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Law, Politics, and Trade Credit in China*

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July 2024

Abstract

This paper explores the interplay between politics and law enforcement in China and its effects on firm financing decisions. By examining a sample of corporate lawsuits involving listed firms in China, we find that politically connected firms are less likely to be defendants, have higher win rates, and experience shorter litigation durations than non-connected firms. Additionally, we observe that firms with higher legal risk extend more accounts receivable and receive less accounts payable, but this relationship holds only for non-connected firms. Our findings support the financing advantage theory for politically connected firms and the legal risk compensation view for non-connected firms. Moreover, reforms in China's judicial system do not appear to mitigate the disadvantages faced by non-connected firms in terms of lawsuit outcomes and trade credit provision. Our findings suggest that well-functioned judicial independence might be still lacking in China, and that political connections continue to negatively impact law enforcement and corporate policies.

JEL Classification: G32; G38; K42

Keywords: Lawsuits; Judicial reforms; Political connections; Trade credit

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Abstract

This paper explores the interplay between politics and law enforcement in China and its effects on firm financing decisions. By examining a sample of corporate lawsuits involving listed firms in China, we find that politically connected firms are less likely to be defendants, have higher win rates, and experience shorter litigation durations than non-connected firms. Additionally, we observe that firms with higher legal risk extend more accounts receivable and receive less accounts payable, but this relationship holds only for non-connected firms. Our findings support the financing advantage theory for politically connected firms and the legal risk compensation view for non-connected firms. Moreover, reforms in China's judicial system do not appear to mitigate the disadvantages faced by non-connected firms in terms of lawsuit outcomes and trade credit provision. Our findings suggest that well-functioned judicial independence might be still lacking in China, and that political connections continue to negatively impact law enforcement and corporate policies.

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“Law is one of the primary products of politics and the goal for which many political conflicts are fought. It might be said that it is closely related to the study of politics because it is the main tool used by the government to impose its will on society. But the law is also a means for the government to organize itself..... Here the law is not only the product of politics but also the constitution of politics.”

Whittington, Kelemen, and Caldeira, 2008

1. Introduction

A burgeoning body of research on law and finance underscores the profound impact of legal institutions on financial and economic outcomes (e.g., La Porta et al., 1998, 1999, 2000). Similarly, another stream of literature emphasizes the significance of political connections in shaping corporate decisions (e.g., Faccio, 2006). Furthermore, research on law and politics argues for their inextricably intertwined nature (e.g., Whittington et al., 2008). However, existing studies often neglect the interactive effects of politics and law on financial outcomes, particularly within individual economies.

This study addresses this gap by explicitly examining the interplay between politics and law, and its economic consequences. We investigate how a country's legal and political institutions, jointly and separately, affect financial outcomes in an emerging and transitional economy. Specifically, we analyze how legal risk (measured by corporate lawsuits and legal reform shocks) and political connections interact to influence firm-level trade credit decisions within the Chinese context.

Trade credit in China offers an ideal setting to study the economic consequences of the interplay between politics and legal enforcement. This informal financing mechanism plays a critical role in fueling firm and economic growth, especially where formal and informal institutions are weaker (Petersen and Rajan, 1997; Fisman and Love, 2003; Allen et al., 2005). Between 2007 and 2017, trade credit accounted for 27% to 34% of public firms' total

debt in China (Wu et al., 2022). Prior research has documented a significant link between firm-level political connections and trade credit provision, supporting the theory of a "financing advantage" (e.g., Chen et al., 2021). Similarly, politically connected firms demand less accounts payable because they have easier access to formal financing sources (Cai et al., 2022). Additionally, other studies have found a negative relationship between lawsuits and accounts payable, supporting the "legal risk compensation" view (e.g., Wu et al., 2022). Despite the established link between political connections and trade credit, few studies have *explicitly* examined how politics and law-related factors interact to influence this behavior. This research addresses this gap by exploring the interplay between politics and law enforcement in China, focusing on their combined effect on firm-level trade credit decisions.

The existing literature on political science and law highlights the intertwined nature of these two spheres. As argued by Whittington, Kelemen, and Caldeira (2008), law is both a product and influencer of political processes. China represents an ideal setting to investigate this complex nexus due to its unique political and legal environment. The Chinese judiciary operates under the control of both central and local governments, potentially leading to biases against entities lacking political connections. Studies such as Firth et al. (2011), Lu et al. (2015), and Xu (2020) support this notion, demonstrating the significant impact of political connections on judicial independence in China. However, Zhang (2023) suggests recent legal reforms are underway to ensure that legal institutions keep pace with the evolving economic landscape.¹

We first explore the interplay between politics and law enforcement in China before extending to the economic consequence of the interplay. Our empirical results reveal a

¹ Fairbairn (2016) argues that judicial independence in China does not exist, but a good progress is observed.

significant bias in the Chinese legal system favoring politically connected firms. We find that these firms exhibit a lower likelihood of being defendants, higher win rates, and shorter lawsuit durations, compared with their non-connected counterparts. Notably, this advantage becomes more pronounced as firms' political connections become stronger. Additionally, the 2013 legal reform, intended to bolster judicial independence, appears to have exacerbated the disadvantage faced by non-connected firms. These findings offer compelling evidence that the Chinese legal system remains susceptible to manipulation by the central and local governments (e.g., Li and Wang, 2023; Zhang and Li, 2016).

We subsequently investigate the dynamic interplay between politics and law and its impact on trade credit decisions. In line with previous research, our findings indicate that companies with political affiliations demonstrate a propensity to extend greater trade credit, thereby corroborating the theory of a financing advantage. Concurrently, aligning with the perspective of the legal risk compensation effect, businesses characterized by elevated legal risk exhibit a tendency to offer more accounts receivable and obtain less accounts payable compared to their counterparts.

Moreover, our analysis reveals that the positive (negative) correlation between legal risk and receivables (payables) is notably evident solely for companies lacking political connections, regardless of their role as plaintiffs or defendants. Additionally, the discernibly adverse effect of the legal reform in 2013 on trade credit is similarly applicable to firms without political affiliations. In essence, these results furnish compelling evidence that, in the realm of corporate decision-making in China, politics wield a substantial influence, overshadowing the role of the legal system.

Our study contributes to the ongoing debate on the intricate relationship between politics and law enforcement in China. Our findings suggest that the Chinese legal system

is susceptible to government influence, aligning with prior studies such as Firth et al. (2011), Lu et al. (2015), and Xu (2020). However, our results, particularly those based on the legal reform in 2013, contradict those presented by Zhang (2023), which is grounded in the anti-corruption campaign initiated by President Xi in 2012. Notably, our study does not observe a positive trajectory in terms of judicial independence in China. Furthermore, few studies have explicitly delved into the interplay between politics and law and its impact on real financial decision making. Therefore, our paper addresses this gap by systematically exploring the economic implications, specifically in terms of trade credit, arising from the complex interrelationship between politics and law. Our empirical results underscore the dominance of politics in the nexus of politics, law, and finance, providing new insights into the critical policy implications for economic outcomes.

Our study also contributes to the literature on the intersection of law and finance. From a law and finance perspective, La Porta et al. (hereafter, LLSV) have provided substantial evidence indicating that cross-country variations in legal origin and institutions could account for differences in financial and economic outcomes globally (e.g., LLSV, 1998, 1999, 2000). However, these cross-country studies fall short in effectively explaining intra-country variations in financial and economic outcomes, particularly in major emerging economies like China (e.g., Allen et al., 2005). Consequently, this paper concentrates on a single-country setting. Our empirical design within a specific economy addresses concerns related to endogeneity and measurement errors that are often encountered in cross-country studies.²

Our study also contributes to the existing literature on the relationship between

² Some cross-country studies also consider the role of macro-level political institution in legal origin and institutions. Our study uses the firm-level political connections proposed by Faccio (2006) to explicitly examine the interaction of law and politics in affecting financial outcomes.

politics and finance. Current research highlights the significant role of political connections in influencing firm value, financing decisions, and insider trades (e.g., Faccio, 2006; Jagolinzer, Larcker, Ormazabal, and Taylor, 2020). Notably, Chen et al. (2021) provide global evidence that state-owned enterprises (SOEs) are more likely to extend trade credit, especially in economies with weak creditor protection, thereby supporting the theory of a financing advantage in trade credit provision. However, their study is confined to a small sample and employs an aggregate proxy for legal institutions. Our study extends this line of inquiry by delving into the role of firm-level legal risk and intra-country legal reforms in the politics-finance relationship within a specific country.

Finally, our study sheds light on the literature on trade credit. While previous research has offered specific explanations such as the financing advantage theory and the legal risk compensation view for trade credit, none of these studies explicitly compare these explanations within a unified framework. Our study presents evidence that the financing advantage theory is more applicable to politically connected firms, whereas the legal risk compensation view is more relevant to non-connected firms facing high legal risk. This observation is made within a unified framework that simultaneously considers political connections and legal enforcement in China.

2. Institutional Background and Hypothesis Development

2.1 Institutional Background

Firth, Rui, and Wu (2011) reveal that politically connected firms enjoy preferential treatment in the judicial process in China. Lu, Pan, and Zhang (2015) corroborate these findings, highlighting that Chinese courts exhibit a bias in favor of firms with political

connections. Interestingly, Lu, Pan, and Zhang (2015) note that this favoritism diminishes in regions with more robust legal institutions. Additionally, Xu (2020) contributes to this discourse by demonstrating that Chinese judges factor in the value of political connections when making decisions, resulting in a proclivity towards firms with political affiliations in China.

China's court system is organized into four levels: Basic People's Courts at the county level, Intermediate People's Courts at the prefecture level, Higher People's Courts (hereafter, HPC) at the province level, and the Supreme People's Court at the nation level. Judges in HPC have the authority to guide and supervise judges in lower court. Lower courts frequently seek advice from HPC when making decisions on judicial cases, which reduces judges' autonomy and wrecks appeal procedures. Court hearings would be held in the jurisdictions in which the defendants are located. The first-instance judgments for most cases are made by Basic and Intermediate People's Courts. The president of HPC has the administrative power to change judicial decision-making of Basic and Intermediate People's Courts within his/her jurisdiction. The legal system in China is subordinated to the Communist Party of China's rule. Prior to the reform, local party committees were responsible for electing the president of the Higher People's Court. Judicial recentralization reform centralizes court personnel management of pilot provinces from local politicians to the central government. The judicial reform means that the central government would coercively transfer a president of HPC from one province to another to take office. The appointment of HPC president in remaining provinces remains under the control of local government.

Trade credit is the most important source of external informal financing for firms (e.g., Petersen and Rajan, 1997; Li, Ng, and Saffar, 2021). Trade credit is crucial for promoting

firm and economic growth, especially in China with imperfect legal and financial institutions (e.g., Fisman and Love, 2003; Allen et al., 2005). For example, Allen, Qian, and Qian (2005) show the findings of the existing research on the law-finance-growth nexus are contradicted by China because small private firms grow much faster even though these firms are not favored in legal protection and external financing in China. The financing view suggests the suppliers that are relatively powerful and profitable would provide more trade credit for customers and the firms with easier access to formal financing demand less trade credit financing from suppliers. Chen et al. (2021) provide evidence that SOEs extend more trade credit, supporting the theory of financing advantage for trade credit provision. Cai et al., (2022) find politically connected firms demand less accounts payable because they have easier access to formal financing.

2.2 Hypothesis Development

Trade credit contracts rely strongly on reputation and trust mechanisms. Litigation signals lack of honesty to stakeholders and results in reputational damage (Godfrey, Merrill, and Hansen, 2009; Deng, Willis, and Xu, 2014). Litigation triggers the suppliers' ethical bottom lines. Therefore, suppliers decrease their assessment of the firms involved in lawsuits, and the trust built up in their regular operations will be challenged (e.g., Xin et al., 2018; Wu et al., 2022). Suppliers would question the commitment of client firms with litigation cases and reassess their incentives to execute the trading contracts. As a result, once a firm is involved in litigation events and it captures the attention of its suppliers, they would probably lower their trade credits to the firm with lawsuits because of confidence crisis.

Companies have powerful incentives to make proactive efforts to attenuate reputational damage and reestablish trust. Johnson, Xie, and Yi (2014) find that supplier

reputation loss from litigation damages public image and this weakens consumer trust, resulting in the termination of supply chain relationships. Cen, Chen, Hou, and Richardson (2018) provide empirical evidence on the positive relation between supplier's litigation risk and the probability of supplier-customer relationship termination. Previous research also provides evidence that trade credit provision is a mechanism to stimulate sales and foster better relations with customers (Long, Malitz, and Ravid, 1993; Molina and Preve, 2009). To repair tarnished reputations and reestablish trust, suppliers involved in litigation have strong incentives to extend trade credit to their customers as a compensation for the risk of litigation. Based on this argument, we propose Hypothesis 1 :

***H1:** There is a positive relationship between firm lawsuits and accounts receivable and a negative relationship between firm lawsuits and accounts payable.*

Considering that political connections may not only reduce litigation risk before legal proceedings but also alleviate the adverse consequences of lawsuits afterward (e.g., Firth et al., 2011; Lu et al., 2015; Xu, 2020; Zhang, 2023), we posit that the impact of firm lawsuits on trade credit is more pronounced in politically non-connected firms. Building on this premise, we propose Hypothesis 2 :

***H2:** The relationship between firm lawsuits and trade credit in H1 is more pronounced among politically non-connected firms than politically connected firms.*

With the centralization of personnel decisions in local courts as a result of the judicial recentralization reform, the influence of local politicians over these decisions has diminished (Miao et al., 2023). In this case, the centralization of local judge appointments may

improve the level of judicial independence. However, Li and Wang (2023) argue that the judicial reform aims to enhance central government oversight of local political elites by exerting greater control over the appointment of local court personnel, ultimately resulting in a reduction of judicial independence. They provide empirical evidence that court officials and judges are more incentivized to serve the economic and political interests of the central government following the reform. Post-reform, local courts are envisioned to align more closely with the interests of the Communist Party of China and the central government. As a result, courts face increased political interference from the central government, decreasing the level of judicial independence. Consequently, we anticipate a heightened inclination for these courts to exhibit bias in favor of politically connected businesses.

H3: Politically connected firms are more favored by the courts following judicial recentralization reform.

With judicial independence weakened after the judicial recentralization reform, the relevance of political connections should increase. If *H3* is validated, we posit that politically non-connected firms would be inclined to increase accounts receivable and reduce accounts payable in response to the judicial recentralization reform. Based on this conjecture, we propose Hypothesis 4 :

H4: Politically non-connected firms provide more accounts receivable and receive less accounts payable following judicial recentralization reform.

3. Sample Data and Research Design

3.1 Data and Sample

We construct our sample using several data sources. Firm financial information is extracted from the Chinese Security Market and Accounting Research Database (CSMAR). Data on corporate lawsuits are sourced from the Chinese Research Data Services Platform. Information on directors' work experience and biographies is obtained from CSMAR's Corporate Governance Research Database of Listed Companies in China, providing comprehensive details on directors. Our sample spans from 2008 to 2018, aligning with the period after the implementation of New Accounting Standards in the Chinese stock market in 2007. Firms in the financial industry are excluded due to their distinct operating activities and financial reporting environments. We further eliminate observations with missing values in our regressions, resulting in a final dataset comprising 13,718 firm-year observations, representing 1,994 unique firms. Of these, the analytical sample includes 8,265 lawsuits. To deal with outliers, we winsorize all continuous variables at levels of 1% and 99%.

3.2 Key Variables

3.2.1 Trade Credit

Following prior research (e.g., Cuñat, 2007), we use accounts receivable to measure the trade credit provision and scaled by total assets (*AccRec1*). Additionally, we define trade credit provision in accordance with Chen et al. (2021) as accounts receivable divided by total sales (*AccRec2*). Following prior literature (e.g., Ge and Qiu, 2007; Wu et al., 2022), we define the other key dependent variable, firms' trade credit access, as accounts payable divided by total assets (*Pay1*) or accounts payable divided by total sales (*Pay2*).

3.2.2 Corporate Lawsuits

We follow Liu, Miao, and Liu (2020) to measure a firm's litigation risk in each year. Liu,

Miao, and Liu (2020) suggest corporate lawsuit data's timing is subject to the listed firm's first announcement date. The first measure *Number* is calculated as the number of times a firm is involved in litigation as a plaintiff or defendant in a year. Another measure *Amount* is the monetary claim against a defendant in lawsuits divided by the firm's total assets.

We use two approaches to measure the outcome of litigation. First, Zhang (2023) and Xu (2020) define plaintiff's success as receiving a monetary benefit at trial. We define *Win* as an indicator equal to one if disclosing companies win lawsuits, and zero otherwise. Second, drawing on the duration of case measured in Li and Ponticelli (2022), we define *Time interval* as the time from acceptance day by court to case closing date (in days). The shorter case duration means courts are more efficient when judging the case (Li and Ponticelli, 2022).

3.2.3 Political Connections

Following prior studies (e.g., Lu, Pan, and Zhang, 2015), the political connection of a firm is calculated in two ways. First, when a firm is an SOE, the dummy variable *SOE* is set to one; otherwise, it equals zero. If the ultimate controlling shareholder of a firm in CSMAR database is the government or one of its agents, the firm qualifies as an SOE. In addition, if a firm has a director who was or is a section chief level or higher government employee, or a chief member of the Chinese People's Political Consultative Conference or National People's Congress, we consider such firm to be politically connected. We create an indicator variable *POLITICAL TIE* set to one if any director of the firm has personal political tie, and zero otherwise. Non-SOEs frequently form political ties to gain political capital. Non-SOEs have more directors with personal political ties to participate in politics compared to SOEs.

3.3 Research Design

To test the political biases in Chinese judiciary, we run the following regression:

$$Litigation_{i,j,t} = \alpha + \mu_j + \mu_t + \beta_1 Political\ Connections_{j,t} + \gamma' X_{j,t} + \varepsilon_{i,j,t} \quad (1)$$

where i , j and t index lawsuit event, firm and year, respectively. The dependent variable is a firm's litigation risk proxied by $Number_{j,t}$ and $Amount_{j,t}$, or the litigation outcome measured by $Win_{i,j,t}$ and $Time\ interval_{i,j,t}$. The key independent variable is whether a firm is an SOE, and whether any director of the firm has personal political tie. u_j represents firm fixed effects, and u_t represents year fixed effects. We control for book leverage (LEV), return on assets (ROA), cash-to-asset ratio ($CASH$), market share ($SHARE$), firm size ($SIZE$), sales growth ($GROWTH$), market-to-book ratio (MTB), the number of employees (EMP), advertising intensity ($ADVERTING$), and tangible assets ($TANGIBLE$).

Deteriorating performance leads to increased litigation risk for firms (Kim and Skinner, 2012). Therefore, we expect a negative coefficient for the variables ROA . Adhikari, Agrawal, and Malm (2019) argue that firms with large size, deep pockets, increase in sales, and high value face greater litigation pressure. Consequently, we anticipate the variables $SIZE$, EMP , $SHARE$, $CASH$, $GROWTH$, and MTB to have positive coefficients. Advertising enhances the positive perception of firms, thereby mitigating the risk of litigation (Barnett, Hartmann, and Salomon, 2018). Additionally, debt limits firms' discretionary cash holdings, which reduces the incentive for potential plaintiffs to sue firms (Adhikari, Agrawal, and Malm, 2019). Tangible assets are easier to monitor and value than intangible assets, and firms with more tangible assets are less likely to be sued for agency issues (Barnett, Hartmann, and Salomon, 2018). Hence, we expect negative coefficients for the control variables $ADVERTING$, LEV , and $TANGIBLE$ in equation (1).

We run the following regressions to separately test the effect of corporate lawsuits on trade credit, and the effect of political connections on trade credit.

$$Trade\ credit_{j,t} = \alpha + \mu_j + \mu_t + \beta_1 Litigation/Political\ Connection_{j,t} + \gamma' Y_{j,t} + \varepsilon_{j,t} \quad (2)$$

where j and t index firm and year respectively. Trade credit provision is measured by $AccRec1_{j,t}$ and $AccRec2_{j,t}$, and trade credit access is measured by $Pay1_{j,t}$ and $Pay2_{j,t}$. We control various corporate characteristics that may affect trade credit. Specifically, we control for book leverage (LEV), return on assets (ROA), cash-to-asset ratio ($CASH$), market share ($SHARE$), firm size ($SIZE$), sales growth ($GROWTH$), market-to-book ratio (MTB), the number of employees (EMP), and business group ($GROUP$). Variable definitions in detail are provided in the Appendix A. All regressions control firm and year fixed effects.

When the dependent variable is accounts receivable, the expected signs of control variables are as follows. The effect of firm size ($SIZE$ and EMP) on the provision of trade credit is ambiguous (Wu, Firth, and Rui, 2014). Large firms have more funds to extend credit to customers because they have better access to financing. However, large firms have more bargaining power, so they might offer less credit to customers. Wu, Firth, and Rui (2014) find that growing firms have not enough time to build good reputation for product quality and have low bargaining power with customers. Therefore, we expect a positive coefficient for the variable $GROWTH$. Zhang (2020) argue that firms with great profits and high value have more capacity to extend credit. Consequently, we anticipate the variables ROA and MTB to carry positive coefficients. Chen et al. (2021) find that firms with less cash offer more trade credit. Prior study indicates a negative association between bargaining power and trade credit provision (Fabbri and Klapper, 2016). There should be a negative coefficient on $CASH$ and $SHARE$. Wu, Firth, and Rui (2014) find that greater financing capacity increases the firm's ability to offer credit, so the coefficient on LEV is predicted to be positive. Hyun (2021) finds that group affiliated firms raise trade credit provision to their affiliates but decrease trade credit provision to unaffiliated clients, so the coefficient on $GROUP$ is also ambiguous.

When the dependent variable is accounts payable, the expected signs of control variables are as follows. Firms with large size, profitability, and market share have high level of creditworthiness, and they have more access to trade credit (Xu, Wu, and Dao, 2020). Petersen and Rajan (1997) find that growth firms are likely to have more opportunities for investment and greater demand for credit. Prior study indicates a positive relationship between sales growth and accounts payable (Fabbri and Klapper, 2016). Consequently, we anticipate the variables *SIZE*, *EMP*, *ROA*, *SHARE*, *MTB*, and *GROWTH* to have positive coefficients. Because trade credit is viewed as a loan substitution (Cull et al., 2009), we expect the coefficient of *LEV* to be negative. Firms with more current assets demand more trade credit (Xu, Wu, and Dao, 2020), so the coefficient on *CASH* is predicted to be positive. The intra-group transactions in business groups could affect the trade credit level and bias the empirical result, so we control for the variable *GROUP*.

Table 1 shows summary statistics. *AccRec1* and *AccRec2* have respective mean values of 0.093 and 0.186. *Pay1* and *Pay2* have respective mean values of 0.111 and 0.191. The sample firms are involved with lawsuits 0.334 times on average. The average value of *Amount* is about 0.316, and its standard deviation is about 1.430. *Win* and *Time interval* have respective mean values of 0.518 and 349.484, similar to prior studies (e.g., Zhang, 2023; Li and Ponticelli, 2022). The mean values of political connection indicators indicate 53.3 percent of sample firms are SOEs, and 44.1 percent of sample firms' directors have personal political ties.

[Insert Table 1]

4. The Interplay between Politics and Law Enforcement

4.1 Political Connections and Corporate Lawsuits

Table 2 presents the summary statistics for lawsuits filings. Our sample includes 8,265 lawsuits. Panel A provides the distribution of lawsuits by case types among politically connected firms. Zhang (2023) classifies lawsuits cases into three categories: cases relating to intercorporate loans and bank loans, cases associated with other (regular business) contracts, and tort cases.³ Loan cases are the main lawsuit type. Panel B reports the distribution of cases by whether disclosing politically connected firms win or not. Following Zhang (2023) and Xu (2020), we define plaintiff's success as receiving a monetary benefit at trial. As demonstrated in Table 2, politically connected firms account for 78% (3,310/4,240) of plaintiff observations but 68% (2,719/4,025) of defendant observations. Additionally, politically connected firms make up 79% (3,366/4,286) of winning cases but 67% (2,663/3,979) of lost cases. Panel C reports the average case durations in each politically connected firm subgroup. The average case durations are shorter for firms with political connections than for firms without political connections (plaintiff: 381 days; defendant: 412 days).

Overall, the evidence in Table 2 suggests that Chinese courts exhibit a bias in favor of firms with political connections. Loan and contract cases account for 90% of lawsuits cases. Importantly, firms with political connections are less likely to be sued and more likely to file lawsuits than firms without political connections in China. In terms of litigation outcomes, firms with political connections have higher win rates than firms without political connections. As for the efficiency of court trials, firms with political connections have shorter case durations than firms without political connections.

³ Tort is defined as a wrongful act or a violation of a right (other than under a contract) resulting in civil liability.

[Insert Table 2]

To further confirm the findings in Table 2, we test the relationship between politics and law using equation (1). Existing studies show that Chinese courts favor non-SOEs with political connections and SOEs, suggesting a lack of judicial independence in China (e.g., Firth et al., 2011; Lu et al., 2015; Xu, 2020).

Table 3 reports the empirical results of equation (1). Panel A reports the results for corporate litigation risk. Here we use two measures to better identify lawsuits. One is the number of times a firm is involved in litigation, and the other is the monetary claim against a defendant in lawsuits divided by the firm's total assets.

In columns (1) and (3), The coefficients of *SOE* are significant and negative, implying that SOEs have fewer lawsuits as the defendant than non-SOEs. In columns (2) and (4), the coefficients of *POLITICAL TIE* are also significant and negative, indicating that firms with political connections have fewer lawsuits as defendants than their counterparts without political connections. However, the coefficients of *SOE* are significant and positive in columns (5) and (7), and the coefficients of *POLITICAL TIE* in columns (6) and (8) are also significantly positive. The evidence in columns (5) to (8) suggests that firms with political connections have more lawsuits as plaintiffs than their counterparts without political connections. Overall, these findings imply that firms with political connections are less likely to be sued and more likely to file lawsuits than firms without political connections in China.

Panels B and C in Table 3 show the results for litigation outcome. Panel B shows the results for the sample of defendants, and Panel C presents the results for the sample of plaintiffs. The estimated coefficients of *SOE* and *POLITICAL TIE* are positive and significant in columns (1) and (2), suggesting that politically connected firms have higher

win rates than politically non-connected firms. The estimated coefficients of *SOE* and *POLITICAL TIE* are negative and significant in columns (3) and (4), implying that politically connected firms have shorter case durations than politically non-connected firms. The evidence in Table 3 is consistent with the findings in Table 2⁴.

[Insert Table 3]

Existing studies argue that the role of political connection strength in judicial independence is neglected in existing studies (e.g., Ge et al., 2022; Zhang, 2023). Therefore, we further test the moderating effect of political connection strength on the relationship between political connection and litigation outcome. First, higher-ranking officials and administrations have more power than lower-ranking counterparts in China. When an official has a higher rank than the president of a court, he or she is able to exert a direct influence on the court's budgetary and personnel decision; however, it is more difficult when an official has a lower rank than a court. Thus, we predict that the effect of political connection is more pronounced among the firms connected to the bureaucrat with a higher rank than that of the court's president. Following Zhang (2023), we create *High* as an indicator equal to one if a firm connected to a bureaucrat with a higher administrative rank than the rank of the president of a court where a lawsuit is judged, and zero otherwise.

Panels A and B of Table 4 present empirical results. When the dependent variable is *Win*, the coefficients of *SOE*×*High* and *POLITICAL TIE*×*High* are positive and significant, implying that the positive impact of political connection on win rates is greater when political connection strength is stronger. When the dependent variable is *Time interval*, the

⁴ In lawsuit regressions, we run pooled regressions including both the *SOE* dummy variable and the political connection dummy variable, as well as their associated interaction terms. The findings are robust in this specification, and the estimated coefficients of *SOE* × *POLITICAL TIE* are statistically insignificant.

coefficients of *SOE × High* and *POLITICAL TIE × High* are negative and significant, suggesting that the negative impact of political connection on litigation durations is greater when political connection strength is stronger.

In addition, Ge et al. (2022) argue that the proportion of directors with political connections is positively associated with a firm's strength of political connection. We set a dummy *Multiple* equal to one if the proportion of directors with political connections is above the sample median, and zero otherwise. Panels C and D of Table 4 show results. The coefficients of *SOE × Multiple* and *POLITICAL TIE × Multiple* are significantly positive when the dependent variable is *Win*, and the coefficients of *SOE × Multiple* and *POLITICAL TIE × Multiple* are significantly negative if the dependent variable is *Time interval*. The findings in Table 4 demonstrate that the influence of political connections is more pronounced among firms with stronger political connection strength.

[Insert Table 4]

In sum, we conduct a thorough empirical analysis of the types, outcomes, and case duration of lawsuits in the context of political connections. The main findings are that firms with political connections are less likely to be defendants, have higher win rates and shorter lawsuit duration than firms without such connections. Political connections and political connection strength matter for the outcomes of the lawsuits of firms in China.

4.2 The Judicial Reform

Prior studies provide ample evidence that the judicial reform increases Communist Party of China and the central government control over local courts without enhancing judicial independence. For example, Li and Wang (2023) find that the judicial reform is

designed to monitor local political elites by the central government through the increased control of local court personnel, and it ultimately weakens the judicial independence. Judicial recentralization reform centralizes court personnel management of pilot provinces from local politicians to the central government. Thus, we expect that politically connected firms are more favored by courts following the judicial recentralization reform. In this subsection, we examine how such a judicial reform affects the legal enforcement in China.

It is an exogenous shock for Chinese listed firms because the mandatory rotation of Higher People's Court's president was decided and implemented by the central government in 2013. Operationally, we construct a treatment group using the firms headquartered in the provinces that are subject to the judicial reform. Then, we use the logit model to predict the likelihood of a firm being treated based on some firm characteristics including market-to-book ratio, book leverage, firm size, and return on assets. For each firm affected by the judicial reform, we choose a non-reform-affected firm with minimal propensity score difference from the same industry and in the same year to construct a control group. Specific difference-in-differences (DiD) framework is as follows.

$$\begin{aligned}
 Litigation_{i,j,t} = & \alpha + \mu_j + \mu_t + \beta_1 Treat \times Post_{j,t} + \beta_2 Treat \times Post \times Political\ Connection_{j,t} \\
 & + \beta_3 Political\ Connection_{j,t} + \gamma' X_{j,t} + \varepsilon_{i,j,t}
 \end{aligned} \tag{3}$$

where i, j and t index lawsuit event, firm and year, respectively. The variable of interest is $Treat \times Post \times Political\ Connection_{j,t}$. The dependent variable is a firm's litigation risk proxied by $Number_{j,t}$ and $Amount_{j,t}$, or the case outcome measured by $Win_{i,j,t}$ and $Time\ interval_{i,j,t}$. We define $Treat$ as an indicator variable equal to one for the firms included in treatment group, and zero otherwise. We construct an indicator $Post$ equal to one for the three years (2013-2015) since the judicial reform is adopted, and zero for the three years (2010-2012) before the judicial reform implementation. Following prior studies (e.g., Lu, Pan, and Zhang,

2015), SOEs and the firms with politically connected directors are defined as politically connected firms. We also control a set of variables, firm and year fixed effect as in equation (1).

Table 5 reports the results of equation (3). Panel A shows the results for the sample of defendants, and Panel B presents the results for the sample of plaintiffs. The estimated coefficients on $Treat \times Post \times SOE$ and $Treat \times Post \times POLITICAL\ TIE$ are significantly negative for two measures of litigation risk in Panel A columns (1) to (4), suggesting that politically connected firms are less likely to be defendants after the judicial reform. The estimated coefficients on $Treat \times Post \times SOE$ and $Treat \times Post \times POLITICAL\ TIE$ are significantly positive for two measures of litigation risk in Panel B columns (1) to (4), indicating that politically connected firms are more likely to be plaintiffs following the judicial reform. The columns (5) to (8) in Panels A and B present the results of litigation outcome. The coefficients of $Treat \times Post \times SOE$ and $Treat \times Post \times POLITICAL\ TIE$ are significantly positive if the outcome variable is *Win*, and the coefficients of $Treat \times Post \times SOE$ and $Treat \times Post \times POLITICAL\ TIE$ are significantly negative if the outcome variable is *Time interval*. These results suggest that politically connected firms have higher win rates and shorter litigation durations following the judicial reform.

Overall, the findings displayed in Table 5 are consistent with our prediction that politically connected firms are more favored by courts following the judicial recentralization reform, which also supports the findings in Li and Wang (2023) that the judicial reform is designed to monitor local political elites by the central government through increased control of local court personnel, and it ultimately weakens judicial independence. These

further evidences point out that the judicial reform is endogenous to the Communist Party of China and government's interests, which impacts both law enforcement and firm decisions.

[Insert Table 5]

5. Politics, Law Enforcement, and Trade Credit

In this section, we further investigate how the interplay between politics and law affects the trade credit decisions. The results in the section 4 suggest that the Chinese legal system remains susceptible to manipulation by central and local governments. Therefore, we expect that the financing advantage theory is more applicable to politically connected firms, whereas the legal risk compensation view finds better resonance with non-connected firms facing high legal risk. First, we re-examine the theory of a "financing advantage" by examining the relationship between political connections and trade credit. Then, we test the relationship between corporate lawsuits and trade credit, and study whether politics dominate the role of the legal system in corporate decisions in China.

5.1 Political Connections and Trade Credit

Political connection is a key factor in corporate decision makings. Chen et al. (2021) provide the global evidence on the positive relationship between trade credit provision and state ownership based on state ownership's financing advantage theory. Guariglia and Mateut (2016) show politically connected firms extend more trade credit than politically non-connected firms during the period of 2000 to 2007 in China. Cai et al. (2022) find that politically connected firms have less demand in accessing trade credit because they have easier access to other financing sources. In this subsection, we re-examine the relation

between political connections and trade credit in China from 2008 to 2018.

Table 6 Panel A reports the results of equation (2) when the independent variable is political connection. The dummy variable *SOE*'s coefficient is significantly positive in column (1), indicating that SOEs tend to extend more trade credit compared with non-SOEs. In addition, the coefficient of *POLITICAL TIE* is positive and significant in column (2), indicating that firms with political connections tend to extend more trade credit than their counterparts without political connections. We calculate economic significance using the estimate in column (1) as an example. SOEs have an increase of 0.012 in *AccRec1* compared to non-SOEs, which is equivalent to 12.9% (0.012/0.093) of its sample mean. In columns (3) to (4), the estimated coefficients on *SOE* and *POLITICAL TIE* are negative and significant, which supports the argument in Cai et al. (2022) that politically connected firms with easier access to formal financing sources have less demand in accessing trade credit⁵. Overall, these results are consistent with the financing advantage of political connections in prior studies.

We further test the moderating effect of political connections strength on the impact of political connections on trade credit. Because Table 6 is not related to litigation, we only employ the proportion of directors with political connections to test the strength's moderating effects. Panel B of Table 6 displays the results. The estimated coefficients on *SOE×Multiple* and *POLITICAL TIE×Multiple* are significantly positive in columns (1) to (2). The estimated coefficients on *SOE × Multiple* and *POLITICAL TIE × Multiple* are significantly negative in columns (3) to (4). Thus, the effect of political connections on trade

⁵ We re-estimate the results of Tables 6-9 using accounts receivable divided by sales (*AccRec2*) and accounts payable divided by sales (*Pay2*). We report the results in Appendix B Table B1. The overall empirical results are not sensitive to either firm assets or sales as the scaling factor of trade credit levels.

credit becomes more pronounced among firms with stronger political connections.

[Insert Table 6]

5.2 Corporate Lawsuits and Trade Credit

We then examine the relationship between a firm's corporate lawsuits and its trade credit.

The results are presented in Table 7. We find both the number of lawsuits and the total monetary claim are positively and significantly associated with trade credit provision in columns (1) to (2). These results suggest that firms with more lawsuits tend to provide more trade credit than firms with fewer lawsuits. When the dependent variable is accounts payable, the estimated coefficients on *Number* and *Amount* are negative and significant, suggesting that corporate lawsuits have a negative relationship with accounts payable. Overall, the results in Table 7 are consistent with H1 that there is a positive relationship between firm lawsuits and accounts receivable and a negative relationship between firm lawsuits and accounts payable⁶.

[Insert Table 7]

5.3 Political Connections, Corporate Lawsuits, and Trade Credit

To better understand the *distinct* and *joint* role of lawsuits and political connections, we examine the nexus of lawsuits, political connections, and trade credit in a unified framework. Most existing studies focus on the influence of either legal institutions or political connections on financial outcomes. We consider these three variables in a

⁶ Trade credit levels could be attributable to legal risk associated with state intervention. To address this issue, we conduct a two-stage regression. First, we regress the lawsuit variables on state ownership, political connections, and other control variables as shown in Table 3. Second, we regress trade credit on the predicted lawsuit values from the first-stage regression. We report the results in Appendix B Table B2. Our findings remain robust in the two-stage regression specifications.

framework so that we can better identify the distinct role of lawsuits and political connections in explaining the trade credit. In this subsection, we examine the relation between lawsuits and trade credit in three subsamples based on state ownership and political connections: SOEs, non-SOEs with political connections, and non-SOEs without political connections. Following prior studies (e.g., Lu, Pan, and Zhang, 2015), we consider a non-SOE to be politically connected if the firm has any director who was or is a government employee at section chief level or higher, or a chief member in the Chinese People's Political Consultative Conference or National People's Congress.

Table 8 reports the results. In columns (1) to (3) of all panels, we find the positive relationship between lawsuits and trade credit provision is significant only in the subsample of non-SOEs without political connections. The results are consistent in terms of the number of lawsuits and the total monetary claims of lawsuits. These results indicate only non-SOEs without political connections need provide more trade credit as compensation for the risk of litigation when these firms are in the trouble of lawsuits and that political connections of SOEs and non-SOEs with political connections could mitigate the negative impact of lawsuits. Moreover, in column (4) of all panels, we employ a pooled regression setting by incorporating both the *Non-political connection* variable and its interaction with lawsuits in equation (2). *Non-political connection* is an indicator that equals one if a non-SOE does not have any director who was or is a government employee at the section chief level or higher, or a chief member in the Chinese People's Political Consultative Conference or National People's Congress, and zero otherwise. The estimated coefficients of $Number/Amount \times Non-political\ connection$ are statistically significant and positive, and the coefficients of *Number/Amount* are statistically insignificant, consistent with the results presented in columns (1) to (3).

In columns (5) to (7) of all panels, the negative impact of lawsuits on accounts payable is significant only in the subsample of non-SOEs without political connections, which is consistent in terms of the number of lawsuits and the total monetary claims of lawsuits. These results indicate only non-SOEs without political connections are greatly affected by litigation shock, and their suppliers would lower trade credits to them due to confidence crisis. In column (8) of all panels, the estimated coefficients of *Number/Amount* \times *Non-political connection* are statistically significant and negative, and the coefficients of *Number/Amount* are statistically insignificant, consistent with the results reported in columns (5) to (7). Overall, these results further suggest political connections are valuable resources for Chinese firms that could influence investment and financing decisions made by firms, especially private firms in China (e.g., Zhang and Li, 2016).

[Insert Table 8]

5.4 The Judicial Reform and Trade Credit

In the subsection 5.3, we find that only non-SOEs without political connections significantly change trade credit because they are more affected by litigation shock. In addition, the results in the subsection 4.2 indicate that politically connected firms are more favored by courts following the judicial recentralization reform. Therefore, we expect that only non-SOEs without political connections significantly change their trade credit decisions following the judicial reform.

We employ the DiD method to explore the role of political connections in the impact of the judicial recentralization reform on trade credit. Our DiD framework is specified as follows:

$$Trade\ credit_{j,t} = \alpha + \mu_j + \mu_t + \beta_1 Treat \times Post_{j,t} + \gamma' Y_{j,t} + \varepsilon_{j,t} \quad (4)$$

where j and t index firm and year respectively. $Y_{j,t}$ is the same set of controls as in equation (2). The key coefficient is β_1 , which compares the changes of trade credit among firms headquartered in provinces that adopt the judicial reform with the changes of trade credit among firms headquartered in provinces that do not adopt the judicial reform. We separately run equation (4) in three subsamples: SOEs, non-SOEs with political connections, and non-SOEs without political connections.

Table 9 shows the expected results. In columns (1) to (3), the positive relationship between the judicial reform and trade credit provision is significant only in the subsample of non-SOEs without political connections. In column (4), the estimated coefficient of $Treat \times Post \times Non-political\ connection$ is statistically significant and positive, and the coefficient of $Treat \times Post$ is statistically insignificant, consistent with the results presented in columns (1) to (3)⁷. In columns (5) to (7), the negative relationship between the judicial reform and trade credit access is significant only in the subsample of non-SOEs without political connections. In column (8), the estimated coefficient of $Treat \times Post \times Non-political\ connection$ is statistically significant and negative, and the coefficient of $Treat \times Post$ is statistically insignificant, consistent with the results presented in columns (5) to (7). Thus, only non-SOEs without political connections significantly change their trade credit decisions following the judicial reform.

In sum, section 5 focuses specifically on how lawsuits and political connections intersect in the realm of trade credit. In terms of explanations for corporate trade credit decisions, we find the financing advantage theory is more applicable to politically connected firms, whereas the legal risk compensation view finds better resonance with non-connected

⁷ We use a pooled regression after incorporating both the Non-political connection variable and its interaction with $Treat \times Post$ in equation (4).

firms facing high legal risk. Results suggest that the relationship between legal risk and trade credit is significantly evident solely for firms without political connection. Essentially, in the realm of corporate decision-making in China, politics wield a substantial influence, overshadowing the role of the legal system.

[Insert Table 9]

6. Conclusion

In this paper, we explore the intricate interplay between politics, law, and finance in the context of China. The empirical findings reveal a notable bias in the Chinese legal system favoring politically connected firms, even in the aftermath of legal reforms. This underscores the persistent influence of politics on financial outcomes.

Our research sheds light on trade credit dynamics, uncovering that politically connected firms extend more accounts receivable and receive less accounts payable, supporting the financing advantage theory. Conversely, non-connected firms facing higher legal risk display a similar inclination, aligning with the legal risk compensation view. Notably, the relationship between legal risk and trade credit is more pronounced for non-connected firms, emphasizing the nuanced relationship between politics, law, and financial decisions.

In addressing the broader dialogue on law and finance, our study underscores the importance of considering micro-level political dynamics and unique legal landscapes within individual countries. By focusing on China, we provide nuanced insights beyond traditional cross-country studies, enhancing our understanding of how politics and law jointly influence financial outcomes.

In conclusion, our findings offer valuable insights to the understanding of the interconnected roles played by politics and law in shaping financial decisions, particularly in the dynamic economic landscape of China. This research offers implications for policymakers and scholars seeking a deeper understanding in the factors influencing financial outcomes in emerging and transitional economies.

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Appendix A: Variable definitions

Variables	Definitions
<i>AccRec1</i>	The ratio of accounts receivable to total assets
<i>AccRec2</i>	The ratio of accounts receivable to sales
<i>Pay1</i>	Accounts payable divided by total assets
<i>Pay2</i>	Accounts payable divided by total sales
<i>Number</i>	The number of times a firm is involved in litigations as a plaintiff or defendant in a year
<i>Amount</i>	The monetary claim against a defendant in lawsuits divided by the firm's total assets
<i>SOE</i>	An indicator variable that is equal to one if a firm is a state-owned enterprise, and zero otherwise
<i>POLITICAL TIE</i>	An indicator variable that is equal to one if the firm has any director who was or is a government employee at the section chief level or higher, or a chief member in Chinese People's Political Consultative Conference or National People's Congress, and zero otherwise
<i>Non-political connection</i>	An indicator that equals one if a non-SOE does not have any director who was or is a government employee at the section chief level or higher, or a chief member in the Chinese People's Political Consultative Conference or National People's Congress, and zero otherwise
<i>LEV</i>	The ratio of the book value of long-term and short-term debts to book value of assets
<i>ROA</i>	Return on assets
<i>CASH</i>	The ratio of cash to total assets
<i>SHARE</i>	The ratio of the firm's sales to total industry sales
<i>SIZE</i>	The natural logarithm of total assets
<i>GROWTH</i>	The growth rate of firm sales
<i>MTB</i>	The ratio of market value of asset to book value of asset
<i>EMP</i>	The natural logarithm of the number of total employees
<i>GROUP</i>	An indicator set to one if a firm affiliated with business group and zero otherwise
<i>ADVERTING</i>	The ratio of advertising expenses to sales
<i>TANGIBLE</i>	The ratio of the firm's tangible assets to sales
<i>Win</i>	An indicator equal to one if disclosing firms win lawsuits and zero otherwise
<i>Time interval</i>	The number of days from the acceptance day by court until the case closing date

Appendix B

Table B1: Alternative measures of trade credit

We re-estimate the results of Tables 6-9 using accounts receivable divided by sales (*AccRec2*) and accounts payable divided by sales (*Pay2*). Panels A and B present the estimation results of Table 6 using an alternative measure of trade credit. Panels C and D present the results of Table 7 using the new variable. Panel E and F show the results of Table 8 using the alternative measure. Panel G reports the results of Table 9.

Panel A Political connections and trade credit				
	<i>AccRec2</i>	<i>AccRec2</i>	<i>Pay2</i>	<i>Pay2</i>
	(1)	(2)	(3)	(4)
<i>SOE</i>	0.028*		-0.046*	
	(1.76)		(-1.68)	
<i>POLITICAL TIE</i>		0.011**		-0.114*
		(2.48)		(-1.77)
Controls	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y
Year FE	Y	Y	Y	Y
Observation	13,718	13,718	12,600	12,600
R ²	0.806	0.806	0.503	0.503

Panel B The moderating effect of political connection strength				
	<i>AccRec2</i>	<i>AccRec2</i>	<i>Pay2</i>	<i>Pay2</i>
	(1)	(2)	(3)	(4)
<i>SOE</i>	0.033**		-0.044**	
	(2.12)		(-1.97)	
<i>POLITICAL TIE</i>		0.009**		-0.089**
		(2.31)		(-2.29)
<i>SOE</i> × <i>Multiple</i>	0.029***		-0.018*	
	(3.46)		(-1.67)	
<i>POLITICAL TIE</i>		0.011***		-0.070**
		(2.66)		(-2.45)
× <i>Multiple</i>	0.026***	0.009**	-0.097	-0.013
	(4.11)	(2.08)	(-0.86)	(-0.24)
Controls	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y
Year FE	Y	Y	Y	Y
Observation	13,718	13,718	12,600	12,600
R ²	0.807	0.812	0.507	0.504

Panel C Lawsuits and trade credit: defendant sample

	<i>AccRec2</i>	<i>AccRec2</i>	<i>Pay2</i>	<i>Pay2</i>
	(1)	(2)	(3)	(4)
<i>Number</i>	0.005* (1.91)		-0.011*** (-3.49)	
<i>Amount</i>		0.004*** (3.07)		-0.008*** (-4.67)
Controls	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y
Year FE	Y	Y	Y	Y
Observation	9,478	9,478	8,706	8,706
R ²	0.806	0.806	0.503	0.503

Panel D Lawsuits and trade credit: plaintiff sample

	<i>AccRec2</i>	<i>AccRec2</i>	<i>Pay2</i>	<i>Pay2</i>
	(1)	(2)	(3)	(4)
<i>Number</i>	0.004* (1.81)		-0.012*** (-3.39)	
<i>Amount</i>		0.003*** (3.20)		-0.009*** (-4.53)
Controls	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y
Year FE	Y	Y	Y	Y
Observation	9,693	9,693	8,903	8,903
R ²	0.811	0.811	0.503	0.503

Panel E Lawsuits, political connections and trade credit: lawsuits measured by *Number*

Defendant sample

	SOEs	non-SOEs with PC	non-SOEs without PC	SOEs	non-SOEs with PC	non-SOEs without PC		
	<i>AccRec2</i>	<i>AccRec2</i>	<i>AccRec2</i>	<i>AccRec2</i>	<i>Pay2</i>	<i>Pay2</i>	<i>Pay2</i>	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	
<i>Number</i>	0.002 (0.64)	0.003 (0.85)	0.016*** (5.52)	0.003 (1.49)	-0.008 (-1.22)	-0.011 (-0.02)	-0.013*** (-3.45)	-0.001 (-0.34)
<i>Number</i> × <i>Non-political connection</i>				0.014*** (3.12)				-0.009*** (-3.24)
<i>Non-political connection</i>				-0.038*** (-5.91)				0.010*** (3.82)
Controls	Y	Y	Y	Y	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y	Y	Y	Y	Y
Year FE	Y	Y	Y	Y	Y	Y	Y	Y
Observation	5,213	2,464	1,801	9,478	4,788	2,264	1,654	8,706
R ²	0.782	0.882	0.777	0.808	0.510	0.480	0.724	0.503

Plaintiff sample								
	SOEs	non-SOEs with PC	non-SOEs without PC		SOEs	non-SOEs with PC	non-SOEs without PC	
	<i>AccRec2</i>	<i>AccRec2</i>	<i>AccRec2</i>	<i>AccRec2</i>	<i>Pay2</i>	<i>Pay2</i>	<i>Pay2</i>	<i>Pay2</i>
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
<i>Number</i>	0.001 (0.42)	0.002 (0.69)	0.015*** (5.37)	0.004 (1.36)	-0.006 (-0.95)	-0.016 (-0.66)	-0.024*** (-2.65)	-0.001 (-0.32)
<i>Number</i> × <i>Non-political connection</i>				0.005*** (2.63)				-0.013* (-1.85)
<i>Non-political connection</i>				-0.042*** (-3.98)				0.010** (2.37)
Controls	Y	Y	Y	Y	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y	Y	Y	Y	Y
Year FE	Y	Y	Y	Y	Y	Y	Y	Y
Observation	5,331	2,520	1,842	9,693	4,897	2,315	1,691	8,903
R ²	0.804	0.897	0.779	0.743	0.510	0.479	0.728	0.503

Panel F Lawsuits, political connections and trade credit: lawsuits measured by *Amount*

Defendant sample								
	SOEs	non-SOEs with PC	non-SOEs without PC		SOEs	non-SOEs with PC	non-SOEs without PC	
	<i>AccRec2</i>	<i>AccRec2</i>	<i>AccRec2</i>	<i>AccRec2</i>	<i>Pay2</i>	<i>Pay2</i>	<i>Pay2</i>	<i>Pay2</i>
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
<i>Amount</i>	0.001 (0.96)	0.002 (0.89)	0.005*** (3.69)	0.002 (0.67)	-0.001 (-0.36)	-0.004 (-1.06)	-0.009** (-1.99)	-0.000 (-0.06)
<i>Amount</i> × <i>Non-political connection</i>				0.002** (2.36)				-0.002** (-2.02)
<i>Non-political connection</i>				-0.037*** (-5.56)				0.057** (2.07)
Controls	Y	Y	Y	Y	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y	Y	Y	Y	Y
Year FE	Y	Y	Y	Y	Y	Y	Y	Y
Observation	5,213	2,464	1,801	9,478	4,788	2,264	1,654	8,706
R ²	0.782	0.882	0.774	0.808	0.468	0.482	0.520	0.504

Plaintiff sample								
	SOEs	non-SOEs with PC	non-SOEs without PC		SOEs	non-SOEs with PC	non-SOEs without PC	
	<i>AccRec2</i>	<i>AccRec2</i>	<i>AccRec2</i>	<i>AccRec2</i>	<i>Pay2</i>	<i>Pay2</i>	<i>Pay2</i>	<i>Pay2</i>
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
<i>Amount</i>	0.001	0.003	0.003**	0.001	-0.002	-0.004	-0.010**	-0.003
	(0.67)	(0.86)	(2.12)	(0.97)	(-0.69)	(-0.75)	(-2.04)	(-1.41)
<i>Amount</i> × <i>Non-political connection</i>				0.000**				-0.008***
				(2.26)				(-2.74)
<i>Non-political connection</i>				-0.025***				0.047*
				(-3.44)				(1.82)
Controls	Y	Y	Y	Y	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y	Y	Y	Y	Y
Year FE	Y	Y	Y	Y	Y	Y	Y	Y
Observation	5,331	2,520	1,842	9,693	4,897	2,315	1,691	8,903
R ²	0.782	0.882	0.828	0.812	0.458	0.484	0.517	0.524

Panel G Judicial reform, political connections and trade credit

	SOEs	non-SOEs with PC	non-SOEs without PC		SOEs	non-SOEs with PC	non-SOEs without PC	
	<i>AccRec2</i>	<i>AccRec2</i>	<i>AccRec2</i>	<i>AccRec2</i>	<i>Pay2</i>	<i>Pay2</i>	<i>Pay2</i>	<i>Pay2</i>
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
<i>Treat</i> × <i>Post</i>	0.007	-0.015	0.019**	0.001	-0.247	-0.339	-	-0.190
	(0.69)	(-1.48)	(2.55)	(0.15)	(-1.32)	(-1.37)	0.085***	(-0.98)
<i>Treat</i> × <i>Post</i> × <i>Non-political connection</i>				0.013**				-0.127**
				(2.11)				(-2.10)
<i>Non-political connection</i>				-0.009*				0.176*
				(-1.70)				(1.74)
Controls	Y	Y	Y	Y	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y	Y	Y	Y	Y
Year FE	Y	Y	Y	Y	Y	Y	Y	Y
Observation	1,816	676	1,068	3,560	1,667	621	981	3,269
R ²	0.889	0.958	0.906	0.922	0.554	0.314	0.819	0.507

Table B2: The second-stage regression

This table reports the results of the second-stage regression. The first-stage model regresses the lawsuit variables on the *SOE*, *POLITICAL TIE*, *SOE*×*POLITICAL TIE*, and other control variables as in Table 3. Then, we regress trade credit on the predicted lawsuit values from the first stage regression. Standard errors are clustered by firm, and T-statistics are reported in parentheses. The symbols ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively. Detailed definitions of variables are presented in the Appendix A.

Panel A Defendant sample								
	<i>AccRec1</i>	<i>AccRec1</i>	<i>AccRec2</i>	<i>AccRec2</i>	<i>Pay1</i>	<i>Pay1</i>	<i>Pay2</i>	<i>Pay2</i>
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
\widehat{Number}	0.005*** (5.73)		0.013*** (4.92)		-0.006*** (-3.83)		-0.016** (-2.22)	
\widehat{Amount}		0.003*** (5.90)		0.008*** (4.91)		-0.002*** (-3.30)		-0.016* (-1.73)
Controls	Y	Y	Y	Y	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y	Y	Y	Y	Y
Year FE	Y	Y	Y	Y	Y	Y	Y	Y
Observation	9,478	9,478	9,478	9,478	8,706	8,706	8,706	8,706
R ²	0.843	0.843	0.775	0.775	0.525	0.525	0.505	0.504

Panel B Plaintiff sample								
	<i>AccRec1</i>	<i>AccRec1</i>	<i>AccRec2</i>	<i>AccRec2</i>	<i>Pay1</i>	<i>Pay1</i>	<i>Pay2</i>	<i>Pay2</i>
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
\widehat{Number}	0.004*** (5.72)		0.012*** (4.85)		-0.003*** (-3.25)		-0.011** (-2.23)	
\widehat{Amount}		0.002*** (5.86)		0.007*** (4.83)		-0.001*** (-3.30)		-0.014* (-1.72)
Controls	Y	Y	Y	Y	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y	Y	Y	Y	Y
Year FE	Y	Y	Y	Y	Y	Y	Y	Y
Observation	9,693	9,693	9,693	9,693	8,903	8,903	8,903	8,903
R ²	0.861	0.861	0.807	0.807	0.511	0.506	0.501	0.504

Table 1: Summary statistics

This table reports descriptive statistics of our analytical sample. Detailed definitions of variables are presented in the Appendix A.

Variables	Obs	Mean	S.D.	P5	P25	Median	P75	P95
<i>AccRec1</i>	13,718	0.093	0.092	0.002	0.024	0.067	0.135	0.274
<i>AccRec2</i>	13,718	0.186	0.197	0.004	0.047	0.128	0.254	0.580
<i>Pay1</i>	12,600	0.111	0.201	0.013	0.045	0.082	0.138	0.286
<i>Pay2</i>	12,600	0.191	1.104	0.024	0.077	0.134	0.223	0.453
<i>Number</i>	13,718	0.334	0.810	0.000	0.000	0.000	0.000	3.000
<i>Amount</i>	13,718	0.316	1.430	0.000	0.000	0.000	0.000	1.415
<i>SOE</i>	13,718	0.533	0.499	0.000	0.000	1.000	1.000	1.000
<i>POLITICAL</i>	13,718	0.441	0.496	0.000	0.000	0.000	1.000	1.000
<i>TIE</i>								
<i>LEV</i>	13,718	0.465	0.211	0.119	0.303	0.468	0.624	0.803
<i>ROA</i>	13,718	0.036	0.065	-0.056	0.011	0.033	0.064	0.128
<i>CASH</i>	13,718	0.057	0.066	-0.028	0.032	0.055	0.086	0.148
<i>SHARE</i>	13,718	0.029	0.071	0.001	0.003	0.008	0.023	0.123
<i>SIZE</i>	13,718	22.174	1.248	20.374	21.309	22.056	22.919	24.401
<i>GROWTH</i>	13,718	0.004	0.165	-0.003	0.000	0.001	0.003	0.008
<i>MTB</i>	13,718	2.087	1.803	0.993	1.232	1.608	2.339	4.581
<i>EMP</i>	13,718	7.618	1.311	5.472	6.834	7.638	8.448	9.749
<i>GROUP</i>	13,718	0.429	0.495	0.000	0.000	0.000	1.000	1.000
<i>ADVERTING</i>	13,695	0.006	0.023	0.000	0.000	0.000	0.002	0.031
<i>TANGIBLE</i>	13,718	0.588	2.268	0.037	0.172	0.363	0.695	1.740
<i>Win</i>	8,265	0.518	0.372	0	0	1	1	1
<i>Time interval</i>	8,265	349.484	394.785	24	130	235	465	1097

Table 2: Descriptive statistics of the sample of lawsuits

Panel A reports the distribution of lawsuits by case types in politically connected firms. Panel B reports the distribution of lawsuits by whether disclosing politically connected firms win or not. Panel C reports the average case duration in each politically connected firm subgroup. We categorize the cases into three types: bank loans and intercorporate loans, other (regular business) contracts, and tort cases. *Win* is an indicator equal to one if disclosing firms win lawsuits and zero otherwise. *Time interval* is the time from acceptance day by court to case closing date (in days).

Panel A Cases type				
		Politically connected firms		
		Plaintiff	Defendant	Total
SOE				
Contract		1,024	788	1,812
Loan		997	909	1,906
Tort		233	211	444
Total		2,254	1,908	
Non-SOE	with political			
Contract		459	380	839
Loan		493	348	841
Tort		104	83	187
Total		1,056	811	
Ratio		plaintiff: 78%; defendant: 68%		

Panel B Win rate				
		Politically connected firms		
		Plaintiff	Defendant	Total
SOE				
<i>Win</i> =1		1,490	992	2,482
<i>Win</i> =0		764	916	1,680
Total		2,254	1,908	
Non-SOE	with political			
<i>Win</i> =1		548	336	884
<i>Win</i> =0		508	475	983
Total		1,056	811	
Ratio		win: 79%; lose: 67%		

Panel C Average case duration				
		Politically connected firms		
		Plaintiff	Defendant	
SOE				
<i>Time interval</i>		310	326	
Non-SOE	with political			
<i>Time interval</i>		325	348	

Table 3: Political connections and lawsuits

This table reports the relationship between political connections and lawsuits. Standard errors are clustered by firm, and T-statistics are reported in parentheses. The symbols ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively. Detailed definitions of variables are presented in the Appendix A.

	Defendant				Plaintiff			
	<i>Number</i>	<i>Number</i>	<i>Amount</i>	<i>Amount</i>	<i>Number</i>	<i>Number</i>	<i>Amount</i>	<i>Amount</i>
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
<i>SOE</i>	-0.145** (-2.11)		-0.247** (-2.04)		0.169** (2.45)		0.290** (2.32)	
<i>POLITICAL</i>		-0.104*** (-3.64)		-0.175*** (-3.45)		0.111*** (3.92)		0.179*** (3.64)
<i>TIE</i>								
<i>LEV</i>	0.090 (0.74)	0.087 (0.72)	0.252 (1.09)	0.247 (1.07)	0.092 (0.76)	0.076 (0.73)	0.255 (1.10)	0.218 (1.07)
<i>ROA</i>	0.910 (1.17)	0.842 (1.02)	1.153 (0.63)	1.174 (0.60)	0.916 (1.19)	0.922 (1.22)	1.163 (0.63)	1.064 (0.64)
<i>CASH</i>	-1.002 (-1.19)	-1.106 (-1.32)	-2.577 (-1.32)	-2.741 (-1.42)	-0.971 (-1.15)	-1.109 (-1.33)	-2.520 (-1.29)	-2.752 (-1.02)
<i>SHARE</i>	0.012 (0.06)	0.022 (0.14)	0.036 (0.14)	0.077 (0.21)	0.010 (0.05)	0.034 (0.15)	0.032 (0.13)	0.071 (0.28)
<i>SIZE</i>	0.048* (1.69)	0.041 (1.47)	0.141*** (2.71)	0.116** (2.37)	0.047* (1.70)	0.040 (1.46)	0.130*** (2.59)	0.120** (2.36)
<i>GROWTH</i>	0.004 (0.70)	0.003 (0.55)	0.022** (2.22)	0.018** (2.10)	0.005 (0.77)	0.003 (0.56)	0.020** (2.31)	0.019** (2.10)
<i>MTB</i>	0.007 (0.88)	0.007 (0.91)	-0.003 (-0.25)	-0.003 (-0.17)	0.007 (0.87)	0.005 (0.89)	-0.003 (-0.26)	-0.002 (-0.19)
<i>EMP</i>	-0.004 (-0.16)	-0.005 (-0.35)	-0.037 (-1.32)	-0.042 (-1.50)	-0.002 (-0.13)	-0.007 (-0.36)	-0.036 (-1.29)	-0.032 (-1.51)
<i>ADVERTIN</i>	0.707 (1.04)	0.748 (1.10)	1.143 (0.83)	1.212 (0.90)	0.701 (1.03)	0.750 (1.10)	1.132 (0.88)	1.213 (0.82)
<i>TANGIBLE</i>	-0.002 (-1.43)	-0.002 (-1.38)	-0.002 (-1.10)	-0.002 (-1.12)	-0.003 (-1.52)	-0.003 (-1.40)	-0.003 (-1.23)	-0.003 (-1.13)
Firm FE	Y	Y	Y	Y	Y	Y	Y	Y
Year FE	Y	Y	Y	Y	Y	Y	Y	Y
Observation	9,478	9,478	9,478	9,478	9,693	9,693	9,693	9,693
R ²	0.442	0.443	0.308	0.309	0.443	0.443	0.308	0.309

Panel B Lawsuit outcome: defendant sample

	<i>Win</i>	<i>Win</i>	<i>Time interval</i>	<i>Time interval</i>
	(1)	(2)	(3)	(4)
<i>SOE</i>	0.054** (2.03)		-0.861*** (-3.34)	
<i>POLITICAL TIE</i>		0.058*** (5.36)		-0.302** (-2.14)
Controls	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y
Year FE	Y	Y	Y	Y
Observation	4,025	4,025	4,025	4,025
R ²	0.393	0.395	0.850	0.843

Panel C Lawsuit outcome: plaintiff sample

	<i>Win</i>	<i>Win</i>	<i>Time interval</i>	<i>Time interval</i>
	(1)	(2)	(3)	(4)
<i>SOE</i>	0.058* (1.78)		-0.845*** (-3.10)	
<i>POLITICAL TIE</i>		0.067*** (5.19)		-0.306** (-2.48)
Controls	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y
Year FE	Y	Y	Y	Y
Observation	4,240	4,240	4,240	4,240
R ²	0.656	0.658	0.852	0.851

Table 4: Moderating effect: political connection strength

This table reports the relationship between political connections and lawsuit outcomes conditional on political connection strength. *High* is an indicator equal to one if a firm connected to a bureaucrat with a higher administrative rank than the rank of the president of a court where a lawsuit is judged, and zero otherwise. *Multiple* is a dummy set to one if the proportion of directors with political connections is above the sample median, and zero otherwise. Panels A and C show the results for the sample of defendants, and Panels B and D present the results for the sample of plaintiffs. Panels A and B show the results for the moderating effect of administrative ranks, and Panels C and D present the results for the moderating effect of multiple politically connected directors. Standard errors are clustered by firm, and T-statistics are reported in parentheses. The symbols ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively. Detailed definitions of variables are presented in the Appendix A.

Panel A The moderating effect of <i>High</i> : defendant sample				
	<i>Win</i>	<i>Win</i>	<i>Time interval</i>	<i>Time interval</i>
	(1)	(2)	(3)	(4)
<i>SOE</i>	0.071*** (2.59)		-0.995*** (-3.47)	
<i>POLITICAL TIE</i>		0.071*** (5.50)		-0.508*** (-3.10)
<i>SOE</i> × <i>High</i>	0.064*** (2.85)		-0.527** (-2.26)	
<i>POLITICAL TIE</i> × <i>High</i>		0.030* (1.80)		-0.502** (-2.44)
<i>High</i>	0.045*** (2.61)	0.013 (1.01)	-0.007 (-1.13)	-0.009* (-1.69)
Controls	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y
Year FE	Y	Y	Y	Y
Observation	4,025	4,025	4,025	4,025
R ²	0.393	0.395	0.852	0.852

Panel B The moderating effect of <i>High</i> : plaintiff sample				
	<i>Win</i>	<i>Win</i>	<i>Time interval</i>	<i>Time interval</i>
	(1)	(2)	(3)	(4)
<i>SOE</i>	0.058 (1.64)		-0.976*** (-3.79)	
<i>POLITICAL TIE</i>		0.053*** (3.37)		-0.398** (-2.42)
<i>SOE</i> × <i>High</i>	0.044** (2.02)		-0.517** (-2.14)	
<i>POLITICAL TIE</i> × <i>High</i>		0.042** (2.46)		-0.706* (-1.79)
<i>High</i>	0.012 (0.67)	0.031** (2.30)	-0.006 (-1.11)	-0.014 (-1.54)
Controls	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y
Year FE	Y	Y	Y	Y
Observation	4,240	4,240	4,240	4,240
R ²	0.656	0.658	0.851	0.852

Panel C The moderating effect of *Multiple*: defendant sample

	<i>Win</i>	<i>Win</i>	<i>Time interval</i>	<i>Time interval</i>
	(1)	(2)	(3)	(4)
<i>SOE</i>	0.084*** (3.02)		-1.025*** (-3.56)	
<i>POLITICAL TIE</i>		0.078*** (5.07)		-0.433** (-2.27)
<i>SOE</i> × <i>Multiple</i>	0.082*** (3.88)		-0.469** (-2.09)	
<i>POLITICAL TIE</i> × <i>Multiple</i>		0.033* (1.82)		-0.392* (-1.72)
<i>Multiple</i>	0.075*** (4.37)	0.011 (0.90)	-0.008 (-1.27)	-0.013** (-2.48)
Controls	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y
Year FE	Y	Y	Y	Y
Observation	4,025	4,025	4,025	4,025
R ²	0.395	0.395	0.852	0.852

Panel D The moderating effect of *Multiple*: plaintiff sample

	<i>Win</i>	<i>Win</i>	<i>Time interval</i>	<i>Time interval</i>
	(1)	(2)	(3)	(4)
<i>SOE</i>	0.059 (1.63)		-1.006*** (-3.38)	
<i>POLITICAL TIE</i>		0.050*** (2.84)		-0.334*** (-2.87)
<i>SOE</i> × <i>Multiple</i>	0.047** (2.08)		-0.460** (-2.21)	
<i>POLITICAL TIE</i> × <i>Multiple</i>		0.037* (1.93)		-0.765* (-1.66)
<i>Multiple</i>	0.007 (0.36)	0.023* (1.74)	-0.004 (-1.10)	-0.004 (-0.53)
Controls	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y
Year FE	Y	Y	Y	Y
Observation	4,240	4,240	4,240	4,240
R ²	0.656	0.658	0.852	0.852

Table 5: Difference-in-Differences regressions: Evidence from the judicial reform

This table reports the relationship between the judicial reform and lawsuits. Each model includes the same set of controls shown in Table 3. Panel A shows the results for the sample of defendants, and Panel B presents the results for the sample of plaintiffs. Standard errors are clustered by the province of headquarter, and T-statistics are reported in parentheses. *, **, and *** denote significance at 10%, 5%, and 1% levels, respectively. Detailed definitions of variables are presented in the Appendix A.

Panel A Defendant sample

	<i>Number</i>	<i>Number</i>	<i>Amount</i>	<i>Amount</i>	<i>Win</i>	<i>Win</i>	<i>Time interval</i>	<i>Time interval</i>
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
<i>Treat</i> × <i>Post</i>	0.317	0.187	0.001	0.000	-0.018	-0.011	0.406	0.393
	(0.03)	(0.14)	(1.31)	(1.20)	(-0.22)	(-0.94)	(1.14)	(0.21)
<i>Treat</i> × <i>Post</i> × <i>SOE</i>	-0.657***		-0.001*		0.031**		-0.602**	
	(-5.66)		(-1.75)		(2.30)		(-2.50)	
<i>Treat</i> × <i>Post</i> × <i>POLITICAL TIE</i>		-0.594**		-0.001**		0.025**		-0.431**
		(-2.48)		(-2.25)		(2.30)		(-2.06)
<i>SOE</i>	-0.393*		-0.000*		0.017*		-0.008**	
	(-1.97)		(-1.88)		(1.73)		(-2.13)	
<i>POLITICAL TIE</i>		-0.746**		-0.000*		0.025*		-0.016*
		(-2.50)		(-1.92)		(1.72)		(-1.68)
Controls	Y	Y	Y	Y	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y	Y	Y	Y	Y
Year FE	Y	Y	Y	Y	Y	Y	Y	Y
Observations	2,471	2,471	2,471	2,471	1,047	1,047	1,047	1,047
R ²	0.508	0.509	0.239	0.238	0.907	0.907	0.910	0.910

Panel B Plaintiff sample

	<i>Number</i>	<i>Number</i>	<i>Amount</i>	<i>Amount</i>	<i>Win</i>	<i>Win</i>	<i>Time interval</i>	<i>Time interval</i>
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
<i>Treat</i> × <i>Post</i>	-0.656 (-0.03)	-0.483 (-1.54)	-0.001 (-0.94)	-0.001 (-0.85)	0.016 (0.62)	0.026 (1.06)	0.508 (1.61)	0.492 (0.13)
<i>Treat</i> × <i>Post</i> × <i>SOE</i>	1.203** (2.24)		0.001* (1.71)		0.045* (1.75)		-0.903** (-2.17)	
<i>Treat</i> × <i>Post</i> × <i>POLITICAL TIE</i>		1.357** (2.13)		0.001*** (3.09)		0.092*** (2.82)		-0.646** (-2.14)
<i>SOE</i>	0.180** (2.35)		0.000* (1.75)		0.095* (1.96)		-0.008** (-1.99)	
<i>POLITICAL TIE</i>		0.167** (2.39)		0.000* (1.71)		0.171*** (4.63)		-0.010* (-1.74)
Controls	Y	Y	Y	Y	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y	Y	Y	Y	Y
Year FE	Y	Y	Y	Y	Y	Y	Y	Y
Observations	2,513	2,513	2,513	2,513	1,089	1,089	1,089	1,089
R ²	0.513	0.517	0.235	0.235	0.784	0.789	0.910	0.910

Table 6: Political connections and trade credit

Panel A reports the relationship between political connections and trade credit. *SOE* is an indicator variable that is equal to one if a firm is an SOE, and zero otherwise. *POLITICAL TIE* is an indicator variable that is equal to one if any director of the firm has personal political tie, and zero otherwise. Panel B reports the relationship between political connections and trade credit conditional on political connection strength. Standard errors are clustered by firm, and T-statistics are reported in parentheses. The symbols ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively. Detailed definitions of variables are presented in the Appendix A.

Panel A Political connections and trade credit				
	<i>AccRec1</i>	<i>AccRec1</i>	<i>Pay1</i>	<i>Pay1</i>
	(1)	(2)	(3)	(4)
<i>SOE</i>	0.012** (2.05)		-0.034* (-1.82)	
<i>POLITICAL -L TIE</i>		0.006*** (3.54)		-0.018** (-2.15)
<i>LEV</i>	0.041*** (4.16)	0.044*** (4.19)	-0.182*** (-10.75)	-0.281*** (-5.85)
<i>ROA</i>	0.036 (0.75)	0.034 (0.72)	0.668*** (5.37)	0.797*** (5.53)
<i>CASH</i>	-0.169*** (-2.87)	-0.163*** (-2.77)	-0.059 (-0.30)	0.060 (0.29)
<i>SHARE</i>	0.009 (0.52)	0.007 (0.41)	0.075** (2.29)	0.128*** (2.93)
<i>SIZE</i>	-0.005** (-2.07)	-0.005** (-2.19)	0.018** (2.53)	0.050*** (3.14)
<i>GROWTH</i>	-0.001 (-1.11)	-0.000 (-0.76)	0.018 (0.62)	0.019 (0.54)
<i>MTB</i>	-0.000 (-0.63)	-0.000 (-0.66)	-0.001 (-1.11)	0.001 (0.90)
<i>EMP</i>	-0.001 (-0.68)	-0.001 (-0.56)	0.010* (1.89)	0.003 (0.60)
<i>GROUP</i>	-0.000 (-0.04)	0.001 (0.34)	0.001 (0.28)	0.016 (1.10)
Firm FE	Y	Y	Y	Y
Year FE	Y	Y	Y	Y
Observation	13,718	13,718	12,600	12,600
R ²	0.860	0.860	0.419	0.355

Panel B The moderating effect of political connection strength

	<i>AccRec1</i>	<i>AccRec1</i>	<i>Pay1</i>	<i>Pay1</i>
	(1)	(2)	(3)	(4)
<i>SOE</i>	0.014** (2.53)		-0.032* (-1.72)	
<i>POLITICA</i> <i>-L TIE</i>		0.003* (1.93)		-0.017** (-2.40)
<i>SOE</i> × <i>Multiple</i>	0.013*** (3.76)		-0.011** (-2.08)	
<i>POLITICA</i> <i>-L TIE</i> × <i>Multiple</i>		0.008*** (3.79)		-0.016* (-1.84)
<i>Multiple</i>	0.013*** (5.17)	0.002 (0.97)	-0.006 (-1.35)	-0.001 (-0.13)
Controls	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y
Year FE	Y	Y	Y	Y
Observation	13,718	13,718	12,600	12,600
R ²	0.861	0.860	0.422	0.356

Table 7: Lawsuits and trade credit

This table reports the relationship between lawsuits and trade credit. The dependent variable is trade credit measured by *AccRec1* and *Pay1*. The test variable is *Number*, defined as the number of times a firm is involved in litigation as a plaintiff or defendant in a year. Another test variable *Amount* is the monetary claim against a defendant in lawsuits divided by the firm's total assets. Panel A shows the results for the sample of defendants, and Panel B presents the results for the sample of plaintiffs. Standard errors are clustered by firm, and T-statistics are reported in parentheses. The symbols ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively. Detailed definitions of variables are presented in the Appendix A.

Panel A Defendant sample				
	<i>AccRec1</i>	<i>AccRec1</i>	<i>Pay1</i>	<i>Pay1</i>
	(1)	(2)	(3)	(4)
<i>Number</i>	0.002*** (3.01)		-0.005** (-2.04)	
<i>Amount</i>		0.001*** (2.86)		-0.001** (-1.98)
<i>LEV</i>	0.043*** (4.17)	0.042*** (4.17)	-0.306*** (-6.34)	-0.306*** (-6.35)
<i>ROA</i>	0.031 (0.65)	0.032 (0.67)	0.997*** (5.10)	0.995*** (5.09)
<i>CASH</i>	-0.165*** (-2.79)	-0.163*** (-2.77)	-0.110 (-0.51)	-0.111 (-0.51)
<i>SHARE</i>	0.008 (0.48)	0.008 (0.47)	0.188*** (3.25)	0.187*** (3.25)
<i>SIZE</i>	-0.003** (-2.04)	-0.005** (-2.01)	0.059*** (3.72)	0.059*** (3.71)
<i>GROWTH</i>	-0.000 (-0.68)	-0.000 (-0.71)	0.602*** (20.72)	0.602*** (20.72)
<i>MTB</i>	-0.000 (-0.70)	-0.000 (-0.68)	0.001 (0.90)	0.001 (0.88)
<i>EMP</i>	-0.001 (-0.62)	-0.001 (-0.59)	0.003 (0.46)	0.003 (0.45)
<i>GROUP</i>	0.001 (0.28)	0.001 (0.28)	0.013 (0.91)	0.013 (0.91)
Firm FE	Y	Y	Y	Y
Year FE	Y	Y	Y	Y
Observation	9,478	9,478	8,706	8,706
R ²	0.860	0.860	0.522	0.522

Panel B Plaintiff sample

	<i>AccRec1</i>	<i>AccRec1</i>	<i>Pay1</i>	<i>Pay1</i>
	(1)	(2)	(3)	(4)
<i>Number</i>	0.003*** (2.70)		-0.006** (-2.24)	
<i>Amount</i>		0.002*** (2.97)		-0.002** (-2.14)
<i>LEV</i>	0.038*** (3.71)	0.038*** (3.70)	-0.317*** (-6.12)	-0.317*** (-6.13)
<i>ROA</i>	0.021 (0.45)	0.021 (0.44)	1.006*** (4.85)	1.003*** (4.85)
<i>CASH</i>	-0.164*** (-2.90)	-0.164*** (-2.91)	-0.128 (-0.55)	-0.128 (-0.55)
<i>SHARE</i>	0.007 (0.44)	0.008 (0.47)	0.191*** (3.17)	0.191*** (3.17)
<i>SIZE</i>	-0.005** (-2.13)	-0.005** (-2.08)	0.063*** (3.71)	0.063*** (3.70)
<i>GROWTH</i>	-0.000 (-0.42)	-0.000 (-0.46)	0.603*** (20.81)	0.603*** (20.80)
<i>MTB</i>	-0.000 (-0.18)	-0.000 (-0.16)	0.001 (0.96)	0.001 (0.92)
<i>EMP</i>	-0.000 (-0.03)	0.000 (0.02)	0.002 (0.38)	0.002 (0.37)
<i>GROUP</i>	0.002 (0.64)	0.002 (0.62)	0.015 (0.99)	0.015 (1.00)
Firm FE	Y	Y	Y	Y
Year FE	Y	Y	Y	Y
Observation	9,693	9,693	8,903	8,903
R ²	0.869	0.869	0.528	0.528

Table 8: Lawsuits, political connections and trade credit

This table reports the relationship between lawsuits and trade credit in SOEs, non-SOEs with political connections (PC) and non-SOEs without political connections, respectively. We define a firm as an SOE if its ultimate controlling shareholder in CSMAR database is the government or the government's agent. As for non-SOEs, we consider a non-SOE to be politically connected if the firm has any director who was or is a government employee at section chief level or higher, or a chief member in Chinese People's Political Consultative Conference or National People's Congress. Each model includes the same set of controls shown in Table 6. Standard errors are clustered by firm, and T-statistics are reported in parentheses. The symbols ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively.

Panel A Lawsuits measured by <i>Number</i>								
Defendant sample								
	SOEs	non-SOEs	non-SOEs		SOEs	non-SOEs	non-SOEs	
		with PC	without PC			with PC	without PC	
	<i>AccRec1</i>	<i>AccRec1</i>	<i>AccRec1</i>	<i>AccRec1</i>	<i>Pay1</i>	<i>Pay1</i>	<i>Pay1</i>	<i>Pay1</i>
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
<i>Number</i>	0.000	0.002	0.007***	0.001	-0.002	-0.008	-0.007**	-0.003
	(0.00)	(1.49)	(7.30)	(0.77)	(-0.25)	(-0.67)	(-2.39)	(-1.10)
<i>Number</i> × <i>Non-</i>				0.004***				-0.012*
<i>political connection</i>				(2.68)				(-1.75)
<i>Non-political</i>				-0.017***				0.015***
<i>connection</i>				(-7.77)				(3.73)
Controls	Y	Y	Y	Y	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y	Y	Y	Y	Y
Year FE	Y	Y	Y	Y	Y	Y	Y	Y
Observation	5,213	2,464	1,801	9,478	4,788	2,264	1,654	8,706
R ²	0.855	0.897	0.803	0.861	0.570	0.467	0.519	0.522
Plaintiff sample								
	SOEs	non-SOEs	non-SOEs		SOEs	non-SOEs	non-SOEs	
		with PC	without PC			with PC	without PC	
	<i>AccRec1</i>	<i>AccRec1</i>	<i>AccRec1</i>	<i>AccRec1</i>	<i>Pay1</i>	<i>Pay1</i>	<i>Pay1</i>	<i>Pay1</i>
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)

<i>Number</i>	0.000 (0.35)	0.002 (1.01)	0.009*** (7.41)	0.001 (1.24)	-0.001 (-0.41)	-0.006 (-1.37)	-0.011* (-1.78)	-0.003 (-0.99)
<i>Number</i> × <i>Non-political connection</i>				0.007*** (3.02)				-0.011* (-1.71)
<i>Non-political connection</i>				-0.016*** (-4.96)				0.016* (1.66)
Controls	Y	Y	Y	Y	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y	Y	Y	Y	Y
Year FE	Y	Y	Y	Y	Y	Y	Y	Y
Observation	5,331	2,520	1,842	9,693	4,897	2,315	1,691	8,903
R ²	0.903	0.912	0.806	0.846	0.570	0.468	0.520	0.523

Panel B Lawsuits measured by *Amount*

	Defendant sample							
	SOEs		non-SOEs		non-SOEs		non-SOEs	
	<i>AccRec1</i>	<i>AccRec1</i>	<i>AccRec1</i>	<i>AccRec1</i>	<i>Pay1</i>	<i>Pay1</i>	<i>Pay1</i>	<i>Pay1</i>
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
<i>Amount</i>	0.000 (0.96)	0.001 (0.74)	0.003*** (5.71)	0.000 (0.59)	-0.001 (-0.79)	-0.000 (-0.09)	-0.002* (-1.71)	-0.001 (-0.93)
<i>Amount</i> × <i>Non-political connection</i>				0.002*** (2.64)				-0.006** (-2.22)
<i>Non-political connection</i>				-0.016*** (-7.33)				0.038* (1.87)
Controls	Y	Y	Y	Y	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y	Y	Y	Y	Y
Year FE	Y	Y	Y	Y	Y	Y	Y	Y
Observation	5,213	2,464	1,801	9,478	4,788	2,264	1,654	8,706
R ²	0.855	0.897	0.799	0.861	0.573	0.510	0.732	0.415

Plaintiff sample								
	SOEs	non-SOEs with PC	non-SOEs without PC		SOEs	non-SOEs with PC	non-SOEs without PC	
	<i>AccRec1</i>	<i>AccRec1</i>	<i>AccRec1</i>	<i>AccRec1</i>	<i>Pay1</i>	<i>Pay1</i>	<i>Pay1</i>	<i>Pay1</i>
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
<i>Amount</i>	0.001	0.001	0.002***	0.000	-0.001	-0.001	-0.003**	-0.000
	(1.32)	(0.71)	(4.09)	(0.05)	(-0.65)	(-0.10)	(-2.57)	(-0.28)
<i>Amount*Non- political connection</i>				0.001*				-0.005**
				(1.66)				(-2.20)
<i>Non-political connection</i>				-0.011***				0.025**
				(-4.33)				(2.12)
Controls	Y	Y	Y	Y	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y	Y	Y	Y	Y
Year FE	Y	Y	Y	Y	Y	Y	Y	Y
Observation	5,331	2,520	1,842	9,693	4,897	2,315	1,691	8,903
R ²	0.854	0.897	0.722	0.857	0.571	0.511	0.721	0.490

Table 9: Judicial reform, political connections and trade credit

This table reports the relationship between the judicial reform and trade credit in SOEs, non-SOEs with political connections and non-SOEs without political connections, respectively. Each model includes the same set of controls shown in Table 6. Standard errors are clustered by the province of headquarter, and T-statistics are reported in parentheses. The symbols ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively. Detailed definitions of variables are presented in the Appendix A.

	SOEs	non-SOEs with PC	non-SOEs without PC		SOEs	non-SOEs with PC	non-SOEs without PC	
	<i>AccRec1</i>	<i>AccRec1</i>	<i>AccRec1</i>	<i>AccRec1</i>	<i>Pay1</i>	<i>Pay1</i>	<i>Pay1</i>	<i>Pay1</i>
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
<i>Treat</i> × <i>Post</i>	0.003	0.005	0.012*	0.005	-0.006	-0.014	-0.034***	-0.003
	(0.58)	(0.72)	(1.83)	(1.17)	(-0.91)	(-1.42)	(-3.34)	(-0.54)
<i>Treat</i> × <i>Post</i> × <i>Non-</i> <i>political connection</i>				0.007*				-0.028**
				(1.83)				(-2.07)
<i>Non-political</i> <i>connection</i>				-0.002*				0.010**
				(-1.80)				(2.41)
Controls	Y	Y	Y	Y	Y	Y	Y	Y
Firm FE	Y	Y	Y	Y	Y	Y	Y	Y
Year FE	Y	Y	Y	Y	Y	Y	Y	Y
Observation	1,816	676	1,068	3,560	1,667	621	981	3,269
R ²	0.927	0.953	0.937	0.929	0.871	0.901	0.785	0.850