risk. Finally, we explore the longer-term value implications of stakeholder orientation by examining

bank crisis performance and find that banks that previously received a statute passage fared significantly better during the financial crises than the size-and-location-matched control banks.

These results have important policy implications. First, we show consistent evidence that bank stakeholder orientation enhances financial stability, thus providing strong empirical support to the increasing call for a greater emphasis on stakeholder value in the current banking regulatory and governance reforms (Macey and O'Hara, 2003, 2016; Becht, Bolton and Röell, 2011; Laeven, 2013). Specifically, our paper addresses an important debate in the current bank governance reforms about whether bank directors' fiduciary duties should owe exclusively to shareholders. We show that banks with directors whose duties are expanded to consider stakeholder and long-term interests reduce risk-taking through altering their capital structures and lending activities, thus lending support to the view that bank directors' legal duties should be broadened for financial stability considerations. Moreover, our findings highlight the significant influence of bank directors on bank strategic decision making, implying that the imposition of additional requirements or responsibilities on bank directors, such as requiring specialized expertise in bank risk control (Macey and O'Hara, 2016), will be essential in limiting the risk of potential future systemic instability.

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TABLE 1
The Enactment of Constituency Statutes

This table shows the staggered enactment of constituency statutes across US states over time and the number of treated BHCs for each statute. The total number of treated BHCs is 166 in 28 states.

State	Year	Number of treated BHCs
Ohio	1984	
Illinois	1985	
Maine	1986	
Arizona	1987	1
Minnesota	1987	1
New Mexico	1987	1
New York	1987	11
Wisconsin	1987	3
Idaho	1988	1
Louisiana	1988	3
Tennessee	1988	4
Virginia	1988	9
Florida	1989	5
Georgia	1989	7
Hawaii	1989	1
Indiana	1989	7
Iowa	1989	4
Kentucky	1989	5
Massachusetts	1989	7
Missouri	1989	5
New Jersey	1989	20
Oregon	1989	2
Mississippi	1990	4
Pennsylvania	1990	23
Rhode Island	1990	2
South Dakota	1990	
Wyoming	1990	
Nevada	1991	1
North Carolina	1993	11
North Dakota	1993	
Connecticut	1997	5
Vermont	1998	1
Maryland	1999	12
Texas	2006	10
Nebraska	2007	
Total	35 states	166 BHCs incorporated in 28 states

TABLE 2
Summary Statistics

This table presents the summary statistics. Our sample consists of 939 (9,248 bank-year observations) publicly traded US BHCs that filed the FR Y-9C reports with the Federal Reserve over 1986-2012. Bank fundamental information is obtained from the Bank Regulatory Database. Bank stock information is downloaded from CRSP. Other accounting information and firm attributes are downloaded from Compustat. The state GDP and population data are downloaded from the US Bureau of Economic Analysis (BEA). To reduce the effects of outliers, we winsorize all continuous variables at the 1st and 99th percentiles. The detailed definitions of the bank and state variables are provided in Appendix A.1.

Variable	Obs.	Mean	Std. Dev.	Min	25%	Median	75%	Max
<i>Total risk</i>	9,248	0.409	0.239	0.129	0.260	0.343	0.471	1.558
<i>IVol</i>	9,248	0.382	0.231	0.115	0.235	0.319	0.447	1.514
<i>Z-score</i>	9,248	0.298	0.165	-0.002	0.186	0.273	0.377	0.958
<i>NPL/TA</i>	7,495	0.0129	0.0157	0.0000	0.0027	0.0074	0.0165	0.0877
<i>Deflated total assets (in mil.)</i>	9,248	17,707	110,729	111	620	1,412	4,600	2,069,691
<i>ROA</i>	9,248	0.011	0.012	-0.043	0.008	0.013	0.018	0.032
<i>Non-interest income/TA</i>	9,248	0.012	0.010	0.001	0.006	0.010	0.014	0.063
<i>Net interest income/TA</i>	9,248	0.088	0.020	0.030	0.076	0.088	0.099	0.143
<i>Non-core deposits/TA</i>	9,248	0.126	0.082	0.016	0.067	0.106	0.161	0.435
<i>Loans (in mil.)</i>	9,248	8,527	50,200	17	369	836	2,531	993,000
<i>Loans/TA</i>	9,248	0.649	0.119	0.250	0.586	0.661	0.726	0.875
<i>Market-to-book equity ratio</i>	9,248	1.480	0.743	0.213	0.968	1.367	1.873	4.091
<i>FREQ</i>	9,248	0.002	0.004	0.000	0.001	0.001	0.003	0.120
<i>Capital/TA</i>	9,248	0.089	0.024	0.033	0.073	0.086	0.101	0.183
<i>Capital/TL</i>	9,248	0.143	0.055	0.050	0.110	0.133	0.163	0.412
<i>Market beta</i>	9,248	0.524	0.554	-0.494	0.104	0.364	0.863	2.115
<i>Annual returns</i>	9,203	0.141	0.375	-0.756	-0.089	0.112	0.341	1.364
<i>State GDP growth</i>	9,248	0.028	0.027	-0.284	0.013	0.026	0.043	0.159
<i>Ln(State population)</i>	9,248	15.861	0.874	13.188	15.396	15.901	16.336	17.455

TABLE 3
Constituency Statutes and Bank Risk-Taking

This table examines the effect of constituency statutes on bank risk using the difference-in-differences model of equation (3) that exploits the staggered enactment of constituency statutes across US states. The dependent variables are bank total risk (*Total risk*), idiosyncratic risk (*IVol*) and Z-score (*Z-score*). The main explanatory variable of interest is *Constituency Statute*, which is a treatment dummy variable taking on a value of one when a constituency statute is enacted in a state where a BHC is incorporated, and a value of zero otherwise. All other bank and state control variables are defined in Appendix A.1. Standard errors reported in parentheses are clustered at the state of incorporation level. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

	<i>Total risk</i>			<i>IVol</i>			<i>Z-score</i>		
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
<i>Constituency Statute</i>	-0.027** (0.010)	-0.028*** (0.010)	-0.027** (0.011)	-0.029*** (0.010)	-0.030*** (0.010)	-0.030*** (0.011)	0.037*** (0.009)	0.037*** (0.009)	0.046*** (0.007)
<i>Ln(TA)</i>	-0.049*** (0.009)	-0.051*** (0.009)	-0.053*** (0.010)	-0.058*** (0.009)	-0.060*** (0.009)	-0.062*** (0.010)	0.032*** (0.007)	0.031*** (0.007)	0.030*** (0.008)
<i>ROA</i>	-6.408*** (0.380)	-6.378*** (0.379)	-6.304*** (0.350)	-6.380*** (0.385)	-6.359*** (0.381)	-6.304*** (0.352)	4.409*** (0.212)	4.398*** (0.214)	4.467*** (0.182)
<i>Non-interest income/TA</i>	3.566*** (0.683)	3.555*** (0.675)	3.440*** (0.651)	3.203*** (0.648)	3.197*** (0.639)	3.117*** (0.601)	-0.072 (0.392)	-0.066 (0.393)	-0.003 (0.389)
<i>Non-core deposits/TA</i>	0.063 (0.047)	0.063 (0.046)	0.062 (0.047)	0.098** (0.044)	0.099** (0.044)	0.099** (0.045)	-0.151** (0.058)	-0.150** (0.058)	-0.147*** (0.051)
<i>Loans/TA</i>	-0.017 (0.051)	-0.020 (0.051)	-0.050 (0.045)	-0.023 (0.050)	-0.025 (0.050)	-0.051 (0.045)	0.056 (0.036)	0.055 (0.036)	0.071** (0.035)
<i>Ln(Market-to-book equity ratio)</i>	-0.076*** (0.011)	-0.075*** (0.011)	-0.070*** (0.010)	-0.084*** (0.010)	-0.083*** (0.010)	-0.079*** (0.010)	-0.016* (0.009)	-0.016* (0.008)	-0.018** (0.008)
<i>FREQ</i>	7.812*** (0.977)	7.770*** (0.998)	7.500*** (1.018)	5.094*** (0.853)	5.046*** (0.869)	4.797*** (0.881)	-0.531 (0.497)	-0.551 (0.500)	-0.396 (0.469)
<i>State GDP growth</i>	—	-0.157** (0.071)	-0.216** (0.086)	—	-0.117 (0.073)	-0.178** (0.087)	—	0.038 (0.098)	0.059 (0.097)
<i>Ln(State population)</i>	—	0.054*** (0.017)	0.071*** (0.026)	—	0.055*** (0.019)	0.068** (0.028)	—	0.014 (0.011)	-0.008 (0.013)
<i>Intercept</i>	0.726*** (0.081)	-0.097 (0.261)	-0.346 (0.380)	0.802*** (0.078)	-0.044 (0.288)	-0.224 (0.420)	-0.002 (0.045)	-0.227 (0.170)	0.147 (0.213)
Bank FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Region×Year FE			Yes			Yes			Yes
Obs.	9,248	9,248	9,248	9,248	9,248	9,248	9,248	9,248	9,248
Adj. R ²	0.596	0.596	0.605	0.548	0.549	0.558	0.406	0.406	0.417

TABLE 4
Robustness Tests

This table presents our robustness tests. The dependent variables are bank total risk (*Total risk*), idiosyncratic risk (*IVol*) and Z-score (*Z-score*). For brevity, we only report the estimated coefficients and cluster-robust (at the state of incorporation level, if not stated otherwise) standard errors of *Constituency Statute*, which is a treatment dummy variable taking on a value of one when a constituency statute is enacted in a state where a BHC is incorporated, and a value of zero otherwise. The bank and state control variables and fixed effects are identical to those used in columns (3), (6) and (9) of Table 3. Row (1) clusters the standard errors at the bank level. Row (2) adjusts for serial correlation in the error terms using the two-step procedure of Bertrand, Duflo and Mullainathan (2004). Row (3) controls for the state of incorporation fixed effects. Row (4) reports the results of weighted least squares (WLS) regressions with weights calculated as the inverse of the number of bank-year observations in each state of incorporation. Row (5) excludes states without statute enactment (excluded 16 states, down to 5,696 observations). Row (6) excludes BHCs that are incorporated in Delaware (down to 7,273 observations). Row (7) estimates the baseline models with no control variables, i.e., only region-year and bank fixed effects. Rows (8) to (14) control for the interaction between the bank controls and the year dummies in the regressions. Rows (15) and (16) restrict the sample to end in 1995 and 2005, respectively. Row (17) controls for banking competition, as measured by the concentration of loans within the states of location. Row (18) excludes 7 states in which there are discrepancies from legal studies about the enactment year of the constituency statutes. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

		Dependent variables:					
		<i>Total risk</i>		<i>IVol</i>		<i>Z-score</i>	
		<i>Coef.</i>	<i>S.E</i>	<i>Coef.</i>	<i>S.E</i>	<i>Coef.</i>	<i>S.E</i>
(1)	Clustered at the state of incorporation level	-0.027**	(0.014)	-0.030**	(0.013)	0.046***	(0.009)
(2)	Serial correlation in the error terms	-0.015*	(0.008)	-0.015**	(0.007)	0.020***	(0.006)
(3)	State of incorporation FE	-0.027	(0.016)	-0.032**	(0.015)	0.030***	(0.008)
(4)	Weighted Least Squares (WLS) regressions	-0.038**	(0.017)	-0.037**	(0.017)	0.051***	(0.011)
(5)	Exclude states without statute enactment (5,696 obs.)	-0.017	(0.011)	-0.022**	(0.010)	0.042***	(0.012)
(6)	Exclude DE-incorporated BHCs (7,273 obs.)	-0.018	(0.012)	-0.021*	(0.011)	0.048***	(0.010)
(7)	Only fixed effects and no control variables	-0.032**	(0.013)	-0.038***	(0.014)	0.052***	(0.009)
(8)	Control for $\ln(TA) \times Year$	-0.021**	(0.010)	-0.025**	(0.010)	0.044***	(0.007)
(9)	Control for $ROA \times Year$	-0.021**	(0.011)	-0.024**	(0.011)	0.046***	(0.007)
(10)	Control for $Non-interest\ income/TA \times Year$	-0.030***	(0.010)	-0.033***	(0.010)	0.046***	(0.007)
(11)	Control for $Non-core\ deposits/TA \times Year$	-0.029**	(0.012)	-0.032***	(0.011)	0.049***	(0.007)
(12)	Control for $Loans/TA \times Year$	-0.024**	(0.011)	-0.027**	(0.011)	0.045***	(0.007)
(13)	Control for $\ln(Market-to-book\ equity\ ratio) \times Year$	-0.021*	(0.011)	-0.024**	(0.011)	0.040***	(0.008)
(14)	Control for $FREQ \times Year$	-0.025**	(0.011)	-0.028**	(0.011)	0.046***	(0.007)
(15)	Time window up to 1995 (3,058 obs.)	-0.037***	(0.013)	-0.039***	(0.013)	0.040***	(0.010)
(16)	Time window up to 2005 (7,025 obs.)	-0.033**	(0.012)	-0.035***	(0.013)	0.041***	(0.008)
(17)	Control for $H-index$ and $H-index^2$ (state of location)	-0.028**	(0.011)	-0.031***	(0.011)	0.046***	(0.007)
(18)	Exclude 7 states with discrepancies in the enactment years of constituency statutes (8,200 obs.)	-0.032**	(0.013)	-0.033**	(0.013)	0.046***	(0.008)

TABLE 5
Dynamic Treatment Models

This table examines the dynamic treatment effects of constituency statutes on bank risk. We regress our bank risk measures (*Total risk*, *IVol* and *Z-score*) on four indicator variables—*Before*^{-2 or -1}, *Current*⁰, *After*⁺¹, and *After*^{>=+2}—to examine *when* the statute effects have occurred. *Before*^{-2 or -1}_{st} is a dummy equal to one if it is one or two years prior to the statute enactment, *Current*⁰_{st} is a dummy equal to one if it is the year of statute enactment, *After*⁺¹_{st} is a dummy equal to one if it is one year after the statute enactment, and *After*^{>=+2}_{st} is dummy equal to one if it is two or more years after the statute enactment. We include the same bank and state controls and fixed effects as in the baseline model and cluster standard errors at the state of incorporation level. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

	<i>Total risk</i>	<i>IVol</i>	<i>Z-score</i>
	(1)	(2)	(3)
<i>Before</i> ^{-2 or -1}	-0.008 (0.007)	-0.011 (0.007)	0.014 (0.012)
<i>Current</i> ⁰	-0.022 (0.015)	-0.028* (0.015)	0.040*** (0.012)
<i>After</i> ⁺¹	-0.026* (0.017)	-0.031* (0.017)	0.043*** (0.015)
<i>After</i> ^{>=+2}	-0.037** (0.014)	-0.042*** (0.014)	0.063*** (0.013)
<i>Ln(TA)</i>	-0.053*** (0.010)	-0.062*** (0.010)	0.030*** (0.008)
<i>ROA</i>	-6.307*** (0.347)	-6.307*** (0.350)	4.472*** (0.181)
<i>Non-interest income/TA</i>	3.441*** (0.651)	3.117*** (0.600)	-0.004 (0.388)
<i>Non-core deposits/TA</i>	0.061 (0.047)	0.097** (0.045)	-0.146*** (0.052)
<i>Loans/TA</i>	-0.049 (0.045)	-0.049 (0.045)	0.069* (0.035)
<i>Ln(Market-to-book equity ratio)</i>	-0.070*** (0.010)	-0.079*** (0.010)	-0.018** (0.008)
<i>FREQ</i>	7.509*** (1.021)	4.807*** (0.884)	-0.411 (0.470)
<i>State GDP growth</i>	-0.213** (0.087)	-0.174* (0.087)	0.054 (0.096)
<i>Ln(State population)</i>	0.073*** (0.026)	0.070** (0.028)	-0.011 (0.012)
<i>Intercept</i>	-0.376 (0.377)	-0.259 (0.417)	0.199 (0.194)
Bank FE	Yes	Yes	Yes
Region×Year FE	Yes	Yes	Yes
Obs.	9,248	9,248	9,248
Adj.R ²	0.605	0.558	0.417

TABLE 6
Controlling for Unobserved Local Economic Conditions

This table examines whether unobserved changes in local economic conditions are driving our results. We match each treated BHC with a control BHC that is located in a bordering state without statute enactment and closest in bank size (pre-treatment). For each matched pair of BHCs, we include the bank-years before and after the statute enactment to construct a matched sample. To increase the likelihood that the treated and control BHCs share similar local economic conditions, we first remove all matched pairs with distance more than 500 miles. We also restrict the distance between the treated and control BHCs to lie within 250 miles and 125 miles, which correspond to the 75th and 50th percentiles distance of the matched sample, respectively. The matching diagnostics are provided in Table IA.5 of the Internet Appendix. On each distance-restricted subsample, we estimate the difference-in-differences regression of equation (3). The dependent variables include bank total risk (*Total risk*), idiosyncratic risk (*IVol*) and Z-score (*Z-score*). The main explanatory variable of interest is *Constituency Statute*, which is a treatment dummy variable taking on a value of one when a constituency statute is enacted in a state where a BHC is incorporated, and a value of zero otherwise. The bank and state controls and fixed effects are identical to those used in the baseline model. Standard errors reported in parentheses are clustered at the state of incorporation level. We only report the estimates for *Constituency Statute* for brevity. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

Panel A: Within 500 miles

	<i>Total risk</i>	<i>IVol</i>	<i>Z-score</i>
	(1)	(2)	(3)
<i>Constituency Statute</i>	-0.084*** (0.024)	-0.079*** (0.024)	0.063** (0.025)
Bank controls	Yes	Yes	Yes
State controls	Yes	Yes	Yes
Bank FE	Yes	Yes	Yes
Region×Year FE	Yes	Yes	Yes
Obs.	520	520	520
Adj. R ²	0.718	0.713	0.367

Panel B: Within 250 miles

	<i>Total risk</i>	<i>IVol</i>	<i>Z-score</i>
	(1)	(2)	(3)
<i>Constituency Statute</i>	-0.079** (0.030)	-0.073** (0.029)	0.057* (0.030)
Bank controls	Yes	Yes	Yes
State controls	Yes	Yes	Yes
Bank FE	Yes	Yes	Yes
Region×Year FE	Yes	Yes	Yes
Obs.	396	396	396
Adj. R ²	0.730	0.727	0.413

Panel C: Within 125 miles

	<i>Total risk</i>	<i>IVol</i>	<i>Z-score</i>
	(1)	(2)	(3)
<i>Constituency Statute</i>	-0.110*** (0.037)	-0.101** (0.037)	0.049 (0.034)
Bank controls	Yes	Yes	Yes
State controls	Yes	Yes	Yes
Bank FE	Yes	Yes	Yes
Region×Year FE	Yes	Yes	Yes
Obs.	176	176	176
Adj. R ²	0.777	0.776	0.481

TABLE 7
Coincidental State Antitakeover Laws

Panel A of this table reports the number of treated BHCs and the years of changes in constituency statutes and three state antitakeover laws, namely the control share acquisition laws, business combination laws and fair price laws. The details for the state antitakeover laws are collected from Bertrand and Mullainathan (2003). *Control share acquisition law* is an indicator variable equal one after the enactment of the control share acquisition laws, and zero otherwise. *Business combination law* is an indicator variable equal one after the enactment of the business combination laws, and zero otherwise. *Fair price law* is an indicator variable equal one after the enactment of the fair price laws, and zero otherwise. We highlight in grey shading 16 “contaminated” states in which the enactment of constituency statutes is either in the one year before, during the year of, or in the one year after an enactment of any one of the three major state antitakeover laws, affecting 66 BHCs in total. In Panel B, we exclude the BHCs that are incorporated in these contaminated states and re-estimate the baseline bank risk models. In Panel C, we jointly control for the three state antitakeover laws in the baseline bank risk models. The regressions in Panels B and C include the same bank and state controls and fixed effects as in the baseline model and cluster standard errors at the state of incorporation level. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

Panel A: Comparing constituency statutes with other anti-takeover laws

State	No. of affected BHCs	Constituency statutes	Control share acquisition laws	Business combination laws	Fair price laws
Ohio		1984	1982	1990	1990
Illinois		1985	—	1989	1985
Maine		1986	—	1988	—
Arizona	1	1987	1987	1987	1987
Minnesota	1	1987	1984	1987	1991
New Mexico	1	1987	—	—	—
New York	11	1987	—	1985	1985
Wisconsin	3	1987	1984	1987	1984
Idaho	1	1988	1988	1988	1988
Louisiana	3	1988	1987	—	1984
Tennessee	4	1988	1988	1988	1988
Virginia	9	1988	1989	1988	1985
Florida	5	1989	1987	—	1987
Georgia	7	1989	—	1988	1985
Hawaii	1	1989	1985	—	—
Indiana	7	1989	1986	1986	1986

Iowa	4	1989	—	1997	—
Kentucky	5	1989	—	1986	1984
Massachusetts	7	1989	1987	1989	—
Missouri	5	1989	1984	1986	1986
New Jersey	20	1989	—	1986	1986
Oregon	2	1989	1987	1991	—
Mississippi	4	1990	1990	—	1985
Pennsylvania	23	1990	1990	1988	1988
Rhode Island	2	1990	—	1990	1990
South Dakota		1990	1990	1990	1990
Wyoming		1990	1990	1989	—
Nevada	1	1991	1987	1991	1991
North Carolina	11	1993	1987	—	1987
North Dakota		1993	—	—	—
Connecticut	5	1997	—	1988	1984
Vermont	1	1998	—	—	—
Maryland	12	1999	1989	1989	1983
Texas	10	2006	—	1997	—
Nebraska		2007	1988	1988	—

Panel B: Excluding states with coincidental state antitakeover laws (2,452 observations excluded; 66 treated BHCs removed)

	<i>Total risk</i>	<i>IVol</i>	<i>Z-score</i>
	(1)	(2)	(3)
<i>Constituency Statutes</i>	-0.022*	-0.026*	0.052***
	(0.013)	(0.013)	(0.013)
Bank controls	Yes	Yes	Yes
State controls	Yes	Yes	Yes
Bank FE	Yes	Yes	Yes
Region×Year FE	Yes	Yes	Yes
Obs.	6,796	6,796	6,796
Adj. R ²	0.619	0.571	0.413

Panel C: Controlling for the coincidental state antitakeover laws

	<i>Total risk</i>	<i>IVol</i>	<i>Z-score</i>
	(1)	(2)	(3)
<i>Constituency Statutes</i>	-0.030*** (0.011)	-0.033*** (0.011)	0.045*** (0.008)
<i>Control share acquisition law</i>	0.013 (0.015)	0.010 (0.016)	0.018 (0.014)
<i>Business combination law</i>	-0.007 (0.013)	-0.003 (0.014)	0.025 (0.015)
<i>Fair price law</i>	0.019 (0.018)	0.017 (0.019)	-0.046 (0.035)
Bank controls	Yes	Yes	Yes
State controls	Yes	Yes	Yes
Bank FE	Yes	Yes	Yes
Region×Year FE	Yes	Yes	Yes
Obs.	9,248	9,248	9,248
Adj. R ²	0.605	0.558	0.418

TABLE 8
Coincidental Banking Policy Changes

Panel A of this table reports the number of treated BHCs and the years of changes in constituency statutes, the interstate and intrastate banking deregulation policies, and the erection of out-of-state entry barriers for interstate branching activities (the Rice and Strahan index). The details for the interstate deregulation are collected from Amore, Schneider and Žaldokas (2013); the details for intrastate deregulation are collected from Jayaratne and Strahan (1996); and the details for the out-of-state entry barriers for interstate branching activities are collected from Rice and Strahan (2010). Following Cornaggia, Mao, Tian and Wolfe (2015), we construct two indicator variables, *Inter* and *Intra*, which equal zero before the interstate and intrastate banking deregulations, and one otherwise. The Rice and Strahan index (*RS index*) has four components. We add one to *RS index* if a state has any one of the following provisions, (i) the minimum age of the target institution, (ii) de novo interstate branching, (iii) the acquisition of individual branches, and (iv) a state-wide deposit cap. The last four columns show the years in which the state has put a provision in place. For some states, we use ↑ and ↓ to denote an addition and removal of an entry barrier, respectively. We highlight in grey shading 10 states in which the enactment of constituency statutes is either in the one year before, during the year of, or in the one year after a banking deregulation policy change, affecting 30 treated BHCs in total. In Panel B, we exclude the BHCs that are incorporated and headquartered in these states and re-estimate the baseline bank risk models. In Panel C, we jointly control for *Inter*, *Intra* and *RS index* in the baseline bank risk models. The regressions in Panels B and C include the same bank and state controls and fixed effects as in the baseline model and cluster standard errors at the state of incorporation level. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

Panel A: Comparing the constituency statutes with other banking deregulation policy changes

State	No. of treated BHCs	Constituency statutes	Interstate deregulation	Intrastate deregulation	<i>RS index</i>			
					(i) Min. of age of institution	(ii) Allows de novo interstate branching	(iii) Interstate branching with acquisitions	(iv) Statewide deposits
Ohio		1984	1985	1979	—	—	—	—
Illinois		1985	1986	1988	↑1997; ↓2004	↑1997; ↓2004	↑1997; ↓2004	—
Maine		1986	1978	1975	—	—	—	—
Arizona	1	1987	1986	1972	1996	1996	↑1996; ↓2001	—
Minnesota	1	1987	1986	—	1997	1997	1997	—
New Mexico	1	1987	1989	1991	1996	1996	1996	—
New York	11	1987	1982	1976	1997	1997	—	—
Wisconsin	3	1987	1987	1990	1996	1996	1996	—
Idaho	1	1988	1985	1972	1995	1995	1995	—
Louisiana	3	1988	1987	1988	1997	1997	1997	—
Tennessee	4	1988	1985	1985	1997	↑1997; ↓2001	↑1997; ↓1998	—
Virginia	9	1988	1985	1978	—	—	—	—
Florida	5	1989	1985	1988	1997	1997	1997	—
Georgia	7	1989	1985	1983	1997	1997	1997	—
Hawaii	1	1989	>1993	1986	↑1997; ↓2001	↑1997; ↓2001	↑1997; ↓2001	—

Indiana	7	1989	1986	1989	1998	—	—	—
Iowa	4	1989	1991	—	1996	1996	1996	1996
Kentucky	5	1989	1984	1990	↑1997; ↓2000	1997	1997	1997
Massachusetts	7	1989	1983	1984	1996	—	—	—
Missouri	5	1989	1986	1990	1995	1995	1995	1995
New Jersey	20	1989	1986	1977	—	1996	—	—
Oregon	2	1989	1986	1985	1997	1997	1997	—
Mississippi	4	1990	1988	1986	1997	1997	1997	1997
Pennsylvania	23	1990	1986	1982	—	—	—	—
Rhode Island	2	1990	1984	1972	—	—	—	—
South Dakota		1990	1988	1987	1996	1996	1996	—
Wyoming		1990	1987	1988	1997	1997	1997	—
Nevada	1	1991	1985	1972	1995	1995	1995	—
North Carolina	11	1993	1985	1972	—	—	—	—
North Dakota		1993	1991	1987	—	↑1997; ↓2003	↑1997; ↓2003	1997
Connecticut	5	1997	1983	1980	1995	—	—	—
Vermont	1	1998	1988	1972	↑1996; ↓2001	↑1996; ↓2001	—	—
Maryland	12	1999	1985	1972	—	—	—	—
Texas	10	2006	1987	1988	1995	↑1995; ↓1999	↑1995; ↓1999	1995
Nebraska		2007	—	—	1997	1997	1997	1997

Panel B: Excluding states with coincidental banking policy changes (2,051 observations excluded; 30 treated BHCs removed)

	Total risk	IVol	Z-score
	(1)	(2)	(3)
Constituency Statute	-0.029** (0.013)	-0.032** (0.013)	0.048*** (0.008)
Bank controls	Yes	Yes	Yes
State controls	Yes	Yes	Yes
Bank FE	Yes	Yes	Yes
Region×Year FE	Yes	Yes	Yes
Obs.	7,197	7,197	7,197
Adj. R ²	0.595	0.557	0.429

Panel C: Controlling for Inter, Intra and RS index

	<i>Total risk</i>	<i>IVol</i>	<i>Z-score</i>
	(1)	(2)	(3)
<i>Constituency Statute</i>	-0.025** (0.011)	-0.029** (0.011)	0.045*** (0.007)
<i>RS index</i>	0.005 (0.003)	0.004 (0.003)	-0.003 (0.005)
<i>Inter</i>	-0.011 (0.020)	-0.016 (0.020)	0.010 (0.017)
<i>Intra</i>	-0.014 (0.016)	-0.012 (0.016)	0.006 (0.026)
Bank controls	Yes	Yes	Yes
State controls	Yes	Yes	Yes
Bank FE	Yes	Yes	Yes
Region×Year FE	Yes	Yes	Yes
Obs.	9,248	9,248	9,248
Adj. R ²	0.605	0.558	0.417

TABLE 9
Constituency Statutes and Bank Capital

This table examines the effects of the enactment of constituency statutes on bank capital. The dependent variables are bank capital-to-asset ratio (*Capital/TA*) and capital-to-loan ratio (*Capital/TL*). In columns (1) and (3), the main explanatory variable of interest is *Constituency Statute*, which is a treatment dummy variable taking on a value of one when a constituency statute is enacted in a state where a BHC is incorporated, and a value of zero otherwise. In columns (2) and (4), we examine the dynamic treatment effects using the decomposed treatment variables as in Table 5 as our main explanatory variables. The bank and state controls as well as fixed effects are identical to those used in the baseline model. We also control for the coincidental state antitakeover laws and the banking deregulation policy changes as defined in Tables 6 and 7. Standard errors are clustered at the state of incorporation level. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

Dependent variables	<i>Capital/TA</i>		<i>Capital/TL</i>	
	(1)	(2)	(3)	(4)
<i>Constituency Statute</i>	0.0061*** (0.0020)	—	0.0110*** (0.0040)	—
<i>Before</i> ^{-2 or -1}	—	0.0011 (0.0021)	—	0.0031 (0.0035)
<i>Current</i> ⁰	—	0.0025 (0.0019)	—	0.0058 (0.0036)
<i>After</i> ⁺¹	—	0.0043* (0.0024)	—	0.0083* (0.0046)
<i>After</i> ^{>=+2}	—	0.0094*** (0.0023)	—	0.0173*** (0.0049)
Bank controls	Yes	Yes	Yes	Yes
State controls	Yes	Yes	Yes	Yes
Control for state antitakeover laws	Yes	Yes	Yes	Yes
Control for banking deregulation	Yes	Yes	Yes	Yes
Bank FE	Yes	Yes	Yes	Yes
Region×Year FE	Yes	Yes	Yes	Yes
Obs.	9,248	9,248	9,248	9,248
Adj. R ²	0.326	0.3284	0.465	0.467

TABLE 10
Constituency Statutes and Bank Lending Activities

This table examines the effect of the enactment of constituency statutes on bank lending activities. The dependent variables are bank log total loans ($Ln(Loans)$), the ratio of non-performing loans to total assets (NPL/TA) and the ratio of net interest income to total assets ($Net\ interest\ income/TA$). Given that data on BHC non-performing loans are only available from 1990 onwards, the analyses in columns (3) to (5) are based on a subsample covering 1990-2012. In columns (1), (3), (4) and (6), the main explanatory variable of interest is *Constituency Statute*, which is a treatment dummy variable taking on a value of one when a constituency statute is enacted in a state where a BHC is incorporated, and a value of zero otherwise. In column (4), we use a matched sample in which each treated BHC is matched to a control bank with the closest bank size and located in a bordering state without statute passage. The diagnostics for the matched sample are provided in Panel B of Table IA.5 of the Internet Appendix. Columns (2), (5) and (7) report the results of the dynamic treatment models. The bank and state controls as well as fixed effects are identical to those used in the baseline model. We also control for the coincidental state antitakeover laws and the banking deregulation policy changes as defined in Tables 6 and 7. Standard errors are clustered at the state of incorporation level. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

Sample	$Ln(Loans)$		NPL/TA			$Net\ interest\ income/TA$	
	Full		Full	Matched	Full	Full	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
<i>Constituency Statute</i>	-0.022 (0.022)	—	-0.0021* (0.0013)	-0.0024** (0.0010)	—	-0.0027*** (0.0009)	—
<i>Before</i> ^{-2 or -1}	—	0.005 (0.023)	—	—	-0.0003 (0.0006)	—	-0.0010 (0.0013)
<i>Current</i> ⁰	—	-0.011 (0.029)	—	—	-0.0038** (0.0017)	—	-0.0036** (0.0017)
<i>After</i> ⁺¹	—	-0.014 (0.030)	—	—	-0.0026* (0.0015)	—	-0.0031* (0.0018)
<i>After</i> ^{>=+2}	—	-0.023 (0.032)	—	—	-0.0016 (0.0018)	—	-0.0033** (0.0015)
Bank controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes
State controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Control for state antitakeover laws	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Control for banking deregulation	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Bank FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Region×Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Obs.	9,248	9,248	7,495	124	7,495	9,248	9,248
Adj. R ²	0.950	0.950	0.650	0.582	0.650	0.386	0.386

TABLE 11
Alternative Explanation: Constituency Statutes As Takeover Defenses

Panel A of this table examines the heterogeneity in the effect of constituency statutes on bank risk. *Constituency Statute* is interacted with two dummy variables. *Any decisions* is a dummy variable taking on a value of one for statutes that allow stakeholder interests to be considered in *any* business decision makings, and a value of zero otherwise. *Only in COC* is defined as one minus *Any decisions* and takes on a value of one for statutes that allow stakeholder interests to be considered in *only* change-of-control (COC) situations, and a value of zero otherwise. The bank and state control variables are the same as those used in the baseline model. We also control for the state antitakeover laws and banking deregulation policy changes. Standard errors are clustered at the state of incorporation level. Panel B presents the state-level analysis examining whether the adoption of constituency statutes significantly affects the BHCs' likelihood of being acquired. The dependent variables include: *No. of BHCs acquired* is the total number of BHCs being acquired in a state; *Proportion of BHCs acquired* is computed as the total number of BHCs being acquired in a state divided by the total number of BHCs incorporated in the same state. The bank control variables are averaged within each state of incorporation. The state controls, state antitakeover laws and banking deregulation policies variables are included. State and region-year fixed effects are accounted for. Standard errors are clustered at the state level. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

Panel A: Can the statute be applied in any business decision-making?

	Total risk (1)	IVol (2)	Z-score (3)
<i>Constituency Statute</i> × <i>Any decisions</i>	-0.040*** (0.014)	-0.044*** (0.013)	0.051*** (0.010)
<i>Constituency Statute</i> × <i>Only in COC</i>	-0.004 (0.012)	-0.005 (0.012)	0.029* (0.017)
Bank controls	Yes	Yes	Yes
State controls	Yes	Yes	Yes
Control for state antitakeover laws	Yes	Yes	Yes
Control for banking deregulation	Yes	Yes	Yes
Bank FE	Yes	Yes	Yes
Region×Year FE	Yes	Yes	Yes
Obs.	9,248	9,248	9,248
Adj. R ²	0.605	0.558	0.418

Panel B: The BHCs' likelihood of being acquired

	No. of BHCs acquired (1)	Proportion of BHCs acquired (2)
<i>Constituency Statute</i>	-0.081 (0.086)	-0.019 (0.017)
<i>Ln(TA)</i>	-0.041 (0.052)	0.003 (0.008)
<i>ROA</i>	-12.578** (4.976)	-2.298* (1.148)
<i>Non-interest income/TA</i>	6.065	-0.859

	(6.600)	(0.954)
<i>Non-core deposits/TA</i>	-0.368	-0.084
	(0.779)	(0.116)
<i>Loans/TA</i>	-0.608	-0.048
	(0.474)	(0.071)
<i>Ln(Market-to-book equity ratio)</i>	0.194*	0.048**
	(0.101)	(0.021)
<i>FREQ</i>	6.266	1.417
	(12.711)	(1.586)
<i>State GDP growth</i>	1.850**	0.104
	(0.899)	(0.193)
<i>Ln(State population)</i>	0.358	-0.017
	(0.385)	(0.054)
<i>Control share acquisition law</i>	0.144	0.032
	(0.265)	(0.028)
<i>Business combination laws</i>	-0.001	0.004
	(0.129)	(0.013)
<i>Fair price laws</i>	-0.143	0.041
	(0.142)	(0.025)
<i>RS index</i>	-0.019	0.004
	(0.048)	(0.005)
<i>Inter</i>	0.021	0.026
	(0.102)	(0.017)
<i>Intra</i>	-0.185	0.000
	(0.159)	(0.029)
Intercept	-4.069	0.335
	(5.584)	(0.789)
State FE	Yes	Yes
Region×Year FE	Yes	Yes
Obs.	1,149	1,149
Adj. R ²	0.061	0.037

TABLE 12
Constituency Statutes and Bank Performance

This table examines the effects of the enactment of constituency statutes on bank performance. The dependent variables include bank return on assets (*ROA*), annual stock returns (*Annual returns*) and log market-to-book equity ratio (*Ln(Market-to-book equity ratio)*). The main explanatory variable of interest is *Constituency Statute*, which is a treatment dummy variable taking on a value of one when a constituency statute is enacted in a state where a BHC is incorporated, and a value of zero otherwise. The bank and state controls as well as fixed effects are identical to those used in the baseline model [except *ROA* and *Ln(Market-to-book equity ratio)* that are excluded]. We also control for the coincidental state antitakeover laws and the banking deregulation policy changes as defined in Tables 6 and 7. To capture a bank's propensity to take excessive risk, we first sort the banks into quintile portfolios annually according to their log total assets, and then divide the banks according to whether its *Total risk* is greater than the portfolio average *Total risk*. *High risk* is a dummy variable taking the value of one if a bank's *Total risk* is greater than that of its size-matched peers in a given year, and zero otherwise. Standard errors are clustered at the state of incorporation level. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

	<i>ROA</i>		<i>Annual returns</i>		<i>Ln(Market-to-book equity ratio)</i>	
	(1)	(2)	(3)	(4)	(5)	(6)
<i>Constituency Statute</i>	0.0011 (0.0010)	0.0005 (0.0011)	-0.013 (0.022)	-0.025 (0.021)	0.018 (0.043)	-0.000 (0.044)
<i>Constituency Statute</i> × <i>High risk</i>	—	0.0013** (0.0006)	—	0.031*** (0.010)	—	0.041** (0.016)
<i>High risk</i>	—	-0.0053*** (0.0005)	—	-0.051*** (0.007)	—	-0.130*** (0.009)
Bank controls	Yes	Yes	Yes	Yes	Yes	Yes
State controls	Yes	Yes	Yes	Yes	Yes	Yes
Control for state antitakeover laws	Yes	Yes	Yes	Yes	Yes	Yes
Control for bank deregulation	Yes	Yes	Yes	Yes	Yes	Yes
Bank FE	Yes	Yes	Yes	Yes	Yes	Yes
Region×Year FE	Yes	Yes	Yes	Yes	Yes	Yes
Obs.	9,248	9,248	9,203	9,203	9,248	9,248
Adj. R ²	0.325	0.351	0.455	0.457	0.570	0.581

TABLE 13
Constituency Statutes and Crisis Performance

This table reports the difference-in-differences analysis examining whether BHCs that were previously treated fared significantly better than the control BHCs during the 1998 crisis and the 2007-08 crisis. Our sample for the 1998 crisis begins with all available BHCs (378 BHCs) over 1997-98. We include all BHCs that have been treated before 1998 (88 BHCs) as the treatment group. Similarly, for the 2007-08 crisis, we begin with all available BHCs (304 BHCs) over 2006-09 of which 42 of them have been treated before 2007. For both crises, we match each treated BHC with a control BHC that is incorporated in a state that has not passed or does not have a constituency statute before 1998 or 2007, is located in a bordering state, and is closest in size before crisis (i.e. in 1997 or in 2006). Following Fahlenbrach, Prilmeier and Stulz (2012), we measure bank crisis performance using bank stock buy-and-hold returns defined as follows:

<i>Crisis₁₉₉₈ RET₁</i> :	From 3 rd August 1998 to the date on which it attains the lowest stock price (before 31 st December 1998).
<i>Crisis₁₉₉₈ RET₂</i> :	From 3 rd August 1998 to 30 th September 1998.
<i>Crisis₁₉₉₈ RET₃</i> :	From 3 rd August 1998 to 30 th October 1998.
<i>Crisis₀₇₋₀₈ RET₁</i> :	From 1 st July 2007 to the date on which it attains the lowest stock price (before 31 st December 2008).
<i>Crisis₀₇₋₀₈ RET₂</i> :	From 1 st July 2007 to 31 st December 2008.
<i>Crisis₀₇₋₀₈ RET₃</i> :	From 1 st July 2007 to 31 st December 2009.

If a bank was delisted during the 1997-98 or 2007-08 periods, we put the proceeds into a daily bank index until the end of 1998 or 2009, to avoid potential survivorship bias. Panel A compares the means of pre-treatment bank and state characteristics between the treatment and control groups and report the *t*-statistics. Panel B reports the before-after differences in bank stock returns, calculated as the crisis returns (*Crisis RET*) minus the pre-crisis bank annual stock returns (*Annual stocks*) for the treatment and control groups, as well as the difference-in-differences estimates between the groups. Panel C reports the difference-in-differences estimates after controlling for the pre-crisis bank and state control variables. Pre-crisis years are defined as 1997 for the 1998 crisis and 2006 for the 2007-08 crisis. *Previously Treated* is a treatment dummy variable equal one for banks that have received a statute enactment prior to the 1998 or 2007-08 crisis, and zero otherwise. The detailed definition of the control variables can be found in Appendix A.1. We report White heteroscedasticity-robust standard errors (in parentheses) in both Panels B and C. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

Panel A: Matching diagnostics for the 1998 crisis and 2007-08 crisis

Crisis	1998 crisis				2007-08 crisis			
	Treatment	Control	Treatment- Control	t-stat	Treatment	Control	Treatment- Control	t-stat
<i>Ln(TA)</i>	8.305	8.268	0.037	0.115	8.391	8.390	0.001	0.005
<i>ROA</i>	0.018	0.018	0.001	0.66	0.016	0.016	0.000	0.081
<i>Non-interest income/TA</i>	0.015	0.013	0.001	0.457	0.015	0.010	0.005**	2.023
<i>Non-core deposits//TA</i>	0.093	0.116	-0.023	-1.507	0.155	0.179	-0.023	-1.132
<i>Loans/TA</i>	0.630	0.652	-0.022	-0.981	0.668	0.707	-0.039	-1.130
<i>FREQ</i>	0.002	0.003	-0.001	-1.184	0.003	0.003	0.000	-0.234
<i>Market beta</i>	0.462	0.472	-0.010	-0.130	1.219	1.233	-0.014	-0.100
<i>State GDP growth</i>	0.054	0.052	0.002	0.710	0.030	0.027	0.003	0.550
<i>Ln(Population)</i>	15.825	15.696	0.128	0.770	16.006	15.557	0.448*	1.770

Panel B: Difference-in-differences estimates

Crisis	1998 crisis			2007-08 crisis		
	(Crisis - Pre-crisis) differences		DiD (Treatment-control)	(Crisis - Pre-crisis) differences		DiD (Treatment-control)
	Treatment	Control		Treatment	Control	
<i>Crisis RET₁</i>	-0.919*** (0.026)	-1.053*** (0.045)	0.133** (0.052)	-0.580*** (0.038)	-0.791*** (0.081)	0.211** (0.089)
<i>Crisis RET₂</i>	-0.798*** (0.028)	-0.919*** (0.048)	0.121** (0.055)	-0.360*** (0.053)	-0.617*** (0.094)	0.258** (0.107)
<i>Crisis RET₃</i>	-0.768*** (0.029)	-0.888*** (0.044)	0.120** (0.052)	-0.514*** (0.058)	-0.756*** (0.089)	0.242** (0.106)

Panel C: Controlling for pre-crisis bank and state characteristics

Crisis definitions	1998 crisis			2007-08 crisis		
	(Crisis - Pre-crisis) differences			(Crisis - Pre-crisis) differences		
	<i>Crisis₁₉₉₈ RET₁</i>	<i>Crisis₁₉₉₈ RET₂</i>	<i>Crisis₁₉₉₈ RET₃</i>	<i>Crisis₀₇₋₀₈ RET₁</i>	<i>Crisis₀₇₋₀₈ RET₂</i>	<i>Crisis₀₇₋₀₈ RET₃</i>
	(1)	(2)	(3)	(4)	(5)	(6)
<i>Previously Treated</i>	0.097** (0.046)	0.065 (0.051)	0.086* (0.048)	0.138*** (0.052)	0.191*** (0.065)	0.338*** (0.083)
<i>Pre-crisis control variables:</i>						
<i>Ln(TA)</i>	0.082*** (0.025)	0.088*** (0.026)	0.091*** (0.027)	0.055* (0.032)	0.069 (0.042)	0.110*** (0.040)
<i>ROA</i>	-6.629* (3.793)	-5.325 (4.111)	-5.962 (4.219)	15.807*** (4.733)	16.208** (6.294)	17.812*** (5.899)
<i>Non-interest income/TA</i>	-2.290 (2.051)	-1.487 (2.179)	-0.845 (2.201)	-5.578 (3.519)	-5.761 (3.931)	-7.786 (5.897)
<i>Non-core deposits/TA</i>	-0.208 (0.390)	-0.340 (0.388)	-0.295 (0.398)	-1.369*** (0.447)	-1.619*** (0.604)	-0.568 (0.580)
<i>Loans/TA</i>	-0.204 (0.182)	-0.290 (0.188)	-0.242 (0.194)	-1.231*** (0.216)	-1.551*** (0.292)	-1.748*** (0.280)
<i>FREQ</i>	-37.876*** (11.632)	-35.303*** (11.532)	-20.041* (11.845)	-40.139*** (13.113)	-55.113*** (17.434)	-64.502*** (17.150)
<i>Market beta</i>	-0.198* (0.115)	-0.246** (0.123)	-0.267** (0.134)	-0.029 (0.044)	0.078 (0.053)	-0.012 (0.060)
<i>State GDP growth</i>	0.313 (1.843)	1.378 (1.934)	0.122 (1.962)	-1.062 (1.033)	-1.021 (1.387)	-2.191 (1.815)
<i>Ln(State population)</i>	-0.049* (0.028)	-0.063* (0.032)	-0.041 (0.029)	0.006 (0.041)	-0.012 (0.053)	-0.016 (0.050)
<i>Pre-crisis Control share acquisition law</i>	0.055 (0.051)	0.055 (0.051)	0.078 (0.054)	-0.072 (0.060)	-0.089 (0.074)	-0.014 (0.095)
<i>Pre-crisis Business combination law</i>	0.022 (0.066)	0.004 (0.068)	0.018 (0.070)	-0.070 (0.072)	-0.177* (0.105)	-0.139 (0.104)
<i>Pre-crisis Fair price law</i>	-0.022 (0.051)	-0.004 (0.054)	-0.035 (0.054)	0.086 (0.064)	0.086 (0.075)	-0.148 (0.121)
<i>Pre-crisis RS index</i>	-0.018 (0.017)	-0.018 (0.018)	-0.014 (0.018)	-0.011 (0.021)	-0.005 (0.026)	0.022 (0.027)
<i>Pre-crisis Intra</i>	-0.144* (0.066)	-0.139 (0.068)	-0.117 (0.070)	-0.341 (0.072)	-0.524 (0.105)	-0.541** (0.104)

	(0.080)	(0.093)	(0.087)	(0.263)	(0.390)	(0.269)
<i>Intercept</i>	-0.335	-0.026	-0.413	0.173	0.956	0.599
	(0.529)	(0.580)	(0.560)	(0.697)	(0.907)	(0.919)
Obs.	176	176	176	84	84	84
Adj. R ²	0.189	0.173	0.140	0.539	0.556	0.519

APPENDIX A.1

Detailed Variable Definitions and Sources

Variables	Description	Source
<u>Bank risk:</u>		
<i>Total risk</i>	A measure of total bank risk, computed as the annualized standard deviation of daily stock returns in a given calendar year.	CRSP
<i>IVol</i>	A measure of bank idiosyncratic risk, computed as the annualized standard deviation of the residuals of the following time-series regressions (estimated for each BHC in each year):	CRSP
$R_{it} = \alpha_i + \beta_{1i} R_{mkt,t} + \beta_{2i} INTEREST_t + \varepsilon_{it}.$		
where R_{it} is the daily stock returns of BHC i, $R_{mkt,t}$ is excess market returns on the value-weighted CRSP market index, and $INTEREST_t$ is the changes in the three-month Treasury bill rates. The time-series regression is estimated for each BHC in each calendar year. We require a minimum of 60 available daily stock return observations for the estimation. Our results are not affected when there is no minimum requirement, or when 30-day, or 90-day minimum requirements are used.		
<i>Z-score</i>	A measure of bank stability, defined as follows:	FR Y-9C; CRSP
$Z_{it} = (ROA_{it} + Capital/TA_{it})/\sigma_{it}$		
where ROA_{it} is return on assets, $Capital/TA_{it}$ is the capital-to-asset ratio, and σ_{it} is the annualized standard deviation of bank daily stock returns.		
<u>Stakeholder orientation:</u>		
<i>Constituency Statute</i>	A treatment dummy variable, equal one when a constituency statute is enacted in a given year and zero otherwise.	Barzuza (2009)
<i>Before^{-1 or -2}</i>	A treatment dummy variable, equal one for each of the two years preceding the enactment of a constituency statute and zero otherwise.	Barzuza (2009)
<i>Current⁰</i>	A treatment dummy variable, equal one for the year of statute enactment and zero otherwise.	Barzuza (2009)
<i>After⁺¹</i>	A treatment dummy variable, equal one if it is one year after a constituency statute is enacted and zero otherwise.	Barzuza (2009)
<i>After^{>=+2}</i>	A treatment dummy variable, equal one if it is two or more years after a constituency statute is	Barzuza (2009)

enacted and zero otherwise.

<i>KLD</i>	A bank-level measure of stakeholder orientation based on KLD data. Following Deng, Kang and Low (2013), we use a two-step approach to construct an overall KLD rating (KLD) for each BHC. First, for each of the five dimensions—community, natural environment, product quality, employees and diversity—we standardize the number of strengths and concerns by the corresponding number of strength and concern indicators. Second, we sum the standardized ratings across the five dimensions of strengths and concerns, respectively, then take the difference between the standardized total strength score and the standardized total concern score to arrive at <i>KLD</i> .	KLD
<u>Bank variables:</u>		
<i>ROA</i>	Bank return on assets, computed as earnings before taxes and extraordinary items divided by total assets.	FR Y-9C
<i>Non-interest income/TA</i>	Ratio of total non-interest income to total assets.	FR Y-9C
<i>Net interest income/TA</i>	Ratio of net interest income to total assets.	FR Y-9C
<i>Non-core deposits/TA</i>	Ratio of "non-core" deposits to total assets. Core deposits include deposits held in domestic offices of subsidiaries of a BHC, excluding all time deposits of over \$100,000 and any brokered deposits. Non-core deposits are calculated by subtracting core deposits from total deposits.	FR Y-9C
<i>Loans</i>	Total loans.	FR Y-9C
<i>Loans/TA</i>	Ratio of total loans to total assets.	FR Y-9C
<i>TA</i>	Deflated total assets, deflated by the US GDP deflator with a base year of 2005.	FRY-9C; FRED
<i>Ln(Market-to-book equity ratio)</i>	Natural logarithm of the ratio of market value of equity to book value of equity. The market value of equity is calculated as the product of stock price and the number of shares outstanding from CRSP.	FR Y-9C; CRSP
<i>FREQ</i>	Ratio of the average daily trading volume of shares in a year to the number of shares outstanding at the beginning of each year.	CRSP; Compustat
<i>Annual return</i>	Bank annual stock returns.	CRSP
<i>Capital/TA</i>	Ratio of bank equity capital to total assets.	FR Y-9C
<i>Capital/TL</i>	Ratio of bank equity capital to total loans.	FR Y-9C
<i>NPL/TA</i>	A measure of loan quality, computed as the ratio of the sum of loans 30 days or more past due and nonaccrual loans to total assets.	FR Y-9C

<i>Market beta</i>	Bank exposure to market systematic risk, defined as the estimated coefficient for $R_{mkt,t}$ from equation (1).	CRSP
<i>H-index (State of location)</i>	Bank competition, calculated as the sum of a BHC's squared market shares in total loans granted in the state of location in a given year.	FR Y-9C; Compustat
<i>Control share acquisition law</i>	A dummy variable taking on the value of zero (one) prior to (from the year of) the passage of control share acquisition law.	Bertrand and Mullainathan (2003)
<i>Business combination law</i>	A dummy variable taking on the value of zero (one) prior to (from the year of) the passage of business combination law.	Bertrand and Mullainathan (2003)
<i>Fair price law</i>	A dummy variable taking on the value of zero (one) prior to (from the year of) the passage of fair price law.	Bertrand and Mullainathan (2003)
<i>RS index</i>	The Rice-Strahan index of interstate banking deregulation based on Rice and Strahan (2010). It takes on values from zero (deregulated) to four (highly regulated) based on deregulation changes in a state.	Rice and Strahan (2010)
<i>Inter</i>	A dummy variable taking on the value of zero (one) prior to (from the year of) interstate deregulation (onward) during the 1980s and 1990s as described in Amore, Schneider and Žaldokas (2013).	Amore, Schneider and Žaldokas (2013)
<i>Intra</i>	A dummy variable taking on the value of zero (one) prior to (from the year of) intrastate deregulation (onward) during the 1970s, 1980s and 1990s as described in Jayaratne and Strahan (1996).	Jayaratne and Strahan (1996).
<i>State GDP growth</i>	State real GDP growth rate.	US Bureau of Economic Analysis (BEA)
<i>Ln(State population)</i>	Natural logarithm of state population.	US Bureau of Economic Analysis (BEA)
<i>Previously Treated</i>	A treatment dummy variable equal one for banks that have received a statute enactment prior to the 1998 financial crisis or the 2007-08 financial crisis, and zero otherwise.	Barzuza (2009)
<i>Crisis₁₉₉₈ RET₁</i>	Buy-and-hold bank stock returns from 3 rd August, 1998 to the date on which it attains the lowest stock price (before 31 st December, 1998).	CRSP
<i>Crisis₁₉₉₈ RET₂</i>	Buy-and-hold stock returns from 3 rd August, 1998 to 30 th September, 1998.	CRSP

<i>Crisis₁₉₉₈ RET₃</i>	Buy-and-hold stock returns from 3 rd August, 1998 to 30 th October, 1998.	CRSP
<i>Crisis₀₇₋₀₈ RET₁</i>	Buy-and-hold stock returns from 1 st July, 2007 to the date on which it attains the lowest stock price (before 31 st December, 2008).	CRSP
<i>Crisis₀₇₋₀₈ RET₂</i>	Buy-and-hold stock returns from 1 st July, 2007 to 31 st December, 2008.	CRSP
<i>Crisis₀₇₋₀₈ RET₃</i>	Buy-and-hold stock returns from 1 st July, 2007 to 31 st December, 2009.	CRSP
<i>Any decisions</i>	A dummy variable equal one when a constituency statute allows stakeholder interests to be considered in <i>any</i> business decision-making, and zero otherwise.	State legislatures
<i>Only in COC</i>	One minus <i>Any decisions</i> . A dummy variable equal one when a constituency statute allows stakeholder interests to be considered <i>only</i> in change-of-control (COC) situations, and zero otherwise.	State legislatures
<i>No. of BHCs acquired</i>	The total number of BHCs acquired in a given state of incorporation.	SDC Platinum
<i>Proportion of BHCs acquired</i>	The total number of BHCs acquired in a given state of incorporation divided by the total number of BHCs incorporated in the same state.	Federal Reserve Bank of Chicago
<i>High risk</i>	A dummy variable taking the value of one if a bank's <i>Total risk</i> is greater than that of its size-matched peers in a given year, and zero otherwise. We first sort the banks into quintile portfolios annually according to their total assets, and then compute the portfolio average <i>Total risk</i> .	FR Y-9C; CRSP

Does Bank Stakeholder Orientation Enhance Financial Stability? Evidence from a Natural Experiment

Internet Appendix
Not included in the paper

This version: 9 February 2017

TABLE IA.1
Details of the Constituency Statutes

This table provides the constituency statutes, the reference locations, the number of words of the statutes, and a variable (Any decision?) of whether stakeholder interests can be considered in *any* business decision makings as opposed to *only* change-of-control (COC) situations

State	Year	Constituency statutes	Clauses	Any decisions?
OH	1984	For purposes of this section, a director, in determining what the director reasonably believes to be in the best interests of the corporation, shall consider the interests of the corporation's shareholders and, in the director's discretion, may consider any of the following: (1) The interests of the corporation's employees, suppliers, creditors, and customers; (2) The economy of the state and nation; (3) Community and societal considerations; (4) The long-term as well as short-term interests of the corporation and its shareholders, including the possibility that these interests may be best served by the continued independence of the corporation.	OHIO REV. CODE ANN. § 1701.59(F)	Y
IL	1985	In discharging the duties of their respective positions, the board of directors, committees of the board, individual directors and individual officers may, in considering the best long term and short term interests of the corporation, consider the effects of any action (including without limitation, action which may involve or relate to a change or potential change in control of the corporation) upon employees, suppliers and customers of the corporation or its subsidiaries, communities in which offices or other establishments of the corporation or its subsidiaries are located, and all other pertinent factors.	805 ILL. COMP. STAT. § 5/8.85	Y
ME	1986	Interests of other constituencies. In discharging their duties, the directors and officers of the corporation may, in considering the best interests of the corporation and of its shareholders, consider the effects of any action upon employees, suppliers and customers of the corporation, communities in which offices or other establishments of the corporation are located and all other pertinent factors.	ME. REV. STAT. tit. 13-C M.R.S. § 831(6)	Y

AZ	1987	In discharging the duties of the position of director under this chapter, a director of an issuing public corporation, in considering the best interests of the corporation, shall consider the long-term as well as the short-term interests of the corporation and its shareholders including the possibility that these interests may be best served by the continued independence of the corporation. This section shall not modify the duties of the position of director in any matter outside the scope of this chapter.	ARIZ. REV. STAT. ANN. § 10-2702	N
MN	1987	In discharging the duties of the position of director, a director may, in considering the best interests of the corporation, consider the interests of the corporation's employees, customers, suppliers, and creditors, the economy of the state and nation, community and societal considerations, and the long-term as well as short-term interests of the corporation and its shareholders including the possibility that these interests may be best served by the continued independence of the corporation.	MINN. STAT. § 302A.251(5) (1987)	Y
NM	1987	For purposes of Subsection B of this section, a director, in determining what he reasonably believes to be in or not opposed to the best interests of the corporation, shall consider the interests of the corporation's shareholders and, in his discretion, may consider any of the following: (1) the interests of the corporation's employees, suppliers, creditors and customers; (2) the economy of the state and nation; (3) the impact of any action upon the communities in or near which the corporation's facilities or operations are located; and (4) the long-term interests of the corporation and its shareholders, including the possibility that those interests may be best served by the continued independence of the corporation.	N.M. STAT. ANN. § 53-11-35(D)	Y
NY	1987	(b) In taking action, including, without limitation, action which may involve or relate to a change or potential change in the control of the corporation, a director shall be entitled to consider, without limitation, (1) both the long-term and the short-term interests of the corporation and its shareholders and (2) the effects that the corporation's actions may have in the short-term or in the long-term upon any of the following: (i) the prospects for potential growth, development, productivity and profitability of the corporation;	N.Y. BUS. CORP. LAW § 717(b)	Y

		(ii) the corporation's current employees; (iii) the corporation's retired employees and other beneficiaries receiving or entitled to receive retirement, welfare or similar benefits from or pursuant to any plan sponsored, or agreement entered into, by the corporation; (iv) the corporation's customers and creditors; and (v) the ability of the corporation to provide, as a going concern, goods, services, employment opportunities and employment benefits and otherwise to contribute to the communities in which it does business.		
WI	1987	Consideration of interests in addition to shareholders' interests. In discharging his or her duties to the corporation and in determining what he or she believes to be in the best interests of the corporation, a director or officer may, in addition to considering the effects of any action on shareholders, consider the following: (1) The effects of the action on employees, suppliers and customers of the corporation. (2) The effects of the action on communities in which the corporation operates. (3) Any other factors that the director or officer considers pertinent.	WIS. STAT. § 180.0827	Y
ID	1988	In discharging the duties of the position of director of an issuing public corporation, a director, in considering the best interests of the corporation, shall consider the long-term as well as the short-term interests of the corporation and its shareholders including the possibility that these interests may be best served by the continued independence of the corporation. In addition, a director may consider the interests of Idaho employees, suppliers, customers and communities in discharging his duties.	IDAHO CODE § 30-1602, 30-1702.	Y
LA	1988	The board of directors, when evaluating a tender offer or an offer to make a tender or exchange offer or to effect a merger or consolidation may, in exercising its judgment in determining what is in the best interest of the corporation and its shareholders, consider the following factors and any other factors which it deems relevant: (1) Not only the consideration being offered in the proposed transaction in	LA. REV. STAT. ANN. § 12:92(G)(2) (2004)	N

relation to the then current market price for the outstanding capital stock of the corporation, but also the market price for the capital stock of the corporation over a period of years, the estimated price that might be achieved in a negotiated sale of the corporation as a whole or in part or through orderly liquidation, the premiums over market price for the securities of other corporations in similar transactions, current political, economic, and other factors bearing on securities prices and the corporation's financial condition and future prospects.

(2) The social and economic effects of such transaction on the corporation, its subsidiaries, or their employees, customers, creditors, and the communities in which the corporation and its subsidiaries do business.

(3) The business and financial conditions and earnings prospects of the acquiring party or parties, including, but not limited to, debt service and other existing or likely financial obligations of the acquiring party or parties, and the possible effect of such conditions upon the corporation and its subsidiaries and the communities in which the corporation and its subsidiaries do business.

(4) The competence, experience, and integrity of the acquiring party or parties and its or their management.

TN	1988	No resident domestic corporation which has a class of voting stock registered or traded on a national securities exchange or registered with the securities and exchange commission pursuant to § 12(g) of the Exchange Act nor any of its officers and directors shall be held liable at law or in equity for either having failed to approve the acquisition of shares by an interested shareholder on or before such interested shareholder's share acquisition date, or for seeking to enforce or implement this part and part 3 of this chapter, or for failing to adopt or recommend any charter or bylaw amendment or provision respecting this part and parts 3-5 of this chapter, or for opposing any proposed merger, exchange, tender offer or significant disposition of the assets of the resident domestic corporation or any subsidiary of such resident domestic corporation because of a good faith belief that such merger, exchange, tender offer or significant disposition of assets would adversely affect the resident domestic corporation's	TENN. CODE ANN. § 48-103-204	N
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		employees, customers, suppliers, the communities in which such resident domestic corporation or its subsidiaries operate or are located or any other relevant factor if such factors, including those factors specifically enumerated in this section, are permitted to be considered by the board of directors under the charter for such resident domestic corporation in connection with a merger, exchange, tender offer or significant disposition of assets.		
VA	1988	Except as expressly provided in this article, the provisions of this article shall not limit actions that may be taken, or require the taking of any action, by the board of directors or shareholders with respect to any potential change in control of the corporation. With respect to any action or any failure to act by the board of directors, the provisions of 13.1-690 shall apply. In determining the best interests of the corporation, a director may consider the possibility that those interests may best be served by the continued independence of the corporation.	VA. CODE ANN. § 13.1-727.1	Y
FL	1989	In discharging his or her duties, a director may consider such factors as the director deems relevant, including the long-term prospects and interests of the corporation and its shareholders, and the social, economic, legal, or other effects of any action on the employees, suppliers, customers of the corporation or its subsidiaries, the communities and society in which the corporation or its subsidiaries operate, and the economy of the state and the nation.	F.S. §607.0830 (3) and (5)	Y
GA	1989	A provision that, in discharging the duties of their respective positions and in determining what is believed to be in the best interests of the corporation, the board of directors, committees of the board of directors, and individual directors, in addition to considering the effects of any action on the corporation or its shareholders, may consider the interests of the employees, customers, suppliers, and creditors of the corporation and its subsidiaries, the communities in which offices or other establishments of the corporation and its subsidiaries are located, and all other factors such directors consider pertinent; provided, however, that any such provision shall be deemed solely to grant discretionary authority to the directors and shall not be deemed to provide to any constituency any right to be	GA. CODE ANN. § 14-2-202(b)(5)	Y

considered.

HI	1989	In determining the best interests of the corporation, a director, in addition to considering the interests of the corporation's shareholders, may consider, in the director's discretion, any of the following factors: (1) The interests of the corporation's employees, customers, suppliers, and creditors; (2) The economy of the State and the nation; (3) Community and societal considerations, including, without limitation, the impact of any action upon the communities in or near which the corporation has offices or operations; and (4) The long-term as well as short-term interests of the corporation and its shareholders, including, without limitation, the possibility that these interests may be best served by the continued independence of the corporation.	HI Rev Stat § 414-221 (b)	Y
IN	1989	(d) A director may, in considering the best interests of a corporation, consider the effects of any action on shareholders, employees, suppliers, and customers of the corporation, and communities in which offices or other facilities of the corporation are located, and any other factors the director considers pertinent. (g) In taking or declining to take any action, or in making or declining to make any recommendation to the shareholders of the corporation with respect to any matter, a board of directors may, in its discretion, consider both the short term and long term best interests of the corporation, taking into account, and weighing as the directors deem appropriate, the effects thereof on the corporation's shareholders and the other corporate constituent groups and interests listed or described in subsection (d), as well as any other factors deemed pertinent by the directors under subsection (d). If a determination is made with respect to the foregoing with the approval of a majority of the disinterested directors of the board of directors, that determination shall conclusively be presumed to be valid unless it can be demonstrated that the determination was not made in good faith after reasonable investigation.	IND. CODE ANN. § 23-1-35-1 (d), (e) and (g)	Y

IA	1989	1. A director, in determining what is in the best interest of the corporation when considering a tender offer or proposal of acquisition, merger, consolidation, or similar proposal, may consider any or all of the following community interest factors, in addition to consideration of the effects of any action on shareholders: a. The effects of the action on the corporation's employees, suppliers, creditors, and customers. b. The effects of the action on the communities in which the corporation operates. c. The long-term as well as short-term interests of the corporation and its shareholders, including the possibility that these interests may be best served by the continued independence of the corporation.	IOWA CODE ANN. § 491.101B (1) and (2)	N
KY	1989	In discharging its duties under this section, or otherwise, the board of directors, in considering the best interests of the corporation, may consider in addition to the interests of the corporation's shareholders, any of the following: (a) The interests of the corporation's employees, suppliers, creditors and customers; (b) The economy of the state and nation; (c) Community and societal considerations; and (d) The long-term as well as short-term interests of the corporation and its shareholders, including the possibility that these interests may be best served by the continued independence of the corporation.	KY. REV. STAT. ANN. § 271B.12- 210(4)	N
MA	1989	A director, officer or incorporator of a corporation shall perform his duties as such, including, in the case of a director, his duties as a member of a committee of the board upon which he may serve, in good faith and in a manner he reasonably believes to be in the best interests of the corporation, and with such care as an ordinarily prudent person in a like position would use under similar circumstances. In determining what he reasonably believes to be in the best interests of the corporation, a director may consider the interests of the corporation's employees, suppliers, creditors and customers, the economy of the state, region and nation, community and societal considerations, and the long-term and short-term interests of the corporation and its stockholders, including the possibility that these interests may be best served by the continued independence of the	MASS. GEN. LAWS ANN. ch. 156B, § 65	Y

		corporation.		
MO	1989	In exercising its business judgment concerning any acquisition proposal, as defined in subsection 2 of this section, the board of directors of the corporation may consider the following factors, among others: (1) The consideration being offered in the acquisition proposal in relation to the board's estimate of: (a) The current value of the corporation in a freely negotiated sale of either the corporation by merger, consolidation or otherwise, or all or substantially all of the corporation's assets; (b) The current value of the corporation if orderly liquidated; (c) The future value of the corporation over a period of years as an independent entity discounted to current value; (2) Then existing political, economic and other factors bearing on security prices generally or the current market value of the corporation's securities in particular; (3) Whether the acquisition proposal might violate federal, state or local laws; (4) Social, legal and economic effects on employees, suppliers, customers and others having similar relationships with the corporation, and the communities in which the corporation conducts its businesses; (5) The financial condition and earning prospects of the person making the acquisition proposal including the person's ability to service its debt and other existing or likely financial obligations; (6) The competence, experience and integrity of the person making the acquisition proposal.	MO. REV. STAT. § 351.347.1	N
NJ	1989	(2) In discharging his duties to the corporation and in determining what he reasonably believes to be in the best interest of the corporation, a director may, in addition to considering the effects of any action on shareholders, consider any of the following: (a) the effects of the action on the corporation's employees, suppliers, creditors and customers; (b) the effects of the action on the community in which the corporation operates; and (c) the long term as well as the short-term interests of the corporation and its shareholders, including the possibility that these interests may best be	NJ Rev Stat § 14A:6-1 (2), (3)	Y

		served by the continued independence of the corporation.		
OR	1989	(5) When evaluating any offer of another party to make a tender or exchange offer for any equity security of the corporation, or any proposal to merge or consolidate the corporation with another corporation or to purchase or otherwise acquire all or substantially all the properties and assets of the corporation, the directors of the corporation may, in determining what they believe to be in the best interests of the corporation, give due consideration to the social, legal and economic effects on employees, customers and suppliers of the corporation and on the communities and geographical areas in which the corporation and its subsidiaries operate, the economy of the state and nation, the long-term as well as short-term interests of the corporation and its shareholders, including the possibility that these interests may be best served by the continued independence of the corporation, and other relevant factors.	OR. REV. STAT. ANN. § 60.357 (4) and (5)	N
MS	1990	For purposes of this section, a director, in determining what he reasonably believes to be in the best interests of the corporation, shall consider the interests of the corporation's shareholders and, in his discretion, may consider any of the following: (1) The interests of the corporation's employees, suppliers, creditors and customers; (2) The economy of the state and nation; (3) Community and societal considerations; (4) The long-term as well as short-term interests of the corporation and its shareholders, including the possibility that these interests may be best served by the continued independence of the corporation.	MISS. CODE ANN. § 79-4-8.30(f)	Y
PA	1990	1715 (a) General rule.--In discharging the duties of their respective positions, the board of directors, committees of the board and individual directors of a business corporation may, in considering the best interests of the corporation, consider to the extent they deem appropriate: (1) The effects of any action upon any or all groups affected by such action, including shareholders, employees, suppliers, customers and creditors of the corporation, and upon communities in which offices or other establishments of the corporation are located. (2) The short-term and long-term interests of the corporation, including	15 PA. CONS. STAT. § 1715(a)(b) 516(a)	Y

benefits that may accrue to the corporation from its long-term plans and the possibility that these interests may be best served by the continued independence of the corporation.

(3) The resources, intent and conduct (past, stated and potential) of any person seeking to acquire control of the corporation.

(4) All other pertinent factors.

516 (a) In discharging the duties of their respective positions, the board of directors, committees of the board and individual directors of a domestic corporation may, in considering the best interests of the corporation, consider the effects of any action upon employees, upon suppliers and customers of the corporation and upon communities in which offices or other establishments of the corporation are located, and all other pertinent factors. The consideration of those factors shall not constitute a violation of section 512 (relating to standard of care and justifiable reliance).

RI	1990	(a) In discharging the duties of their respective positions with respect to any proposed business combination, as defined in § 7-5.2-3(5), the board of directors, committees of the board, individual directors, and individual officers may, in considering the best interest of the corporation, in addition to considering the effects on shareholders, consider any of the following: (1) The effect on the corporation's employees, suppliers, creditors, and customers; (2) The effect on the communities in which the corporation operates; (3) The long-term as well as short term interests of the corporation and its shareholders, including the possibility that these interests may be best served by the continued independence of the corporation.	R.I. GEN. LAWS § 7-5.2-8 (a) and (b)	N
SD	1990	(1) In discharging the duties of their respective positions in taking action which may involve or relate to a change or potential change in the control of a domestic public corporation, and in determining what they reasonably believe to be in the best interest of the corporation, the board and individual directors may, in addition to considering the effects of any such action on the shareholders, consider any of the following: (a) The long-term as well as the short-term interests of the corporation and its shareholders, including the possibility that these interests may be best served by the continued independence of the corporation;	S.D. CODIFIED LAWS § 47-33-4 (1) and (2)	N

		(b) The effects of the action on the corporation's employees, customers, creditors and suppliers of goods and services; (c) The effects of the action upon any community in which an office or other facility of the corporation is located; and (d) The economy of this state and the nation. The consideration of those factors shall not constitute a violation of the director's fiduciary duty to the corporation or its shareholders, including, without limiting the generality of the foregoing, a director's duty of loyalty.		
WY	1990	For purposes of subsection (a) of this section, a director, in determining what he reasonably believes to be in or not opposed to the best interests of the corporation, shall consider the interests of the corporation's shareholders and, in his discretion, may consider any of the following: (i) The interests of the corporation's employees, suppliers, creditors and customers; (ii) The economy of the state and nation; (iii) The impact of any action upon the communities in or near which the corporation's facilities or operations are located; (iv) The long-term interests of the corporation and its shareholders, including the possibility that those interests may be best served by the continued independence of the corporation; and (v) Any other factors relevant to promoting or preserving public or community interests.	WYO. STAT. ANN. § 17-16-830(g)	Y
NV	1991	4. Directors and officers, in exercising their respective powers with a view to the interests of the corporation, may consider: (a) The interests of the corporation's employees, suppliers, creditors and customers; (b) The economy of the State and Nation; (c) The interests of the community and of society; and (d) The long-term as well as short-term interests of the corporation and its stockholders, including the possibility that these interests may be best served by the continued independence of the corporation.	NEV. REV. STAT. § 78.138 (4) and (6)	Y
NC	1993	The duties of a director weighing a change of control situation shall not be any different, nor the standard of care any higher, than otherwise provided	N.C. GEN. STAT. § 55-8-30 (d)	Y

		in this section.		
ND	1993	In discharging the duties of the position of director, a director may, in considering the best interests of the corporation, consider the interests of the corporation's employees, customers, suppliers, and creditors, the economy of the state and nation, community and societal considerations, and the long-term as well as the short-term interests of the corporation and its shareholders, including the possibility that these interests may be best served by the continued independence of the corporation.	N.D. CENT. CODE § 10-19.1-50(6)	Y
CT	1997	(d) For purposes of sections 33-817, 33-830, 33-831, 33-841 and 33-844, a director of a corporation which has a class of voting stock registered pursuant to Section 12 of the Securities Exchange Act of 1934, as the same has been or hereafter may be amended from time to time, in addition to complying with the provisions of subsections (a) to (c), inclusive, of this section, shall consider, in determining what he reasonably believes to be in the best interests of the corporation, (1) the long-term as well as the short-term interests of the corporation, (2) the interests of the shareholders, long-term as well as short-term, including the possibility that those interests may be best served by the continued independence of the corporation, (3) the interests of the corporation's employees, customers, creditors and suppliers, and (4) community and societal considerations including those of any community in which any office or other facility of the corporation is located. A director may also in his discretion consider any other factors he reasonably considers appropriate in determining what he reasonably believes to be in the best interests of the corporation.	CONN. GEN. STAT. § 33-756 (d) and €	N
VT	1998	(a) A director shall discharge his or her duties as a director, including the director's duties as a member of a committee: (1) in good faith; (2) with the care an ordinarily prudent person in a like position would exercise under similar circumstances; and (3) in a manner the director reasonably believes to be in the best interests of the corporation. In determining what the director reasonably believes to be in the best interests of the corporation, a director of a corporation which has a class of voting stock registered under section 12 of the Securities Exchange Act of 1934, as the same may be amended from time to time,	VT. STAT. ANN. tit. 11A, § 8.30(a) and (d)	Y

		may, in addition, consider the interests of the corporation's employees, suppliers, creditors and customers, the economy of the state, region and nation, community and societal considerations, including those of any community in which any offices or facilities of the corporation are located, and any other factors the director in his or her discretion reasonably considers appropriate in determining what he or she reasonably believes to be in the best interests of the corporation, and the long-term and short-term interests of the corporation and its stockholders, and including the possibility that these interests may be best served by the continued independence of the corporation; provided that nothing in this subdivision shall affect in any way the interests that may be considered by the director of a corporation which does not have a class of voting stock registered under section 12 of the Securities Exchange Act of 1934, as the same may be amended from time to time, in determining what such director reasonably believes to be in the best interests of the corporation.		
MD	1999	(9) A provision that allows the board of directors, in considering a potential acquisition of control of the corporation, to consider the effect of the potential acquisition of control on: (i) Stockholders, employees, suppliers, customers, and creditors of the corporation; and (ii) Communities in which offices or other establishments of the corporation are located.	MD. CODE. ANN., Corps. & Ass'ns. § 2-104(b)(9)	N
TX	2006	(b) In discharging the duties of director under this code or otherwise and in considering the best interests of the corporation, a director is entitled to consider the long-term and short-term interests of the corporation and the shareholders of the corporation, including the possibility that those interests may be best served by the continued independence of the corporation. (d) Subject to direction by the board of directors of the corporation, in discharging the duties of an officer under this code or otherwise, an officer is entitled to consider: (1) the long-term and short-term interests of the corporation and of the corporation's shareholders, including the possibility that those interests may be best served by the continued independence of the corporation; and	TEX. BUS. ORGS. CODE ANN. § 21.401 (b)-(e)	Y

		(2) any social purposes specified in the corporation's certificate of formation.		
NE	2007	(1) A director shall discharge his or her duties as a director, including his or her duties as a member of a committee: (a) In good faith; (b) With the care an ordinarily prudent person in a like position would exercise under similar circumstances; and (c) In a manner he or she reasonably believes to be in the best interests of the corporation. A director may, but need not, in considering the best interests of the corporation, consider, among other things, the effects of any action on employees, suppliers, creditors, and customers of the corporation and communities in which offices or other facilities of the corporation are located. (4) A director shall not be liable for any action taken as a director, or any failure to take any action, if he or she performed the duties of his or her office in compliance with this section.	NEB. REV. ST. § 21-2095 (1) and (4)	Y

TABLE IA.2
Constituency Statutes and Bank Stakeholder Performance

This table examines the effect of the enactment of constituency statutes on the bank's likelihood of large negative changes in employee number and bank effective tax rates. The main explanatory variable of interest is *Constituency Statute*, which is a treatment dummy variable taking on a value of one when a constituency statute is enacted in a state where a BHC is incorporated, and a value of zero otherwise. Columns (1) and (2) are both logit regressions. The dependent variable in column (1) [(2)] is dummy variable equal one when a bank's rate of change in the number of employees is less than zero [less than the 10th percentile rate of change in employee number], and zero otherwise. Column (3) is an OLS regression where the dependent variable is the effective tax rate (*GAAP ETR*), computed as the ratio of tax expense to pre-tax earnings. The bank and state controls are identical to those used in the baseline model. The logit regressions include year fixed effects and the regression in column (3) includes both bank and year fixed effects. Standard errors reported in parentheses are clustered at the state of incorporation level. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

	<i>Indicator(%Δ in employee number is)</i>		<i>ETR</i>
	<i><0</i>	<i><10th percentile</i>	
	Logit		OLS
	(1)	(2)	(3)
<i>Constituency Statute</i>	-0.102 (0.087)	-0.206** (0.088)	0.068*** (0.015)
<i>Ln(TA)</i>	0.124*** (0.021)	0.030 (0.022)	0.051*** (0.011)
<i>ROA</i>	-26.352*** (2.679)	-45.158*** (3.558)	2.877*** (0.450)
<i>Non-interest income/TA</i>	11.548*** (3.084)	29.704*** (3.806)	0.174 (0.402)
<i>Non-core deposits/TA</i>	-2.594*** (0.978)	-0.502 (0.617)	-0.035 (0.065)
<i>Loans/TA</i>	-0.388 (0.343)	0.617** (0.307)	0.202*** (0.047)
<i>Ln(Market-to-book equity ratio)</i>	-0.574*** (0.084)	-0.498*** (0.098)	0.002 (0.011)
<i>FREQ</i>	-0.470 (4.480)	6.219 (6.549)	-0.740 (0.726)
<i>State GDP growth</i>	-6.236*** (1.207)	-9.009*** (1.783)	-0.013 (0.097)
<i>Ln(State population)</i>	0.036 (0.042)	0.183*** (0.037)	0.020 (0.048)
<i>Intercept</i>	-1.351** (0.637)	-5.774*** (0.793)	-0.707 (0.799)
Bank FE			Yes
Year FE	Yes	Yes	Yes
Obs.	9,049	9,049	6,395
Pseudo R ² /Adj. R ²	0.068	0.110	0.084

TABLE IA.3
Placebo Tests

This table reports the results of the three placebo tests that randomize the assignment of the enactment of constituency statutes. In placebo test 1, we obtain the event year distribution of the constituency statutes and then randomly assign states into each of these enactment years (without replacement) following the distribution. In other words, we keep the distribution of the enactment years but disrupt the correct assignment of enactment years to states. In placebo test 2, among the 35 treated states, we randomly assign the enactment years to these states. Therefore, we keep the distribution of the state unchanged, but disrupt the correct timing of the enactment. In placebo test 3, we randomize both the treatment years and states (with no replacement, i.e., there are no multiply-treated states). For each test, within each randomized placebo sample, we regress bank risk-taking on the placebo constituency statute treatment variable following the baseline specification as shown in columns (2), (5) and (8) of Table 3, and store its coefficient estimates. We repeat this procedure for 5,000 times to obtain a distribution of the placebo statute estimates and then compare them with the coefficients estimated from the real data sample. Panel A reports the average coefficients and standard errors for the placebo constituency statute treatment variable across the 5,000 placebo samples for each placebo test for the three risk-taking measures. Panel B reports the number of cases (and in percentage) in which the placebo coefficient estimate for *Constituency Statute* are smaller than the coefficient estimate from the real data sample (reported in Table 3). ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

Panel A: Falsification tests

		<i>Total risk</i>	<i>IVol</i>	<i>Z-score</i>
		(1)	(2)	(3)
Placebo test 1 (Keeping the distribution of the enactment year the same)	<i>Placebo Constituency Statute</i>	0.0015 (0.014)	0.0015 (0.014)	-0.0031 (0.013)
Placebo test 2 (Randomizing the enactment years)	<i>Placebo Constituency Statute</i>	-0.0028 (0.010)	-0.0029 (0.010)	-0.0033 (0.009)
Placebo test 3 (Randomizing both the enactment years and states)	<i>Placebo Constituency Statute</i>	0.0000 (0.010)	-0.0001 (0.010)	-0.0003 (0.009)

Panel B: Comparing the actual coefficient estimate with the placebo estimates

Number of placebo samples with smaller placebo coefficient estimate than the actual coefficient estimate for <i>Constituency Statute</i> (as reported in Table 3).	Placebo test 1	Yes	362	306	4,995
		No	4,638	4,694	5
		%	0.928	0.939	0.999
	Placebo test 2	Yes	47	22	5,000
		No	4,953	4,978	0
		%	0.991	0.996	1.000
	Placebo test 3	Yes	53	46	4,998
		No	4,947	4,954	2
		%	0.989	0.991	0.9996

TABLE IA.4
Details of the Placebo States for Section 4.3.3

Panel A of this table provides the details of the placebo states that are bordering the treated states and have the closest state GDP in the year prior to the treatment. Panel B reports the univariate comparison (at the state level) of the pre-treatment GDP across the treated and the placebo states using mean and median tests. Panel C reports the results of the baseline models using the placebo constituency statute. The bank and state controls and fixed effects are identical to those used in the baseline model. Standard errors reported in parentheses are clustered at the state of incorporation level. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

Panel A: Descriptions of the placebo bordering states

Year	Treatment states		Placebo bordering states	
	State	State GDP pre-treatment	Bordering states	State GDP pre-treatment
1987	Arizona	55,881	Colorado	60,970
1987	Minnesota	79,450	Iowa	43,226
1987	New Mexico	21,807	Oklahoma	48,997
1987	New York	390,104	Pennsylvania	187,386
1987	Wisconsin	77,824	Indiana	86,437
1988	Idaho	13,996	Wyoming	10,370
1988	Louisiana	78,488	Arkansas	32,664
1988	Tennessee	80,715	North Carolina	113,262
1988	Virginia	117,603	Maryland	91,380
1989	Florida	224,848	Alabama	66,008
1989	Georgia	126,565	South Carolina	57,329
1989	Hawaii	26,799	—	—
1989	Indiana	99,492	Michigan	180,621
1989	Iowa	49,088	Minnesota	91,896
1989	Kentucky	61,851	West Virginia	25,876
1989	Massachusetts	151,625	Connecticut	90,707
1989	Missouri	95,760	Kansas	46,698
1989	New Jersey	194,709	New York	456,557
1989	Oregon	49,138	Nevada	24,987
1990	Mississippi	37,208	Tennessee	91,579
1990	Pennsylvania	233,162	Ohio	217,817
1990	Rhode Island	21,059	New Hampshire	23,777
1990	South Dakota	11,790	North Dakota	10,729
1990	Wyoming	11,437	Montana	12,630
1991	Nevada	30,980	Utah	31,249
1993	North Carolina	159,337	Virginia	158,990
1993	North Dakota	12,896	South Dakota	14,886
1997	Connecticut	129,111	Rhode Island	26,454
1998	Vermont	15,521	Maine	30,775
1999	Maryland	171,402	Delaware	35,955
2006	Texas	999,641	Louisiana	200,436

2007	Nebraska	78,581	Missouri	234,124
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Panel B: Comparing the pre-treatment state GDP between the treated and placebo states

	Treatment states		Placebo bordering states		<i>p</i> -value (Treatment-Placebo)	
	Mean	Median	Mean	Median	Mean	Median
<i>State GDP</i>	122,121	78,535	90,477	57,329	0.351	0.464

Panel C: Baseline results using the placebo statute

	<i>Total risk</i>	<i>IVol</i>	<i>Z-score</i>
	(1)	(2)	(3)
<i>Placebo Constituency Statute (bordering states)</i>	0.004 (0.014)	0.006 (0.013)	-0.007 (0.014)
Bank controls	Yes	Yes	Yes
State controls	Yes	Yes	Yes
Bank FE	Yes	Yes	Yes
Region×Year FE	Yes	Yes	Yes
Obs.	9,248	9,248	9,248
Adj. R ²	0.605	0.557	0.414

TABLE IA.5
Diagnostics for the Matched Samples for Tables 6 and 10

Panels A and B of this table present the diagnostics for the matched samples used in Tables 6 and 10, respectively. In Panel A, columns (1) to (3) report the matched sample restricting the distance between each matched pair to be within 500 miles; columns (4) to (6) restrict the distance to be within 250 miles; columns (7) to (9) restrict the distance to be within 125 miles. In both panels, we report the average pre-treatment bank and state characteristics for both the treatment and control groups and present the differences and statistical inference based on two-sample *t*-tests. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

Panel A: Diagnostics for samples matched by bank size, distance and bordering state for Table 6

Samples	Within 500 miles (130 pairs)			Within 250 miles (99 pairs)			Within 125 miles (44 pairs)		
	Treatment	Control	T-C	Treatment	Control	T-C	Treatment	Control	T-C
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
<i>Total risk</i>	0.333	0.300	0.033*	0.332	0.299	0.033	0.351	0.311	0.040
<i>IVol</i>	0.320	0.290	0.030*	0.321	0.292	0.029	0.345	0.306	0.039
<i>Z-score</i>	0.284	0.331	-0.047**	0.286	0.331	-0.046**	0.269	0.334	-0.065*
<i>Ln(TA)</i>	7.796	7.759	0.037	7.659	7.627	0.032	7.400	7.380	0.020
<i>ROA</i>	0.013	0.012	0.002*	0.013	0.012	0.001	0.013	0.013	0.001
<i>Non-interest income/TA</i>	0.012	0.009	0.002**	0.011	0.009	0.002**	0.009	0.008	0.001
<i>Non-core deposits/TA</i>	0.106	0.128	-0.022**	0.100	0.126	-0.026***	0.099	0.123	-0.024
<i>Loans/TA</i>	0.623	0.620	0.004	0.630	0.619	0.011	0.664	0.637	0.027
<i>Ln(Market-to-book equity ratio)</i>	0.275	0.217	0.059	0.283	0.201	0.081	0.366	0.207	0.159*
<i>FREQ</i>	0.001	0.002	-0.001***	0.001	0.002	-0.001***	0.001	0.002	-0.001**
<i>State GDP growth</i>	0.047	0.043	0.005	0.049	0.044	0.005	0.049	0.041	0.008
<i>Ln(State population)</i>	15.730	15.440	0.290***	15.732	15.430	0.302***	15.705	15.509	0.196

Panel B: Diagnostics for the subsamples matched by bank size and bordering state for Table 10

Sample	31 matched pairs; mean (median) distance is 188.7 (142.6) miles		
	Treatment	Control	T-C
	(1)	(2)	(3)
<i>NPL/TA</i>	0.0032	0.0029	0.0003
<i>NPL/TL</i>	0.0052	0.0044	0.0008
<i>Total risk</i>	0.362	0.406	-0.045
<i>IVol</i>	0.338	0.382	-0.044
<i>Z-score</i>	0.319	0.324	-0.005
<i>Ln(TA)</i>	7.729	7.803	-0.074
<i>ROA</i>	0.016	0.015	0.001
<i>Non-interest income/TA</i>	0.014	0.011	0.002
<i>Non-core deposits/TA</i>	0.105	0.099	0.006
<i>Loans/TA</i>	0.603	0.629	-0.026
<i>Ln(Market-to-book equity ratio)</i>	0.505	0.609	-0.104
<i>FREQ</i>	0.002	0.002	-0.001
<i>State GDP growth</i>	0.067	0.054	0.013*
<i>Ln(State population)</i>	15.893	15.789	0.104

TABLE IA.6
Summary Statistics of the KLD-Merged BHC Sample

The table presents the summary statistics of the KLD-merged BHC sample. This sample consists of 314 (1,619 bank-year observations) publicly traded US BHCs that filed FR Y-9C reports with the Federal Reserve over 1991-2010. Bank fundamental information is downloaded from the Bank Regulatory Database. Bank stock information of the BHCs is downloaded from CRSP. Other accounting information and firm attributes are collected from Compustat. The state GDP and population data are downloaded from the US Bureau of Economic Analysis (BEA). To reduce the effects of outliers, we winsorize all continuous variables at the 1st and 99th percentiles.

Variables	Obs.	Mean	Std. Dev.	Min	25%	Median	75%	Max
<i>Total risk</i>	1,619	0.395	0.235	0.140	0.244	0.310	0.457	1.301
<i>IVol</i>	1,619	0.316	0.189	0.110	0.195	0.255	0.368	1.147
<i>Z-score</i>	1,619	0.344	0.190	0.013	0.211	0.322	0.437	1.124
<i>Deflated total assets (in mil.)</i>	1,619	46,929	178,321	429	2,096	4,768	18,647	2,063,178
<i>ROA</i>	1,619	0.013	0.015	-0.054	0.009	0.015	0.020	0.059
<i>Non-interest income/TA</i>	1,619	0.020	0.034	0.002	0.009	0.013	0.019	0.316
<i>Non-core deposits/TA</i>	1,619	0.144	0.091	0.012	0.082	0.120	0.186	0.501
<i>Loans/TA</i>	1,619	0.645	0.150	0.051	0.598	0.674	0.733	0.884
<i>Market-to-book equity ratio</i>	1,619	1.814	0.870	0.270	1.225	1.727	2.210	5.145
<i>FREQ</i>	1,619	0.005	0.006	0.000	0.002	0.003	0.005	0.091
<i>State GDP growth</i>	1,619	0.019	0.027	-0.100	0.007	0.019	0.034	0.126
<i>Ln(State population)</i>	1,619	15.965	0.912	13.249	15.540	16.004	16.368	17.435

Table IA.7
Evaluating the Inclusion Restriction Using the KLD Index

This table evaluates the inclusion restriction by regressing bank risk-taking on an alternative firm-level stakeholder orientation measure constructed based on KLD data. The dependent variables are bank total risk (*Total risk*), idiosyncratic risk (*IVol*) and Z-score (*Z-score*). The main explanatory variable of interest is *KLD*. To construct *KLD*, we follow the two-step approach of Deng, Kang and Low (2013). First, in each of the five dimensions—community, natural environment, product quality, employees and diversity—we standardize the number of strengths and concerns by the corresponding number of strength and concern indicators. Second, we sum the standardized ratings across the five dimensions for strengths and concerns, respectively, and then take the difference between the standardized total strength score and the standardized total concern score. This difference is *KLD* of which a larger value is assigned to a more stakeholder-oriented BHC. The bank and state variables are identical to those used in the baseline model. Panel A presents the regressions estimating with bank and year fixed effects. Panel B reports the one-step dynamic panel system GMM estimator developed by Arellano and Bover (1995) and Blundell and Bond (1998). We use the three-period lagged bank risk measures and all two-period lagged right hand side variables as instruments for the difference equation and the corresponding lagged differences as instruments for the regressions in level. We report the *p*-value of the Sargan test of over-identifying restrictions. Standard errors reported in parentheses are clustered at the bank level. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

Panel A: Bank Fixed Effects Models

	<i>Total risk</i>	<i>IVol</i>	<i>Z-score</i>
	(1)	(2)	(3)
<i>KLD</i>	-0.024*** (0.009)	-0.015* (0.008)	0.024* (0.013)
Bank controls	Yes	Yes	Yes
State controls	Yes	Yes	Yes
Bank FE	Yes	Yes	Yes
Year FE	Yes	Yes	Yes
Obs.	1,619	1,619	1,619
Adj. R ²	0.881	0.835	0.635

Panel B: Dynamic Panel Regressions

	<i>Total risk</i>	<i>IVol</i>	<i>Z-score</i>
	(1)	(2)	(3)
<i>Risk (-1)</i>	0.490*** (0.071)	0.465*** (0.075)	0.727*** (0.116)
<i>Risk (-2)</i>	-0.149** (0.067)	-0.096 (0.063)	0.127 (0.100)
<i>KLD</i>	-0.057*** (0.018)	-0.046*** (0.014)	0.058** (0.025)
Bank controls	Yes	Yes	Yes
State controls	Yes	Yes	Yes
Year FE	Yes	Yes	Yes
Obs.	981	981	981
Sargan <i>p</i> -value	0.646	0.697	0.232

References (Internet Appendix)

Arellano, M., Bover, O., 1995. Another look at the instrumental variable estimation of error-components models. *Journal of Econometrics* 68, 29-51.

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