Democratic Judges, Litigation Risk, and Voluntary Disclosure via 8-K Filings

Reeyarn Zhiyang Li *

Hong Kong University of Science and Technology

This draft: February, 2016†

Abstract

This paper develops an exogenous measure of litigation risk and studies how litigation risk affects the firm's voluntary disclosure. Specifically, I use the political party affiliation of federal court judges to measure the firm's litigation risk. This measure strongly predicts the filing of shareholders lawsuits, as well as the litigation outcomes. I find that with a higher proportion of judges being appointed by Democratic presidents in the firms' head-quarter circuit, these firms face a higher risk of shareholders class action, and these lawsuits are less likely to be dismissed. Using this measure, I find that with a higher litigation risk exposure, firms make fewer voluntary disclosure via SEC's Form 8-K, and especially for disclosure that contains material forward-looking earnings information. The effects are stronger among large firms, consistent with the notion that large firms have "deep pockets" and are more likely to be the target of shareholders lawsuits.

*I would like to thank my supervisor Kai Wai Hui for his precious guidance and generous support. This paper has benefited from the helpful comments from Kevin Chen, Szu Fan Chen, Allen Huang, Mingyi Hung, Derrald Stice, John Wei, Guochang Zhang, and seminar participants at 2015 EAA Talent Workshop and HKUST Accounting Workshop. All errors are my own.

†This is a very preliminary draft. Please do not cite or circulate without the author's permission.

1 Introduction

The threat of shareholders litigation is a major concern for corporations in their disclosure decisions. Litigation can affect the firm's voluntary disclosure in two ways (Healy and Palepu, 2001): First, litigation can increase voluntary disclosure, in that managers may have more incentives to release bad news in a timely manner[1] when facing a higher threat of potential legal actions against inadequate or untimely disclosure of bad news. Second, shareholders litigation can reduce managers' incentives to disclose their private information, and forward-looking earnings information in particular. This is also known as the "muzzling effect" of shareholders lawsuits on firm disclosure[2]: firms that disclose their own forecasts in good faith in ex ante may be penalized in shareholders lawsuits ex post, if bad news emerges and stock prices fall, and investors cannot distinguish between a genuine forecast error and deliberately manipulated forecast biases.

Prior studies on litigation risk and voluntary disclosure have been inconclusive. Some suggest a positive relation between litigation risk and disclosure. Cao and Narayanamoorthy (2011) use the Directors' and Officers' (D&O) liability insurance premium to measure litigation risk. They find that managers are more likely to issue bad news earnings forecast with a bigger D&O protection. Billings and Cedergren (2015) also find that when facing a higher litigation risk, firms are more likely to issue warnings of negative earnings news.

In contrast, others point to a negative relation between litigation risk and disclosure. Johnson et al. (2001) study the change in disclosure surrounding the passage of the Private Securities Litigation Reform Act of 1995 (PSLRA). They find that after PSLRA which reduces legal exposure, firms in high-tech industries issue more forward-looking disclosure. Baginski et al. (2002) compare voluntary disclosure made by US and Canadian firms. They find that with a less litigious environment, Canadian firms issue more earnings forecasts that are also more precise and of a longer horizon. Moreover, Rogers and Van Buskirk (2009) find that firms make fewer and less precise earnings forecast after being sued in a shareholders class action.

[1]Evidences in prior studies on earnings surprise and preemptive disclosure are mixed. Skinner (1994) documents that managers predisclose bad news more often in quarters with negative earnings news than in quarters with positive earnings news. In contrast, Francis et al. (1994) show that 87% of observations with large earnings decline do not predisclose the bad news until the formal earnings announcement.

[2]House Conference Report, (1995): Fear that inaccurate projections will trigger the filing of securities class action lawsuit has muzzled corporate management.

One major challenge that prior studies usually face is the endogeneity between litigation risks and voluntary disclosure. Firms with a higher ex ante litigation risk also have a higher tendency to predisclose bad news, and after their bad news predisclosure these firms are also more likely getting sued (Francis et al., 1994). It appears like more disclosure is associated with more lawsuits, even though more disclosure could increase transparency and reduce litigation cost (Skinner, 1997).

Another challenge is the lack of a good litigation risk measure. The researches so far have adopted several approaches in measuring litigation risk. The first approach, commenced by Francis et al. (1994), uses industry-level litigation risk to capture a firm's litigation risk exposure, and use high litigation industry membership (biotechnology, computers, electronics, and retailing), as a proxy for high litigation risk exposure. But as the industry membership does not change much over time, it is not a good predictor of actual lawsuits (Kim and Skinner, 2012), and thus not a good measure of litigation risk.

The second approach uses a firm's actual lawsuit occurrence as the dependent variable in a probabilistic prediction model, and uses the firm's stock price variables such as turnover and volatility, and firm characteristics, as input variables, to predict litigation risks for all the firms across the cross-section (Kim and Skinner, 2012). The advantage is that the predicted litigation risk has a larger variation over the cross-section and is more powerful in the tests, but it has endogenous problems, because it relies on the firm's actual litigation occurrence, as well as the firm's own stock price and earnings performance as input variables, which are both associated with the firm's voluntary disclosure, and these input variables invite endogeneity to the predicted litigation risk measure.

Others such as Cao and Narayanamoorthy (2011), use the D&O insurance premium as a measure of ex ante litigation risk. But since D&O insurance covers the liabilities of potential shareholders litigation, the firm's exposure to the risk is greatly reduced by the insurance protection. Besides, as Baker and Griffith (2007) has pointed out, the D&O insurer also plays a monitoring role in the firms' corporate governance and disclosure practices. As a result, the presence of the D&O insurance and its insurer adds an additional layer into the endogenous problem between litigation risk and disclosure. It is thus not a real exogenous measure of litigation risk.

This paper uses the political party affiliation of federal judges in the Court of Appeals as an exogenous measure of a firm's litigation risk. The rationales are twofold. First, the congress has divided the continental United States into twelve geographical appellate circuits (See Figure 1), and the twelve Courts of Appeals for each circuit have very different case law precedents, and they implement varying pleading standards for the shareholders class action lawsuits[3]. As a result, the chance of having a favorable ruling for the firm varies apparently among these twelve circuits. If a firm is located in a state with a circuit court that holds more stringent pleading standards for shareholder litigation, then the firm would face a lower litigation risk, as the plaintiffs would face a higher hurdle rate for passing the pleading standards.

Second, a Democratic president usually nominates federal court judges that promote the party's liberal policy agenda in general, and protect small equity investors more vigorously in shareholders lawsuits in particular. For example, Pinello (1999) finds that political party affiliation can explain up to 48 percent of ideological variance in court rulings, and Democratic judges are usually more liberal than Republican judges. As a result, if a firm's headquarter is located within a circuit with more Democratic judges, the firm faces a less corporate-friendly court were it be sued by shareholders. It is thus easier for plaintiffs to litigate the firms in these circuits, and these firms face a higher litigation risk.

Consistent with this prediction, I find that with a higher proportion of judges being appointed by a Democratic president in the Court of Appeals for the firms' headquarter circuit ("Democratic judges"), these firms face a higher rate of being sued in a shareholders class action. The result is robust after controlling for industry membership and other firm-specific variables pertaining to litigation. To further alleviate the endogeneity concerns, I also control for other variables such as state level GDP growth, unemployment rate, and presidential election outcomes. Moreover, with more Democratic judges in the Court of Appeals, the shareholders lawsuits are less likely ended up being dismissed, after controlling for the estimated damages of the case and the type of specific allegations in the complaint filings.

In other words, with more Democratic judges in the firms' headquarter circuit, these firms face a higher litigation risk, and also a higher cost to settle the lawsuits. These results are

[3]For example, different circuit courts have very different readings on the statutory Safe Harbor for Forward-Looking Statements; see section 2.1.3 for a more detailed discussion.

not subject to endogeneity, as the measure of Democratic judges is exogenously determined: the process by which a Democratic president appoints federal court judges is out of control by individual companies, equity investors, and shareholder litigation attorneys. As a result, Democratic judges can serve as an exogenous measure of litigation risk.

Using Democratic judges as a measure of litigation risks, I then examine how litigation risk affects firms' voluntary disclosure. I retrieve the firms' 8-K filings from SEC's EDGAR website and extract the press release attached in the Form 8-K to construct measures of voluntary disclosure (Cooper et al., 2015). I find that with more Democratic judges in the firms' headquarter circuit, firms are less likely to provide voluntary disclosure to the market, the frequency reduced, and the timing delayed. The results are stronger for disclosure that contains material forward-looking earnings information, and stronger among large firms, consistent with a litigation explanation.

These results are not inconsistent with the literature. Prior studies such as Field et al. (2005) and Billings and Cedergren (2015) only examine the disclosure in the quarter of big negative earnings news, about litigation risk and firms' warning of quarterly bad earnings surprise. In contrast, this study examines the firm's voluntary disclosure in general, including disclosure of both good news and bad news. Consistent with Rogers and Van Buskirk (2009), I find that the firm reduces or delays its voluntary disclosure when facing a higher litigation risk.

This study contributes to the literature in the following ways. First, it suggests a novel measure of litigation risk that is truly exogenous to the firm, which circumvents the endogeneity problem that prior studies on litigation and disclosure have long been trying to solve (Field et al., 2005). Second, this paper finds that in circuits with more Democratic judges, the firms face a higher risk of being sued by shareholders. While prior legal studies generally find that the political party affiliation can explain judges' court rulings, to my best knowledge this is a first paper that documents judges' political party affiliation can also affect the choice of plaintiffs in picking potential defendants to file a lawsuit complaint.

Third, using Democratic judges to measure litigation risk, this paper finds that firms reduce their voluntary disclosure with a higher litigation risk. This finding extends the results in Rogers and Van Buskirk (2009) that firms reduce voluntary disclosure after being sued. Fourth, this

paper is among the early studies that construct measures of voluntary disclosure using the firm's Form 8-K filings to the SEC. The advantage of this approach is that the voluntary disclosure measures cover a broader sample and are not affected by the selection bias of the CIG database used by prior studies (Chuk et al., 2013).

Section 2 reviews the institutional background about judges, litigation, and disclosure, and develops the paper's hypotheses. Section 3 describes the data of judges and lawsuits, and reports the results of the litigation test. Section 4 reports the disclosure test results. Section 5 concludes.

2 Institutional Background and Hypotheses

2.1 Federal Judges and Shareholders Lawsuits

In this section, I discuss the federal court judges in relation to shareholders lawsuits, where judges make judicial decisions and determine the outcome of the lawsuits.

2.1.1 Structure of Federal Courts

The modern structure of the U.S. Federal courts consists of three layers: the district court for initial trial, the court of appeals for the appeal as of right, and the Supreme Court for the discretionary final review (Baker, 2009). The 50 states in the U.S. are geographically defined into 11 numbered circuit regions, plus the D.C. circuit. There is one Court of Appeals in each circuit. In each of the 50 states, there are from one to four district courts, and there are 89 district courts in the 50 states in total. Figure 1 shows the map of the geographical boundaries of the circuit court of appeals and the underneath district courts[4].

[Insert Figure 1 Around Here]

[4] http://www.uscourts.gov/file/document/us-federal-courts-circuit-map

The district courts have *original jurisdiction*, namely to hear a case for the first time, for civil cases brought under a federal law, whenever the defendants can be found within the boundary of the district[5]. The district court can witness evidence and testimony, make factual and legal determinations regarding the material presented, and make judicial decisions regarding remedies for the civil liability cases, such as securities class actions. Parties who disagree with the district court's decisions are allowed to make one appeal to the upper level, the Court of Appeals, for the circuit that the district court is in.

Significance of Court of Appeals The courts of appeals are among the most influential courts in the United States. Because they have direct judicial supervision of the district courts within the circuits, and they are able to set legal precedents in their circuit regions that cover several states, they are viewed as having strong policy influence on US law. They are the "norm enforcers" and "important creators of public policy" (Songer et al., 2000). Although the Supreme Court can, at its sole discretion [6], choose to review any lower court ruling, it is extremely rare for average cases to be reviewed by it. While the Supreme Court's decisions are of paramount importance, the decisions by Court of Appeals are far more numerous[7], and are of much greater practical influence collectively (Howard Jr, 2014).

2.1.2 Judges' Ideological Preferences and Judicial Decision Making

Law schools commonly teach that judges make judicial decisions based on no more than legal reasons — a neutral application of the statutes set by the Congress and the precedents made in

[5]28 U.S. Code 1391: (b) Venue in General. — *A civil action may be brought in — (1) a judicial district in which any defendant resides*, if all defendants are residents of the State in which the district is located; ... (c) Residency. — For all venue purposes — ... (2) an entity with the capacity to sue and be sued in its common name under applicable law, whether or not incorporated, shall be deemed to reside, if a defendant, in any judicial district in which such defendant is subject to the courts personal jurisdiction with respect to the civil action in question ... (d) Residency of Corporations in States With Multiple Districts. — For purposes of venue under this chapter, in a State which has more than one judicial district and in which a defendant that is a corporation is subject to personal jurisdiction at the time an action is commenced, *such corporation shall be deemed to reside in any district in that State within which its contacts would be sufficient to subject it to personal jurisdiction* if that district were a separate State, and, if there is no such district, the corporation shall *be deemed to reside in the district within which it has the most significant contacts. ...*

[6] In 1925, Congress dramatically expanded the Supreme Courts discretion over which case to review via the passage of The Judiciary Act of 1925.

[7]Today the Supreme Court would chooses to review only less than 1% of the more than 10,000 cases filed with it annually (Cordray and Cordray, 2001)

earlier court decisions; this is known as the *legal model* of judicial decision making. However, this view is challenged by the legal realist movement in early 20th century (Leiter, 2002), as the legal materials available to judges, such as statutes and precedents, may not uniquely dictate a clear decision, and consequently, the legal outcomes are also determined by the minds of individual judges, and their policy preferences are likely to come into play.

Political scientists also propose at least two alternative theories. First, the *political model* [8] contends that the judicial decisions are instead driven by the personal ideologies of judges, which generally fall along a liberal-to-conservative continuum (Sisk et al., 1998). Judge Posner, who serves as a judge on the United States Court of Appeals for the Seventh Circuit, suggests that judges may wish to "*impose their political vision on society through rulings*", just as an artist imposes an aesthetic vision on society (Posner, 1995). Second, the *strategic model* predicts that judges make decisions that are least likely to be reversed by other institutions such as an upper level court.

Many legal empirical studies[9] use the party of the judge's appointing president as a proxy for the judge's own political ideology, where it is presumed that judges appointed by Reagan are likely to make more conservative decisions than judges appointed by Clinton. This presumption is well grounded in political science[10]: in selecting nominees of a federal judge, presidents employ a mix of criteria that includes agreement with the president's basic political and constitutional philosophy or more simply, ideology [11], as well as other criteria such as professional qualification and personal friendship (Gerhardt, 2003; Law, 2004).

Pinello (1999) analyzes 84 legal studies on judges' political party affiliation and the judicial ideological decision making, and finds that political party affiliation explains up to 48 percent of ideological variance in non-unanimous federal court rulings. He concludes that Democratic judges are more liberal on the bench than Republican judges.

[8]The political model is also known as the attitudinal model, see Cross (1997) for a good review.

[9]For example, Goldman (1975) found that the party of the president who appointed the judge can explain a significant portion of variance in judicial decisions by court of appeals judges, for criminal procedure (9.2%), civil liberties (8.8%), labor welfare (17.7%) and economic liberalism such as (de)regulation of the government (15.2%).

[10]For example, (Gerber and Park, 1997) view it a standard assumption that Republican judges tend to reach more conservative decisions than do Democratic judges.

[11]The Republican platform of 1980 openly proclaimed that "We pledge ... the appointment of women and men ... whose judicial philosophy ... is consistent with the belief in the decentralization of the federal system and efforts to return decision making power to state and local elected officials. We will work for the appointment of judges at all levels of judiciary who respect traditional family values and the sanctity of innocent human life. "

2.1.3 Shareholders' Class Action Lawsuits

A securities litigation is a private lawsuit filed by investors who, with reliance on a company's misleading disclosure or omissions of material information, purchased the company's securities at inflated prices and suffered economic damages. It is a civil liability lawsuit arising under the Securities Exchanges Act of 1934 ("The 1934 Act") Section 10b, and the SEC's Rule 10b-5 promulgated thereunder, which prohibits *"any person ... (b) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading ... in connection with the purchase or sale of any security."* As most securities litigations arise under the 1934 Act and SEC's Rule 10b-5, these cases belong to federal-question jurisdiction category and are contested in the venue of federal courts[12].

The wordings of the 1934 Act and SEC's Rule 10b-5 have long been viewed by law scholars and practitioners as using too general terms, and it provides room for judges to make decisions in various factual situations. Over its history of more than 70 years, the federal courts' evolving interpretations of SEC's Rule 10b-5 have largely defined it. Since the first shareholder lawsuit filed in 1946, thousands of cases have been brought to the courts under Rule 10b-5, and various legal issues have been heavily contested. The judges have developed a set of pleading requirements, for which the lawsuit complaints must satisfy by providing factual allegations in the complaints, with strength and specificity, of the wrongdoings done by the company and its officers.

Divergence of opinions among circuit Court of Appeals over 10b-5 lawsuits Courts of Appeals in the US have promulgated very divergent legal standards for pleading securities class actions in different circuits (Pritchard and Sale, 2005). Shareholders lawsuits are carried out differently in the circuits, known as *circuit split* in the law literature (Wallace, 1983). The circuit courts of appeals disagree on a range of issues about shareholders class action lawsuits arising from SEC's Rule 10b-5, with varying pleading requirements for scienter (Guido, 2000;

[12]"The district courts shall have original jurisdiction of all civil actions arising under the Constitution, laws, or treaties of the United States." 28 U.S. Code 1331.

Miller, 2011), loss causation (Hill, 2009), investors' reliance on the firm's disclosure (Silverman, 2010), and application of the Safe Harbor for forward-looking statements (Wang, 2006).

PSLRA and Safe Harbor for forward-Looking disclosure There have been heated debates concerning whether the private securities litigation can help deter fraud and protect investors, or, to the contrary, whether too many frivolous shareholders' lawsuits have been brought under Rule 10b-5, usually at the cost of shareholder's net wealth, as remedies claimed by a group of shareholders will almost always come out of the pockets of another groups of shareholders (Arlen and Carney, 1992). In the 1990s the Congress stated that it had observed "significant evidence of abuse in private securities lawsuit" , where class action lawyers routinely file complaints against deep pocket companies, sometimes completely meritless, whenever there is a significant drop in its stock price House Conference Report, (1995).

These debates have led to the passage of the Private Securities Litigation Reform Act of 1995 (PSLRA, or the "Reform Act"). The Reform Act raises the pleading standards to a heightened level, and makes it much harder for investors to file a 10b-5 lawsuit against corporations. However, it also introduces new problems, as the Reform Act adopts a set of languages that are sometimes "ambiguous and even contradictory" as viewed even by the courts[13].

One major change to shareholders lawsuits brought by PSLRA is the statutory Safe Harbor for Forward-Looking Statement ("the Safe Harbor"). The creation of Safe Harbor was intended to give corporations the freedom to provide forward-looking disclosure and protect them from 10b-5 lawsuit liabilities for making such disclosure (House Conference Report, (1995)). It states that a company "shall not be liable with respect to any forward-looking statement, whether written or oral, (I) if and to the extent that the forward-looking statement is identified as a forward-looking statement, and is accompanied by *meaningful cautionary statements* identifying important factors that could cause actual results to differ materially from those in the forward-looking; or immaterial; (II) or the plaintiff fails to prove that the forward-looking statement . . . was made with actual knowledge . . . that the statement was false or misleading."

[13]In re Advanta Corp. Sec. Litig., 180 F.3d 525, 531 (3 rd Cir. 1999) ("The Reform Act's legislative history on this point is ambiguous and even contradictory.").

The prongs are joined by the disjunctive term "or", meaning that shareholders have to prevail on both prongs to survive a motion to dismiss. According to the plain text of Safe Harbor and its legislative history as is in House Conference Report, (1995), a motion to dismiss under the first prong does not depend on the "state of mind". Thus, even a knowingly false or misleading statement is protected by the Safe Harbor, as long as it is accompanied by adequate "meaningful cautionary statements" (Schneider and Dubow, 1996).

Das (2010) argues that the first prong of the Safe Harbor contradicts a basic goal of securities acts, as the Supreme Court ruled that the 1934 Act were designed to protect investors against fraud and to promote ethical standards of honesty and fair dealing (Ernst & Ernst v. Hochfelder). Senators Sarbanes and Boxer (both Democrats) also expressed their concerns that the Safe Harbor in PSLRA has effectively created "a license to lie".

Split of opinions among circuit Court of Appeals over the Safe Harbor Judicial readings of the statutory Safe Harbor vary widely among different circuit courts. Some courts follow the plain text of the Safe Harbor, and hold that as long as the company identifies the forward-looking statement as such, and provides sufficient cautionary warnings, the first prong is satisfied, and it is protected under the Safe Harbor, disregard of the second prong or the defendant's state of mind. For example, the Sixth Circuit took this interpretation in its ruling in *Miller v. Champion Enterprises* (6th Cir. 2003).

A contrary reading takes into consideration the defendant's state of mind in the analysis of the first prong. As long as the plaintiffs successfully allege that the forward-looking statement is made with the company's actual knowledge that it is false and misleading, the cautionary statement cannot be deemed "meaningful", and the defendant is not protected under the Safe Harbor. For example, the Ninth Circuit states that a "strong inference of actual knowledge" will except the forward-looking statement from the safe harbor protection altogether (*In re SeeBeyond Technologies Corp. Securities Litigation*, 9th Cir. 2003).

The divergent opinions on the interpretation of the Safe Harbor hinge on the word "meaningful" in its text. As the Seventh Circuit Judge Easterbrook has pointed out in a widely cited

ruling, *Asher v. Baxter, 7th Cir. 2004*, that "the fundamental problem is that the statutory requirement of 'meaningful cautionary statements' is not itself meaningful", and "it is the result of a compromise between legislators...Compromises of this kind lack spirit...and we must make something of it." The ambiguities in the plain text of the Safe Harbor obviously leave much room for judges to exert discretion in judicial decisions. And judicial decisions are affected by a judge' ideological preferences, which in turn, are associated with the judge's political party affiliation.

As is discussed in section 2.1.1, the Courts of Appeals have great influence on the district court's rulings, and thus on the policy implications for shareholders lawsuits, and on the firms' litigation risks. Other things being equal, Democratic judges would favor the underprivileged parties in a lawsuit, which is the class of investors in the context of a shareholders lawsuit, as against the defendant corporation and its officers. If both the investors and the plaintiff lawyers are aware of the above knowledge, with other things being equal, they would choose to file shareholders lawsuits against those firms whose Court of Appeals comprises of more Democratic judges. As a result, these firms would face a higher litigation risk. Thus, I state the first hypothesis (in alternative form) of this article as follows:

Hypothesis 1 *Ceteris paribus, when there are more Democratic judges in the Court of Appeals for the firms' headquarter circuit, the firm faces a higher litigation risk.*

2.2 Voluntary Disclosure

Management provided forward-looking information is useful in the financial market (Seligman, 1994; Anilowski et al., 2007). Investors rely heavily on management's forecasts of future earnings, sales, and other financial statement items, in evaluating firm value and making investment decisions (Clement et al., 2003); analysts also view management's earnings forecasts critical to their stock recommendations (Chen and Matsumoto, 2006). For these reasons, the Securities and Exchange Commission encourages firms to disclose forward-looking information (SEC, 1979; SEC, 1994).

When it is costless to make disclosure and impossible to lie, firms would always disclose all the good news to boost the stock price (Milgrom, 1981). However, when making disclosure incurs certain costs, such as giving the opponents an undue advantage in product market competition (Verrecchia, 1983), hiring an external party to verify the disclosure (Ball et al., 2012), or increasing the firm's exposure to the risk of being sued in a shareholders' class action (Morgan, 2003), the firms would make less disclosure.

Litigation can affect the firm's voluntary disclosure in two ways (Healy and Palepu, 2001). First, a higher litigation risk can compel firms to make more transparent disclosure and release bad news early (Skinner, 1994; Kothari et al., 2009). Yet the empirical results for this prediction are mixed. For example, Francis et al. (1994) show that most firms with large earnings decline do not predisclose the bad news until the formal earnings announcement. Second, litigation risk may deter the issuance of forward-looking disclosure. This is known as the "muzzling effect" of private securities class action on disclose in the legal community (Seligman, 1994). Managers could be reluctant to make forward-looking earnings forecasts in the fear that the negative forecast errors simply due to bad luck may trigger shareholder lawsuits if stock prices decline sharply. A survey study by Graham, Harvey, and Rajgopal (2005) suggests that managers view the threat of litigation as a major concern that deters them from making forward-looking disclosures to the public.

These conflicting views motivate this paper's main research question: How does a firm's litigation risk affect its voluntary disclosure decisions? Following my reasoning in Section 2.1 and the Hypothesis 1, I state my second hypothesis (in alternative form) as follows:

Hypothesis 2 *Ceteris paribus, when a firm faces a higher litigation risk, the firm tends to make* fewer *voluntary disclosure.*

Firm size and litigation risk Large firms are usually the more likely targets for shareholders lawsuits (Field et al., 2005), perhaps because of their "deep pockets" for providing large settlements. If consistent with my Hypothesis 2, the empirical results demonstrate a statistical association between Democratic judges and voluntary disclosure, and the effect on voluntary disclosure is really driven by litigation risks, then the association should be more pronounced in the large firms sample, as large firms face a higher litigation risk.

Forward-looking earning disclosure and litigation risk Providing forward-looking information to the market makes a firm more vulnerable to shareholders lawsuit allegations (House Conference Report, 1995; Johnson et al., 2001), and it is risker than providing non-forward-looking disclosure.

In terms of materiality, earnings-related forward-looking disclosure is more *material* than non-earnings-related ones. The Supreme Court has defined an information as *material* if the information "might have been considered important by a reasonable" investor, and if it has "a significant propensity to affect" investors[14]. Forward-looking earnings disclosure are more material than disclosure of other types of information, because when actual realizations are announced in later periods, stock price reacts more strongly when a previous forecast is not met (Morgan, 2003). Thus, I postulate that the effect of litigation risk on voluntary disclosure would be stronger for forward-looking earnings disclosure, stated below:

Hypothesis 2a *Ceteris paribus, when a firm faces a higher litigation risk, the firm tends to make* fewer *forward-looking earning disclosure.*

3 Empirical Tests of Judges and Lawsuits

This paper has two sets of empirical tests. The first set of tests examines whether Democratic judges do affect a firm's litigation risk exposure (the lawsuit test). The second set of tests examine how litigation risks, as measured by Democratic judges, affect firms' voluntary disclosure (the disclosure test). This section reports the results for the litigation test, and the next section reports the disclosure test.

In the subsections below, I first describe the data of judges in section 3.1, and specify the data for the lawsuit tests in sections 3.2. Section 3.3 and 3.4 reports the design and the empirical results for the lawsuit tests.

[14]In Mills v Electric Auto-lite Co., 396 U.S. 375 (1970).

3.1 Democratic Judges Data

This study measures a firm's litigation risk using the political party affiliation of federal court judges, who would determine the outcome of a lawsuit were the firm actually sued by investors. As discussed in previous sessions, the idea is that a Democratic judge would be more inclined to protect small investors than one from the Republican Party, which is more aligned with the interest of big corporations. As a result, judicial decisions made by a Democratic judge would be less favorable to the firm, were it actually sued to face a court. I use the number of federal judges that have been appointed by a Democratic president, in the Circuit Court of Appeals, to construct the measure of litigation risk. I look into the Court of Appeals, which adjudicates over the District Court where a shareholders lawsuit against the firm would be filed.

In particular, for each firm-quarter, I calculate the litigation risk measure *Dem_Judges* using the estimated probability that a three judges panel in the Court of Appeals is dominated by Democratic judges, where the Court of Appeals adjudicates over the district which the firm headquarters' main contact address is located in[15].If the total number of judges currently serving at the Court of Appeals that have been appointed by a Democratic President is D, and the total number of judges in the court is N, both are as of the beginning of the quarter, then the probability that a randomly assigned three-judges panel would be dominated by at least two Democratic judges equals

$$\text{Dem\_Judges} = \left(\binom{D}{3} + \binom{D}{2} \binom{(N-D)}{1} \right) / \binom{N}{3}$$

I obtain a dataset of judicial appointment history from the Federal Judicial Center (FJC) website[16], which provides the biographical data of all the federal judges since 1789, including the name of the judge, the specific court the judge served, the date on which the judge was appointed, the name of President who appointed the judge, the date on which the judge terminated service on the court, and the particular reason (fully retire, resign, die, be elevated to another court, or be removed from office) for which the judge terminated the service.

[15] 28 U.S.C. §1391: (b) Venue in General. — *A civil action may be brought in — (1) a judicial district in which any defendant resides*, (2) ... (d) Residency of Corporations in States With Multiple Districts. *...the corporation shall be deemed to reside in the district within which it has the most significant contacts.*

[16] `http://www.fjc.gov/public/home.nsf/hisj`

[Insert Table 1 Around Here]

Table 1 summarizes the litigation risk measure, *Dem_Judges*. Panel A shows the summary statistics of the litigation risk measure by each circuit. Notably, the 9th circuit has the highest proportion of Democratic presidents appointed judges, followed by the 2nd circuit. These two circuits have a percentage of Democratic judges of over 50%. Compared with other circuits courts, these two circuits also happen to have relatively low pleading requirements for 10b-5 class action lawsuits, especially for the 9th circuit (Forseter, 1974; Stoker, 2010). Panel B shows the summary statistics of the litigation risk measure by year, which demonstrates a decreasing (increasing) trend during Bush (Clinton, and Obama) years.

3.2 Shareholders Lawsuits Data

I obtain the data of 3,898 cases of shareholders class action from Stanford Law School Securities Class Action Clearinghouse (SCAC) website during 1996–2014. I exclude lawsuits against firms not traded on NYSE, AMEX, NASDAQ, or firms with headquarter outside US, or lawsuits not involving Rule 10b-5 claims. After that, I match the name of defendants with the company names in CRSP. After this process, 1,485 cases remain in the sample. After requiring non-missing control variables, 315 more observations are dropped. My final sample consists of 92,396 firm-years, including 1,170 lawsuit cases, which overlap with 2,399 firm-year observations. Table 2 shows the process of litigation occurrence data.

[Insert Table 2 Around Here]

For the 1,170 cases in our lawsuit sample, 1,103 have known litigation outcomes. 33% of the cases have reached a settlement between firms and shareholders, and 61% have been dismissed by the court with prejudice, which means the case has been closed without any settlement payment offered by the company.

3.3 Test of Lawsuit Occurrence

Univariate Test Hypothesis 1 postulates that when there are more Democratic judges, the firm faces a higher litigation risk. To test this prediction, I partition the whole sample into five groups by the quintiles of *Dem_Judges*, and compare the chances at which a firm is involved in a shareholders class action. The statistics are shown in Table 3.

[Insert Table 3 Around Here]

In Panel A, Table 3, for 92,396 firm-year observations, 2.60% are involved in a lawsuit. For the lowest *Dem_Judges* quintile (Q1), 2.09% of observations are involved in a lawsuit. In comparison, for the highest *Dem_Judges* quintile (Q5), 3.90% of observations are sued. The differences between that in Q1 and Q5 are statistically significant; the t-statistics for the two samples comparison of average rate of lawsuit is 10.14, significant at less than 0.01 level.

Francis et al. (1994) note that in certain industries (FPS industries: biotech, computer, electronics, and retails) firms have a higher chance of being sued by shareholders. To examine whether the explanatory power of *Dem_Judges* exists after controlling for the high litigation risk industries membership, I partition the full sample by both FPS and *Dem_Judges* quintiles. Panel B and C shows the percentages of being sued in Non-FPS- and FPS- industries, respectively. Within each group of industries, the differences between Q1 and Q5 of *Dem_Judges* are always significantly positive. And the magnitude of the differences is larger for FPS industries in Panel C, suggesting that the measure *Dem_Judges* does capture an aspect of the firms' litigation risk exposure that is orthogonal to FPS industries.

Multivariate Logit Test To test if judges' political party affiliation can predict lawsuit occurrence, I follow Kim and Skinner (2012) and adopt their litigation risk prediction model, and augment it with my measure of litigation risk Dem_Judges,

$$Logit(SUED) = f(Dem\_Judges, controls\_liti) + \varepsilon \tag{1}$$

where the *controls_sued* contains a vector of factors identified by Kim and Skinner (2012) that predicts litigation occurrence: *FPS*, *Size*, *SalesGR*, *RetSD*, *Return*, *RetSkw*, *Turnover*. To control for the industry risk factors that could potentially drive litigation, I also control for the return and volatility of the industry portfolio, *IndRet* and *IndRetSD*, respectively. To alleviate the concern that the results could be affected by the time varying factors or state level local economic factors other than judges per se being over-captured by Dem_Judges, I also control for the market return *MktRet*, the state's GDP growth *GdpGr*, local unemployment rate *Unemp*, and state level presidential election outcomes *BlueState*. Details of these variables are in Appendix A.

[Insert Table 4 Around Here]

Table 4, Panel A, presents the results of this test. Column (1) shows the results of the baseline model, which only includes the controls used by Kim and Skinner (2012): *FPS*, *Size*, *SalesGR*, *RetSD*, *Return*, *RetSkw*, *Turnover*. As expected, *Dem_Judges* is associated with a higher rate of litigation occurrence, with the coefficient being 1.088, significant at below one-percent level. With one standard deviation increase of *Dem_Judges*, the litigation risk would increase by 0.42%. This number is economically significant, noting that the average litigation is only 2.60%. Translating the economic effect into relative terms, with one standard deviation increase of *Dem_Judges*, the chance of being sued increases by 16% relatively.

Column (2) adds additional variables into the logit model: the market and industry controls *MktRet*, *IndRet*, *IndRetSD*, and state level variables *GdpGr*, *Unemp*, and *BlueState*. The association between *Dem_Judges* and litigation occurrence is still significant, now being 0.863, significant at below one-percent level.

Column (3) adds the circuit fixed effect, to test if the result survives after removing between-circuits differences among the observations. With only time-series variations of *Dem_Judges* being present, the coefficient on *Dem_Judges* now equals 1.744, even larger than that in Column (4), suggesting that the effect of *Dem_Judges* on lawsuits is not solely driven by cross-sectional differences between different circuits. With one standard deviation increase of *Dem_Judges*, the

chances of being sued increase by 0.67% (relatively 26%). In comparison, with one standard deviation increase of FPS, the chances of being sued increase by 0.49% (relatively 19%), in the same equation.

In Column (4), I replace the circuit fixed effect with the state fixed effect. The result on *Dem_Judges* is unaffected.

3.4 Test of Litigation Outcomes

Most of the shareholders lawsuits are either dismissed by the court or settled by a cash payment from the firm to the class of shareholders. If *Dem_Judges* can predict the litigation outcomes of these lawsuits, it provides more evidence that the measure captures the firm's litigation risk exposure. In particular, if more Democratic judges are associated with a smaller chance of cases being dismissed, then the firm faces higher necessity of making cash payment to settle the case, and it means *Dem_Judges* is positively associated with the cost of litigation.

To test if *Dem_Judges* is associated with the cost of litigation, I employ the following logit model.

$$Logit(Dismissed) = f(Dem\_Judges, controls\_dismissed) + \varepsilon \tag{2}$$

where the *controls_dismissed* contains firm characteristics such as *FPS*, *Size*, *IO*, state level controls *GdpGr*, *Unemp*, *BlueState*, as well as case specific variables, *Damage*, *IsGaapv*, and *IsInsider*.

I include the estimated shareholders damage during the class period *Damage*, as a control for the merit of the lawsuit. Following Skinner (1997), *Damage* is calculated as the log of one plus (MVE · Ret · (1- (1-Turnover)^X), where MVE is the market capitalization of equity before the end of the class period, Ret is the stock return cumulated over the class period, Turnover is the average trading volume as a percentage of shares outstanding during the class period, and X is the length of the class period. The individual stock price variables used to calculate *Damage* are not included in the equation. I also controls for the specific types of the allegations

in the complaint: whether the case involves GAAP violation *IsGaapv*, or illegal insider tradings *IsInsider*.

The results of this test are reported in Panel B, Table 4. Column (1) reports that *Dem_Judges* is associated with a lower rate of case dismissal, with the coefficient being -1.210. *Damage* also has a negative coefficient, suggesting that when cases are more severe, it is less likely being dismissed.

Column (2) test the model for cases with no specific allegations, and column (3) for cases with allegations of either GAAP violation or illegal insider trading. *Dem_Judges* is significant in (2), but not in (3). It seems that the dismissal result is driven by cases without specific allegations. This result is reasonable, as when cases have no specific allegations, it leaves the judges with a larger gray area to make their decisions, and *Dem_Judges* has a stronger explanatory power in this situation.

Overall, the measure *Dem_Judges* predicts both the filing of shareholders lawsuits and the litigation outcomes. Using *Dem_Judges* as a litigation risk measure is thus valid and economically meaningful.

4 Empirical Results of Disclosure Test

4.1 Designing Disclosure Test

Voluntary Disclosure Data

I measure voluntary disclosure using SEC's Form 8-K. It is a valid source of data for voluntary disclosure because SEC has required firms that voluntarily disclose "non-public financial information" also furnish to SEC a Form 8-K within five business days of the disclosure (SEC, 2003, Release No. 33–8176). It was first proposed as "Item 12" in 2002, then re-numbered as "Item 2.02" in August 23, 2004.

The reason for not using the company issued guidance (CIG) in the First Call historical database is that, as documented by Chuk, Matsumoto, and Miller (2013) , CIG covers the

firms with more analyst following, higher institutional ownership, and better prior performance. These factors are associated with both the CIG coverage of disclosure and the firm's intrinsic litigation risk.

Form 8-K has both mandatory and voluntary disclosure (Lerman and Livnat, 2010). To make sure my measure captures only voluntary disclosure, I screen Form 8-K by its item titles, and keep only the following voluntary items: Item 2.02 Results of operations and financial condition, Item 7.01 Regulation FD disclosure, and Item 8.01 Other events (Cooper et al., 2015).

For each Compustat firm-quarter, I match an 8-K filing with it if the 8-k filing date falls within the window of one day after the lagged quarterly earnings announcement date to the week prior to the earnings announcement date of the current quarter, so that it would not capture earnings announcement furnished via Form 8-K.

The sample for disclosure test starts with the Compustat-CRSP merged file for fiscal year end date during November 2004 and December 2013. It begins on November 2004, as SEC promulgated a new rule about Form 8-K on Aug 23, 2004 (SEC, 2004), and amended the item lists and disclosure requirements for SEC registrants (Lerman and Livnat, 2010).

[Insert Table 5 Around Here]

Panel A of table 5 reports the composition of the voluntary disclosure data. 997,093 Form 8-K's filed during August 2004 and December 2014 are retrieved from SEC's EDGAR website. 526,426 of which contains either Items 2.02, 7.01, or 8.01. After matching with Compustat/CRSP firm quarters by CIK, and requiring the filing date to be during one day after prior quarter's earnings announcement date till the week prior to current quarter's earnings announcement date, 231,031 Form 8-K's remain. After requiring non-missing variables for disclosure test, 102,580 Form 8-K's are in the final dataset, including 30,988 filings with Item 2.02, 28,584 ones with Item 7.01, and 43,942 ones with Item 8.01.

Parsing Form 8-K For each filing, I first remove those sentences that are likely a boilerplate statement, if they contains any keywords related with legal language, such as "hereunder", "pursuant to" (Li, 2010), or any keywords that are typically used by the PSLRA's cautionary statements, such as "forward-looking", "safe harbor", etc. A full list of keywords for boilerplate contents are in Appendix B.

Following Li (2010), for each remaining sentence, I classify it as containing forward-looking disclosure if it contains keywords that indicate future tense. Any sentence that is in past perfect sense is not classified as forward-looking, nor is one that announces the schedule of a conference call immediately following the filing. A full list of keywords for identifying forward-looking statements is in Appendix B.

These forward-looking sentences are identified as earnings-related if they contain both forward-looking statement keywords and any of the keywords directly related with earnings: earning, eps, income, profit, loss.

Panel B of Table 5 shows in each year the number of VD 8-K's, number of those that are forward-looking, and number of those that are both forward-looking and are earnings-related disclosures. Around 86% of all the VD 8-K's in the full sample are identified as forward-looking, and around 32% of them are forward-looking and related with earnings.

Specs for the Disclosure Test

To examine how litigation risks affect voluntary disclosure, I study the model

$$\textit{Voluntary Disclosure}_q = f(\textit{Dem\_Judges}, \textit{controls}) + \varepsilon \tag{3}$$

Following Ajinkya et al. (2005), I examine a firm's quarterly voluntary disclosure in three aspects: issuance, frequency, and horizon.

Issue = 1 if the firm issues an VD 8-K during the quarter, and 0 otherwise.

Freq = Natural log of one plus the number of VD 8-K's that a firm issues during the quarter.

Horizon = Natural log of one plus the number of days between a quarter's first VD 8-K to its quarterly earnings announcement date, and 0 if there is no any VD 8-K during the quarter.

Control variables For the control variables, I obtain financial statement data from Compustat, stock price data from CRSP, analyst following data from I\B\E\S, institutional holdings data from Thomson Reuters Financial.

The literature suggests a list of control variables. First, I control for firm size.

Size = firm's market capitalization, measured at the beginning of quarter.

Empirical studies on disclosure almost always include firm size in the test model. Larger firms face a higher demand for information, and their disclosure are more visible in the market. Waymire (1985) notes that larger firms have a higher chance of being covered by Wall Street Journal when they make a disclosure. The ex ante prediction on *Size* is positive, as prior studies suggest that larger firms makes more voluntary disclosure (Ajinkya et al., 2005).

I also include leverage ratio as a control variable. The predicted sign on leverage is also positive, as lenders could have a monitoring effect on corporate disclosure.

Lev = firm's leverage ratio, measured at the beginning of quarter.

To control for proprietary cost and growth opportunity, I include research and development expense and market-to-book ratio.

RD = firm's research and development expense, scaled by total assets.

MB = firm's market-to-book ratio, measured at the beginning of quarter.

Lev and Zarowin (1999) argue that historical information in mandatory reports becomes less relevant for firms with more intangible investment and more growth opportunities. These firms may face a higher demand for information from voluntary disclosure, to supplement the information provided by mandatory reports. As a result, R&D could be positively associated with disclosure. On the other hand, R&D intensive firms and firms with higher valuation multiples tend to have a higher proprietary cost (Verrecchia, 1983), and are expected to make fewer disclosures. The predictions on RD and MB are both two-ways.

Concurrent earnings affect the firm's decision to make voluntary disclosure (Miller, 2002). Following Rogers and Van Buskirk (2013), I include three variables to control for concurrent earnings news:

Loss = one if the firm's quarterly income before extraordinary items is negative, and zero otherwise.

NegNews = An indicator variable for negative earnings news for the quarter, taking value one if the firm's the firm's earnings before extraordinary items is lower than that of the same quarter in the past year, and zero otherwise.

News = Absolute value of the differences between the firm's earnings per share before extraordinary items and that in the previous year for the same quarter, scaled by the stock price at beginning of quarter.

Earnings information in mandatory reports are less relevant for loss firms (Hayn, 1995). And loss firms may face a higher demand for voluntary disclosure, as they need to preempt the bad news (Skinner, 1994), suggesting a positive prediction for *Loss*. On the contrary, Miller (2002) finds that when firm performance deteriorates, they would reduce disclosure, suggesting a negative prediction for *Loss*. The predicted sign for *Loss* is two-ways.

NegNews is expected to have a positive sign, as (Skinner, 1994) finds that firms with negative earnings news are likely to preempt it via voluntary disclosure.

News is expected to have a positive sign, as firms with more news have a higher tendency to make voluntary disclosure too.

I also control for the firm's information environment (Billings and Cedergren, 2015).

Analyst = number of analysts who issue earnings forecast for the firm during the quarter.

IO = percentage of firm's shares held by 13-F institutional investors.

Big4 = one if the firm's auditor is one of the Big Fours for the year, and zero otherwise.

Volatility = standard deviation of the firm's monthly raw stock returns.

SDROA = standard deviation of the firm's quarterly return-on-assets ratio.

I expect *Analyst*, *IO*, *Big4* to have positive signs, as financial analysts, institutional investors, and big auditors all could monitor the firm and makes its disclosure more transparent. *Volatility*

and *SDROA* are expected to have negative signs, as more volatile information environment would increase the difficulty for firms to make forecasts.

Fqtr4 = one if it is the fourth fiscal quarter for the firm, and zero otherwise.

Finally, *Fqtr4* is expected to have a positive sign.

All continuous variables are winsorized at 1% and 99% percentile. Panel C of Table 5 shows the descriptive statistics for all the variables used in the disclosure test.

4.2 Testing Hypothesis 2

This study is primarily interested in how litigation risk affects a firm's voluntary disclosure decisions, as stated in my Hypothesis 2. As is described section 4.1, I look into the issuance, frequency, and horizon, of the firm's voluntary disclosure. Table 6 presents the this set of empirical results.

[Insert Table 6 Around Here]

In Panel A, Table 6, it shows the logit test for the issuance of disclosure. Column (1) presents the result for a univariate logit test. *Dem_Judges* appears negatively associated with the firm's decision to issue a voluntary disclosure via the Form 8-K.

Column (2) includes the control variables for firm characteristics, such as *Size, Lev, RD, MB*, quarterly earnings news, such as *Loss, NegNews, News*, and information environment, such as *Analyst, IO, Big4, Volatility, SDROA, and Fqtr4*. Column (2) also includes the year and industry fixed effects. The coefficient on *Dem_Judges* is –0.606, significant both statistically and economically, implying a magnitude of 5% decrease in the probability that firm makes voluntary disclosure, with a one-standard-deviation increase in *Dem_Judges*. Noting that this effect is circuit wide, the economic magnitude is large.

Column (3) replaces the year fixed effect in column (2) with circuit fixed effects, to test if the result still holds after removing between-circuits differences. The coefficient on *Dem_Judges*

is –0.702. Column (4) removes the observations from the 9th circuit, the circuit with highest proportion of Democratic judges. The coefficient on *Dem_Judges* is –0.547, still significant at 5% level.

Panel B of Table 6 presents the results for the frequency of disclosure in the quarter. Similarly, *Dem_Judges* is associated with a lower frequency of voluntary disclosure. In column (3), with all controls and circuit and industry fixed effects present, the coefficient on *Dem_Judges* is –0.137. With one standard deviation increase in *Dem_Judges*, the firms in a circuit make about 3% fewer voluntary disclosures.

Panel C shows the results for the horizon of voluntary disclosure of the quarter. *Dem_Judges* is associated with a shorter horizon of voluntary disclosure. In Column (3), the full model spec, the coefficient on *Dem_Judges* is –0.743. With one standard deviation increase in *Dem_Judges*, the first intra-quarter voluntary disclosure is delayed by about 5.18 days, in circuit wide.

In Table 6, the coefficients of *Size* always have a positive sign over the tests, consistent with the notion that larger firms make more voluntary disclosure. As expected, *Lev* also have a positive sign. The signs on *Loss* and *NegNews* are both positive, consistent with the notion that in bad news quarters the firms release more information voluntarily to predisclose the bad news.

In general, the empirical evidences in Table 6 is consistent with the Hypothesis 2, that with a higher litigation risk coming from more *Dem_Judges*, the firms become less likely to make voluntary disclosure, the disclosure frequency reduced, and the horizon shortened.

The effect of firm size

If the measure *Dem_Judges* actually captures the effect of litigation risk on a firm's decisions to make voluntary disclosure, the effect must be stronger for firms with a bigger market capitalization, because larger firms are more likely to be the target by the shareholders lawsuit attorneys, as potential recoverable damages by large firms are also much greater. This is known as the "'deep pockets" phenomenon. To test this prediction, I partition the sample into small and large firms subsamples.

[Insert Table 7 Around Here]

Table 7 reports the results for this set of tests. As predicted, *Dem_Judges* has a negative sign for all three disclosure measures in the large firms sample, but insignificant in the small firms sample, suggesting that the result of *Dem_Judges* is mainly driven by large firms.

Forward-looking and Non-forward-looking disclosure

Voluntary disclosure of forward-looking information are believed to have a higher litigation risk than that of non-forward-looking information. To test if the effect of *Dem_Judges* on voluntary disclosure is stronger for that with forward-looking information, I modify the disclosure measures into capturing those with forward-looking (non-forward-looking) disclosure only, and examine the three aspects of disclosure: Issue, Frequency, and Horizon.

[Insert Table 8 Around Here]

Table 8 presents this set of tests. The effect of *Dem_Judges* on voluntary disclosure is stronger for disclosure of forward-looking information. As shown in column (1), (3), and (5), the coefficients on *Dem_Judges* are negative and significant for forward-looking disclosure. In comparison, *Dem_Judges* does not load for non-forward-looking disclosure, consistent with the notion that voluntary disclosure consisting only of non-forward-looking information are of lower litigation risks.

Forward-looking earnings information and Other information

Hypothesis 2a predicts that the effect of *Dem_Judges* on voluntary disclosure is stronger for those with forward-looking earnings information, as they are more material for investors. To test this prediction, I modify the disclosure measures into capturing those with (without) forward-looking earnings information and examine the three aspects of disclosure: Issue, Frequency, and Horizon.

[Insert Table 9 Around Here]

In Table 9, the results show that *Dem_Judges* reduces voluntary disclosure that contains forward-looking earnings information, but have no effect when the disclosure doesn't contain these type of information. Consistent with the notion that forward-looking earnings information are more material, and are more pertinent to shareholders litigations.

Overall, the results in Table 6, 7, 8 and 9 indicate that firms facing a higher litigation risk that is attributable to a higher proportion of judges being appointed by Democrats would actually reduce its voluntary disclosure, and especially for those that contains forward-looking information, and those that contains forward-looking earnings information.

5 Conclusion

Prior studies on litigation risk and disclosure have been inconclusive (Healy and Palepu, 2001). Francis et al. (1994) document that early disclosure of bad news increases a firm's chance of being sued, while Skinner (1994, 1997) argue otherwise. Field et al. (2005) adopt a simultaneous equations approach and find that firms facing higher litigation risk tend to issue earnings warnings more often. But they do not answer the question in broader situations, how does a higher litigation risk affect a firm's decision to make voluntary disclosure in general, for good news as well as for bad news. Rogers and Van Buskirk (2009) study the effect of litigation risk on disclosure in a specific sample, firms after actually being sued, and they find that firms reduce the level of disclosure after the lawsuit. But their results are not readily applicable to all the firms. As a result the previous studies on litigation and disclosure have not reached a conclusion.

In this study, I develop a novel measure of litigation risk, using the judges' political party affiliation in the Court of Appeals, which is out of control by firms and individual investors. I find that with a one standard deviation increase in litigation risk resulting from a larger proportion of judges being appointed by a Democratic president, a firm's litigation risk exposure

is reduced by around 26% relatively, after controlling for firm characteristics, industry membership, and stock market variables. The firms in a circuit with more Democratic judges make fewer voluntary disclosure, and especially for those that contains material forward-looking earnings information. This finding is not subject to the endogeneity problem that prior studies commonly face, as my litigation risk measure is exogenous in nature.

Unlike the bulk of prior studies on voluntary disclosure which uses First Call CIG data to construct measures of voluntary disclosure, this study uses the firm's 8-K filings to construct the measures of voluntary disclosure. This approach is quite new and needs further examination, as only a few concurrent studies have also availed this data source to measure voluntary disclosure (Bozanic et al., 2015; Cooper et al., 2015).

This study is silent on the question whether firms that predisclosure quarterly bad earnings news are driven by litigation concerns or not, as my litigation risk measure is not at the firm level and does not vary with firm specific litigation risk factors.

Notwithstanding the limitations of the data, the methodology, and the findings in the paper, this study sheds new light on how private securities litigation affects the firm's disclosure behavior in general, and provides insights for policy makers that are interested in further reforming the private securities litigation.

References

Ajinkya, B., Bhojraj, S., Sengupta, P., 2005. The association between outside directors, institutional investors and the properties of management earnings forecasts (digest summary). Journal of accounting research 43 (3), 343–376.

Anilowski, C., Feng, M., Skinner, D. J., 2007. Does earnings guidance affect market returns? the nature and information content of aggregate earnings guidance. Journal of Accounting and Economics 44 (1), 36–63.

Arlen, J. H., Carney, W. J., 1992. Vicarious liability for fraud on securities markets: Theory and evidence. University of Illinois Law Review, 691.

Baginski, S. P., Hassell, J. M., Kimbrough, M. D., 2002. The effect of legal environment on voluntary disclosure: Evidence from management earnings forecasts issued in us and canadian markets. The Accounting Review 77 (1), 25–50.

Baker, T., Griffith, S. J., 2007. Predicting corporate governance risk: Evidence from the directors' and officers' liability insurance market. Chicago Law Review 74, 487.

Baker, T. E., 2009. A primer on the jurisdiction of the US Courts of Appeals. Florida International University Legal Studies Research Paper.

Ball, R., Jayaraman, S., Shivakumar, L., 2012. Audited financial reporting and voluntary disclosure as complements: A test of the confirmation hypothesis. Journal of Accounting and Economics 53 (1), 136–166.

Billings, M. B., Cedergren, M. C., 2015. Strategic silence, insider selling and litigation risk. Journal of Accounting and Economics 59 (2), 119–142.

Bozanic, Z., Roulstone, D. T., Buskirk, A. V., 2015. Management earnings forecasts and other forward-looking statements. Unpublished Working Paper.

Cao, Z., Narayanamoorthy, G. S., 2011. The effect of litigation risk on management earnings forecasts. Contemporary Accounting Research 28 (1), 125–173.

Chen, S., Matsumoto, D. A., 2006. Favorable versus unfavorable recommendations: The impact on analyst access to management-provided information. Journal of Accounting Research 44 (4), 657–689.

Chuk, E., Matsumoto, D., Miller, G. S., 2013. Assessing methods of identifying management forecasts: Cig vs. researcher collected. Journal of Accounting and Economics 55 (1), 23–42.

Clement, M., Frankel, R., Miller, J., 2003. Confirming management earnings forecasts, earnings uncertainty, and stock returns. Journal of Accounting Research, 653–679.

Cooper, M. J., He, J., Plumlee, M., 2015. Voluntary disclosure and investor sentiment. Available at SSRN.

Cordray, M. M., Cordray, R., 2001. The supreme court's plenary docket. Washington and Lee Law Review 58, 737.

Cross, F. B., 1997. Political science and the new legal realism: A case of unfortunate interdisciplinary ignorance. Northwestern University Law Review 92, 251.

Das, A., 2010. A license to lie: The private securities litigation reform act's safe harbor for forward-looking statements does not protect false or misleading statements when made with meaningful cautionary language. Cath. UL Rev. 60, 1083.

Field, L., Lowry, M., Shu, S., 2005. Does disclosure deter or trigger litigation? Journal of Accounting and Economics 39 (3), 487–507.

Forseter, B., 1974. Rule 10b-5 violations in the ninth circuit: I know it when I see it. Business Lawyer 30, 773.

Francis, J., Philbrick, D., Schipper, K., 1994. Shareholder litigation and corporate disclosures. Journal of accounting research, 137–164.

Gerber, S. D., Park, K., 1997. The quixotic search for consensus on the us supreme court: A cross-judicial empirical analysis of the rehnquist court justices. American Political Science Review 91 (02), 390–408.

Gerhardt, M. J., 2003. The federal appointments process: A constitutional and historical analysis. Duke University Press.

Goldman, S., 1975. Voting behavior on the united states courts of appeals revisited. American Political Science Review 69 (02), 491–506.

Graham, J. R., Harvey, C. R., Rajgopal, S., 2005. The economic implications of corporate financial reporting. Journal of accounting and economics 40 (1), 3–73.

Guido, J. C., 2000. Seeking enlightenment from above: Circuit court split on the interpretation of the reform act's heightened pleading requirement. Brooklyn Law Review 66, 501.

Hayn, C., 1995. The information content of losses. Journal of accounting and economics 20 (2), 125–153.

Healy, P. M., Palepu, K. G., 2001. Information asymmetry, corporate disclosure, and the capital markets: A review of the empirical disclosure literature. Journal of accounting and economics 31 (1), 405–440.

Hill, E., 2009. Rule 10b-5 suit: Loss causation pleading standards in private securities fraud claims after dura pharmaceuticals, inc. v. broudo, the. Fordham Law Review 78, 2659.

House Conference Report, 1995. Private Securities Litigation Reform Act of 1995. House of Representatives, Report No 369, 104th Congress, 1st Session.

Howard Jr, J. W., 2014. Courts of appeals in the federal judicial system: A study of the second, fifth, and District of Columbia circuits. Princeton University Press.

Johnson, M. F., Kasznik, R., Nelson, K. K., 2001. The impact of securities litigation reform on the disclosure of forward-looking information by high technology firms. Journal of Accounting Research, 297–327.

Kim, I., Skinner, D. J., 2012. Measuring securities litigation risk. Journal of Accounting and Economics 53 (1), 290–310.

Kothari, S. P., Shu, S., Wysocki, P. D., 2009. Do managers withhold bad news? Journal of Accounting Research 47 (1), 241–276.

Law, D. S., 2004. Appointing federal judges: The president, the senate, and the prisoner's dilemma. Cardozo Law Review 26, 479.

Leiter, B., 2002. American legal realism. In: Golding, M. P., Edmundson, W. A. (Eds.), The Blackwell guide to the philosophy of law and legal theory. John Wiley & Sons, p. 50.

Lerman, A., Livnat, J., 2010. The new form 8-k disclosures. Review of Accounting Studies 15 (4), 752–778.

Lev, B., Zarowin, P., 1999. The boundaries of financial reporting and how to extend them (digest summary). Journal of Accounting research 37 (2), 353–385.

Li, F., 2010. The information content of forward-looking statements in corporate filingsa naïve bayesian machine learning approach. Journal of Accounting Research 48 (5), 1049–1102.

Milgrom, P. R., 1981. Good news and bad news: Representation theorems and applications. Bell Journal of Economics, 380–391.

Miller, C. J., 2011. Don't blame me, blame the financial crisis: A survey of dismissal rulings in 10b-5 suits for subprime securities losses. Fordham L. Rev. 80, 273.

Miller, G. S., 2002. Earnings performance and discretionary disclosure. Journal of Accounting Research 40 (1), 173–204.

Morgan, G., 2003. Earnings guidance: The goood, the bad, and the ugly. Wall Street Lawyer.

Pinello, D. R., 1999. Linking party to judicial ideology in american courts: A meta-analysis. The Justice System Journal, 219–254.

Posner, R. A., 1995. Overcoming law. Harvard University Press.

Pritchard, A. C., Sale, H. A., 2005. What counts as fraud? an empirical study of motions to dismiss under the Private Securities Litigation Reform Act. Journal of Empirical Legal Studies 2 (1), 125–149.

Rogers, J. L., Van Buskirk, A., 2009. Shareholder litigation and changes in disclosure behavior. Journal of Accounting and Economics 47 (1), 136–156.

Rogers, J. L., Van Buskirk, A., 2013. Bundled forecasts in empirical accounting research. Journal of Accounting and Economics 55 (1), 43–65.

Schneider, C. W., Dubow, J. A., 1996. Forward-looking informationnavigating in the safe harbor. The Business Lawyer, 1071–1100.

Securities And Exchange Commission (SEC), 1979. Report of the advisory committee on corporate disclosure to the securities and exchange commission, securities act release no. 6084. 95th Congress, 1st session. Committee print, 95-29.

Securities And Exchange Commission (SEC), 1994. Safe harbor for forward-looking statements, securities act release no. 33- 7101. Federal Register 59.

Securities And Exchange Commission (SEC), 2004. Final rule: Additional form 8-k disclosure requirements and acceleration of filing date. Financial Reporting Release No. 33-8400, 34-49424.

Seligman, J., 1994. SEC's unfinished soft information revolution, the. Fordham Law Review 63, 1953.

Silverman, M., 2010. Fraud created the market: presuming reliance in rule 10b-5 primary securities market fraud litigation. Fordham Law Review 79, 1787.

Sisk, G. C., Heise, M., Morriss, A. P., 1998. Charting the influences on the judicial mind: An empirical study of judicial reasoning. New York University Law Review 73 (5).

Skinner, D. J., 1994. Why firms voluntarily disclose bad news. Journal of Accounting Research 32 (1), 38–60.

Skinner, D. J., 1997. Earnings disclosures and stockholder lawsuits. Journal of Accounting and Economics 23 (3), 249–282.

Songer, D. R., Sheehan, R. S., Haire, S. B., 2000. Continuity and change on the United States Courts of Appeals. University of Michigan Press.

Stoker, B. J., 2010. Opening the rule 10b-5 floodgates: Ninth circuit split in gilead sciences leaves the loss causation pleading standard in limbo. BYU Law Review, 301.

Verrecchia, R. E., 1983. Discretionary disclosure. Journal of accounting and economics 5, 179–194.

Wallace, J. C., 1983. The nature and extent of intercircuit conflicts: A solution needed for a mountain or a molehill? California Law Review, 913–941.

Wang, A., 2006. Problem of meaningful language: Safe harbor protection in securities class action suits after asher v. baxter, the. Northwestern University Law Review 100, 1907.

Waymire, G., 1985. Earnings volatility and voluntary management forecast disclosure. Journal of Accounting Research, 268–295.

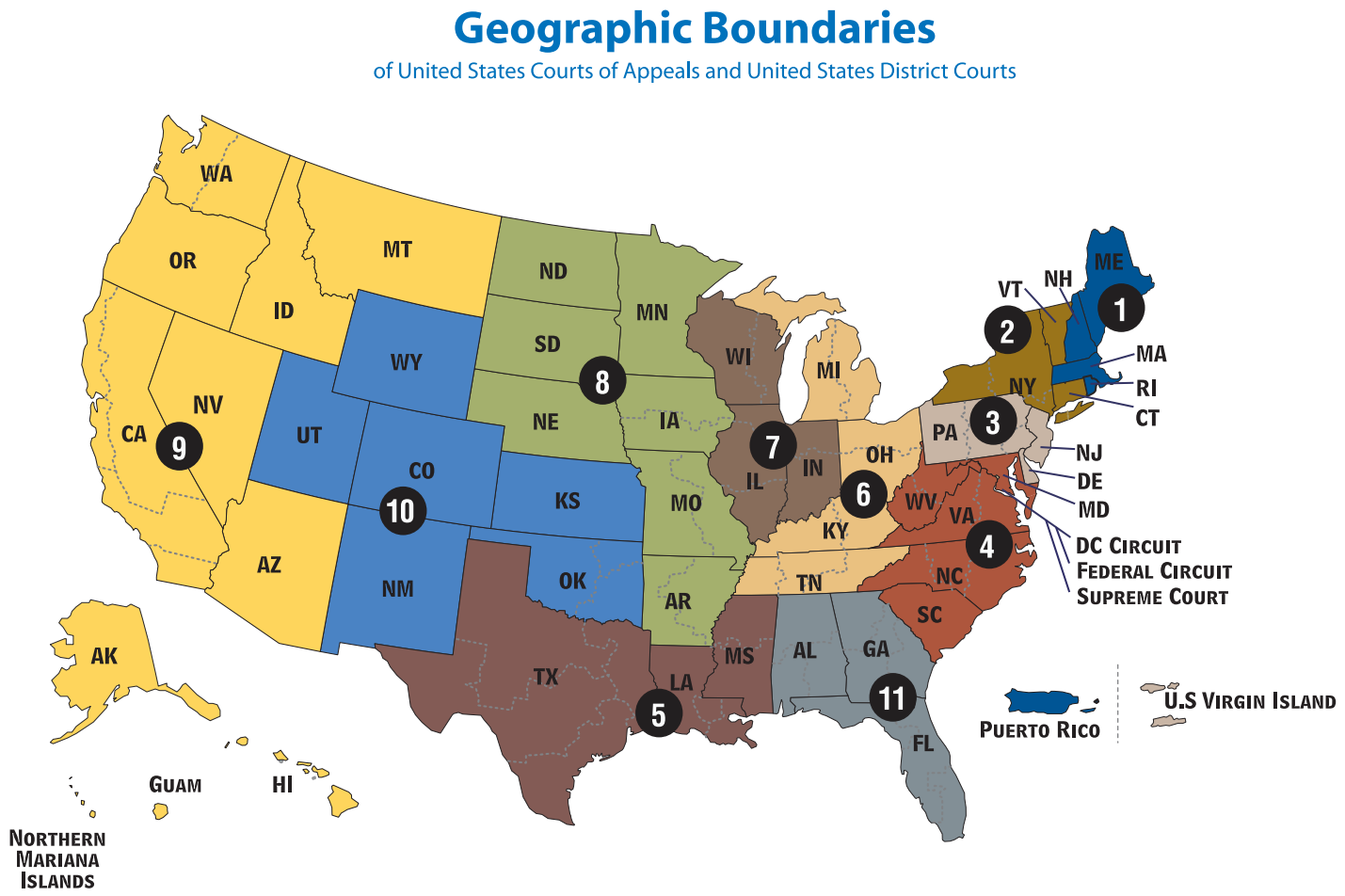

Figure 1: Geographic Boundaries of United States Courts of Appeals

Appendix A

Variable Definitions

Main Test Variable

Dem_Judges_t	The probability that a randomly assigned three-judges panel in the United States Court of Appeals for the firm's headquarter circuit would be dominated by Democratic judges, i.e. by judges appointed by a Democratic President. It is calculated as $\left(\binom{D}{3} + \binom{D}{2}\binom{(N-D)}{1}\right) / \binom{N}{3}$, where D and N are the number of Democratic judges and the total number of judges in the USCOA circuit, respectively, and the firm's headquarter as of the beginning of the fiscal period is obtained from form 10-K and 10-Q.

Variables for Litigation Occurrence Test (Annual)

Sued_t	An indicator variable, taking value one if the firm-year overlaps with the class period of a shareholders lawsuit, and zero otherwise.
FPS_t	An indicator variable, taking value one if the firm is in one of the high ligation risk industries, as defined in Francis et al. (1994), with SIC code in either 2833–36, 8731–34 (biotech), 3570–77, 7370–74 (computer), 3670–74 (electronics), or 5200–5961 (retail) range, and zero otherwise.
SalesGr_{t-1}	Sales of year t-1 minus sales of year t-2, scaled by total assets of year t-2.
Return_{t-1}	Market-adjusted stock returns compounded over the 12 months prior to year t.
RetSkw_{t-1}	Skewness of the firm's monthly stock returns, over the 12 months prior to year t.
RetSD_{t-1}	Standard deviation of monthly returns, over the 12 months prior to year t.
Turnover_{t-1}	Monthly stock trading volume deflated by number of shares, summed over the 12 months prior to year t.
MktRet_{t-1}	Value weighted market returns accumulated over the 12 months prior to year t.
IndRet_{t-1}	Returns of the 4-digits-SIC portfolio accumulated over the 12 months prior to year t.
IndRetSD_{t-1}	Firm level standard deviations of monthly returns averaged over the 4-digits-SIC industry.
GdpGr_t	The rate of GDP growth in the firm's headquarter state for the year t.
Unemp_t	The unemployment rate in the firm's headquarter state for the year t.
BlueState_t	An indicator variable, taking value one if the firm's headquarter state favors a Democratic candidate in the latest presidential election prior to year t, and zero otherwise.
Damage_k	The estimated shareholders damage during the class period, log of one plus MVE $\cdot$ Ret_k $\cdot$ (1- (1-Turnover_k)^X), where MVE is the market capitalization of equity before the end of the class period, Ret_k is the stock return cumulated over the class period, Turnover_k is the avarage trading volume as a percentage of shares outstanding during the class period, and X is the length of the class period.
IsGaapv_t	An indicator variable, taking value one if the lawsuit complaint includes alleged violations of US GAAP, and zero otherwise.
IsInsider_t	An indicator variable, taking value one if the lawsuit complaint includes alleged illegal insider tradings by the firm's officers, and zero otherwise.

Disclosure Variables (Quarterly)

Issue_q	An indicator variable, taking value one if the firm files at least one Form 8-K during the quarter* that contains either Item 2.02, Item 7.01, or Item 8.01, and zero otherwise.

Appendix A

(Continued)

Freq_q	Log of one plus the number of Form 8-K during the quarter* that contains either Item 2.02, Item 7.01,or Item 8.01.
Horizon_q	Log of one plus the number of days between the firm's first Form 8-K during the quarter* that contains either Item 2.02, Item 7.01, or Item 8.01, and the quarterly earnings announcement date.
Issue_Fwl_q	An indicator variable, taking value one if the firm files at least one Form 8-K during the quarter* that contains either Item 2.02, Item 7.01, or Item 8.01, with forward-looking keywords in its non-boilerplate contents**, and zero otherwise.
Freq_Fwl_q	Log of one plus the number of Form 8-K during the quarter* that contains either Item 2.02, Item 7.01, or Item 8.01, with forward-looking keywords in its non-boilerplate contents**.
Horizon_Fwl_q	Log of one plus the number of days between the firm's first Form 8-K during the quarter* that contains either Item 2.02, Item 7.01, or Item 8.01, with forward-looking keywords in its non-boilerplate contents**, and the quarterly earnings announcement date.
Issue_Nfwl_q	An indicator variable, taking value one if the firm files at least one Form 8-K during the quarter* that contains either Item 2.02, Item 7.01, or Item 8.01, with no forward-looking keywords in its non-boilerplate contents**, and zero if it doesn't file any such Form 8-K in the quarter.
Freq_Nfwl_q	Log of one plus the number of the Form 8-K during the quarter* that contains eitherItem 2.02, Item 7.01, or Item 8.01, with no forward-looking keywords in its non-boilerplate contents**.
Horizon_Nfwl_q	Log of one plus the number of days between the firm's first Form 8-K during the quarter* that contains either Item 2.02, Item 7.01, or Item 8.01, with no forward-looking keywords in its non-boilerplate contents**, and the quarterly earnings announcement date.
Issue_FwlE_q	An indicator variable, taking value one if the firm files at least one Form 8-K during the quarter* that contains either Item 2.02, Item 7.01, or Item 8.01, with forward-looking keywords and earnings-related keywords in a same sentence in its non-boilerplate contents**, and zero otherwise.
Freq_FwlE_q	Log of one plus the number of the Form 8-K during the quarter* that contains either Item 2.02, Item 7.01, or Item 8.01, with forward-looking keywords and earnings-related keywords in a same sentence in its non-boilerplate contents.
Horizon_FwlE_q	Log of one plus the number of days between the firm's first Form 8-K during the quarter* that contains either Item 2.02, Item 7.01, or Item 8.01, with forward-looking keywords and earnings-related keywords in a same sentence in its non-boilerplate contents**, and the quarterly earnings announcement date.
Issue_NfwlE_q	An indicator variable, taking value one if the firm files at least one Form 8-K during thequarter* that contains either Item 2.02, Item 7.01, or Item 8.01, not with forward-looking keywords and earnings-related keywords in a same sentence in its non-boilerplate contents**, and zero otherwise.
Freq_NfwlE_q	Log of one plus the number of the Form 8-K during the quarter* that contains either Item 2.02, Item 7.01, or Item 8.01, not with forward-looking keywords and earnings-related keywords in a same sentence in its non-boilerplate contents.

Appendix A

(Continued)

Horizon_NfwlE$_q$	Log of one plus the number of days between the firm's first Form 8-K during the quarter* that contains either Item 2.02, Item 7.01, or Item 8.01, not with forward-looking keywords and earnings-related keywords in a same sentence in its non-boilerplate contents, and the quarterly earnings announcement date.
Control Variables for Disclosure Tests (Quarterly)	
Size$_{q-1}$	Log of market capitalization (CSHOQ*PRCCQ) at quarter q-1.
Lev$_{q-1}$	Total assets (ATQ) scaled by book value of common equity (CEQQ) at quarter q-1.
RD$_q$	Quarterly research & development expense (RDQ) at quarter q, scaled by total assets (ATQ) at quarter q-1.
MB$_{q-1}$	The ratio of the firm's market capitalization (CSHOQ*PRCCQ) to book value of common equity (CEQQ), both at quarter q-1.
Loss$_q$	An indicator variable, taking value one if income before extraordinary items (IBQ) is negative for quarter q, and zero otherwise.
NegNews$_q$	An indicator variable, taking value one if earnings per share excluding extraordinary items (EPSPXQ) of quarter q is less than that of quarter q-4, and zero otherwise.
News$_q$	Absolute value of the differences between earnings per share excluding extraordinary items (EPSPXQ) of the quarter q and that of quarter q-4 deflated by the stock price at the beginning of quarter q.
Analyst$_q$	Log of one plus the number of analysts who issue at least one earnings forecast for the firm-quarter.
IO$_q$	Number of the firm's shares held by 13F institutional investors (SHARES) scaled by total shares outstanding (SHROUT2 times 1,000) as of at the beginning of the quarter.
Big4$_q$	One if the firm's auditor is one of the Big Four's for the year, and zero otherwise.
Volatility$_q$	Standard deviation of the firm's monthly raw stock returns (RET), during the 12 months immediately prior to the quarter.
SDROA$_q$	Standard deviation of the firm's quarterly return-on-assets ratio (IBQ/ATQ), during the 8 quarters immediately prior to the quarter.
Fqtr4$_q$	An indicator variable, taking value one if it is the fourth fiscal quarter for the firm,and zero otherwise.

* A Form 8-K is coded as containing voluntary disclosure if it contains either Item 2.02 Results of Operations and Financial Condition, Item 7.01 Regulation FD Disclosure, or Item 8.01 Other Events. For matching a Form 8-K with a fiscal quarter, the Form 8-K must be filed at least one day after the previous quarter's earnings announcement day, and till the week prior to the current quarter's earnings announcement date.
** Lists of keywords mentioned above are in Appendix B.

Appendix B
Keywords for Forward-Looking Disclosure and Forward-Looking Earnings Disclosure

Keywords for boilerplate contents

Following Li (2010), a sentence would be ignored if there appears keywords related with either legal language, or words typical used in a cautionary statement pursuant to the Safe Harbor for forward-looking statement: *undersigned, herein, hereof, hereon, hereto, hereunder, hereafter, thereto, theretofore, therein, thereof, thereon, pursuant, whereas, preceding, clause, notwithstanding, Act of 1933, Act of 1934, differ materially, forward-looking, not limited to, Safe Harbor*.

Keywords for forward-looking disclosure

Following Li (2010), a sentence is coded as containing forward-looking statement (FLS) if it contains either of the words: *will, should, can, could, may, might, expect, anticipate, believe, plans to, planned, planning, hope, intend, seek, predict, project, forecast, forward, objective, goal, target*. For the first word on the left of the keyword matched, if it is either *was*, *were*, *had*, *had been*, the sentence is not coded as containing FLS. Besides, if a sentence mentions *conference call*, or any keywords of boilerplate contents mentioned above, it is not coded as containing FLS.

Keywords for forward-looking earnings disclosure

A sentence is coded as containing forward-looking earnings disclosure If a sentence is coded as FLS and contains either *income, earning, loss, profit, EPS*. Earnings related keywords are from Bozanic et al. (2010).

Appendix C1.
Example of a Forward-Looking Earnings Disclosure in Positive Tones
Furnished via Form 8-K

http://edgar.sec.gov/Archives/edgar/data/8868/000095010305000159/0000950103-05-000159-index.htm
CIK: 8868; 8-K Filing Date: 2005-02-01

Item 2.02 Results of Operations and Financial Condition.
On February 1, 2005, Avon issued a press release announcing its results of operations for the fourth quarter and full year 2004. The press release included Avons consolidated statements of income, condensed consolidated balance sheets and consolidated statements of cash flows, and a supplemental schedule that provided additional information regarding Avons regional results and product category sales, for the three-month and twelve-month periods ended December 31, 2004. A copy of that press release is attached hereto as Exhibit 99.1 and is incorporated herein by reference.

Exhibit. 99.1 Press Release of Avon Products, Inc., dated February 1, 2005, relating to fourth quarter and full year 2004 earnings.

NEW YORK, N.Y., February 1, 2005 Avon Products, Inc. (NYSE:AVP) today announced fourth-quarter 2004 EPS of $.61 per share, as expected, up 11% from $.55 per share in the fourth quarter of 2003.

Avon said that dollar-denominated and local-currency sales in the fourth quarter increased 10% and 7%, respectively, with sales of Beauty products advancing a healthy 16%, well ahead of overall dollar-sales growth. Units and active Representatives both rose 10% in the quarter.

(9 paragraphs about backward-looking discussions are omitted)

2005 Outlook. *As announced in December, Avon* `expects` *to deliver another year of standout growth in 2005, reflecting ongoing* `strength` *in its international operations. Local-currency total revenues are projected to grow 10% year over year, driven by double-digit* `gains` *in units and active Representatives, with Beauty growth outpacing overall revenue growth. Operating margin* `is forecast` *to expand 50-80 basis points, and* `earnings per share are expected` *to be in the range of $1.95 -$2.00, with a 2005 effective tax rate of approximately 31%. Additionally, cash flow from operations* `is projected` *to reach a record $1 billion this year.*

For the first quarter, Avon said it `expects` *local-currency revenue growth in line with fourth quarters growth. Dollar-based revenue growth should again outpace local-currency growth, with a slightly less favorable foreign exchange impact than in the fourth quarter. Operating* `profit is projected` *to grow at least in line with dollar revenue growth. The company* `anticipates` `earnings` *to be in the range of $.35 per share, versus $.31 per share in the first quarter 2004.*

(4 more paragraphs about backward-looking discussions are omitted, including safe harbor cautionary statements)

Item 8.01 Other Events. (omitted)

Exhibit. 99.2 Press Release of Avon Products, Inc., dated February 1, 2005, relating to an increase in the Companys quarterly dividend and to the Companys share repurchase program. (omitted)

Forward-looking sentences in positive tones are in italics. Forward-looking keywords, words in positive tones, and earnings-related keywords are in typewriter font.

Appendix C2.
Example of a Forward-Looking Earnings Disclosure in Form 8-K
Being Involved in a 10b-5 Lawsuit

http://edgar.sec.gov/Archives/edgar/data/10456/000095013101503976/0000950131-01-503976-index.htm

CIK: 10456; 8-K Filing Date: 2001-11-05

Lawsuit: *Asher v. Baxter International Inc.* Class Period: 2001-11-05 — 2002-07-17. Complaint Filed: 2002-08-07.

Item 5. Other Events.

On November 5, 2001, a Baxter International Inc. subsidiary announced that preliminary tests lead Baxter to believe that a processing fluid used in the manufacturing operation in Baxter's Ronneby, Sweden, facility may have played a role in recent hemodialysis patient deaths. As detailed in the press release, Baxter expects to take a fourth-quarter after-tax charge of approximately $100-150 million to cover the cost of discontinuing its series A dialyzer product line and other related costs. The press release is filed as Exhibit 99 and incorporated by reference.

(one more paragraph omitted)

Item 7. Exhibits. Press Release dated November 5, 2001

FOLLOWING EXTENSIVE INVESTIGATION, BAXTER IDENTIFIES PROBABLE
CAUSE OF RECENT HEMODIALYSIS PATIENT DEATHS

DEERFIELD, ILL, November 5, 2001 - A Baxter International Inc. subsidiary announced today a key finding from its comprehensive dialyzer investigation that could account for many of the unexplained recent hemodialysis deaths reported in several countries. Preliminary tests completed over the weekend lead Baxter to believe that a processing fluid used in the manufacturing operation in its Ronneby, Sweden, facility may have played a role.

(four more paragraphs omitted)

Baxter `expects` to take a fourth-quarter after-tax charge of approximately $100-$150 million to cover the cost of discontinuing this product line and other related costs. The after-tax cash impact `is estimated` to be no more than $50 million. *Excluding this charge, Baxter `expects` to meet the full-year 2001 financial commitments of sales growth in the low double-digits, `earnings growth` in the mid-teens and operational cash flow of more than $500 million. In addition, Baxter reiterated it `will` also meet its 2002 full-year commitments of sales growth in the low-teens (at current foreign exchange rates), `earnings-per-share` in the mid-teens and operational cash flow of at least $500 million.*

(one more paragraph omitted)

This news release contains forward-looking statements that involve risks and uncertainties, including technological advances in the medical field, product demand and market acceptance, the effect of economic conditions, actions of regulatory bodies, results of ongoing product testing, the impact of competitive products and pricing, foreign currency exchange rates and other risks detailed in the company's filings with the Securities and Exchange Commission. These forward-looking statements are based on estimates and assumptions made by management of the company and are believed to be reasonable, though are inherently uncertain and difficult to predict. Actual results or experience could differ materially from the forward-looking statements.

Sentences of earnings-related forward-looking statements are highlighted in italics. Forward-looking keywords, and earnings-related keywords are in typewriter font.

Table 1
U.S. Court of Appeals and Judges' Party Affiliaction

This table reports the descriptives of judges' party affiliaction at different circuit Courts of Appeals during 1996 – 2014. Panel A shows the statistics of the judge partisanship Dem_Judges by each circuit, Panel B by year, and Panel C by each of the three Presidents during the sample period. Variable definitions are in Appendix A.

Panel A: Court of Appeals Judges' Party Affiliaction by Circuits

Circuit	Mean	Std. Dev.	Min	Q1	Median	Q3	Max
1th	0.222	0.054	0.083	0.183	0.183	0.279	0.364
2th	0.520	0.106	0.296	0.466	0.500	0.612	0.692
3th	0.265	0.076	0.121	0.227	0.270	0.329	0.435
4th	0.438	0.114	0.304	0.360	0.400	0.500	0.704
5th	0.252	0.114	0.117	0.155	0.209	0.388	0.421
6th	0.302	0.059	0.220	0.250	0.287	0.371	0.440
7th	0.187	0.026	0.136	0.176	0.191	0.214	0.214
8th	0.197	0.140	0.046	0.046	0.169	0.360	0.412
9th	0.599	0.069	0.434	0.562	0.613	0.651	0.715
10th	0.328	0.086	0.202	0.247	0.296	0.400	0.500
11th	0.423	0.063	0.304	0.360	0.412	0.458	0.571
DC	0.262	0.090	0.176	0.176	0.236	0.364	0.437

Panel B: Court of Appeals Judges' Party Affiliaction by Year

Year	Mean	Std. Dev.	Min	Q1	Median	Q3	Max
1996	0.334	0.110	0.121	0.244	0.353	0.420	0.500
1997	0.345	0.118	0.121	0.247	0.360	0.437	0.571
1998	0.371	0.119	0.121	0.291	0.388	0.453	0.571
1999	0.378	0.131	0.121	0.279	0.379	0.458	0.612
2000	0.397	0.126	0.191	0.279	0.400	0.452	0.651
2001	0.400	0.125	0.214	0.287	0.400	0.446	0.651
2002	0.368	0.124	0.214	0.279	0.326	0.412	0.651
2003	0.331	0.120	0.183	0.247	0.279	0.406	0.651
2004	0.300	0.125	0.155	0.212	0.258	0.368	0.613
2005	0.292	0.132	0.155	0.183	0.247	0.360	0.613
2006	0.280	0.132	0.080	0.183	0.250	0.333	0.613
2007	0.266	0.140	0.046	0.176	0.237	0.360	0.578
2008	0.265	0.151	0.046	0.165	0.227	0.360	0.578
2009	0.266	0.151	0.046	0.176	0.224	0.372	0.581
2010	0.291	0.168	0.046	0.176	0.220	0.423	0.588
2011	0.319	0.185	0.046	0.176	0.267	0.474	0.671
2012	0.343	0.206	0.046	0.180	0.297	0.521	0.715
2013	0.369	0.196	0.046	0.209	0.316	0.539	0.692
2014	0.410	0.196	0.097	0.250	0.406	0.605	0.715

Panel C: Court of Appeals Judges' Party Affiliaction by President in Office

President	Mean	Std Dev	Min	Q1	Median	Q3	Max
WJ. Clinton	0.365	0.123	0.121	0.279	0.371	0.453	0.651
GW. Bush	0.313	0.139	0.046	0.214	0.279	0.399	0.651
BH. Obama	0.333	0.190	0.046	0.183	0.284	0.453	0.715

Table 2
Descriptive Statistics for Shareholders Lawsuit Sample

This table reports the formation of shareholders lawsuits filing sample, the litigation outcomes, the distribution of lawsuits across year and circuits, and summary statistics for the variables used in the litigation occurrence test.

Panel A: Lawsuit filings and outcomes

		# Lawsuits
Lawsuit filings during 1996–2014 From SCAC website		3,898
Less: (1,872) filings against companies not listed on NYSE, AMEX, NASDAQ or non-US companies		2,026
Less: (78) IPO allocation cases, hedge fund, mutual fund, and analyst cases		1,948
Less: (209) Non Rule 10b-5 violation cases		1,739
Less: (254) Compustat or CRSP identifiers not available		1,485
Less: (315) Variables missing in the relevant firm-year		1,170
Lawsuits that have been settled	33%	710
Lawsuits that have been dismissed	61%	393
Still pending	6%	67
Total		1,170
		# Firm-Years
# Firm-year's that overlaps with a class period	2.60%	2,399
# Total firm-year's from Compustat during 1996–2014		92,396

Panel B: Distribution of Lawsuits by Year and Circuit

Year	1st	2nd	3rd	4th	5th	6th	7th	8th	9th	10th	11th	DC	All Cir.
1996	4	7	5	1	3	1	1	0	18	2	7	0	49
1997	7	8	7	2	3	4	4	3	20	3	9	1	71
1998	8	8	9	5	10	6	0	2	29	3	11	0	91
1999	9	6	5	4	9	5	7	2	23	4	11	0	85
2000	5	12	4	6	7	4	4	1	26	2	13	0	84
2001	10	10	5	5	5	1	6	6	50	9	9	0	116
2002	5	8	11	5	6	5	6	7	25	2	12	0	92
2003	6	3	5	4	4	6	0	3	15	3	10	0	59
2004	5	3	7	4	8	0	1	3	43	1	4	0	79
2005	8	7	4	2	4	2	3	6	22	2	5	1	66
2006	3	4	4	2	3	0	3	1	26	3	6	1	56
2007	5	4	3	1	2	2	0	1	21	1	4	1	45
2008	1	3	8	2	1	3	0	1	12	5	5	0	41
2009	1	3	2	1	3	2	6	1	12	1	1	0	33
2010	1	5	1	4	2	2	2	2	15	2	0	0	36
2011	2	3	1	2	7	1	4	2	20	0	2	0	44
2012	6	6	3	3	3	0	1	1	12	2	2	0	39
2013	4	3	6	1	4	0	3	2	19	1	3	1	47
2014	2	4	6	2	1	0	2	1	17	0	1	1	37
Total	92	107	96	56	85	44	53	45	425	46	115	6	1,170

Table 2
(Continued)

Panel C. Univariate Statistics

	Obs	Mean	Std. Dev.	Min	Q1	Median	Q3	Max
Sued	92,396	0.025	0.157	0.000	0.000	0.000	0.000	0.000
Dem_Judges	92,396	0.372	0.161	0.046	0.247	0.360	0.479	0.715
FPS	92,396	0.234	0.423	0.000	0.000	0.000	0.000	0.000
Size	92,396	5.510	2.067	0.282	3.963	5.420	6.941	11.208
SalesGr	92,396	0.103	0.351	-1.539	-0.006	0.034	0.165	4.045
Rreturn	92,396	0.034	0.615	-0.962	-0.308	-0.057	0.221	6.099
RetSkw	92,396	0.340	0.860	-2.110	-0.232	0.289	0.861	2.883
RetSD	92,396	0.144	0.101	0.022	0.075	0.117	0.181	0.758
Turnover	92,396	1.613	1.746	0.042	0.469	1.035	2.101	12.175
IO	92,396	0.318	0.344	0.000	0.000	0.173	0.621	0.000
MktRet	92,396	0.121	0.195	-0.441	-0.008	0.162	0.264	0.576
IndRet	92,396	0.034	0.376	-0.962	-0.186	-0.013	0.178	6.057
IndRetSD	92,396	0.144	0.073	0.022	0.090	0.130	0.180	0.766
GdpGr	92,396	0.049	0.028	-0.132	0.035	0.050	0.067	0.218
Unemp	92,396	0.069	0.031	0.023	0.047	0.062	0.082	0.407
BlueState	92,396	0.680	0.466	0.000	0.000	0.000	0.000	0.000
Dismissed	1,103	0.356	0.479	0.000	0.000	0.000	0.000	0.000
Damage	1,103	9.126	5.056	0.000	9.014	11.260	12.289	17.763
IsGaapv	1,103	0.162	0.369	0.000	0.000	0.000	0.000	1.000
IsInsid	1,103	0.300	0.459	0.000	0.000	0.000	1.000	1.000

Panel D. Correlation Coefficients

	Sued	Dem_Judges	FPS	Size	SalesGr	Return	RetSkwW	RetSD	Turnover	IO	MktRet	IndRet	IndRetSD	GdpGr	Unemp	BlueState
Sued		*0.05*	*0.09*	*0.05*	*0.08*	*0.02*	*0.02*	*0.11*	*0.15*	*0.04*	*-0.01*	*0.01*	*0.10*	*0.02*	*0.02*	*0.02*
Dem_Judges	*0.05*		*0.11*	*-0.04*	*-0.01*	-0.00	*0.04*	*0.13*	*0.06*	*0.07*	*-0.10*	*0.03*	*0.13*	*0.05*	*0.29*	*0.15*
FPS	*0.09*	*0.11*		-0.01	*0.06*	*-0.04*	*0.06*	*0.27*	*0.25*	*0.07*	*-0.03*	0.00	*0.35*	-0.00	*0.09*	*0.10*
Size	*0.04*	*-0.03*	-0.01		*0.16*	*0.29*	*-0.23*	*-0.36*	*0.42*	*0.40*	*-0.01*	*0.16*	*-0.23*	*-0.07*	*0.10*	*-0.03*
SalesGr	*0.09*	-0.01	*0.03*	*0.08*		*0.17*	*-0.02*	*0.02*	*0.17*	*-0.01*	*0.06*	*0.05*	*0.04*	*0.18*	*-0.08*	-0.01
Return	*0.06*	*0.03*	*0.02*	*0.19*	*0.15*		*0.10*	*-0.11*	*0.03*	*0.14*	*-0.03*	*0.61*	*-0.09*	*-0.06*	*0.05*	*-0.03*
RetSkew	*0.02*	*0.04*	*0.06*	*-0.23*	-0.00	*0.15*		*0.30*	*-0.06*	*-0.12*	*0.05*	*0.06*	*0.19*	*0.05*	*-0.01*	*0.03*
RetSD	*0.10*	*0.12*	*0.23*	*-0.34*	*0.02*	*0.15*	*0.40*		*0.31*	*-0.05*	*-0.08*	*-0.03*	*0.76*	*0.01*	*0.04*	*0.05*
Turnover	*0.17*	*0.07*	*0.23*	*0.29*	*0.12*	*0.10*	-0.00	*0.31*		*0.37*	*-0.05*	*0.04*	*0.29*	*-0.03*	*0.17*	*0.03*
IO	*0.04*	*0.05*	*0.07*	*0.45*	*-0.03*	*0.09*	*-0.15*	*-0.12*	*0.35*		*-0.32*	*0.15*	*-0.01*	*-0.28*	*0.19*	*-0.05*
MktRet	*-0.01*	*-0.10*	*-0.03*	*0.02*	*0.07*	*-0.01*	*0.05*	*-0.12*	*-0.05*	*-0.21*		*-0.02*	*-0.08*	*0.24*	*0.04*	*0.07*
IndRet	*0.03*	*0.05*	*0.03*	*0.12*	*0.06*	*0.61*	*0.09*	*0.11*	*0.07*	*0.10*	*-0.02*		*-0.01*	*-0.10*	*0.08*	*-0.04*
IndRetSD	*0.10*	*0.14*	*0.32*	*-0.23*	*0.03*	*0.09*	*0.24*	*0.72*	*0.27*	*-0.05*	*-0.17*	*0.15*		*-0.01*	*0.03*	*0.07*
GdpGr	*0.02*	*0.05*	-0.00	*-0.06*	*0.15*	*-0.03*	*0.04*	*-0.03*	*-0.06*	*-0.23*	*0.26*	*-0.07*	*-0.06*		*-0.25*	*-0.15*
Unemp	*0.02*	*0.32*	*0.10*	*0.09*	*-0.06*	*0.03*	*-0.01*	*0.03*	*0.16*	*0.19*	*0.04*	*0.04*	*0.01*	*-0.31*		*0.20*
BlueState	*0.02*	*0.16*	*0.10*	*-0.02*	*-0.01*	*-0.01*	*0.03*	*0.05*	*0.03*	*-0.04*	*0.07*	*-0.03*	*0.06*	*-0.13*	*0.22*	

Pearson (Spearman) correlation are in lower left (upper right) corner. Coefficients in italic indicate significance at 0.01 level.

Table 3
Shareholders Lawsuits By FPS Industries and Quintiles of Judges Partisanship

This table reports the distribution of lawsuits by FPS litigation risk industry groups and by quintiles of Dem_Judges, and tests the differences of lawsuit occurrence between 1st and 5th quintile of Dem_Judges, within both FPS and Non-FPS industries group. Panel A shows lawsuit occurrence by Quintile of Dem_Judges for all industries, Panel B shows that for Non-FPS industries, and Panel C for FPS industries. Variable definitions are in Appendix A.

Panel A: All Industries

	All Circuits	Q1	Q2	Q3	Q4	Q5	Q5–Q1	T-stat
Total # Obs.	92,396	18,234	18,428	19,060	18,592	18,082		
# Obs. Sued	2,399	381	372	433	508	705		
%Obs. Sued	2.60	**2.09**	2.02	2.27	2.73	**3.90**	**1.81**	**10.14** ***

Panel B: Non-FPS Industries

	All Circuits	Q1	Q2	Q3	Q4	Q5	Q5–Q1	T-stat
Total # Obs.	70,761	13,836	14,555	14,336	14,254	13,780		
# Obs. Sued	1,274	204	201	210	303	356		
%Obs. Sued	1.80	**1.47**	1.38	1.46	2.13	**2.58**	**1.11**	**6.54** ***

Panel C: FPS Industries

	All Circuits	Q1	Q2	Q3	Q4	Q5	Q5–Q1	T-stat
Total # Obs.	21,635	4,398	3,873	4,724	4,338	4,302		
# Obs. Sued	1,125	177	171	223	205	349		
%Obs. Sued	5.20	**4.02**	4.42	4.72	4.73	**8.11**	**4.09**	**8.03** ***

Panel D: Differences between Non-FPS and FPS Industries

	All Circuits	Q1	Q2	Q3	Q4	Q5	Q5–Q1	
%Obs. Sued	3.40	**2.55**	3.04	3.26	2.60	**5.53**	**2.98**	**7.16** ***

Table 4

Judge Partisanship and Shareholders Litigation

Panel A. Lawsuit Occurrence

This panel reports the results for the lawsuit occurrence tests, for the logit model Logit(Sued$_t$) = f(Dem_Judges$_t$, controls_sued$_{t-1}$) + ε. The sample consists of 92,396 firm-years during 1996–2014, including 1,170 class action lawsuits. Column (1–4) report the results over the full sample, and column (5–6) report the partition test results by firm size. Cluster robust *t* statistics are reported below coefficient in parentheses, with standard errors clustered by both firm and quarters. *, **, *** indicates significance at 0.1, 0.05, and 0.01 level, respectively. Variable definitions are in Appendix A.

		Full Sample				Small	Large
		(1)	(2)	(3)	(4)	(5)	(6)
Dependent Variable:		Sued	Sued	Sued	Sued	Sued	Sued
Dem_Judges	+	1.088***	0.863***	1.744***	1.716***	1.035	1.971***
		(4.37)	(3.34)	(3.78)	(3.77)	(1.63)	(3.79)
FPS	+	0.649***	0.520***	0.483***	0.480***	0.299**	0.513***
		(6.66)	(5.22)	(4.95)	(5.01)	(2.11)	(4.73)
Size	+	0.0994***	0.0814***	0.0854***	0.0856***	0.586***	−0.134***
		(4.36)	(3.39)	(3.55)	(3.49)	(10.74)	(−2.71)
SalesGr	+	0.717***	0.684***	0.689***	0.677***	0.525***	0.744***
		(10.55)	(9.90)	(9.90)	(9.75)	(6.12)	(7.17)
Return	+	0.0790**	0.153***	0.152***	0.149***	0.0840	0.113**
		(2.14)	(4.30)	(4.31)	(4.23)	(1.33)	(2.55)
RetSkw	-	−0.0639**	−0.0445	−0.0444	−0.0452	−0.0422	0.00451
		(−2.00)	(−1.38)	(−1.37)	(−1.45)	(−0.89)	(0.11)
RetSD	+	2.376***	0.633*	0.617*	0.569	0.523	0.821
		(6.39)	(1.73)	(1.68)	(1.54)	(0.83)	(1.50)
Turnover	+	0.219***	0.215***	0.218***	0.219***	0.210***	0.214***
		(12.30)	(11.28)	(11.92)	(12.04)	(8.70)	(10.70)
IO	.		0.302**	0.260*	0.251*	−0.160	0.155
			(2.06)	(1.78)	(1.74)	(−0.57)	(1.09)
MktRet	.		0.116	0.123	0.209	−0.631	0.431
			(0.31)	(0.37)	(0.66)	(−1.33)	(1.53)
IndRet	-		−0.232**	−0.239**	−0.236**	−0.320***	−0.210*
			(−2.05)	(−2.19)	(−2.22)	(−2.77)	(−1.69)
IndRetSD	+		3.981***	3.888***	3.779***	3.314***	4.716***
			(7.19)	(6.85)	(6.63)	(4.38)	(5.41)
GdpGr	+		4.748***	5.291***	3.731***	5.567**	5.166***
			(4.08)	(5.32)	(3.23)	(2.51)	(6.15)
Unemp	.		0.461	1.776	−0.403	2.955	2.252*
			(0.42)	(1.56)	(−0.29)	(1.37)	(1.67)
BlueState	.		0.0857	−0.0810	−0.238	0.193	−0.279*
			(1.01)	(−0.65)	(−1.64)	(1.32)	(−1.81)
Intercept		−5.865***	−6.432***	−6.142***	−19.81***	−8.185***	−4.568***
		(−35.77)	(−30.15)	(−26.27)	(−13.52)	(−18.40)	(−10.82)
Circuit FE		No	No	Yes	No	Yes	Yes
State FE		No	No	No	Yes	No	No
N		92,396	92,396	92,396	91,768	46,198	46,198
pse R^2		0.113	0.120	0.125	0.130	0.104	0.149
Testing coefficient equality for Dem_Judges between (5) and (6):							
Chi^2						2.930 *	
p-val						0.087	

Table 4
(Continued)

Panel B. Litigation Outcomes

This panel reports the results for the litigation outcome tests, for the logit model Logit(Dismissed$_t$) = f(Dem_Judges$_t$, controls_dismissed$_{t-1}$) + ε. The sample consists of 92,396 firm-years during 1996–2014, including 1,103 class action lawsuits with known outcomes. Column (1) tests the model over the full sample, column (2) tests the same model for lawsuits with non-specific allegations, and column (3) tests the same model for lawsuits with specific allegations. Cluster robust *t* statistics are reported below coefficient in parentheses, with standard errors clustered by both firm and quarters. *, **, *** indicates significance at 0.1, 0.05, and 0.01 level, respectively. Variable definitions are in Appendix A.

		Full Sample	Non-Spec.	Spec.
		(1)	(2)	(3)
Dependent Variable:		Dismissed	Dismissed	Dismissed
Dem_Judges	-	-1.210^{***}	-2.169^{***}	0.317
		(-2.62)	(-3.69)	(0.42)
Damage	-	-0.0276^{**}	-0.0355^{**}	-0.0162
		(-2.22)	(-2.16)	(-0.85)
FPS	.	-0.0884	-0.0604	-0.115
		(-0.65)	(-0.34)	(-0.53)
Size	+	0.113^{**}	0.156^{**}	0.0655
		(2.43)	(2.53)	(0.91)
IO	+	0.777^{***}	0.634^{*}	0.902^{***}
		(3.41)	(1.92)	(2.84)
GdpGr	.	-6.243^{**}	-8.115^{**}	-4.524
		(-2.31)	(-2.37)	(-1.04)
Unemp	.	7.925^{***}	11.95^{***}	1.767
		(3.04)	(3.44)	(0.43)
BlueState	.	0.123	0.0957	0.203
		(0.74)	(0.42)	(0.81)
IsGaapv	-	-0.164		
		(-0.89)		
IsInsider	-	0.367^{**}		
		(2.52)		
Intercept		-1.185^{***}	-1.108^{**}	-1.141^{*}
		(-3.14)	(-2.22)	(-1.86)
N		1,103	671	432
pseudo R^2		0.064	0.083	0.037
Testing coefficient equality for Dem_Judges between (2) and (3):				
Chi^2			6.792 ***	
p-val			0.009	

Table 5
Descriptive Statistics for Voluntary Disclosure via Form 8-K

This table reports the descriptive statistics for the disclosure sample. Panel A shows the process of sample formation; Panel B shows the the distribution of observations by fiscal year; Panel C shows univariate statistics for the variables used in the disclosure test. Variable definitions are in Appendix A.

Panel A: 8-K Voluntary Disclosure Sample

	Form 8-K's	Firm-quarters
Form 8-K retrieved for 2004–2014	997,093	
Form 8-K pertaining to Items 2.02, 7.01, 8.01 (VD 8-K's)	526,426	
Matching with Compustat/CRSP	231,031	120,474
Final Sample (requiring non-missing variables) :	102,580	100,614
Item 2.02 Results of Operations and Financial Condition	30,988	
Item 7.01 Regulation FD Disclosure	28,584	
Item 8.01 Other events	43,942	

Panel B. Distribution of 8-K's By year

Fiscal year	# Firm-quarters	% Issuing VD 8-K's	# All VD 8-K's	# Forward-looking VD 8-K's	# Forward-looking Earnings VD 8-K's
2,004	6,380	61.1%	7,319	6,503	2,914
2,005	12,152	58.4%	13,284	11,822	4,740
2,006	11,807	56.1%	12,143	10,596	3,991
2,007	11,536	56.4%	11,833	10,284	3,839
2,008	11,374	55.1%	11,309	9,732	3,716
2,009	10,776	52.9%	10,435	8,908	3,280
2,010	10,302	52.4%	10,026	8,489	2,948
2,011	9,954	53.4%	9,817	8,322	2,800
2,012	9,637	52.5%	9,630	8,113	2,822
2,013	6,696	52.5%	6,784	5,725	1,967
Total	100,614	55.0%	102,580	88,494	33,017

Table 5
(Continued)

Panel C: Univariate Statistics

Variable	N	Mean	Std Dev	Min	Q1	Median	Q3	Max
Dem_Judges	100,614	0.360	0.192	0.046	0.183	0.332	0.564	0.715
Issue	100,614	0.550	0.497	0.000	0.000	1.000	1.000	1.000
Freq	100,614	0.537	0.559	0.000	0.000	0.693	0.693	4.060
Horizon	100,614	2.255	2.108	0.000	0.000	3.091	4.394	5.403
Size	100,614	6.055	1.980	0.328	4.627	6.038	7.397	10.929
Lev	100,614	2.735	3.604	1.018	1.384	1.835	2.641	44.462
RD	100,614	0.017	0.037	0.000	0.000	0.000	0.019	0.430
MB	100,614	3.516	5.748	0.137	1.315	2.127	3.614	83.208
Loss	100,614	0.341	0.474	0.000	0.000	0.000	1.000	1.000
NegNews	100,614	0.436	0.496	0.000	0.000	0.000	1.000	1.000
News	100,614	0.042	0.137	0.000	0.003	0.009	0.027	3.500
Volatility	100,614	0.136	0.082	0.027	0.081	0.116	0.166	0.717
SDROA	100,614	0.035	0.144	0.001	0.006	0.013	0.031	6.380
Analyst	100,614	1.522	1.024	0.000	0.693	1.609	2.303	3.466
IO	100,614	0.532	0.349	0.000	0.193	0.586	0.855	1.000
Big4	100,614	0.714	0.452	0.000	0.000	1.000	1.000	1.000
FPS	100,614	0.330	0.470	0.000	0.000	0.000	1.000	1.000
Fqtr4	100,614	0.272	0.445	0.000	0.000	0.000	1.000	1.000
Issue_Fwl	100,614	0.502	0.500	0.000	0.000	1.000	1.000	1.000
Issue_Nfwl	100,614	0.108	0.310	0.000	0.000	0.000	0.000	1.000
Freq_Fwl	100,614	0.471	0.531	0.000	0.000	0.693	0.693	3.932
Freq_Nfwl	100,614	0.086	0.259	0.000	0.000	0.000	0.000	3.761
Horizon_Fwl	100,614	2.065	2.106	0.000	0.000	1.792	4.344	5.403
Horizon_Nfwl	100,614	0.428	1.249	0.000	0.000	0.000	0.000	5.263
Issue_FwlE	100,614	0.265	0.441	0.000	0.000	0.000	1.000	1.000
Issue_NFwlE	100,614	0.398	0.490	0.000	0.000	0.000	1.000	1.000
Freq_FwlE	100,614	0.207	0.360	0.000	0.000	0.000	0.693	2.197
Freq_NFwlE	100,614	0.371	0.507	0.000	0.000	0.000	0.693	4.043
Horizon_FwlE	100,614	1.087	1.842	0.000	0.000	0.000	2.708	5.403
Horizon_NFwlE	100,614	1.606	2.015	0.000	0.000	0.000	4.025	5.366

Table 6
Litigation Risk and Voluntary Disclosure

Panel A reports the result for the logit tests using Dem_Judges to explain the likelihood of firms' issuing voluntary disclosure via Form 8-K during a quarter. The sample consists of 100,614 firm-quarters during 2004-2013. Column (1) includes only Dem_Judges; Column (2) addes control variables and year and industry fixed effects; Column (3) replaces the year fixed effect with circuit fixed effects; and Column (4) excludes observations in the 9th circuit. Cluster robust *t* statistics are reported below coefficient in parentheses, with standard errors clustered by both firms and quarters. *, **, *** indicates significance at 0.1, 0.05, and 0.01 level, respectively. Variable definitions are in Appendix A.

Panel A: Issuance of Voluntary Disclosure

		(1)	(2)	(3)	(4)
Dependent Variable:		Issue	Issue	Issue	Issue
Dem_Judges	–	-0.910^{***}	-0.606^{***}	-0.702^{***}	-0.547^{**}
		(-9.36)	(-6.01)	(-3.18)	(-2.55)
Size	+		0.111^{***}	0.105^{***}	0.095^{***}
			(6.89)	(6.59)	(5.07)
Lev	+		0.024^{***}	0.020^{***}	0.020^{***}
			(4.62)	(3.85)	(3.39)
RD	.		0.400	0.651	0.829
			(0.82)	(1.33)	(1.32)
MB	.		-0.005	-0.002	-0.003
			(-1.49)	(-0.61)	(-0.85)
Loss	+		0.078^{**}	0.086^{***}	0.092^{**}
			(2.51)	(2.76)	(2.55)
NegNews	+		0.120^{***}	0.116^{***}	0.118^{***}
			(6.97)	(6.55)	(6.28)
News	+		0.143^{**}	0.086	0.076
			(2.10)	(1.29)	(0.88)
Analyst	.		-0.057^{**}	-0.073^{***}	-0.072^{**}
			(-2.20)	(-2.81)	(-2.30)
IO	.		0.034	0.024	0.054
			(0.54)	(0.39)	(0.80)
BIG4	.		-0.048	0.003	0.034
			(-1.00)	(0.05)	(0.59)
Volatility	.		0.332^{**}	0.095	0.050
			(2.03)	(0.55)	(0.24)
SDROA	.		0.122^{*}	0.102	0.143^{*}
			(1.94)	(1.62)	(1.72)
FQTR4	+		0.287^{***}	0.318^{***}	0.302^{***}
			(15.25)	(6.92)	(6.71)
Constant		0.531^{***}	-0.430	-1.036^{**}	-1.107^{*}
		(10.69)	(-1.05)	(-2.51)	(-1.79)
Year FE		No	Yes	No	No
SIC2 FE		No	Yes	Yes	Yes
Circuit FE		No	No	Yes	Yes
N		100,614	100,614	100,614	76,114
pseudo R^2		0.005	0.032	0.032	0.030

Table 6
(Continued)

Panel B reports the result for the OLS tests using Dem_Judges to explain the frequency of firms' voluntary disclosure via Form 8-K during a quarter. The sample consists of 100,614 firm–quarters during 2004–2013. Column (1) includes only Dem_Judges; Column (2) addes control variables and year and industry fixed effects; Column (3) replaces the year fixed effect with circuit fixed effects; and Column (4) excludes observations in the 9th circuit. Cluster robust *t* statistics are reported below coefficient in parentheses, with standard errors clustered by both firms and quarters. *, **, *** indicates significance at 0.1, 0.05, and 0.01 level, respectively. Variable definitions are in Appendix A.

Panel B: Frequency of Voluntary Disclosure

		(1)	(2)	(3)	(4)
Dependent Variable:		Freq	Freq	Freq	Freq
Dem_Judges	–	-0.268^{***}	-0.166^{***}	-0.137^{**}	-0.112
		(-8.34)	(-5.44)	(-1.98)	(-1.62)
Size	+		0.042^{***}	0.040^{***}	0.040^{***}
			(8.20)	(7.94)	(6.50)
Lev	+		0.009^{***}	0.007^{***}	0.008^{***}
			(5.14)	(4.48)	(4.14)
RD	.		0.315^{**}	0.404^{***}	0.539^{***}
			(2.12)	(2.71)	(2.69)
MB	.		-0.002^{**}	-0.001	-0.002^{*}
			(-2.41)	(-1.55)	(-1.85)
Loss	+		0.033^{***}	0.036^{***}	0.042^{***}
			(3.87)	(4.13)	(4.15)
NegNews	+		0.029^{***}	0.028^{***}	0.027^{***}
			(6.54)	(5.85)	(4.86)
News	+		0.062^{***}	0.044^{**}	0.042^{*}
			(3.17)	(2.28)	(1.73)
Analyst	.		-0.011	-0.016^{*}	-0.017^{*}
			(-1.36)	(-1.95)	(-1.76)
IO	.		0.003	-0.000	0.006
			(0.16)	(-0.01)	(0.30)
BIG4	.		-0.023^{*}	-0.007	0.007
			(-1.70)	(-0.53)	(0.43)
Volatility	.		0.190^{***}	0.115^{**}	0.094
			(4.08)	(2.17)	(1.46)
SDROA	.		0.055^{**}	0.050^{**}	0.064^{**}
			(2.54)	(2.32)	(2.51)
FQTR4	+		0.101^{***}	0.110^{***}	0.109^{***}
			(15.67)	(7.65)	(7.35)
Constant		0.633^{***}	0.314^{**}	0.120	0.116
		(36.96)	(2.29)	(0.87)	(0.54)
Year FE		No	Yes	No	No
SIC2 FE		No	Yes	Yes	Yes
Circuit FE		No	No	Yes	Yes
N		100,614	100,614	100,614	76,114
adj. R^2		0.008	0.073	0.074	0.072

Table 6
(Continued)

Panel C reports the result for the OLS tests using Dem_Judges to explain the horizon of firms' voluntary disclosure via Form 8-K during a quarter. The sample consists of 100,614 firm–quarters during 2004–2013. Column (1) includes only Dem_Judges; Column (2) addes control variables and year and industry fixed effects; Column (3) replaces the year fixed effect with circuit fixed effects; and Column (4) excludes observations in the 9th circuit. Cluster robust *t* statistics are reported below coefficient in parentheses, with standard errors clustered by both firms and quarters. *, **, *** indicates significance at 0.1, 0.05, and 0.01 level, respectively. Variable definitions are in Appendix A.

Panel C: Horizon of Voluntary Disclosure

		(1)	(2)	(3)	(4)
Dependent Variable:		Horizon	Horizon	Horizon	Horizon
Dem_Judges	–	-1.056^{***}	-0.701^{***}	-0.743^{***}	-0.616^{**}
		(-9.77)	(-6.47)	(-2.75)	(-2.31)
Size	+		0.096^{***}	0.089^{***}	0.078^{***}
			(5.82)	(5.45)	(4.03)
Lev	+		0.023^{***}	0.018^{***}	0.018^{***}
			(4.54)	(3.66)	(3.22)
RD	.		0.177	0.489	0.642
			(0.35)	(0.96)	(0.98)
MB	.		-0.004	-0.001	-0.002
			(-1.39)	(-0.47)	(-0.69)
Loss	+		0.042	0.050	0.052
			(1.31)	(1.55)	(1.42)
NegNews	+		0.110^{***}	0.105^{***}	0.108^{***}
			(6.67)	(6.17)	(5.72)
News	+		0.146^{**}	0.087	0.082
			(2.24)	(1.32)	(0.94)
Analyst	.		-0.060^{**}	-0.075^{***}	-0.069^{**}
			(-2.13)	(-2.73)	(-2.15)
IO	.		0.045	0.038	0.076
			(0.70)	(0.61)	(1.09)
BIG4	.		-0.057	-0.003	0.031
			(-1.12)	(-0.06)	(0.51)
Volatility	.		0.324^{*}	0.096	0.046
			(1.84)	(0.50)	(0.20)
SDROA	.		0.098^{*}	0.077	0.099
			(1.73)	(1.35)	(1.33)
FQTR4	+		0.428^{***}	0.461^{***}	0.452^{***}
			(17.23)	(8.85)	(8.63)
Constant		2.635^{***}	1.702^{***}	1.027^{**}	0.967
		(42.46)	(3.89)	(2.33)	(1.46)
Year FE		No	Yes	No	No
SIC2 FE		No	Yes	Yes	Yes
Circuit FE		No	No	Yes	Yes
N		100,614	100,614	100,614	76,114
adj. R^2		0.009	0.048	0.049	0.044

Table 7
Firm Size, Litigation Risk, and Voluntary Disclosure

This table reports the testing results in subsamples partitioned by firm size. The full sample consists of 100,614 firm–quarters during 2004–2013, and the small and large firms sample each consists of 50,307 firm–quarters. Columns (1), (3), and (5), are small firms sample, and columns (2), (4), and (6), are large firms sample. Columns (1) and (2) conduct the logit test, using Dem_Judges to predict the likelihood of firms' issuance of voluntary disclosure. Columns (3) and (4) conduct the OLS test for the frequency of firms' voluntary disclosure. Columns (5) and (6) conduct the OLS test for the horizon of firms' voluntary disclosure. All models include all the control variables, and the industry and circuit fixed effects. Cluster robust *t* statistics are reported below coefficient in parentheses, with standard errors clustered by both firms and quarters. *, **, *** indicates significance at 0.1, 0.05, and 0.01 level, respectively. Variable definitions are in Appendix A.

Dependent Variable:		Issue		Freq		Horizon	
Firm Size Subsample:		Small	Large	Small	Large	Small	Large
		(1)	(2)	(3)	(4)	(5)	(6)
Dem_Judges	–	−0.301	−1.004***	−0.009	−0.218***	−0.354	−1.013***
		(−0.99)	(−3.39)	(−0.10)	(−2.58)	(−0.91)	(−3.44)
Size	+	0.204***	0.029	0.065***	0.020**	0.199***	0.010
		(7.21)	(1.05)	(8.49)	(2.22)	(6.60)	(0.38)
Lev	+	0.016***	0.027***	0.005***	0.011***	0.016***	0.022***
		(2.61)	(3.22)	(2.85)	(3.94)	(2.60)	(2.99)
RD	.	0.887*	−1.135	0.465***	−0.208	0.772	−1.616
		(1.75)	(−0.98)	(3.07)	(−0.61)	(1.48)	(−1.35)
MB	.	−0.003	−0.003	−0.001	−0.002*	−0.003	−0.001
		(−0.68)	(−0.56)	(−0.92)	(−1.69)	(−0.88)	(−0.17)
Loss	+	0.072*	0.142***	0.030***	0.054***	0.030	0.115***
		(1.94)	(3.19)	(2.99)	(4.15)	(0.76)	(2.63)
NegNews	+	0.081***	0.139***	0.018***	0.034***	0.091***	0.104***
		(3.67)	(5.68)	(3.19)	(5.32)	(4.16)	(4.82)
News	+	0.229***	0.176	0.086***	0.051	0.231***	0.119
		(3.07)	(0.69)	(4.10)	(0.78)	(3.21)	(0.55)
Analyst	.	−0.060*	−0.080**	−0.012	−0.018	−0.069**	−0.070*
		(−1.94)	(−2.05)	(−1.32)	(−1.47)	(−2.08)	(−1.82)
IO	.	−0.145	−0.078	−0.038	−0.026	−0.156	−0.063
		(−1.42)	(−1.00)	(−1.41)	(−1.05)	(−1.44)	(−0.79)
BIG4	.	−0.036	−0.144	−0.020	−0.035	−0.042	−0.164
		(−0.70)	(−1.39)	(−1.45)	(−1.22)	(−0.77)	(−1.61)
Volatility	.	0.068	−0.002	0.099**	0.137	0.048	0.081
		(0.36)	(−0.01)	(1.97)	(1.28)	(0.23)	(0.25)
SDROA	.	0.136*	−0.052	0.060***	−0.006	0.104	−0.054
		(1.96)	(−0.29)	(2.82)	(−0.10)	(1.61)	(−0.30)
FQTR4	+	0.341***	0.296***	0.119***	0.101***	0.528***	0.390***
		(7.24)	(6.55)	(8.54)	(6.88)	(9.20)	(8.52)
Constant		−0.875**	−0.825**	0.209	0.113	1.124**	1.295***
		(−2.07)	(−2.19)	(1.43)	(1.01)	(2.41)	(3.19)
Circuit FE		Yes	Yes	Yes	Yes	Yes	Yes
Industry FE		Yes	Yes	Yes	Yes	Yes	Yes
N		50,307	50,307	50,307	50,307	50,307	50,307
psu./adj. R^2		0.027	0.042	0.057	0.089	0.044	0.063

Table 8
Litigation Risk and Voluntary Forward-Looking Disclosure

This table reports the testing results for forward-looking (Fwl) versus non-forward-looking (Non-Fwl) disclosure. The full sample consists of 100,614 firm–quarters during 2004–2013. Columns (1), (3), and (5), are for forward-looking disclosures. Columns (2), (4), and (6), are for non-forward-looking disclosures. Columns (1) and (2) conduct the logit test, using Dem_Judges to predict the likelihood of firms' issuance of voluntary disclosure. Columns (3) and (4) conduct the OLS test for the frequency of firms' voluntary disclosure. Columns (5) and (6) conduct the OLS test for the horizon of firms' voluntary disclosure. All models include the control variables, and the industry and circuit fixed effects. Cluster robust *t* statistics are reported below coefficient in parentheses, with standard errors clustered by both firms and quarters. *, **, *** indicates significance at 0.1, 0.05, and 0.01 level, respectively. Variable definitions are in Appendix A.

Dependent Variable:		Issue		Freq		Horizon	
		Fwl	Non-Fwl	Fwl	Non-Fwl	Fwl	Non-fwl
		(1)	(2)	(3)	(4)	(5)	(6)
Dem_Judges	–	−0.630***	0.085	−0.123*	0.014	−0.655**	0.036
		(−2.79)	(0.23)	(−1.85)	(0.50)	(−2.36)	(0.26)
Size	+	0.099***	0.155***	0.038***	0.013***	0.085***	0.057***
		(6.52)	(7.42)	(8.02)	(6.99)	(5.32)	(6.61)
Lev	+	0.019***	0.019***	0.007***	0.003***	0.018***	0.009***
		(3.84)	(3.13)	(4.22)	(2.71)	(3.62)	(2.87)
RD	.	0.421	−1.633**	0.365**	−0.098***	0.254	−0.491***
		(0.90)	(−2.56)	(2.52)	(−2.61)	(0.52)	(−2.77)
MB	.	−0.001	−0.003	−0.001	−0.001	−0.000	−0.002
		(−0.42)	(−0.82)	(−0.98)	(−1.57)	(−0.11)	(−1.12)
Loss	+	0.101***	0.054	0.042***	0.006*	0.076**	0.016
		(3.34)	(1.28)	(4.87)	(1.76)	(2.33)	(0.99)
NegNews	+	0.112***	0.021	0.027***	0.001	0.106***	0.006
		(6.46)	(0.83)	(5.68)	(0.66)	(6.08)	(0.58)
News	+	0.106	0.127	0.047**	0.009	0.111	0.045
		(1.51)	(1.31)	(2.39)	(1.08)	(1.55)	(1.16)
Analyst	.	−0.049*	−0.093**	−0.011	−0.006*	−0.050*	−0.037**
		(−1.90)	(−2.40)	(−1.41)	(−1.80)	(−1.85)	(−2.28)
IO	.	0.035	0.055	0.000	0.004	0.048	0.020
		(0.59)	(0.67)	(0.00)	(0.46)	(0.75)	(0.57)
BIG4	.	0.018	−0.042	−0.002	−0.005	0.013	−0.020
		(0.37)	(−0.66)	(−0.13)	(−0.99)	(0.24)	(−0.85)
Volatility	.	0.357**	0.693***	0.186***	0.052***	0.337*	0.221***
		(2.00)	(3.37)	(3.49)	(2.95)	(1.70)	(2.65)
SDROA	.	0.108	0.183***	0.053**	0.023**	0.088	0.077**
		(1.46)	(2.65)	(2.25)	(2.39)	(1.29)	(1.99)
Fqtr4	+	0.279***	0.284***	0.093***	0.025***	0.422***	0.142***
		(5.55)	(9.72)	(6.05)	(10.70)	(7.36)	(11.11)
Constant		−0.999***	−3.462***	0.082***	−0.027**	1.090***	−0.050
		(−8.48)	(−20.50)	(2.62)	(−2.06)	(8.41)	(−0.85)
Circuit FE		Yes	Yes	Yes	Yes	Yes	Yes
N		100,614	100,614	100,614	100,614	100,614	100,614
psu./adj. R^2		0.017	0.019	0.038	0.016	0.027	0.014

Table 9
Litigation Risk and Voluntary Forward-Looking Earnings Disclosure

This table reports the testing results for forward-looking-earnings (FwlE) versus non-forward-looking-earnings (Non-FwlE) disclosure. The full sample consists of 100,614 firm–quarters during 2004–2013. Columns (1), (3), and (5), are for forward-looking-earnings disclosures. Columns (2), (4), and (6), are for non-forward-looking-earnings disclosures. Columns (1) and (2) conduct the logit test, using Dem_Judges to predict the likelihood of firms' issuance of voluntary disclosure. Columns (3) and (4) conduct the OLS test for the frequency of firms' voluntary disclosure. Columns (5) and (6) conduct the OLS test for the horizon of firms' voluntary disclosure. All models include the control variables, and the industry and circuit fixed effects. Cluster robust *t* statistics are reported below coefficient in parentheses, with standard errors clustered by both firms and quarters. *, **, *** indicates significance at 0.1, 0.05, and 0.01 level, respectively. Variable definitions are in Appendix A.

Dependent Variable:		Issue		Freq		Horizon	
		FwlE	Non-FwlE	FwlE	Non-FwlE	FwlE	Non-fwlE
		(1)	(2)	(3)	(4)	(5)	(6)
Dem_Judges	–	-0.882^{***}	-0.238	-0.131^{***}	-0.014	-0.696^{***}	-0.232
		(-3.62)	(-1.01)	(-3.56)	(-0.22)	(-3.73)	(-0.84)
Size	+	0.046^{***}	0.141^{***}	0.010^{***}	0.043^{***}	0.026^{*}	0.129^{***}
		(2.70)	(9.35)	(3.81)	(9.22)	(1.91)	(8.64)
Lev	+	0.021^{***}	0.018^{***}	0.004^{***}	0.006^{***}	0.018^{***}	0.017^{***}
		(4.52)	(3.71)	(4.31)	(3.99)	(4.29)	(3.38)
RD	.	-4.309^{***}	1.877^{***}	-0.449^{***}	0.683^{***}	-2.547^{***}	1.847^{***}
		(-6.08)	(4.13)	(-6.88)	(5.05)	(-7.56)	(4.11)
MB	.	-0.007^{**}	-0.000	-0.001^{***}	-0.001	-0.005^{**}	0.000
		(-2.36)	(-0.03)	(-2.85)	(-0.64)	(-2.26)	(0.16)
Loss	+	-0.006	0.153^{***}	0.001	0.048^{***}	-0.028	0.128^{***}
		(-0.20)	(5.22)	(0.22)	(5.65)	(-1.12)	(4.17)
NegNews	+	0.138^{***}	0.048^{**}	0.022^{***}	0.010^{**}	0.097^{***}	0.045^{**}
		(8.00)	(2.37)	(7.64)	(2.05)	(7.25)	(2.42)
News	+	0.004	0.168^{**}	0.006	0.051^{***}	0.004	0.169^{**}
		(0.07)	(2.25)	(0.63)	(2.68)	(0.07)	(2.33)
Analyst	.	0.037	-0.091^{***}	0.007	-0.021^{***}	0.022	-0.088^{***}
		(1.23)	(-3.55)	(1.37)	(-2.73)	(0.92)	(-3.21)
IO	.	0.160^{**}	-0.058	0.020^{*}	-0.016	0.144^{**}	-0.064
		(2.47)	(-1.04)	(1.73)	(-0.96)	(2.55)	(-1.15)
BIG4	.	0.046	-0.018	0.006	-0.011	0.027	-0.023
		(0.78)	(-0.41)	(0.70)	(-0.96)	(0.60)	(-0.54)
Volatility	.	0.057	0.661^{***}	0.019	0.232^{***}	0.020	0.604^{***}
		(0.28)	(4.10)	(0.59)	(5.13)	(0.13)	(3.44)
SDROA	.	-0.190^{**}	0.269^{***}	-0.014^{**}	0.087^{***}	-0.098^{***}	0.236^{***}
		(-2.06)	(3.14)	(-2.15)	(3.41)	(-2.96)	(3.43)
Fqtr4	+	0.251^{***}	0.262^{***}	0.045^{***}	0.080^{***}	0.260^{***}	0.372^{***}
		(3.75)	(9.49)	(3.77)	(10.29)	(4.75)	(11.10)
Constant		-1.707^{***}	-1.645^{***}	0.076^{***}	-0.024	0.616^{***}	0.446^{***}
		(-12.81)	(-14.60)	(4.23)	(-0.83)	(6.30)	(4.00)
Circuit FE		Yes	Yes	Yes	Yes	Yes	Yes
N		100,614	100,614	100,614	100,614	100,614	100,614
psu./adj. R^2		0.022	0.018	0.027	0.038	0.025	0.027