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## Anti-corruption campaign, political connections, and court bias: Evidence from Chinese corporate lawsuits

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## ABSTRACT

This paper establishes the presence of political corruption in court and identifies a novel channel-interfering with court decisions-through which local corrupt politicians provide political favors for politically connected firms. Using a unique data set of 11,238 commercial lawsuits involving Chinese listed firms, we examine how China's recent anti-corruption campaign, one of whose goals is to combat political interference in the courts, affects court advantages of politically connected firms. We find that connected firms' win rates dropped by 6.3% after the anti-corruption, suggesting that the campaign stopped corrupt politicians transferring 1.8% of total monetary amounts of commercial disputes from unconnected to politically connected parties by influencing trials. The effect is more salient for firms connected to more powerful officials, noncontract-based cases, lower-level courts, regions with weak legal environments, and courts that depend more on local government. Moreover, anti-corruption promotes a better judicial environment, not only improves the quality of judicial decisions, but also boosts public confidence in the judicial system, and encourages firms to settle conflicts through court. Finally, we explore the campaign's broader economic influences and find that after the campaign, cities with initially poorly functioning judiciaries gained more investment, employed more labor, produced more output, and attracted more new firms, particularly in those industries with high contract intensity. Overall, the anti-corruption campaign significantly improved the judicial and economic environment in China.

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## 1. Introduction

Scholars have long documented that corruption hinders growth, and rent-seeking and corruption are thought to be pervasive around the world<sup>1</sup>. And it is no secret that corrupt officials usually divert resources into personal benefits for their families, patronage networks, and business partners, especially in transition economies where government officials have considerable discretion over determinants of economic activity. Thus, political connections are widely prevalent among firms in these countries for the explicit purpose of securing certain benefits not otherwise obtainable. In particular, while some of the favors received by politically connected firms are legitimate<sup>2</sup>, more occur through corrupt channels, which results

and even political instability. Thus, to develop more effective anticorruption policies, identifying the presence of, or corruption channels through which, corrupt officials provide political favors for politically connected firms is essential. A large body of literature has examined the corruption channels and documented that corrupt officials transfer wealth from the non-favored to politically favored parties by various means, including easier access to debt financing (Khwaja and Mian, 2005; Malesky and Taussig, 2009; Khwaja and Mian, 2011), lower land

transacted price (Chen et al., 2018; Chen and Kung, 2019), favor-

able tax treatment (Faccio, 2006), winning government contracts

(Goldman et al., 2013) and so on. However, to the best of our knowledge, none of the previous studies demonstrated direct evidence of whether courts are utilized by corrupt officials to transfer

wealth from the non-favored to politically favored parties, a novel

channel that has been largely neglected in the existing literature

and the causal relationship between corruption and court out-

comes remains little known. Examining this question is vital to

our understanding of corruption itself and its relationship to

in allocative inefficiency, undermining market competition order,

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<sup>&</sup>lt;sup>1</sup> See Krueger (1974), Murphy et al. (1993), Shleifer and Vishny (1993), Mauro (1995), Fisman and Svensson (2007), Ayyagari et al. (2014).

<sup>&</sup>lt;sup>2</sup> For instance, Acemoglu et al. (2016) find that the seemingly abnormal returns accrued to financial firms well connected to former US Secretary of the Treasury, can actually be explained by the managerial ability of the firms' owners. Bertrand et al. (2014) and Gao and Huang (2016) find that, by building connections with politicians, firms and hedge funds are able to gain superior information advantages that are not available in other ways.

judicial independence and impartiality<sup>3</sup>: there is no doubt that courts play an important role in securing private property rights and enforcing contracts, and make substantive welfare redistribution decisions. However, many developing countries have long lacked judicial independence and impartiality, and judges are often affected by corrupt local polititians, leading to massive unjust rulings and judicial corruption.

This paper exploits the staggered roll-out of China's recent anticorruption campaign, one of whose goals is to combat political interference in the courts, to examine how the campaign affects connected firms' win rates, which helps to identify whether corrupt politicians provide favors for connected firms by influencing judges. The Chinese political system was not founded on the premise of the separation of powers. Instead, Chinese courts traditionally have been viewed as part of the government. Particularly, by design, local governments directly control the funds and personnel of local courts, making it easier for corrupt local politians to interfere with court decisions. Consequently, corrupt local politicians have always been a major source of external interference in the judicial process. Aware of the seriousness of judicial corruption, President Xi Jinping promised to bring the "rule of law" upon coming to power, and in particular to make the courts immune from local politics. In 2012, President Xi launched an anti-corruption campaign whose scale and profound impact exceeded public expectations. While this anti-corruption serves a wide range of objectives, combating politicians' interference in the judiciary is one of its main goals.<sup>4</sup> This anti-corruption inspection is carried out by the Central Commission for Discipline Inspection (CCDI), the highest internal control body within the party system, and in this campaign President Xi has strengthened the CCDI and granted it unprecedented powers. Since 2012, the CCDI started to conduct regular central inspections and dispatch the central inspection teams (CITs) to all the provinces to conduct investigations, an innovative step never before taken in anti-corruption efforts. Particularly, corrupt local politicians have always been a major source of extrajudicial influence, and they are precisely the main targets of this anticorruption inspection.<sup>5</sup> In short, this anti-corruption campaign has generated a strong deterrent effect on corrupt politicians and profoundly changed their behavior in the long term, thus deterring them from interfering with court decisions<sup>6</sup>.

China is an ideal laboratory for examining the effect of the anticorruption campaign on court bias. Before the anti-corruption campaign, politicians' interference in trials is not rare, leading to many unjust rulings where politically connected parties have always won by a clear margin in court. Meanwhile, due to the large population and rapid economic growth, courts in China are playing an increasingly important role in dispute resolution and make considerable welfare redistribution decisions each year.<sup>7</sup> Therefore, promoting judicial independence and impartiality by eliminating local political interference would likely have profound welfare consequences. In addition, in 1998, the Chinese Stock Exchanges began to require all listed companies to disclose their involvement in litigation, which allows us to access the data set involving the most comprehensive information available yet on Chinese listed firms' lawsuits.

We collected 11,238 commercial lawsuits from Chinese listed firms' reports, covering 2009 to 2018, with detailed case-level information (e.g., the time and types of the dispute, outcomes, the amount claimed, court levels, etc.). Referring to common practice in the existing literature, we hand-collected information about all members of top executives' political ties from their curriculum vitae and employed the political background of firms' executives as a measure of political connections<sup>8</sup>. Using these unique datasets, we examine how China's recent anti-corruption campaign, one of whose goals is to combat political interference in the courts, affects the court advantages of politically connected firms. We find strong evidence that after the anti-corruption campaign, win rates of connected firms experience a sharp decline by 6.3% compared to unconnected firms, and the magnitude of these benefits is enormous: the anti-corruption campaign stopped corrupt politicians from transferring 1.8% of total monetary amounts of commercial disputes in the same period from unconnected firms to politically connected parties by interfering with court decisions. Furthermore, we examine whether the impact of the anti-corruption campaign on court bias varies across the strength of the political connection. In Chinese politics, administrative rank is crucial, with higher-rank administrative agencies and officials having more authority over lower-rank counterparts. When a politician's rank is higher than the president of the court, influencing court decisions is relatively easy: otherwise, it is tough. Indeed, we find the impact of the anticorruption campaign is more pronounced on firms connected to officials with a higher rank than that of the court than those associated with officials of a lower rank than the court.

We provide several pieces of evidence in favor of the identification assumption underlying our difference-in-differences estimation. First, the win-rate disparity between politically connected and unconnected firms across the treatment and control groups is statistically insignificant before the anti-corruption investigation. Second, we find that there are no significant changes in most of the key firm characteristics for these two types of firms following the campaign. And our results remain robust to a restricted sample in which we require firms to have lawsuits available both before and after the campaign. To address the selection bias caused by changes in the types of lawsuits, we restrict the sample to cases admitted before the campaign and obtain similar results. Third, the hazard model suggests that the legal environment and other local factors did not affect the timing of the investigation across different provinces. Fourth, consistent with the unanticipated nature of the campaign, we find no evidence of expectation effects. In addition, to correct for the potential biases caused by the heterogeneous treatment effects in settings with staggered treatment roll-

<sup>&</sup>lt;sup>3</sup> Throughout the paper, we define "judicial independence and impartiality" as courts make independent and impartial decisions with no or little interference from local governments and corrupt politicians. Particularly, the definition of "judicial independence and impartiality" follows Article 131 of the Constitution of People's Republic of China that "The people's scurts shall, in accordance with the provisions of law, independently exercise adjudicatory power, and shall not be subject to interference from any administrative organ, social organization or individual.".

<sup>&</sup>lt;sup>4</sup> In his anti-corruption manifesto, President Xi repeatedly pointed out the rampant presence of judicial corruption caused by politicians' interference, and explicitly highlighted that "some politicians, out of personal interest, interfere with the trial of specific cases in overt or covert ways, forcing the courts to rule against the law, which is a chronic malady that leads to judicial corruption. For the sake of justice, we must focus on resolving the issue of illegal interference in the judiciary by leading officials.".

<sup>&</sup>lt;sup>5</sup> In order to obtain information on judicial corruption of politicians, CITs have full power to investigate courts, which must comply with the CITs' investigation requests. And CIT members have the authority to search for all relevant court documents and evidence, summon court leaders and judges, and question parties involved in relevant cases.

 $<sup>^6</sup>$  This is also echoed by the Rule of Law ("ROL") index from the Worldwide Governance Indicators for China. The ROL indicator ranges from -2.5 to 2.5, with higher numbers representing a higher level of rule of law in society. Over the almost two decades before the campaign (1996–2011), China's ROL Indicator was quite stable, ranging roughly from -0.4 to -0.6. However, this indicator has improved impressively since the anti-corruption campaign, rising sharply from -0.5 in 2012, the year before the campaign, to -0.05 in 2020.

 $<sup>^7</sup>$  For example, the total numbers of adjudicated cases in all Chinese courts rose from 7.2 million in 2014 to 23 million in 2019.

<sup>&</sup>lt;sup>8</sup> Specifically, if any director of a specific firm is (or was) a government official at the level of section chief (kezhang) or above or a chief member (chairman or vice-chairman) of the People's Congress or the People's Political Consultative Conference at the national or the subnational level, the firm is identified as politically connected firm.

outs, we use the novel imputation estimator proposed by Borusyak et al. (2021)<sup>9</sup> and find that treatment effect heterogeneity is less of a concern in our setting.

Moreover, we also discuss two major alternative interpretations. To start with, we provide evidence against the competing explanation that the reduction in the win rate of connected firms simply reflects a decline in their financial performance following the anti-corruption campaign, which may make them harder to hire better lawyers. However, we do not find empirical evidence that anti-corruption has a differential impact on the financial performance between connected and unconnected firms. More importantly, we find no evidence that the anti-corruption heterogeneously affected the quality of law firms hired by firms with and without connections. The second alternative interpretation is that there are no corrupt politicians and undue political influence on the judges, but rather collusion between corrupt judges and connected firms, and the anti-corruption directly eradicated corrupt judges so that the connected firms won less. However, it is difficult to explain why absent the intervention of politicians, judges would be more likely to be captured by and favor politically connected firms than unconnected ones<sup>10</sup>. Moreover, this alternative explanation is also incompatible with this campaign's targets and some of our empirical findings and is therefore less of a concern in our context. On the one hand, in China, corrupt local politicians have always been a major source of external interference in trials, and they are precisely the main targets of this inspection. On the other hand, results in Sections 4.3 and 5 further validate our claims that this campaign reduces court bias primarily by deterring politicians from interfering with trials. Specifically, we find that the impact of anti-corruption on court bias varies between courts with different levels of dependence on governments or between firms with different strengths of political connections. If the alternative hypothesis holds, we should not observe such differences.11

Our heterogeneity analysis reveals that the impact of the anticorruption campaign on court bias varied across provinces, cases, and courts in a theoretically predictable manner, which provides greater confidence in the conclusions. First, anti-corruption plays a more significant role in weak legal environment regions where politically connected parties can manipulate legal proceedings to their advantage relatively easier. Second, the effect of anticorruption is more pronounced in low-ranking courts, where judges are more vulnerable to external interference from corrupt local politicians than in higher-level courts, as a distinctive feature of Chinese politics is the heavy emphasis on political rank. Third, the results are more significant in noncontract-based disputes than contract disputes because the rights and obligations of both parties are clearly set out in the contractual agreement and therefore there is little room for political maneuver in deciding contract disputes.

Then, we explore whether the impact of the anti-corruption varies across courts with different levels of dependence on local governments, whereby we hope to provide suggestive evidence on how or why local corrupt politicians can interfere with trials, thus further validating our proposition. Specifically, in China, the local courts depend on the local government for personnel appointments and budgets, and the more dependent local courts are on local government, the more difficult it is for them to defend themselves against corrupt political interference. Consistent with our interpretation, we find that in courts that rely more on local government (where some court leaders faced stronger career concerns or some courts were under greater financial pressures), politically connected companies have a higher pre-campaign win rate, and in such cases, the anti-corruption campaign's effects were stronger.

Moreover, we explore the anti-corruption campaign's broader impact on the local judicial environment. Across various measures commonly used in the law literature, we find consistent evidence that the anti-corruption campaign has not only made court rulings less favorable toward politically connected firms but also led to significant improvements in the quality of judicial decisions: (a) trial efficiency increased by around 20%; (b) court verdicts provided more detailed judicial reasoning in judgment files<sup>12</sup>; (c) judges were less likely to cite discretionary codes in judicial reasoning<sup>13</sup>; (d) judges became more likely to approve requests for key evidence examination<sup>14</sup>. In addition, we also find that following the anti-corruption investigation, public confidence in the judicial system witnessed a considerable increase, and firms were increasingly resorting to litigation to resolve disputes. In short, these findings provide strong evidence that this anti-corruption campaign has promoted a better judicial environment.<sup>15</sup>

Finally, beyond judicial outcomes, we further link judicial independence and impartiality to economic growth by investigating how regional economic performance has responded to the increase in judicial independence and impartiality caused by anticorruption campaigns<sup>16</sup>. The intuition is that the poorer the local judicial quality before the anti-corruption, the more the anticorruption campaign improves its judicial environment, and thus the greater the impact on local economic performance. We find that after the anti-corruption campaign, the cities with initially poorly functioning judiciaries gained more investment, employed more labor, produced more output, and witnessed a more pronounced increase in productivity than the cities with well-functioning judiciaries. Then, we examine how the anti-corruption campaign affects firms' entry decisions. Our findings show that cities with initially weak judiciaries attracted more new firms and industries with high

<sup>&</sup>lt;sup>9</sup> This imputation method is similar to other proposed estimators (Wooldridge, 2021; Gardner, 2022), which allows for unrestricted treatment effect heterogeneity and avoids the OLS parameter weighting problem. Several robust estimators have been recently proposed to correct for the potential biases of the traditional staggered DID approach. Particularly, relative to these estimators (e.g., de Chaisemartin and D'Haultfoeuille, 2020; Sun and Abraham, 2021), the imputation approach proposed by Borusyak et al. (2021) has attractive efficiency properties, is transparent, and has conservative standard errors that can be calculated analytically, and thus has been widely used in the recent literature. More importantly, to our knowledge, the imputation estimator of Borusyak et al. (2021) is the only new estimator that can both handle repeated cross-section data and allow for a triple difference design, and is therefore best suited to our situation. And our lawsuit data is a repeated cross-section, and we primarily use a triple difference design.

<sup>&</sup>lt;sup>10</sup> One may argue that connected firms tend to have greater financial capabilities and resources, making them easier to capture the courts, even without the influence of politicians. But, in our matched sample, we observe no significant differences between connected and unconnected firms in most firm characteristics, except for their political connection status.

<sup>&</sup>lt;sup>11</sup> In Section 5, we find that when some court leaders face stronger career concerns or courts are under greater financial pressure, corrupt politicians' interference in trials becomes more common and connected firms have a higher win rate before the campaign, and the effects of anti-corruption are more salient in such a scenario. And in Section 4.3, we find that anti-corruption has a greater impact on firms connected to officials with a higher rank than that of the court. If the alternative hypothesis holds, we would not observe differences in the impact of anti-corruption on court bias between courts with different levels of dependence on local governments or between firms with different strengths of political connections.

<sup>&</sup>lt;sup>12</sup> Longer judicial reasoning has been documented to correlate with decision quality (Liu, 2018).

<sup>&</sup>lt;sup>13</sup> A verdict is potentially more distorted if the judge imposes excessive discretion in his judicial reasoning (Liu and Li, 2019).

<sup>&</sup>lt;sup>14</sup> Allowing key evidence examination is associated with more fair trials (Edmond and Roberts, 2011).

<sup>&</sup>lt;sup>15</sup> These results rule out the alternative explanation that anti-corruption did not actually lead to better court decisions, but instead enabled judges to make negligent rulings, in which case the courts replace one bias with another and the decline in connected firms' win rates may not indicate an improvement in judicial decisions' quality.

<sup>&</sup>lt;sup>16</sup> Specifically, we adopt a triple difference strategy to compare the differences in changes in economic performance following the anti-corruption campaign between cities with initially poorly and well-functioning judiciaries.

Journal of Public Economics 222 (2023) 104861

contract intensity benefit more from the improvement in the judicial environment, as these industries are more dependent on the judiciary than others due to the need for relationship-specific investments.

This study makes several contributions to the literature. First, our study augments the literature on channels through which corruption and rent provision occur. Prior research documents that corrupt officials provide political benefits for their families, patronage networks, and important business partners by various means, including interference in the financial market, land market, tax collection, government contracts, etc.<sup>17</sup> However, whether corrupt officials provide benefits for politically favored parties by interfering with court decisions has been largely neglected in the existing literature, given that courts are important institutions for wealth redistribution in the market economy. Our study is the first to establish the presence of political corruption in court, and identify the novel channel-influencing court decisions-through which, corrupt officials in countries with weak judicial systems provide political favors for politically connected firms. In addition, it also speaks to the literature on judicial independence and impartiality and economic development. While considerable theoretical work and cross-country literature have long stressed the role of judicial independence and impartiality in economic growth<sup>18</sup>, nevertheless, there has been little rigorous causal evidence on how judicial independence and impartiality affects court outcomes and thus economic activities<sup>19</sup>. We contribute to this literature by showing how regional economic performance responds to an increase in judicial independence and impartiality induced by the anti-corruption campaign targeting political influence on judges. Therefore, we provide empirical support for the theory and mechanisms behind many of these seminal studies.<sup>20</sup>

Second, the paper speaks to the recent and vibrant literature on the determinants of judicial independence and impartiality. Our contribution lies in highlighting periodic anti-corruption campaigns aimed at combating undue political influence in courts as a new source of insulating judges from local corrupt political interference and enhancing judicial independence and impartiality in countries where corrupt politicians have always been a major source of rampant judicial corruption. Previous research has focused on various institutional factors that influence the independence and impartiality of the judicial system, including the power relationship between the presidency and the congress (Iaryczower et al., 2002; Franck, 2009) and the appointment procedures or tenures of judges (Hanssen, 2004; La Porta et al., 2004; Klerman and Mahoney, 2005; Cameron et al., 2019; Mehmood, 2022). All these previous studies focus on the changes in pressure faced by judges coming from tenure status of positions or the intensity of the parliamentary struggle. In contrast, we exploit exogenous variation in the incentives of politicians (rather than judges) and show that in countries with weak judicial systems, anti-corruption campaigns targeting politicians' interference in court decisions can significantly improve judicial independence and impartiality by increasing the risks and costs of political interference in the judiciary, without causing substantive changes of the judicial system. In this sense, our study sharpens our understanding of judicial independence and impartiality itself, particularly how it can be promoted practically in developing countries with the weak judicial system.

Third, our paper contributes to the sizable literature on the value of firms' political connections. Prior work shows that politically connected firms receive various favors, including access to bank loans, favorable tax treatment, government-sponsored bailouts, winning government contracts, and so on. However, unlike previous literature, we focus on the court advantage of politically connected firms, an issue that has been largely neglected in the existing literature<sup>21</sup>. Our contribution is to exploit a change in the institutional environment that largely deterred politicians from interfering with court decisions, namely China's anti-corruption campaign, and to show that after the campaign, win rates of connected firms experienced a sharp decline, which even completely offset the positive effect of political connections on court outcomes before the campaign. Our analysis is the first to provide causal evidence that the courts' favoritism toward politically connected companies arises from the corruption channel.

The rest of the paper is organized as follows. Section 2 introduces the institutional background on the judicial system of China and the anti-corruption campaign. Section 3 presents empirical strategy and data. Section 4 presents and discusses the main results. Section 5 explores whether the impact of the anticorruption campaign on court bias varies across courts with different levels of dependence on local governments. Section 6 further examines the effects of the anti-corruption campaign on other judicial outcomes, while Section 7 discusses the economic impact of the increase in judicial independence and impartiality caused by this campaign. Section 8 concludes.

## 2. Institutional background

## 2.1. China's judicial system and its dilemma

In this section, we provide background on the structure of China's judiciary, its relationship with the government, and some of the current problems the courts face.

## 2.1.1. The legal environment and court system in China

China's legal system is a large civil law system, reflecting the influence of continental European legal systems and especially the German civil law system of the nineteenth and early twentieth centuries. Recent developments include the recognition of private

<sup>&</sup>lt;sup>17</sup> See Khwaja and Mian (2005), Faccio (2006), Malesky and Taussig (2009), Khwaja and Mian (2011), Goldman et al. (2013), Chen et al. (2018), and Chen and Kung (2019), and so on.

<sup>&</sup>lt;sup>18</sup> See Smith (1937), Hamilton (1788), Hayek (1960), Buchanan (1974), North (1986), Glaeser and Shleifer, (2002), La Porta et al. (2004, 2008), Besley and Persson (2011), and Acemoglu and Robinson (2012).

<sup>&</sup>lt;sup>19</sup> Although a growing body of literature has exploited judicial reforms to identify the causal effect of judiciary (Visaria, 2009; Chemin, 2009; Chemin, 2012; Lilienfeld-Toal et al., 2012; Lichand and Soares, 2014; Ponticelli and Alencar, 2016; Chemin, 2020; Chemin, 2021), these reforms have primarily targeted access to justice or judicial efficiency rather than judicial independence and impartiality. Notable exceptions are Mehmood (2022), which finds that when the judge selection procedure changed from Presidential appointment to appointment by peer judges, rulings in favor of the government declined dramatically and real estate investments increased.

<sup>&</sup>lt;sup>20</sup> Our work also contributes to the literature on the economic consequences of corruption, including economic growth, investment, provision of public goods, and firm profitability and innovation (e.g., Mauro, 1995; Paunov, 2016; Reinikka and Svensson, 2004; O'Toole and Tarp, 2014). We provide evidence that corruption also worsens the judicial environment, undermining judicial impartiality and public confidence in the judicial system.

<sup>&</sup>lt;sup>21</sup> To the best of our knowledge, only a few recent studies have examined the link between political connections and court outcomes. For instance, He and Su (2013), Lu et al. (2015), and Xu (2020) find that politically connected firms have a higher win rate in court than unconnected firms. However, all of the above studies examine court outcomes of political connections by comparing simple differences in court outcomes between firms with and without political connections, which may tell us little about the causal effect. In particular, differences in outcomes between connected firms and others may reflect different managerial abilities, resources, or other characteristics associated with political connection has a positive effect on court outcomes, whether or not the court advantage obtained through such connections constitutes corruption remains a contentious issue. For instance, the court advantage of politically, informational advantage or other characteristics associated with political connections.

property rights and the enactment of laws and procedures concerning commercial disputes. China's modern market-supporting laws, such as the Contract Law (1994), Company Law (2005), Bankruptcy Law (2006), and Property Law (2007), are similar to their counterparts in Germany, Switzerland, and Japan. Since the 1990s, with China's market-oriented reforms, there has been a dramatic increase in the use of the courts as an important means of dispute resolution in China, and the total number of adjudicated cases in all Chinese courts rose from 0.61 million in 1978 to 25 million in 2017, a more than 40-fold increase.

China's government is divided into four levels ranging from the central government to the governments at the provincial, city (prefecture)<sup>22</sup>, and county levels. Accordingly, courts in China are institutionalized at four levels. In particular, to facilitate the conduct of trials and the participation of citizens in litigation, local courts in China are set up based on administrative regions. At the top of the structure is the Supreme People's Court (SPC) in Beijing. Below it. at the provincial level, are the thirty Higher Level People's Courts (HLPC). Below the HLPCs are the 389 Intermediate Level People's Courts (ILPC), which serve at the city level. At the bottom are over 3,000 Basic Level People's Courts (BLPC), which exist at the county level. Courts at the lower three levels are collectively referred to as "local courts." In practice, local courts, especially county-level and city-level courts, are the most numerous, geographically extensive, and broadest jurisdictional level in the entire court system. According to the 2019 Supreme People's Court Work Report, more than 90% of cases nationwide are adjudicated by local courts at the county and city levels. The level of court where a case is heard depends on the monetary amounts of commercial disputes rather than the legal issue at hand<sup>23</sup>. Meanwhile, court hearings take place in the jurisdiction where the defendant is located. Thus, litigants have no discretion in choosing the level of court to hear their cases or in finding a more favorable jurisdiction.

#### 2.1.2. Judiciary and corruption before the anti-corruption campaign

It is critical to note that the Chinese political system was not founded on the premise of separation of powers. Instead, Chinese courts traditionally have been viewed as part of the government. Under the current institutional framework, the most striking characteristic of China's judicial system lies in the relationship between the judiciary and local governments<sup>24</sup>. Specifically, the dependence of the judiciary can be mainly attributed to several specific institutional arrangements, which made China's local courts subordinate to powerful local corrupt officials before the anti-corruption campaign.

First, local governments have personnel power over the judiciary. Chinese judges have no security of tenure and are appointed and removed by the local government at the same level. For example, the president and main leaders of the court are appointed by the local government at the corresponding level, in turn, appoint vice presidents and division heads of the same courts. Through this hierarchy, local governments can effectively control the appointment and promotion of judges and thus wield significant influence over court adjudications. Second, the dependent status of courts in China is also due to its lack of financial autonomy. Under the current organizational structure, each court's annual budget is approved and managed by the local government at its corresponding levels where it is located. As the local judiciary is dependent on the local government for their expenditures, including judges' salaries and bonuses, office supplies, vehicles, and court buildings, local judges are naturally vulnerable to the interference of local officials (Peerenboom, 2009; Wang, 2013).

In short, local courts in China are neither financially nor administratively independent of local governments at their corresponding levels. This dependence grants local governments significant leverage over the courts, thus exposing judicial decisions to constant administrative interference. Since judges, similar to politicians, have incentives for their career prospects and material welfare (Segal et al., 2011; Epstein and Knight, 2013), corrupt local politicians who have strong control over judges' careers and court budget can interfere with the judicial process and instruct court leaders and judges to favor firms with close political connections in their trials by using their political and fiscal influence over the local judiciary (Peerenboom,2009; Ang and Jia, 2014; Ng and He, 2017; Wang, 2018).

As a result, in developing countries, it is common that courts are utilized to transfer wealth from the non-favored to politically favored parties (Ginsburg and Moustafa, 2008). Parties with stronger political ties come out ahead by a clear margin in the court, whereas others without political backgrounds are conceivably disadvantaged. Particularly, this form of judicial corruption caused by corrupt local politicians' interference has long been widely identified as a fundamental problem of China's judicial system, not only by legal scholars but also by many local and supreme court judges. In commercial lawsuits, it is widely believed that those powerful corrupt local officials in China often pressure local courts to rule in favor of their patronage networks and business partners, which has created significant judicial biases before the anti-corruption campaign. The impact of power and relationships on court decisions has become so pervasive that some instances are referred to as "power cases" and "relationship cases". This terminology reflects public dissatisfaction with politicians' interference in trials and suggests the court's inability to operate impartially and honestly.

Surveys on local judges and officials also suggest that local courts are vulnerable to political interference from local officials before the anti-corruption campaign. For example, according to a survey of 280 judges published in 1993, nearly 70% stated that they were subject to outside interference, with local officials as the source of interference in more than a third (34%) of cases.<sup>25</sup> In another study of 100 intermediate and basic court judges in Chongq-ing in 1998, 59% claimed interference from the local officials.<sup>26</sup>

# 2.1.3. How corrupt politicians interfere with court decisions before the anti-corruption campaign

In this subsection, we further elaborate on how politicians interfere with court decisions and how court decisions, tainted by corruption, are carried out in the process of ruling in China's courts before the anti-corruption campaign. Corrupt local officials can interfere local courts through various means, including budget control, cadre assessment, and even direct punishment (He, 2012; Li, 2016; Peerenboom, 2002; Su, 2000; Wang, 2018).

Specifically, on the one hand, the existing literature on Chinese politics suggests that political career concerns are the primary attribute of political interference in judicial decisions (He, 2012; Liebman, 2017). Some local judges find it difficult to turn down requests from local corrupt politicians for fear of losing their stipends and even their jobs (Bergara et al., 2003; Harvey and

 $<sup>^{\</sup>rm 22}\,$  We use the terms prefecture and city interchangeably throughout.

<sup>&</sup>lt;sup>23</sup> The monetary threshold for hearing cases in specific level courts varies across provinces, depending on the province's economic development. Take higher courts as an example, and if the damages claimed exceed RMB 100 million in the three wealthiest provinces, then the case must be heard by a HLPC at the provincial level. In contrast, in the poorest provinces, the threshold is only one-tenth of the former, at RMB 10 million. Compared with judges in the lower-level courts, judges in the higherlevel courts tend to be better qualified, and therefore more professional and impartial in adjudicating cases.

<sup>&</sup>lt;sup>24</sup> The local government includes local Party and government organs.

<sup>&</sup>lt;sup>25</sup> See Gong Xiangrui, ed. (1993: 33).

<sup>&</sup>lt;sup>26</sup> See Jiang Mingan (1998: 63).

Friedman, 2006; Segal et al., 2011). There have been numerous reports of judges being disciplined or removed from office for not following local politicians' instructions. For instance, a judge in Zhengzhou was removed from office simply because he tried a case in accordance with the law. However, this impartial ruling was clearly against the interests of the local politicians; thus, retaliation from the corrupt officials followed<sup>27</sup>. On the other hand, local corrupt politicians can also leverage their budgetary powers to pressure local courts to defer to their mandates. In practice, by threatening to cut court funding, salaries, and bonus, powerful local officials pressure the court to rule in favor of their patronage networks and business partners. A critical operational obstacle faced by Chinese courts, especially lower-level courts, is the lack of funding, leaving judges beholden to their government counterparts (Peerenboom, 2009; Henderson, 2009; Wang, 2013). Gechlik (2005) also finds that judges in Shanghai courts are significantly less prone to judicial corruption because they are better paid than their colleagues in other areas. In some cases, corrupt officials have threatened to cut off the funding needed to build housing for court personnel (Clarke, 1996).

Next, to get a more intuitive picture of how local politicians in China interfere with court decisions, we discuss the specific strategies local corrupt officials will take to instruct local courts to rule in favor of their allies notwithstanding the law. Since it is impossible to gather systematic quantitative evidence on officials' covert operations, we rely on qualitative evidence to explore how corrupt local politicians in China interfere with judicial decisions. Specifically, we consult primary sources, including court rulings, informal interviews with lawyers, judges, and officials, press releases from courts or relevant investigative bodies, as well as secondary sources including media reports, judges' diaries, and qualitative research in law journals. According to this evidence, we show that through their control over the courts' personnel and budgets, local corrupt politicians employ a combination of formal and informal tactics to influence court decisions, and some judges are forced to obey their instructions before the anti-corruption campaign.

To start with, we describe some overt and formal ways in which corrupt local officials interfere with court decisions before the anticorruption campaign. Given that local politicians do not attend court hearings, or write or draft court decisions, they usually exercise their decision-making power by giving instructions to their subordinates, including court leaders or judges, in regular or ad hoc meetings or private conversations with or without written decrees (Zhao, 2009). Specifically, first, the main local leaders have the power to guide and give their preferred opinions on the verdicts of important cases occurring in their jurisdictions by convening special debriefings or coordination meetings on the work of the judiciary. For instance, one is through the Political-Legal Committee-a powerful party body that controls the police, procuratorates, and courts. When cases involving important companies are involved, the powerful corrupt officials talk directly to the court president to convey their instructions through the Political-Legal Committee. Second, local corrupt authorities can also send official letters to the local courts on behalf of the government, asking them to rule in their favor or even warning them. This type of intervention takes the form of government documents, which usually have a crowning reason, such as for local economic development and social stability, etc. Third, some local corrupt politicians even direct issue internal orders to the court leaders or give instructions on relevant documents or letters in response to specific cases. Besides, another is through the Adjudication Committee-an adhoc committee and the highest decision-making body

within the court, usually composed of the court's executive leadership (e.g., the party secretary, the president, the vice president, and the division heads of the court concerned) rather than the three judges hearing the case. For some important cases, the adjudication committee will step in and make a decision behind closed doors (He and Su, 2013).

Then, we show the primary covert and informal means by which local corrupt politicians compel judges to favor their allies. For example, some local corrupt officials intercede for the parties involved in the case by making phone calls and private interviews with court leaders, giving tendentious opinions on the verdict of the case. And Hendley (2009) refers to such practices as "telephone law" because judges must follow the instructions of politicians, which are usually conveyed through phone calls. In addition, corrupt officials may write simple comments on a motion provided by the litigant with political connections, endorsing the latter's claims. In practice, not to appear dictating to the court, such instructions are usually worded in apparently objective or neutral terms, such as "handle the case properly, with care and expedition", "please adjudicate the case by the law," or "this case needs careful review". Subordinate judges interpret such instructions according to the personal preferences conveyed explicitly or implicitly by the instructor, which the subordinates are expected to observe (Jiang, 2010). Judges who are less politically savvy may be contacted by local corrupt politicians or intermediaries who give hints as to the stakes at hand. For example, one judge said that he once received an anonymous letter listing a firm's stakeholders whose case is in the judge's docket. The letter includes the names, titles, and political connections of the firm's owners (Xu, 2020).

In the process of local politicians interfering with adjudications, a notable feature is that the authority of the instructions is all borne in the rank of the instructors, from local leaders to court leaders and from court leaders to the judge handling the case. Particularly, the instruction need not be accompanied by any form of reasonable consideration, relieving local corrupt politicians from the burden of justification and from the need to base the decision on the basic premises and principles required by law (Li, 2012b). As a result, this decision-making mechanism allows corrupt powerful local officials to dictate court rulings in selected cases in which they have personal interests, without having to oversee the day-to-day operation of court affairs, which increases the capacity of powerful politicians to engage in more judicial corruption in a limited span of time.

A substantial amount of misconduct took place in the factfinding process during the trial. The most prevalent forms included admitting or excluding evidence without giving the parties equal opportunities to contest it, tampering with evidence (Tan, 2003; Zhi, 2003)<sup>28</sup>, and obstructing access to evidence by violating discovery procedures or manipulating the forensic examination results (Tan, 2000; Zhu, 2007). Besides, another common misconduct is that some judges can deliberately misrefer to the law to support politically connected firms at the behest of corrupt local officials. Through the above judicial misconduct, local judges try some cases according to the preferences of local corrupt politicians rather than the law.

Taken together, corrupt local politicians in China can force local courts to follow their instructions to rule in favor of politically connected firms by employing various overt and covert tactics, leading to a large number of unjust adjudications and serious judicial corruption before the anti-corruption campaign.

<sup>&</sup>lt;sup>27</sup> The Chinese news report can be found at https://news.sina.com.cn/c/2006-03-13/ 06319334790.shtml (accessed on September 25, 2022).

<sup>&</sup>lt;sup>28</sup> See also XinhuaNet. 2007. https://news.shangdu.com/category/10003/2007/11/ 30/2007-11-30\_840426\_10003. shtml.

#### 2.2. China's anti-corruption campaign

#### 2.2.1. The development of anti-corruption campaign in China

Many recent empirical studies have documented high levels of corruption in developing countries (Sukhtankar, 2015). Since the economic reforms of the early 1980s, corruption in China has increased significantly, which has spread into China's political, business, and even judicial systems<sup>29</sup>. Considering that corruption is an obstacle to economic growth and is hard to eliminate, the fight against corruption remains a theme in China's efforts to restore economic growth and reduce the consequences of corruption. Although previous Chinese leaders have also been critical of corruption and have made some efforts to combat it, they have had little success, especially since top officials are hardly ever investigated. On November 14, 2012, at the end of the Party's 18th National Congress, President Xi linping officially assumed the title of the General Secretary of the Communist Party of China (CPC) and Chairman of the Party Central Military Commission. In particular, China's new leadership has realized that corruption is not only a drag on economic growth but more importantly, it can seriously erode public confidence in the party and become a major threat to its survival. Thus, almost immediately upon assuming power, President Xi launched an anticorruption campaign whose scale and profound impact exceeded public expectations and is considered the most ambitious anticorruption campaign since the Mao era (Oster, 2014).

Anticorruption efforts are carried out by the Central Commission for Discipline Inspection (CCDI), the highest internal control body within the party system whose goal is to root out corrupt officials. In this fight against corruption, President Xi has strengthened the CCDI and granted it unprecedented powers. Under the leadership of Wang Qishan, secretary of the CCDI, the CCDI has announced that it would start to conduct regular central inspections and dispatch the central inspection teams (CITs) to all provinces to conduct thorough anti-corruption investigations. In particular, the launch of the central inspection was an innovative step never before taken in anti-corruption efforts. During this campaign, the reformed CCDI relied on their own intelligence and dispatched inspection teams to the targeted units without warning: this allegedly renders the campaign more effective (Yuen, 2014; Pei, 2016).<sup>30</sup> To obtain information on the corruption of their targets, CITs have full power to investigate all organizations at all levels, including local party and government organs, courts, procuratorates, public security, etc., and they must comply with the CITs' investigation requests. CIT members have the authority to search for all relevant documents and evidence, summon officials, question witnesses, interview officials and citizens, and participate in officials' meetings, among other things. And during this anti-corruption campaign, CITs are granted unlimited powers to investigate, detain, and interrogate

almost anyone potentially involved in corruption, no matter how high ranking they are<sup>31</sup>.

During 2012–2015, the CCDI conducted four phases of inspections, covering 31 provinces in China. Specifically, in 2012, the first investigation team was assigned to two provinces, Sichuan and Guangdong, where senior government officials have been arrested. The second phase of the investigation began in 2013 and was spread to eight additional provinces. In 2014, the third phase started, covering another 12 provinces. Geographically, as of early 2016, at least one provincial official in each of the 31 provinces had been investigated for corruption. After finishing the first-round investigation, the CITs started the second-round investigations to "look back" at previously inspected provinces in 2016 and completed them in 2017, to check the progress of rectification of the last inspection.

This Chinese anti-corruption investigation shows the following salient features. First, the design of the anti-corruption inspections reduces the possibility of inspectors being captured or colluding with the target province. Specifically, members of CITs do not inspect their own localities, functional areas, or workplaces; so, they do not continuously investigate the same province. In addition, the appointments of inspection team leaders are also not permanent. Instead, they are replaced upon completion of each assignment. Second, the anti-corruption campaign came as a relatively exogenous event, largely a surprise to the general public, firms, and local governments. The relevant literature<sup>32</sup> points out that it is unprecedented that the announcement of the anticorruption came only 20 days after the National Congress, rather than a year later, during the Third Plenary Session of the Central Committee, when new policies are usually announced. Particularly, CITs maintain a low profile and are required to follow inspector discipline, with information about the investigation being kept strictly confidential. Thus, the public, media, and companies did not know which province inspection team was investigating until the anticorruption investigation was disclosed on the CCDI website. Moreover, according to the 'three un-fixed' policy implemented by the central government, the inspection team, the time and location of the inspection to be carried out are all unfixed, making it more difficult for local offcials to anticipate the movement of inspectors. Third, in addition to the wide range of indictments, President Xi's anti-corruption campaign featured high persistence, covering his entire tenure (2012-present) (Chen and Kung, 2019; Chen et al., 2020). The CITs often adopt a circumvented approach, in which local investigations consist of several iterations and random recurrence. For instance, less than a year after wrapping up the first-round investigation in 31 provinces, to check the progress of rectification of the last inspection, in 2016, the CITs started the second-round investigation to "look back" to previously inspected provinces and completed in 2017. At the beginning of his second term (2017-2022), President Xi started the third round of investigations in the provinces in 2018 and completed the round in 2020. The unprecedented intensity and frequency of inspections enabled CITs to curb corruption more thoroughly and, as a result, this campaign is believed to have generated a very strong deterring effect on officials, making them "unable and unwilling to be corrupt". In sum, anticorruption not only eradicated a large number of corrupt officials; it also changed the ruling pattern of uninvestigated officials in the long term.

This anti-corruption campaign is incomparable and different from any previous anti-corruption measures in its broad scope, enormous strength, profound influence, and fruitful achievements in the fight against corruption. For example, according to the data

<sup>&</sup>lt;sup>29</sup> According to a 2003 survey by Transparency International, China ranked in the bottom half of the Corruption Perceptions Index with a score of 3.5 (on a scale of 1 to 10, with lower scores indicating greater public perceptions of corruption); in 2015, that score (now on a scale of 1 to 100) rose to 37.

<sup>&</sup>lt;sup>30</sup> Previously, the local commission's efforts to detect corruption had been hampered by their provincial superiors from the same province who understandably wanted to cover up scams at the lower levels.

<sup>&</sup>lt;sup>31</sup> Due to the fact that Chinese courts traditionally have been viewed as part of the government, powerful local politicians in China have strong control over the local courts. As a result, if the case was investigated in an open process, powerful local officials and the leaders of local courts may collude to allow corrupt officials to escape punishment, which could undermine the effectiveness of the anti-corruption campaign. Thus, in order to reduce local elite capture and break the collusion between the courts and local politicians, in this campaign, once a case is approved, the accused official is placed under "double restraint", meaning that the accused is confined for questioning at a stipulated time and place under the supervision of the CCDI, without judicial involvement or oversight. According to the CCDI, this policy gives the CITs priority over the judiciary when investigating corruption of local politicians, and facilitates the gathering of evidence.

<sup>&</sup>lt;sup>32</sup> See Lin et al. (2016), Pan and Tian (2020), Fang et al. (2018), Li et al. (2022), Sun et al. (2018), and Giannetti et al. (2021).

of Chinafile, between the 18th National Congress of the Communist Party of China (NCCPC) and June 2016, 174 high-ranking government officials, including five national leaders, and more than 270 thousand bureaucrats at different levels were arrested and punished for corruption activities, with a total value of RMB 2 billion in funds and assets involved in these cases (Xu and Yano, 2017).

## 2.2.2. How the anti-corruption campaign affected political interference in the judiciary

While inspections under President Xi have served a wide range of goals, combating interference in the judiciary by politicians, is one of the targets in his anti-corruption campaign shortly after assuming office in 2012, and this target even spanned his entire tenure. In his anti-corruption manifesto<sup>33</sup>, President Xi repeatedly pointed out the rampant presence of judicial corruption caused by politicians' interference, and explicitly highlighted that "some politicians, out of personal interest, interfere with the trial of specific cases in overt or covert ways, forcing the courts to rule against the law, which is a chronic malady that leads to judicial corruption. For the sake of justice, we must focus on resolving the issue of illegal interference in the judiciary by leading officials." In his speech at the Central Conference on Political and Legal Work on January 7, 2014, President Xi stressed that "we must take the fight against judicial corruption as an important task in the anti-corruption campaign." It is clear from President Xi's many speeches on anti-corruption that he has made combating judicial corruption as one of the main objectives of the fight against corruption<sup>34</sup>. Moreover, in the "Regulations on Inspection Work of the Communist Party of China" published by the CCDI<sup>35</sup>, it is clearly stated that one of the priorities of inspection work is to monitor and investigate whether there are serious problems with party leaders interfering in the judiciary and undermining the rule of law.

Particularly, it is commonly acknowledged that in China, local corrupt powerful politicians have always been a major source of external interference in the judicial process and of judicial corruption, and they are precisely the main targets of this anti-corruption inspection. According to the CCDI, the central inspection teams mainly investigated corruption in the local party and government organs, including party committees, governments, the People's Congresses, and the People's Political Consultative Conferences<sup>36</sup>, which are decision-making bodies of local governments and hold the greatest power and authority over local governance, and are

<sup>35</sup> See: https://www.81.cn/gnxw/2015-08/16/content\_6633263.htm.

therefore the most prevalent source of extrajudicial influence in China.

The common procedure of the CCDI's anti-corruption investigation mainly includes several steps: The first is preparation for the inspection. The CITs collect corruption issues of inspected provinces from the organs of the CCDI, the Central Organization Department, the Audit Office, the State Bureau of Letters and Visits, and other authorities, and then formulate the inspection work plan. Second, more extensive information on corruption is further gathered during their visits. The CITs then stay in the inspected provinces for about two months, with their contact information open to the public, during which they will extensively gather information on corruption activities through various channels, such as local disciplinary inspectors, anti-graft agency officials, retired officials, and the public, as well as audits and interrogations. All the evidence or clues of corruption cases would be reported to the CCDI for further information gathering and investigations through access to relevant institutions and individuals. For instance, when relevant clues or charges of judicial corruption are received, the inspection team may visit the following organs for further investigations: local party and government organs such as the discipline inspection commission, the political and legal affairs commission, the organization department, the procuratorate, the public security bureau; relevant courts and judges; law firms and legal experts; parties involved in relevant cases and other organs and persons with knowledge of the case. Third, once a case is approved, the CCDI implements formal investigative procedures, such as Shuanggui (the practice of detaining individual party members for investigation). In particular, to prevent interference from local protectionism, the inspection teams have unlimited powers to investigate, detain and interrogate almost any officials who may be involved in corruption, no matter how high ranking they are. Fourth, after the inspection, the CITs summarize their findings based on numerous corruption-related problems they identified and report them to the CCDI, and provide instructions to provincial governments on how to address these corruption issues. And the CITs regularly monitor and check the rectification of the inspected provinces.

In particular, in this campaign, information-gathering plays an important role in discovering corruption, especially illegal political interference in court decisions, as judicial corruption is often covert and difficult to be detected directly. The CCDI has developed general procedures for CITs to facilitate information collection. Specifically, inspectors reportedly relied on several main channels to gather information on corruption in targeted provinces: first of all, accepting complaints in the form of letters, mails, calls, and visits. Bottom-up citizen participation has played an important role in exposing and reporting the judicial corruption of local politicians. Before the campaign, some citizens and the media were afraid to expose judicial corruption due to the sensitive nature of this issue. In these campaigns, attention from the central government in the campaigns provides an opportunity for them to report judicial corruption, with less fear of retaliation from accused officials than usual. Since the anti-corruption campaign, the CCDI has received a total of 10.78 million whistleblower-type letters or visits from the public.<sup>37</sup> Second, reading and copying documents, files, and meeting minutes. This method is effective in detecting judicial corruption where politicians interfered with trials in a formal way, which, as we mentioned in Section 2.1.3, may be recorded in secret court documents. These documents are usually classified as adjudicative secrets and archived in separate dossiers to which litigants do not have access, but the CITs are authorized to access these documents, which helps them to uncover evidence of judicial corruption. Third, local visits and field trips. After receiving clues or

<sup>&</sup>lt;sup>33</sup> See the book "Excerpts from Xi Jinping's Discourses on the Construction of a Clean and Honest Administration and Anti-Corruption Struggle". On January 11, 2015, the book "Excerpts from Xi Jinping's Discourses on the Construction of a Clean and Honest Administration and Anti-Corruption Struggle", edited by the CCDI, was published. The book includes nine chapters with more than 40 key documents, consisting of President Xi's speeches, articles and instructions on China's anti-corruption campaign between 2012 and 2014, many of which were published publicly for the first time, an important source of information for identifying this anti-corruption's priorities. Particularly, two of the nine chapters highlighted judicial corruption.

<sup>&</sup>lt;sup>34</sup> In addition, at the national political and legal work conference held in January 2013, President Xi demanded that legal personnel must believe in and adhere to the rule of law, obey only the facts and the law, and set up isolation walls against extralegal interference in all aspects of law enforcement and case handling, and whoever violates the system should be given the most severe punishment and be held criminally responsible. And, at the Third Plenum of the 18th Congress of the Chinese Communist Party held in 2013, President Xi proposed to "build a China under the rule of law" and made the rule of law as its theme, which is unprecedented in the history of the Chinese Communist Party. Even on January 24, 2021, at the fifth plenary session of the 19th Central Discipline Inspection Commission, Xi again emphasized the critical areas of anti-corruption, and judicial corruption was one of them.

<sup>&</sup>lt;sup>36</sup> These four departments make up the entire local political system in China, and their leaders (taking prefecture as an example) are the party secretary, the mayor, the chairman of the Municipal People's Congress and the chairman of the People's Political Consultative Conference, all of whom are the most powerful leaders in local governments.

<sup>&</sup>lt;sup>37</sup> See https://www.mnw.cn/news/china/1714107.html.

charges of judicial corruption, the CITs would visit involved courts and parties or victims, who are asked to cooperate with the CITs to provide more evidence. Fourth, hiring and consulting experts for expertise, and convening forums to hear opinions. Considering the professional and hidden nature of judicial corruption, the CITs would seek the help and guidance of legal experts or law firms in uncovering judicial corruption. Fifth, conducting interviews and private talks with officials and the public, as well as surveys and questionnaires. During the inspections, the CITs conducted 53,000 interviews, which helped them to discover more clues. In addition, they also collect evidence by attending meetings or meeting with or listening to briefings by local leaders and officials.

Through these rigorous measures and extensive information collection, the CCDI and CITs can obtain comprehensive and detailed information on judicial corruption among officials in the inspected provinces, which has a strong deterrent effect on local officials. Some quantitative evidence also shows that this anticorruption inspection is effective in detecting and combating the judicial corruption of local politicians. From the post-inspection reports from CITs, 22 of the 31 provinces were criticized by the inspection team for judicial corruption<sup>38</sup>. And, as reflected in the reports on inspection rectification progress, these provinces have developed many extensive and detailed measures to combat judicial corruption in response to the inspection's criticisms. Moreover, according to the rule of law index<sup>39</sup> from the Worldwide Governance Indicators (WGI) for China, over the almost two decades before the anti-corruption campaign (1996-2011), China's Rule of Law ("ROL") Indicator was quite stable, ranging roughly from -0.4 to -0.6. However, this indicator has improved impressively since the anticorruption campaign, rising sharply from -0.5 in 2012, the year before the campaign, to -0.05 in 2020.

Taken together, the unprecedented anti-corruption campaign, with combating political interference in courts as one of its objectives, has not only eradicated numerous corrupt officials, but more importantly has generated a very strong deterrent effect on officials in office, and profoundly changed their behavior, thus deterring them from interfering with court decisions. Based on that, we posit that after the anti-corruption campaign, the interference in court decisions by politicians has been curbed and judges no longer favor politically connected firms, so the win rates of connected firms declined significantly compared with that of unconnected firms.

#### 3. Empirical strategy and data

#### 3.1. Methodology

To identify the causal impact of the anti-corruption campaign on the win-rate disparity in court between politically connected firms and unconnected firms, we employ a difference-indifferences estimation methodology to overcome potential endogeneity concerns. In particular, the exogenous cross-province, cross-year variation in the timing of the anti-corruption campaign, and the DID approach rule out the possibility that the macroeconomic trend or policy in aggregate could drive the effect. Specifically, following Lu et al. (2015), Xu (2020), and Liu (2020), the benchmark specification is as equation (1):

$$Win_{i,t} = \alpha + \beta_1 In vestigation_{p,t} + \beta_2 Connect_{j,t} + \beta_3 In vestigation_{p,t} * Connect_{j,t} + \gamma_1 lawsuit_{charac_{i,t}} + \gamma_2 firm_{charac_{j,t-1}} + \gamma_3 pro v_{charac_{p,t-1}} + \delta_j + v_t + \sigma_{p,t} + \gamma_{ind,t} + \varepsilon_{i,t}$$
(1)

where *i* indexes each lawsuit event, *j* indexes firm, *p* indexes province where the trial took place, t represents the year of the lawsuit adjudicated.  $Win_{i,t}$  is a dummy variable that equals 1 when the disclosing firm *j* wins the lawsuit. *Investigation*<sub>nt</sub> is the regressor of interest, indicating the province's anti-corruption status, a dummy variable equals 1 in affected province p for both the investigation year t and the following years, and 0 for other years.<sup>40</sup>-*Connect<sub>i,t</sub>* is a dummy variable equal to 1 for firms with political connections and 0 for firms without political ties. lawsuit\_characi,t is a vector of lawsuit characteristics relevant to determining the lawsuit outcome, as discussed in Section 3.4.4. firm\_charac<sub>p.t-1</sub> is a vector of firm characteristics. *prov\_charac<sub>p.t-1</sub>* is a set of province characteristics, including the natural logarithm of GDP, total population, and foreign direct investment.  $\delta_i$  indexes firm fixed effects, capturing time-invariant firm characteristics that may influence the outcomes of lawsuits.  $v_t$  represents year fixed effects, which capture all of the time trends common to all provinces, such as aggregate trends in the Chinese judicial environment, macro shocks, and business cycles. In augmented specifications, we additionally control for province and industry fixed effects interacted with linear time trends ( $\sigma_{v,t}$  and  $\gamma_{ind,t}$ , respectively), to rule out the possibility that our results are driven by a general time trend across industries and provinces.  $\varepsilon_{i,t}$  is the error term. To address the potential serial correlation and heteroscedasticity, we cluster the standard errors at the province level. The coefficient  $\beta_2$  measures the average win-rate disparity between connected firms and unconnected firms before the anticorruption campaign. In particular,  $\beta_3$  is the coefficient of interest, and we expect  $\beta_3$  to be significantly negative, indicating that the win rates of firms with political connections in litigation declined significantly compared with that of unconnected firms after the anti-corruption campaign.

## 3.2. Propensity score matching

In this section, we explain why propensity score matching is required in the proposed triple-difference method, then demonstrate how this matching approach is implemented<sup>41</sup>, followed by univariate comparisons between connected and unconnected firms to assess the quality of the match.

One potential concern is that our results might be affected by systematic differences in firm attributes between politically connected and unconnected firms, such as firm size, financial capabilities, or other firm characteristics that may influence both the likelihood of establishing the political connection and a firm's win rates in court. Although we include many control variables in the regressions, the omission of certain variables is inevitable. In particular, if these firm characteristics also cause win rates of politically connected firms to be more sensitive to the anticorruption campaign than unconnected firms, then the trends in win rates for these firms may differ for reasons unrelated to political connections.

<sup>&</sup>lt;sup>38</sup> The CCDI stipulates that, after each visit, the CITs summarize their findings based on numerous corruption-related problems they identified and report them to the provincial authority, i.e., "Reports on Issues Identified by the Inspection". We manually collected post-inspection reports of all provinces from the CCDI website and read and categorized corruption-related issues identified by the inspectors.

<sup>&</sup>lt;sup>39</sup> The ROL indicator ranges from -2.5 to 2.5, with higher numbers representing a higher level of rule of law in society. Source: https://databank.worldbank.org/source/worldwide-governance-indicators#.

<sup>&</sup>lt;sup>40</sup> Our definition of the main variable (*Investigation*) as taking value 1 for all years after the investigation in the affected province is similar to the extensive existing literature on China's anti-corruption campaign started in 2012, which also argues that the effects of the inspection last longer than just the investigation. See Chen and Kung (2019), Kong and Qin (2021), Xu et al. (2021), Li et al. (2021), Fang et al. (2022), Li et al. (2022).

<sup>&</sup>lt;sup>41</sup> We thank the reviewer for suggesting the use of propensity score matching.

One standard way of mitigating this concern is to perform propensity score matching (PSM) by pairing politically connected firms with unconnected firms that have similar observed attributes. Rosenbaum and Rubin (1983) and Dehejia and Wahba (2002) document that the PSM method succeeds in focusing attention on the small subset of comparison units with similar characteristics to the treated units, hence eliminating the bias caused by the systematic differences between the treatment and control groups. Therefore, in this study, we adopt the PSM approach to address potential selection bias.

Specifically, the PSM process involves three steps. First, we require that the candidate unconnected firm for the matching shares the same province, year, and industry class (the same two-digit Standard Industrial Classification (SIC) code, i.e., SIC-2) as the connected firm. The second step obtains the propensity score, which is the predicted probability that a firm has political connections, given its characteristics. To calculate the propensity score, we employ a comprehensive set of firm characteristics that could capture the likelihood of a given firm being politically connected, as documented in previous studies. More specifically, we use size, leverage, market share, state ownership, profitability (ROA), market-to-book, and cross-listing as connected firms are likely to be different from nonconnected peers along these characteristics (see, e.g., Leuz and Oberholzer-Gee, 2006; Bunkanwanicha and Wiwattanakantang, 2009; Faccio, 2006, 2010). The third step matches a treated firm with an untreated firm based on their propensity scores, referring to prior research (Smith and Todd, 2005; Lemmon and Roberts, 2010). Among the potential control sample firms, we select the optimal match based on the one-to-one<sup>42</sup> nearest neighbor propensity score matching without replacement to control for differences in characteristics between connected and nonconnected firms (3652 matches). We require that the matching firms fall in the common support of estimated propensity scores.<sup>43</sup> Fourth, to balance sample size and matching quality, referring to Faccio et al. (2006), if no candidate company satisfies these criteria, we broaden the industry classification (SIC-2) to the same one-digit SIC code (SIC-1) and repeat the procedure (1258 additional matches). If still no match results for a connected firm, we further broaden the province to the geographical region<sup>44</sup> using the industry classification (SIC-1) (a further 709 matches). This procedure ensures that most connected firms are matched with unconnected firms with similar characteristics.

After obtaining the matched firms using propensity scores, we construct the sample for applying the triple difference approach. In the end, the number of observations decreases from 16,203 to 11,238, evenly distributed between connected and unconnected firms by province, industry, and year. We call this sample the propensity-score-matched sample and perform all the analyses on the propensity-score-matched sample.

The next step is to check whether the matching has successfully balanced the two groups. A crucial criterion of conditional independence is that, after matching, there should be no significant differences in the matching dimension covariates between the control and treatment groups. Table 1 reports the univariate comparisons

in firm characteristics between politically connected and unconnected firms before and after the matching. As shown in columns 1–3 of Table 1, before the matching, the mean values of certain covariates are significantly different between connected and unconnected firms. Particularly, politically connected firms are slightly larger, have a larger market share, and are more likely to be privately owned. However, as indicated in columns 4-6 of Table 1, after matching, none of the observed differences between the connected and unconnected firms in these firm characteristics is statistically significant, suggesting that the propensity score matching process eliminates meaningful observable differences in covariates between the two groups of firms. As a result, the matching procedure increases the likelihood that the observed difference in win-rate changes between connected and unconnected firms is caused by the anti-corruption campaign. And the combination of PSM and DID can further increase our confidence in our inference.

## 3.3. Data and sample selection

To investigate the relationship between anti-corruption and court bias, we construct our sample based on Chinese listed companies from 2009 to 2018. And we employ four datasets for our empirical analyses: a new data set of Chinese listed firms' commercial lawsuits, a sample of corruption cases, and data on firm-level and city-level characteristics.

We obtain Chinese listed firms' material lawsuits from 2009 to 2018 mainly from listed company announcements.<sup>45</sup> In 1998, the Chinese Stock Exchanges began to require all listed companies to disclose their involvement in litigation if the stakes (of a single case or cumulative cases within one year) exceeds RMB 10 million (\$1.6 million) and exceeds 10% of the company's net assets based on the previous year's audited financial statements. For litigation where the stakes are below this threshold, disclosure should also be made if the board of directors believes the case will have a material impact on the company's securities. Generally, this mandatory disclosure requirement covers almost all lawsuits that significantly impact the company, allowing us to access the data set involving the most comprehensive information available yet on Chinese listed firms' lawsuits. In this paper, we consider only the verdict from the first ruling in each case. This is a common practice in the relevant literature, as there are extra and complex requirements for second instances or retrials, which may introduce unnecessary complications (see Lu et al., 2015; Kahn and Li, 2019).

Since 2012, the central government has demanded immediate public disclosure of information on officials under investigation for corruption to increase transparency in public sector governance. We manually collected detailed information on corruption cases involving government officials from 2012 to 2016 by searching documents published by the Central Commission for Discipline Inspection of the Communist Party of China (CCDI), which lists the time of the filing of corruption investigations in China as well as the number of arrested officials in each province, and supplemented by web searches on Baidu and Google.

The financial data of each listed company was obtained from the China Stock Market and Accounting Research Database (CSMAR). We match the company's financial data in year t-1 to the cases tried in year t. As many of the counterparties in the litigation are not listed on the stock market, there is no access to their financial information. Nevertheless, we introduce a variable denoting the ownership status of the counterparty, which we purchased from the State Administration for Industry and Commerce of China

<sup>&</sup>lt;sup>42</sup> Due to the fact that the number of unconnected firms is roughly twice that of connected firms, we are unable to expand the 1:1 match to even a 1:2 match for our treatment firms; hence, this test is only implemented with a 1:1 treatment–control group.

<sup>&</sup>lt;sup>43</sup> We use one-to-one nearest neighbor propensity score matching rather than caliper (or radius) matching or nearest-neighbor matching within caliper, so we do not set for maximum distance of controls.

<sup>&</sup>lt;sup>44</sup> China can be divided into seven regions according to geographic and economic characteristics, and provinces in each of these regions share more common characteristics. They are North China (Beijing, Tianjin, Hebei, Shanxi, and Inner Mongolia), Northeast China (Liaoning, Jilin, and Heilongjiang), Eastern China (Shanghai, Jiangsu, Zhejiang, Anhui, Fujian, Jiangxi, and Shandong), Central China (Henan, Hubei, and Hunan), Southern China (Guangdong, Hainan, and Guangxi), Southwest China (Chongqing, Sichuan, Guizhou, Yunnan, and Tibet), and Northwest China (Shaanxi, Gansu, Ningxia, Qinghai, and Xinjiang).

<sup>&</sup>lt;sup>45</sup> We also cross-check and supplement our data information with China Judgements Online, the official website of Supreme People's Court that publishes court rulings, the Wind Database and the China Research Data Service (CNRDS) database, datasets similar to the CRSP and COMPUSTAT databases, and Qichacha, a third-party platform that publishes basic information of Chinese firms.

**Table 1**Firm Characteristics Before and After the Matching.

Variable	Prematch			Postmatch		
	Connected Firms (1)	Nonconnected Firms (2)	Difference (3)	Connected Firms (4)	Nonconnected Firms (5)	Difference (6)
lnSize	22.6512	22.5319	0.1192** (0.0488)	22.6429	22.6320	0.0109 (0.0565)
Lev	0.4809	0.4794	0.0015 (0.0072)	0.4810	0.4888	-0.0078 (0.0083)
ROA	0.0291	0.0277	0.0014	0.0290	0.0263	0.0027 (0.0038)
Cross	0.0709	0.0797	-0.0088 (0.0085)	0.0706	0.0740	-0.0034 $(0.0095)$
МВ	4.0654	4.2853	-0.2199 (0.2441)	4.0748	4.2159	-0.1411 (0.2759)
Share	0.0096	0.0076	0.0020* (0.0011)	0.0094	0.0084	0.0009 (0.0014)
SOE	0.3324	0.3861	-0.0537*** (0.0154)	0.3333	0.3388	-0.0054 (0.0174)

Notes: This table reports the univariate comparisons in firm characteristics between connected and unconnected firms before and after the matching. We use size (*InSize*), leverage (*Lev*), market share (*Share*), state ownership (*SOE*), profitability (*ROA*), market-to-book (*MB*), and cross-listing (*Cross*) as connected firms are likely to be different from non-connected peers along these characteristics. All variables are defined in Section 3.4. Columns 1, 2, 4, and 5 show the means of corresponding variables. Columns 3 and 6 display the average difference between connected firms with standard errors in parentheses. \*\*\* denotes significance at 1%, \*\* at 5%, and \* at 10%.

(SAIC), which contains detailed information on the firms' registered address, date of registration, the current state of existence, and ownership status. And we retrieve city-level characteristics from the China City Statistical Yearbook (CCSY).

Furthermore, we exclude four types of cases from the sample: non-commercial (criminal and administrative) cases, cases that were not tried in China, cases that were filed but later withdrawn, and cases in which the verdict was not disclosed. Then, we match the litigation data, corruption cases, firm-level characteristics, and city-level characteristics. The final sample includes 11,238 commercial lawsuits from 2009 to 2018.

## 3.4. Variable construction

## 3.4.1. Lawsuit success

Our dependent variable, *Win*, is a dummy variable equal to 1 when the disclosing firm wins the lawsuit. Referring to the conventional literature (Clermont and Eisenberg 1991; Kessler et al., 1996) and recent empirical studies (Lu et al., 2015; Wang, 2018; Xu, 2020), we define a plaintiff's success as being awarded monetary benefit at trial.

#### 3.4.2. Anti-corruption

To measure the anti-corruption campaign, we construct a dummy variable (*Investigation*), which equals 1 in the affected province for the investigation year and years after, and zero for all other years. Following Pan and Tian (2020), and Kong and Qin (2021), a province whose provincial senior officers are investigated is considered to be targeted by the anti-corruption campaign. Specifically, we defined provincial senior officers as those in provincial governments with administrative ranks at or above the deputy minister level, including party and governmental officials, as they can build an extensive political network and have significant control of economic resources (see also Ding et al., 2020; Pan and Tian, 2020; Kong and Qin, 2021).<sup>46</sup>

In particular, we focus on provincial senior officers for the following reasons. First, provincial senior officers tend to have a more substantial impact on the overall local judicial system and regional economy than low-level officials. Second, these cases may alleviate potential endogenous concerns that firms' court outcomes may lead to enforcement of the anti-corruption campaign, as these corruption cases are political in nature and unlikely to result from their favoritism toward certain companies. Third, these cases usually draw more public attention, so there is better disclosure of information about these cases. Moreover, our identification of high-level corruption cases is also in line with existing research in China, which also focuses on cases at or above the provincial level (Li and Zhou, 2005; Fan et al., 2008; Piotroski and Zhang, 2014; Pan and Tian, 2020; Kong and Qin, 2021). We retain only the earliest investigation of an official in a province as our event date since this filtering method captures the arrival of new information about corrupt provinces and the exogenous shock to the local judicial environment.

Table 2 shows the distribution of senior government officials investigated in China at the province-year level from 2012 to 2015. Beginning in 2012, the central government first implemented investigations into senior government officials in Guangdong and Sichuan provinces, and more senior government officials were investigated in 2013, 2014, and 2015, which is consistent with the anti-corruption policy implemented by the NCCPC. The exogenous cross-province, cross-year variation in the timing of the anti-corruption campaign constitutes a quasi-natural experiment that can effectively identify the causal effects of anticorruption campaigns on the win-rate disparity in court between politically connected firms and unconnected firms.

## 3.4.3. Political connections

The reliability of the identification of political connections is crucial to this study. In the lack of a widely acknowledged definition of corporate political connections, we developed our measure for this study by referring to prior relevant research and based on the Chinese institutional environment. Specifically, since in China the government has considerable discretion over determinants of economic activity, it is prevalent for companies to establish political connections with the government to obtain certain benefits that would not otherwise be available, and the common way they do this is by hiring government officials. Therefore, the existing literature generally employs the political background of firms' exec-

<sup>&</sup>lt;sup>46</sup> In China's bureaucratic hierarchy, there are five administrative levels for public servants, from highest to lowest: state (guo), ministry (bu), department (ju or ting), division (chu), section (ke), which corresponds to central, province, city, county, and town-level government. Each administrative level includes both full and deputy posts. Generally, the rank of governor or provincial party secretary is ministry level, while the rank of deputy governor or deputy provincial party secretary is deputy ministry level. Moreover, our identification of provincial senior officers is also consistent with existing studies in China, which also focus on cases at the ministerial level or above (Li and Zhou, 2005; Fan et al., 2008; Piotroski and Zhang, 2014).

Table 2			
Distribution of Inve	stigated Senior	Government	Officials.

Province	Date of investigation	Province	Date of investigation
Sichuan	2012	Qinghai	2014
Guangdong	2012	Heilongjiang	2014
Jiangxi	2013	Tianjin	2014
Guangxi	2013	Hainan	2014
Jiangsu	2013	Shaanxi	2014
Inner Mongolia	2013	Chongqing	2014
Guizhou	2013	Ningxia	2015
Hunan	2013	Shanghai	2015
Anhui	2013	Fujian	2015
Hubei	2013	Zhejiang	2015
Yunnan	2014	Jilin	2015
Shandong	2014	Gansu	2015
Hebei	2014	Xizang	2015
Shanxi	2014	Beijing	2015
Liaoning	2014	Xinjiang	2015
Henan	2014		

Notes: This table shows the distribution of senior provincial government officials investigated at the province-year level in China during 2012–2015.

utives as a measure of political connections (Faccio, 2006; Faccio et al., 2006; Fan et al., 2007; Calomiris et al., 2010; Chen et al., 2011a,b; Fisman and Wang, 2015; Chen et al., 2017).

Following that, our measure of political connections is based on the previous employment histories of top executives at each firm. We define a company to be politically connected if at least one of its top officers (defined as the company's Chairman, Vice-Chairman, CEO, Vice-CEO, independent directors<sup>47</sup>, and other directors) is (or was) a government official at the level of section chief (kezhang)<sup>48</sup> or above or a chief member (chairman or vicechairman) of the People's Congress or the People's Political Consultative Conference at the national or the subnational level. A dummy variable (Connect) is constructed to measure whether a firm is politically connected and equal to 1 for politically connected firms and 0 otherwise. Moreover, while quantifying the strength of a firm's political connections, we give priority to the background of politically connected executives with the highest administrative rank if a firm employs two or more connected executives, as administrative rank largely determines an official's political power and social networks.

Information on top executive teams is provided by companies' annual reports, based on year-end employment. Since 2004, the disclosure rules of the China Securities Regulatory Commission (CSRC) required firms to publish the biographies and curriculum vitae of executives and senior officers in their annual reports, including those of their CEOs, chairpersons, and other senior officers (e.g., directors, vice-CEOs, chief financial officer, and board secretary). In particular, Chinese listed firms must disclose information on these senior managers' current or former positions, tenure, and rank in China's political system, in addition to demographic and educational information (Chen et al., 2011a,b; Chen et al., 2017; Liu et al., 2021). To identify political connections, we collected the resumes of senior managers for our sample of firms from the China Stock Market and Accounting Research (CSMAR) and the Wind database, the two largest vendors of raw financial data in China. For cases with ambiguous disclosure, we search Baidu or Google as a cross-check. From the profile, we traced the

executive's political connections by examining whether he or she was currently or formerly a government officer.

Before the matching, 34.3% of the full sample firms appointed politically connected executives who were current or former government bureaucrats, suggesting that establishing political ties with the government is common in China. Furthermore, to explore the heterogeneity of political connections, we present more information on the distribution of different types of politically connected executives in our sample, as shown in Online Appendix Table A1. Firstly, Panel A reports the sample by type of position held by connected executives. We see that nearly a third of them serve as Chairman or CEO, the two positions with the most power in influencing corporate strategy. In addition, the other eleven percent are either vice-chairmen or vice-CEOs, while 32% serve as directors, and 25% serve as independent directors. Secondly, we present the distribution of the administrative level<sup>49</sup> of connected executives in Panel B. As shown, the highest percentage of connected executives is at the department level (33%), followed by the ministry and division levels, both at around 29%, while the section and state levels are the lowest, at around 7% and 2% respectively. Thirdly, based on the administrative rank, we further report the sample by relative power between connected executives and the president of the court where the lawsuit is tried, as the rank difference largely determines the success of politicians' interventions in the judiciary.<sup>50</sup> Panel C shows that in our observations, most of the connected executives rank higher than or equal to the court chief<sup>51</sup> (around 90%), with less than 10% below. Finally, Panel D reports the sample by type of government agency where connected executives ever served. We see that the highest percentage of connected executives served in government functional departments (around 50%), followed by the party committee and government (around 33%), with approximately 7.7% and 7.3% serving in the People's Congress and the People's Political Consultative Conference.

#### 3.4.4. Other variables

We control for several characteristics that may affect the firm's probability of winning the lawsuit (Lu et al., 2015; Xu, 2020). Precisely, we first control for the following lawsuit-level variables to obviate the confounding effect of lawsuit heterogeneity: (1) to overcome the plaintiff effect in explaining firms' win rate, we control for *Plaintiff\_dummy*, a dummy variable which equals 1 if the disclosing firm is the plaintiff, and 0 otherwise; (2) the variable *InMoney*, which proxies for the litigation stakes; (3) we employ Court\_level to control for the three levels of courts in Chinese judicial system since it is related to the unobserved case and judge features (such as the quality of the judge or the political sensitivity of a case); (4) to control different suit types, we include *Case\_type*, equal to 1 for cases related to bank loans and intercorporate loans, equal to 2 for cases related to other (regular business) contracts, and equal to 3 for tort cases; (5) to address concerns that the result may be driven by the firm's familiarity with legal procedures, we construct a dummy variable Repeats to identify whether the firm is a "one-shotter" or a repeat player in court, which takes a value

<sup>&</sup>lt;sup>47</sup> In addition to directors, Chinese companies also build political connections by appointing government officials as independent directors (also known as an outside director) (Cheng, 2018; Wei et al., 2020; Berkowitz et al., 2022; Xiao and Shen, 2022). <sup>48</sup> In China's bureaucratic hierarchy, there are five administrative levels for public servants, from highest to lowest: state (guo), ministry (bu), department (ju or ting), division (chu), section (ke), which corresponds to central, province, city, county, and town-level government. Each administrative level includes both full and deputy posts.

<sup>&</sup>lt;sup>49</sup> In Chinese politics, administrative rank is a crucial element, with higher-rank administrative agencies and officials having more authority over lower-rank counterparts. Specifically, there are five administrative levels for public servants, from highest to lowest: state (guo), ministry (bu), department (ju or ting), division (chu), section (ke), which corresponds to central, province, city, county, and town-level government.

<sup>&</sup>lt;sup>50</sup> Under the current organizational structure in China, when the rank of an officer is higher than the court chief, exerting influence over the court is relatively easy; however, when an official's status is below the court's, it is more difficult.

<sup>&</sup>lt;sup>51</sup> Local courts in China are under the direct control of the local government at their corresponding levels, and the judiciary traditionally has a lower status in China's political hierarchy. As a result, local politicians at the same rank as the court presidents can also exert influence on the courts.

of one if the disclosing firm is involved in more than four other lawsuits (the sample median) and zero otherwise.

In addition, we also control the following firm-level variables to eliminate the interference of the firm's heterogeneity: (1) firm size (*lnSize*), defined as the natural log of the firm's total book assets, capturing the resources of the firm; (2) liquidity (*Cash\_ratio*), defined as total cash over total assets; (3) capital structure (*Leverage*), defined as total leverage over total assets; (4) sales revenue (*Sales*), the log of total sales revenue; (4) state-owned enterprises (*SOE*), which equals one if the disclosing firm is state-owned and zero otherwise, since government ownership may help firms win lawsuits; and (5) we also include the ownership status of the counterparty in the litigation using *Other\_SOE*, which equals one if the counterparty is a state-owned enterprise.

Furthermore, to ensure that the heterogeneity of cities does not drive the results, we add the following control variables to cover city characteristics: (1) economic performance (*InGDP*), defined as the natural logarithm of GDP, which may be associated with the judicial environment and local government intervention; (2) total population (*InPop*), defined as the natural logarithm of the total population in the city; (3) openness of the city (*FDI*), defined as the total foreign investment over GDP in the city, which may have an impact on the development of local legal institutions.

Detailed variable definitions and descriptive statistics are presented in Table 3. To eliminate the effects of extreme values, the main continuous variables are winsorized at the 1% level.

## 4. Empirical results and analyses

We report the empirical results in the following subsections. We first evaluate the effect of the anti-corruption campaign on the win-rate disparity in court between firms with and without political connections. Then, to ensure a clean identification, we discuss and address our underlying assumptions. Moreover, we examine whether the impact of the anti-corruption campaign varies across the strength of the political connection. In addition, we conduct several additional empirical exercises to further rule out the alternative hypothesis. Finally, we explore the heterogeneous effects of the anti-corruption campaign on the above court outcomes by local legal environments, case types, and court levels.

## 4.1. The effect of anti-corruption campaign on court outcomes

In Table 4, we estimate the impact of the anti-corruption campaign on court outcomes based on the propensity-score-matched sample. The coefficient of *Connect* measures the average win-rate disparity between connected firms and unconnected firms before the anti-corruption campaign. Of interest is the coefficient of *Investigation\*Connect*, which measures how the win-rate disparity is affected by the anti-corruption campaign.

We start off the estimation by only controlling for fixed effects of the province, year, and industry in column 1. It turns out that, on average, politically connected firms have a higher win rate in court than unconnected firms before the anti-corruption campaign. However, the higher win rate of connected firms decreased significantly after the anti-corruption campaign. In columns 2–4, we further control for the lawsuit, firm, and city heterogeneity, respectively. The coefficients of *Investigation\*Connect* are persistently negative and statistically significant at the 1% level. Columns 5 and 6 take a step further to include province and industry fixed effects interacted with linear time trends, respectively, ruling out the possibility that our results are driven by a general time trend across industries and regions. In particular, column 6 displays our preferred specification, including province, industry, and year fixed effects as well as the interaction of province and industry fixed effects with linear time trends. As shown, the coefficients of *Investigation\*Connect* retain similar patterns and are all significantly negative at the 1% level. In column 7, we control for the firm fixed effects, and the number of observations is reduced since some firms have only one lawsuit during our sample period. We find that the coefficient of *Investigation\*Connect* decreases only slightly and remains negatively significant. As shown, our main results are quite robust across these alternative specifications.

Then, we interpret the magnitude of the main coefficients using the preferred specification in column 7. Specifically, the coefficient of *Connect* is 0.042 and significant at the 5% level, implying that, on average, politically connected firms have an economically and statistically significantly higher win rate than unconnected firms—by 4.2 percentage points—before the anti-corruption campaign. Furthermore, the coefficient of *Investigation\*Connect* in column 7 is -0.063 and significant at the 1% level, suggesting that the higher win rate of connected firms decreased by 6.3 percentage points after the anti-corruption campaign.

The economic magnitude of the effect is sizable. On average, the anti-corruption campaign narrows the win-rate disparity between politically connected and unconnected firms by 6.3 percentage points, a much larger reduction than the gap in win rates between the two-4.2 percentage points-before the anti-corruption campaign. Furthermore, out of the total monetary amount of 2,250 billion RMB in commercial disputes after the anti-corruption campaign, 642 billion, or more than a quarter of it (28.5%) was involving politically connected firms. Given that our estimate of the decline in win-rate of connected firms is approximately 6.3%, political rents amount to 40.4 billion RMB (642\*0.063), approximately 1.80% (40.4/2250) of total monetary amounts of commercial disputes for the same period. In other words, this result means that the anti-corruption campaign stopped corrupt officials from transferring 1.80% of total monetary amounts of commercial disputes in the same period from unconnected firms to connected parties by interfering with court decisions, benefits of an enormous scale.

## 4.2. Identification assumptions

We now examine several key threats to identification that could undermine the causal interpretation of these estimates.

## 4.2.1. Parallel trend assumption

The validity of the DID approach depends on satisfying the key identifying assumption behind this strategy, the parallel trend assumption, which requires that the average trends in the winning gaps between politically connected and unconnected firms are parallel during the pre-treatment period for both the treatment and control groups. If the timing of the anti-corruption campaign is correlated with pre-treatment differences in the win-rate disparity between politically connected and unconnected firms across provinces, our results may be driven by pre-existing trends in court outcomes, and the estimation results above would be biased. To test the plausibility of the parallel trend assumption<sup>52</sup>, following Bertrand and Mullainathan (2003) and Serfling (2016), we construct dynamic DID models to examine the dynamic effect as equation (2):

<sup>&</sup>lt;sup>52</sup> As a preliminary test, we also plot the time trends in the win-rate disparity between connected and unconnected firms of the treatment and control groups. We find that trends in the win-rate disparity between connected and unconnected firms are relatively similar between treated groups and control groups in the pre-shock period. See Online Appendix Figure F1 for more details.

## P. Zhang

Variable	Definition	Moan	s D
Vallable	Demitton	Iviedii	3.D.
Main variables			
Win	= 1 if the disclosing firm wins the lawsuit; =0 otherwise	0.580	0.494
Investigation	= 1 in the affected province for the year of the investigation and years after, and zero for all other years	0.684	0.465
Connect	= 1 if the company has political connections; =0 otherwise	0.500	0.500
Connect_High	= 1 if the disclosing firm has connections to a bureaucrat with a rank equal to or higher than that of the president of the court where the case is heard; =0 otherwise.	0.455	0.498
Connect_Low	= 1 if the disclosing firm has connections with a bureaucrat whose administrative rank is lower than that of the president of the court where the lawsuit is tried; =0 otherwise.	0.045	0.207
Time to Disposition	the time span (in days) of each lawsuit from filing to judgment.	128	175
Lower Court	= 1 if the trial occurs in county-level basic courts, and 0 for intermediate courts and higher courts.	0.881	0.323
Control variables			
Plaintiff dummv	= 1 if the disclosing firm was the plaintiff: =0 otherwise	0.559	0.497
InMonev	natural logarithm of the amount claimed by the plaintiff (¥)	12.954	3.089
Court_level	a categorical variable, denoting four levels of courts, assigned from 1 to 3 (the higher the value, the higher the court level)	1.120	0.328
Case_type	= 1 for cases related to bank loans and intercorporate loans; = 2 for cases related to other (regular business) contracts, and = 3 for tort cases	1.761	0.646
Repeats	= 1 if the disclosing firm is involved in more than four other lawsuits: =0 otherwise	0.551	0.497
InSize	the natural log of the firm's total book assets (¥)	24,467	2.855
Cash ratio	total cash over total assets	0 104	0.098
Leverage	total leverage over total assets	0.597	0.268
Sales	natural logarithm of total sales revenue (¥)	0.517	0.479
SOE	= 1 if the disclosing firm is state-owned and zero otherwise	0.472	0.499
Other SOE	= 1 if the counterparty is a state-owned enterprise and zero otherwise	0.027	0.163
InGDP	natural logarithm of GDP	10.413	0.633
InPop	natural logarithm of the total population	8.544	0.584
FDI	total foreign investment over GDP	0.023	0.014
Other variables			
Judicial Reasoning	the natural logarithm of word count in judicial reasoning.	5.852	1.416
Discretionary Codes	= 1 if the judge cites discretionary codes, and 0 otherwise.	0.300	0.458
Deny Requests for Evidence Examination	= 1 if the judge disapproves of the parties' request for evidence examination and expert witness testimony, and 0 otherwise	0.104	0.305
InLawfirm Size	the natural logarithm of one plus the law firm's registered capital	3 2 7 7	1 186
InLawfirm Age	the natural logarithm of one plus the number of years since the law firm was founded.	2.403	0.744
Fis_Depend	= 1 in the affected court (i.e., constructing new buildings) for two years before and after each construction, implying greater fiscal pressure on the court, and 0 for all other years.	0.277	0.448
Election	= 1 in the year of the National Congress of the Communist Party and the year before.	0.192	0.394
Competition	= 1 when leaders of the court c face greater promotion pressure, and 0 otherwise.	0.479	0.500
Notes: This table shows the	summary statistics of the matched sample. Definitions, means, and standard deviation are reported. Data sources are de	escribed ir	n full in
Section 3.3			

#### Table 4

Anti-Corruption Campaign, Political Connections, and Court Outcomes.

	Dependent Variable: Win						
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Investigation	0.086***	0.034	0.042*	0.046*	0.067**	0.081***	0.032
	(0.030)	(0.023)	(0.023)	(0.024)	(0.030)	(0.027)	(0.033)
Connect	0.055***	0.053***	0.059***	0.060***	0.056***	0.064***	0.042**
	(0.018)	(0.012)	(0.010)	(0.012)	(0.016)	(0.016)	(0.021)
Investigation*Connect	$-0.088^{***}$	-0.068***	-0.081***	-0.081***	$-0.079^{***}$	$-0.088^{***}$	-0.063***
	(0.024)	(0.014)	(0.013)	(0.014)	(0.020)	(0.018)	(0.019)
Case-Level Controls		Yes	Yes	Yes	Yes	Yes	Yes
Firm-Level Controls			Yes	Yes	Yes	Yes	Yes
City-Level Controls				Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes	Yes	Yes	
Province FE	Yes	Yes	Yes	Yes	Yes	Yes	
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Industry FE*Time linear trends					Yes	Yes	Yes
Province FE*Time linear trends						Yes	Yes
Firm FE							Yes
Observations	11,238	11,238	11,238	11,238	11,238	11,238	10,726
Adj R-squared	0.223	0.398	0.402	0.403	0.416	0.417	0.471

Notes: This table reports impacts of the anti-corruption campaign on court outcomes based on DID estimations. We perform these analyses on the matched sample. The dependent variable is *Win*, which equals one if the disclosing firm wins the lawsuit. *Investigation* is a dummy variable that equals one in the affected province for both the investigation year and the following years, and zero for other years. *Connect* is a dummy variable equal to 1 for firms with political connections, and 0 for firms without political ties. All other variables are defined in Section 3.4. Robust standard errors clustered at the province level are reported in parentheses. \*\*\*, \*\*, and \* indicate significance at the 1%, 5%, and 10% levels, respectively.

$$\begin{aligned} Win_{i,t} &= \alpha + \beta_1 Before_{p,t}^{-4+} * Connect_{j,t} + \beta_2 Before_{p,t}^{-3} * Connect_{j,t} \\ &+ \beta_3 Before_{p,t}^{-2} * Connect_{j,t} + \beta_4 Current_{p,t} * Connect_{j,t} \\ &+ \beta_5 After_{p,t}^{1} * Connect_{j,t} + \beta_6 After_{p,t}^{2} * Connect_{j,t} \\ &+ \beta_7 After_{p,t}^{3} * Connect_{j,t} + \beta_8 After_{p,t}^{4+} * Connect_c + \partial X_{p,t} \\ &+ \gamma_1 lawsuit\_charac_{i,t} \\ &+ \gamma_2 firm\_charac_{j,t-1} + \gamma_3 prov\_charac_{p,t-1} + \delta_j + v_t \\ &+ \sigma_{p,t} + \gamma_{ird,t} + \varepsilon_{i,t} \end{aligned}$$

where  $Before_{n,t}^{-k}$  (k = 2,3,4+) is a dummy variable equals 1 if the observation is k years before the investigation year for the affected province, and 0 otherwise.  $current_{p,t}$  is a dummy variable for the investigation year for province *p*. After  $_{nt}^{s}$  (*s* = 1,2,3,4+) is a dummy variable that equals 1 for s years after the investigation year for an affected province j, and 0 otherwise. In particular, Before<sup>4+</sup><sub>nt</sub> denotes four years or more before the investigation year, while After $_{nt}^{4+}$  denotes four years or more after the investigation year. The omitted time category is one year before the investigation year so that the estimated effects  $\beta_1$ - $\beta_8$  are relative to the period one year before the start of the investigation. Specifically, the coefficients of  $\beta_1$ - $\beta_3$  measure the time trend of differences in the winrate disparity between politically connected and unconnected firms for affected provinces and unaffected provinces, whereas the coefficients of  $\beta_5$ - $\beta_8$  measure the lagged effects of the anti-corruption campaign, and  $\beta_4$  reflects the current effect.  $X_{p,t}$  includes Connect<sub>c</sub>, Before  $_{n,t}^{-k}$  (k = 2,3,4+), Current<sub>p,t</sub>, After  $_{p,t}^{s}$  (s = 1,2,3,4+) and control variables. All the other variables are defined as in equation (1).

Fig. 1 plots the results corresponding to specification (2). As shown, the coefficients of  $Connect^*Before_{p,t}^{-k}$ (k = 2,3,4+) are all insignificant, suggesting that before the anti-corruption campaign, the average trend in the win-rate disparity between politically connected and unconnected firms is similar for both treatment and control groups, confirming our identification strategy's validity. Furthermore, most of the coefficient estimates of  $Connect^*After_{p,t}^s$  (s = 1,2,3,4+) are negative and statistically significant, which is consistent with our baseline findings.<sup>53</sup>

## 4.2.2. Addressing the selection issue

Another concern is that the anti-corruption campaign itself may change the composition of firms or types of lawsuits in the sample, causing our estimation results to be biased. We now examine these two selection issues respectively.

To start with, the anti-corruption campaign itself may affect the composition of firms, leading to the possibility that our results are driven by differences in systematic changes in key firm attributes between politically connected and unconnected firms, especially given that our lawsuit data is a repeated cross-section.

To alleviate this concern, Table 5 compares the changes in key firm characteristics of these two types of firms following the anti-corruption campaign. We examine firm size (*InSize*), leverage (*Lev*), market share (*Share*), state ownership (*SOE*), profitability (*ROA*), market-to-book (*MB*), and cross-listing (*Cross*). As shown, the table reveals no meaningful changes in most of these firm characteristics for both connected and unconnected firms following the anti-corruption campaign. The only characteristic that changed significantly following the anti-corruption campaign is the state ownership of unconnected firms. However, we find that the differ-



**Fig. 1. Parallel Trend Test using the conventional DID estimations**, Notes: This figure illustrates the event studies using conventional DID estimations. Bars around point estimates represent 95% confidence intervals.

ences in the change in state ownership between politically connected and unconnected firms are statistically insignificant and therefore unlikely to bias our results. In particular, in Online Appendix Table C1, we add the interaction term *Investigation\*SOE* to the triple-difference analysis and find that the coefficients of *Investigation\*Connect* remain negative, statistically significant at the 1% level, and very similar in magnitude to the baseline results, implying that the impact of the anti-corruption campaign is not driven by the changes in key firm attributes.

To further address the selection issue resulting from the anicorruption campaign, we restrict the sample and require the firms to have lawsuits available both before and after the ani-corruption campaign. As shown in column 1 of Table 6, our result is robust to this restricted sample and the coefficient of *Investigation\*Connect* is negative and statistically significant.

Still, cautious readers may wonder whether the types of lawsuits change after the anti-corruption campaign and whether the lower winning rate of connected firms after the anti-corruption may be driven by firms' strategic calculations. However, this explanation is counter-intuitive. Specifically, after losing their advantage in court, politically connected firms may become more selective of the lawsuit cases that they submit to courts after the anti-corruption campaign, and thus those lawsuits that are difficult to win will not be submitted to courts. Therefore, such strategic behavior would lead to a higher win rate of the connected firm after the anti-corruption, not a lower win rate, which might only bias our baseline estimates downward, resulting in our estimates representing the lower bound on the true effects of the anti-corruption campaign. Nevertheless, to further address these unobserved selection biases of lawsuit cases, we restrict our sample to those cases admitted before the anticorruption campaign. Particularly, these cases are less likely to fall prey to the problem of strategic selection since firms submit their cases before the campaign was launched. We repeat our analysis with this more restricted sample and obtain similar result, as shown in column 2 of Table 6. Taken together, the above findings suggest that our results are less likely to be driven by the selection issue.<sup>54</sup>

<sup>&</sup>lt;sup>53</sup> It is worth noting that, the coefficient of *After*<sup>4+\*</sup>*Connect* remains negative and significant at the 5% level, but it decreases in magnitude, suggesting that anticorruption campaigns still had a sustained effect after four years, but declined.

<sup>&</sup>lt;sup>54</sup> One further possible concern is the political struggle and protection, which could induce a correlation between the implementation of the anti-corruption campaign and the win rate in court. However, we do not find that anti-corruption is a political struggle. See Online Appendix G for more details.

#### Table 5

Firm Characteristics Before and After the Anti-Corruption Campaign.

Variable	Nonconnected	Nonconnected Firms			Connected Firms		
	Before (1)	After (2)	Difference (3)	Before (4)	After (5)	Difference (6)	(7)
lnSize	22.5676	22.6414	0.0737 (0.1314)	22.4538	22.6706	0.2168 (0.1337)	0.1431 (0.1874)
Lev	0.4701	0.4915	0.0214 (0.0177)	0.4846	0.4804	-0.0042 (0.0176)	-0.0256
ROA	0.0284	0.0260	-0.0024 (0.0081)	0.0348	0.0282	-0.0066 (0.0081)	-0.0042 (0.0114)
Cross	0.0856	0.0723	-0.0132 (0.0203)	0.0957	0.0669	-0.0288 (0.0202)	-0.0156 (0.0286)
МВ	4.3482	4.1966	-0.1515 (0.5861)	3.6589	4.1356	0.4767 (0.5847)	0.6282 (0.8280)
Share	0.0125	0.0078	-0.0047	0.0137	0.0087	-0.0050 (0.0041)	-0.0003
SOE	0.4011	0.3297	-0.0714* (0.0382)	0.3617	0.3292	-0.0325 (0.0374)	0.0388 (0.0535)

Notes: This table compares firm characteristics before and after the anti-corruption campaign based on the matched sample. We examine firm size (*InSize*), leverage (*Lev*), market share (*Share*), state ownership (*SOE*), profitability (*ROA*), market-to-book (*MB*), and cross-listing (*Cross*). All variables are defined in Section 3.4. In columns 3, 6, and 7, standard deviations are reported in parentheses.

#### Table 6

Addressing the Selection Issue.

	Dependent Variable: Win					
	restrict our sample to					
	firms having cases available both before and after the campaign (1)	cases admitted before the anti-corruption campaign (2)				
Investigation	-0.003	-0.093				
	(0.045)	(0.131)				
Connect	0.023	0.243***				
	(0.025)	(0.061)				
Investigation*Connect	$-0.043^{**}$	$-0.180^{**}$				
	(0.019)	(0.085)				
Controls	Yes	Yes				
Firm FE	Yes	Yes				
Year FE	Yes	Yes				
Industry FE*Time linear trends	Yes	Yes				
Province FE*Time linear trends	Yes	Yes				
Observations	5655	1775				
Adj R-squared	0.494	0.588				

Notes: This table reports the results addressing the selection issue based on the matched sample. In column 1, we require the firms to have lawsuits available both before and after the ani-corruption campaign, whereas we restrict our sample to those cases admitted before the anti-corruption campaign in column 2. The dependent variable is *Win*, which equals one if the disclosing firm wins the lawsuit. *Investigation* is a dummy variable that equals one in the affected province for both the investigation year and the following years and zero for other years. *Connect* is a dummy variable equal to 1 for firms with political connections, and 0 for firms without political ties. All other variables are defined in Section 3.4. Robust standard errors clustered at the province level are reported in parentheses. \*\*\*, \*\*, and \* indicate significance at the 1%, 5%, and 10% levels, respectively.

## 4.2.3. Robustness tests on heterogeneous treatment effects

Recent advances in the econometric literature highlighted concerns about the interpretability of conventional DID estimates in settings with staggered treatment rollouts and heterogeneous treatment effects (e.g., Borusyak et al., 2021; De Chaisemartin and d'Haultfoeuille, 2020; Callaway and Sant'Anna, 2021; Sun and Abraham, 2021; Goodman-Bacon, 2021). They find that in the presence of heterogeneous treatment effects, models estimated using OLS may be biased, and cause incorrect conclusions due to negative weights being placed on some individual treatment effects. To address this issue, several robust estimators have been recently proposed to correct the potential biases of the traditional staggered DID approach. Particularly, relative to these estimators (e.g., De Chaisemartin and d'Haultfoeuille, 2020; Sun and Abraham, 2021), the imputation approach proposed by Borusyak et al. (2021) has attractive efficiency properties, is transparent, and has conservative standard errors that can be calculated analytically, and thus has been widely used in the recent literature. More importantly, to our knowledge, the imputation estimator of Borusyak et al. (2021) is the only new estimator that can both handle repeated cross-section data and allow for a triple difference design, and is therefore best suited to our situation<sup>55</sup>.

Thus, we test the robustness of our estimates by using the novel imputation estimator proposed by Borusyak et al. (2021), an imputation method similar to other proposed estimators (Gardner, 2022; Wooldridge, 2021), which allows for unrestricted treatment effect heterogeneity and avoids the OLS parameter weighting problem. Specifically, we present event studies using the Borusyak et al. (2021) imputation approach in Fig. 2, where we again find no evidence of pre-trends of concern and clear evidence of declines in the win rate of politically connected firms in provinces affected by anti-corruption relative to those not yet affected. In conclusion, this robustness test suggests that treatment effect heterogeneity is less of a concern in our setting.

## 4.2.4. Reverse causality test

Our empirical analysis also relies on the assumption that the cross-province timing of the anti-corruption campaign was not affected by our main dependent variable (Win). Specifically, while anti-corruption may affect court outcomes, especially reduce the court advantage of connected firms, by reducing government intervention in trilas, the implementation of the anti-corruption campaign could also stem from the local judicial environment (e.g., the large number of lawsuits in a province and the low win-rate of unconnected firms due to the judicial corruption). This is the typical reverse causality concern. To alleviate the concern about reverse causality, following Kroszner and Strahan (1999) and Beck et al. (2010), we conduct a hazard model of the anticorruption campaign, which can incorporate both the investigation of a given province and its timing, thereby allowing us to assess the effect of local factors (e.g., the lawsuits number of the province, win rates of unconnected firms, GDP, population, and FDI) on the time when an investigation is launched. And in Online Appendix Table B1, we find that the timing of the anti-corruption campaign

<sup>&</sup>lt;sup>55</sup> To date, most of these approaches can be implemented only when using true panel data with multiple observations per unit over time as well as difference-indifferences method. In contrast, our lawsuit data is a repeated cross-section, and we primarily use a triple difference design.



**Fig. 2. Parallel Trend Test using** Borusyak et al. (2021) **imputation estimator.** Notes: This figure illustrates the event studies using Borusyak et al. (2021) imputation approach. Bars around point estimates represent 95% confidence intervals. We use the *did\_imputation* command to perform a pre-trend analysis, via the *pretrends ()* option. Notice that the Borusyak et al. approach does not require "dropping" the t = -1 period (i.e., normalizing the difference to zero in that period) as is common when using an Ordinary Least Squares approach. And according to the STATA package *did\_imputation*, the reference group for the pretrend test is all periods more than *k* periods prior to the event date (and all never-treated observations, if available).

across different provinces does not vary with the degree of the preexisting judicial environment (the lawsuit number and win rates of unconnected firms in the province) and main economic factors. The detailed discussions are described in Online Appendix B.

## 4.2.5. No-anticipation assumption

The "no anticipation" assumption requires that the treatment group did not anticipate the policy shock during the pretreatment period and further take measures. Violations of this assumption may arise if the policy is anticipated before its implementation, which will cause our estimation results to be biased. However, the design and context of the anti-corruption campaign alleviate these concerns about the expectation effect, as follows.

First, given its sudden and rapid announcement, the anticorruption campaign came as a relatively exogenous event, largely a surprise to the general public, firms, and local governments. The announcement of a major new party policy barely 20 days into a new term was unprecedented, as previous administrations had typically announced policy changes approximately one year after into office. Second, the design of the anti-corruption inspections further limits these concerns about the expectation effects, as the specific time and sequence of the inspections are randomized across the provinces, and previous work has strongly established the validity of this randomization (Kong and Qin, 2021; Li et al., 2021; Xu et al., 2022).<sup>56</sup> Third, in China, anti-corruption campaigns were generally launched following an important political transition, and often such campaigns were short-lived. As a result, although several provinces were investigated earlier by the CITs in 2012, the expectation of many local officials of later inspected provinces was that this was yet another routine anti-corruption campaign by President Xi that would be short-lived, like the previous ones. This view is validated by substantial anecdotal evidence<sup>57</sup>, especially interviews with corrupt officials who were later arrested, who had speculated that this anti-corruption, like previous ones, would be short-term and gradually wane in intensity.<sup>58</sup>

Moreover, parallel trend tests of Fig. 1 and Fig. 2 show that before the anti-corruption campaign, the average trend in the win-rate disparity between politically connected and unconnected firms is similar for both treatment and control groups. According to these results, we find no evidence of anticipation effects of concern.

Nevertheless, we conduct additional empirical exercises to further alleviate the concerns. Specifically, the intuition is that if the expectation effect exists, later investigated provinces and nearby provinces were more subject to an increased anti-corruption threat and may be better able to anticipate the arrival of inspection teams. To rule out the possibility that some provinces, especially those that were later investigated and nearby provinces, anticipated the inspection's precise timing in advance, we provide the following evidence. Firstly, given that the first two anticorruption investigations targeting ten provinces in 2012 and 2013 are more exogenous and unpredictable, we first re-estimate our results employing only the first two anti-corruption investigations. As shown in column 1 of Table 7, the coefficient of Investigation\*Connect remains negative and statistically significant, and very similar in magnitude to the baseline results, implying that our results are quite robust. In addition, we drop all the neighboring provinces once a certain province has been investigated, in case border provinces anticipate being investigated in the next stage. Under these circumstances<sup>59</sup>, six provinces (e.g., Anhui, Beijing, Guangdong, Inner Mongolia, Sichuan, and Tianjin) are left. The results are reported in column 2 in Table 7, the coefficient of Investigation\*Connect is negative and significant at least 5% level. In sum, the above estimated results mitigate our concerns about the anticipation effect.

## 4.3. The strength of political connection

In the benchmark result, we examine the role of political connections as measured by the presence or absence of political ties. We find that judges are susceptible to interference and pressure from litigants' underlying political power and favor politically connected parties deliberately. In this subsection, we make further distinctions about the strength of political connections which has been largely neglected in the existing literature, and examine whether the impact of the anti-corruption campaign on connected firms' win rates varies across the strength of the political connection.

<sup>&</sup>lt;sup>56</sup> In practice, the CCDI decides when to dispatch a Central Inspection Team (CIT) to specific provinces. And the specific time and sequence of CIT site visits are required to be kept strictly confidential and exogenous to local government officials and their jurisdictions. Particularly, according to the 'three un-fixed' policy implemented by the central government, the inspection team, the time and location of the inspection to be carried out are all unfixed, making it more difficult for later inspected provinces to anticipate the movement of inspectors. Moreover, we searched the media for speculation on when specific provinces might be inspected from 2012 to 2015. However, we found few such predictions. Furthermore, we also test for this in Section 4.2.5, where we conduct a hazard model to examine the correlations of the investigation timing with observable local economic factors. No significant relationships are observed. Taken together, these evidence provide strong confidence that later investigated provinces can hardly anticipate when they will be investigated.

<sup>&</sup>lt;sup>57</sup> We searched judicial decisions, newspapers and other media for interviews with corrupt officials who were arrested in the latter rounds of inspections. And these officials said they had believed that this anti-corruption campaign, like previous ones, would be short-lived and soon stop, and that they were unlikely to be investigated, which led to them not stopping their corrupt activities while other provinces were being inspected.See https://baijiahao.baidu.com/s?id=1603799139878065515&wfr= spider&for=pc; https://fanfu.people.com.cn/n/ 2015/0922/c64371-27617067.html; https://www.thepaper.cn/newsDetail\_forward\_1302126?from= singlemessage &isappinstalled=0.

<sup>&</sup>lt;sup>58</sup> Consequently, the earlier rounds of the inspections did not have a strong deterrent effect on corruption officials in the later inspected provinces until the CITs arrived in their provinces and began investigation activities.

<sup>&</sup>lt;sup>59</sup> For example, Sichuan province was investigated in 2012. We thus drop its neighboring seven provinces, Qinghai, Gansu, Shaanxi, Chongqing, Yunnan, Guizhou, and Tibet since these provinces may have anticipated being investigated soon.

#### Table 7

Expectation Effects.

	Dependent Variable: Win					
	Using only the first two investigations (1)	Dropping nearby provinces once a province was inspected (2)				
Investigation	0.008 (0.046)	0.100				
Connect	0.128**	0.142*				
	(0.054)	(0.073)				
Investigation*Connect	$-0.078^{**}$	$-0.194^{**}$				
	(0.038)	(0.075)				
Controls	Yes	Yes				
Firm FE	Yes	Yes				
Year FE	Yes	Yes				
Industry FE*Time linear trends	Yes	Yes				
Province FE*Time linear trends	Yes	Yes				
Observations	3809	2171				
Adj R-Squared	0.458	0.448				

Notes: This table reports the robustness tests on expectation effects. We perform these analyses on the matched sample. In column 1, we re-estimate our results employing only the first two anti-corruption investigations. In column 2, we drop all the neighboring provinces once a certain province has been investigated. The dependent variable is *Win*, which equals one if the disclosing firm wins the lawsuit. *Investigation* is a dummy variable that equals one in the affected province for both the investigation year and the following years, and zero for other years. *Connect* is a dummy variable equal to 1 for firms with political connections, and 0 for firms with political ties. All other variables are defined in Section 3.4. Robust standard errors clustered at the province level are reported in parentheses. \*\*\*, \*\*, and \* indicate significance at the 1%, 5%, and 10% levels, respectively.

In Chinese politics, administrative rank is a crucial element, with higher-rank administrative agencies and officials having more authority over lower-rank counterparts (Kung and Chen, 2011). Thus, in practice, judges encounter different pressure and interference when officials associated with the firm are at different administrative ranks, resulting in disparities in the judges' bias towards politically connected firms. Specifically, under the current organizational structure, when the rank of an officer is higher than the president of the court, exerting influence over the court's personnel and budget decisions is relatively straightforward; however, when an official's status is below the court's, it is more difficult. Consequently, before the anti-corruption campaign, the higher the rank of the official connected to the firm, the more pressure and interference the judges were subjected to in making their decisions. And the anti-corruption campaign will immunize courts from the influence of local officials, especially those at higher ranks. Thus, we anticipate that compared to unconnected firms, the anticorruption campaign has a greater impact on firms connected to officials with a higher rank than that of the court, while having a less pronounced effect on firms associated with officials of a lower rank than the court.

Then, we test whether our results are robust under different definitions of political connections. To start with, we redefine the political connection (represented as *Connect\_New*), and only those firms connected to officials at a higher administrative level than the president of the court hearing the lawsuit are defined as having political connections. Results using this alternative definition are reported in column 1 in Table 8. As shown, the corresponding estimate of *Investigation\* Connect\_New* is -0.064, nearly identical to our baseline results, and is statistically significant at the 1% level.

To further examine the role of political connection's strength, we classify connected firms into those connected to officials with a rank equal to or higher than that of the court and those connected to officials with a rank lower than that of the court. Specifically, we estimate the following model as equation (3):

$$\begin{aligned} \text{Win}_{i,t} &= \alpha + \theta_1 \text{In } \textit{vestigation}_{p,t} + \theta_2 \text{Connect } \textit{Low}_{j,t} \\ &+ \theta_3 \text{Connect } \textit{High}_{j,t} + \theta_4 \text{In } \textit{vestigation}_{p,t} \\ &* \text{Connect } \textit{Low}_{j,t} + \theta_5 \text{In } \textit{vestigation}_{p,t} * \text{Connect } \textit{High}_{j,t} \\ &+ \gamma_1 \text{lawsuit } \textit{charac}_{i,t} \\ &+ \gamma_2 \text{firm } \textit{charac}_{j,t-1} + \gamma_3 \text{pro } \textit{v} \textit{-charac}_{p,t-1} + \delta_j + \textit{v}_t \\ &+ \sigma_{p,t} + \gamma_{ind,t} + \varepsilon_{i,t} \end{aligned}$$
(3)

where *Connect\_Low*<sub>*j*,*t*</sub> is a dummy variable that equals 1 when the disclosing firm *j* has connections with a bureaucrat whose administrative rank is lower than that of the president of the court where the lawsuit is tried, and 0 otherwise. *Connect\_High*<sub>*j*,*t*</sub> is also a dummy that equals 1 when the disclosing firm *j* has connections to a bureaucrat with a rank equal to or higher than that of the court where the case is heard. All the other variables are defined as in equation (1). In regression (3),  $\theta_4$  and  $\theta_5$  are the coefficients of interest. In particular,  $\theta_4$  measures that, compared to unconnected firms, how the anti-corruption campaign affects win rates of firms connected to the officials with a lower rank than the court. Similarly,  $\theta_5$  allows us to test how this campaign affects the win rates of firms connected to the official with a rank equal to or higher than that of the court.

The results corresponding to specification (3) are reported in column 2 of Table 8. As shown, the coefficient of *Investigation\*Connect\_High* is negative and statistically significant at the 1% level, indicating that the anti-corruption campaign significantly reduced win rates of firms connected with officials with a higher rank than that of the court. Additionally, the coefficients of *Investigation\*Connect\_Low* is also negative but not statistically significant and smaller in magnitude than that of *Investigation\*Connect\_High*. Taken together, these findings indicate that high-ranking officials have more influence on court decisions than lower-ranking officials and are therefore more affected by the campaign, which is in line with our proposition.

## 4.4. Cross-sectional heterogeneity

In this section, to provide additional evidence that the anticorruption campaign reduces the court advantage of politically connected firms by combating judicial corruption, especially stopping corrupt officials from interfering with court decisions and not through some other mechanisms, we assess whether the impact of the anti-corruption campaign on court bias varied across provinces, cases, and courts in a theoretically predictable manner. Specifically, if win rates of connected firms experience a more significant decline after anti-corruption, mainly due to stopping corrupt officials interfering with court decisions, then anticorruption should have had a more pronounced effect on the court bias in those provinces, courts, and cases, where court judgments are vulnerable to intervention by corrupt officials (e.g., the levels of judicial corruption are higher, or there is more room and flexibility for political maneuver in adjudicating cases). If the results are as we expect, these findings will increase confidence in the conclusions, shed empirical light on the mechanisms through which anticorruption influenced court outcomes, and reduce concerns about reverse causality.

#### 4.4.1. Local legal institution

In this section, we first examine whether the influence of the anti-corruption campaign on court outcomes varies across provinces with different legal institutions before the anti-corruption. If our main findings that the higher win rate of connected firms reflect the intervention of officials in judicial trial and deliberate favoritism toward connected firms is correct, then we should find that anti-corruption plays a more significant role in eliminating P. Zhang

#### Table 8

The Strength of Political Connection.

	Dependent Variable: Win	
	(1)	(2)
Investigation	0.037	0.032
Connect_New	(0.030) 0.052** (0.022)	(0.032)
Investigation*Connect_New	(0.022) $-0.064^{***}$ (0.021)	
Investigation*Connect_High1	()	-0.063***
Investigation*Connect_Low		(0.019) -0.025
Connect_High		(0.094) $0.047^{**}$ (0.022)
Connect_Low		0.039
Controls	Yes	Yes
Firm FE	Yes	Yes
Year FE	Yes	Yes
Industry FE*Time linear trends	Yes	Yes
Province FE*Time linear trends	Yes	Yes
Observations	10,726	10,726
Adj R-Squared	0.471	0.471

Notes: This table examines whether the impact of the anti-corruption campaign on connected firms' win rates varies across the strength of the political connection. We perform these analyses on the matched sample. The dependent variable is Win, which equals one if the disclosing firm wins the lawsuit. Investigation is a dummy variable that equals one in the affected province for both the investigation year and the following years and zero for other years, we redefine the political connection (represented as Connect\_New) and only those firms connected to officials at a higher administrative level than the court hearing the lawsuit are defined as having political connections. Rank\_Low is a dummy variable that equals 1 when the disclosing firm *j* has connections with a bureaucrat whose administrative rank is lower than that of the court where the lawsuit is tried, and 0 otherwise, Rank High is also a dummy that equals 1 when the disclosing firm *j* has connections to a bureaucrat with a rank equal to or higher than that of the court where the case is heard. All other variables are defined in Section 3.4. Robust standard errors clustered at the province level are reported in parentheses. \*\*\*, \*\*, and \* indicate significance at the 1%, 5%, and 10% levels, respectively.

<sup>1</sup> Investigation\*Connect\_High and Investigation\*Connect\_Low are not mutually exclusive because Connect includes Connect\_High, Connect\_Low, and firms without political connections.

court advantages of connected firms when the trial took place in a region with a worse legal institution.

To test this proposition, following Lu et al. (2015), we measure the local legal environment according to whether a province was forced to open to foreigners as a treaty port or a leased territory after the First Opium War in 1842. Specifically, after the First Opium War in 1842, the Chinese government was forced to sign treaties with foreign countries to open the port establish treaty ports or leased territories in several of its provinces, which increased China's openness and promoted business contacts and cultural exchange with the rest of the world. In particular, to handle disputes involving foreigners, a system of extraterritoriality was implemented, and foreign courts were established in these regions, which had long-term positive impacts on the development of local legal institutions (Fan et al., 2013). Therefore, we construct a dummy variable Weak\_Legal equal to 0 for the province forced to open as a port or became a leased territory, and 1 otherwise. Next, we introduce the triple interaction term of Weak\_Legal, Investigation, and Connect to the regression.

The results are reported in column 1 of Table 9. As shown, the coefficient of the triple interaction term is negative and statistically significant, suggesting that after the anti-corruption campaign, connected firms in regions with a weak legal environment have a greater decline in win rates than those in strong legal environment regions.

#### Table 9

The Heterogeneous Effects of Anti-Corruption Campaign on Win Rates.

	Dependent Variable: Win					
	The Heterogeneous Effects in different dimensions $(X)$					
	X is Weak_Legal (1)	X is Noncontract (2)	X is Lower_Court (3)			
Investigation*Connect*X	$-0.130^{**}$	$-0.229^{*}$	$-0.280^{**}$			
Investigation*X	0.067*	0.096	0.014			
Connect*X	0.093*	$-0.220^{**}$	0.154			
Investigation*Connect	-0.021	(0.037) $-0.036^{**}$ (0.018)	0.195			
Investigation	(0.021) (0.002) (0.032)	0.037	0.012			
Connect	0.020	0.044*	-0.098			
X	(0.029)	(0.024) -0.161 (0.124)	(0.110) -0.071 (0.145)			
Controls	Yes	Yes	Yes			
Firm FE	Yes	Yes	Yes			
Year FE	Yes	Yes	Yes			
Industry FE*Time linear trends	Yes	Yes	Yes			
Province FE*Time linear trends	Yes	Yes	Yes			
Observations	10,726	10,726	10,726			
Adj R-squared	0.471	0.492	0.472			

Notes: This table analyzes how the impact of anti-corruption on court outcomes varies with the development of local legal institutions, dispute types, and court levels, respectively. We perform these analyses on the matched sample. The dependent variable is Win, which equals one if the disclosing firm wins the lawsuit. Investigation is a dummy variable that equals one in the affected province for both the investigation year and the following years and zero for other years. Connect is a dummy variable equal to 1 for firms with political connections, and 0 for firms without political ties. Weak\_Legal proxies for the local legal environment, equal to 0 if a province was forced to open to foreigners as a treaty port or leased territory and 1 otherwise. Noncontract equals 1 for noncontract-related cases and 0 for contract cases. Lower\_Court equals 1 when the trial takes place in county-level basic courts, and 0 for intermediate courts and higher courts. All specifications include a full set of lawsuit-level, firm-level, and province-level control variables. All other variables are defined in Section 3.4. Robust standard errors clustered at the province level are reported in parentheses. \*\*\*, \*\*, and \* indicate significance at the 1%, 5%, and 10% levels, respectively.

## 4.4.2. Dispute types

While political connections may play a role in judges' decisionmaking, the potential for political maneuvering varies across different types of cases. In particular, compared to non-contract cases, in contract cases, the rights and obligations of both parties are stipulated in a relatively clear manner in contractual agreements. As a result, in contract cases, it is difficult for judges to deliberately distort facts in the fact-finding process. Prior studies have shown that contract disputes are different from noncontract-related disputes in that contracts confer more predictability and legitimacy on the contracting parties' claims since both parties can observe the contractual terms and relevant actions (Kessler et al., 1996; Shavell, 1996; Siegelman and Waldfogel, 1999; Wang, 2018; Xu, 2020).<sup>60</sup> Since contracts grant the contracting parties more predictability

<sup>&</sup>lt;sup>60</sup> Wang (2018) and Xu (2020) also document that there is less room for political maneuver in adjudicating contract-based disputes compared to non-contract cases. Particularly, Xu (2020) argues that this finding is in line with the interview responses of the trial judges he interviewed, who said that there was little room for political maneuver in deciding contract cases. And the judges he interviewed said that they had to respect the agreements reached between the disputing parties, and it was relatively easy to rule on the claims based on the rights and obligations delineated in contractual agreements. Thus, the judges generally agree that contract cases are more predictable than other types of cases.

and legitimacy in their claims, judges have to adjudicate a claim based on the rights and obligations delineated in the contractual agreement, and to some extent, honor the agreement reached among the disputing parties. Therefore, compared with contract cases, there is more room for political maneuver in adjudicating noncontractrelated cases. Judges' decisions are more susceptible to interference from external extra-judicial factors in trials against noncontractrelated cases. Thus, the intuition is that the anti-corruption campaign has a greater impact on noncontract-based disputes than contract disputes.

To test that, we construct a dummy variable (*Noncontract*) to categorize all cases into two types of disputes: contract cases and noncontract-related cases. Specifically, *Noncontract* equals 1 for noncontract-related cases and 0 for contract cases. We then add triple interaction terms of *Noncontract*, *Investigation*, and *Connect* to the regression. As expected, in column 2 of Table 9, the coefficient of the triple interaction term is negative and significant at least 10% level, indicating that win rates of connected firms experience a more significant decline in noncontract-related cases than contract cases after the anti-corruption campaign, which is in line with our expectations. Overall, our results suggest that contractual agreements can, to some extent, reduce the interference of local officials in judicial decisions.

## 4.4.3. Court level

Local courts in China are institutionalized at three levels, from low to high, including more than 3,500 county-level basic courts, over 400 intermediate courts located in municipalities, and 32 higher courts located in the provinces. In particular, lower-level judges are more vulnerable to external interference than higherlevel judges due to the unique institutional arrangements that local governments control over judges' careers and court budgets. First, a distinctive feature of Chinese politics is a heavy emphasis on political rank. And Chinese courts traditionally have been viewed as part of the government. For local courts, not only can local governments at their corresponding levels have personnel power over the judiciary, but higher local governments can also influence judges' careers by interfering in the decisions of lower-level local governments. As a result, judges' careers in county-level courts can be influenced by county, city, and provincial governments, while the career development of city-level court judges would be shaped by city and provincial governments, and judges' careers in 32 province-level courts are mainly controlled by provincial governments. Consequently, judges in the lower courts are subject to more interference from corrupt local officials than in the higher courts. Second, in China, local courts are dependent on local governments at their corresponding levels for finance resources. Meanwhile, compared to provincial governments or prefecturelevel, county-level governments face larger fiscal deficits because higher-level governments have the power to allocate local revenues and favor their own urban districts, while responsibility for most public services and expenditures mainly falls on countylevel governments under the fiscal system. As a result, given the shortage of financial resources of lower-level governments, lower-level courts are frequently underfunded and even unable to meet basic expenses (Peerenboom, 2009; Wang, 2013), which makes lower-level courts even more deterred from disobeying orders from local corrupt officials in order to secure financial support. As a result, judges in higher-level courts are typically more immune to political interference than judges in lower-level courts, and they are thus expected to be more impartial in adjudicating cases (Zhang, 2012). Then we should find that the anticorruption campaign imposed a more significant influence when the case is tried in lower-level courts than in higher-level courts.

To test the court-level effect, we construct a dummy variable (*Lower\_Court*) to classify courts into higher or lower levels, which

equals 1 when the trial occurs in county-level basic courts, and 0 for intermediate courts and higher courts. Then we add the triple interaction terms of *Lower\_Court*, *Investigation*, and *Connect* to the regression. As shown in column 3 of Table 9, the coefficient of *Investigation\*Connect\*Lower\_Court* is negative and statistically significant, denoting that the win rate of connected firms experiences a more significant decline when the case is tried in lower-level courts than higher-level courts after the anti-corruption campaign. Overall, these results support our supposition.

## 4.5. Discussion of alternative explanations

In this subsection, we consider two major alternative interpretations about our key results and discuss how our evidence helps rule out these competing explanations.

## 4.5.1. The first alternative explanation

A major alternative hypothesis might be that the greater reduction in the win rate of politically connected firms simply reflects a larger decline in their financial performance following the anti-corruption campaign, assuming that a firm's win rate is positively correlated with its financial capacity. Specifically, before the anti-corruption campaign, politically connected firms could receive some preferential treatment from governments (e.g., access to credit, government contracts, or subsidies). With these extra resources, they have greater financial capabilities and thus can win more in court (for example, by hiring better lawyers). The anti-corruption campaign severs that link and politically connected firms perform worse and therefore win less. In this story, the higher win rate of politically connected firms would not be evidence of court bias, but rather their greater financial capacity.

However, this alternative hypothesis is incompatible with most of our empirical results. First, in our specifications, we already introduce some firm performance indicators as additional controls (e.g., market share and profitability). More importantly, to eliminate the bias caused by the systematic differences (e.g., financial capacity) between connected and unconnected firms, we apply PSM matching. Thus, this alternative hypothesis cannot explain why we still observe a higher win rate of connected firms than unconnected firms during the pre-campaign period, after we pair politically connected firms with unconnected firms that have similar observed attributes by the PSM matching. Second, the cross-sectional heterogeneity provides additional evidence to support our main hypotheses. This alternative hypothesis also fails to explain why the positive effect of the anti-corruption is more pronounced in noncontract-based lawsuits and in lower-level courts, where court decisions are vulnerable to local officials' intervention, but there are no substantial variations in financial performance. We acknowledge that the above results may not completely rule out the alternative explanation. Therefore, we conduct three additional empirical exercises to further rule out this alternative hypothesis.

(a) The Effects of Anti-Corruption Campaign on Firm Financial Performance

To start with, we directly check whether the anti-corruption campaign indeed led to heterogeneous changes in the financial circumstances across firms with and without political connections. Specially, we construct a firm-year panel dataset spanning the 2009–2018 period to test this issue using Chinese listed firms. Following the literature (Hao et al., 2020; Kuang et al., 2021), our measures of firms' financial performance include (1) sales revenue (*Revenue*), defined as the log of total sales revenue; (2) profit margin (*Profit\_Ratio*), defined as the net profits over sales; (3) return on assets (*ROA*). Table 10 reports the results. Inconsistent with the

#### Table 10

The Effects of Anti-Corruption Campaign on Firm Financial Performance.

	Firm Financial Performance		Controlling for		Law Firm Quality		
				Policy Favors	Quality of law firms		
Dependent Variable:	Revenue	Profit_Ratio	ROA	Win		lnLawfirm_Size	lnLawfirm_Age
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Investigation	-0.006	-0.011	-0.001	0.044	0.060*	0.426***	0.300***
	(0.014)	(0.021)	(0.003)	(0.027)	(0.034)	(0.063)	(0.069)
Connect	0.004	-0.025	-0.001	0.051**	0.086***	0.036	-0.063
	(0.012)	(0.022)	(0.002)	(0.023)	(0.030)	(0.162)	(0.078)
Investigation <sup>*</sup> Connect	0.020	0.036*	0.001	$-0.077^{***}$	-0.105***	-0.037	0.086
	(0.019)	(0.020)	(0.003)	(0.026)	(0.031)	(0.168)	(0.066)
Controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Firm FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Industry FE*Time linear trends	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Province FE*Time linear trends	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Control for policy favors				Yes	Yes		
Control for quality of law firms					Yes		
Observations	24,292	24,292	24,294	7823	9917	9364	9364
Adj R-Squared	0.948	0.167	0.352	0.466	0.466	0.448	0.337

Notes: This table reports the results that help us to rule out the first alternative explanation. Columns 1–3 examine the effects of the anti-corruption campaign on firms' financial performance. We construct a firm-year panel dataset spanning the 2009–2018 period to test this issue using all Chinese listed firms. The dependent variables are sales revenue (*Revenue*), profit margin (*Profit\_Ratio*), and return on assets (*ROA*), respectively. Column 4 reports the result including policy favors as additional control variables. We perform these analyses on the matched sample. The dependent variable is *Win*, which equals one if the disclosing firm wins the lawsuit. The policy favors include: the cost of debt (*Debt\_Cost*), defined as interest expenses divided by total debt; the tax rate(*Tax\_Rate*), defined as the total tax over firm profit; government subsidies (*Subsidy*), defined as the logarithm of one plus the total amount of government subsidies received by the firm; the value of procurement contracts(*Procurement*), defined as the logarithm of one plus the total amount of government subsidies received by the firm; the value of procurement contracts(*Procurement*), defined as the logarithm of one plus the total value of government procurement contracts obtained by the firm; and transacted price(*Land*), defined as the logarithm of one plus the average land price paid by the firm. Column 5 reports the results controlling for the quality of law firms. We perform these analyses on the matched sample. The dependent variable is *Win*. We measure the quality of law firms by two indicators: registered capital (*InLawfirm\_Size*), defined as the natural logarithm of one plus the firm's registered capital; and age (*InLawfirm\_Age*), defined as the natural logarithm of one plus the number of years since the firm was founded. Columns 6 and 7 examine whether anticorruption leads to a decline in the quality of law firms. We perform these analyses on the matched sample. The dependent variable are form without political ton

alternative explanation, using all measures of financial performance, our estimates in columns 1-3 show that China's anticorruption did not have a significant negative impact on the financial performance of connected firms. Note that these findings are consistent with Hao et al. (2020) and Pan and Tian (2020), who also find that China's anti-corruption did not have a significant negative impact on the financial performance of connected firms. Moreover, based on evidence from Brazil, Colonnelli et al. (2022) also show that politically connected firms did not see a decline in size following the anti-corruption campaign. In other words, there is no empirical evidence that the anti-corruption campaign has a differential impact on the financial performance between connected and unconnected firms, and in particular, a negative impact on the performance of connected firms. We argue that although politically connected firms tend to receive policy favors from local governments, these are not costless. Particularly, firms' political connections may indicate severe government intervention, which distorts the ultimate objectives of firms. For example, to fulfill social or political goals favored by the government, firms tend to be compelled to invest in unprofitable but politically favored projects, resulting in investment inefficiency (Chen et al., 2011a,b; Giannetti et al., 2021). In addition, Hao et al. (2020) find that in China, politically connected firms often pay large charitable donations in exchange for policy favors. Meanwhile, a growing body of literature documents that connected firms tend to operate inefficiently, especially in emerging market economies (Johnson and Mitton, 2003; Khwaja and Mian, 2005; Li et al. 2008). Consequently, after the campaign, policy favors received by connected firms may be diminished, but the political costs to those enterprises may also be mitigated, resulting in the little negative impact of anti-corruption on the financial performance of politically connected firms.

## (b) Including Policy Favors as Additional Control Variables

In this subsection, we include a range of policy favors that connected firms in China tend to receive as additional control variables to further rule out the possibility that our results are driven by connected firms' greater financial capacity due to policy favors. Specifically, in China, the government can grant firms, especially connected firms, various preferential treatments, mainly including preferential bank credit, more government subsidies or government contracts, favorable tax treatment, and lower land transacted prices. We then quantify the above policy favors and introduce them in the model in turn, including (1) the cost of debt (Debt\_Cost), defined as interest expenses divided by total debt; (2) the tax rate (Tax\_Rate), defined as the total tax over firm profit; (3) government subsidies (Subsidy), defined as the logarithm of one plus the total amount of government subsidies received by the firm; (4) the value of procurement contracts (*Procurement*), defined as the logarithm of one plus the total value of government procurement contracts obtained by the firm; (5) land transacted price (Land), defined as the logarithm of one plus the average land price paid by the firm. To construct these variables, we mainly employ the following datasets: data on taxes at the firm level is retrieved from the China Center for Economic Research (CCER) database; data on federal public procurement come from the website of the China Government Procurement (https://www. ccgp.gov.cn/); the land transaction data set is obtained from the website of the Land Transaction Monitoring System (https:// www.landchina.com/); other data is obtained from the China Stock Market and Accounting Research Database (CSMAR).

Column 4 of Table 10 reports the results including these policy favors as additional control variables. As shown, the coefficient of *Investigation\*Connect* retains similar pattern, is significantly negative, and similar in magnitude to the baseline results, which

provides additional evidence to support our main hypotheses.

(c) The Role of Law Firms

The alternative explanation mentioned earlier for the drop in the win rate of the connected firms after the anti-corruption is that their financial performance became worse, causing them to be unable to afford to hire high-quality law firms, a primary mechanism for the validity of this competing story. Therefore, in this subsection, we first control for the quality of the law firm engaged by the disclosing firm in its lawsuit, and the inclusion of these measures as covariates in regressions should lead to a decrease in the magnitude of the coefficient on *Investigation\*Connect* if our results are driven by a decline in the financial performance of politically connected firms and thus the quality of law firms hired. Then, we further investigate whether the anti-corruption campaign leads to a decline in the quality of law firms hired by connected firms.

To gauge law firm quality, we extract the name of the law firm employed by the disclosing firm from the raw judgment documents utilizing textual analysis tools. Next, we get data on these law firms from the State Administration for Industry and Commerce of China (SAIC), which including detailed information on firms' registered addresses, date of registration, registered capital, enterprise type, and so on. Considering the availability of the data, we measure the quality of law firms by two indicators: registered capital (*lnLawfirm\_Size*), defined as the natural logarithm of one plus the firm's registered capital; and age (*lnLawfirm\_Age*), defined as the natural logarithm of one plus the number of years since the firm was founded. In general, the larger and older the law firm, the more experienced and the higher quality it tends to be, which is also verified by our empirical results below that cases conducted by larger or older law firms are more likely to win.

Column 5 of Table 10 reports the results after controlling for the quality of the law firm engaged by the disclosing firm. As shown, the coefficient of *Investigation\*Connect* remains negative and significant. Note that the estimated treatment effect becomes even larger. In addition, the coefficients of *InLawfirm\_Size* and *InLawfirm\_Age* are both positive and statistically significant<sup>61</sup>, which suggests that cases conducted by larger or older law firms are more likely to win, further justifying our measure of law firm quality by these two indicators, i.e., size and age.

Then, we further examine whether the anti-corruption campaign leads to a decline in the quality of law firms hired by connected firms. We do so by repeating our baseline model (1) using variables of the quality of the law firm hired by the disclosing firm (i.e., *lnLawfirm\_Size* and *lnLawfirm\_Age*) as the dependent variable. Columns 6 and 7 of Table 10 report the results. Inconsistent with the alternative explanation, using two measures of law firm quality, our estimates show weak and statistically insignificant effects of the anti-corruption campaign on the quality of law firms retained by connected firms. In other words, no empirical evidence exists to suggest that the anti-corruption campaign heterogeneously affects the quality of law firms hired by firms with and without political connections.

Taken together, these three additional empirical exercises provide additional confidence that our results are not driven by this alternative explanation, i.e., a decline in the financial performance of politically connected firms, which further validates our main story.

## 4.5.2. The Second alternative explanation

The second alternative interpretation is that, there are no corrupt politicians and undue political influence on the judges, but rather collusion between corrupt judges and politically connected firms, and the anti-corruption directly eradicated these corrupt judges so that the connected firms won less. However, it is difficult to explain why absent the intervention of politicians, judges would be more likely to be captured by and favor politically connected firms than non-politically connected ones. One may argue that connected firms tend to have greater financial capabilities and resources, making them easier to capture the courts, even without the influence of politicians. But, in our matched sample, we observe no significant differences between connected and unconnected firms in most firm characteristics, except for their political connection status.

Moreover, this alternative explanation is also incompatible with this anti-corruption campaign's targets and some of our empirical findings and is therefore less of a concern in our context. On the one hand, in terms of the main targets of this anti-corruption inspection, the CCDI, responsible for the implementation of this anti-corruption, has clearly stated that this investigation primarily targeted politicians. According to the CCDI, the CITs mainly investigated corruption in the local party and government organs, including party committees, governments, the People's Congresses, and the People's Political Consultative Conferences<sup>62</sup>, which are decision-making bodies of local governments and hold the greatest power and authority over local governance, and are therefore the most prevalent source of extrajudicial influence in China. And it is commonly acknowledged that in China, local corrupt politicians have always been a major source of external interference in the judicial process, and they are precisely the main targets of this anticorruption inspection. On the other hand, results in Sections 4.3 and 5 further validate our claims that this campaign reduces court bias primarily by deterring politicians from interfering with trials and reduce concerns about this alternative explanation. Specifically, in Section 5, we find that when some court leaders face stronger career concerns or some courts are under greater financial pressure, politicians' interference in trials becomes more common and connected firms have a higher win rate before the campaign, and the effects of anti-corruption are more salient in such a scenario. And in Section 4.3, we find that anti-corruption has a greater impact on firms connected to officials with a higher rank than that of the court. If the alternative hypothesis holds, we would not observe differences in the impact of anti-corruption on court bias between courts with different levels of dependence on local governments or between firms with different strengths of political connections.

## 4.6. Other robustness checks

In this section, we conduct several sensitivity analyses to check the robustness of our results. The analyses are conducted by conducting a placebo test, by controlling for the interaction term *Investigation\*SOE*, including judge fixed effect, and using different matching algorithms. Our main results remain unchanged. The detailed discussions are described in Online Appendix C.

## 5. How politicians interfere with trials: An exploratory analysis on the heterogeneity in the dependence of courts on local governments

As described previously, in China, corrupt local politicians have always been a major source of extrajudicial influence, largely because local courts, especially their personnel and resource allocation (e.g., budget, land, infrastructure upgrades, and court buildings), are under the control of the local government, making it

<sup>&</sup>lt;sup>61</sup> To save space, we do not report the coefficients of *lnLawfirm\_Size* and *lnLawfirm\_Age*, but they are available on request.

<sup>&</sup>lt;sup>62</sup> These four departments make up the entire local political system in China, and their leaders (taking prefecture as an example) are the party secretary, the mayor, the chairman of the Municipal People's Congress and the chairman of the People's Political Consultative Conference, all of whom are the most powerful leaders in local governments.

difficult for judges to remain shielded from local corrupt political influences.

In this section, we explore whether the impact of the anticorruption on court bias varies across courts with different levels of dependence on local governments, whereby we hope to provide suggestive evidence on how or why politicians can exactly interfere with trials, thus further validating our proposition. Specifically, in our main proposition, we argue that the higher precampaign win rates of politically connected firms are largely due to political interference, and the anti-corruption campaign reduced judicial bias in favor of connected firms, primarily through effectively combating politicians' interference in trials. And the courts' dependence on local governments can reflect the vulnerability of courts to political interference. The intuition is that the more dependent local courts are on local government, the more difficult it is for them to defend themselves against undue political interference. If our main proposition holds, we should observe that connected firms have a higher pre-anti-corruption win rate in courts that rely more heavily on local government, and anti-corruption should be more effective in such cases. Particularly, these results would provide greater confidence in our proposition, shed empirical light on why politicians can interfere with trials, and also reduce concerns about other alternative interpretations<sup>6</sup>

Measuring the courts' dependence on local governments is, of course, extremely challenging. In this section, we quantify the extent of courts' reliance on local governments based on the institutional features mentioned above, namely, the direct control of local governments over resource allocation (e.g., finances and land) and personnel of local judiciaries. As we described earlier, on the one hand, local governments have personnel power over the judiciary and can effectively control the appointment and promotion of judges; on the other hand, each court's budget is determined by the local government where it is located. As a result, when faced with stronger career concerns or greater fiscal pressures, local courts are more dependent on the local government and thus more likely to defer to the mandates of local politicians. If our main story is valid, we predict that when court leaders face stronger career concerns or courts are under greater financial pressure, politicians' interference in trials will become more common, and connected firms have a higher win rate before the campaign, and thus effects of the anti-corruption campaign are more pronounced in such a scenario.

## 5.1. Career concerns

The existing literature on Chinese politics suggests that the political career concerns of court leaders are the primary attribute of the local politicians' political interference in court decisions (He, 2012; Liebman, 2017). Then, we provide suggestive evidence on whether the win rate of connected firms increases with court leaders' career concerns, and therefore, the effects of anti-corruption are more prominent in such cases. In China, local governments have personnel power over the judiciary. To achieve their objectives of career advancement, some court leaders and judges in local courts strategically cater to the needs of political interests and avoid offending corrupt local politicians before the anticorruptioni campaign. In particular, some court leaders with stronger career concerns are more motivated in courts' daily work to make sure that their rulings look after the vested interests of local corrupt politicians, and are therefore more subservient to political pressure. Thus, we propose that connected firms have a higher win rate before the anti-corruption and the effects of anti-corruption campaigns are more salient when trials take place in courts where court leaders have stronger career concerns.

Gauging the career concerns of court leaders is challenging. In this section, we propose two tests. First, referring to the study on electoral cycles, we argue that some court leaders and judges have stronger career concerns in election years. And the study on electoral cycles suggests that officials' political incentives vary with election cycles, peaking in the run-up to and in election years. Therefore, in election years, some judges' decisions are expected to be more sensitive to local political interference, since court leaders are more likely to require judges to favor connected firms when doing so will increase the likelihood of the court leaders obtaining votes for him/ her self from corrupt local politicians. As a result, though local officials often attempt to influence trials, such political interference may be more likely to succeed in the periods leading up to elections, when some court leaders face stronger career concerns and thus have to cater to the needs of political interests and rule in favor of corrupt local politicians and their allies to achieve personal career advancement. Thus, we predict that connected firms exhibit higher win rates in local election years than in non-election years, and the decline in court advantage of connected firms is significantly larger in election years following the anti-corruption campaign.

To test that, we construct the election dummy (Election), which takes a value of one in the year of the National Congress of the Communist Party and the year before, when court leaders face stronger career concerns.<sup>64</sup> The results are presented in Table 11. Specifically, Election \*Connect measures that, before the anticorruption campaign, the average difference in the win-rate disparity between connected and unconnected firms across courts in the election and non-election years. Investigation\*Connect\*Election measures, how the average difference in the win-rate disparity between connected and unconnected firms across courts in election and nonelection years is affected by the anti-corruption campaign. As shown in column 1 of Table 11, the coefficient of *Election\*Connect* is positive and statistically significant, indicating that before the anticorruption campaign, politically connected firms exhibit higher win rates in election years than in non-election years, consistent with our proposition. In addition, the coefficient of Investigation\*Connect\*Election is negative and statistically significant, implying that the decline in the win rate of connected firms is larger in election years following the anti-corruption.

Second, we measure the promotion pressure of court leaders by the number of their competitors. The intuition underlying the relationship is simple: the pressure on court leaders to advance increases as the number of competitors grows, making the courts more subservient to local politicians. Specifically, in China, the promotion of officials is particularly competitive because of the limited number of positions available for career advancement but a large number of competitors. In terms of the judiciary, leaders of different lower courts tend to compete for positions in higherlevel courts within the same jurisdiction. There are primarily three levels of subnational governments in China, in descending order: the provincial level, the prefecture level (or city level), and the county level. For example, leaders of different courts at the county level in the same prefecture are competitors in the pool of candidates for prefecture-level court positions in the prefecture where they are located. Given the similar number of prefecture-level court positions across different prefectures, the greater the number of county-level courts there are in a prefecture, the more pressure there is on county-level court leaders to advance, and thus the more likely they are to defer to the local politicians' mandates

<sup>&</sup>lt;sup>63</sup> For example, another alternative explanation is that there was no undue political influence on the judges, but rather collusion between judges and connected firms, and the anti-corruption eradicated these corrupt judges, so that connected firms won less. And if the alternative hypothesis is true, we would not see the above results.

<sup>&</sup>lt;sup>64</sup> Note that the Congress of the Communist Party is held in the same year across all provinces, consistent with the National Congress of the Communist Party.

## Table 11 The Role of Career Concerns and Budgetary Allocations.

	Dependent Variable: Win				
	The Role of				
	Career Con	cerns	Budgetary allocations		
	X is Election (1)	X is Competition (2)	X is Fis_Depend		
Investigation*Connect*X	-0.225* (0.118)	$-0.131^{***}$ (0.040)	$-0.063^{**}$ (0.025)		
X*Connect	$0.240^{**}$ (0.111)	0.153 <sup>***</sup> (0.032)	0.102 <sup>***</sup> (0.023)		
Investigation*X	0.057 (0.060)	-0.051* (0.026)	0.061 (0.037)		
Investigation*Connect	$-0.077^{*}$ (0.039)	$-0.077^{*}$ (0.039)	$-0.048^{***}$ (0.018)		
Investigation	0.058* (0.031)	0.014 (0.037)	0.037 (0.025)		
Connect	0.050 (0.035)	0.029 (0.034)	0.037 (0.033)		
X		$0.104^{**}$ (0.044)	$-0.041^{*}$ (0.022)		
Controls <sup>1</sup>	Yes	Yes	Yes		
Firm FE	Yes	Yes	Yes		
Year FE	Yes	Yes	Yes		
Industry FE*Time linear trends	Yes	Yes	Yes		
Province FE*Time linear trends	Yes	Yes	Yes		
Observations	10,726	10,726	10,726		
Adj R-Squared	0.487	0.491	0.488		

Notes: This table conducts an exploratory analysis on the heterogeneity in courts' dependence on governments in terms of the career concerns of court leaders and budgetary allocations. We perform these analyses on the matched sample. The dependent variable is Win, which equals one if the disclosing firm wins the lawsuit. Investigation is a dummy variable that equals one in the affected province for both the investigation year and the following years, and zero for other years. Connect is a dummy variable equal to 1 for firms with political connections, and 0 for firms without political ties. Election is a dummy variable, which takes a value of one in the year of the National Congress of the Communist Party and the year before. Competition is a dummy variable, which equals 1 when leaders of the court c face greater promotion pressure, and 0 otherwise. Fis\_Depend<sub>c.t</sub> measures court c's fiscal pressure, a dummy variable that equals 1 in the affected court (i.e., constructing new buildings) for two years before and after each construction, implying greater fiscal pressure on the court, and 0 for all other years. All specifications include a full set of lawsuit-level, firm-level, and province-level control variables. All other variables are defined in Section 3.4. Robust standard errors clustered at the province level are reported in parentheses. \*\*\*, \*\*, and \* indicate significance at the 1%, 5%, and 10% levels, respectively.

<sup>1</sup> *Election* dummy is absorbed by the year fixed effects since the Congress of the Communist Party is held in the same year across all provinces.

for their career advancement. And the same holds for prefecturelevel court leaders.

Therefore, we manually collect information on courts nationwide and calculate the number of courts of the same level within the same judicial district. In other words, we count the number of county-level courts within the same prefecture and the number of prefecture-level courts within the same province, and then match them to the trial court in our litigation sample. According to our statistics, the number of county-level courts within different prefectures varies greatly, from a minimum of 4 to a maximum of 23, suggesting that the promotion pressure of court leaders varies widely across regions. Then we divide the courts into those where court leaders face greater promotion pressure and those where they face less according to the median of the number of courts of the same level within the same judicial district. Based on that, we construct a dummy variable (*Competition*) that equals 1 when leaders of the court *c* face greater promotion pressure, and 0 otherwise.

Column 2 of Table 11 reports the results. As shown, the coefficient of *Competition\*Connect* is positive and significant at the 1%

level. The results suggest that, before anti-corruption, compared to courts where their leaders have less promotion pressure, politically connected firms have a higher win rate when the case is heard in courts where their leaders have greater promotion pressure. In terms of *Investigation\*Connect\*Competition*, the estimates is negative and significant. That is, the decline in win rates of connected firms after the anti-corruption campaign is significantly larger in courts where their leaders have greater promotion pressure, consistent with our expectations.

## 5.2. Budgetary allocations

Then, we explore whether the win rates of connected firms are higher when cases are tried in courts with greater fiscal pressure than in those with less fiscal pressure, and thus whether the effects of anti-corruption in reducing court bias are more pronounced in financially stressed courts. Local courts are financed by local governments at the same territorial level and depend on local governments for such necessities, including judges' salaries and bonuses, office supplies, vehicles, and court buildings. In particular, in China's political hierarchy, the judiciary traditionally has a lower status and weaker bargaining position than other party-state organs, making the courts vulnerable to underfunding in the allocation of local funds. Each year, the court prepares a budget to submit to the local government, which determines how much financial resources are allocated to the court. As a result, local corrupt politicians can use their budgetary powers to interfere with judges' decisions and pressure them to rule in favor of their patronage networks and important business partners. Therefore, we expect that when trials take place in courts facing greater financial pressures, connected firms have a higher win rate before the anti-corruption, and the effects of anti-corruption campaigns are more salient.

Notoriously, it is extremely challenging to measure the courts' fiscal pressure or their dependence on local government for financial resources since most courts do not disclose their financial information. In this section, we develop one novel indicator of fiscal pressure on the courts based on the land transfer data. According to the statistics of the Supreme Court, since 2000, more than 70% of courts nationwide have built new people's courts, trial courts, and office buildings, and the resulting huge financial expense has increased the financial pressure on the courts. Since the court relies heavily on the local government for financial resources, the building costs are largely borne by local governments, which determine how much of the budget should be spent on new court buildings or infrastructure, hence increasing the courts' reliance on them. Moreover, since the 1990s, land and other natural resources have been decentralized to local governments, thus the courts are required to apply to local governments for the land needed to build new buildings. Therefore, we treat the construction of court buildings as a relatively exogenous shock that increases the financial pressure on the court and its dependence on the local government. It is worth noting that this measure is echoed by extensive anecdotal evidence. In some cases, corrupt government officials have threatened to sever funding needed to build housing for court personnel (Clarke, 1996; Wang, 2008).

Specifically, we obtain the data on the construction of new court buildings from the website of the Land Transaction Monitoring System (https://www.landchina.com/)<sup>65</sup>. We extracted the date of each time the court built a new building based on this data.

<sup>&</sup>lt;sup>65</sup> Under the Land Management Law, the local bureau of land and resources is required to report the allocation and use of each land parcel within its jurisdiction electronically on this website. Whenever a local government handled a parcel of a land, whether it is redevelopment of urban land or conversion of rural land to urban use, it is announced on this website. For each land allocation, the announcement usually contains information on transaction ID, address of land parcel, land usage, land users, appointed construction start date, land area, price, etc.

According to our statistics, 1,069 of the 2,302 courts in our sample had ever constructed new buildings during the period 2009-2018. Based on that, we construct a dummy variable (Fis\_Depend), which equals 1 in the affected court (i.e., constructing new buildings) for two years before and after each construction, implying greater fiscal pressure on the court, and 0 for all other years. We construct this variable in this way for the following reasons: on the one hand, before constructing a new building, the court generally needs to prepare a construction plan and budget at least one year in advance to submit to the local government for review and approval. Therefore, we argue that at least two years before the construction of a new building, the courts anticipate the financial pressure brought by the construction in the following years and thus have to conform to the local officials's mandate in the present to avoid offending the local officials to secure future financial support. On the other hand, the average construction period for a new building after obtaining land parcels is about one to two years, with large capital expenditures during this period. Taken together, we view the two years before and after the construction of the new building as the time when the court felt more financial pressure and therefore became more dependent on local officials. Then we estimate the following model as equation (4):

$$\begin{split} & \text{Win}_{i,t} = \alpha + \beta_1 \text{In} \textit{vestigation}_{p,t} + \beta_2 \text{Connect}_{j,t} + \beta_3 \text{Fis}\_Depend_{c,t} & \text{pairs}_{i,t} \\ & + \beta_4 \text{In} \textit{vestigation}_{p,t} * \text{Connect}_{j,t} + \beta_5 \text{In} \textit{vestigation}_{p,t} & \text{vals}_{i,t} \\ & * \textit{Fis}\_Depend_{c,t} + \beta_6 \text{Connect}_{j,t} * \textit{Fis}\_Depend_{c,t} & \text{whs}_{i,t} \\ & + \beta_7 \text{In} \textit{vestigation}_{p,t} * \text{Connect}_{j,t} & \text{whs}_{i,t} \\ & * \textit{Fis}\_Depend_{c,t} + \gamma_1 \text{lawsuit}\_charac_{i,t} & \text{firm}_{i,t} \\ & + \gamma_2 \text{firm}\_charac_{j,t-1} + \gamma_3 \text{pro} \textit{v}\_charac_{p,t-1} + \delta_j + \textit{v}_t & \text{corrs}_{i,t} \\ & + \sigma_{p,t} + \gamma_{ind,t} + \varepsilon_{i,t} & (4) & \text{uncerted}_{i,t} \end{split}$$

where Fis\_Depend<sub>c,t</sub> measures the court c's dependence on officials in terms of budgetary allocations, a dummy variable that equals 1 in the affected court (i.e., constructing new buildings) for two years before and after each construction, implying greater fiscal pressure on the court, and 0 for all other years. All the other variables are defined as in equation (1). In regression (4),  $\beta_6$  and  $\beta_7$ are the coefficients of interest. In particular,  $\beta_6$  measures that, before the anti-corruption campaign, the average difference in the win-rate disparity between connected and unconnected firms across courts with more and less financial pressure. And we expect  $\beta_6$  to be positive, indicating that connected firms have a higher win rate when cases are heard in courts with greater fiscal pressure than in those with less fiscal pressure. Moreover,  $\beta_7$  measures, how the average difference in the win-rate disparity between connected and unconnected firms across courts with more and less financial pressure is affected by the anti-corruption campaign. We expect  $\beta_7$  to be significantly negative, suggesting that the effects of anti-corruption in reducing court bias are more salient in financially stressed courts, which are more dependent on local officials.

Column 3 of Table 11 reports the results. As predicted, the coefficient of *Fis\_Depend\*Connect* is positive and statistically significant, suggesting that before the anti-corruption campaign, connected firms have a higher win rate in financially stressed courts than in less financially stressed courts. Furthermore, the coefficient of *Investigation\*Connect \*Fis\_Depend* is negative and statistically significant, implying that the effects of anti-corruption in reducing court bias are more salient in financially stressed courts, consistent with our proposition. In other words, compared to courts under less fiscal pressure, courts under more fiscal pressure experience greater improvements in the judicial environment following anti-corruption campaigns since they are more dependent on local governments for finance resources and thus more vulnerable to local political interference.

# 6. Further analysis: Does anti-corruption campaign promote a better judicial environment

We interpret the results documented in Section 4.1 as evidence that the courts have become less biased after the anti-corruption campaign. However, an alternative interpretation is that, after the anti-corruption campaign, as courts are no longer compelled by local governments or politicians to favor politically connected firms, they may simply make negligent rulings. In such cases, the court merely replaces one bias with another, and the observed declines in connected firms' win rates may not indicate an improvement in the quality of judicial rulings.

If the anti-corruption campaign has indeed curbed the interference of extra-legal forces behind the scenes in judges' decisions, which helps to enhance judicial independence and impartiality, then the intuition is that this positive effect would be reflected in an improved judicial environment, in addition to a narrowing of the win rate gap between firms with and without political connections. In this section, to examine this alternative hypothesis, we provide empirical evidence on whether the anti-corruption camign promotes a better judicial environment, which, if true, would lidate our main findings. We begin by investigating whether the ti-corruption campaign has improved judges' decision quality, ich can help us to better understand the mechanisms through nich anti-corruption affects the win rates of politically connected ms. We then examine the impact of anti-corruption on public ist in the judicial system. Finally, we test whether the antirruption campaign eventually encourages more firms, especially connected firms, to settle disputes through the courts.

## 6.1. Quality of judicial decisions

To better understand the mechanisms through which the anticorruption campaign affected politically connected firms' win rates, to start with, we directly examine how the campaign has affected the quality of judicial decisions. Referring to the law literature, we measure the quality of judicial decisions in four different ways, including trial efficiency, the richness of judicial reasoning in judgments, the frequency of citing discretionary codes in rulings, and the court's disapproval rate of requests to examine the evidence.

We begin our investigation of the quality of judicial decisions by examining how the anti-corruption campaign affected trial efficiency (in the spirit of Djankov et al., 2003; Ponticelli and Alencar, 2016), as judges delayed cases as a tactic to deliver biased decisions (Mehmood and Seror, 2022). In developing countries, local officials could intervene in court decisions by deliberately delaying the verdict process, which could help them achieve their desired court outcome. Firstly, delaying the verdict process would reduce judicial efficiency and increase the lawsuit cost of the related parties, which may force the relevant enterprises to withdraw the lawsuit. Secondly, the longer the verdict process is delayed, the more time local officials have to help connected firms win the lawsuit, such as destroying unfavorable evidence. In addition, another purpose of officials to delay the trial process is to solicit bribes from related entrepreneurs, who are hard to bear the long verdict process and hope to improve judicial efficiency. After the anti-corruption campaign, the above judicial corruption will be effectively suppressed. Therefore, we expect that judicial efficiency witnesses a more remarkable improvement after the anticorruption, and we should observe this effect to be more pronounced in cases involving connected firms.

#### Table 12

Anti-Corruption Campaign and Judges' Decision Quality.

Dependent Variable	ln (1 + Time to	Disposition)	Judicial Reasoning	Discretionary Codes	Deny Requests for Evidence Examination
	(1)	(2)	(3)	(4)	(5)
Investigation	-0.211***	-0.047	-0.181	0.122***	0.039
	(0.054)	(0.055)	(0.198)	(0.016)	(0.024)
Connect		0.151	-0.002	0.107*	0.078
		(0.102)	(0.106)	(0.057)	(0.058)
Investigation*Connect		$-0.293^{**}$	0.280*	-0.105*	$-0.096^{*}$
		(0.113)	(0.152)	(0.062)	(0.057)
Controls	Yes	Yes	Yes	Yes	Yes
Firm FE	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes
Industry FE*Time linear trends	Yes	Yes	Yes	Yes	Yes
Province FE*Time linear trends	Yes	Yes	Yes	Yes	Yes
Observations	9641	9641	10,725	10,725	10,725
Adj R-Squared	0.273	0.221	0.182	0.186	0.121

Notes: This table reports the impacts of the anti-corruption campaign on the quality of judicial decisions. We perform these analyses on the matched sample. In columns 1 and 2, we examine the impact of anti-corruption on trial efficiency, with the dependent variable being *Time to Disposition*, measured as the time span of each lawsuit from filing to judgment. Columns 3, 4, and 5 present DiD estimates for word count, the frequency of the judge citing discretionary codes, and courts' disapproval rates for evidence examination requests in judicial reasoning, respectively. *Investigation* is a dummy variable that equals one in the affected province for both the investigation year and the following years, and zero for other years. *Connect* is a dummy variable equal to 1 for firms with political connections, and 0 for firms without political ties. All specifications include a full set of lawsuit-level, firm-level, and province-level control variables. All other variables are defined in Section 3.4. Robust standard errors clustered at the province level are reported in parentheses. \*\*\*, \*\*, and \* indicate significance at the 1%, 5%, and 10% levels, respectively.

Columns 1 and 2 in Table 12 study the effect of the anticorruption campaign on trial efficiency. Specifically, we construct a variable (*Time to Disposition*) as a proxy for the trial efficiency, measured as the time span (in days) of each lawsuit from filing to judgment. The larger the variable (*Time to Disposition*), the lower the trial efficiency. Specifically, in column 1, the coefficient of *investigation* is negative and significant at the 1% level, indicating the anti-corruption campaign significantly improved the trial efficiency. Then, we further examine whether the above effects vary between connected and unconnected firms. As shown in column 2, the coefficient of *Investigation\*Connect* is also negative and statistically significant, indicating that the efficiency of the trial involving connected firms experiences a greater increase than that involving unconnected firms after the campaign.

However, it could still be argued that shorter case delays after the campaign reflect less deliberation in these cases, indicating poorer-quality judicial decisions. Yet, three additional pieces of evidence give us confidence that the decline in connected firms' win rates and case delays actually reflects better-quality judicial rulings. Specifically, besides the trial efficiency, we further follow the law literature and measure the quality of judicial decisions in three different ways: First, the richness of judicial reasoning in the judgment file (measured by word count). In general, the decision is considered more solid in law if a judgment contains more words explaining the judicial reasoning behind the verdict (Liu, 2018). Second, the frequency of citing discretionary codes in the judgment file. Decisions are likely to be more distorted if judges impose too much discretion in their judicial reasoning (Liu and Li, 2019).<sup>66</sup> Third, the court's disapproval rate of requests to examine evidence or invite an expert witness. Generally, the denial of requests for review of key evidence or testimony of an expert witness is associated with less fair trials (Edmond and Roberts, 2011).

Columns 3–5 in Table 12 show that, across all three quality measures, the quality of judicial decisions involving politically connected firms has improved significantly following the anticorruption campaign: (a) in column 3, *Judicial Reasoning* is defined as the natural logarithm of one plus the word count of the judicial reasoning section. As shown, the coefficient of Investigation\*Connect is positive and significant at least 10% level, suggesting that judges provide more detailed legal reasoning for rulings involving politically connected firms after the campaign (as seen by a roughly 30% increase in the length of judicial reasoning); (b) in column 4, we construct Discretionary Codes that takes the value of 1 if the judge cites Discretionary Law Code in the decision, and 0 otherwise. The coefficient of Investigation\*Connect in column 4 is negative and significant. These results imply that judges are 10% less likely to cite discretionary codes when conducting legal reasoning in trials involving politically connected firms, an around 40% decrease over the sample mean; (c) in column 5, we construct Discretionary Codes that takes the value of 1 if the judge does not approve the request to examine key evidence or expert witness testimony in the trial, and 0 otherwise. As shown, the coefficient of Investigation\*Connect is negative and statistically significant. We find that, after the anti-corruption campaign, the court's disapproval rate for requests to review key evidence or expert witness testimony dropped significantly by around 10%.

Taken together, these results paint a consistent picture that the anti-corruption campaign has significantly improved the quality of judicial decisions, with the reduction in post-corruption campaign rulings in favor of politically connected firms reflecting more 'correct' or higher quality judicial decisions. The anti-corruption campaign appears to have removed these judicial biases previously imposed on firms without political connections.

## 6.2. Public trust in the judicial system

According to the above results, the anti-corruption campaign significantly improves the quality of judicial decisions and reduces courts' deliberate favoritism toward politically connected parties. Then, if the effect indeed exists and the economic magnitude of the effect is sizable, the intuition is that we should find that the public has more trust in the judicial system after the anticorruption campaign, which can also validate our main findings. In particular, relative to employees, employers' trust in the judicial system would experience a greater increase as they are more closely linked to the court and judges. Furthermore, given that unconnected firms are commonly disadvantaged in court, we should observe the positive effect to be more pronounced for employers in unconnected firms than those in connected firms.

<sup>&</sup>lt;sup>66</sup> "Discretionary codes" are moral remedies to which judges may resort when formal legal codes contain gaps. For instance, "fairness" is a discretionary code in Chinese law, which calls on the judge to make a fair decision for both parties. Abusing discretionary codes is recognized as a common means to bypass the law and favor one side.

## P. Zhang

To test that, we use individual-level data from the Chinese General Social Survey (CGSS), a national, comprehensive, and continuous social survey dataset carried out in 24 provincial units of China from 2003 to 2017. And the results are all consistent with our proposition. Specifically, we find that anti-corruption indeed enhancespublic trust in the court, especially among employers, and that employers in unconnected firms experience a more significant increase in trust in the court than those in connected firms. The detailed discussions are described in Online Appendix D. Table D1 in the Online Appendix shows that as public trust in the courts has increased, the anti-corruption campaign has also led to more companies settling disputes through the courts, especially those without political connections.

# 7. Economic impacts: Anti-corruption campaigns, improved judicial quality, and regional economic performance

We documented in the previous sections that China's anticorruption campaign has reduced local politicians' interference in court decisions and promoted judicial independence and impartiality, thereby creating a better judicial environment. In this section, we further link judicial quality to economic development and explore how regional economic performance responds to an increase in judicial quality induced by the anti-corruption campaign. Specifically, we adopt a triple difference strategy to compare the differences in changes in economic performance following the anti-corruption campaign between cities with initially poorly and well-functioning judiciaries. The poorer the local judicial quality before the anti-corruption, the more the anti-corruption campaign improves its judicial environment, and thus the greater the impact on local economic performance. Overall, this identification method helps to disentangle changes in the judicial environment from other channels that may also affect local economic performance, thus allowing for an examination of how improvements in the judicial quality induced by the anti-corruption campaign facilitate economic development. In this section, our analysis starts by focusing on the key components of the production function: output, productivity, capital investment, and employment. Then, we examine how the anti-corruption campaign affects firms' entry decisions by enhancing the judicial environment, especially in sectors relying more on judiciaries due to their need for relationshipspecific investments.

## 7.1. Economic production

In this subsection, we link judicial independence and impartiality caused by the anti-corruption campaign to local economic growth and mainly focus on several key components of the production function: output, productivity, capital investment, and employment. Scholars have long hypothesized that an independent and impartial, well-functioning judiciary, by enforcing contracts and securing property rights, may foster investment and drive economic development (North, 1990; La Porta et al., 1997, 1998; Henisz, 2000; Djankov et al., 2003; Acemoglu and Robinson, 2012). Thus, we predict that cities with poorly functioning judiciaries witness a more pronounced increase in economic production following the anti-corruption campaign than those with well-functioning judiciaries. Specifically, we use the following specification:

$$Y_{c,t} = \alpha + \theta Investigation_{p,t} + \beta Investigation_{p,t} * Jud_Poor_c + (X_c * \lambda_t) \eta + \mu_c + \lambda_t + \varepsilon_{c,t}$$
(5)

where  $Y_{c,t}$  represents the economic performance of city c in year t. We focus on four outcomes: i) total output (*Output*), measured by gross value added; productivity (*Productivity*), defined as gross value added per employee; investment (Invest), measured as the fixed asset investment<sup>67</sup>; employment (Employment), defined as the number of employees. Investigation<sub>p,t</sub> indicates the province's anti-corruption status, a dummy variable equals one in affected province *p* for both the investigation year *t* and the following years, and zero for other years. Jud Poor, measures the local judicial environment, with larger values implying poorer judicial quality.<sup>68</sup>  $\mu_c$  is a city fixed effects term capturing time-invariant city characteristics such as geographic location;  $\lambda_t$  is a year fixed effect; and  $\varepsilon_{c,t}$  is the error term. Additionally, we also control for province fixed effect interacted with linear time trends. X<sub>c</sub> is a vector of baseline city characteristics. Following Li et al. (2016) and Lu et al. (2019), we introduce the X<sub>c</sub> variables interacted with the year dummies  $\lambda_t$ , which more flexibly control for the time effects of  $X_c$  on the outcome variables. Referring to the existing literature, the city-level baseline characteristics include a city's distance from a port and the provincial capital, total population, the ratio of government expenditure to revenue, Internet penetration rate, number of college students, and highway mileage, all in 2010. The standard errors are clustered at the province level.

Panels A and B of Table 13 report the results with and without controlling for baseline city characteristics. Four outcomes reported are considered in columns 1–4: output, productivity, investment, and employment. The logarithms of those outcome data are presented. The estimated coefficients of all four outcomes are consistently positive and statistically significant, suggesting that after the anti-corruption campaign, the cities with initially poorly functioning judiciaries gained more investment, employed more labor, produced more output, and witnessed a more pronounced increase in productivity than the cities with well-functioning judiciaries. These findings are consistent with law and economics literature which highlights that the judicial environment matters for economic development.

## 7.2. Firm entry

Then, we explore how the anti-corruption campaign affects firms' entry decisions by enhancing the judicial environment, especially in sectors relying more on judiciaries due to their need for relationship-specific investments. Examining this question is crucial to our understanding of how judicial independence and impartiality affects real economic activity since entrepreneurship is usually identified as an important determinant of aggregate productivity and long-term growth (e.g., Schumpeter, 1911; Kirzner, 1978; Hause and Du Rietz, 1984; Banerjee and Newman 1993; Aghion and Bolton 1997; Black and Strahan, 2002). Theoretically, an independent and impartial judiciary can act as an important constraint on the executive power and makes expropriating, stealing, and bribing more difficult for officials. Consequently, an independent and impartial judicial system can provide good protection for property rights and contract enforcement, thus ensuring that

<sup>&</sup>lt;sup>67</sup> In terms of regional investment activities, the National Bureau of Statistics of China only provides data on fixed asset investment. Specifically, fixed asset investment comprises investment in capital construction, renovation and renewals of existing facilities, real-estate development, other fixed assets by state-owned units and other fixed assets by collective-owned units, as well as private investment in housing construction.

<sup>&</sup>lt;sup>68</sup> Specifically, we collect the raw data from the World Bank's 2005 China Investment Climate Survey, which surveys 12,400 companies in 120 cities in China and is broadly representative. Firms' perceptions of local judicial quality are best captured by their responses to survey question j31, "how much confidence do you have that the disputes will be settled justly by the local legal system", with higher scores (from 0 to 100) indicating greater independence and and impartiality of the local judiciary. Referring to Zhang et al. (2019), to generate a city-level judicial quality index (JQI), we calculate the average of the scores of all firms in a city. Then, to facilitate the interpretation of the results, *Jud\_Poor* is constructed to be equal to (100 – JQI)/100, so that a larger value implies a poorer quality of judicial quality.

#### Table 13

Anti-Corruption, Improved Judicial Environment, and Economic Production.

Dependent Variable	Output (1)	Productivity (2)	Invest (3)	Employment (4)
Panel A: Without controlling for covariates				
Investigation	$-0.044^{***}$	$-0.096^{***}$	-0.085**	$-0.023^{**}$
-	(0.016)	(0.033)	(0.041)	(0.010)
Investigation *Jud_Poor	0.227****	0.414***	0.326*	0.103*
	(0.071)	(0.134)	(0.167)	(0.056)
Panel B: Controlling for covariates				
Investigation	-0.037***	$-0.090^{**}$	$-0.088^{**}$	$-0.024^{**}$
	(0.014)	(0.041)	(0.037)	(0.011)
Investigation *Jud_Poor	0.175***	0.364**	0.273*	0.104**
	(0.058)	(0.162)	(0.156)	(0.052)
City FE	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes
Province FE*Time linear trends	Yes	Yes	Yes	Yes
Observations	1150	1150	1150	1150

Notes: This table examines how the anti-corruption campaign affects local economic production. In columns 1–4, the dependent variables are the natural log of the measure of total output, productivity, invest, and employment, respectively. *Investigation* is a dummy variable that equals one in the affected province for both the investigation year and the following years. *Jud\_Poor* measures the local judicial environment before the anti-corruption campaign, with larger values implying poorer judicial quality. Covariates include city-level characteristics listed in Section 7.1, interacted with the year dummy. The standard errors are reported in parentheses, clustered by province. All regressions control for city fixed effects, year fixed effects, and province fixed effect interacted with linear time trends. \*\*\*, \*\*, and \* indicate significance at the 1%, 5%, and 10% levels, respectively.

future returns to private investments are secured and promises of future payments are fulfilled, ultimately spurring entrepreneurship. Therefore, we predict that, following the campaign, cities with previously poorly functioning judiciaries will see more new enterprises established than cities with previously wellfunctioning judiciaries, especially in industries that are more dependent on the judiciary.

Following Kong and Qin (2021), we quantify firms' entry decisions using new firm entry data from the SAIC. According to the literature (e.g., Black and Strahan, 2002; Kerr and Nanda, 2009;

#### Table 14

Anti-Corruption	, Improved	Judicial	Environment,	and	Firm	Entry.
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Dependent Variable	Firm	Firm entry in industries with				
	entry (1)	Higher contract intensity (2)	Lower contract intensity (3)			
Panel A: Without controlling for covariates						
Investigation	-0.030	-0.040	-0.055			
	(0.040)	(0.094)	(0.095)			
Investigation *Jud_Poor	0.261*	0.661*	0.042			
	(0.152)	(0.374)	(0.403)			
Panel B: Controlling for co	ovariates					
Investigation	-0.045	-0.018	-0.042			
	(0.043)	(0.096)	(0.113)			
Investigation *Jud_Poor	0.353**	0.781**	0.013			
	(0.166)	(0.383)	(0.515)			
City FE	Yes	Yes	Yes			
Year FE	Yes	Yes	Yes			
Province FE*Time linear trends	Yes	Yes	Yes			
Observations	1150	1150	1150			

Notes: This table examines how the anti-corruption campaign affects entrepreneurship by enhancing the judicial environment, especially in sectors relying more on judiciaries due to their need for relationship-specific investments. In column1, the dependent variable is the natural logarithm of one plus a city's total number of new firms per 100,000 people. The dependent variables in columns 2 and 3 measure firm entry in high- and low-contract intensity industries, respectively. *Investigation* is a dummy variable that equals one in the affected province for both the investigation year and the following years, and zero for other years. *Jud\_Poor* measures the local judicial environment before the anti-corruption campaign, with larger values implying poorer judicial quality. Covariates include city-level characteristics listed in Section 7.1, interacted with the year dummy. The standard errors are reported in parentheses, clustered by province. All regressions control for city fixed effects, year fixed effects, and province fixed effect interacted with linear time trends. \*\*\*, \*\*, and \* indicate significance at the 1%, 5%, and 10% levels, respectively.

Faggio and Silva, 2014), we aggregate data up to the city level and calculate the natural logarithm of one plus a city's total number of new firms per 100,000 people during the year to obtain the variable *Firm\_Entry*, which represents the city's entrepreneurship level. The results are presented in column 1 of Table 14. As shown, regardless of whether we control for baseline city characteristics, the coefficients of *Investigation\*Jud\_Poor* are both positive and statistically significant, suggesting that after the anti-corruption campaign, cities with initially poor judiciary attracted more new firms since the anti-corruption had a greater impact on their judicial environment than cities with the initially better judiciary, which is in line with our proposition.

Next, we focus on a specific channel through which the judiciary matters: firms in sectors that rely more on the judiciary should be more affected by contract enforcement mechanisms; hence, they benefit more from the improvements in the local judicial environment caused by the anti-corruption campaign.

To quantify the reliance of different industries on justice, we use a well-established insight in economics: some sectors are more dependent on the judiciary than others due to the need for relationship-specific investments (Klein et al., 1978; Nunn, 2007; Levchenko, 2007; Amirapu, 2021). Consider a buyer who requires the seller to produce a customized good. As there is no other customer for this product, the buyer can negotiate prices down once such a product is produced. To avoid this dilemma, the seller does not enter this relationship and as a result, no customized goods are produced and the economy is trapped in producing generic goods. One solution to this dilemma is to defend the contract through third-party enforcement. Consequently, sectors requiring relationship-specific investments may be especially reliant on a well-functioning judiciary. To capture the sectoral demand for relationship-specific investments, one approach proposed by Nunn (2007) is to measure the fraction of inputs used by a sector that is neither reference priced nor traded on an organized exchange at the 3-digit ISIC level<sup>69</sup>. The intuition is that inputs sold on an organized exchange are generic, whereas inputs not sold on organized exchanges are specific, thus necessitating relationshipspecific investments. We use the contract intensity index developed by Nunn (2007) for 342 industries according to the US NAICS 1997 industry clarification, assuming that the Chinese input-output table

<sup>&</sup>lt;sup>69</sup> Full details on the construction of this variable are available in Nunn (2007).

is the same as the US input–output table at the NAICS 1997 classification level<sup>70</sup>. Then, we classify industries into higher or lower contract intensity according to the median of the contract intensity index.

Columns 2 and 3 of Table 14 examine how the positive effect of the anti-corruption campaign on firm entry varies across industries with different contract intensities. As shown, the coefficient of Investigation\*Jud\_Poor in column 2 is positive and statistically significant, while the estimated coefficient in column 3, although also positive, is statistically insignificant, suggesting that high contract intensity industries benefit more than low contract intensity ones from the improvement in the judicial environment. In conclusion, we find that an independent and impartial judiciary may be less vital for generic commodities, but it is essential for the emergence of the more specific and complicated types of commodities produced, i.e., the development of a modern economy. Our results highlight a precise channel through which the judiciary matters: it encourages firms to undertake relationship-specific investments, confirming the findings of prior research that the judiciary has a significant impact on economic activity, particularly in sectors dependent on relationship-specific investments. These results are important because they provide empirical evidence of the fundamental importance of the judiciary in the economic development process.

#### 8. Conclusion

Using a unique data set of 11,238 commercial lawsuits involving Chinese listed firms, we provide the first empirical analysis to establish the presence of political corruption in court, and identify a novel channel-interfering with court decisions-through which, corrupt officials provide political favors for politically connected firms. We find robust empirical evidence that the anti-corruption campaign alleviates Chinese courts' favoritism toward politically connected parties, while connected firms witness a significant decrease in the probability of winning the lawsuit. These main results still hold after a series of endogeneity and robustness tests. In addition, the impact of the anti-corruption campaign on court outcomes varies in a theoretically predictable manner: the effect is more salient for firms connected to officials with a higher rank than that of the court, noncontract-based cases, lower-level courts, and regions with weak legal environments, under which judges' decisions are more susceptible to interference from external extra-judicial factors. An exploratory analysis on the courts' dependence on local government shows that when courts rely more heavily on local government, connected firms have a higher precampaign win rate, and in this case, the anti-corruption campaign's effects are also stronger. Moreover, anti-corruption promotes a better judicial environment, including improving the quality of judicial decisions, boosting public confidence in the judicial system, and encouraging firms to settle conflicts more often through court. Finally, we further explore the campaign's broader economic influences and find that after the campaign, cities with initially poorly functioning judiciaries gained more investment, employed more labor, and produced more output, while also attracting more new firms, particularly in those industries with high contract intensity.

Our empirical findings likely reflect the fact that the state is endeavoring to draw on anti-corruption campaigns to curb its judiciary from redistributing wealth from parties that are not politically favored to those that are. Moreover, evidence from China is informative about emerging economies with weak legal systems. In these countries, the use of courts to resolve disputes has increased dramatically as a result of market-oriented reforms, with many welfare redistribution decisions made by courts each year, whereas with the lack of an independent and impartial judiciary, judges' decisions are more susceptible to interference from external extra-judicial factors, particularly the underlying political connections of litigants. Our results suggest that regulators in developing economies must focus on eliminating judicial corruption to safeguard private property rights and constrain the corrupt officials from appropriating private property rights. Overall, our study provides timely implications for policymakers in emerging markets concerned about the causal effects of anti-corruption on legal institutions, and suggests that the anti-corruption campaign significantly improved the judicial and economic environment.

## **Declaration of Competing Interest**

The authors declare that they have no known competing financial interests or personal relationships that could have appeared to influence the work reported in this paper.

## Appendix A. Supplementary data

Supplementary data to this article can be found online at https://doi.org/10.1016/j.jpubeco.2023.104861.

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